

PEARSON



**Lehman Brothers  
New York Media Conference**

14 June 2006

# PEARSON



**Robin Freestone**

Chief Financial Officer

# Agenda

## Introduction

### School

#### Steve Dowling/Doug Kubach

- Special needs education (AGS)
- Teacher certification (NES)
- Student Information Systems (PowerSchool and Chancery)

### Higher Education/International

#### Will Ethridge/Jim Behnke

- Content + (EET)
- International expansion (PBM)

# Strong organic growth

## 2005 results

Sales **£4.1bn**

**9%**

Adjusted EPS **34.1p**

**24%**

Free cash flow/share **54p**

**52%**

ROIC **7.2%**  
**(CER)**

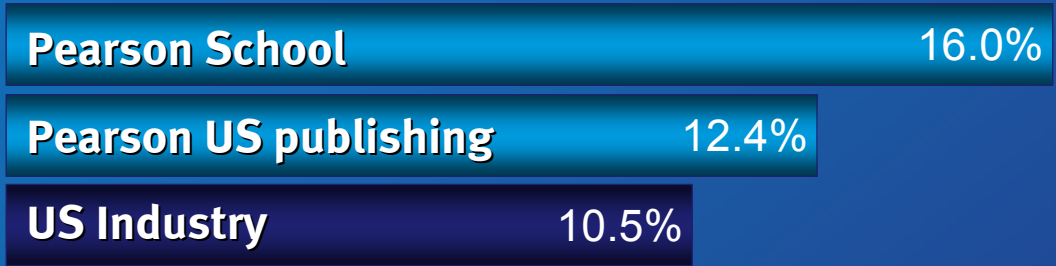
**1.0 pts**

Dividend **27p/**  
**share**

**6%**

# Faster growth 2005 market share gains

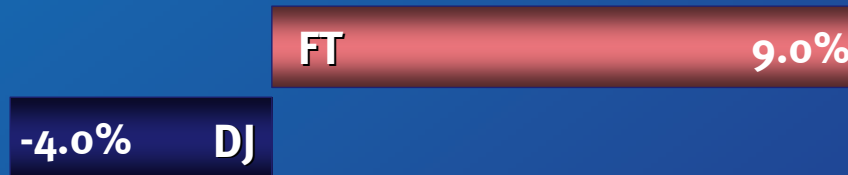
## School



## Higher Education



## Business advertising



## Financial information



Sources: AAP, company reports, Pearson estimates

# Our track record

Year	Publishing	Financial information
2002	Abrams, DDC	SPS
2003	Edexcel, LessonLab	Comstock
2004	Altona Ed, BBC Children's, Causeway, Dominie Press, KAT	Futuresource
2005	AGS, BBC Adult, Co-nect, Index Books	IS Teledata

**Total acquisition cost : \$700m**

**2005 ROIC : 14%**

Represents pro-forma 2005 results and includes integration costs

# 2006 acquisitions

2006	Company	2005 revenues
Jan	<b>Promissor</b> Professional testing	\$68m
Apr	<b>Effective Education Technologies (EET)</b> Adaptive learning	n/a
Apr	<b>National Evaluation Systems (NES)</b> Teacher certification	\$73m
May	<b>Paravia Bruno Mondadori (PBM)</b> Italian curriculum content	€70m
May	<b>PowerSchool</b> Student information	n/a
May	<b>Chancery</b> Student Information	n/a

Source: Pearson

# Bolt-on acquisitions: Our financial goals

- Hurdle rates based on:
  - IRR
  - Payback
- ROIC\* > WACC in first full year
- Earnings\* accretive in first full year

\*After integration costs



# **Bolt-on acquisitions: Our operating goals**

- Build on existing leadership positions
- Expand our market opportunity
- Good, reliable growth markets
- Extend our competitive advantage
- Clear synergies and rapid integration

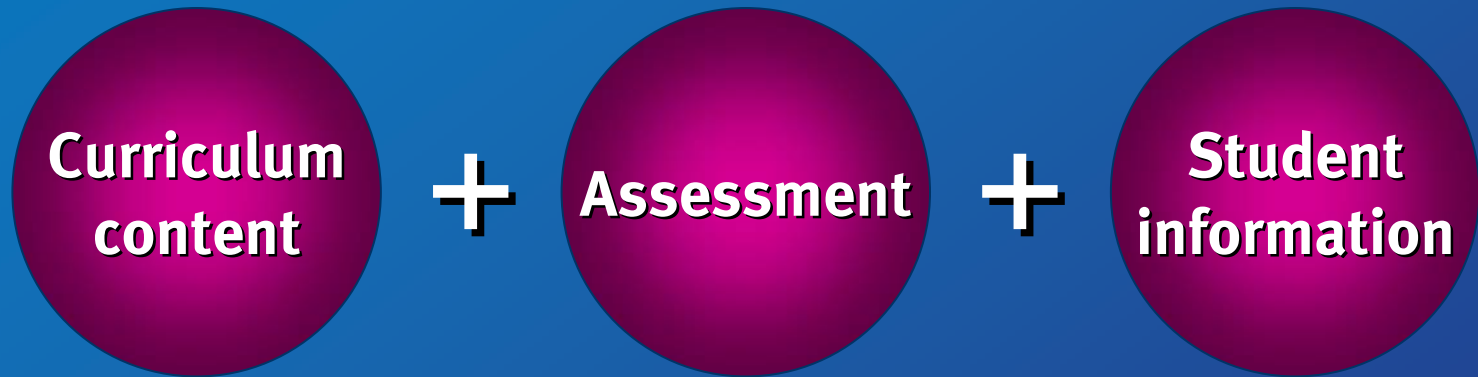
# PEARSON



**Steven Dowling**

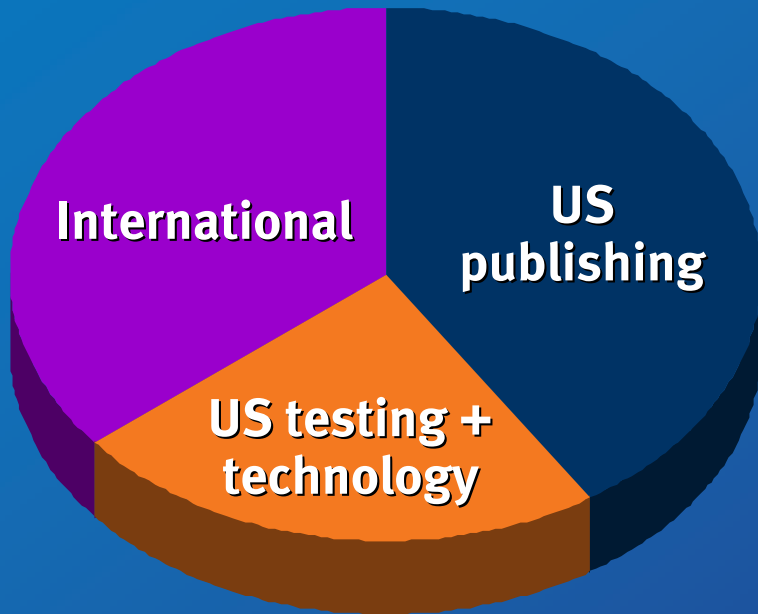
President and CEO  
Pearson School Companies

# Our School strategy



**Personalised learning  
and effective education**

# Our School business: strength in breadth



**2005 SALES : £1.3BN**

## Above-market growth in 2005

- Total School business +16%
- US publishing +12.4%
- Testing up 20%+
- Technology +9%
- Margins +150bp to 11.4%

# School: Solid growth in 2006

- US K-12 publishing market level with 2005
  - New adoption opportunity lower at \$620m
  - Pearson participation higher at 95%
  - Good growth in open territories, supplemental
- Breadth of school business counts again
  - Good growth in testing, technology, international
  - Further margin improvement

