PEARSON

Pearson plc Annual Report 1998

COMPACT INTERNET VERSION

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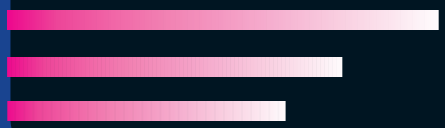
## Financial highlights £M $M*

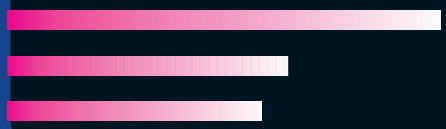
| | 1998 | 1997 | 1998 | 1997 | % |
|---|---|---|---|---|---|
| Sales | 2,395 | 2,293 | 3,976 | 3,806 | + 4 |
| Operating profit** | 389 | 328 | 646 | 544 | + 19 |
| Operating cash flow** | 392 | 159 | 651 | 264 | + 147 |
| Adjusted earnings per share | 42.0p | 34.9p | 69.7¢ | 57.9¢ | + 20 |
| Dividends per share | 21.0p | 19.5p | 34.9¢ | 32.4¢ | + 8 |

## Adjusted earnings PER SHARE



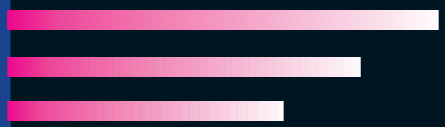
| | |
|---|---|
| 98 | 42.0p |
| 97 | 34.9p |
| 96 | 30.6p |

## Free cash flow PER SHARE



| | |
|---|---|
| 98** | 43.2p |
| 97*** | 22.9p |
| 96 | 19.2p |

## Dividends PER SHARE

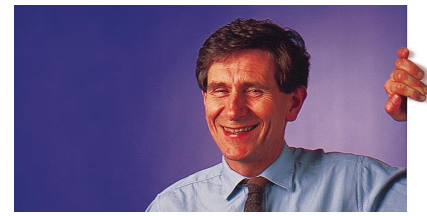


| | |
|---|---|
| 98 | 21.0p |
| 97 | 19.5p |
| 96 | 18.0p |

* US dollars at an exchange rate of $1.66
** Before goodwill and exceptional costs
*** Before effect of Penguin improper accounting

## Dennis Stevenson

CHAIRMAN



The overriding aim of your board and management is to deliver better and more consistent results for Pearson. In 1997, we reported progress. For 1998, we've taken another step in that right direction. Adjusted earnings were up 20%, and based on this, the board recommends a dividend of 21p, up 8% over last year.

In spite of a few scares, a generally benign economic environment in our major markets helped. But our progress has been due mostly to the creative and commercial talents of our people. We are achieving better results because our management have the confidence to set both more adventurous strategic goals and more demanding financial targets, and all the people who work in Pearson have the ability and motivation to meet them.

We have continued to rationalise and reshape Pearson. As a result, computer games, consumer magazines and theme parks no longer figure in our future. Our television, consumer publishing and business information operations are all using their stronger market positions to launch themselves in new directions. And we've made by far the largest single investment in Pearson's history to create the world's leading education business. The integration of the Simon & Schuster businesses is the most complex – and potentially rewarding – project we've ever undertaken.

As a result of all this activity, the company described in this report is very different from the Pearson of two years ago, even the Pearson of one year ago. Consequently, the value of the Company and the future expectations of our shareholders are both much greater than they were a year ago.

If we are to meet our shareholders' expectations we must ensure that we are able to retain the outstanding managers who have created the success and indeed recruit more of the same. The majority of our top executives work outside the UK and their current compensation is uncompetitive on an international basis.

At this year's AGM, therefore, we will be proposing a new approach to the long-term incentivisation of our senior managers which is consistent with our overall compensation approach. The details are set out in the circular to shareholders which accompanies this report. In principle, we are proposing a scheme which will ensure that if our management produce outstanding performance, they will earn rather more than under the current scheme. They will get these rewards, however, only if they deliver exceptional benefit to shareholders.

This was a good year for Pearson. We delivered good results, and we made progress toward creating better results more consistently. These results are the work of more than 20,000 Pearson colleagues who work in over 50 countries around the world. The board thanks them for their success and welcomes the fact that, through the new Company-wide bonus and share ownership plans we have introduced, they all now have the chance of a much more direct benefit from Pearson's future success. That keeps us all going in the same direction.

Dennis Stevenson

# It pays to think big, as long as you pay attention to the details.

1998 was one of the best years in Pearson's history. Looking at the big picture, in virtually every country trends continued to move in the direction of our businesses – the focus on public education; the rise of the English language; the shift of power from sellers to customers, who can increasingly design for themselves the information packages they want. We put our money on these trends, reshaping Pearson into four related businesses with commanding market positions, and the results so far have been rewarding.

To prepare the way, we sold almost £1bn of our assets, many of them fine businesses in their own right that were simply worth more to others. We regretted, for instance, the need to part with The Tussauds Group, a business that had added to both Pearson's charm and its bottom line for the last 20 years.

But these disposals created room for us to complete the largest acquisition in Pearson's history, paying £2.9bn for the Simon & Schuster businesses. This tripled the size of Pearson Education and jumped us to the front of the expanding worldwide education market, a business that will produce healthy growth and profits for many years. But profits are not our only goal. As a result of this acquisition, Pearson Education now has emerged as the world's leading supplier of the tools for education.

Education hasn't been the only business in which we've achieved the scale we need to succeed. As we've slimmed down, we've built up quite a bit of muscle. In two years, the FT Group has increased its profits by 33% while doubling the investment in its future growth. Penguin and Pearson Television are both half as big again as they were two years ago.

Attending to the details counts for just as much as size, of course. Big ideas and market scale are no good if we don't turn them into profits, make our shareholders wealthy and create a company that will last. In 1998 we made progress on all counts. We promised to deliver double-digit growth in earnings and we did. In the process, the value of the company – measured by the share price – grew strongly.

The operating success in 1998 was not accidental. We had promised the year before that we would concentrate on running things better, on making better products and on taking better advantage of the brands and assets we have. We did, and the progress has been encouraging.

In the Financial Times Group we made headway through international and electronic expansion. The initial instalments of our £100m commitment to invest in the *FT* over the last two years have begun to help the newspaper grow faster. In the US, for instance, the circulation grew from 32,000 at the beginning of 1997 to 70,000 at the end of 1998. Money spent on our electronic information services also began to produce results. FT.com expanded its service and reach and is now one of the most visited business websites in the world. Meanwhile, cost reduction and economies of scale around the FT Group further helped improve margins.

At Penguin, we continued to take advantage of the revolution in book publishing. As we built up our pipeline of great books of tomorrow, we also continued to strengthen the business, making our production and distribution more efficient by improving information systems. In the process, we reduced the number of unsold books returned by retailers in the US to a level not achieved by Penguin for many years. We also made real progress in our UK business and set up a stronger global footing to launch us into 2000.

For Pearson Television, its integration with All American Communications now complete, the story was better margins and more new products. One of the new shows, *First Wave*, will be seen in 1999 in some 30 countries around the world. Our game shows are back on US television, too (though our biggest, *The Price is Right*, never went away). And we are making new serial dramas in Germany, Sweden, Hungary and Finland. As a result, less than 40% of our television business is now in the UK.

But our success in acquiring the Simon & Schuster education business drew the most attention last year. The deal didn't close until the very end of the year, but Addison Wesley Longman's results are evidence that people didn't stop working while they were waiting. Both our school and our higher education businesses began to take off. We were hit hard by inclement economic weather in Asia, but we worked to make sure lost sales didn't translate into lost profits.

All these efforts, large and small, in 1998 created wealth for Pearson's shareholders, a group that increasingly includes Pearson's staff. Over the last 18 months we've given everyone – in all 53 countries in which we have offices – the chance to save to buy shares in Pearson. About a third of us (myself included) have now taken that opportunity. In addition, this year for the first time the Company-wide bonus plan paid 15 shares, plus a small cash award, to each qualifying employee. We welcome these colleagues to the growing ranks of Pearson employee-owners.

All around the Company, people are inventing ways to enter new markets, win new readers, sign new authors, commission new programmes and seize the potential of new media. In the process, we are creating a more durable, exciting Pearson for tomorrow without compromising today.

# The management team

## Marjorie Scardino

CHIEF EXECUTIVE

PEARSON PLC

## John Makinson

GROUP FINANCE DIRECTOR

PEARSON PLC

## David Bell

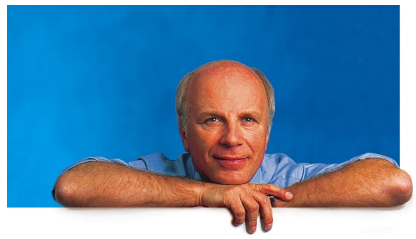
DIRECTOR FOR PEOPLE

PEARSON PLC

## Peter Jovanovich

CHAIRMAN AND CHIEF EXECUTIVE

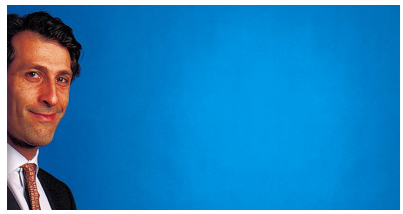
PEARSON EDUCATION



## Greg Dyke

CHAIRMAN AND CHIEF EXECUTIVE

PEARSON TELEVISION



## Michael Lynton

CHAIRMAN AND CHIEF EXECUTIVE

PENGUIN GROUP

## Stephen Hill

CHIEF EXECUTIVE

FINANCIAL TIMES GROUP

**MARJORIE** *spent four years as chief executive of The Economist Group. Has set ambitious growth targets, committing Pearson to generating double-digit earnings growth every year to create a more durable and valuable company. Wants everyone in Pearson to be a shareholder because she believes it to be "better to be an owner than an employee." Also takes a wider perspective of the business: "People want to work for a company that cares for what they care about, doing something they think is important and having a good time".*

**JOHN**, *former managing director of the* Financial Times *newspaper and before that founder of an investor relations firm, plays a key role in knitting Pearson companies together. He is also directing the Company's drive to improve its systems and his commitment to leading the campaign for cash flow in 1998 delivered the goods. His challenge for 1999 is more of the same: "Cash is crucial to Pearson – it's what gives us greater confidence to make the revenue investment needed to build our businesses."*

**DAVID**, *chairman of the* Financial Times *and a member of the Pearson board, has taken on a new Company-wide role as Director for People. His brief is to increase the resources and creativity Pearson devotes to recruiting, motivating, developing and rewarding the people who work in the Company. His vision is "to make Pearson simply the best company to work for in the world." His key challenge in 1999: "To continue to develop a culture and an approach across Pearson that entices our most talented and creative people to make their careers with us."*

**PETER** *has spent his whole career in educational publishing. He joined Pearson in August 1997 with the brief to create the world's leading education business. The acquisition of the Simon & Schuster businesses, completed in November, fulfilled the brief in one fell swoop. Peter does not underestimate the challenge of successfully bringing the two companies together, but knows it can be done. He says: "These are the most exciting times in education for 30 years. But we must always remember what we are all about: helping students to learn and teachers to teach."*

**GREG** *has spent most of his career in the television industry. A member of the Pearson board, he has led Pearson Television since 1995. Sees the key challenge in 1999 as capitalising on the international success of the business to develop new formats and break into new markets: "With strong local talent, a good format and an international production team who know what they're doing, we can deliver hit shows in any language or culture. With All American fully integrated, we are set up to create successful new shows and break into new markets."*

**MICHAEL** *has spent most of his career in the film and book industries. He has led Penguin since late 1996 and he also leads Pearson's cross-company Intellectual Property Rights exploitation. He is leading Penguin's efforts to continue to build its front-list of repeat, best selling authors with new talent and to change the economics of book publishing: "We are building a stronger global publishing house and we'll see the benefits of that in 1999. Printing on demand, new distribution technologies and internet retailing are all changing the landscape of our business. We have to make those changes work for us."*

**STEPHEN** *was head of Pearson Group strategy and ran the FT newspaper before taking on the FT Group role. He sees the key challenge in 1999 as sharpening the FT's competitive edge in international and electronic markets: "We are all about developing trusted relationships with business people around the world. We don't just tell them about what happened, but what it means for them and their business and, crucially, we apply a global perspective."*

# The Pearson company

## our business

*is in things that appeal to the mind. Whether it's educational, entertaining, or informative, whether it makes you laugh or helps you get a job or pass a test, we are in the business of feeding or exciting your mind. This is the business of all our companies. In addition to this, many things bind them together – brands, content, scale, people, values.*

## our brands

*are some of the strongest anywhere. Penguin is one of the most recognisable brands in consumer publishing. The* Financial Times *is a potent force in world business. Our education imprints are known to teachers and students from Hong Kong to Havana. Our television programmes command audience loyalty year after year. If we are careful, we can make these brands more valuable by sharing them across the Company. For example, Pearson Education and the FT are combining to launch a new management education business. Pearson Television's new animation business draws on Penguin's extensive range of children's characters. And Penguin's consumer appeal adds to the allure of our English Language Teaching business.*

## our content

*makes us players in the internet age. The Pearson Technology Centre, our in-house technology hub, and Headland, our digital publishing arm, work with businesses across the Company to capture the opportunities. We are building FT.com into one of the leading portals on the web for global strategic information. The internet gives Pearson Education the chance to take educational publishing into a new age, with greater and richer content and a degree of interactivity and immediacy central to teaching and learning. Internet retailing offers Penguin a chance to reach new customers and to show off its rich back-list of more than 25,000 titles. Pearson Television uses the web to exploit the on-line equity of its game shows. Revenues from internet activities are still small in proportion to the whole. But the internet is becoming a more important tool of both creativity and distribution across the Company.*

## our scale

*helps to reduce costs as we share purchases and processes across the Company. With the Simon & Schuster acquisition, Pearson is now one of the world's largest consumers of paper, printing and binding, and a major buyer of other commodities and services. A global sourcing team manages the supply processes across all Pearson businesses. In 1999, it will reduce our costs substantially. We are also continuing to reduce the costs of doing business by integrating back office functions. Bringing together the shared services initiatives of Pearson and Simon & Schuster for accounting, transactions and administrative functions will save money and increase efficiency.*

## our people

*are our most important asset. We expect a lot of ourselves and, if Pearson as a company does well, we want everyone to share in the success. So over 20,000 staff in 53 countries now have a direct stake in Pearson's future with the chance to participate in Company-wide bonus and save-for-shares plans. Record profits and real progress against our three financial goals in 1998 resulted in our first Company-wide bonus and an award of 15 Pearson shares to colleagues across the Company. The number of Pearson staff saving to buy shares in the Company has more than doubled to 6,000. And we aim to see that number increase significantly in the year ahead.*

## our values

*hold us together. We are working hard to communicate better across the Company so that everyone understands our strategy, goals and ways of doing business. We are doing much more to meet the challenge of finding, exciting and developing the people who work in Pearson. We are clear about the Company we want to be – a company that across all its businesses and cultures always strives to be imaginative, brave and decent.*

# The Pearson goals

In 1997, ambitious for the future growth of our Company, we established a financial benchmark for our progress: we aimed to achieve double-digit growth in adjusted earnings per share every year. To underpin this objective, we chose three financial measures by which we could gauge the annual performance of our Company. We aim to improve the rate of underlying sales growth; increase trading margins; and raise the proportion of profits that we convert into cash. We track the performance of each business against these measures and gear bonus payments to them. In 1998, as in 1997, we made good progress.

## Adjusted earnings PER SHARE

the measure of our underlying earnings, grew by 20%, up from 34.9p in 1997 to 42.0p in 1998. On the strength of this, a dividend of 21p has been recommended by the board.

## Sales UNDERLYING GROWTH

which represents the year-on-year, like-for-like increase in sales (excluding portfolio changes and movements in exchange rates) was 6.7%, up marginally from 6.5% in 1997. Total sales increased by 4%, with the increase in sales from the addition of the Simon & Schuster businesses in December more than offset by the loss of revenues from disposals made during the year.

## Trading margin

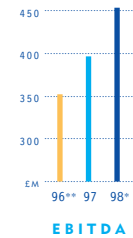
The trading margin, which is the proportion of sales turned into operating profit (excluding profits from associates and passive investments), was 13.1%, up from 11.5% in 1997. Taking into account changes in portfolio, restructuring charges and exchange rates, underlying profits increased by £26m (8%).

## Cash conversion

the proportion of operating profits received as cash in the full year, increased from 74% (after stripping out the exceptional impact on cash flow of the improper accounting at Penguin Putnam reported in the 1996 accounts but affecting 1997) to 101%. The much stronger cash performance in 1998 was a direct result of the work all Pearson's businesses, especially those in book publishing, did to improve cash flow. It was also helped by non-recurring cash items and timing variances, that we would not expect to be repeated in 1999. Free cash flow before Simon & Schuster integation costs was £255m, more than adequate to fund dividend payments of £116m. Free cash flow per share increased by 89% to 43.2p.

## EBITDA

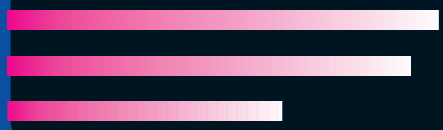
earnings before interest, tax, depreciation and amortisation, is increasingly used by investors as a measure of a company's underlying performance. In 1998, EBITDA, before exceptional items, increased by 16% to £455m.



## Adjusted earnings PER SHARE

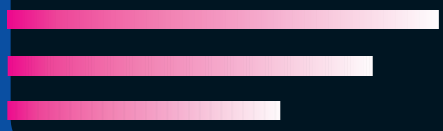
| | |
|---|---|
| **98** | 42.0p |
| **97** | 34.9p |
| **96** | 30.6p |

## Sales UNDERLYING GROWTH



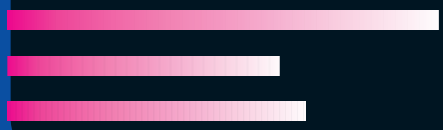
| | |
|---|---|
| **98** | 6.7% |
| **97** | 6.5% |
| **96** | 5.6% |

## Trading margin



| | |
|---|---|
| **98** | 13.1% |
| **97** | 11.5% |
| **96** | 9.2% |

## Cash conversion



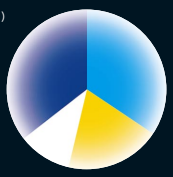
| | |
|---|---|
| **98*** | 101% |
| **97**** | 74% |
| **96** | 78% |

* Before exceptional costs
** Before impact of Penguin improper accounting

# The Results

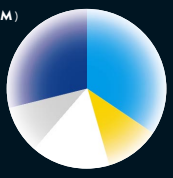
## Sales BY SECTOR (£M)

| | |
|---|---|
| Pearson Education | 702 |
| FT Group | 683 |
| Penguin Group | 523 |
| Pearson Television | 343 |



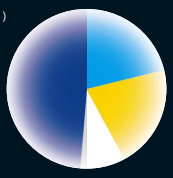
## Profit BY SECTOR* (£M)

| | |
|---|---|
| Pearson Education | 99 |
| FT Group | 118 |
| Penguin Group | 48 |
| Pearson Television | 61 |
| Lazard | 42 |



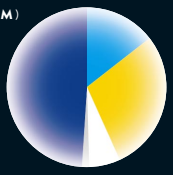
## Sales BY REGION (£M)

| | |
|---|---|
| North America | 1,078 |
| United Kingdom | 497 |
| Europe | 461 |
| Asia/Pacific | 161 |
| Rest of world | 54 |

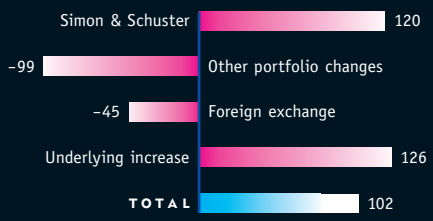


## Profit BY REGION* (£M)

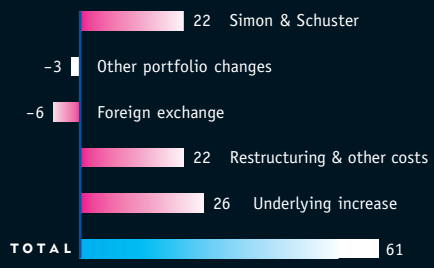
| | |
|---|---|
| North America | 181 |
| United Kingdom | 51 |
| Europe | 114 |
| Asia/Pacific | 16 |
| Rest of world | 6 |



## Underlying sales analysis (£M)



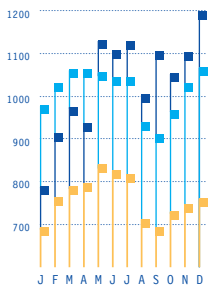

## Underlying profit analysis (£M)




* Before goodwill and other items

In 1998, Pearson's sales grew from £2,293m to £2,395m and operating profit, before goodwill and other items, from £328m to £389m. Profits at the FT Group rose by 9%, despite the disposal of non-core activities and substantial investment in the growth of the newspaper and electronic services. The continuing success of the *Financial Times* newspaper again contributed strongly to the overall performance. Pearson Education also increased its operating profits by 28%, before taking account of the contribution made in December by the Simon & Schuster businesses and the related integration charges. This growth was driven by the success of our US school business and the benefit of lower restructuring charges. The Simon & Schuster businesses, acquired at the end of November, recorded operating profits of £22m during December. The operating profit of the Penguin Group fell by 17%, due principally to several non-recurring items, including a £4m provision for the closure of the Ladybird site at Loughborough. Penguin UK, in particular, had a very strong year. Pearson Television's operating profits more than doubled to £61m, thanks in large part to a full year contribution from All American Communications, acquired at the end of 1997, and to a reduction in start-up losses from our investment in Channel 5.

As we continued to sharpen operations across Pearson in 1998, so we also continued to reshape the Company by building stronger market positions in a smaller number of businesses. We sold businesses that either lacked real market scale or which we believed were worth more to others than to Pearson. And we continued to dispose of passive investments which brought us no strategic value. We sold the Tussauds Group, Mindscape, Pearson New Entertainment, our specialist law, tax and medical publishing operations, our 20% stake in the *Canadian Financial Post*, our 6.3% stake in SES (the owners of the Astra satellite system), our stake in Flextech, and made a number of smaller disposals. In total, we raised £983m from these disposals.




***Pearson Share Price In 1998 (in pence)***

PEARSON

FTSE 100 REBASED

MEDIA SECTOR REBASED

We also continued to invest in building businesses in markets with good growth prospects where we have a chance to become a leading player. We'd begun this process with the acquisitions of Putnam Berkley in 1996 and All American Communications in 1997, which enabled Penguin and Pearson Television to build strong positions in consumer publishing and international television production. And we'd also started to make substantial revenue investment in the international and electronic expansion of the *Financial Times*. In 1998, we made our single biggest investment with the acquisition of the Simon & Schuster education, business & professional and reference divisions from Viacom Inc. for £2.9bn.

With this further tightening of our portfolio, focusing on a smaller number of larger, more actively managed and complementary businesses, where and how we make our sales and profits continues to shift. For example, in 1998, 31% of our sales were in education. In 1999, we expect that more than half will be. In 1998, 48% of sales from continuing operations were earned in North America and this is likely to increase significantly in 1999 as we consolidate the first full year results from the Simon & Schuster businesses.

As the changes in the Company's portfolio increased the proportion of sales and profits earned in overseas currencies, the strength of sterling had a modest but negative impact on our published results. If exchange rates had remained at 1997 levels, it is estimated that total sales would have been higher by £45m and operating profits by £6m. Stripping out the benefit of lower restructuring costs and portfolio changes and the adverse impact of exchange rates, underlying operating profit increased by 8%.

On the pages that follow, we describe our major businesses, reviewing their performance in 1998 and their plans for future growth.

# Pearson Education

**Education is a great growth industry. Global demand for educational materials and programmes is strong, consistently outstripping rises in GDP. Favourable demographics, the spread of public education in the developing world, and increasing demand to learn English are all factors driving this growth.**

In addition, governments, parents and students are all spending more on education. A worldwide drive to improve educational standards is generating a growing need for more effective teaching programmes. And the burgeoning use of computers in schools, colleges and at home stimulates the development of new products and services.

In the US, demand is expected to grow at around 8% per year over the next five years with estimates of some $6bn spent on printed and electronic educational materials in elementary, secondary and higher education in 1998. Outside the US, the international market in English Language Teaching (ELT) materials is of growing significance, with the British Council calculating that, around the world, there are some one billion people learning English. In indigenous markets, growth is more variable. In the short term, growth rates in some Asian and Latin American countries are being held back by the current economic conditions. But there is tremendous longer term potential. In Europe, annual growth of up to 10% is expected over the next few years, particularly in central and eastern European markets.