**3-5% SALES GROWTH; HIGHER MARGINS**

# School: Healthy adoption cycle

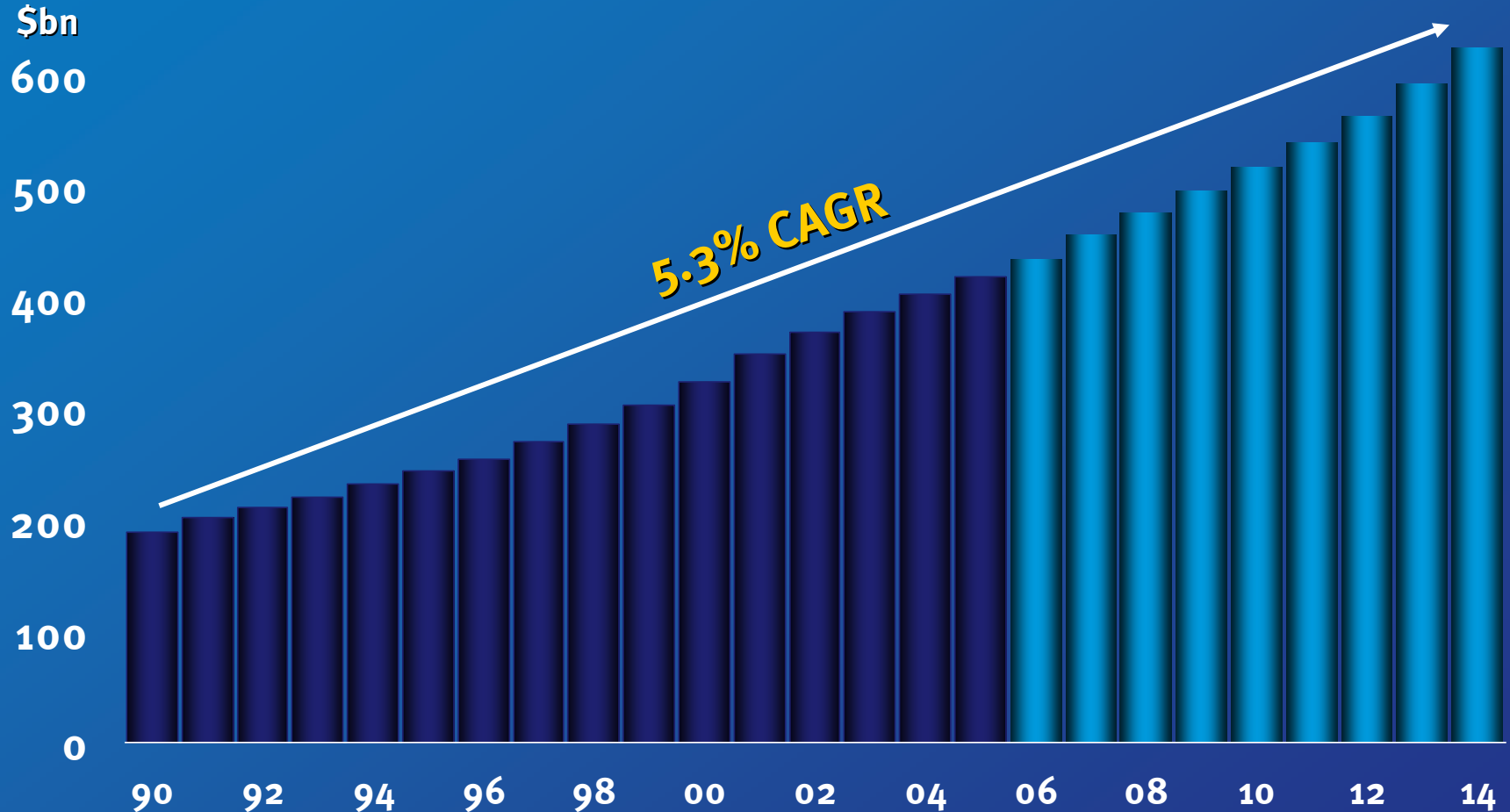
## Estimated Opportunity

## Pearson participation



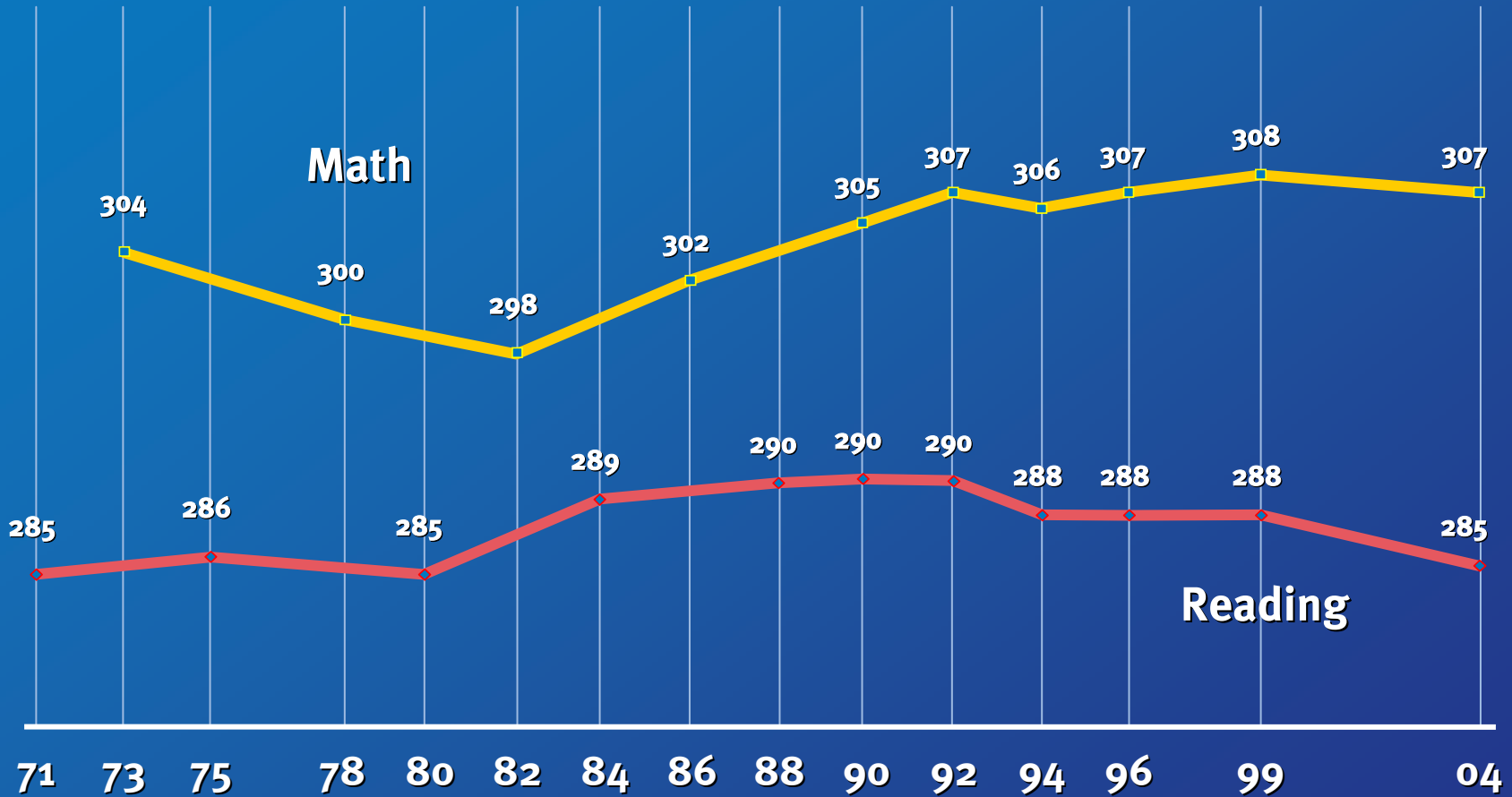
# School: Long-term growth

## Total spending US public schools



Source: National Centre for Education Statistics  
2009-2014 – Pearson estimates

# Student performance is languishing



Source: US Dept Education, Institute of Education Sciences, National Center for Education Statistics, National Assessment of Educational Progress (NAEP), selected years, 1973-2004 Long-Term Trend Mathematics Assessments

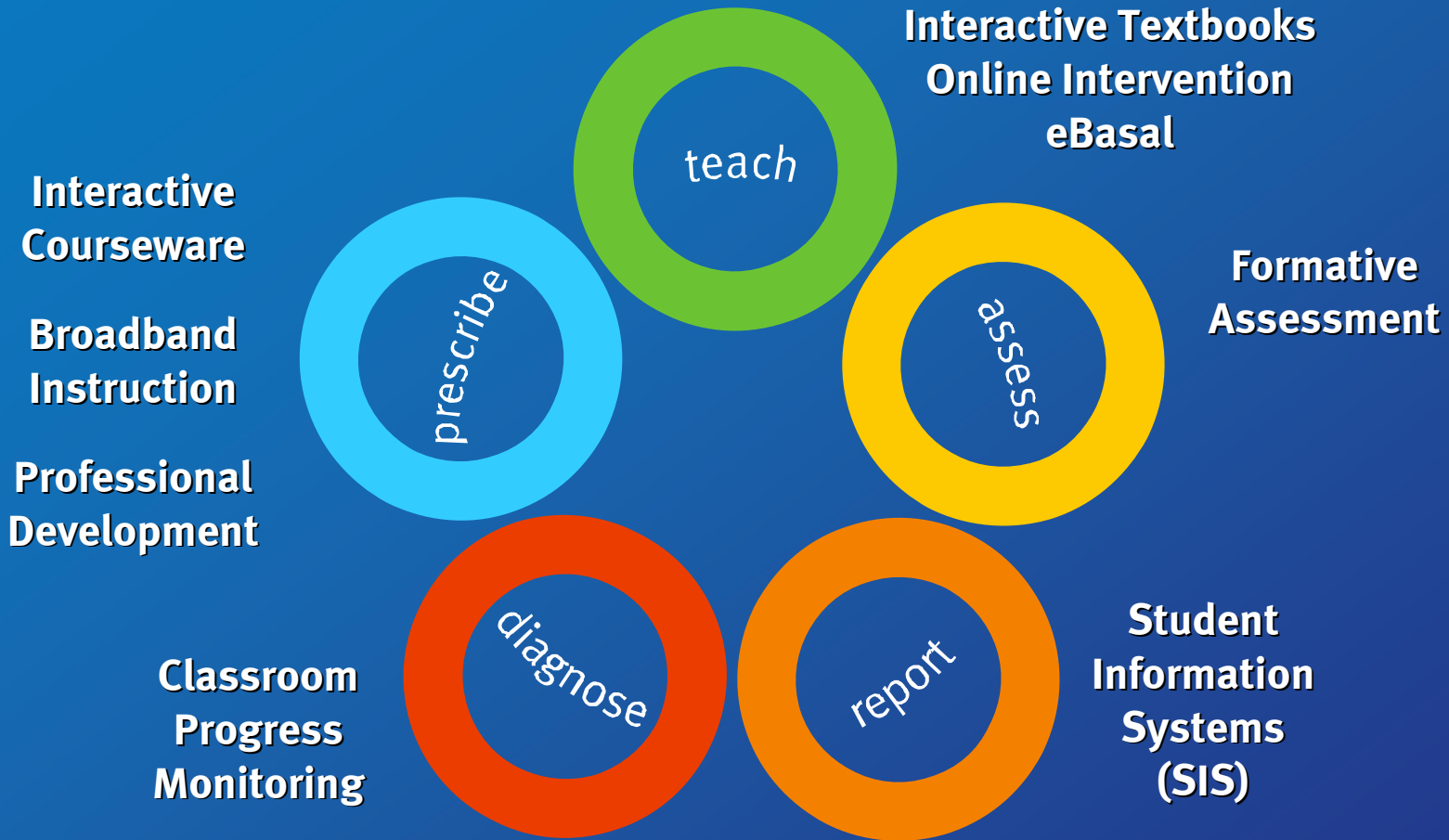


# The School market: NCLB

- Focus on student performance
  - Schools measure student (AYP) performance through annual tests
  - Requires complex data management and reporting
  - Identifies struggling students
  - Informed intervention through formative assessment and personalised instruction
- Student results linked to teacher quality and professional development

***More than one quarter of US schools are failing to meet 'AYP' and face escalating sanctions***

# Our School strategy



**The essentials of personalised learning**

# PEARSON



**Douglas Kubach**

President/CEO

US Assessments & Testing

# Market leadership in testing

## School and professional testing revenues

05 **\$810m**

04 **\$613m**

03 **\$507m**

02 **\$293m**

01 **\$282m**



# Our US businesses



Large-scale educational measurement services, primarily for states, the US government, and national organizations.  
*(High-stakes summative assessments)*



Tests, surveys and data capture tools and technologies for classroom, clinical and corporate settings.  
*(Diagnostic and formative assessments)*

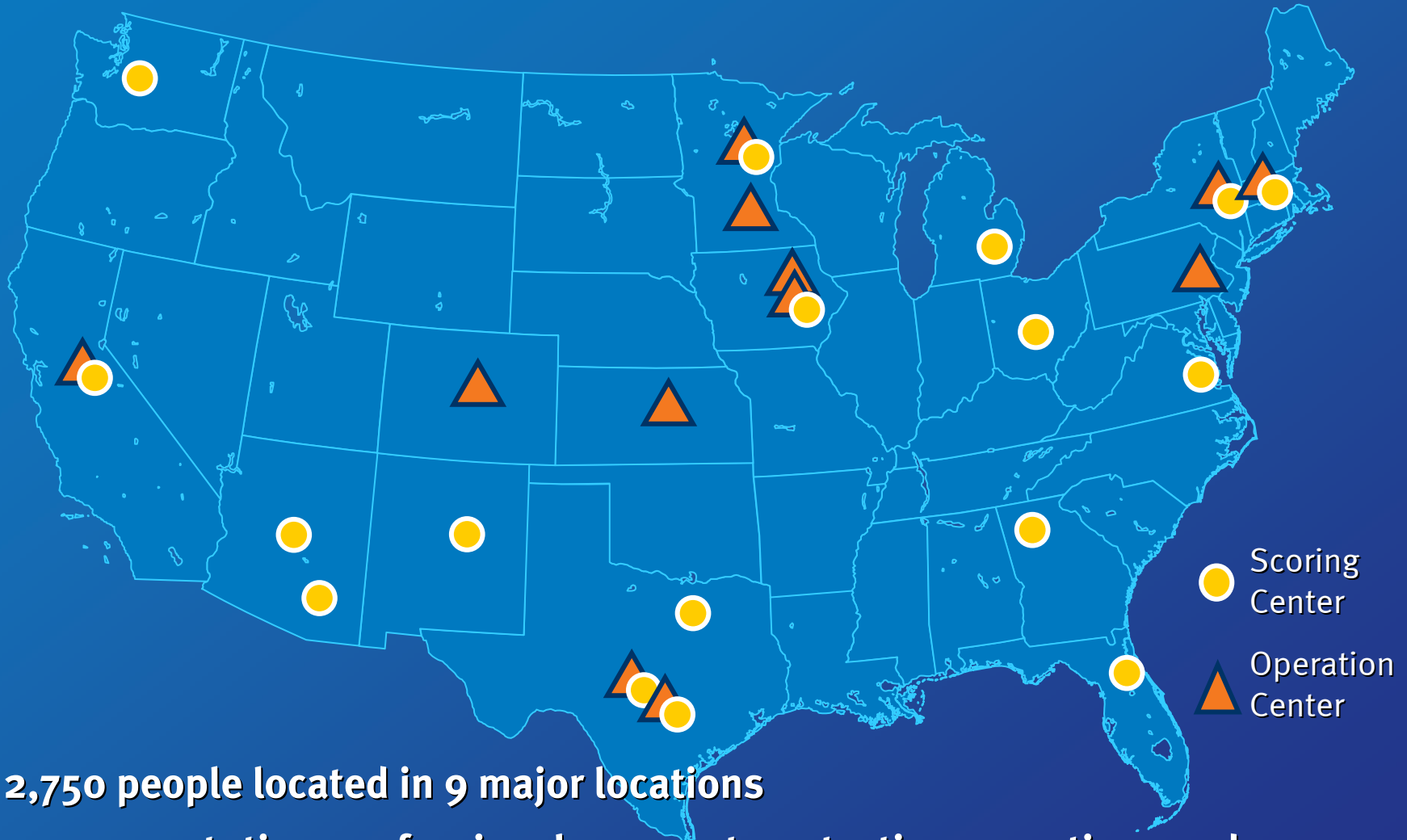


Automated tools for reading and writing assessment and practice.



Teacher certification testing programs customized to state standards

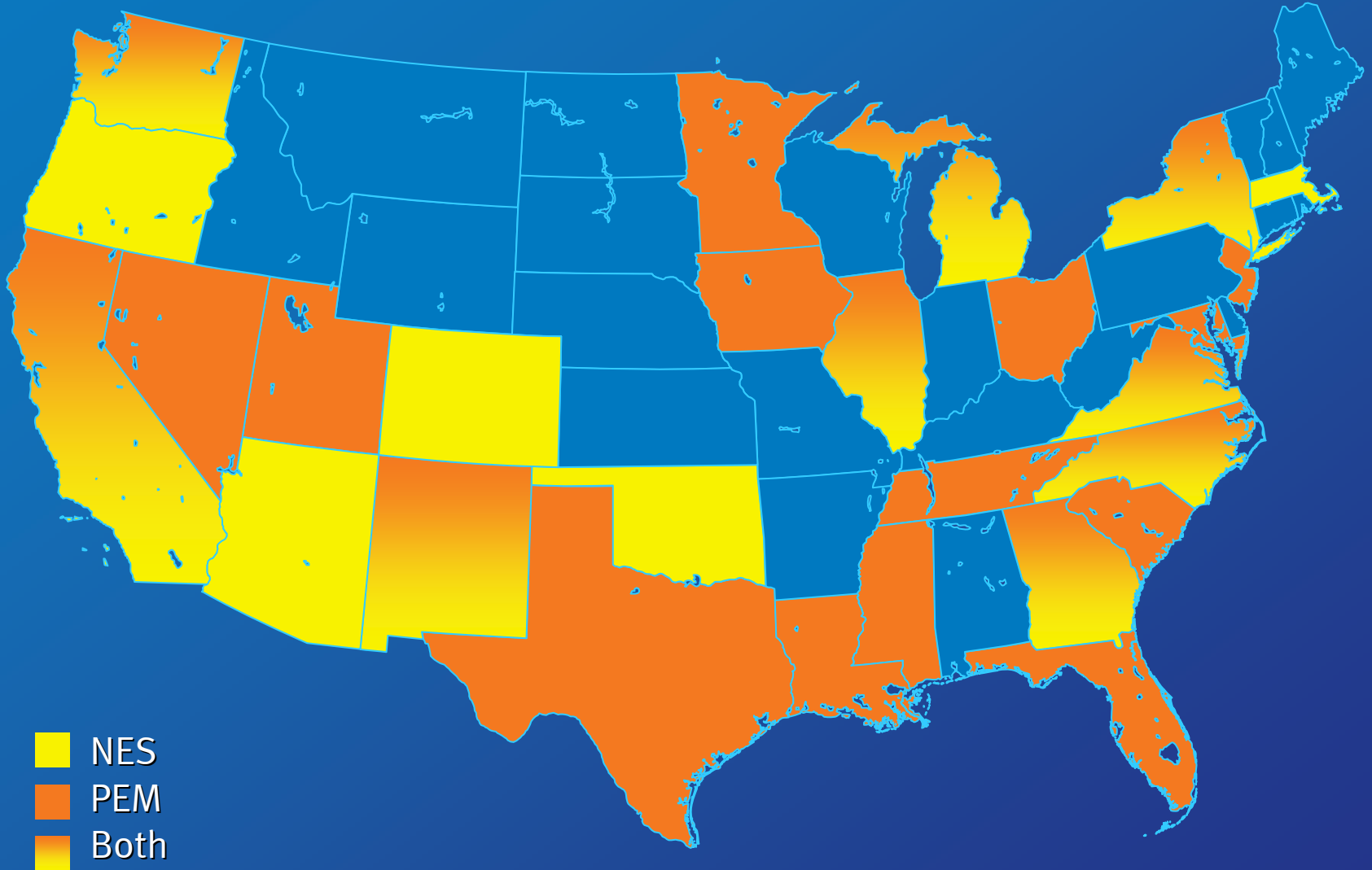
# Our people and locations



**2,750 people located in 9 major locations**

**35,000 part-time professionals support our testing operations and Performance Scoring**

# State testing contracts

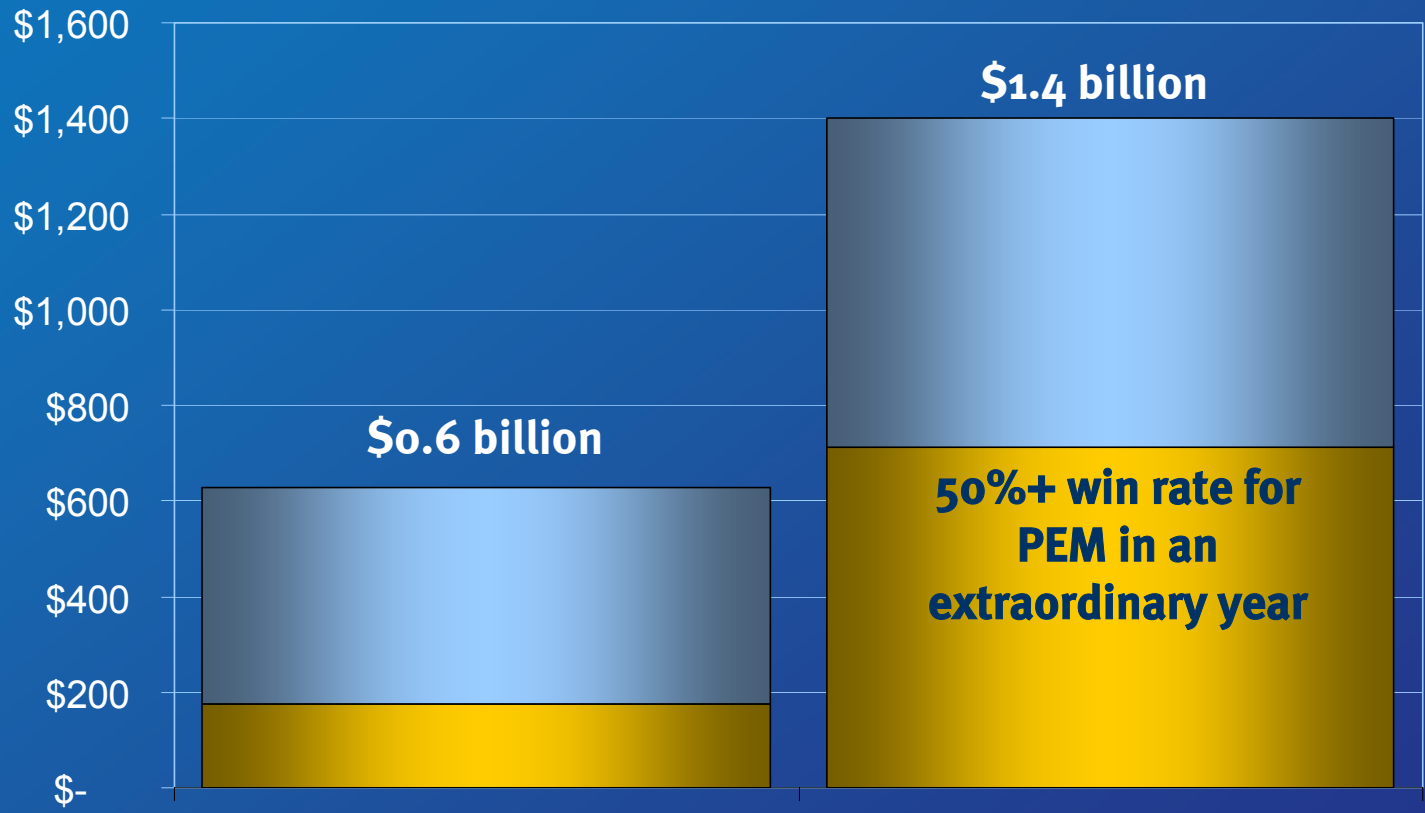


# PEM success in 2005

## Statewide student testing market

Lifetime value of contracts awarded (\$M)