Bringing the Addison Wesley Longman (AWL) and Simon & Schuster businesses together to create Pearson Education has to be done with imagination, vigour – and great care. We have to achieve the efficiencies and economies of scale which will realise the anticipated savings and significantly improve trading margins. Most importantly, we must deliver the quality and relevance teachers and students alike expect from the world's leading educational publisher.

AWL performed well in 1998. Underlying sales increased by 8.5%, with operating profits, boosted by lower restructuring costs and tighter cost control, up by 28%.

Astronomy Today
PRENTICE HALL
*Comes complete with CD-ROM providing animation and videos, integrated links to a text-specific website and an interactive, self-scoring multi-media guide*

Baku Rekod Amali Sains
LONGMAN
*Practical science Level 1 workbook is our best selling title in Malaysia*

Longman Active Study Dictionary
LONGMAN
*If you're serious about learning English, this is the dictionary for you. This best selling title is aimed at intermediate learners of English as a second language*

The KnowZone
SCOTT FORESMAN
ADDISON WESLEY
*Makes the process of learning math interactive and enjoyable – and helps American schoolchildren pass their standardised tests*

In the US, AWL capitalised on strong market growth. It was the first year of major new math adoptions from kindergarten through to grade 8 in a number of Southern states. AWL's new math programme was a winner, gaining market share. Its competitiveness was enhanced by the launch of the KnowZone, a new internet based product. And another new electronic product, the Waterford Early Reading Program, contributed to good sales growth. The school business also did well in new biology and foreign language programmes. And by investing both in new authors and new technology, the higher education publishing group made strong progress.

Outside the US, the international business as a whole had to work hard just to mitigate the impact of lower growth rates in Asia and Latin America. There was a strong performance in the UK; the school publishing business gained market share in Hong Kong; and, although the ELT business did suffer in Asia, the fact that trading held up better than the economy as a whole, is encouraging for future years.

The Simon & Schuster businesses got off to a strong start with Pearson, contributing revenues of £120m and profits of £22m in December. Although the integration process started some months later than we had hoped, it is progressing well with a number of key milestones already met. It is on track to deliver $130m of annual costs savings by the end of the year 2000. And, as we run this dynamic business, we will also be committed to serving the cause of education and seizing our chance to play a full role in helping people learn all around the world.

*In the US, 20 states, which account for over 50% of the total US school population of some 52 million students, buy educational programmes by means of a periodic statewide 'adoption'. These cover new programmes in core subject areas. A state committee or commission selects a short-list of education programmes, from which the school districts choose their preferred programmes. In the 'open territories' – the 30 states without adoptions – local school districts choose educational programmes themselves.*

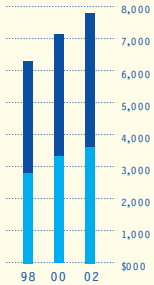
## Pearson Education in summary

***Pearson Education aims to be the world's leading educational publisher. Created in November 1998 through the merger of the Simon & Schuster and AWL education businesses, it boasts many of the most respected imprints in classrooms around the world, with a full range of outstanding electronic, as well as print, products and programmes.***

***The US school business supplies print and electronic educational programmes for use by teachers and students from kindergarten through grade 12. With more than 90% of education spending in the US financed at a state or local level, its major customers are education boards and school districts.***

***The US higher education business publishes programmes chosen by faculty but bought by 14 million students, who spend around $300 a year each on college materials. They are looking not just for textbooks but also for integrated, interactive, multi-media texts, teaching and testing programmes. Pearson Education is also the world's leading technology publisher, with a comprehensive range of books and electronic materials aimed at all audiences from computer novices through to IS&T professionals.***

***Outside the US, Pearson Education's international publishing business is the world's leading ELT publisher. It is also a leading publisher of indigenous works in the school, university and professional markets in countries all around the world.***




***Projected Sales Growth of US Education market, US Schools and US Higher Education sales of textbooks***

SOURCE: VERONIS, SUHLER & ASSOCIATES, INC.

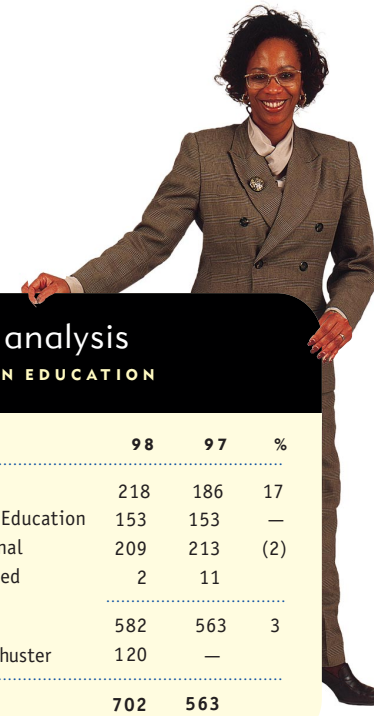
Tom Ahearn
MAIL CLERK
PEARSON EDUCATION
NEW JERSEY

## Sales
PEARSON EDUCATION

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| | 702 | 563 | 554 |

## Operating profit
PEARSON EDUCATION

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| | 99 | 60 | 60 |



## Sales analysis
PEARSON EDUCATION

| (£M) | 98 | 97 | % |
|---|---|---|---|
| US School | 218 | 186 | 17 |
| US Higher Education | 153 | 153 | — |
| International | 209 | 213 | (2) |
| Discontinued | 2 | 11 | |
| | 582 | 563 | 3 |
| Simon & Schuster | 120 | — | |
| **TOTAL** | **702** | **563** | |

Concha Ordoñez
EDITORIAL DIRECTOR
ALHAMBRA LONGMAN
MADRID

Janice McDonald
SEN. ADMIN. CO-ORDINATOR
PEARSON EDUCATION
NEW JERSEY

## Operating profit analysis
PEARSON EDUCATION

| (£M) | 98 | 97 |
|---|---|---|
| US School | 28 | 18 |
| US Higher Education | 23 | 20 |
| International | 26 | 22 |
| | 77 | 60 |
| Simon & Schuster | 22 | — |
| **TOTAL** | **99** | **60** |

Juliane Heinecke
ADMINISTRATION MANAGER
PEARSON EDUCATION
LONDON

Naresh Budhrani
HUMAN RESOURCES EXECUTIVE
PEARSON EDUCATION CHINA
HONG KONG

# The Penguin Group

**More people are buying more books than ever before. The global market for English language consumer books is currently valued at around $20bn a year. And it is set to grow by around 4% per year over the next five years. But the Penguin Group is looking to capitalise on the changing nature of consumer publishing to grow faster than the market as a whole.**

Rainbow Six
TOM CLANCY
*Another blockbusting best seller around the world*

The Beach
ALEX GARLAND
*A runaway best seller, soon a major motion picture*

Death of a Salesman
ARTHUR MILLER
*A special edition to mark its 50th anniversary*

Peter Rabbit
BEATRIX POTTER
*The perrenial children's favourite*

We are working more closely with book retailers, creating the potential to increase sales by taking a more sophisticated approach to merchandising and marketing. Internet retailing is reaching a new breed of customers who rarely set foot in a bookshop – sales of our books by internet tripled last year. Changes in technology are enabling Penguin to print, store, and distribute its titles more efficiently than ever before. For example, we expect to start 'printing on demand' some of our back-list titles in 1999.

We are continuing to build our front-list. In the US (where we are known as Penguin Putnam), we are increasing investment in balancing the front-list of brand name authors with new talent. Around the world, our imprints are working together to market new titles more effectively. For example, Tom Clancy's *Rainbow Six* was one of the first titles to be published simultaneously in all Penguin's major markets. And the power of the Penguin is helping us to break into new markets. Penguin Music Classics, which pair the most celebrated classical music with personal essays by some of the world's most renowned authors, is one of a number of initiatives to stretch the Penguin brand.

The Penguin Group's underlying profitability was up 6% over 1997. These underlying profits were impacted by a number of exceptional factors, including one-off restructuring costs to make the UK children's business stronger. We are making progress in putting Penguin on a much sounder commercial footing. In the US, sales per title increased by 13%, we increased our investment in new front-list signings, and returns fell below 30% for the first time in many years. In the UK, Penguin recorded good sales and profit growth. Cash flow across the Penguin Group was very strong.

In the US, Penguin Putnam published titles notched up a record 228 weeks on the *New York Times* hard cover best seller lists. Books by Putnam Berkley authors Tom Clancy, Patricia Cornwell, Nora Roberts and Dutton's James Van Praagh all reached the number one spot. It was a good year for Penguin Putnam's Young Readers' division, which is now the largest children's trade publisher in the US.

In the UK, Penguin was named Publisher of the Year at the annual British Book Awards. The award was well deserved. Penguin UK recorded its best front-list performance for many years, with six number one titles on the *Sunday Times* best seller lists and twice the number of top ten titles as in 1997. Its children's publishing division, buoyed by a Government initiative to encourage schools to give greater priority to reading in primary schools, turned in a strong trading performance. A strong front-list, led by *Jessica*, a new title by Bryce Courtenay, Australia's best selling author, enabled Penguin Australia to retain its position as the country's leading publisher.

The revived publishing platform that Penguin needed is now being put in place. Potential front-list sales are stronger than for many years as the Group steps up its investment in building new and established authors. The power of Penguin's brand and its international reach are now being realised. The way books are conceived, made, distributed and sold is changing more rapidly than in a generation, giving Penguin the chance to improve its margins and sustain stronger cash flow. Penguin now has a great opportunity to build a bigger, better and more profitable consumer publishing business.

## The Penguin Group in summary

***The Penguin Group is one of the world's most renowned English-language publishers. It publishes in all consumer formats for all English language markets, with pre-eminent market positions in the US, the UK, Australia, New Zealand, Canada and India. The Penguin Group publishes a well-balanced portfolio of fiction and non-fiction, literary and more commercial works. It combines a strong front-list of new books with a deep back-list of more than 25,000 titles. Penguin is also a leading publisher of children's books, featuring both renowned classic characters such as Spot and Peter Rabbit and best selling authors.***

***Penguin Imprints:***

**Penguin**

**Penguin Classics**

**Twentieth Century Classics**

**Michael Joseph**

**Hamish Hamilton**

**Viking**

**G.P. Putnam's Sons**

**Riverhead Books**

**Berkley Books**

**North American Library**

**Allen Lane**

**Dutton**

**Plume**

**Puffin**

**Ladybird**

**Frederick Warne**

**Penguin Business**

**Penguin Reference**

Alastair Rolfe
PUBLISHING DIRECTOR
THE PENGUIN PRESS
LONDON

## Sales
PENGUIN GROUP

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| | 523 | 525 | 380 |

## Operating profit
PENGUIN GROUP

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| | 48 | 58 | 27 |

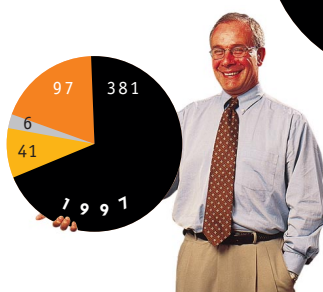
Paul Slovak
VP, PUBLICITY & SENIOR EDITOR
VIKING PENGUIN
NEW YORK

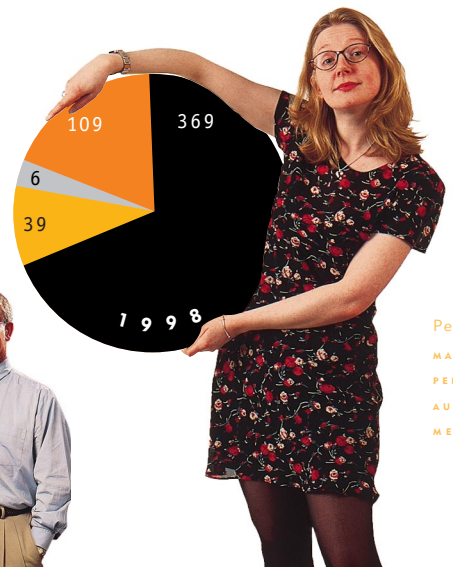
## Underlying operating profit analysis
PENGUIN GROUP

| (£M) | |
|---|---|
| 1997 operating profit | 58 |
| Portfolio changes | (3) |
| Foreign exchange | (2) |
| Restructuring and other | (8) |
| Underlying increase | 3 |
| **1998 OPERATING PROFIT** | **48** |

Tracy Tang
PRESIDENT & PUBLISHER
PUFFIN BOOKS, USA
NEW YORK

Auriol Bishop
SENIOR MARKETING OFFICER
PENGUIN UK
LONDON




Peter Field
MANAGING DIRECTOR
PENGUIN BOOKS,
AUSTRALIA
MELBOURNE

# Pearson Television

**As digital technology extends the number of television channels in homes throughout the world, the demand for popular entertainment continues to grow. We own and create the programme formats – game shows, serial dramas, action adventure and situation comedies – that have the universal appeal to meet this demand.**

First Wave
CANADA
*Sci-fi drama – boasts the first three season contract of any show on US cable television*

Fort Boyard
UNITED KINGDOM
*All action game show, boosting Channel 5's ratings*

Match Game
UNITED STATES
*Re-emergence in the US proves value of good formats*

The Adventures of Spot
UNITED KINGDOM
*We move into the animation business – and acquire the rights to Penguin property*

Salatut Elämät
FINLAND
*First episode of new daily drama attracted a record audience of 1.13 million*

Hinter Gittern
GERMANY
*Adapted from a cult Australian drama, HG captures the youth market*

The first and biggest challenge of 1998 was to complete successfully the integration of All American Communications. We did, creating a platform from which we can develop the next stage of the international growth of our business. The All American acquisition, completed in November 1997, helped boost revenues in 1998 by 39%. Operating profits, excluding Pearson's share of Channel 5 losses and income from BSkyB, increased by 54%.

The enduring popularity of our established shows in our four biggest markets – the UK, the US, Australia and Germany – continues to be the bedrock of the business. This is not something we can take for granted. Innovations in formats and story lines have kept our biggest shows on top, sustaining or improving their viewing audience shares. We have also enjoyed some success in developing new projects. For example, *First Wave*, a science-fiction drama distributed and co-produced by Pearson Television, has been sold to broadcasters in over 30 countries around the world. We are launching new productions from our library of game show formats, such as *MatchGame*, *100%* and *Family Feud* because we believe this genre is now back in business on US television. A number of new shows that we first produced for Channel 5 are winning audiences in new markets. And we extended our range of popular serial dramas, with new shows in Germany, Sweden, Hungary and Finland.

These successes were offset by more difficult trading conditions in a number of important emerging markets in Asia and Latin America. In these markets, demand for new programming has been suppressed by the general economic uncertainty. By December 1998, Channel 5 had increased its average weekly audience share of UK viewing, the key driver of future advertising revenues, to 4.6%. Pearson's share of Channel 5's start up losses, after amortisation of start up expenses, fell to £14m from £24m in 1997.

We have also made moves to secure Pearson Television's continuing growth. Through smaller acquisitions, we strengthened our production business in a number of important national markets. We have created our own television animation business, with Pearson Television and the Penguin Group working together to exploit the full potential of Penguin's extensive range of children's characters and literary rights. We are exploring the on-line potential of our game show formats and brands and developing partnerships to capitalise on other internet and interactive television opportunities. But, most importantly, in 1998, we won a greater number of new programme commissions, which will air around the world in the course of 1999 and keep the world watching Pearson Television productions well into the new millennium.

## Pearson Television in summary

***Pearson Television is the world's leading independent international television producer. It owns the largest selection of game show formats in the world, is the largest producer of serial dramas and makes a wide range of entertainment programmes, including action adventures and situation comedies. It makes most of these shows locally, using local production staff and adapting the formats to the indigenous language and culture. With more than 150 programmes in production in more than 30 countries around the world, television production generates over 70% of Pearson Television's annual revenues.***

***In the last four years, Pearson Television has grown rapidly through a number of acquisitions and, although its production business is now fully integrated, its programmes are produced under a number of household names – including Thames TV, Grundy and Fremantle.***

***Pearson Television is also active in a number of related businesses. Its US syndication business enables it to create a virtual broadcast network, selling programmes to more than 200 local television stations throughout the US in exchange for cash or airtime that it then repackages and sells to advertisers.***

***Through its international distribution business, Pearson Television sells its own programmes (it has a library of 15,000 hours of programmes stretching back through more than 30 years of television history) and those produced by other smaller, independent producers, to broadcasters in 100 countries around the world. It invests in broadcasting in markets where it will enhance the growth of its production or distribution business. It currently owns a 24% stake in the UK's Channel 5, a 20% stake in M-RTL in Hungary and a 20% stake in UKTV in Australia. And, from its studios in central London, Pearson Television also runs a fast growing transmission business.***

***Some of Pearson Television's most popular programmes in 1998:***

Baywatch
US, SYNDICATION
INT DISTRIBUTION

The Bill
UK, ITV

Salatut Elämät
FINLAND, MTV3

Skilda Världar
SWEDEN, TV4

Goede Tijden, Slechte Tijden
NETHERLANDS, RTL4

Neighbours
AUSTRALIA, NETWORK 10
UK, BBC1

Baratok Kozt
HUNGARY, RTL-KLUB

Gute Zeiten, Schlechte Zeiten
GERMANY, RTL

Verbotene Liebe
GERMANY, ARD

Unter Uns
GERMANY, RTL

Hinter Gittern
GERMANY, RTL

First Wave
CANADA, SPACE TV
INT DISTRIBUTION

***Pearson Television's catalogue of game show formats includes:***

THE PRICE IS RIGHT

FAMILY FEUD (FAMILY FORTUNES)

LYRICS BOARD

NIGHT FEVER

LET'S MAKE A DEAL

CARD SHARKS

100%

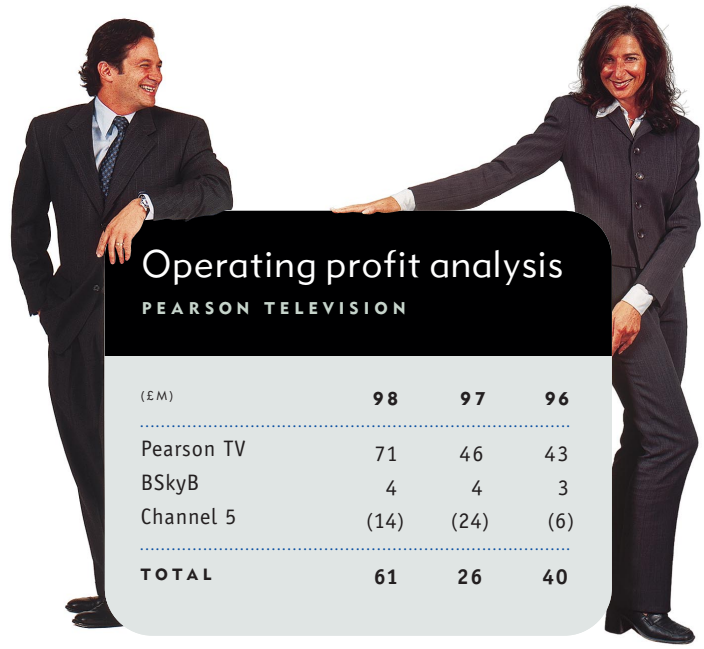
MATCH GAME (BLANKETY BLANK)

## Sales + operating profit

PEARSON TELEVISION

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| Sales | 343 | 247 | 204 |
| Operating profit | 61 | 26 | 40 |

Lizé Annick
PRODUCER
PEARSON TELEVISION
PARIS



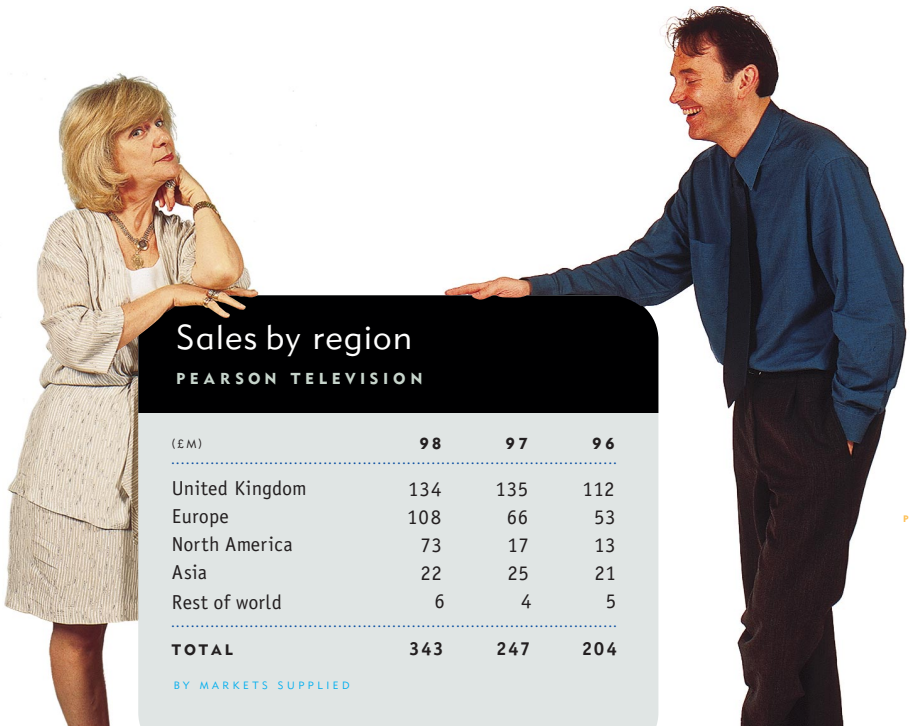
## Operating profit analysis

PEARSON TELEVISION

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| Pearson TV | 71 | 46 | 43 |
| BSkyB | 4 | 4 | 3 |
| Channel 5 | (14) | (24) | (6) |
| **TOTAL** | **61** | **26** | **40** |

Richard Mann
SENIOR VP, CREATIVE SERVICES
PEARSON TELEVISION
NEW YORK

Cathy Simon
PRIZE DIRECTOR
PEARSON TELEVISION
MELBOURNE



## Sales by region

PEARSON TELEVISION

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| United Kingdom | 134 | 135 | 112 |
| Europe | 108 | 66 | 53 |
| North America | 73 | 17 | 13 |
| Asia | 22 | 25 | 21 |
| Rest of world | 6 | 4 | 5 |
| **TOTAL** | **343** | **247** | **204** |

BY MARKETS SUPPLIED

Jan Russ
CASTING DIRECTOR
& ASSISTANT
PRODUCER
PEARSON TELEVISION
MELBOURNE

Philippe Thuillier
DIRECTOR GENERAL
PEARSON TELEVISION
PARIS

# The Financial Times Group

**Business is now global, and the demand for strategic business information – the combination of news, data, comment, analysis and context in which the FT Group excels – is growing fast. Most conservative estimates put the annual value of this market at some $10bn and anticipate growth of some 10% per year.**

Exxon and Mobil in merger talks
WRITTEN BY WILLIAM LEWIS
THURSDAY 26 NOV 98

Serial Utopia
WRITTEN BY CHRISTIAN TYLER
SAT/SUN 21/22 MARCH 98

The facts of life
WRITTEN BY DAVID PILLING
WEDNESDAY 9 DEC 98

The euro moves in next door
WRITTEN BY JEAN EAGLESHAM
SAT/SUN 15/16 AUG 98

Real-time accounts
WRITTEN BY PETER MARTIN
TUESDAY 2 MARCH 99

Bear necessities
WRITTEN BY WILLIAM LEWIS JAMES HARDING GEOFF DYER
SAT/SUN 26/27 SEP 98

This makes it a good time to invest in the international and electronic expansion of the Financial Times Group, building on the success of the newspaper to create a global business information brand. The FT Group made good progress in achieving this strategic objective in 1998, while also turning in a strong operating performance. Underlying revenue growth was up 12% and operating profits increased by 9% to £118m.

The *Financial Times* newspaper, the flagship of the Group, led the way. In 1998, we stepped up the revenue investment in its international expansion to some £20m, financing new print sites in Milan and Chicago, an improved distribution network in key US business communities and a sustained marketing effort. And the editorial content of the newspaper proved itself worthy of the investment. For example, the *FT* carried the earliest and most comprehensive coverage of the emerging economic crisis in Asia and was first to report many of the year's biggest global stories.

The financial and editorial investment paid off. In December 1998, average daily circulation topped 385,000, up 12.6% on December 1997. In continental Europe, the *FT* now consistently sells more than 100,000 copies a day – and a new survey confirmed that it is read by twice as many senior managers as any other English language publication. And in the US, circulation increased sharply to 70,000. With advertising revenue up 17% on the previous year, and the benefits of a more resilient cost base flowing through, the *FT* was able to post record profits – up 20% to £42m – while also sustaining the biggest investment in the newspaper's history.