PEM Others



2004

2005

50%+ win rate for PEM in an extraordinary year



# NES: (National Evaluation Systems)



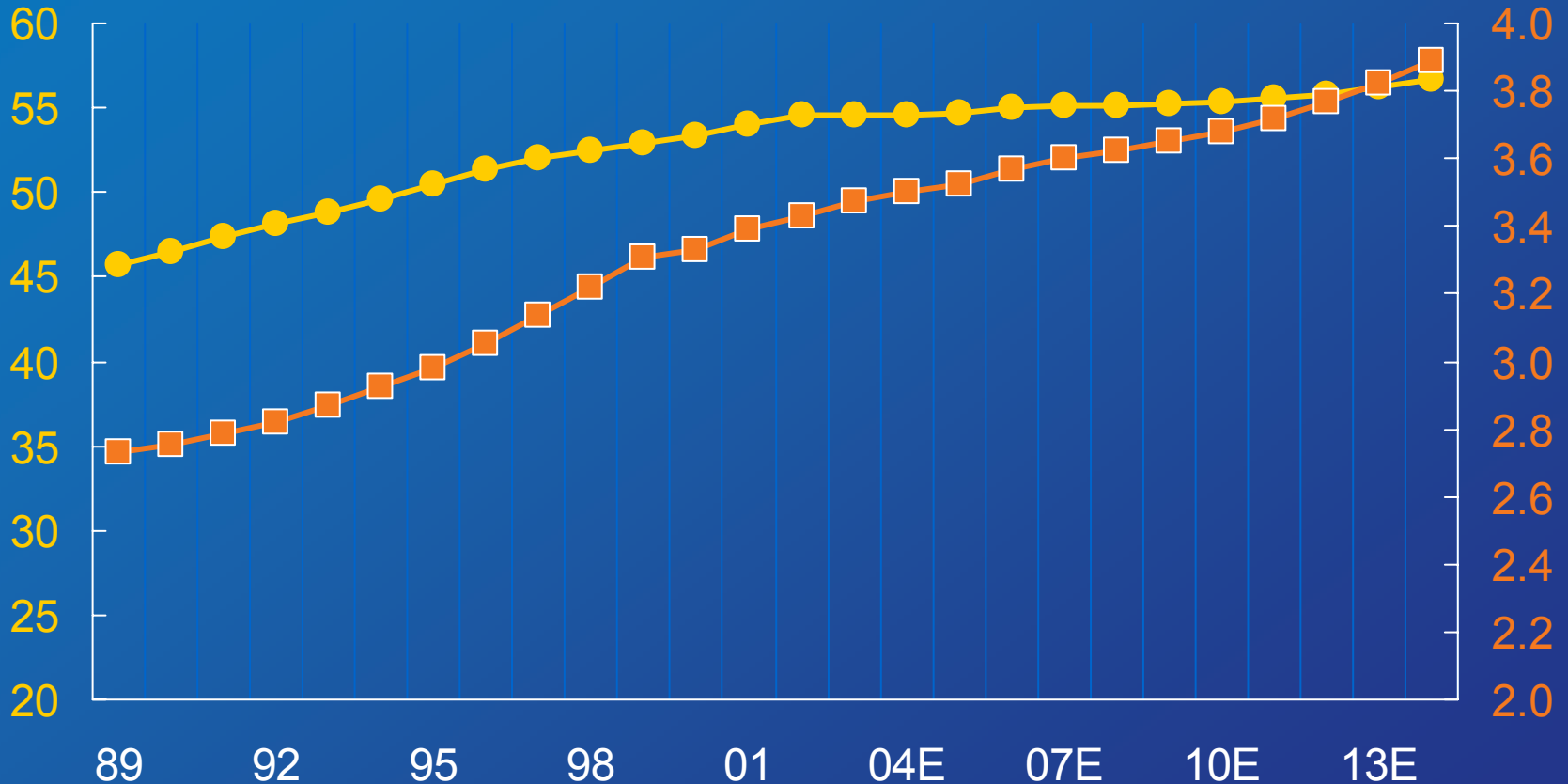
- Leader in customised state assessments for teacher certification;
  - 100 subject areas
- Develops and administers must-have licensure tests for new or transferring teachers
- Long-term contracts with fifteen states (c. 1 million tests/yr)
- Controls entire process from research, test development and psychometrics, through to test administration, processing and scoring

# Favourable demographics: Growth and demand for teacher certification

Number of K-12 students and teachers

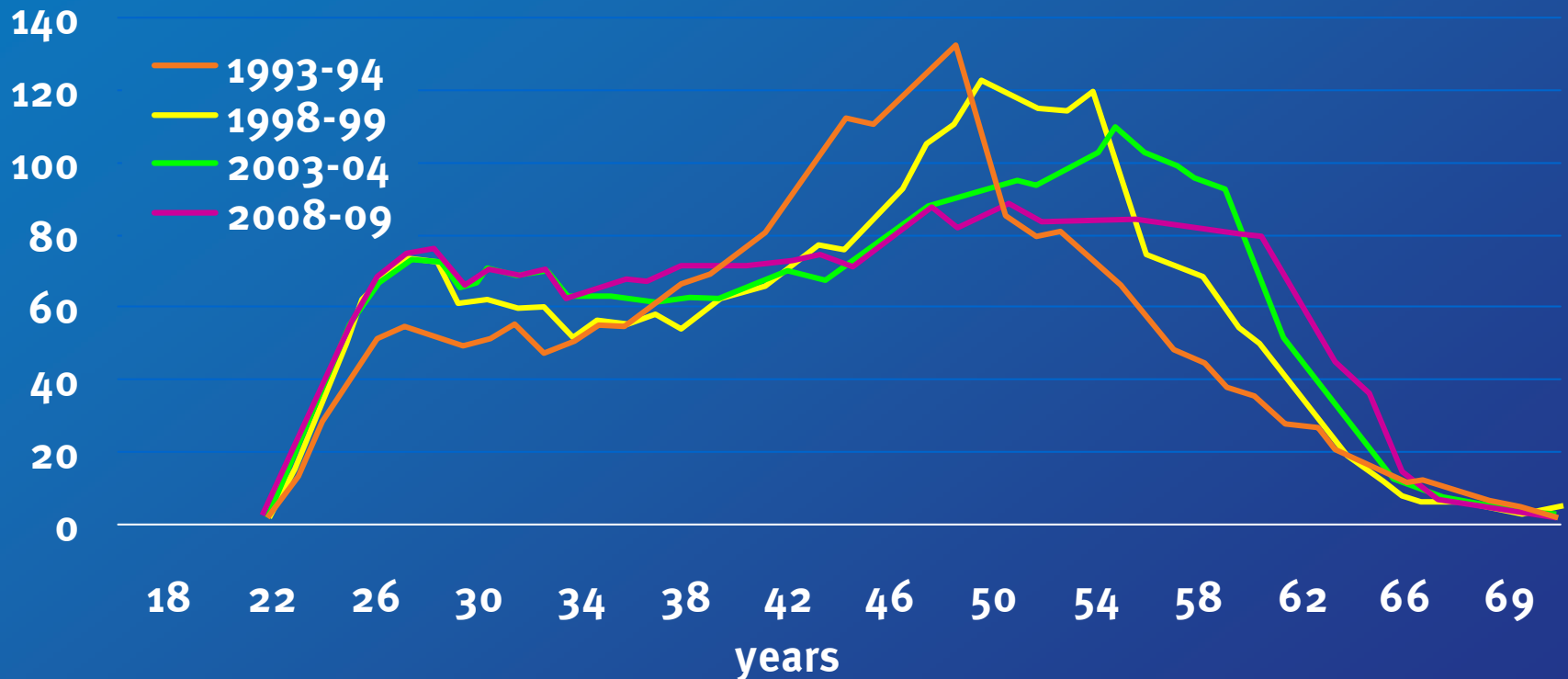
Students (m)

Teachers (m)



# Retirements driving growth for new teacher certification

Number of teachers (000s)\*



Source : NCES

\* Full-time-equivalent public school teachers using constant pupil/teacher ratio and continuation rates

# AGS: (American Guidance Services)

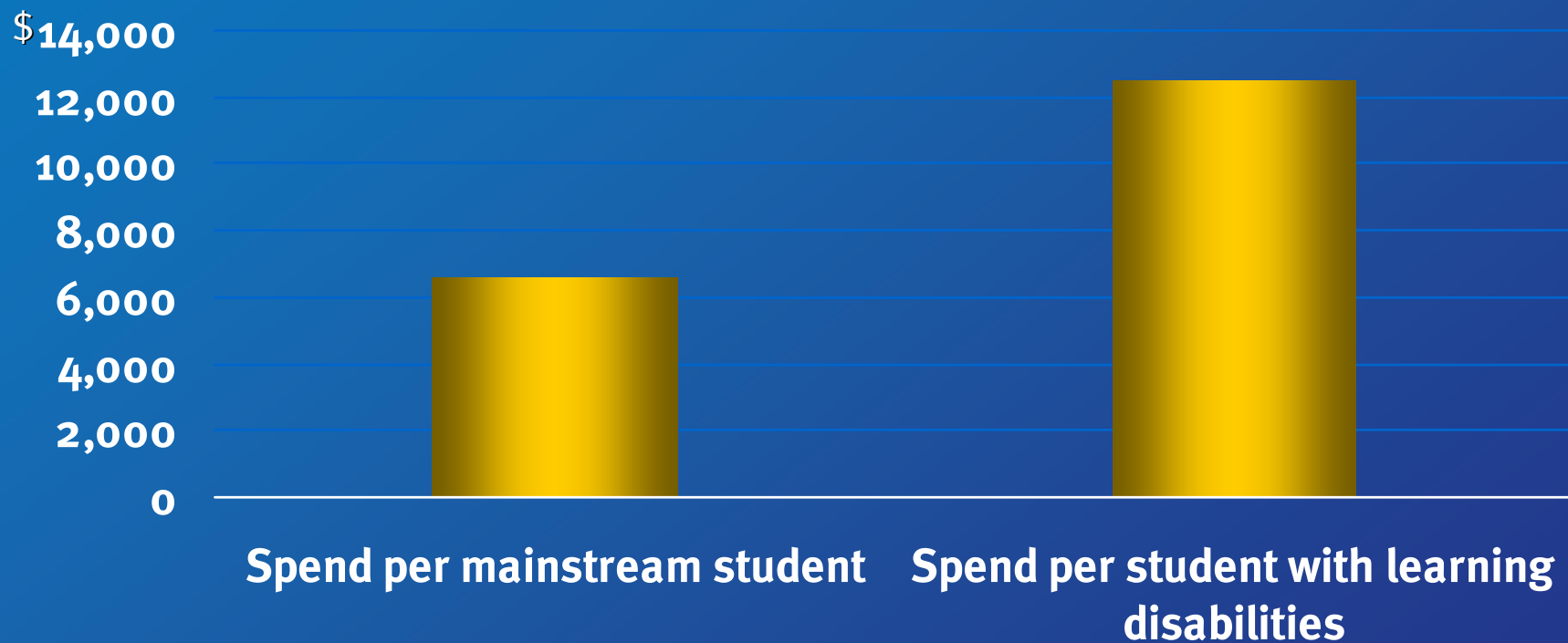
- Pearson acquires AGS in July 2005
- Publisher of assessments and curriculum materials for preK- adults primarily for struggling and special needs students
- Approximately 2/3 of sales in assessments
- \$23M operating profit in 2004

# More special needs students

- Almost 3M special needs students in US
- NCLB requires AYP for ALL students
- Special needs students were excluded from state reporting of test results prior to NCLB
- AGS assessments diagnose individual needs for rapid and effective intervention and remediation
- AGS curriculum materials provide prescriptive instruction for special needs students

# Special needs: higher spend per student

## Federal expenditure per student



# AGS:

## Clear synergies and rapid integration

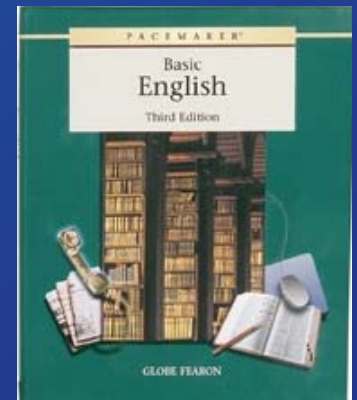
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Assessments

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AGS Globe

- Complete integration in 2006
- AGS assessment products folded into Pearson Assessments
- Adds complementary products in growing special needs segment
- AGS curriculum products combined with Globe Fearon imprint
- Create dedicated business focused on 6-12 supplemental curriculum segment



# The new Pearson Assessments

- #1 in classroom and school assessment systems
- #1 in personality, behavioral, social assessments
- #2 in speech language, hearing, and career interest and skills assessments
- #3 in achievement and ability assessments
- Focus on fast-growing formative/standards-based achievement market segment



- Full service provider of testing and ancillary services
  - Test development
  - Test delivery
  - Content management and testing software
  - Licensing services
- Own exam content tailored for suitability state-by-state
- Clear synergies and rapid integration
  - Test centers
  - Technology
  - G&A

# Pearson VUE:

## A global leader in professional testing



- Delivering over 4 million exams annually
- 4,400 test centers
- 151 countries
- 19 languages
- 12 currencies
- Multilingual service centers throughout the world

# Markets we serve



## PEARSON VUE

Distance Learning

Financial Services

Information Technology

Health and Medicine

Academic Admissions

Human Resources

Driving Assessments

## PROMISSOR

Insurance

Nurse Aide

Real Estate

Cosmetology

U.K. Awarding Bodies

# NES, AGS and PROMISSOR: Value-added benefit

- NES and PROMISSOR expand addressable market into attractive adjacent market
- AGS increases our strength in an existing market with good cost synergy potential
- Together they:
  - Benefit from Pearson assessment technology
  - Use existing capabilities
  - Are good growth markets
  - Build on competitive strength
  - Bring strong management teams
  - Are earnings and value enhancing

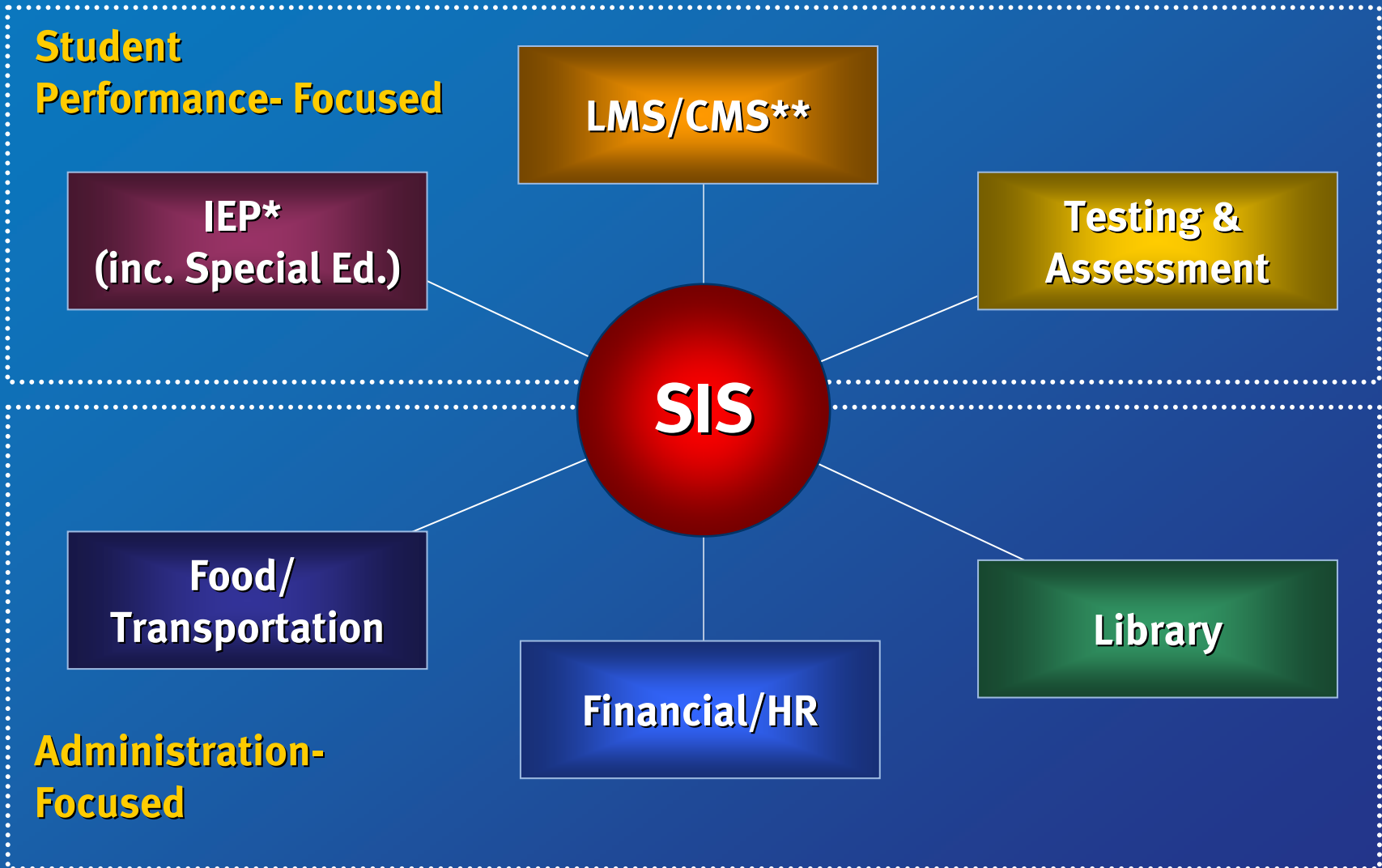


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**PowerSchool and Chancery:  
Student Information Systems**

# SIS is the education hub



Source: Pearson

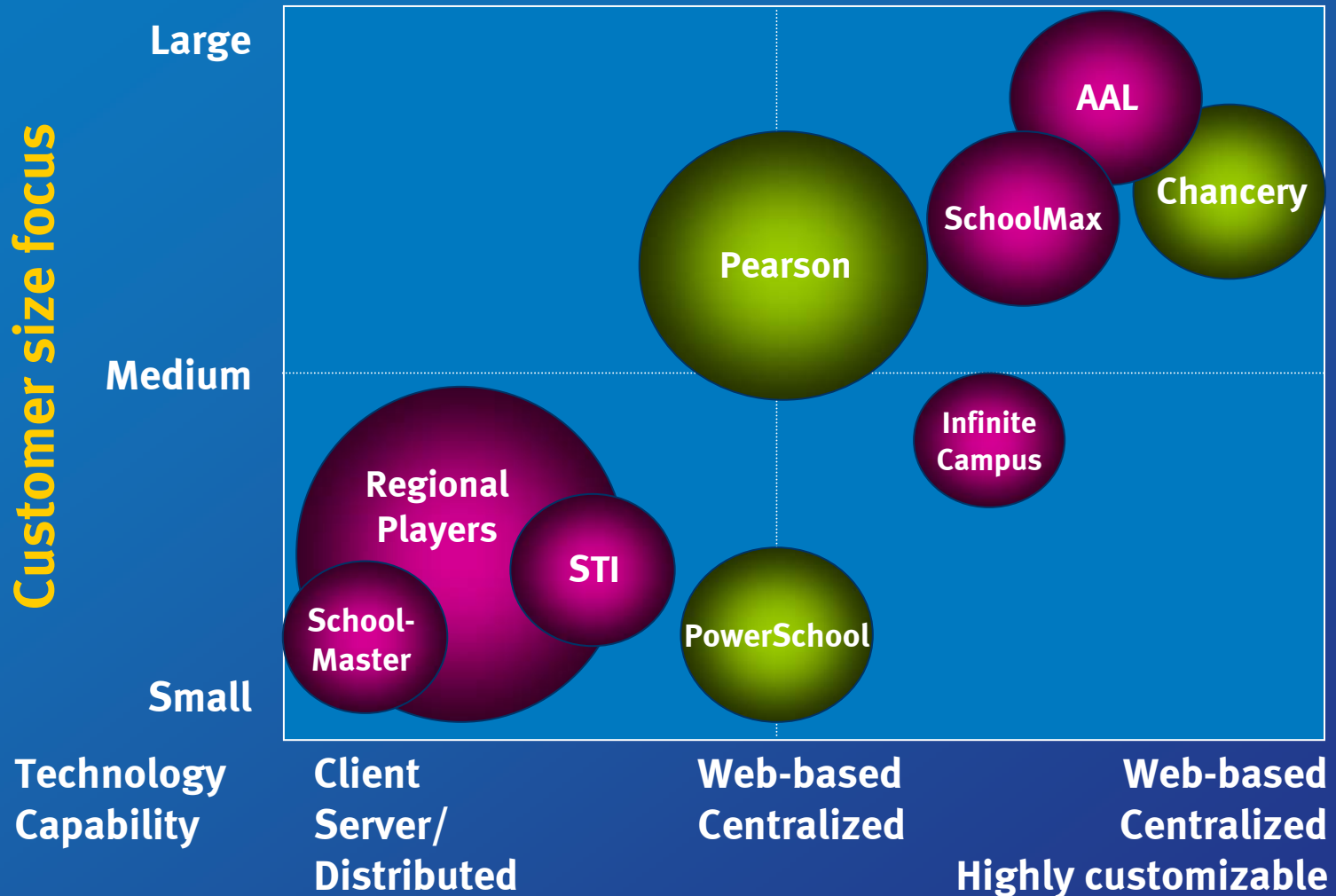
\* Individual Education Plan; \*\* Learning/Content Management System