Stripping out the benefit of lower restructuring costs and the impact of disposals made in the course of the year, FT branded businesses increased underlying operating profits by 7%. We increased our investment in the electronic expansion

of the Financial Times brand, establishing FT.com as the main gateway of all our existing electronic products. FT.com doubled its registered users to more than 1.4 million, making it Europe's leading business website and one of the top ten finance websites in the world. Although it generates more advertising revenue than any other website in the UK, this business is still very much at the development stage. We are continuing to invest in improving the content of the site, with more global company and market information, more extensive coverage of topics such as personal finance and more sophisticated search and interactive tools.

At FT Business, new management set about reducing costs through the more effective sharing of administrative and marketing roles, improving margins and providing the funds to invest in the more dynamic publishing engine that will drive its future growth. FT Asset Management also improved its margins by merging its IDC operations in the US and EXSHARE operations in the UK to create a unified global asset management business. It also notched up a third year of record new sales in the US and retained its competitive edge by investing in a number of new electronic products aimed at the US mutual funds and securities markets.

Strong circulation growth, strict cost control and buoyant advertising enabled Groupe Les Echos to increase operating profits by 33% to £12m. *Les Echos* strengthened its position as France's leading business daily newspaper, with circulation up 4% to over 114,600 and advertising revenues up 20%. We continued to invest in editorial and marketing support of the newspaper, lesechos.fr, which is the leading media website in France, and the business magazine, *Enjeux-Les Echos*, which increased its weekly circulation by 5% to 118,000.

In all our strategic business operations, we are investing in the expansion of the FT brand, building its already formidable reputation as the premier source of global news, comment and analysis.

*Pearson also aims to be the leading publisher of business news and analysis in important national markets throughout Europe. Groupe Les Echos is France's leading business newspaper and magazine publisher; Recoletos publishes the leading Spanish business and financial newspaper and has a 50% stake in its Portuguese counterpart. And The Financial Times Group and Gruner + Jahr, one of Germany's leading newspaper and magazine publishers, have formed a joint venture to produce a German language business newspaper.*

## The Financial Times Group in summary

***The Financial Times Group aims to be the authoritative source of strategic business information and analysis for senior managers around the world. The flagship of the Group is the* Financial Times *newspaper. Printed in twelve cities around the world, the FT gives more space and resources to global business events than any other newspaper. But its news and analysis stretches beyond business to international politics and economics, making it essential reading for a growing number of senior managers around the world.***

***FT branded businesses is a group of operations that aim to build on the strength of the Financial Times brand. FT.com aims to be the leading business portal on the web – a fast, flexible gateway to all the FT's electronic services. With a real-time news alert system, specialist company information and financial data, it holds records on 14,000 companies and has an archive of over four million articles from over 3,500 publications.***

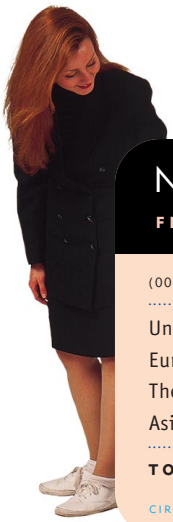
***FT Business spearheads the Group's efforts to add more specialist in-depth information to professionals throughout the world, specialising in the finance, energy, media and telecom sectors.***

***FT Asset Management, which trades as Interactive Data in the US and EXSHARE in the UK, is also focused on a highly specialist audience. It provides pricing, dividend, corporate action and descriptive information to trading houses, custodians and fund managers, and covers more than 3.5 million securities. Its databases are used by its clients to value many of the world's investment funds.***

Jon Banks
NATIONAL SALES DEVELOPMENT
FINANCIAL TIMES
LONDON

## Sales + operating profit
FINANCIAL TIMES GROUP

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| Sales | 683 | 676 | 692 |
| Operating profit | 118 | 108 | 89 |



## Newspaper circulation
FINANCIAL TIMES

| (000s) | 98 | 97 |
|---|---|---|
| United Kingdom | 180 | 180 |
| Europe | 119 | 101 |
| The Americas | 72 | 47 |
| Asia + rest of world | 14 | 14 |
| **TOTAL** | **385** | **342** |

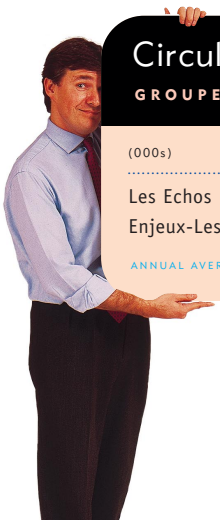
CIRCULATION AT DECEMBER SOURCE: ABC

Martha Ramirez
ADMINISTRATIVE ASSISTANT
FINANCIAL TIMES
NEW YORK

Kim Tomkins
MARKETING MANAGER
FT ELECTRONIC PUBLISHING
LONDON

## Operating profit analysis
FINANCIAL TIMES GROUP

| (£M) | 98 | 97 | % |
|---|---|---|---|
| FT Newspaper | 42 | 35 | 20 |
| FT branded businesses – continuing | 24 | 19 | 26 |
| FT branded businesses – sold | (5) | — | — |
| Les Echos | 12 | 9 | 33 |
| Recoletos | 30 | 30 | — |
| Associates | 15 | 15 | — |
| **TOTAL** | **118** | **108** | **9** |



## Circulation
GROUPE LES ECHOS

| (000s) | 98 | 97 |
|---|---|---|
| Les Echos Newspaper | 115 | 110 |
| Enjeux-Les Echos | 118 | 112 |

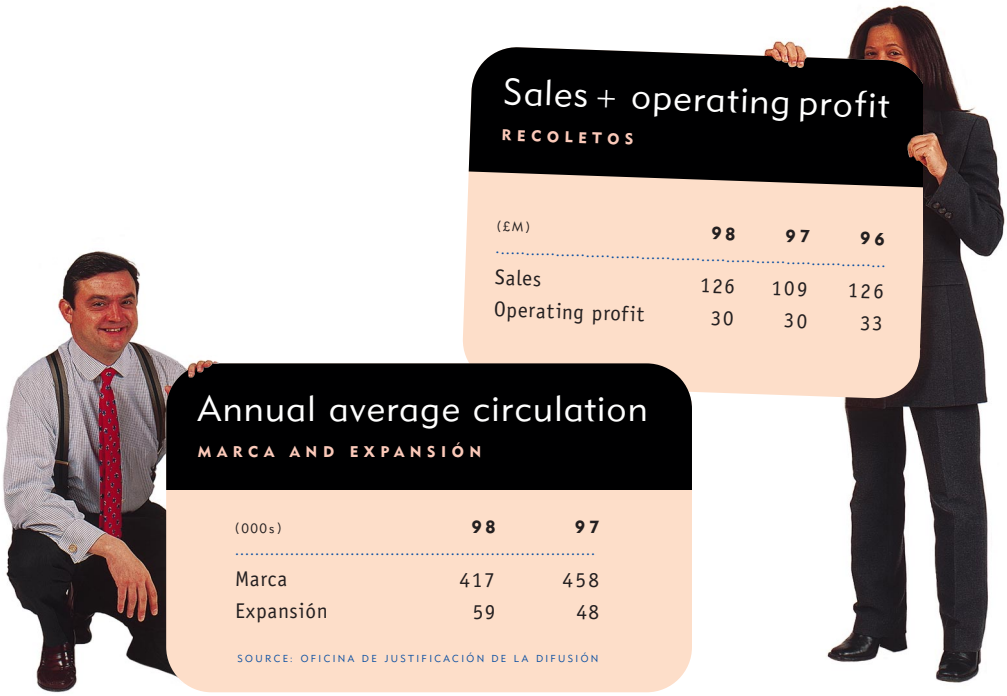
ANNUAL AVERAGE CIRCULATION

Nicolas Beytout
EDITOR IN CHIEF
LES ECHOS
PARIS

David Guiraud
CEO
GROUPE LES ECHOS
PARIS

Miguel Angel Belloso
DEPUTY EDITOR
EXPANSIÓN
MADRID

Silvia Ballesteros
BANKING EDITOR
EXPANSIÓN
MADRID



## Sales + operating profit

RECOLETOS

| (£M) | 98 | 97 | 96 |
|---|---|---|---|
| Sales | 126 | 109 | 126 |
| Operating profit | 30 | 30 | 33 |

## Annual average circulation

MARCA AND EXPANSIÓN

| (000s) | 98 | 97 |
|---|---|---|
| Marca | 417 | 458 |
| Expansión | 59 | 48 |

SOURCE: OFICINA DE JUSTIFICACIÓN DE LA DIFUSIÓN

**Spanish and Portuguese are important languages for Pearson. Recoletos is pursuing vigorously its strategy of building one of the most creative and profitable media groups in the Iberian Peninsula. It is also expanding into new markets in Latin America.**

*When it completes the acquisition of its stake in Unedisa, Recoletos and its partners will lead all other Spanish media groups with total daily newspaper sales of around 900,000. It will have a total circulation of around half a million for weekly and monthly magazines in the Iberian Peninsula.*

In 1998, in Spanish pesetas, Recoletos increased underlying sales by 16%. Profits were virtually unchanged as it invested heavily in new products and services and in improving *Marca*, Europe's leading sports newspaper. *Expansion*, boosted by editorial improvements in the newspaper and buoyed by a strong Spanish stock market, increased average daily circulation to a record 59,400, up 22% on the previous year, with advertising revenues up by 25%. *Marca's* circulation dipped by 9% to 417,000 as it faced increased competition from other daily sports newspapers and from more extensive sports coverage by other media. Circulation has picked up again in the first quarter of 1999. It is investing in increased colour printing, improved editorial and enhanced marketing to grow its still strong market leading position. *Expansion Financiera* was launched in October 1998 and is already attracting good viewing figures and significant advertising revenues throughout Latin America.

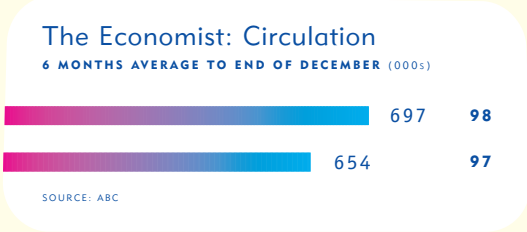
Recoletos is on track to complete the acquisition of up to a 30% stake in Unedisa, which publishes *El Mundo*, one of Spain's leading daily newspapers. It has completed the acquisition of a 50% stake in Economica, which publishes Portugal's leading daily financial and business newspaper. These acquisitions will help Recoletos to realise significant economies of scale in newsprint, printing and distribution across its newspaper operations. And with its active investment in *Economica*, Recoletos can apply its know-how in financial news and analysis in a fast growing market.

Recoletos is in a strong position to continue to grow in its domestic markets and, working with its partners and other Pearson businesses, it is better positioned than ever to grow rapidly in Latin America.

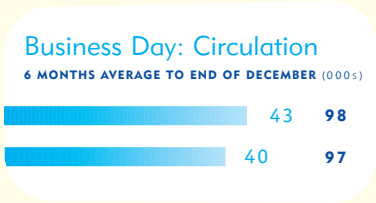
## Recoletos in summary

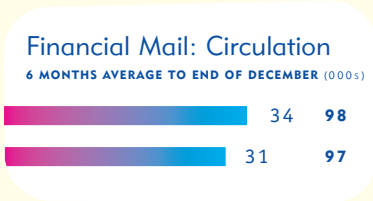
***Recoletos is one of the leading media groups in the Iberian Peninsula. It publishes Spain's leading financial and business publication,* Expansion, *and Europe's best selling sports newspaper,* Marca. *It will soon complete the acquisition of a significant stake – and play an active management role – in Unedisa, which publishes* El Mundo, *one of Spain's leading daily newspapers and owns a stake in* Economica, *which publishes Portugal's leading daily financial and business newspaper. Recoletos is working in alliance with Telefonica, Spain's leading telecommunications company, to broaden its reach both within Spain and in the Spanish and Portuguese speaking Latin American markets. It has a 10% stake in the broadcaster Antena 3 and has recently launched a business television channel, Expansion Financiera, which is broadcast from Madrid to Spanish and Latin American financial centres on the satellite digital platform, Via Digital.***

**The Economist** Pearson owns a 50% stake in The Economist Group, which publishes the world's leading weekly business and current affairs journal. It also provides data and perspectives on the world's countries through the Economist Intelligence Unit and information for special communities of interest in government, the professions, trade and transportation. In 1998, the Group had another good year. Circulation of *The Economist* increased to 697,194 from 654,000 in 1997 and, across the Group, it continued to move paper-bound publications to electronic formats and invest in new products and infrastructure.

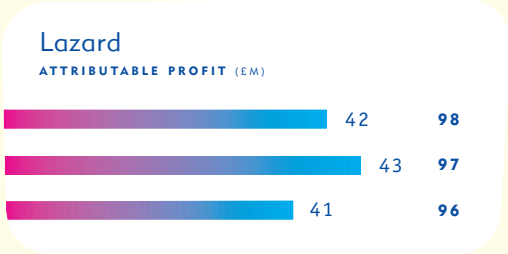



**Business Day/Financial Mail** the South African publishing business, in which we own a 50% stake, performed well meeting expectations for copy sales and advertising revenue growth despite the difficult economic climate in the autumn. For the six months to end of December, both publications grew circulation to record levels. Average sales of *Business Day* rose to 43,000, up by 7.5%, compared to 1997, and *Financial Mail* rose to 33,800, also up 7.5%.




**Lazard** Pearson owns, directly and indirectly, a 50% interest in Lazard Brothers the UK merchant bank, and smaller holdings in the Lazard banking houses in New York and Paris. In 1998, Lazard turned in good profits, sustaining a strong deal flow across all three houses and coming close to matching the exceptional contribution to our profits of 1997. In the UK, Lazard Brothers advised on many of the year's major mergers and acquisitions. And Lazard Asset Management continues to enjoy strong growth.



# Financial review

## Simon & Schuster

The acquisition of Simon & Schuster has had a significant impact on the 1998 Accounts in the following areas:

**Exceptional items** Pearson recorded significant exceptional charges of £120m against 1998 operating income relating to the acquisition of Simon & Schuster. Provisions of £72m were made for the cost of integrating our education companies. Further integration costs are anticipated in 1999 though we do not expect the charge for the two years taken together to exceed £190m. In addition a charge of £27m was made to reflect the alignment of certain Addison Wesley Longman accounting bases with those of Simon & Schuster and a write-down of £37m was taken relating to assets created for the implementation of the Pearson Shared Services Project which are no longer required since Simon & Schuster had already developed its own equivalent project.

### Simon & Schuster

EXCEPTIONAL COSTS

| | $M | £M |
|---|---|---|
| 1998 integration costs | 119 | 72 |
| AWL accounting basis alignment | 45 | 27 |
| Shared Service write down | 61 | 37 |
| | 106 | 64 |
| Total | 225 | 136 |
| Analysed as: exceptional costs | | 120 |
| Analysed as: non operating costs | | 16 |

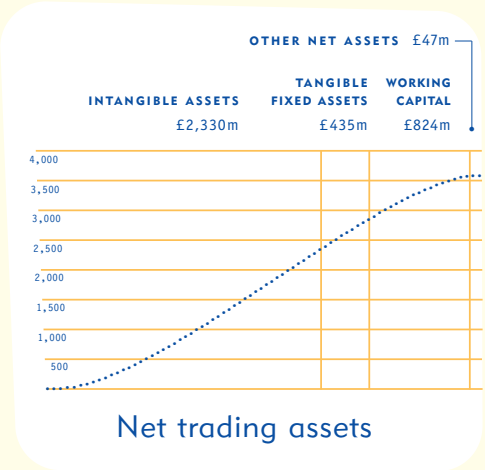
**Goodwill** The acquisition of Simon & Schuster has resulted in the recording of substantial goodwill, the difference between the purchase price paid and the net tangible assets acquired, on the Group's balance sheet. The goodwill will be amortised over a period of 20 years, in accordance with an accounting standard discussed in greater detail under 'accounting policies' on page 38, and has given rise to a charge of £10m in 1998. A full year charge in respect of Simon & Schuster of approximately £120m will be recorded from 1999 onwards. The charge has no impact on the Group's cash flow and is excluded from the calculation of adjusted earnings in order to show results on a comparable basis.

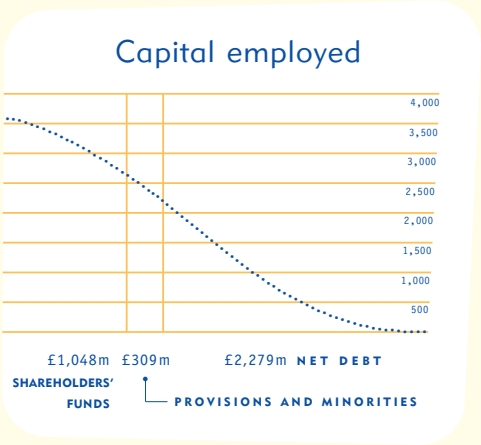
**Business & professional and reference assets** Pearson announced in May 1998 plans to sell on the business & professional and reference assets acquired as part of the Simon & Schuster transaction to Hicks, Muse, Tate & Furst Inc., a US leveraged buy-out firm. This transaction was not completed and accordingly Pearson has inherited these assets. It is Pearson's intention to retain Macmillan Computer Publishing and New York Institute of Finance, the majority of the assets by value, but to dispose of the remainder. The businesses being held for resale have been recorded in the balance sheet at their estimated disposal proceeds of $275m less costs.

**Provisional fair value adjustments** have been made to the Simon & Schuster net assets acquired and these are set out in note 25 to the accounts. They reflect adjustments to harmonise certain Simon & Schuster accounting policies with those of Pearson Education; the revaluation of net assets to their 'fair value'; and the inclusion of the anticipated proceeds from the sale of certain business & professional and reference assets referred to above. Since the acquisition was completed so close to the year end further fair value adjustments are anticipated in 1999.

### Provisional fair value adjustments (£M)

| | BOOK VALUE | ACCOUNTING POLICY ALIGNMENT | REVALUATIONS | OTHER | FAIR VALUE |
|---|---|---|---|---|---|
| Fixed assets | 137 | — | (9) | (2) | 126 |
| Current asset investments | — | — | — | 151 | 151 |
| Working capital | 516 | (50) | (71) | (26) | 369 |
| Other | (84) | — | (6) | — | (90) |
| | 569 | (50) | (86) | 123 | 556 |




**Loan facility** In order to finance the Simon & Schuster transaction, Pearson negotiated a $6bn loan facility with a group of international banks. This loan facility, which also refinanced all existing structured bank debt, has three elements:

**1.** A 364 day revolving credit facility (initially for $1.5bn but reduced by cancellation to $349m at the balance sheet date) maturing in May 1999;
**2.** A term revolving credit facility (for $2bn) which begins to amortise in May 2000 and matures in May 2003;
**3.** A term loan facility (for $2.5bn, of which $2.21bn was drawn at the balance sheet date) which begins to amortise in May 2000 and matures in May 2003.

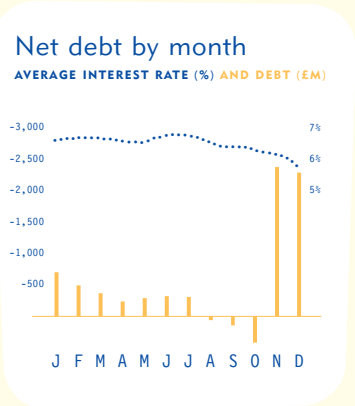
There are two key covenants under the terms of this loan facility, one an interest cover covenant and the other a net debt to EBITDA (earnings before interest, taxation, depreciation and amortisation) covenant. The Group does not currently foresee any difficulties in complying with the terms of these covenants.

## Non operating items

Non operating items were again significant in 1998 following the disposal of a number of non-core businesses and these helped boost pre-tax profits from £129m in 1997 to £629m. The disposals of Pearson New Entertainment and The Tussauds Group yielded non operating profits of £41m and £157m respectively whilst the disposal of the investment in Société Européenne des Satellites resulted in a non operating profit of £133m.

## Interest

Net interest fell slightly to £39m but this figure does not tell the whole story as there were several significant factors which affected the overall financing position of the Group. Debt fell over the first 10 months of the year as the businesses generated cash and proceeds were received from the businesses sold as well as from our equity issue which raised £327m in August. Although floating interest rates in both sterling and US dollars fell during the last four months of the year, taking the year as a whole they were higher in 1998 than 1997 in sterling and virtually unchanged in US dollars.



However, the acquisition of Simon & Schuster at the end of November increased year end net debt to £2.3bn and added approximately £12m to the interest charge for the year. Future gross debt levels are likely to be nearer to the year end debt figure of £2,624m than the levels of previous years and so a significantly higher interest charge will be a feature of the Pearson profit and loss account in the forseeable future.

Interest cover, defined as the ratio of operating profit before exceptional items and goodwill amortisation to net interest payable, stood at 10 times.

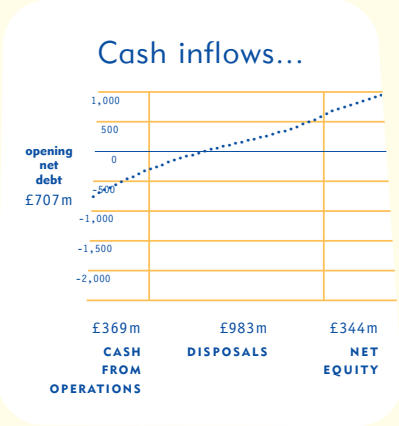
## Taxation

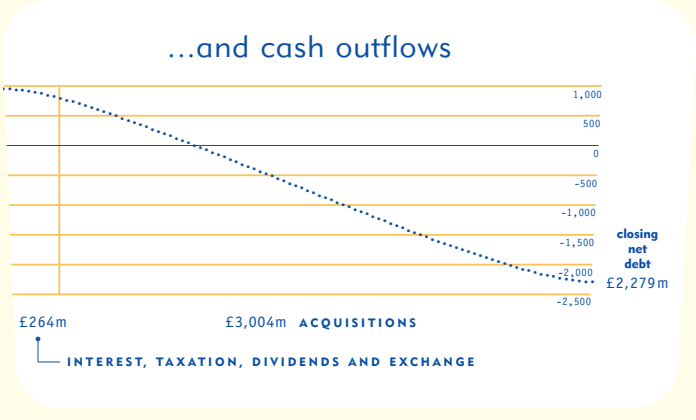
The tax charge of £188m represents an effective rate of 29.9% on profit before taxation of £629m. The comparable 1997 effective tax rate of 68.9% was abnormally high because there was no current tax relief for a charge of £212m in respect of Mindscape goodwill; excluding this factor the 1997 effective tax rate was 26%. The increase from 26% to 29.9% is largely accounted for by the fact that only limited tax relief has been recognised on the Simon & Schuster integration costs in 1998. The overall tax rate on items excluded to arrive at adjusted earnings was 32.3%; the effect of the treatment of the Simon & Schuster provision was largely offset by the fact that, as in 1997, the tax rate on profits on disposals benefited from the use of losses brought forward and from indexation and other differences between book and tax bases for the calculation of gains.

The tax rate on adjusted earnings fell from 29.4% to 28%. As in 1997, the availability of tax losses in the US meant that no significant tax needed to be provided on the Group's profits arising there, and this factor alone largely accounted for the difference between the UK statutory rate of 31% and the effective rate of 28% on adjusted profits. The 1998 tax rate also benefited from the release of some provisions for earlier years' tax following settlement of the liability for those years, and this factor more or less offset the effect of disallowed expenses and the Group's exposure to higher tax rates in countries other than the UK and the US.

## Minorities

Minority interests increased in 1998 to £4m following the strategic alliance with Telefónica, Spain's leading telecommunications company, which took a 20% stake in Recoletos at the start of the year.



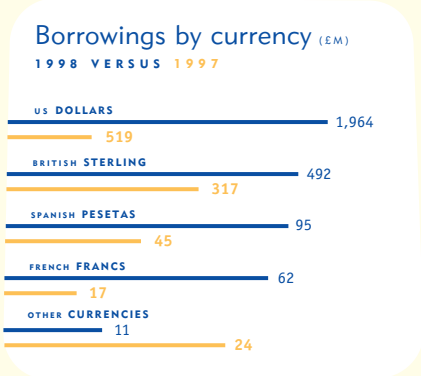
# Financial policy

**Dividend policy** Pearson has a long unbroken record of increasing the dividend paid to shareholders. The Company's management is committed to build on that tradition, increasing dividends at a rate comfortably in excess of UK price inflation. At the same time, management sees opportunities to earn a return in excess of the Company's cost of capital through investment in the business and has therefore stated an objective of rebuilding dividend cover (adjusted earnings per share expressed as a multiple of net dividend per share) to a minimum level of two times. In making a dividend recommendation to shareholders the board also takes into consideration the level of the Company's free cash flow. In addition, the board will consider the return of capital to shareholders when that course of action is justified by a high level of corporate liquidity, a shortage of investment proposals which meet our criteria or the level of the Company's share price. The board is recommending to shareholders a final dividend of 13p, making a full year total of 21p, representing an increase of 8% on the 1997 total. The recommended dividend is covered twice by adjusted earnings and will be fully funded from 1998 free cash flow.