# Student Information Systems

## US market penetration

Pearson School Systems	Chancery	PowerSchool
<ul style="list-style-type: none"> <li>#1</li> </ul>	<ul style="list-style-type: none"> <li>#2</li> </ul>	<ul style="list-style-type: none"> <li>#3</li> </ul>
<ul style="list-style-type: none"> <li>#1 mid-sized districts</li> </ul>	<ul style="list-style-type: none"> <li>#1 large districts</li> </ul>	<ul style="list-style-type: none"> <li>#2 small and mid-sized districts</li> </ul>
<ul style="list-style-type: none"> <li>20.0m students</li> </ul>	<ul style="list-style-type: none"> <li>2.4m students</li> </ul>	<ul style="list-style-type: none"> <li>&gt; 3m students</li> </ul>
<ul style="list-style-type: none"> <li>16,000 schools</li> </ul>	<ul style="list-style-type: none"> <li>6,000 schools</li> </ul>	<ul style="list-style-type: none"> <li>7,200 schools</li> </ul>
<ul style="list-style-type: none"> <li>Web-based &amp; customised</li> </ul>	<ul style="list-style-type: none"> <li>Customised</li> </ul>	<ul style="list-style-type: none"> <li>Web-based</li> </ul>

# The enterprise software market

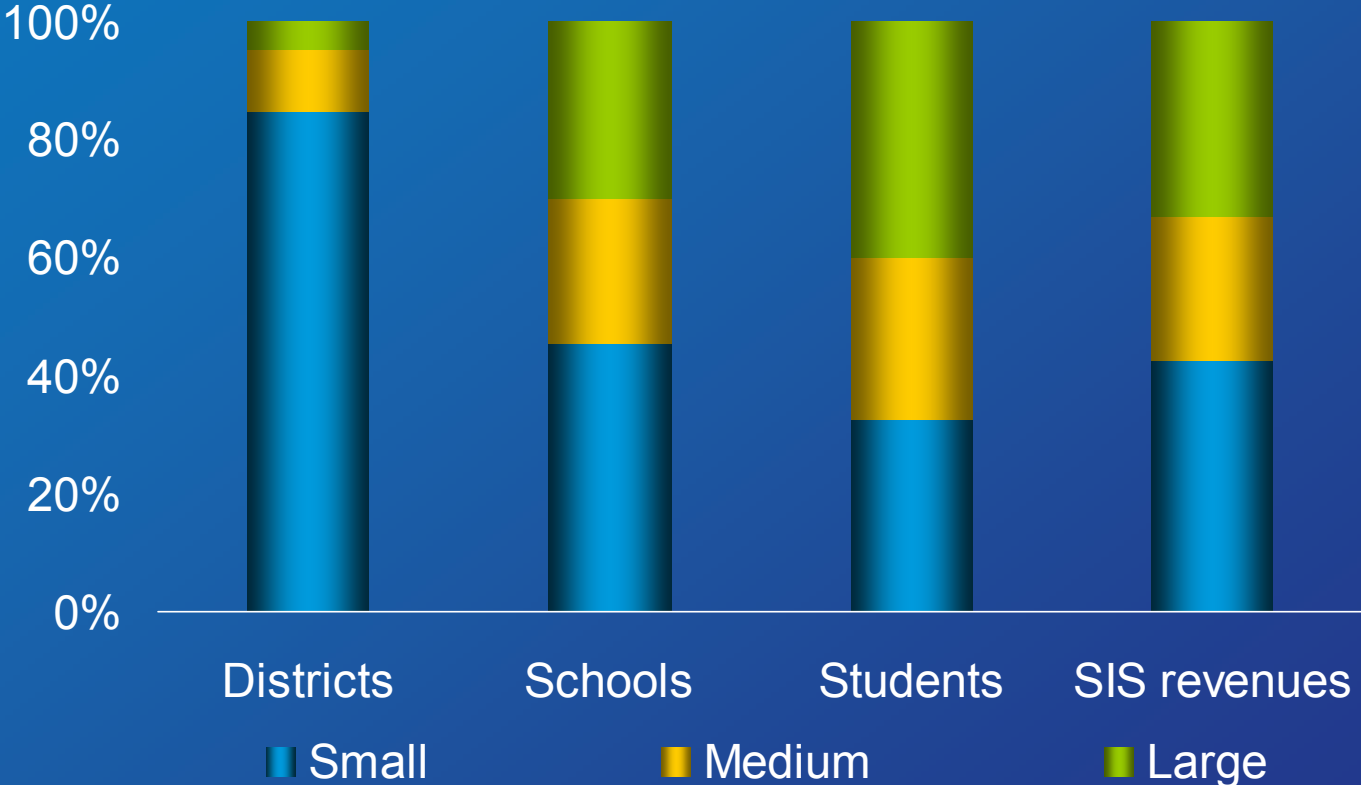




# Pearson now leads in all market segments

Segmentation of PK-12 market by size, value

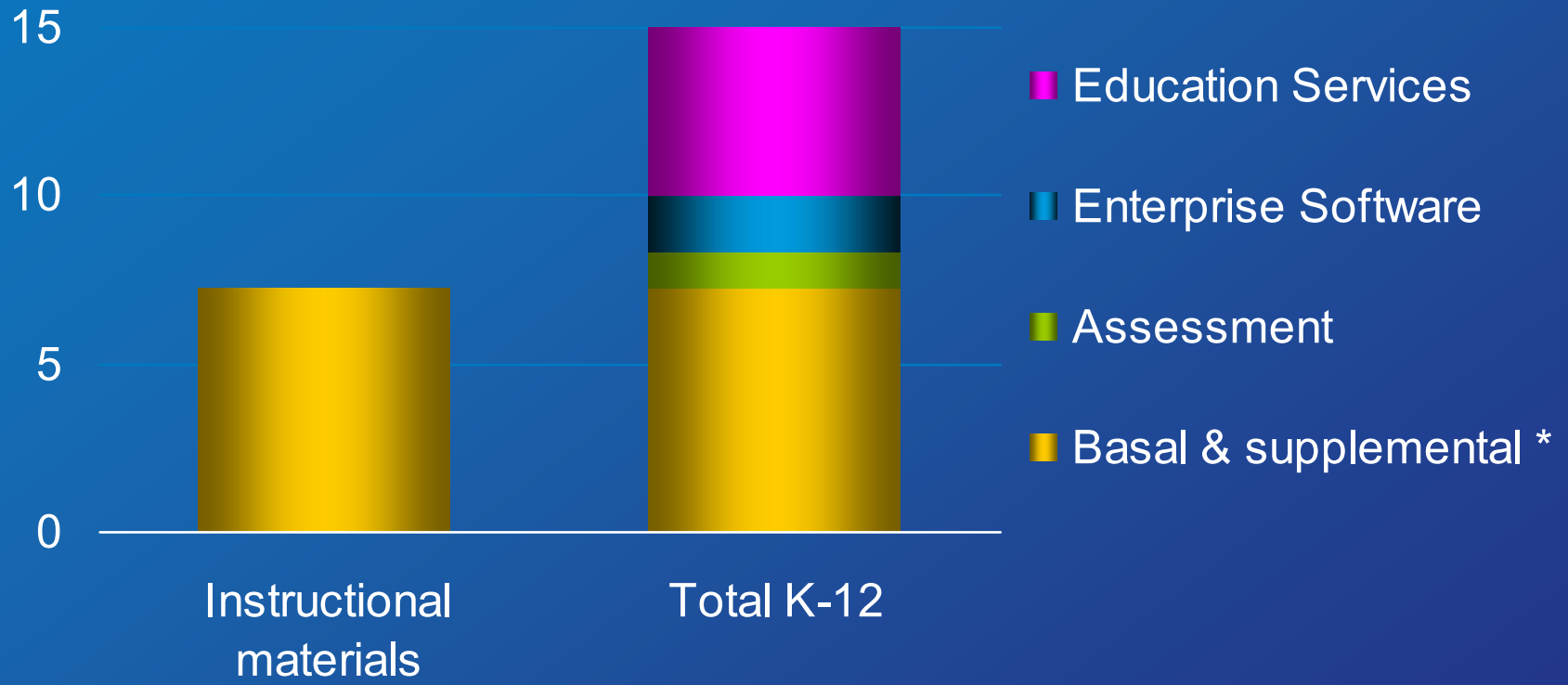
% of total



Source: Quality Education Data (QED), 2005 Data Guide, Headway Strategies 2003 SIS report

# Expanding market opportunity

K-12 addressable market  
\$bn



Source: Eduventures  
\* Includes Curriculum Software

# SIS acquisitions: Added value and scale to Pearson

- Chancery expands addressable market
- Both use existing capabilities;  
clear cost synergies
- Growth market
- Builds competitive strength
- Strong management team
- Earnings and value enhancing