**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 from 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, sterling and euro 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 1998. A treasury committee of the board receives reports on the Group's treasury activities, which are also 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. At the beginning of the year the Group's objective was that at least one-third of its sterling and US dollar borrowings (taken at the year end, net of cash) should be hedged (ie fixed or capped). At the end of 1998 that ratio was 32%. In connection with the acquisition of Simon & Schuster, during the year the Group decided to increase the hedged proportion, particularly for the years 1999 and 2000. In particular it entered into interest rate swaps for a nominal amount of $600m which will only become effective during 1999. Taking into account these swaps together with other hedging transactions effected since the year end, on a pro forma basis the proportion of sterling and US dollar net borrowings which were hedged at the end of 1998 was 53%. On that pro forma basis a 1% change in the Group's variable sterling and US dollar interest rates would have an £11m effect on its profit before tax. The Group intends to increase further the fixed rate element of its borrowings in 1999.

**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. It has a policy that the weighted average maturity of its core gross borrowings (treating short term advances as having the final maturity of the facilities available to refinance them) should be between three and eight years, and that non bank sources should provide between 25% and 75% of such core gross borrowings.

At the beginning of the year, the average maturity of such core gross borrowings was 6.1 years, and non-banks provided approximately 51% of them. The acquisition of Simon & Schuster at the end of November was financed with a combination of the cash previously received from disposals and an equity issue and drawings under the new bank facility. At the end of 1998 the average maturity of gross borrowings was 4.4 years, and non banks provided approximately 18% of them. It is the Group's intention to extend the average maturity of its borrowings through refinancing the bank facility by issues in the medium term capital markets.

Borrowings: fixed & floating (£M)

| | 1998 PRO FORMA | 1998 | 1997 |
|---|---|---|---|
| Floating rate | 1,408 | 1,905 | 642 |
| Fixed rate | 1,216 | 719 | 280 |

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. In the course of considering in March the terms on which it would be prepared to acquire Simon & Schuster, the Group concluded that its improved business risk profile following the acquisition, taken together with the prevalence of low inflation and interest rates in its key markets, would support a higher level of financial risk and, accordingly a lower level of interest cover. Following the success of its bid the Group's long term credit ratings were reduced from A2 to Baa1 by Moody's and from A to BBB+ by Standard & Poor's, and its short-term ratings from P1 to P2 and A1 to A2 respectively. The Group intends, however, to 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 1998 these amounted to £835m, and their weighted average maturity was 2.7 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 ratings (among other things) into account, are approved by the Group finance director.

**Currency risk** Although the Group is based in the UK, it has a significant investment in overseas operations. The acquisition of Simon & Schuster greatly increased the amount of the Group's trading which is conducted in the US dollar, making it by far the most important currency for the Group, although the value of its operating profits from sterling and the euro bloc are also significant.

In 1997 the Group determined that transactional conversions between currencies (for example, to pay receivables, payables or interest) should be effected at the relevant spot exchange rate. This policy continued to be followed in 1998. As in previous years, no unremitted profits were hedged with foreign exchange contracts. During the year the Group reviewed and amended its policy for the use of foreign currency debt. At the beginning of the year the policy was normally to borrow in each principal foreign currency around 20% of the capital employed (inclusive of purchased goodwill) in that currency. The policy has been amended to align the composition of the Group's debt more closely with the currency in which operating profits arise. Long term core borrowing is now limited to the US dollar, sterling and the euro, reflecting their collective share of total Group operating profit. However, the Group still borrows small amounts in other currencies, typically for seasonal working capital needs.

The new policy aims to dampen the impact of changes in foreign exchange rates on consolidated interest cover and earnings. At the year end US dollar borrowings accounted for 75% of total borrowings, sterling

borrowings for 19%, Spanish peseta borrowings for 4% and French franc borrowings for 2% (so that pro forma euro borrowings accounted for 6%).

**European Monetary Union** With over 50% of the Group's sales outside continental Europe and the UK, even prior to the impact of the acquisition of Simon & Schuster, the introduction of the euro is not an issue for sizeable parts of the Pearson Group. Those businesses affected have focused in 1998 on preparation for the treasury and related administrative issues and on completing strategic reviews of the impact of the euro on their competitive environments. Recoletos, Les Echos and other business units based in continental Europe have been working in dual currencies with little or no difficulty since 1 January 1999. Within the UK based businesses, the FT Group has been most affected, with FT Information launching an entire portfolio of euro-based products on 1 January 1999. All UK operations have established contingency plans in the event the UK decides to join the euro-zone. The financial costs of preparations for the euro have not been material to the Group.

**Accounting policies** The significant accounting policies of the Group are shown on pages 58 and 59. During the year a number of new UK Financial Reporting Standards were either issued or became effective. FRS9 'Associates and Joint Ventures' has been implemented with the result that the profit and loss account now shows separately the operating profit and interest from associates and additional disclosure is given in the notes. The prospective implementation of FRS10 'Goodwill and Intangible Assets' has significantly changed the appearance of both our profit and loss account and balance sheet. Purchased goodwill is now required to be shown as an asset on the balance sheet and amortised over its useful economic life, presumed to be not greater than 20 years unless shown otherwise. The amortisation charge is taken through the profit and loss account. In order to show results on a comparable basis, this goodwill amortisation has been excluded from adjusted earnings.

FRS13 'Derivatives and Other Financial Instruments', which requires additional narrative and numerical disclosures in respect of financial instruments, has been implemented as has FRS14 'Earnings Per Share' which has also added to the disclosure requirements, now requiring diluted earnings per share to be shown in addition to changing the calculation of the weighted average number of shares in issue.

FRS12 'Provisions, Contingent Liabilities and Contingent Assets' will be adopted in the 1999 Accounts although the provisions held in the balance sheet at December 1998 do meet the criteria imposed by the new standard. The effect of the standard is to relate the timing of provisions more closely to the period in which the sums provided will actually be spent.

**Risk management** The Group control department, which has an independent reporting line to the Audit Committee, checks our effectiveness at managing risk. Through regular audits and reviews, it seeks to identify under-managed risks, and then works with the responsible line management to resolve any issues arising. This includes ensuring that the policies and procedures operating throughout the Group, which were reviewed and revised during 1998, are suitably comprehensive and up-to-date.

All the main operating companies in the Group are visited regularly by members of Group control. Smaller companies not visited are required to complete control and risk assessment questionnaires. Responses are monitored by Group control in conjunction with the divisions and appropriate actions are taken to mitigate any under-managed risks.

The acquisition of Simon & Schuster presents the Group with considerable challenges, as well as great potential for growth and efficiencies. The integration of the Simon & Schuster and AWL businesses into Pearson Education is managed by a Steering Committee which has board representation. This group has been working for several months with the line managers selected to lead the combined organisation on the key decisions and processes required to ensure a smooth integration into the new division. Group control monitors progress against plan and undertakes various audits and reviews to support an efficient and timely integration.

# Board of directors

## Chairman

**Sir Dennis Stevenson** chairman, aged 53, has been a non-executive director of Pearson since 1986 and became executive chairman in 1997. He is also chairman of AerFi Group plc, a non-executive director of British Sky Broadcasting Group plc and of Manpower Inc. in the US.

## Executive directors

**Marjorie Scardino** chief executive, aged 52, 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 W H Smith Group plc and of ConAgra Inc.

**David Bell** aged 52, became a director of Pearson in March 1996. He is chairman of the Financial Times Group, having been chief executive of the *Financial Times* since 1993. 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 chairman of the Millennium Bridge Trust.

**Greg Dyke** aged 51, has been chairman and chief executive of Pearson Television since 1995. He became an executive director of Pearson in March 1996 and is also chairman of Channel 5 Television Group Limited and a non-executive director of Manchester United plc.

**John Makinson** aged 44, 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

**Michel David-Weill** aged 66, is chairman of Lazard Partners, deputy chairman of Lazard Brothers, chairman of Lazard Frères, New York, and managing director of Lazard Frères, Paris as well as a director of a number of companies, including Groupe Danone and ITT Industries Inc. He joined the Pearson board in 1970.

**Gill Lewis**[+] aged 55, is the managing partner of Heidrick & Struggles in the UK and Eire. She became a non-executive director of Pearson in 1992.

**Reuben Mark**[*+] aged 60, is chairman and chief executive of the Colgate Palmolive Company and a director of Citigroup Inc. and Time Warner Inc. He became a non-executive director of Pearson in 1988.

**Vernon Sankey**[*] aged 49, was previously chief executive of Reckitt & Colman plc and is a non-executive director of Allied Zurich plc. He became a non-executive director of Pearson in 1993.

**David Verey**[*] aged 48, joined Lazard Brothers in 1972 and became its chairman in 1992. He was appointed an alternate director of Pearson in 1995 and became a non-executive director in 1996.

## Directors who retired during the year

**David Veit** retired from the board at the Annual General Meeting on 1 May 1998 after 25 years with Pearson, including 17 years on the board.

[*] *A member of the audit committee.* [+] *A member of the personnel committee.*

# Report of the directors

***The directors are pleased to present their report to shareholders, together with the financial statements for the year to 31 December 1998 on pages 54 to 88. Details of the businesses, the development of the Group and its subsidiaries and likely future developments are given on pages 12 to 35 of this annual report. Sales and profits of the different sectors and geographical markets are given on pages 60 and 61.***

**Results and dividend** The profit for the financial year to 31 December 1998 was £437m (1997: £38m). The profit retained for the year was £311m (1997: loss £74m) and has been transferred to reserves. A final dividend of 13p per share is recommended for the year ended 31 December 1998. This, together with the interim dividend already paid, makes a total for the year of 21p (1997: 19.5p). The final dividend will be paid on 4 June 1999 to shareholders on the register at the close of business on 26 March 1999, the record date.

**Dividend reinvestment plan (DRIP)** The Company has, in common with many other *FT-SE 100* companies, decided to terminate the current share dividend plan and to replace it with a dividend reinvestment plan with effect from and including the final dividend for the year to 31 December 1998. The new plan will provide similar benefits by giving shareholders the right to buy the Company's shares on the London stock market with the cash dividend. Full details of the new plan will be sent to shareholders on 26 April 1999.

**Significant acquisitions and disposals** Details of these transactions can be found in notes 25 and 26 to the accounts on pages 79 to 82 and on pages 12 to 35.

**Transactions with related parties** Details of transactions with related parties, which are reportable under FRS8, are given in note 30 to the accounts on page 84.

**Capital expenditure** The analysis of capital expenditure and details of capital commitments are shown in note 12 to the accounts on page 68.

**Directors** Biographical details of the directors who served throughout the year are shown on page 39. Details of their remuneration and interests in ordinary shares and options of the Company are contained in the personnel committee report on pages 46 to 52. Three directors, Greg Dyke, Dennis Stevenson and David Verey, will retire by rotation at the forthcoming annual general meeting (AGM) on 30 April 1999. All three, being eligible, will offer themselves for re-election. Details of directors' service contracts can be found on page 48. 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. The 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 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 non-executive directors as it considers that the most formal and transparent procedure for the appointment of a new non-executive director is for this to be a matter for the whole board.

The Company also complies with the best practice provisions on remuneration committees prescribed in Section A of the annexure to the Listing Rules of the London Stock Exchange, and has done so throughout the year ended 31 December 1998.

**The board** The board currently comprises five executive directors, including the chairman, who is part-time, and five non-executive directors. The majority 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. Michel David-Weill and David Verey are not considered to be independent under the terms of the Code due to their connection with the Company through Lazard Frères and Lazard Brothers, respectively, but excuse themselves from discussions of all matters related to the Company's holdings in these businesses. A selection process is currently being undertaken by the board with a view to appointing an additional non-executive member.

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:

***Audit committee*** This committee is chaired by Vernon Sankey and its other members are Reuben Mark and David Verey. 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.

***Personnel committee*** This committee is chaired by Gill Lewis and its other member is Reuben Mark. Both 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 and reviewing the Group's management development and succession plans. The board considers three members to be the ideal number in line with the recommendations of the Greenbury Report and intends to appoint an additional non-executive member following the completion of the selection process currently being undertaken by the board. The committee reports to the full board and its report, which has been considered and adopted by the board, is set out on pages 46 to 52.

***Treasury committee*** This committee comprises the finance director, one other executive director and one non-executive director namely, John Makinson, Dennis Stevenson and David Verey. The committee sets the policies for the Company's treasury department and reviews its procedures on a regular basis.

**Internal financial control** The board of directors has overall responsibility for the Group's system of internal financial controls, which it exercises through an organisational structure with clearly defined levels of responsibility and authority, and appropriate reporting procedures. This structure includes the audit committee which, with the finance director, has reviewed the effectiveness of the internal financial control environment of the Group. The audit committee meets regularly and considers, inter alia, reports from internal and external auditors covering such matters.

The directors consider that the Group's system of internal financial controls is appropriately designed to provide reasonable but not absolute assurance against material misstatement or loss. The main elements of these internal financial controls are as follows:

***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 but conforming to Group standards and guidelines. These include procedures to identify and then mitigate financial, operating and compliance risks.

***Self assessment*** Each year, chief executives of the main operating companies are required to certify that they had in place, throughout the year, a comprehensive system of controls and that they have conducted a review of the effectiveness of those internal controls. The Group control department reviews the chief executives' submissions and reports its conclusions to the audit committee.

***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 taken by the directors as appropriate.

***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.

***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, systems and procedures in all main operating companies, agrees with operating companies their plans to mitigate risks and improve controls and systems, and reports regularly to the audit committee. Group control ensures that operating companies take steps to eliminate or mitigate these risks where possible. For further details on Group control see page 38 of the financial review.

***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.

During 1999, the directors will undertake a review of the internal control system in the light of the Code provision D2.1 and will report on the results of the review next year, after guidance from the Turnbull Committee has been issued. In the meantime, as allowed by the London Stock Exchange, the directors continue to report on their review of internal financial control.

**Going concern** Having reviewed the Group's liquid resources and borrowing facilities, and the 1999 and 2000 cash flow forecasts contained in the Group budget for 1999, 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.

**Year 2000** Like all other companies, the Year 2000 issue presents a significant risk to the Group. Pearson is very aware of the need for all its products, services and computer systems, as well as those of its suppliers and customers, to be Year 2000 compliant. To achieve this end it established an overall Year 2000 programme in 1997 led by John Makinson, the finance director, with the full support of the board. Progress on the overall project is reported to the board on a regular basis.

An overall Group timetable was established to which all Pearson operating companies were required to work. By the end of January 1999, remedial work and thorough testing of all systems had been completed such that all operating companies within the Pearson organisation, apart from the Simon & Schuster businesses, had achieved material internal Year 2000 compliance. Activities being undertaken in the overall project include understanding legal implications, dealing with the embedded system issue as it relates to all equipment and facilities, and co-ordinating with key suppliers and customers.

At the end of November 1998, Pearson acquired the Simon & Schuster businesses which now form part of Pearson Education. These businesses have similarly been working towards the achievement of Year 2000 compliance, but to varying timescales. A co-ordinated worldwide programme has been reaffirmed for this new part of the organisation and is being overseen by the Pearson Year 2000 programme office. Plans are now fully established to accomplish the significant work yet to be done. This work is progressing to schedule with the aim of achieving material compliance by the end of August 1999.

Pearson is highly sensitive to the risks associated with its key suppliers and customers. The continuity of supply of services from the providers of telecommunications and power represents a particular risk to the Group. All operating companies are in correspondence and discussion with their key suppliers and customers to ensure that the state of Year 2000 readiness of each is fully understood.

The Group will work throughout 1999 to ensure that, in so far as possible, compliance is maintained, to plan for the move into the new millennium and to prepare contingency plans to deal with any business disruption which may arise.

As at January 1999, the estimated cost to resolve the Year 2000 problem for the whole of Pearson is £19m of which £5m remains to be spent. These figures include all remedial work, upgrades, hardware replacement and additional external resources. However, they do not include the cost of internal resources, nor the introduction of new IT systems where there are significant functional enhancements, over and above simply resolving the Year 2000 issue. Where new systems are required to support the ever-changing business needs and also resolve any Year 2000 problems, these replacement systems are being accounted for in the normal way.

**Shareholder communications** Management continues to develop, increase and improve communications 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 1998 results and general AGM business. In addition, Pearson has developed a comprehensive institutional investor communications programme, as well as communicating with employees.

**Employment** The average number of Group employees in 1998 was 18,400, of whom some 7,903 were employed in the UK. 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 (i.e. the Disability Discrimination Act 1995 in the UK) 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 a non-disabled person.

***Training and development*** The Group is committed to the improvement of performance through training and development of its employees. In addition to development opportunities offered by the Group, operating companies have their own programmes and courses to meet the needs of their employees and their business. Pearson also encourages employees to develop their careers by taking up opportunities in other parts of the Group.

***Employee participation*** The directors believe that the key to the success of the Company lies in a motivated workforce. In 1998, Pearson completed the implementation of the incentive and reward programmes first announced under the heading 'Changegear' the previous year. This included a Group profit sharing plan and the Worldwide Save for Shares plan. For success in 1998, eligible

employees will receive a cash bonus and an award of Pearson shares under the Group profit sharing plan. Under the Save for Shares plan, employees worldwide have been given the opportunity to save from their pay and acquire Pearson shares. About one-third of eligible employees took up this offer in 1998 and the Company plans to make a similar offer in 1999. In 1998, shareholders approved a reduction in the qualifying period to take part in the plan to six months, thereby making the plan accessible to more employees.

***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 1998.

***Employee communications*** Employee communications continue 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; the introduction of 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.

**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 1998 were equivalent to 25 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 1998, charitable donations in the UK amounted to £1,031,000 (1997: £809,000) and overseas to £308,000 (1997: £458,000). Approximately half of this was given by the Company to charities working on educational, literacy and youth projects, including the Pearson sponsored Gallery of Living Words at the British Library, which opened in 1998. The other half was given by Pearson's operating companies which take active roles in supporting their local communities and industries. Many of the operating companies already match the funds raised by their employees for charities which amounted to £30,000 in 1998. Pearson does not make party political donations but it does support a number of independent research institutes across the political spectrum.

**The environment** Pearson does not operate in industries where there is potential for serious industrial pollution. However, the Company recognises its responsibility to be aware of, and take steps to control and minimise, any damage its operating companies may cause to the environment.

**Share capital** Details of share issues are given in note 23 to the accounts on page 77. On 4 August 1998 Pearson announced the placing for cash of 28.88 million new ordinary shares representing approximately 5% of its then existing issued ordinary share capital. The shares were subscribed for by institutional investors at a price of £11.35 per share. The purpose of the placing was to refinance part of the debt incurred as a result of the acquisition of the Simon & Schuster businesses. At the AGM held on 1 May 1998, the Company was authorised, subject to certain conditions, to acquire up to 57.7 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 30 April 1999.

At 10 March 1999, 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 |
|---|---|---|
| Companies associated with Lazard Frères et Cie, Paris | 43,088,523 | 7.07 |
| Prudential Corporation plc | 21,398,274 | 3.51 |

**Annual general meeting** The notice convening the AGM to be held at 12 noon on Friday, 30 April 1999 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE, is contained in the circular to shareholders dated 30 March 1999.

**Registered auditors** On 1 July 1998, the Group's auditors, Price Waterhouse, merged with Coopers & Lybrand following which Price Waterhouse resigned and the directors appointed the new firm, PricewaterhouseCoopers, as auditors. In accordance with sections 384 and 390A 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, special notice having been given pursuant to sections 379 and 388(3) of the Act.

**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 54 to 88 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.

Paul Vickers
SECRETARY
10 MARCH 1999

# Personnel committee report

Pearson's personnel committee is responsible for approving the remuneration and benefits packages of the executive directors and the chief executives of the main operating subsidiaries. It also recommends the chairman's remuneration to the board and reviews the Group's management development and succession plans.

As a result of the committee's work in 1998, the Company's package of incentives and rewards now includes bonus and share ownership plans which have strengthened the link between performance and reward and more closely aligned the interests of employees and shareholders.

Share ownership is at the heart of Pearson's remuneration philosophy. All staff worldwide have been given the opportunity to own Pearson shares through a savings contract linked to a share plan. An executive share option plan covers about 1,000 employees around the world. The Group's most senior executives are also encouraged to invest their own funds in Pearson shares, again strengthening the links between their own and shareholders' interests, through the annual bonus share matching plan. In addition to share ownership, staff also may benefit from a Group profit sharing plan which gives employees the chance to receive an annual bonus linked to the Group's profitability. The report of the committee sets out this philosophy in more detail, particularly as it applies to executive directors.

**Composition and compliance** The committee is chaired by Gill Lewis and its other member is Reuben Mark. Both are non-executive directors. The board will add at least one further independent director to the committee when the board's complement of non-executive directors is increased as the result of a selection process currently being undertaken by the board.

The London Stock Exchange requires companies to comply with the principles of good governance and the Code. The committee has considered these provisions and believes that the Company has complied throughout the year with Section A on remuneration committees and followed the provisions of Section B in determining remuneration policy for executive directors and senior executives.

**Remuneration policy for executive directors** The Company's executive remuneration policy aims to attract, retain and motivate high calibre senior executives through pay and other arrangements which are competitive and represent best practice. The philosophy that guides the Company's policy is to help employees own shares and to ensure that the rewards for the most senior executives follow from, and are consistent with, the overall system of compensation that applies to Pearson's employees. Within a framework of linking reward to performance, the philosophy also seeks to align the interests of directors and senior management with the interests of shareholders by creating an overall compensation system to enable the Company to attract and retain the highest calibre executives worldwide by giving significant rewards but only for outstanding achievement.

The main components of the Company's remuneration policy 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 1998 related to the Company's stated goals of increasing earnings per share, revenue growth, margin improvement and cash generation. In the case of two executive directors, David Bell and Greg Dyke, part of their rewards also related to the performance of the Financial Times Group and Pearson Television respectively.

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. For 1998, a discretionary bonus of £100,000 was paid to Marjorie Scardino. For 1998, a special performance-related bonus of £275,000 was paid to Greg Dyke, delivered in the form of Pearson shares which have to be held for three years. Bonuses do not form part of pensionable earnings.

**Annual bonus share matching plan** At the AGM on 1 May 1998, shareholders approved a share matching plan which 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 for certain specified periods of time, will be matched by the Company on a gross basis. Details of directors' matching awards are set out in tables 3 and 4 on page 51 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.

Some changes to the long-term incentive plans are being put to shareholders at the AGM. Details of these changes have been set out in a separate circular to shareholders dated 30 March 1999. The two main reasons for these changes are that the existing long-term incentive plans do not provide a strong enough connection between performance and reward and that, having reorganised Pearson into four complementary businesses all of which are number one or number two in their markets in the world, the Group is now competing internationally for its top executives with reward packages which, at the moment, are not competitive.

**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.

The three-year performance period for the incentive share plan award made in 1996 ended on 31 December 1998. Since Pearson's total shareholder return out-performed that of the *FT-SE 100* by 30% over the period, 150% of the shares awarded in 1996 were released to participants. None of the current directors received an award in 1996, and so none were eligible for a release of shares.

The only outstanding award under this plan was made in 1997 and directors' interests in this are set out in tables 3 and 4 on page 51 of this report. To the extent that the Company has provided funds to the trust for the purchase of shares, provision has been made in the accounts for the costs associated with the plan.

Subject to shareholder approval at the AGM of the new long-term incentive arrangements, no further awards will be made under the incentive share plan.

**Share option plans** In 1998, shareholders approved at the AGM a new executive share option plan which took account of changes in market practice and institutional share plan guidelines since the previous plans were introduced and which has worldwide application. Options at market value at the date of grant are granted to eligible employees based on guidelines approved by the committee. These guidelines govern the total number of options which may be granted and the frequency of awards and ensure that the

progression to maximum awards are within the individual and overall limits authorised by shareholders. Subject to shareholder approval of the new long-term incentive arrangements, no further awards of share options under the 1998 plan will be made to executive directors.

**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 1995, non-executive directors have received an annual fee of £25,000 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.

**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 $5,000 to the Pearson Inc. funded, approved, defined contribution (401k) arrangement.

David Bell, John Makinson and Greg Dyke 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). Both John Makinson and Greg Dyke are 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. Greg Dyke receives a supplement of 50% of his annual base salary to compensate him for the loss of pension provision as a result of pensions cap regulations.

David Veit retired with effect from 1 May 1998. In the US, he participated in the funded, approved Pearson Inc. Pension Plan. He was additionally entitled to a pension supplement under his service agreement. In combination, these arrangements provided a level pension from retirement. The Company also contributed $5,000 to the Pearson Inc. funded, approved, defined contribution (401k) arrangement.

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 50 of this report.

## Table 1

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

| ALL FIGURES IN £000 | SALARIES/ FEES | BONUS | 1998 OTHER* | 3-YEAR ISP | TOTAL | 1997 TOTAL |
|---|---|---|---|---|---|---|
| **Chairman** | | | | | | |
| Sir Dennis Stevenson | 250 | — | — | — | 250 | 203 |
| **Executive directors** | | | | | | |
| Marjorie Scardino | 445 | 545 | 53 | — | 1,043 | 752 |
| David Bell | 240 | 240 | 16 | — | 496 | 303 |
| Greg Dyke | 275 | 480 | 13 | — | 768 | 371 |
| John Makinson | 270 | 270 | 15 | — | 555 | 351 |
| David Veit | 139 | — | 331 | 251 | 721 | 392 |
| **Non-executive directors** | | | | | | |
| Michel David-Weill | 25 | — | — | — | 25 | 25 |
| Gill Lewis | 30 | — | — | — | 30 | 28 |
| Reuben Mark | 32 | — | — | — | 32 | 32 |
| Vernon Sankey | 30 | — | — | — | 30 | 28 |
| David Verey | 25 | — | — | — | 25 | 25 |
| **Total** | 1,761 | 1,535 | 428 | 251 | 3,975 | 2,510 |
| Total 1997** | 2,148 | 483 | 237 | — | — | 2,868 |

** 'Other' excludes pension contributions*

*** Includes amounts to former directors*

**NOTE:** *Marjorie Scardino was the highest paid director in 1998. Her total remuneration, including pension contributions, amounted to £1,167,611. For Marjorie Scardino, David Bell, Greg Dyke and John Makinson, 'other' emoluments include company car and health care benefits. Also included in 'other' emoluments for Marjorie Scardino is £33,185 in respect of housing costs. A sum of $550,000 (£331,000) was paid to David Veit as compensation for early termination of his contract on 1 May 1998. The release of shares to David Veit under the incentive share plan relates to the performance period 1 January 1996 to 31 December 1998. The value of these shares shown is based on the middle market value of Pearson shares of 1338p on 10 March 1999 (being the date on which the results for the final year of the three-year performance period were announced).*

## Table 2

| Directors' pensions | AGE AT 31 DEC 98* | DIRECTORS' CONTRIBUTIONS OVER THE PERIOD £000 PA | INCREASE IN ACCRUED PENSION OVER THE PERIOD £000 PA | ACCRUED PENSION AT 31 DEC 98* £000 PA | PENSION AND RELATED BENEFITS COSTS TO THE COMPANY OVER THE PERIOD £000 PA |
|---|---|---|---|---|---|
| Marjorie Scardino | 51 | — | 0.7 | 1.9 | 125.0 |
| David Bell | 52 | 12.0 | 6.1 | 117.3 | — |
| Greg Dyke | 51 | 4.2 | 1.5 | 5.5 | 148.7 |
| John Makinson | 44 | 4.2 | 2.0 | 11.8 | 88.7 |
| David Veit | 59 | — | 2.6 | 220.1 | 4.6 |

* *Or date of retirement, if earlier.*

**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 1998. As members of the UK plan, David Bell, John Makinson and Greg Dyke have the option to pay Additional Voluntary Contributions (AVCs). They did not pay any AVCs in 1998.*

**NOTE 2:** *The column headed 'pensions 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) plan and notional contributions to Marjorie Scardino's notional defined contribution plan.*

**NOTE 3:** *David Veit retired with effect from 1 May 1998. The figure shown for him in the column headed 'accrued pension at 31 December 1998' represents his accrued pension entitlement payable at age 62, with early retirement reduction factors applicable if retirement occurred before age 60. In the event, this pension became payable to him on an unreduced basis at his date of retirement. The above pension was payable in the form of a ten-year certain and continuous life annuity with no contingent spouse's pension and no pension increases, or any actuarial equivalent thereof. No pension increases have been awarded since his retirement.*

*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 for relevant directors).*

*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. In the case of Greg Dyke, the relevant percentage is 67%.*

*Children's pensions may also be payable to dependant 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, David Bell and Greg Dyke 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 or David Veit.*

## Table 3

| | 31 Dec 98+ | 1 Jan 98 | 31 Dec 98+ | 1 Jan 98 | 31 Dec 98 | 1 Jan 98 | 31 Dec 98 | 1 Jan 98 |
|---|---|---|---|---|---|---|---|---|
| | ORDINARY SHARES† | ORDINARY SHARES | OPTIONS – ORDINARY SHARES | OPTIONS – ORDINARY SHARES | INCENTIVE SHARE PLAN ORDINARY SHARES+++ | INCENTIVE SHARE PLAN ORDINARY SHARES+++ | ANNUAL BONUS MATCHING SHARES†† | ANNUAL BONUS MATCHING SHARES†† |
| **Interests of directors were** | | | | | | | | |
| Sir Dennis Stevenson | 69,452 | 68,606 | 2,243 | — | 63,271 | 62,500 | — | — |
| Marjorie Scardino | 15,418 | 10,101 | 165,835 | — | 65,227 | 64,432 | 6,967 | — |
| David Bell††† | 12,661 | 12,997 | 67,911 | 58,163 | 25,062 | 24,757 | — | — |
| Michel David-Weill++ | 48,129,727 | 48,129,727 | — | — | — | — | — | — |
| Greg Dyke | 3,330 | — | 201,643 | 139,100 | — | — | 5,551 | — |
| Gill Lewis | — | — | — | — | — | — | — | — |
| John Makinson | 6,457 | 3,000 | 197,084 | 169,784 | — | — | 4,096 | — |
| Reuben Mark | 7,600 | 7,600 | — | — | — | — | — | — |
| Vernon Sankey | — | — | — | — | — | — | — | — |
| David Veit | 357,191 | 357,091 | 141,791 | 141,891 | 18,628 | 23,661 | — | — |
| David Verey | — | — | — | — | — | — | — | — |

+ *Or date of retirement, if earlier.*

++ *Michel David-Weill's interests include 48,088,523 ordinary shares owned by companies associated with Lazard Frères et Cie., Paris. On 4 January 1999 Michel David-Weill's interests were reduced to 43,129,727 following the sale of 5 million shares by a company associated with Lazard Frères et Cie., Paris.*

+++ *The number of shares shown represents the maximum number of shares, plus accumulated share dividend shares, comprised in the original award which may be transferred to the individual concerned.*

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

†† *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.*

††† *On 8 January 1999 David Bell sold 1,500 shares and repurchased 1,380 for a discretionary PEP.*

**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 333,000 Pearson ordinary shares of 25p each at 31 December 1998 and also at 10 March 1999, the latest practicable date prior to the printing of this report.*

## Table 4

| **Movements in directors' interests under the incentive share and annual bonus share matching plans** | SHARES OUT-STANDING AT 1 JAN 98 | INCENTIVE SHARE PLAN+ | ANNUAL BONUS SHARE MATCHING PLAN | NUMBER OF SHARES VESTED AND RELEASED | NUMBER OF SHARES LAPSED | MARKET PRICE ON DATE OF RELEASE | NUMBER OF SHARES OUT-STANDING AT 31 DEC 98 |
|---|---|---|---|---|---|---|---|
| Sir Dennis Stevenson | 62,500 | 771 | — | — | — | — | 63,271 |
| Marjorie Scardino | 64,432 | 795 | 6,967 | — | — | — | 72,194 |
| David Bell | 24,757 | 305 | — | — | — | — | 25,062 |
| Greg Dyke | — | — | 5,551 | — | — | — | 5,551 |
| John Makinson | — | — | 4,096 | — | — | — | 4,096 |
| David Veit | 23,661 | — | — | — | 5,033 | — | 18,628 |

+ *The award as stated is the maximum number of shares, including share dividend on plan shares, which may vest, subject to the performance conditions being fulfilled.*

## Table 5

| Movements in directors' interests in share options | | 1 JAN 98 | GRANTED | EXERCISED | 31 DEC 98+ | WEIGHTED AVERAGE OPTION PRICE (p) | GAIN ON EXERCISE (£) | OPTION PRICE IN RESPECT OF EXERCISED OPTIONS (p) | MARKET PRICE ON EXERCISE (p) |
|---|---|---|---|---|---|---|---|---|---|
| Sir Dennis Stevenson | A | — | — | — | — | — | — | — | — |
| | B | — | 2,243** | — | 2,243 | 769 | — | — | — |
| Total | | — | 2,243 | — | 2,243 | 769 | — | | |
| Marjorie Scardino | A | — | — | — | — | — | — | — | — |
| | B | — | 163,300* | — | 165,835 | 1085 | — | — | — |
| | | — | 2,535** | — | | | | | |
| Total | | — | 165,835 | — | 165,835 | 1085 | — | | |
| David Bell | A | 29,300 | — | 9,000 | 20,300 | 545 | 45,990 | 545 | 1056 |
| | B | 28,863 | 18,300* | — | 47,611 | 816 | — | — | — |
| | | — | 448** | — | | | | | |
| Total | | 58,163 | 18,748 | 9,000 | 67,911 | 735 | 45,990 | | |
| Greg Dyke | A | 73,300 | — | — | 73,300 | 545 | — | — | — |
| | B | 65,800 | 60,300* | — | 128,343 | 817 | — | — | — |
| | | — | 2,243** | — | | | | | |
| Total | | 139,100 | 62,543 | — | 201,643 | 718 | — | | |
| John Makinson | A | 68,000 | — | — | 68,000 | 611 | — | — | — |
| | B | 101,784 | 27,300* | — | 129,084 | 797 | — | — | — |
| Total | | 169,784 | 27,300 | — | 197,084 | 733 | — | | |
| David Veit | A | 82,791 | — | 100 | 82,691 | 334 | 646 | 334 | 980 |
| | B | 59,100 | — | — | 59,100 | 545 | — | — | — |
| Total | | 141,891 | — | 100 | 141,791 | 422 | 646 | | |

*+ Or date of retirement, if earlier.*

**NOTE:** *Shares under option on 31 December 1998 are designated as:* **A**) *where the options are exercisable, and* **B**) *where the options are not yet exercisable* ■ *Total combined gain on the exercise of the options for all directors during 1998 amounted to £46,636. 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. No options lapsed during the year. The market price on 30 December 1998 was 1193p per share and the range during the year was 761.5p to 1200p per share. Outstanding executive 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.*

*Options are held under the executive and Save for Shares plans. Option grants marked * above were made under the executive plan at prices between 948.5p and 1090p and are exercisable between 2001 and 2008. Grants marked ** were made under the Save for Shares plan at a price of 769p and are exercisable between 2003 and 2006.*

# Report of the auditors to the members of Pearson plc

We have audited the financial statements on pages 54 to 88 (including additional disclosures on pages 46 to 52 relating to the remuneration of the directors of Pearson plc specified for our review by the London Stock Exchange) which have been prepared under the historical cost convention (as modified by the revaluation of certain fixed assets) and the accounting policies set out on pages 58 and 59.

**Respective responsibilities of directors and auditors** The directors are responsible for preparing the annual report including, as described on page 45, the financial statements. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board, the Listing Rules of the London Stock Exchange 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 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 on page 40 reflects the Company's compliance with those provisions of the Combined Code specified for our review by the London Stock Exchange, and we report if it does not. We are not required to form an opinion on the effectiveness of the Group's corporate governance procedures or its internal controls.

**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 1998 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 10 MARCH 1999

# Consolidated profit and loss account

*For the year ended 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 OPERATING ACTIVITIES | 1998 OTHER ITEMS | 1998 TOTAL | 1997 RESTATED TOTAL | NOTE |
|---|---|---|---|---|---|
| **Sales** | | | | | |
| Continuing operations | 2,121 | – | 2,121 | 2,011 | |
| Acquisitions | 130 | – | 130 | – | |
| | 2,251 | – | 2,251 | 2,011 | |
| Discontinued operations | 144 | – | 144 | 282 | |
| **Total sales** | 2,395 | – | 2,395 | 2,293 | 2 |
| Cost of sales | (1,127) | (49) | (1,176) | (1,114) | 3 |
| **Gross profit** | 1,268 | (49) | 1,219 | 1,179 | |
| Net operating expenses – before goodwill amortisation | (930) | (78) | (1,008) | (898) | |
| Net operating expenses – goodwill amortisation | (12) | – | (12) | – | 3 |
| Net operating expenses | (942) | (78) | (1,020) | (898) | 3 |
| **Operating profit** | | | | | |
| Continuing operations – Group | 292 | (77) | 215 | 252 | |
| Acquisitions – Group | 11 | (50) | (39) | – | |
| | 303 | (127) | 176 | 252 | |
| Discontinued operations – Group | 23 | – | 23 | 29 | |
| **Total operating profit – Group** | 326 | (127) | 199 | 281 | |
| Share of operating profit/(loss) of associates: | | | | | |
| Continuing operations | 53 | – | 53 | 43 | 13 |
| Discontinued operations | (2) | – | (2) | 4 | 13 |
| **Total share of operating profit of associates** | 51 | – | 51 | 47 | 13 |
| Total operating profit analysed between: | | | | | |
| Operating profit before goodwill amortisation | 389 | (127) | 262 | 328 | 2 |
| Goodwill amortisation | (12) | – | (12) | – | 3 |
| **Total operating profit** | 377 | (127) | 250 | 328 | 2 |
| Continuing operations: | | | | | |
| Profit on sale of fixed assets and investments | | | 142 | 23 | 4 |
| Profit on sale of businesses and associates | | | 50 | 33 | 5 |
| Discontinued operations: | | | | | |
| Profit/(loss) on sale of businesses and associates | | | 215 | (212) | 5 |
| | | | 407 | (156) | |
| Continuing operations: | | | | | |
| Profit/(loss) on sale of businesses and associates by an associate | | | 11 | (1) | 13 |
| **Profit before interest** | | | 668 | 171 | |
| Net interest payable – Group | | | (36) | (37) | 6 |
| Net interest payable – associates | | | (3) | (5) | 13 |
| **Total net interest payable** | | | (39) | (42) | |
| **Profit before taxation** | | | 629 | 129 | |
| Taxation | | | (188) | (89) | 7 |
| **Profit after taxation** | | | 441 | 40 | |
| Equity minority interests | | | (4) | (2) | |
| **Profit for the financial year** | | | 437 | 38 | |
| **Dividends on equity shares** | | | (126) | (112) | 8 |
| **Profit/(deficit) retained** | | | 311 | (74) | |
| **Adjusted earnings per equity share** | | | 42.0p | 34.9p | 9 |
| **Earnings per equity share** | | | 74.1p | 6.6p | 9 |
| **Diluted earnings per equity share** | | | 73.3p | 6.4p | 9 |
| **Dividends per equity share** | | | 21.0p | 19.5p | 8 |

**NOTE:** *1997 has been restated to reflect the adoption of FRS9 'Associates and Joint Ventures' and FRS14 'Earnings Per Share' (see note 1). There were no 'other items' in 1997.*

# Consolidated balance sheet

*As at 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 | NOTE |
|---|---|---|---|
| **Fixed assets** | | | |
| Intangible assets | 2,330 | — | 11 |
| Tangible assets | 435 | 506 | 12 |
| Investments: | | | |
| Associates | 145 | 198 | 13 |
| Other | 168 | 140 | 14 |
| | 3,078 | 844 | |
| **Current assets** | | | |
| Stocks | 614 | 379 | 15 |
| Debtors | 1,127 | 807 | 16 |
| Investments | 153 | 8 | 17 |
| Cash at bank and in hand | 345 | 215 | 18 |
| | 2,239 | 1,409 | |
| **Creditors – amounts falling due within one year** | | | |
| Short term borrowing | (72) | (313) | 19 |
| Other creditors | (1,282) | (918) | 20 |
| | (1,354) | (1,231) | |
| **Net current assets** | 885 | 178 | |
| **Total assets less current liabilities** | 3,963 | 1,022 | |
| **Creditors – amounts falling due after more than one year** | | | |
| Medium and long term borrowing | (2,552) | (609) | 19 |
| Other creditors | (54) | (45) | 20 |
| | (2,606) | (654) | |
| **Provisions for liabilities and charges** | | | |
| Deferred taxation | (20) | (37) | 21 |
| Other provisions for liabilities and charges | (253) | (175) | 22 |
| **Net assets** | 1,084 | 156 | |
| **Capital and reserves** | | | |
| Called up share capital | 152 | 144 | 23 |
| Share premium account | 498 | 158 | 24 |
| Revaluation reserve | 1 | 3 | 24 |
| Other reserves | 1 | 1 | 24 |
| Profit and loss account | 396 | (154) | 24 |
| **Equity shareholders' funds** | 1,048 | 152 | |
| **Equity minority interests** | 36 | 4 | |
| | 1,084 | 156 | |

The Company balance sheet is shown in note 31.

The financial statements were approved by the board of directors on 10 March 1999 and signed on its behalf by

Sir Dennis Stevenson

John Makinson

# Consolidated statement of cash flows

*For the year ended 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 | NOTE |
|---|---|---|---|
| **Net cash inflow from operating activities** | 402 | 204 | 27 |
| **Dividends from partnerships and other associates** | 53 | 40 | |
| Interest received | 52 | 35 | |
| Interest paid | (88) | (72) | |
| Debt issue costs | (21) | — | |
| Dividends paid to minority interests | (3) | (1) | |
| **Returns on investments and servicing of finance** | (60) | (38) | |
| **Taxation** | (80) | (75) | |
| Purchase of tangible fixed assets | (125) | (110) | |
| Sale of tangible fixed assets | 14 | 22 | |
| Purchase of investments | (53) | (12) | |
| Sale of investments | 199 | 148 | |
| **Capital expenditure and financial investment** | 35 | 48 | |
| Purchase of subsidiary undertakings | (2,936) | (269) | |
| Net cash acquired with subsidiary undertakings | (2) | 3 | |
| Purchase of associates | (13) | (67) | |
| Sale of subsidiary undertakings | 718 | 54 | |
| Net cash disposed with subsidiary undertakings | (17) | (1) | |
| Sale of associates | 77 | 46 | |
| **Acquisitions and disposals** | (2,173) | (234) | 25/26 |
| **Equity dividends paid** | (113) | (106) | |
| **Net cash outflow before management of liquid resources and financing** | (1,936) | (161) | |
| Disposal of asset backed securities | — | 89 | |
| Liquid resources acquired | (1,261) | (123) | |
| Liquid resources disposed | 1,306 | 123 | |
| **Management of liquid resources** | 45 | 89 | 27 |
| Issue of equity share capital | 344 | 27 | |
| Capital element of finance lease rentals | (1) | (1) | |
| Unsecured bank loans repaid | (141) | — | |
| Loan facility advanced | 2,115 | — | |
| Loan stock repaid | — | (68) | |
| Net movement in other borrowings | (280) | 184 | |
| **Financing** | 2,037 | 142 | |
| **Increase in cash in the year** | 146 | 70 | 27 |

# Statement of total recognised gains and losses

*For the year ended 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Profit for the financial year | 437 | 38 |
| Other net gains and losses recognised in reserves: | | |
| Currency translation differences | (8) | (20) |
| **Total recognised gains relating to the year** | 429 | 18 |

# Note of historical cost profits and losses

*For the year ended 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Reported profit before taxation | 629 | 129 |
| Realisation of property revaluations | 2 | 2 |
| Historical cost profit on ordinary activities before taxation | 631 | 131 |
| **Historical cost profit/(loss) retained after taxation, equity minority interests and dividends** | 313 | (72) |

# Reconciliation of movements in equity shareholders' funds

*For the year ended 31 December 1998*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Profit for the financial year | 437 | 38 |
| Dividends on equity shares | (126) | (112) |
| | 311 | (74) |
| Other net recognised losses relating to the year (see above) | (8) | (20) |
| Goodwill arising on prior year acquisitions | (16) | (402) |
| Goodwill written back | 262 | 233 |
| Shares issued | 347 | 27 |
| Net movement for the year | 896 | (236) |
| Equity shareholders' funds at beginning of the year | 152 | 388 |
| **Equity shareholders' funds at end of the year** | 1,048 | 152 |

# Notes to the accounts

## 1. Accounting policies

Accounting policies have been consistently applied. FRS9 'Associates and Joint Ventures' has been adopted and comparative figures have been restated to reflect associates' interest in net interest payable. Net interest income arising within Lazard is included in operating profit, being part of its normal operating activities. FRS14 'Earnings Per Share' has also been adopted and comparative figures have been restated. FRS10 'Goodwill and Intangible Assets' (see B below), FRS11 'Impairment of Fixed Assets and Goodwill', and FRS13 'Derivatives and Other Financial Instruments: Disclosures' have also been adopted.

A. **Basis of accounting** The accounts are prepared under the historical cost convention, modified by the revaluation of certain land and buildings and investments, 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, partnerships and other associates 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. 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 profit of partnerships and other associates, and the consolidated balance sheet includes the Group's interest in partnerships and other associates at the book value of attributable net tangible assets. The figures included in the financial statements have been based on audited accounts, adjusted where necessary by reference to unaudited management accounts for the subsequent 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.

D. **Foreign currencies** Profit and loss accounts in overseas currencies are translated into sterling at weighted 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 currencies for the Group are the US dollar and the Spanish peseta. The weighted average rates for the year against sterling were $1.66 and Pta248.1 (1997: $1.63 and Pta242.1) and the year end rates were $1.66 and Pta235.8 (1997: $1.65 and Pta250.8).

E. **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.

**F. 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.

**G. Channel 5** The Group's share of certain Channel 5 initial costs is being amortised. These costs will be amortised by the end of the 10 year licence period. The Group's share of other profits and losses is being equity accounted.

**H. Tangible fixed assets** The cost or subsequent valuation of tangible fixed assets other than freehold land and investment properties is depreciated over estimated economic lives in equal annual amounts at the rates indicated in note 12.

**I. Leases** Finance lease rentals are capitalised at the total amount of rentals payable under the leasing agreement (excluding finance charges) and depreciated in accordance with policy H 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.

**J. Fixed asset investments** Fixed asset investments are stated at cost less provisions for diminution in value, or as revalued by the directors.

**K. Stocks** Stocks and work in progress are valued at the lower of cost and net realisable value.

**L. Product 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 editorial content, distribution and remote printing. The extra costs arising are expensed as incurred. ■ Pre publication costs, the direct costs incurred in the development of titles prior to their publication, are included within stocks and are amortised over their estimated economic lives. ■ Advances to authors are included within debtors net of any provision required for net realisable value and are expensed at contracted rates based on sales of the related titles. ■ Television programme production costs are included within stocks and are amortised over the estimated period in which the related revenue is forecast to be earned.

**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, including those arising from the revaluation of fixed assets, 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.