# Our School strategy



**Personalised learning  
and effective education**

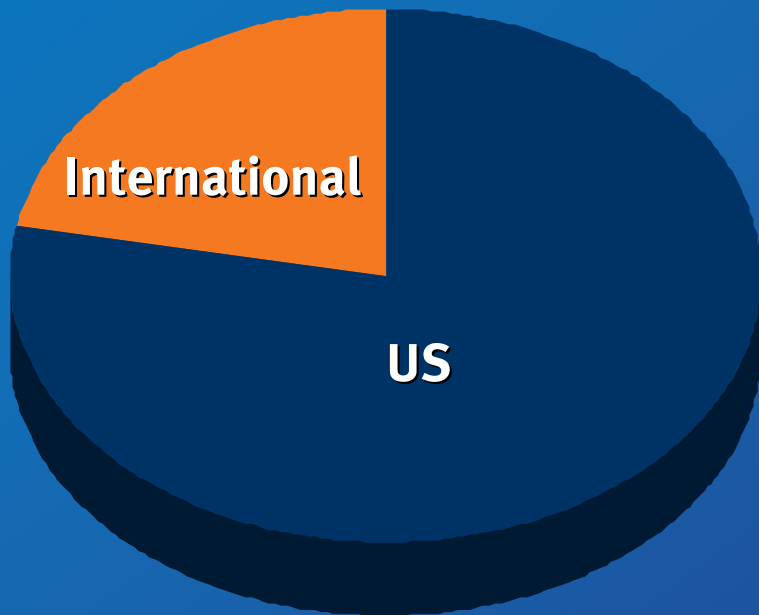
# PEARSON



**Will Ethridge**

President and CEO  
Higher Education, International  
and Professional

# Global leader in higher education



**2005 SALES : £779M**

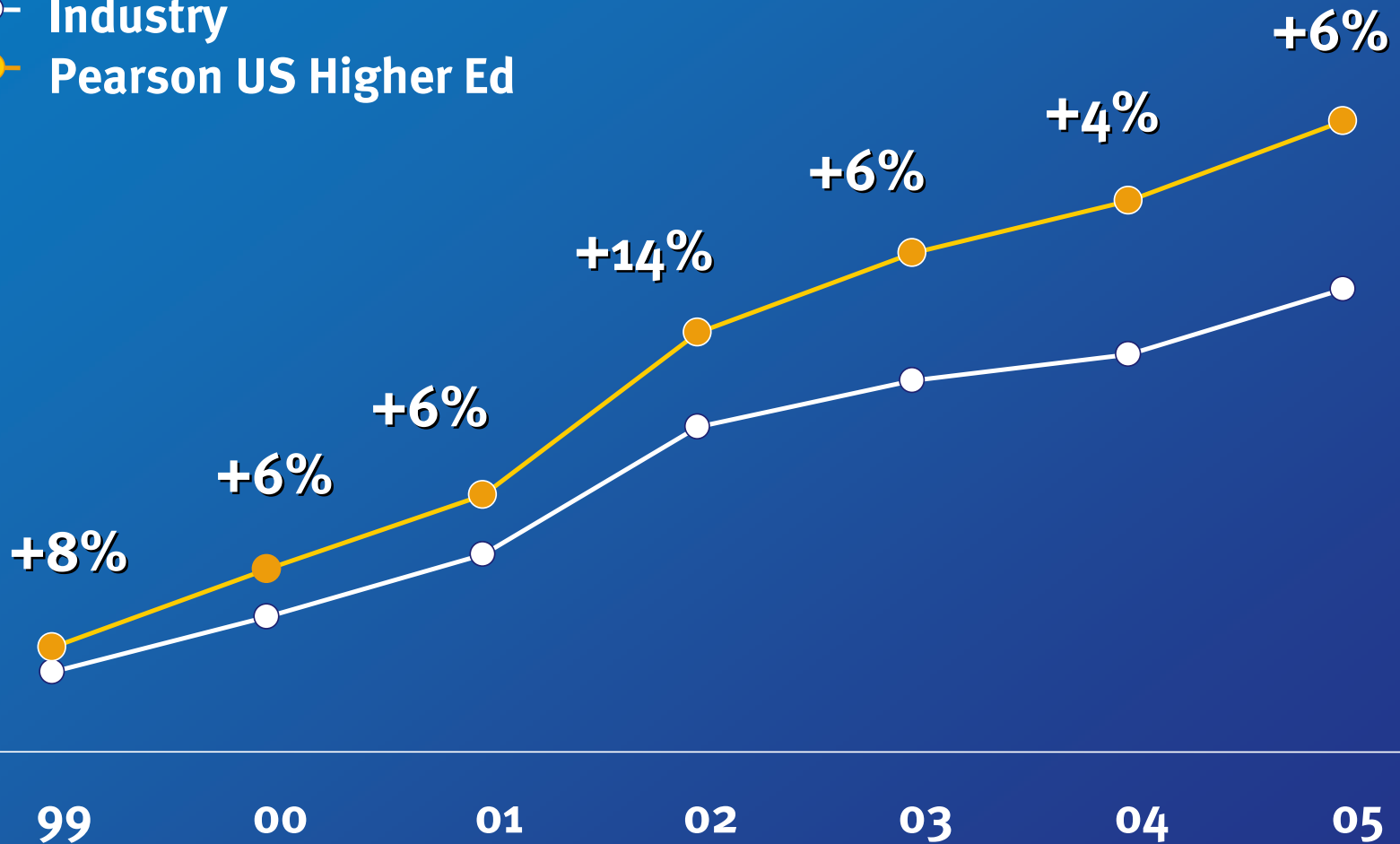
## Above-market growth in 2005

- Total Higher Ed business +5%
- US Higher Ed +6%: outperformed market for 7<sup>th</sup> straight year
- Margins +230bp to 20%

# Higher education: Faster organic growth

● Industry

● Pearson US Higher Ed



# Global scale

## GLOBAL HIGHER ED

United States

Int'l Higher Ed  
US Imports, Adaptations,  
Local Publishing



Custom

Central Media Group

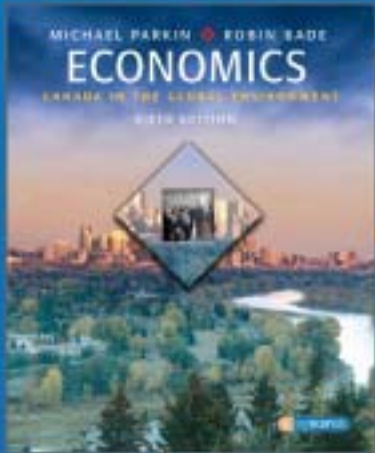
Back Office



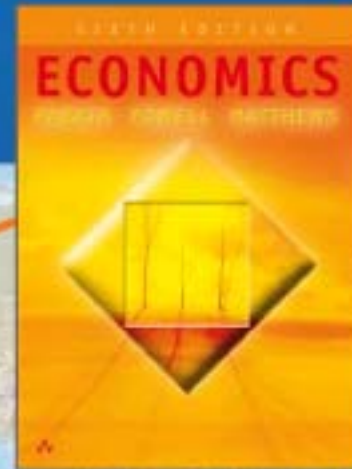
# Benefits of scale

- Shared content
- Global sourcing and production efficiencies
- Global learning platforms
- Shared best practices and global expertise

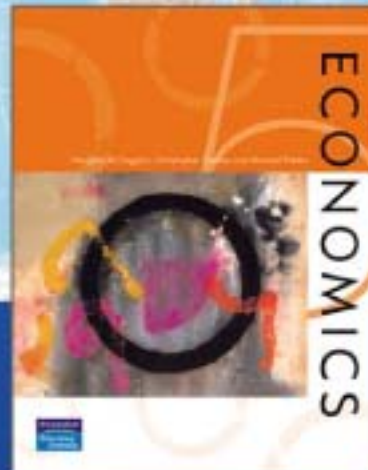
# Benefits of scale



10% improvement  
in sell-through



50% 1st  
year sales  
increase



38% 1st year  
sales increase

# Transforming higher education through Content +



- Customised text
- Choices of format
  - Print, digital, audio

- Learning platform
  - Diagnostics, homework, assessment, resources
- e-commerce platform

- Instructional support
- Data
  - Communities, tutoring, test prep

# Market dynamics

- Rising demand for post-secondary education
- Rising costs for students and institutions
- Accountability: measuring learning outcomes
- Student expectations: “digital natives”

# Improved share

Compelling value proposition drives adoptions

- Choice of great content
- Customised to course objectives
- Content integrated with learning platform
- Saves professors' time, e.g., automating grading
- Motivated and successful students
- One-stop partnership and support from Pearson

# Improved sell-through

- Product central to students
- Used books are not substitute in Content +
- One-to-one relationship with students opens new revenue opportunities

# Improved return on investment

- Scale benefits and extensibility
- Increased switching costs
- Global content management efficiencies

# PEARSON



**Jim Behnke**  
**Chief Publishing Officer**

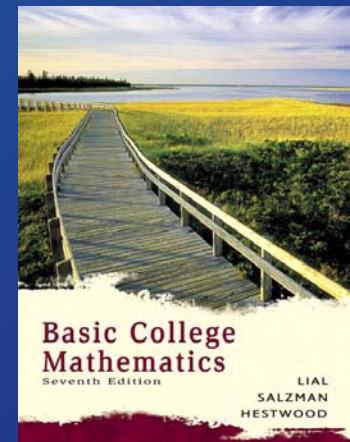
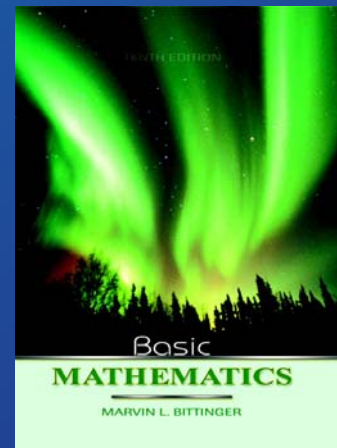
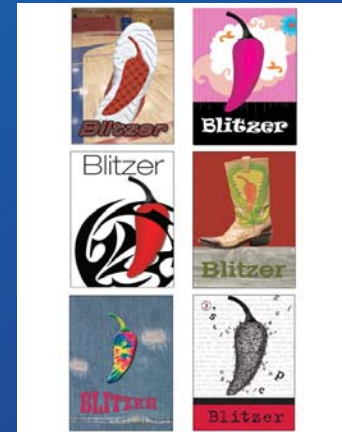
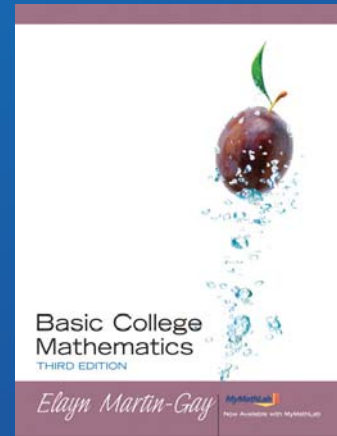
**Driving sales and share gains  
with Content +**



# What is MyMathLab?



- Online learning program
- Providing multimedia instruction for over 200 textbooks
- Unlimited student practice/ personalized study plan
- Automatically graded homework and tests
- Fully customizable
- Access code purchase and student registration required