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

**O. 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.

**P. 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.

## 2. a) Analysis of sales and operating profit

| ALL FIGURES IN £ MILLIONS | 1998 SALES | 1998 OPERATING PROFIT BEFORE GOODWILL & OTHER ITEMS | 1998 OPERATING PROFIT AFTER GOODWILL & OTHER ITEMS | 1997 SALES | 1997 RESTATED OPERATING PROFIT |
|---|---|---|---|---|---|
| **Business sectors** | | | | | |
| FT Group | 683 | 118 | 114 | 676 | 108 |
| Pearson Education | 702 | 99 | (34) | 563 | 60 |
| The Penguin Group | 523 | 48 | 46 | 525 | 58 |
| Pearson Television | 343 | 61 | 61 | 247 | 26 |
| Lazard | — | 42 | 42 | — | 43 |
| Continuing operations | 2,251 | 368 | 229 | 2,011 | 295 |
| Discontinued operations | 144 | 21 | 21 | 282 | 33 |
| | 2,395 | 389 | 250 | 2,293 | 328 |
| **Geographical markets supplied** | | | | | |
| United Kingdom | 497 | 51 | 48 | 487 | 54 |
| Continental Europe | 461 | 114 | 111 | 382 | 77 |
| North America | 1,078 | 181 | 54 | 916 | 134 |
| Asia Pacific | 161 | 16 | 11 | 179 | 23 |
| Rest of World | 54 | 6 | 5 | 47 | 7 |
| Continuing operations | 2,251 | 368 | 229 | 2,011 | 295 |
| Discontinued operations | 144 | 21 | 21 | 282 | 33 |
| | 2,395 | 389 | 250 | 2,293 | 328 |

**NOTE:** *In 1998 'other items' comprises exceptional items of £120m and Year 2000 costs of £7m. ■ Exceptional items of £120m comprise integration costs following the acquisition of Simon & Schuster. These all relate to the Pearson Education business sector. ■ 1997 operating profit is stated after restructuring costs of £34m which were classified as exceptional within operating activities. These related to FT Group, £14m, Pearson Education, £12m, Pearson Television, £4m, and discontinued businesses, £4m, and are shown mainly within United Kingdom, £16m, and North America, £17m. In 1998 operating restructuring costs of £11m were incurred of which £6m were in the FT Group and £5m in The Penguin Group. ■ 1997 has been re-analysed to reflect expanded business groups. ■ Discontinued operations relate to the withdrawal of the Group from the consumer software business following its disposal of Mindscape Inc. in March 1998, the withdrawal of the Group from the consumer magazine business following its disposal of Pearson New Entertainment in April 1998 and the withdrawal of the Group from the visitor attractions business following its disposal of The Tussauds Group in October 1998. ■ 1997 has been restated to reflect the adoption of FRS9 'Associates and Joint Ventures' (see note 1). ■ Analyses of the profits of associates are shown in note 13.*

## 2. a) Analysis of sales and operating profit (cont'd)

| ALL FIGURES IN £ MILLIONS | 1998 TOTAL BY SOURCE | 1998 INTER-REGIONAL | 1998 SALES | 1997 TOTAL BY SOURCE | 1997 INTER-REGIONAL | 1997 SALES |
|---|---|---|---|---|---|---|
| **Geographical source of sales** | | | | | | |
| United Kingdom | 728 | (52) | 676 | 703 | (46) | 657 |
| Continental Europe | 355 | (6) | 349 | 302 | (7) | 295 |
| North America | 1,108 | (28) | 1,080 | 928 | (19) | 909 |
| Asia Pacific | 129 | (4) | 125 | 144 | (7) | 137 |
| Rest of World | 22 | (1) | 21 | 13 | — | 13 |
| Continuing operations | 2,342 | (91) | 2,251 | 2,090 | (79) | 2,011 |
| Discontinued operations | 144 | — | 144 | 284 | (2) | 282 |
| | 2,486 | (91) | 2,395 | 2,374 | (81) | 2,293 |

**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.*

## 2. b) Analysis of capital employed

| ALL FIGURES IN £ MILLIONS | 1998 CAPITAL EMPLOYED | 1997 CAPITAL EMPLOYED |
|---|---|---|
| **Business sectors** | | |
| FT Group | 143 | 98 |
| Pearson Education | 3,200 | 380 |
| The Penguin Group | 143 | 176 |
| Pearson Television | 39 | 103 |
| Lazard | 111 | 123 |
| Continuing operations | 3,636 | 880 |
| Discontinued operations | — | 195 |
| | 3,636 | 1,075 |
| **Geographical location** | | |
| United Kingdom | 220 | 136 |
| Continental Europe | 223 | 86 |
| North America | 3,055 | 616 |
| Asia Pacific | 96 | 29 |
| Rest of World | 42 | 13 |
| Continuing operations | 3,636 | 880 |
| Discontinued operations | — | 195 |
| | 3,636 | 1,075 |
| **Reconciliation of capital employed to net assets** | | |
| Capital employed | 3,636 | 1,075 |
| Less: deferred taxation | (20) | (37) |
| Less: other provisions | (253) | (175) |
| Less: net debt | (2,279) | (707) |
| **Net assets** | 1,084 | 156 |

## 3. Analysis of consolidated profit and loss account

| ALL FIGURES IN £ MILLIONS | 1998 CONTINUING | 1998 DISCONTINUED | 1998 TOTAL | 1997 CONTINUING | 1997 DISCONTINUED | 1997 TOTAL |
|---|---|---|---|---|---|---|
| **Cost of sales** | (1,138) | (38) | (1,176) | (1,003) | (111) | (1,114) |
| Distribution costs | (168) | (1) | (169) | (123) | (3) | (126) |
| Administration and other expenses | (848) | (85) | (933) | (701) | (143) | (844) |
| Other operating income (see below) | 79 | 3 | 82 | 68 | 4 | 72 |
| **Net operating expenses** | (937) | (83) | (1,020) | (756) | (142) | (898) |
| Analysed as: | | | | | | |
| Net operating expenses – before exceptional items and goodwill amortisation | (854) | (83) | (937) | (726) | (138) | (864) |
| Net operating expenses – exceptional items | (71) | — | (71) | (30) | (4) | (34) |
| Net operating expenses – goodwill amortisation | (12) | — | (12) | — | — | — |
| **Net operating expenses** | (937) | (83) | (1,020) | (756) | (142) | (898) |

**NOTE:** *The following amounts are included in the 1998 totals in respect of acquisitions: cost of sales £74m and net operating expenses £95m. The exceptional expense of £120m in 1998 is included within cost of sales £49m and administration and other expenses £71m (see note 2). The exceptional expense of £34m in 1997 is included within administration and other expenses.*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Other operating income** | | |
| Income from other investments: | | |
| Listed | — | 2 |
| Unlisted | 14 | 13 |
| BSBH loan stock interest | 4 | 4 |
| Other operating income (mainly royalties, rights and commission income) | 64 | 53 |
| | 82 | 72 |
| **Profit before taxation is stated after charging:** | | |
| Depreciation | 66 | 65 |
| Operating lease rentals: | | |
| Plant and machinery | 17 | 12 |
| Properties | 41 | 36 |
| Year 2000 costs | 7 | — |
| Auditors' remuneration: | | |
| Audit | 2 | 2 |
| Non-audit – UK – PricewaterhouseCoopers (Company £nil; 1997: £nil) | 2 | 2 |
| Non-audit – Other – PricewaterhouseCoopers | 2 | — |

**NOTE:** *Non-audit fees of £4m for PricewaterhouseCoopers in 1998 include £3m paid to Price Waterhouse and £1m paid to Coopers & Lybrand prior to the date of appointment of PricewaterhouseCoopers as auditors. Non-audit fees in 1997 comprise solely amounts paid to the previous auditors Price Waterhouse. In addition to the non-audit fees (UK) of £2m (1997:£2m), consultancy fees of £7m (1997:£8m) have been incurred in respect of the Shared Services initiative. These fees have been capitalised. Fees of £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 (1997: £0.1m).*

## 4. Profit on sale of fixed assets and investments

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Continuing operations: | | |
| Profit on sale of investment in Société Européenne des Satellites (see note 14) | 133 | — |
| Profit on sale of investment in Flextech plc (see note 14) | 27 | 24 |
| Loss on sale of Simon & Schuster related fixed assets | (6) | — |
| Profit on sale of investment in Television Broadcasts Limited | — | 4 |
| Net loss on other investments and property interests | (12) | (5) |
| | 142 | 23 |
| Taxation | (40) | (4) |

## 5. Profit/(loss) on sale of businesses and associates

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Continuing operations: | | |
| Profit on sale of Law & Tax publishing business (see note 26) | 61 | — |
| Profit on sale of 20% of Recoletos (see note 26) | 34 | — |
| Loss on sale of Register group (see note 26) | (20) | — |
| Loss on closure of Simon & Schuster businesses (see note 26) | (10) | — |
| Profit on sale of Churchill Livingstone | 2 | 30 |
| Profit on sale of Troll Communications LLC | — | 13 |
| Net loss on sale of other businesses and associates | (25) | (10) |
| Profit on sale of Canadian Financial Post (see note 13) | 8 | — |
| | 50 | 33 |
| Discontinued operations: | | |
| Profit on sale of The Tussauds Group (see note 26) | 157 | — |
| Profit on sale of Pearson New Entertainment (see note 26) | 41 | — |
| Profit on sale of Port Aventura SA (see note 13) | 28 | — |
| Loss on sale of Mindscape Inc. (see note 26) | (11) | — |
| Provision against goodwill on the sale of Mindscape Inc. | — | (212) |
| | 215 | (212) |
| Taxation | (63) | (1) |

## 6. Net interest payable – Group

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Interest payable and similar charges:** | | |
| On borrowing repayable wholly within five years not by instalments | (43) | (32) |
| On borrowing repayable wholly or partly after five years | (44) | (45) |
| | (87) | (77) |
| **Interest receivable and similar income:** | | |
| On deposits and liquid funds | 48 | 37 |
| Amortisation of swap proceeds (see note 20) | 3 | 3 |
| **Net interest payable** | (36) | (37) |

## 7. Taxation

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| UK: | | |
| Corporation tax at 31% (1997: 31.5%) | 134 | 37 |
| Deferred taxation | (4) | 11 |
| Double taxation relief | (1) | (1) |
| Associates | 8 | 5 |
| Overseas: | | |
| Overseas tax | 45 | 30 |
| Deferred taxation | 1 | 2 |
| Associates | 5 | 5 |
| | 188 | 89 |

| ALL FIGURES IN PERCENTAGES | | |
|---|---|---|
| **Tax rate reconciliation** | | |
| UK tax rate | 31.0 | 31.5 |
| Effect of utilisation of tax losses in the US | (2.7) | (4.3) |
| Other items | (0.3) | 2.2 |
| Tax rate reflected in adjusted earnings | 28.0 | 29.4 |
| Effect of profits/(losses) excluded from adjusted earnings | 1.9 | 39.5 |
| **Tax rate reflected in earnings** | 29.9 | 68.9 |

**NOTE:** *The Group continues to have substantial tax losses available in the US which are not recognised in the accounts and more than offset both 1998 and 1997 US profits, so reducing the Group tax rate reflected in adjusted earnings. Relief has not been taken for the Simon & Schuster integration costs to the extent that they arose in the US, hence increasing the effective tax rate on earnings. This was largely offset by the fact that, as in 1997, the tax payable on profits on disposals benefited from the use of losses brought forward, indexation and from other differences between book and tax bases for the calculation of gains. 1997 was also affected by no relief being taken for the provision against the goodwill on the sale of Mindscape Inc.*

## 8. Dividends

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | PENCE PER SHARE | £M | PENCE PER SHARE | £M |
| Interim paid | 8.0 | 47 | 7.5 | 43 |
| Final proposed | 13.0 | 79 | 12.0 | 69 |
| **Dividends for the year** | 21.0 | 126 | 19.5 | 112 |

## 9. Earnings per share

In order to show results from operating activities on a comparable basis an adjusted earnings per equity share has been calculated which excludes profits or losses on the sale of fixed assets and investments, businesses and associates (see notes 4 and 5), Year 2000 compliance costs and integration costs in respect of the acquisition of Simon & Schuster (see note 2). Following the prospective implementation of FRS10 'Goodwill and Intangible Assets', goodwill amortisation has also been excluded from adjusted earnings in order to show results on a comparable basis.

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | £M | EARNINGS PER SHARE PENCE | £M | EARNINGS PER SHARE PENCE |
| Basic earnings | 437 | 74.1 | 38 | 6.6 |
| Less: | | | | |
| (Profit) on sale of fixed assets and investments: continuing operations | (142) | (24.1) | (23) | (4.0) |
| (Profit) on sale of businesses and associates: continuing operations | (50) | (8.5) | (33) | (5.8) |
| (Profit)/loss on sale of businesses and associates: discontinued operations | (215) | (36.4) | 212 | 37.0 |
| (Profit)/loss on sale of businesses and associates by an associate: continuing operations | (11) | (1.9) | 1 | 0.2 |
| Add: | | | | |
| Goodwill amortisation | 12 | 2.0 | — | — |
| Simon & Schuster integration costs | 120 | 20.3 | — | — |
| Year 2000 compliance costs | 7 | 1.2 | — | — |
| Taxation on above items | 90 | 15.3 | 5 | 0.9 |
| Adjusted earnings | 248 | 42.0 | 200 | 34.9 |
| Earnings | 437 | | 38 | |
| Tax on the conversion of ordinary shares | (1) | | (1) | |
| Diluted earnings | 436 | | 37 | |
| Weighted average number of equity shares (millions) – for earnings and adjusted earnings | 589.8 | | 572.8 | |
| Effect of dilutive share options | 5.1 | | 4.7 | |
| Weighted average number of equity shares (millions) – for diluted earnings | 594.9 | | 577.5 | |
| Adjusted earnings per equity share | 42.0p | | 34.9p | |
| Earnings per equity share | 74.1p | | 6.6p | |
| Diluted earnings per equity share | 73.3p | | 6.4p | |

**NOTE:** *1997 weighted average number of equity shares has been restated in accordance with FRS14 'Earnings Per Share'.*

## 10. Employee information

The details of the emoluments of the directors of Pearson plc are shown on pages 49 to 52 and form part of these audited financial statements.

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Staff costs** | | |
| Wages and salaries | 476 | 454 |
| Social security costs | 54 | 46 |
| Post-retirement costs | 13 | 10 |
| | 543 | 510 |

## 10. Employee information (cont'd)

| | UK | US | OTHER | TOTAL |
|---|---|---|---|---|
| **Average number employed 1998** | | | | |
| FT Group | 2,780 | 832 | 1,858 | 5,470 |
| Pearson Education | 764 | 3,171 | 1,489 | 5,424 |
| The Penguin Group | 989 | 1,728 | 601 | 3,318 |
| Pearson Television | 585 | 113 | 450 | 1,148 |
| Other | 171 | 48 | — | 219 |
| Continuing operations | 5,289 | 5,892 | 4,398 | 15,579 |
| Discontinued operations | 2,614 | 131 | 76 | 2,821 |
| | 7,903 | 6,023 | 4,474 | 18,400 |
| **Average number employed 1997** | | | | |
| FT Group | 3,093 | 902 | 1,834 | 5,829 |
| Pearson Education | 818 | 2,498 | 1,279 | 4,595 |
| The Penguin Group | 895 | 1,728 | 582 | 3,205 |
| Pearson Television | 278 | 40 | 362 | 680 |
| Other | 124 | 93 | — | 217 |
| Continuing operations | 5,208 | 5,261 | 4,057 | 14,526 |
| Discontinued operations | 3,187 | 424 | 169 | 3,780 |
| | 8,395 | 5,685 | 4,226 | 18,306 |

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Post-retirement costs** | | |
| Defined benefit pension schemes | | |
| UK Group plan: Regular pension cost | 8 | 9 |
| UK Group plan: Amortisation of surplus | (9) | (13) |
| Net pension credit | (1) | (4) |
| Other defined benefit pension schemes | 6 | 6 |
| Defined contribution pension schemes | 5 | 6 |
| Medical benefits | 3 | 2 |
| | 13 | 10 |

**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 results of the most recent actuarial valuation, using the projected unit method of valuation, of the principal funded UK scheme, are shown in the table on page 67. The principal assumptions used are also shown in the table on page 67. The net assets of the UK Group plan at 31 December 1998 are included in the pension plan accounts at £1,035m (unaudited).

## 10. Employee information (cont'd)

| | UK GROUP PLAN |
|---|---|
| Assets at market value at latest full actuarial valuation on 1 January 1996* | £774m |
| Real return on investments per annum | 4.8% |
| Real increase in earnings per annum | 1.9% |
| Real increase in pensions in payment per annum | 0% |
| Level of funding** | 122% |

**Stated after a transfer of £2m to the scheme of a former subsidiary. **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, over the expected remaining service lives of the current employees, resulting in a credit to the profit and loss account of £1m (1997: £4m).

The total market value of the assets of the non UK defined benefit schemes (mainly in the US), valued this year, was £63m (1997: £48m).

**Other post-retirement benefits** The Group provides certain health care and life insurance 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 based upon the business division in which the retiree worked. Plan choices and retiree contributions are dependent on retirement date, business unit, option chosen, and length of service.

The principal assumptions affecting the provision for other post-retirement benefits were: medical inflation rate of 6.5% and a discount rate of 6.75%.

## 11. Intangible assets

| ALL FIGURES IN £ MILLIONS | GOODWILL TOTAL |
|---|---|
| **Cost** | |
| At 31 December 1997 | — |
| Exchange differences | (6) |
| Additions (see note 25) | 2,348 |
| **At 31 December 1998** | 2,342 |
| **Amortisation** | |
| At 31 December 1997 | — |
| Provided in the year | (12) |
| **At 31 December 1998** | (12) |
| **Net carrying amount** | |
| At 31 December 1997 | — |
| **At 31 December 1998** | 2,330 |

## 12. Tangible fixed assets

| ALL FIGURES IN £ MILLIONS | FREEHOLD AND LEASEHOLD PROPERTY | PLANT AND EQUIPMENT | ASSETS IN COURSE OF CONSTRUCTION | TOTAL |
|---|---|---|---|---|
| **Cost or as valued** | | | | |
| At 31 December 1997 | 319 | 485 | 37 | 841 |
| Exchange differences | — | 2 | — | 2 |
| Reclassifications | — | 13 | (13) | — |
| Owned by subsidiary undertakings acquired | 42 | 205 | 1 | 248 |
| Capital expenditure | 15 | 60 | 34 | 109 |
| Disposals | (7) | (43) | (35) | (85) |
| Owned by subsidiary undertakings disposed | (120) | (195) | (6) | (321) |
| **At 31 December 1998** | 249 | 527 | 18 | 794 |
| **Depreciation** | | | | |
| At 31 December 1997 | (71) | (264) | — | (335) |
| Exchange differences | — | — | — | — |
| Reclassifications | 1 | (1) | — | — |
| Impairment in value | (6) | (5) | — | (11) |
| Provided in the year | (10) | (56) | — | (66) |
| Subsidiary undertakings acquired | (12) | (93) | — | (105) |
| Disposals | 3 | 37 | — | 40 |
| Subsidiary undertakings disposed | 17 | 101 | — | 118 |
| **At 31 December 1998** | (78) | (281) | — | (359) |
| **Net book value** | | | | |
| At 31 December 1997 | 248 | 221 | 37 | 506 |
| **At 31 December 1998** | 171 | 246 | 18 | 435 |

**Freehold and leasehold property** Net book value includes: freehold of £133m (1997: £206m), short leases of £38m (1997: £39m) and long leases of £nil (1997: £3m). On an original cost basis, cost would have been included at £248m, and accumulated depreciation at £78m.

**Depreciation** Fixed assets are depreciated over their 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. Land, amounting to £40m, is not depreciated.

**Capital commitments** The Group had capital commitments for fixed assets, including finance leases, already under contract amounting to £45m at 31 December 1998.

**Other notes** The net book value of Group tangible fixed assets includes £20m in respect of assets held under finance leases. Depreciation on these assets charged in 1998 was £1m. The net book value of Group tangible fixed assets includes £nil (1997: £3m) in respect of capitalised interest.

## 13. Associates

| | 1998 | | 1997 | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | VALUATIONS | BOOK VALUES | VALUATIONS | BOOK VALUES |
| Partnership interests | 200 | 111 | 200 | 123 |
| Unlisted associates | 189 | (31) | 130 | (32) |
| Loans | 65 | 65 | 95 | 107 |
| | 454 | 145 | 425 | 198 |

**NOTE:** *Principal associates are listed on page 88. The valuations of unlisted partnerships and other associates are at directors' valuations as at 31 December 1998. If realised at these values there would be an estimated liability for taxation, at year end rates, of £68m. The Group had no capital commitments to subscribe for further capital and loan stock.*

## 13. Associates (cont'd)

| ALL FIGURES IN £ MILLIONS | EQUITY | SHARE OF LOANS | RESERVES | TOTAL |
|---|---|---|---|---|
| **Summary of movements** | | | | |
| At 31 December 1997 | 87 | 107 | 4 | 198 |
| Exchange differences | (2) | — | — | (2) |
| Additions | 2 | 11 | — | 13 |
| Goodwill written back | 16 | — | 1 | 17 |
| Owned by subsidiary undertakings disposed | — | (6) | — | (6) |
| Disposals | (26) | (47) | 22 | (51) |
| Retained loss for the year | — | — | (24) | (24) |
| **At 31 December 1998** | 77 | 65 | 3 | 145 |

**NOTE:** *During the year the Group sold its 40.5% share in Port Aventura SA for £56m giving rise to a profit on sale of £28m before tax estimated at £6m. This includes compensation of £18m from Port Aventura SA for the cancellation of the management agreement. During the year the Group sold its 20% share in the Canadian Financial Post for £13m giving rise to a profit on sale of £8m before tax estimated at £4m.*

| | 1998 | | 1997 | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | OPERATING PROFIT | NET ASSETS | OPERATING PROFIT | NET ASSETS |
| **Analysis of partnerships and other associates** | | | | |
| **Business sectors** | | | | |
| FT Group | 15 | 6 | 16 | (3) |
| Pearson Education | 4 | 5 | 3 | 5 |
| The Penguin Group | — | — | 1 | 1 |
| Pearson Television | (8) | 23 | (20) | 49 |
| Lazard | 42 | 111 | 43 | 123 |
| Continuing operations | 53 | 145 | 43 | 175 |
| Discontinued operations | (2) | — | 4 | 23 |
| | 51 | 145 | 47 | 198 |
| **Geographical markets supplied and location of net assets** | | | | |
| United Kingdom | 10 | 109 | (1) | 138 |
| Continental Europe | 11 | 13 | 9 | 11 |
| North America | 29 | 15 | 30 | 19 |
| Rest of World | 3 | 8 | 5 | 7 |
| Continuing operations | 53 | 145 | 43 | 175 |
| Discontinued operations | (2) | — | 4 | 23 |
| | 51 | 145 | 47 | 198 |

| ALL FIGURES IN £ MILLIONS | 1998 |
|---|---|
| **Reconciliation to retained loss** | |
| Operating profit of partnerships and other associates | 51 |
| Net interest of other associates | (3) |
| Profit on sale of an associate by an associate | 11 |
| UK taxation | (8) |
| Overseas taxation | (5) |
| Distributions receivable in respect of the year from partnership interests | (59) |
| Dividends (including tax credits) from unlisted associates | (11) |
| **Retained loss for the year** | (24) |

## 13. Associates (cont'd)

The aggregate of Pearson's share in its associates, excluding the interest in Lazard Partners Limited Partnership and the three Lazard Houses, is shown below.

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Sales | 239 | 225 |
| Fixed assets | 57 | 130 |
| Current assets | 126 | 126 |
| Liabilities due within one year | (88) | (101) |
| Liabilities due after one year or more | (61) | (80) |
| **Net assets** | 34 | 75 |

Pearson's interest in Lazard Partners Limited Partnership and the three Lazard Houses is shown below.

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| Profit before tax | 53 | 43 |
| Taxation | (7) | (6) |
| Profit after taxation | 46 | 37 |
| Fixed assets | 28 | 48 |
| Current assets | 5,151 | 3,925 |
| Liabilities due within one year | (4,829) | (3,753) |
| Liabilities due after one year or more | (239) | (97) |

**NOTE:** *Pearson's indirect general partnership interest in Lazard Frères et Cie and Maison Lazard et Cie held directly and indirectly through Lazard Partners Limited Partnership is an unlimited liability interest. Pearson holds these partnership interests through a subsidiary undertaking registered in England, with no other material assets. The aggregate liabilities of these partnerships included above are £851m (1997: £930m). Pearson also holds direct interests in Lazard Frères & Co., a New York Limited Liability Company.*

| **Interests in the Lazard Houses** | COUNTRY OF INCORPORATION OR REGISTRATION | BENEFICIAL INTEREST PER CENT | CLASS OF SHARE | SHARE CAPITAL MILLIONS |
|---|---|---|---|---|
| Lazard Partners Limited Partnership (which, with direct interests in the US and French partnerships gives the following interests in the Lazard Houses): | US | 50.0 | | Partnership |
| Lazard Brothers & Co., Ltd | England | 34.6 | Ord £1 | 25.3 |
| Lazard Brothers & Co., Ltd | England | 80.0 | Def £1 | 5.0 |
| Lazard Brothers & Co., Ltd | England | 50.0 | SFr 1 | 0.4 |
| Lazard Frères & Co., 'LLC' | US | 11.5 | | LLC* |
| Lazard Frères et Cie/Maison Lazard et Cie | France | 9.1 | | Partnership |

**Limited Liability Company.*

**NOTE:** *The beneficial percentages held for the investment banking partnership interests are interests in partnership profits.*

With effect from 1 January 1996, Lazard Frères & Co., 'LLC', Lazard Frères et Cie, Maison Lazard et Cie and Lazard Brothers & Co., Limited (together known as the three Lazard Houses) created a new system of interhouse profit sharing through the establishment of the Three Houses Pooling Partnership (the 'Pool') which became a limited partner of Lazard Partners Limited Partnership. As a result, the members, directors or partners in a particular Lazard House receive an interest in the profits of the other Lazard Houses in exchange for part of their existing profit entitlement in their own House. Pearson received additional

## 13. Associates (cont'd)

income in 1998 (the 'Pearson Adjustment') to reflect the reduction in its profit entitlements from its direct holding in Lazard Frères & Co, 'LLC', Lazard Frères et Cie and Maison Lazard et Cie and accordingly did not receive any income through the Pool. The share of net distributable profits of Lazard Partners Limited Partnership (after the Pool's profit share and the Pearson Adjustment) is divided in accordance with the respective capital interests of the original partners (Pearson plc – 50%).

On 8 December 1998 Lazard Brothers & Co. Limited's holding in Les Fils Dreyfus & Cie., Banquiers, a private bank incorporated in Switzerland, was reduced from 30% to 13% on the cancellation of some of its shares. The Group's share of the resulting profit was £11m, before tax of £1m.

## 14. Other fixed asset investments

| | 1998 | | 1997 | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | VALUATIONS | BOOK VALUES | VALUATIONS | BOOK VALUES |
| Listed | 2 | 1 | 1 | 1 |
| Unlisted | 331 | 167 | 464 | 139 |
| | 333 | 168 | 465 | 140 |

**NOTE:** *During the year the Group sold its 6.3% shareholding in Société Européenne des Satellites for £160m. The sale was made cum dividend and consequently £4m has been included in operating profit leaving a profit of £133m before tax estimated at £30m. During the year the Group sold its 4.8 million shareholding in Flextech plc for £28m. The profit on sale amounted to £27m before tax estimated at £8m. During the year the Group acquired a 10% stake in Antena 3, a commercial television channel in Spain for £40m. If all investments were realised at valuation there would be an estimated liability for taxation, at year end rates, of £49m.*

| ALL FIGURES IN £ MILLIONS | BSBH | OTHER | TOTAL |
|---|---|---|---|
| **Summary of movements** | | | |
| At 31 December 1997 | 90 | 50 | 140 |
| Exchange differences | — | 5 | 5 |
| Additions | — | 53 | 53 |
| Owned by businesses disposed | — | (5) | (5) |
| Disposals | — | (27) | (27) |
| Release of provisions for permanent diminution in value | — | 2 | 2 |
| **Book value at 31 December 1998** | 90 | 78 | 168 |
| **Valuation at 31 December 1998** | 255 | 78 | 333 |

## 15. Stocks

| | 1998 | 1997 |
|---|---|---|
| ALL FIGURES IN £ MILLIONS | | |
| Raw materials | 32 | 22 |
| Work in progress | 126 | 89 |
| Finished goods | 456 | 268 |
| | 614 | 379 |

**NOTE:** *The replacement cost of stocks is not materially different from book value.*

## 16. Debtors

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Amounts falling due within one year** | | |
| Trade debtors | 763 | 558 |
| Associates | 39 | 17 |
| Other debtors | 198 | 139 |
| Prepayments and accrued income | 105 | 56 |
| | 1,105 | 770 |
| **Amounts falling due after one year** | | |
| Other debtors | 14 | 17 |
| Prepayments and accrued income | 8 | 3 |
| Advance corporation tax recoverable | — | 17 |
| | 22 | 37 |
| | 1,127 | 807 |

**NOTE:** *The Pearson Employee Share Trust and Pearson plc Employee Share Ownership Trust hold 386,977 (1997:326,784) Pearson plc ordinary shares with a market value of £5m at 31 December 1998 (1997:£3m) inclusive of accumulated scrip dividend shares. Amounts included within other debtors for own shares are £2m (1997:£2m).*

## 17. Current asset investments

| ALL FIGURES IN £ MILLIONS | 1998 | | 1997 | |
|---|---|---|---|---|
| | VALUATIONS | BOOK VALUES | VALUATIONS | BOOK VALUES |
| Unlisted | 5 | 5 | 8 | 8 |
| Businesses held for resale | 148 | 148 | — | — |
| | 153 | 153 | 8 | 8 |

**NOTE:** *Investments are at directors' valuations. If all investments were realised at valuation there would be no liability for taxation.*

| ALL FIGURES IN £ MILLIONS | |
|---|---|
| **Summary of movements** | |
| At 31 December 1997 | 8 |
| Owned by businesses acquired (see note 25) | 151 |
| Disposals | (6) |
| **At 31 December 1998** | 153 |

## 18. Cash at bank and in hand

| ALL FIGURES IN £ MILLIONS | 1998 | | 1997 | |
|---|---|---|---|---|
| | GROUP | COMPANY | GROUP | COMPANY |
| Cash, bank current accounts and overnight deposits | 305 | — | 144 | 1 |
| Certificates of deposit and commercial paper | 20 | — | 44 | — |
| Term bank deposits | 20 | 6 | 27 | 14 |
| | 345 | 6 | 215 | 15 |

## 19. Financial instruments

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

| | 1998 | | 1997 | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | GROUP | COMPANY | GROUP | COMPANY |
| **Maturity of borrowings** | | | | |
| **Short term** | | | | |
| Loans or instalments due within one year | — | — | 8 | — |
| Bank loans, overdrafts and commercial paper | 72 | 172 | 305 | 295 |
| Total due within one year | 72 | 172 | 313 | 295 |
| **Medium and long term** | | | | |
| Loans or instalments thereof repayable: | | | | |
| From one to two years | 151 | 151 | 1 | — |
| From two to five years | 2,036 | 1,935 | 242 | 141 |
| After five years not by instalments | 365 | 100 | 366 | 100 |
| Total due after more than one year | 2,552 | 2,186 | 609 | 241 |
| **Total borrowings** | 2,624 | 2,358 | 922 | 536 |

**NOTE:** *In the absence of enforceable contracts from the relevant lenders to refinance current advances as they fall due, at 31 December 1998 £755m (1997:£141m) of debt currently classified from two to five years would be repayable within one year. The short term bank loans, overdrafts and commercial paper of the Group are lower than those of the Company because of bank offset arrangements.*

| | 1998 | | |
|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | GROUP FINANCE LEASES | GROUP OTHER FINANCIAL LIABILITIES | GROUP TOTAL |
| **Maturity of other financial liabilities** | | | |
| Amounts falling due: | | | |
| In one year or less or on demand | 9 | — | 9 |
| In more than one year but not more than two years | 5 | 32 | 37 |
| In more than two years but not more than five years | 4 | 3 | 7 |
| In more than five years | 1 | — | 1 |
| | 19 | 35 | 54 |

| | 1998 | | 1997 | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | GROUP | COMPANY | GROUP | COMPANY |
| **Borrowing by instrument** | | | | |
| **Secured** | | | | |
| Bank loans and overdrafts | — | — | 1 | — |
| **Unsecured** | | | | |
| 10.5% Euro-sterling Bonds 2008 | 100 | 100 | 100 | 100 |
| 9.5% Euro-sterling Bonds 2004 | 117 | — | 117 | — |
| 10.75% Euro-sterling Bonds 2002 | 100 | — | 100 | — |
| Other unsecured borrowings | — | — | 8 | — |
| Unsecured bank loans and overdrafts, commercial paper and medium term notes | 2,307 | 2,258 | 596 | 436 |
| **Total borrowings** | 2,624 | 2,358 | 922 | 536 |

## 19. Financial instruments (cont'd)

| ALL FIGURES IN £ MILLIONS | 1998 |
|---|---|
| **Undrawn committed borrowing facilities** | |
| Expiring within one year | — |
| Expiring between one and two years | 3 |
| Expiring in more than two years | 832 |
| | 835 |

**NOTE:** *All of the above committed borrowing facilities incur commitment fees at market rates.*

| | 1998 | | | | |
|---|---|---|---|---|---|
| | | | | FIXED RATE BORROWINGS | |
| **Currency and interest rate risk profile of borrowings** | BORROWINGS £M | TOTAL VARIABLE RATE £M | TOTAL AT FIXED RATE £M | WEIGHTED AVERAGE INTEREST RATE PER CENT | WEIGHTED AVERAGE PERIOD FOR WHICH RATE IS FIXED – YEARS |
| US dollar | 1,964 | 1,365 | 599 | 6.0 | 4.6 |
| Sterling | 492 | 372 | 120 | 9.4 | 6.3 |
| Spanish peseta | 95 | 95 | — | — | — |
| French franc | 62 | 62 | — | — | — |
| Other currencies | 11 | 11 | — | — | — |
| | 2,624 | 1,905 | 719 | | |

**NOTE:** *The figures shown in the table above take into account interest rate and currency swaps entered into by the Group. Variable rate borrowings bear interest at rates based on relevant national LIBOR equivalents.*

| | 1998 | | | |
|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | OTHER FINANCIAL LIABILITIES | TOTAL VARIABLE RATE | TOTAL FIXED RATE | TOTAL NO INTEREST PAID |
| **Currency and interest rate risk profile of other financial liabilities** | | | | |
| US dollar | 45 | — | 19 | 26 |
| Sterling | 5 | — | — | 5 |
| Spanish peseta | 2 | 2 | — | — |
| Other currencies | 2 | — | — | 2 |
| | 54 | 2 | 19 | 33 |

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

| | 1998 | | | | | |
|---|---|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | NET FOREIGN MONETARY ASSETS/(LIABILITIES) | | | | | |
| | STERLING | US DOLLAR | FRENCH FRANC | SPANISH PESETA | OTHER | TOTAL |
| **Functional currency of entity** | | | | | | |
| Sterling | — | 42 | 1 | 2 | 17 | 62 |
| US dollar | (133) | — | 1 | — | 12 | (120) |
| Spanish peseta | (1) | — | — | — | — | (1) |
| Other currencies | (8) | (8) | — | — | — | (16) |
| | (142) | 34 | 2 | 2 | 29 | (75) |

## 19. Financial instruments (cont'd)

| ALL FIGURES IN £ MILLIONS | 1998 | | | |
|---|---|---|---|---|
| | CASH AT BANK AND IN HAND | SHORT TERM DEPOSITS | OTHER FINANCIAL ASSETS | TOTAL |
| **Currency and interest rate risk profile of financial assets** | | | | |
| US dollar | 123 | 10 | 2 | 135 |
| Sterling | 32 | 17 | — | 49 |
| Spanish peseta | 67 | — | — | 67 |
| French franc | 17 | 3 | 1 | 21 |
| Other currencies | 66 | 10 | 1 | 77 |
| | 305 | 40 | 4 | 349 |
| Floating rate | 199 | 4 | — | 203 |
| Fixed rate | 89 | 36 | — | 125 |
| No interest paid | 17 | — | 4 | 21 |
| | 305 | 40 | 4 | 349 |

**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 7.5%.*

| ALL FIGURES IN £ MILLIONS | 1998 | |
|---|---|---|
| | BOOK VALUE | FAIR VALUE |
| **Primary financial instruments held or issued to finance the Group's operations** | | |
| Other financial assets | 4 | 4 |
| Other financial liabilities | 54 | 54 |
| Cash at bank and in hand | 305 | 305 |
| Short term deposits | 40 | 40 |
| Short term borrowings | 72 | 72 |
| Medium and long term borrowings | 2,552 | 2,635 |
| **Derivative financial instruments held to manage the interest rate and currency profile** | | |
| Interest rate swaps | — | (15) |
| Currency swaps | — | 24 |

**NOTE:** *Other financial assets, other financial liabilities, cash at bank and in hand and short term deposits: the fair value approximates to the carrying value due to the short maturity periods of these financial instruments. ■ 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 1998 the notional principal value of these swaps was £368m. ■ Currency swaps: the fair value of these contracts is based on market values. At 31 December 1998 the Group had £117m of such contracts outstanding. The unrecognised net gain on hedges as at 31 December 1998 amounted to £9m, none of which is expected to be recognised in 1999.*

## 20. Other creditors

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Amounts falling due within one year** | | |
| Trade creditors | 371 | 273 |
| Taxation | 299 | 225 |
| Social security and other taxes | 33 | 27 |
| Other creditors | 101 | 42 |
| Accruals and deferred income | 388 | 282 |
| Obligations under finance leases | 9 | — |
| Dividends | 81 | 69 |
| | 1,282 | 918 |
| **Amounts falling due after one year** | | |
| Trade creditors | 21 | 19 |
| Other creditors | 7 | 5 |
| Accruals and deferred income | 16 | 20 |
| Obligations under finance leases | 10 | 1 |
| | 54 | 45 |

**NOTE:** *Accruals and deferred income includes £7m (1997:£10m) 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% Euro-sterling Bonds 2002. The profit is being amortised over the remaining life of the bonds. £5m is due after one year. None of the amount falls due after five years.*

## 21. Deferred taxation

| ALL FIGURES IN £ MILLIONS | |
|---|---|
| **Summary of movements** | |
| At 31 December 1997 | 37 |
| Exchange differences | 1 |
| Subsidiary undertakings acquired/(disposed) | (14) |
| Net release in the year | (3) |
| Transfer to current taxation | (1) |
| **At 31 December 1998** | 20 |

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Deferred taxation derives from** | | |
| Capital allowances | 7 | 25 |
| Other timing differences | 13 | 12 |
| | 20 | 37 |
| **Deferred taxation not provided** | | |
| Relating to revalued assets and timing differences | (1) | 7 |
| Relating to gains subject to rollover relief | 12 | 18 |
| | 11 | 25 |

## 22. Other provisions for liabilities and charges

| ALL FIGURES IN £ MILLIONS | POST-RETIREMENT | OTHER | TOTAL |
|---|---|---|---|
| At 31 December 1997 | 34 | 141 | 175 |
| Exchange differences | — | (1) | (1) |
| Subsidiary undertakings acquired/disposed | 63 | 31 | 94 |
| Deferred consideration arising on acquisitions | — | 1 | 1 |
| Transfers | — | 7 | 7 |
| Released | (1) | (1) | (2) |
| Provided | 14 | 47 | 61 |
| Utilised | (10) | (72) | (82) |
| **At 31 December 1998** | 100 | 153 | 253 |

**NOTE:** *Post-retirement provisions are in respect of pensions, £30m and post-retirement medical benefits, £70m. Other provisions are mainly in respect of future costs relating to the purchase of subsidiary and associated undertakings £34m, litigation £12m, reorganisations and redundancies £51m, disposals and closures £6m, and lease commitments £35m. Amounts utilised include £5m in respect of provisions relating to subsidiary undertakings acquired.*

## 23. Share capital

| | NUMBER (000's) | £M |
|---|---|---|
| **Authorised** | | |
| Ordinary shares of 25p each | 846,000 | 212 |
| **At 31 December 1998** | 846,000 | 212 |
| **Called up, allotted and fully paid** | | |
| Ordinary shares of 25p at 31 December 1997 | 576,772 | 144 |
| Issued under share option and employee share schemes | 3,611 | 1 |
| Issued under scrip dividend scheme | 292 | — |
| Issued under placing | 28,880 | 7 |
| **At 31 December 1998** | 609,555 | 152 |

**NOTE:** *The ordinary shares referred to above, as defined in the memorandum and articles of association of the Company, are equivalent to equity shares as defined by FRS4. The consideration received in respect of shares issued during the year was £347m (1997: £27m). Options granted under certain of the Company's employee share option schemes were adjusted following the demerger of Royal Doulton plc. In the case of those 'Save As You Earn' and executive share options which were not adjustable, compensation is to take the form of additional Pearson shares distributed from an employee share trust when the options are exercised. If all these options are exercised the maximum amount of equity shares to be issued is estimated at 12,145 under the Save for Shares scheme and 10,822 under the executive schemes. Shares issued include £3m under the scrip dividend plan.*

## 23. Share capital (cont'd)

| Options outstanding at 31 December 1998 | WHEN GRANTED | NUMBER OF SHARES (000s) | ORIGINAL SUBSCRIPTION PRICE (P) | EXERCISE PERIOD |
|---|---|---|---|---|
| Worldwide Save for Shares plans | 1991 | 64 | 299 | 1996 – 1999 |
| | 1992 | 268 | 242 | 1997 – 2000 |
| | 1994 | 478 | 509 | 1999 – 2002 |
| | 1995 | 583 | 436 | 2000 – 2003 |
| | 1996 | 455 | 578 | 2001 – 2004 |
| | 1997 | 601 | 593 | 2000 – 2005 |
| | 1998 | 1,674 | 769 | 2001 – 2006 |
| | | 4,123 | | |
| Executive share option plans | 1989 | 10 | 376 | 1992 – 1999 |
| | 1990 | 231 | 307 – 334 | 1993 – 2000 |
| | 1991 | 59 | 364 – 377 | 1994 – 2001 |
| | 1992 | 275 | 327 – 379 | 1995 – 2002 |
| | 1993 | 125 | 396 | 1996 – 2003 |
| | 1994 | 460 | 635 | 1997 – 2004 |
| | 1995 | 658 | 545 | 1998 – 2005 |
| | 1996 | 1,316 | 654 – 682 | 1999 – 2006 |
| | 1997 | 2,605 | 744 – 757 | 2000 – 2007 |
| | 1998 | 3,167 | 948 – 1,090 | 2001 – 2008 |
| | | 8,906 | | |

**NOTE:** *The subscription prices have been rounded down to the nearest whole penny.*

## 24. Reserves

| ALL FIGURES IN £ MILLIONS | SHARE PREMIUM ACCOUNT | REVALUATION RESERVE | OTHER RESERVES | PROFIT AND LOSS ACCOUNT | TOTAL |
|---|---|---|---|---|---|
| **Summary of movements** | | | | | |
| At 31 December 1997 | 158 | 3 | 1 | (154) | 8 |
| Exchange differences | — | — | — | (8) | (8) |
| Premium on issue of 33m equity shares | 340 | — | — | (1) | 339 |
| Goodwill arising (see note 25) | — | — | — | (16) | (16) |
| Goodwill written back (see note 26) | — | — | — | 262 | 262 |
| Realisation of revaluation reserve | — | (2) | — | 2 | — |
| Profit retained for the year | — | — | — | 311 | 311 |
| **At 31 December 1998** | 498 | 1 | 1 | 396 | 896 |
| **Analysed as:** | | | | | |
| Partnerships and other associates | — | — | 1 | 2 | 3 |
| Group excluding partnerships and other associates | 498 | 1 | — | 394 | 893 |

**NOTE:** *Cumulative goodwill relating to acquisitions made prior to 1998, which was deducted from reserves, amounts to £1,912m (1997: £2,162m). Had the Group continued to apply its previous policy in respect of goodwill, an additional £2,348m would have been included in the goodwill reserve, which would have then shown a balance of £4,254m. Retained profit for the year would have been £323m reflecting the lack of amortisation of goodwill in respect of subsidiaries. The Group's balance sheet would have shown net liabilities of £1,246m at 31 December 1998. ■ During 1998 Pearson plc received £17m on the issue of shares in respect of the exercise of options awarded under various share option plans. Employees paid £16m to the Group for the issue of these shares and the balance of £1m comprised contributions to the qualifying employee share ownership trust (QUEST) from subsidiary undertakings.*

## 25. Acquisitions

In November 1998 the Group acquired the education, reference and business & professional publishing divisions of Simon & Schuster Inc. All acquisitions have been consolidated applying acquisition accounting principles.

| ALL FIGURES IN £ MILLIONS | 1998 SIMON & SCHUSTER | 1998 OTHER | 1998 TOTAL | 1997 TOTAL |
|---|---|---|---|---|
| **Acquisition analysis of subsidiaries and businesses** | | | | |
| Tangible fixed assets | 126 | 17 | 143 | 2 |
| Stocks | 299 | — | 299 | 36 |
| Debtors | 306 | 5 | 311 | 64 |
| Current asset investments | 151 | — | 151 | — |
| Creditors | (236) | (22) | (258) | (80) |
| Provisions | (86) | — | (86) | (4) |
| Deferred taxation | (1) | 2 | 1 | — |
| Equity minority interests | — | 2 | 2 | 1 |
| Net (borrowing)/cash acquired | (3) | 1 | (2) | (117) |
| Net assets/(liabilities) acquired at fair value | 556 | 5 | 561 | (98) |
| Fair value of consideration: | | | | |
| Cash | (2,865) | (53) | (2,918) | (252) |
| Deferred cash consideration | — | 1 | 1 | (19) |
| Costs accrued | (3) | (1) | (4) | — |
| Net prior year adjustments | — | (4) | (4) | (15) |
| Total consideration | (2,868) | (57) | (2,925) | (286) |
| **Goodwill arising** | 2,312 | 52 | 2,364 | 384 |
| Analysed as: | | | | |
| Goodwill capitalised | 2,312 | 36 | 2,348 | — |
| Goodwill written off to reserves | — | 16 | 16 | 384 |
| | 2,312 | 52 | 2,364 | 384 |

**NOTE:** *Goodwill written off to reserves relates to acquisitions made before 1 January 1998.*

| ALL FIGURES IN £ MILLIONS | 1998 SIMON & SCHUSTER | 1998 OTHER | 1998 TOTAL |
|---|---|---|---|
| **Acquisition goodwill and fair values** | | | |
| Acquisition cost | 2,868 | 57 | 2,925 |
| Book value of net assets acquired | 569 | 15 | 584 |
| Fair value adjustments | (13) | (10) | (23) |
| Fair value to the Group | 556 | 5 | 561 |
| **Goodwill arising** | 2,312 | 52 | 2,364 |

**NOTE:** *Other fair value adjustments comprise the revaluation of net assets £(12)m and adjustments to tax £2m.*

## 25. Acquisitions (cont'd)

| ALL FIGURES IN £ MILLIONS | BOOK VALUE AT 27 NOV | ACCOUNTING POLICY ALIGNMENT | REVALUATIONS | OTHER ITEMS | PROVISIONAL FAIR VALUE |
|---|---|---|---|---|---|
| **Simon & Schuster** | | | | | |
| Tangible fixed assets | 137 | — | (9) A | (2) | 126 |
| Stocks | 364 | (9) | (19) B | (37) | 299 |
| Debtors | 389 | (41) | (21) C | (21) | 306 |
| Current asset investments | — | — | — | 151 | 151 |
| Creditors | (237) | — | (31) D | 32 | (236) |
| Provisions | (70) | — | (16) E | — | (86) |
| Deferred tax | (11) | — | 10 F | — | (1) |
| Net borrowing | (3) | — | — | — | (3) |
| **Net liabilities acquired** | 569 | (50) | (86) | 123 | 556 |

**NOTE:** *Simon & Schuster was acquired at the end of 1998 and therefore all fair value adjustments are provisional.*

### Accounting policy alignment

Simon & Schuster's accounting policies have been changed to make them consistent with Pearson Education's accounting policies. The main items are to expense internal software product development costs capitalised by Simon & Schuster's software publishing company and to expense freight costs as incurred.

### Revaluations

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

**B.** Pre publication expenditure has been reduced by £12m to its net realisable value. This relates primarily to titles required to be sold under the Department of Justice ruling. Finished goods of £5m have also been written off in respect of obsolete product to bring it to net realisable value.

**C.** Debtors have been reduced by £19m to bring them to their net realisable value. This is principally to increase the reserve for returns to reflect current return rates.

**D.** Additional accruals have been made, primarily for remuneration and retention obligations (£28m) existing at acquisition date. A further £6m has been included in provisions in respect of this.

**E.** Provisions have been made for various outstanding legal claims and other remuneration obligations (refer above) identified at acquisition.

**F.** Deferred taxation liabilities recorded in respect of the US have been written off as the availability of tax losses in the Pearson US Group means that these obligations will not crystallise within the reasonably foreseeable future. Deferred tax has not been provided on the revaluations described above to the extent that they arise in the US.

### Other items

Other items relate to the businesses of Simon & Schuster that Pearson do not intend to retain. The net assets of these businesses have not been consolidated in the individual balance sheet lines, but are included in current asset investments at the anticipated net proceeds from sale.

| ALL FIGURES IN £ MILLIONS | 1 JANUARY 1998 TO 27 NOVEMBER 1998 | 1 JANUARY 1997 TO 31 DECEMBER 1997 |
|---|---|---|
| **Simon & Schuster financial information** | | |
| Sales | 1,001 | 1,153 |
| Operating profit | 54 | 157 |
| Profit before taxation | 51 | 149 |

The above results are shown using the accounting policies of Simon & Schuster prior to acquisition (before goodwill amortisation). Taxation numbers are not available as the taxation of Simon & Schuster was accounted for as part of a larger group. Accordingly, no statement of recognised gains and losses is presented.

## 25. Acquisitions (cont'd)

| ALL FIGURES IN £ MILLIONS | COST | NET ASSETS ACQUIRED | 1998 GOODWILL |
|---|---|---|---|
| **Total goodwill arising on acquisitions** | | | |
| Subsidiaries and businesses (see page 79) | 2,925 | 561 | 2,364 |
| Associates | 13 | 13 | — |
| | 2,938 | 574 | 2,364 |

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Cash flow from acquisitions** | | |
| Cash – current year acquisitions (see page 79) | 2,918 | 252 |
| Deferred payments for prior year acquisitions and other items | 18 | 17 |
| **Net cash outflow** | 2,936 | 269 |

**NOTE:** *Contributions to the cash flow from acquisitions in 1998 are as follows: net cash inflow from operating activities £15m, returns on investments and servicing of finance £(1)m, taxation £(1)m, and capital expenditure and financial investment £(7)m.*

## 26. Disposals

| ALL FIGURES IN £ MILLIONS | 1998 MINDSCAPE INC. | PEARSON NEW ENTER-TAINMENT | THE TUSSAUDS GROUP | OTHER | TOTAL | 1997 TOTAL |
|---|---|---|---|---|---|---|
| **Disposal analysis of subsidiaries and businesses** | | | | | | |
| Tangible fixed assets | (2) | (4) | (183) | (14) | (203) | (4) |
| Investments | (5) | — | — | — | (5) | — |
| Associates | — | — | (6) | — | (6) | — |
| Stocks | (4) | (3) | (3) | (6) | (16) | (12) |
| Debtors | (19) | (21) | (7) | (19) | (66) | (14) |
| Creditors and taxation | 1 | 36 | 15 | 32 | 84 | 3 |
| Provisions | 2 | — | — | (10) | (8) | (3) |
| Deferred taxation | — | — | 13 | — | 13 | (1) |
| Equity minority interest | — | — | — | (30) | (30) | 1 |
| Net borrowing | — | (4) | (5) | (2) | (11) | (1) |
| Net (assets)/liabilities disposed of | (27) | 4 | (176) | (49) | (248) | (31) |
| Proceeds received | 91 | 125 | 352 | 194 | 762 | 62 |
| Deferred consideration | — | — | — | 2 | 2 | 3 |
| Costs | (5) | (8) | (5) | (24) | (42) | (4) |
| Net prior year adjustments | — | — | — | — | — | (1) |
| Profit on sale | 59 | 121 | 171 | 123 | 474 | 29 |
| Goodwill written back | (70) | (80) | (14) | (81) | (245) | (9) |
| **Net profit/(loss) on sale** | (11) | 41 | 157 | 42 | 229 | 20 |

**NOTE:** *Included within 'other' above are the following: the sale of the Law & Tax publishing business for £66m giving rise to a profit of £61m; the sale of 20% of Recoletos for £87m giving rise to a profit on sale of £34m; the sale of the Register Group for £8m giving rise to a loss on sale of £20m; and a £10m loss on the closure of certain Simon & Schuster businesses.*

## 26. Disposals (cont'd)

| ALL FIGURES IN £ MILLIONS | 1998 |
|---|---|
| **Total goodwill written back on disposal** | |
| On disposal of subsidiaries | 245 |
| On disposal of associates | 16 |
| On disposal by associates | 1 |
| | 262 |

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Cash flow from disposals** | | |
| Cash – current year disposals (see page 81) | 762 | 62 |
| Costs paid | (38) | (3) |
| Deferred receipts and payments from prior year disposals and other amounts | (6) | (5) |
| **Net cash inflow** | 718 | 54 |

**NOTE:** *Contributions to the cash flow from disposals in 1998 are as follows: net cash inflow from operating activities £45m, returns on investments and servicing of finance £(3)m, taxation £(11)m and capital expenditure and financial investment £(14)m.*

## 27. Notes to consolidated statement of cash flows

| | 1998 | | | 1997 | | |
|---|---|---|---|---|---|---|
| ALL FIGURES IN £ MILLIONS | CONTINUING | DISCONTINUED | TOTAL | CONTINUING | DISCONTINUED | TOTAL |
| **A. Reconciliation of operating profit to net cash inflow from operating activities** | | | | | | |
| Operating profit – total | 229 | 21 | 250 | 295 | 33 | 328 |
| Share of profit of partnerships and other associates | (53) | 2 | (51) | (43) | (4) | (47) |
| Depreciation charges | 54 | 12 | 66 | 49 | 16 | 65 |
| Goodwill amortisation | 12 | — | 12 | — | — | — |
| Decrease/(increase) in stocks | 43 | 1 | 44 | 7 | (2) | 5 |
| (Increase)/decrease in debtors | (67) | 5 | (62) | (131) | (8) | (139) |
| Increase/(decrease) in creditors | 113 | — | 113 | (8) | 4 | (4) |
| Increase/(decrease) in operating provisions | 2 | — | 2 | (3) | (1) | (4) |
| Other and non-cash items | 28 | — | 28 | (1) | 1 | — |
| **Net cash inflow from operating activities*** | 361 | 41 | 402 | 165 | 39 | 204 |
| Purchase of fixed assets and finance leases | (113) | (13) | (126) | (93) | (18) | (111) |
| Sale of operating tangible fixed assets | 12 | 1 | 13 | 14 | — | 14 |
| Dividends from partnerships and other associates | 53 | — | 53 | 40 | — | 40 |
| Other | 25 | 2 | 27 | 10 | 2 | 12 |
| **Operating cash flow** | 338 | 31 | 369 | 136 | 23 | 159 |

**Net cash inflow for 1998 includes a £7m outflow relating to exceptional items charged in 1998 and a £14m outflow relating to exceptional items charged in prior years.*

## 27. Notes to consolidated statement of cash flows (cont'd)

| ALL FIGURES IN £ MILLIONS | CASH | OVER-DRAFTS | SUB-TOTAL | SHORT TERM DEPOSITS | DEBT DUE WITHIN ONE YEAR | DEBT DUE AFTER ONE YEAR | FINANCE LEASES | TOTAL |
|---|---|---|---|---|---|---|---|---|
| **B. Analysis of net debt** | | | | | | | | |
| At 31 December 1997 | 144 | (23) | 121 | 71 | (290) | (609) | (1) | (708) |
| Exchange differences | (30) | 1 | (29) | 14 | — | 10 | — | (5) |
| Acquired with subsidiary* | — | — | — | — | — | — | (19) | (19) |
| Disposed with subsidiary* | — | — | — | — | 5 | 1 | — | 6 |
| Debt issue costs | — | — | — | — | — | 21 | — | 21 |
| Other non-cash items | — | — | — | — | — | (1) | — | (1) |
| Net cash flow | 191 | (45) | 146 | (45) | 280 | (1,974) | 1 | (1,592) |
| **At 31 December 1998** | 305 | (67) | 238 | 40 | (5) | (2,552) | (19) | (2,298) |
| At 31 December 1996 | 139 | (69) | 70 | 160 | (105) | (555) | (2) | (432) |
| Exchange differences | (8) | (11) | (19) | — | — | (3) | — | (22) |
| Acquired with subsidiary* | — | — | — | — | (54) | (66) | — | (120) |
| Transfers | — | — | — | — | (8) | 8 | — | — |
| Net cash flow | 13 | 57 | 70 | (89) | (123) | 7 | 1 | (134) |
| **At 31 December 1997** | 144 | (23) | 121 | 71 | (290) | (609) | (1) | (708) |

*Excluding cash and overdrafts.

**NOTE:** *Finance leases are included within other creditors in the balance sheet (see note 20).*

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **C. Reconciliation of net cash flow to movement in net debt** | | |
| Decrease in net debt from net cash flow | 146 | 70 |
| (Increase) in net debt from management of liquid resources | (45) | (89) |
| (Increase) in net debt from other borrowings | (1,694) | (116) |
| Decrease in finance leases | 1 | 1 |
| Acquired with subsidiary | (19) | (120) |
| Disposed with subsidiary | 6 | — |
| Debt issue costs | 21 | — |
| Other non cash items | (1) | — |
| Exchange differences | (5) | (22) |
| Movement in net debt in the year | (1,590) | (276) |
| Net debt at beginning of year | (708) | (432) |
| **Net debt at end of year** | (2,298) | (708) |

**D. Tax paid** includes £3m (1997: £4m of credits) relating to items excluded from operating profit.

## 28. Commitments under leases

At 31 December 1998, the Group had commitments under leases other than finance leases, to make payments in 1999 as follows:

| ALL FIGURES IN £ MILLIONS | LAND AND BUILDINGS | OTHER |
|---|---|---|
| **For leases expiring:** | | |
| In 1999 | 6 | 2 |
| Between 2000 and 2003 | 25 | 18 |
| Thereafter | 32 | 6 |
| | 63 | 26 |

## 29. 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 associates. In addition there are contingent liabilities of the Group in respect of legal claims and general partnership interests (see note 13). None of these claims is expected to result in a material gain or loss to the Group.

## 30. Related parties

**Associates** Loans and equity advanced to associates during the year and at the balance sheet date are shown in note 13. Amounts falling due from partnerships and other associates are set out in note 16. Dividends receivable from partnerships and other associates are set out in note 13. Details of individually significant transactions are shown below.

**Troll Communications LLC** During 1997 the Group sold its 44.1% interest in the equity of Troll Communications LLC. £2m in interest income on the subordinated debt and £1m dividend income on the preferred stock were earned in the period to 31 December 1997. As at 31 December 1997 no interest was outstanding and no dividend was outstanding.

**Port Aventura SA** During the year the Group sold its 40.5% interest in the equity of Port Aventura SA. Management fees of £nil (1997: £2m) were earned in the period of which none (1997: £1m) was outstanding at the year end.

**Channel 5 Television Group Ltd** The Group has a 24% economic interest in the equity of Channel 5 Television Group Ltd. During the year £32m of loans were repaid (1997: £47m advanced).

During the year the Group provided £24m (1997: £23m) 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 (1997: £2m) for Channel 5 Engineering Services Ltd, a subsidiary of Channel 5 Television Group Ltd. At 31 December 1998 £6m was outstanding (1997: £6m).

**European Channel Management Ltd** During the year the Group sold its 45% interest in European Channel Management Ltd. During the year the Group paid £1m (1997: £1m) for £6m (1997: £4m) of tax losses.

**UK TV** The Group has a 20% interest in UK TV. During the year the Group provided programmes and services to the value of £1m (1997: £3m) none of which was outstanding at the year end (1997: £nil).

**Grundy associates** During the year the Group received £6m (1997: £4m) for management fees, format rights and royalties from a number of associates of Grundy Worldwide Ltd, none of which (1997: £nil) was outstanding at the year end. No individual transactions were material to the Group.

**Magyar-RTL** The Group has a 20% interest in Magyar-RTL. During the year £2m of loans were advanced (1997: £4m).

During the year the Group provided programmes and services to the value of £1m (1997: £nil) none of which was outstanding at the year end (1997: £nil).

**Lazard Partnership** Details of the ownership structure and profit sharing arrangements are set out in note 13.

The Group periodically places funds on deposit with the Lazard Houses. The investments are made on an arm's length basis and no transactions are individually material in the context of the Group treasury transactions. The Group also uses the Lazard Houses to provide professional advice. Fees for such services for the year to 31 December 1998 totalled £5m (1997: £4m).

**Other** There were no transactions with directors and officers of the Company.

## 31. Company balance sheet as at 31 December 1998

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 | NOTE |
|---|---|---|---|
| **Fixed assets** | | | |
| Investments: | | | |
| Subsidiaries | 2,598 | 1,963 | 32 |
| | 2,598 | 1,963 | |
| **Current assets** | | | |
| Debtors: | | | |
| Advance corporation tax recoverable | — | 17 | |
| Subsidiaries – due within one year | 2,774 | 687 | |
| Subsidiaries – due after one year | 1,268 | 535 | |
| Other debtors | 8 | 7 | |
| Prepayments and accrued income | 10 | 7 | |
| Cash at bank and in hand | 6 | 15 | 18 |
| | 4,066 | 1,268 | |
| **Creditors – amounts falling due within one year** | | | |
| Short term borrowing | (172) | (295) | 19 |
| Subsidiaries | (2,082) | (931) | |
| Taxation | (5) | (11) | |
| Other creditors | — | (1) | |
| Accruals and deferred income | (28) | (11) | 32 |
| Dividends | (79) | (69) | |
| | (2,366) | (1,318) | |
| **Net current assets/(liabilities)** | 1,700 | (50) | |
| **Total assets less current liabilities** | 4,298 | 1,913 | |
| **Creditors – amounts falling due after more than one year** | | | |
| Medium and long term borrowing | (2,186) | (241) | 19 |
| Subsidiaries | (225) | (225) | |
| Accruals and deferred income | (5) | (8) | 32 |
| **Provisions for liabilities and charges** | | | |
| Deferred taxation | (1) | — | 32 |
| Other provisions for liabilities and charges | (2) | (2) | |
| | (2,419) | (476) | |
| **Net assets** | 1,879 | 1,437 | |
| **Capital and reserves** | | | |
| Called up share capital | 152 | 144 | 23 |
| Share premium account | 498 | 158 | 32 |
| Special reserve | 397 | 397 | 32 |
| Other reserves | 50 | 50 | 32 |
| Profit and loss account | 782 | 688 | 32 |
| **Equity shareholders' funds** | 1,879 | 1,437 | |

The financial statements were approved by the board of directors on 10 March 1999 and signed on its behalf by

Sir Dennis Stevenson

John Makinson

## 32. Notes to the company balance sheet

| ALL FIGURES IN £ MILLIONS | 1998 | 1997 |
|---|---|---|
| **Tangible fixed assets (leasehold property)** | | |
| Cost | 1 | 1 |
| Depreciation | (1) | (1) |
| **Net book value** | — | — |

**NOTE:** *There were no capital commitments for fixed assets at 31 December 1998.*

| ALL FIGURES IN £ MILLIONS | |
|---|---|
| **Investment in subsidiaries** | |
| At 31 December 1997 | 1,963 |
| Acquisition from subsidiaries | 22 |
| Subscription for additional share capital in subsidiaries | 700 |
| Disposals | (89) |
| Revaluations | 2 |
| **At 31 December 1998** | 2,598 |

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

| ALL FIGURES IN £ MILLIONS | |
|---|---|
| **Deferred taxation** | |
| At 31 December 1997 | — |
| Charged in the year | (1) |
| **At 31 December 1998** | (1) |

**NOTE:** *Deferred taxation derives from other timing differences.*

**Accruals and deferred income** Accruals and deferred income includes £7m (1997: £10m) 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% Euro-sterling Bonds 2002. The profit is being amortised over the remaining life of the Bonds. £5m is due after one year. None of the amount falls due after five years.

## 32. Notes to the company balance sheet (cont'd)

| ALL FIGURES IN £ MILLIONS | SHARE PREMIUM ACCOUNT | SPECIAL RESERVE | OTHER RESERVES | PROFIT AND LOSS ACCOUNT | TOTAL |
|---|---|---|---|---|---|
| **Reserves** | | | | | |
| **Summary of movements** | | | | | |
| At 31 December 1997 | 158 | 397 | 50 | 688 | 1,293 |
| Premium on issue of 33m equity shares | 340 | — | — | — | 340 |
| Profit for the financial year | — | — | — | 220 | 220 |
| Dividends | — | — | — | (126) | (126) |
| **At 31 December 1998** | 498 | 397 | 50 | 782 | 1,727 |

**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

| Subsidiaries | COUNTRY OF INCORPORATION OR REGISTRATION |
|---|---|
| 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. | |
| **FT Group** | |
| Financial Times Group Ltd* | England |
| Les Echos SA | France |
| Recoletos Compañiá Editorial SA (76.4%) | Spain |
| **Pearson Education** | |
| Addison Wesley Longman, Inc. | US |
| Pearson Education Ltd | England |
| Prentice Hall Inc. | US |
| Silver BurdettGin Inc. | US |
| **The Penguin Group** | |
| Penguin Putnam Inc. | US |
| The Penguin Publishing Co Ltd | England |
| Penguin Books Australia Ltd | Australia |
| **Pearson Television** | |
| Pearson Television Ltd* | England |
| Thames Television Ltd | England |
| Pearson Television North America Inc. | US |
| Pearson Television International Ltd | England |

**Direct investment of Pearson plc.*

| Associates | COUNTRY OF INCORPORATION OR REGISTRATION | BENEFICIAL INTEREST % | CLASS OF SHARE | SHARE CAPITAL £M | ACCOUNTING YEAR END |
|---|---|---|---|---|---|
| **FT Group** | | | | | |
| The Economist Newspaper Ltd | England | 50 | Ord 5p | 1.1 | March |
| | | 100 | 'B' 5p | 0.1 | |
| | | Nil | 'A' 5p | | |
| | | Nil | Trust 5p | — | |
| **Pearson Television** | | | | | |
| Channel 5 Television Group Ltd | England | 20 | Ord 1p voting | 0.8 | December |
| | | 25 | Ord 1p non-voting | 4.0 | |
| | | 19.2 | Preference | — | |
| | | 1.7 | Deferred | — | |

The principal partnerships are shown on page 70.

# Five year summary

| ALL FIGURES IN £ MILLIONS | 1994 | 1995 | 1996 | 1997 | **1998** |
|---|---|---|---|---|---|
| **Sales** | | | | | |
| Continuing operations | 1,260 | 1,484 | 1,830 | 2,011 | 2,251 |
| Discontinued operations | 290 | 346 | 356 | 282 | 144 |
| | 1,550 | 1,830 | 2,186 | 2,293 | 2,395 |
| **Profits** * | | | | | |
| FT Group | 54 | 68 | 89 | 108 | 114 |
| Pearson Education | 44 | 23 | 60 | 60 | (34) |
| The Penguin Group | 35 | 26 | (73) | 58 | 46 |
| Pearson Television | 68 | 65 | 40 | 26 | 61 |
| Cedar Fair | 7 | 10 | 16 | — | — |
| Lazard | 30 | 40 | 41 | 43 | 42 |
| **Continuing operations** | 238 | 232 | 173 | 295 | 229 |
| Discontinued operations | 33 | 35 | 16 | 33 | 21 |
| **Operating profit** | 271 | 267 | 189 | 328 | 250 |
| Operating profit before goodwill and other items | 271 | 267 | 289 | 328 | 389 |
| Profit/(loss) on sale of fixed assets and investments | 27 | 123 | (14) | 23 | 142 |
| Profit/(loss) on sale of businesses and associates | 15 | 6 | 229 | (180) | 276 |
| **Profit before interest** | 313 | 396 | 404 | 171 | 668 |
| **Net interest payable*** | (15) | (31) | (37) | (42) | (39) |
| Loan stock redemption premium | — | — | (10) | — | — |
| **Profit before taxation** | 298 | 365 | 357 | 129 | 629 |
| Taxation | (74) | (93) | (109) | (89) | (188) |
| **Profit after taxation** | 224 | 272 | 248 | 40 | 441 |
| Equity minority interests | (1) | (11) | (8) | (2) | (4) |
| **Profit for the financial year** | 223 | 261 | 240 | 38 | 437 |
| **Earnings per equity share** ** | 40.4p | 47.1p | 42.8p | 6.6p | 74.1p |
| **Diluted earnings per equity share** | 39.9p | 46.4p | 42.5p | 6.4p | 73.3p |
| **Adjusted earnings per equity share** *** | 34.1p | 28.8p | 30.6p | 34.9p | 42.0p |
| **Dividends per equity share** | 15.0p | 16.5p | 18.0p | 19.5p | 21.0p |

**FRS9 'Associates and Joint Ventures' has been adopted and, accordingly, prior year figures have been restated to reflect associates' interest in net interest payable. **FRS14 'Earnings Per Share' has been adopted and, accordingly, prior year figures have been restated. ***Adjusted in accordance with note 9. Other items comprise a £100m charge for Penguin improper accounting in 1996 and Year 2000 costs of £7m and integration costs of £120m in 1998.*

# Five year summary

| ALL FIGURES IN £ MILLIONS | 1994 | 1995 | 1996 | 1997 | **1998** |
|---|---|---|---|---|---|
| **Capital employed** | | | | | |
| Net assets | 1,052 | 856 | 393 | 156 | 1,084 |
| Deferred tax and other provisions | 234 | 134 | 189 | 212 | 273 |
| Net debt | 146 | 63 | 430 | 707 | 2,279 |
| | 1,432 | 1,053 | 1,012 | 1,075 | 3,636 |
| **Share statistics** | | | | | |
| Equity shares – weighted average** | 551.4m | 554.1m | 560.6m | 572.8m | 589.8m |
| Share price – year end | 555p | 624p | 750p | 791p | 1193p |
| Share price – high | 725p | 684p | 760p | 849p | 1193p |
| Share price – low | 554p | 543p | 601p | 665p | 757p |
| **Average number employed** | | | | | |
| Continuing operations | 10,761 | 12,540 | 13,741 | 14,526 | 15,579 |
| Discontinued operations | 6,454 | 6,882 | 6,206 | 3,780 | 2,821 |
| | 17,215 | 19,422 | 19,947 | 18,306 | 18,400 |

*** FRS14 'Earnings Per Share' has been adopted and, accordingly, prior year figures have been restated.*

# 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 Systems (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 another address, please inform our Registrar, Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA. Telephone 01903 502541.

**UK tax on capital gains** At 31 March 1982, the base date for capital gains tax, the value of each of the Company's ordinary shares (adjusted for the one for one capitalisation issues in May 1985 and June 1992) was 62p. The market quotations of Pearson plc ordinary shares and Royal Doulton plc ordinary shares on the first day of dealing in Royal Doulton shares, following the demerger in 1993, as calculated in accordance with section 272(3) of the Taxation of Chargeable Gains Act 1992 and as derived from the London Stock Exchange Daily Official List on 2 December 1993 were:

| | |
|---|---|
| Pearson plc ordinary shares of 25p | 592p |
| Royal Doulton plc ordinary shares of £1 | 203.5p |

**Personal Equity Plans (PEPs)** Following the Government's proposal to restrict the tax advantages of PEPs, the Company has arranged that Lloyds TSB Registrars will offer Individual Savings Accounts (ISAs) in Pearson shares. Existing Corporate PEP and Single Company PEP holders who require further information about their PEPs should ring the Halifax helpline on Freephone 0800 371769.

**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 stockbrokers, Cazenove & Co., 12 Tokenhouse Yard, London EC2R 7AN. Telephone 0171 588 2828.

**Information about the Pearson share price** The current price of Pearson ordinary shares can be obtained from Financial Times CityLine on telephone 0891 433620. Calls are charged at 40p per minute cheap rate and 50p per minute at all other times, inclusive of VAT.

**American Depository Receipts (ADRs)** Pearson introduced a sponsored Level One ADR programme in March 1995. Each ADR represents one ordinary share. The programme is administered by the Bank of New York, ADR Department, 101 Barclay Street, New York, NY 10286, telephone 1 800 524 4458. However, as holders of ADRs are not registered shareholders, they do not automatically have the right to receive the Pearson report and accounts or other communications, nor are they able to attend or vote at the Annual General Meeting.

**Advisers** AUDITORS PricewaterhouseCoopers ▪ BANKERS Midland Bank plc, National Westminster Bank Plc ▪ BROKER Cazenove & Co. ▪ FINANCIAL ADVISERS Lazard Brothers & Co. Limited, J. Henry Schroder & Co. Limited ▪ SOLICITORS Freshfields, Herbert Smith and Morgan, Lewis & Bockius.

**FINANCIAL CALENDAR FOR 1999**

| | | |
|---|---|---|
| Ex-dividend date | MONDAY | 22 MARCH |
| Record date | FRIDAY | 26 MARCH |
| Despatch of dividend reinvestment information | MONDAY | 26 APRIL |
| Annual General Meeting | FRIDAY | 30 APRIL |
| Last date for dividend reinvestment election | THURSDAY | 20 MAY |
| Payment date for dividend | FRIDAY | 4 JUNE |
| Share purchase date for dividend reinvestment | FRIDAY | 4 JUNE |
| Interim results | MONDAY | 2 AUGUST |
| Interim dividend | | OCTOBER |

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# Principal offices


**Pearson plc**
*registered office*

3 Burlington Gardens, London W1X 1LE, UK
**TEL** 0171 411 2000 **FAX** 0171 411 2390
**WEB SITE** http://www.pearson.com
**E-MAIL** *firstname.lastname*@pearson.com
**REGISTERED NUMBER** 53723 (England)

**Pearson Inc.**

30 Rockefeller Plaza, 50th floor
New York City, NY 10112-5095, USA
**TEL** 001 212 641 2400 **FAX** 001 212 641 2500
**E-MAIL** *firstname.lastname*@pearson-inc.com

**Pearson Education**

One Lake Drive
Upper Saddle River, NJ 07458, USA
**TEL** 001 201 236 7000 **FAX** 001 201 236 3381
**E-MAIL** *firstname.lastname*@pearsoned.com

**Penguin Group**

375 Hudson Street
New York City, NY 10014, USA
**TEL** 001 212 366 2000 **FAX** 001 212 366 2666
**E-MAIL** *initiallastname*@penguin.com

**Pearson Television**

1 Stephen Street
London W1P 1PJ, UK
**TEL** 0171 691 6000 **FAX** 0171 691 6100
**E-MAIL** *firstname.lastname*@pearsontv.com

**Financial Times Group**

Number One Southwark Bridge
London SE1 9HL, UK
**TEL** 0171 873 3000 **FAX** 0171 407 5700
**E-MAIL** *firstname.lastname*@ft.com

**Les Echos**

46 Rue la Boétie
Paris 75008, France
**TEL** 00 33 149 53 6565 **FAX** 00 33 142 89 1400
**E-MAIL** *initiallastname*@lesechos.fr

**Recoletos**

Paseo de la Castellana 66
28046 Madrid, Spain
**TEL** 00 34 91 337 3220 **FAX** 00 34 91 337 3771
**E-MAIL** *initiallastname*@recoletos.es