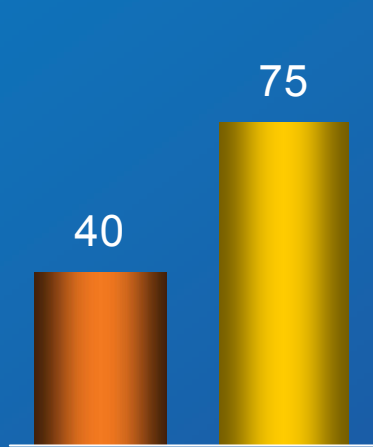


# MyMathLab raises student performance



## Success rate

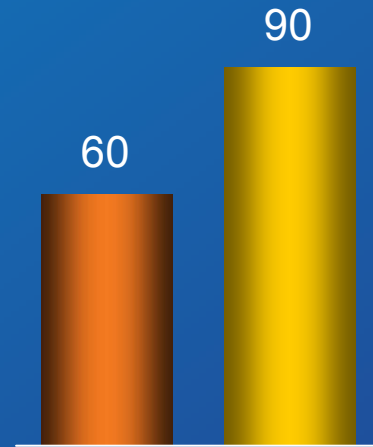
University of  
Alabama,  
Tuscaloosa



Traditional MML

## Exam score

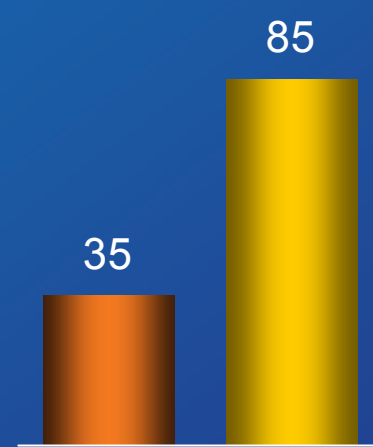
Onondaga CC,  
New York



Traditional MML

## Success rate

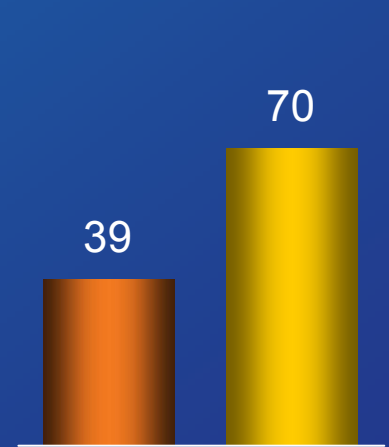
Youngstown State  
University, Ohio



Traditional MML

## Success rate

DeVry / Miramar  
Campus

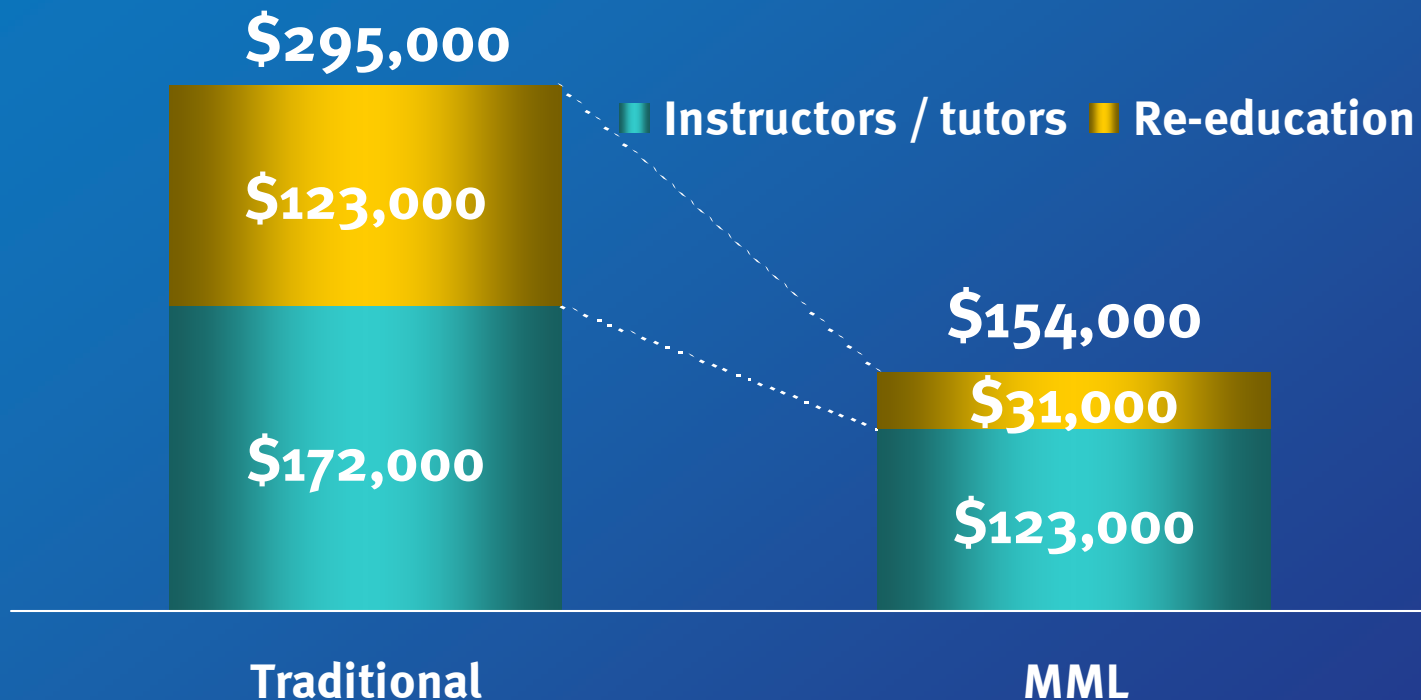


Traditional MML

% pass rates, grade C or better

# Institutional cost savings

## Traditional vs. MML



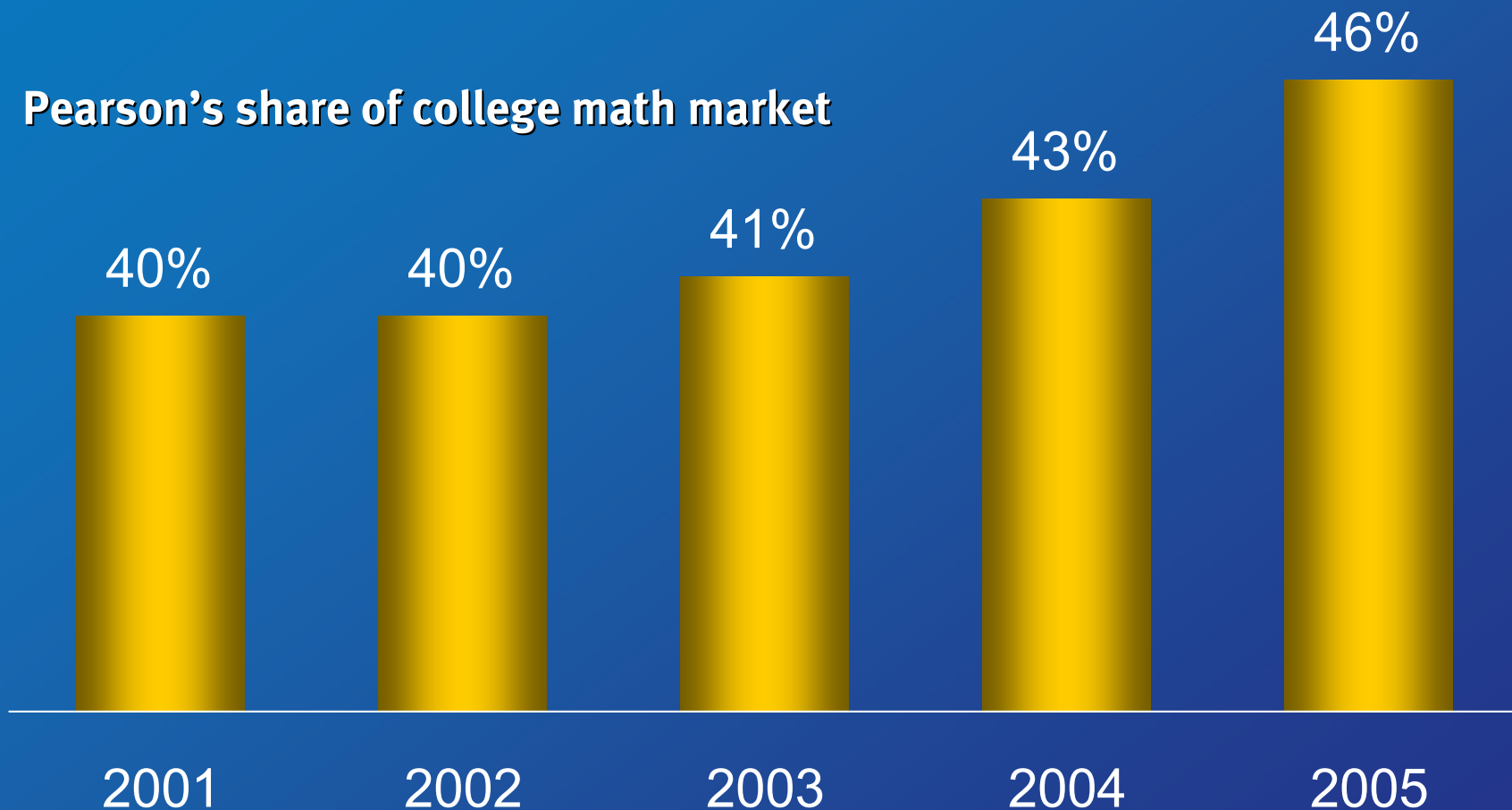
**University of Alabama: Course Math 110**  
1,480 students

Source: Joe Benson, University of Alabama

# MyMathLab gains share and grows sales



Pearson's share of college math market



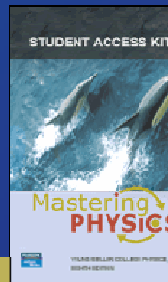
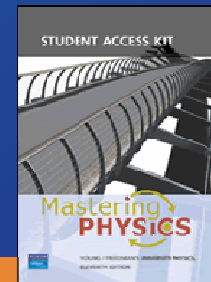
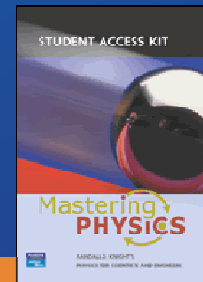
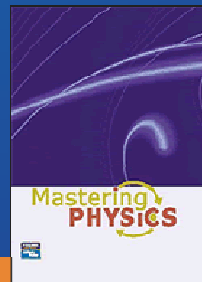
Source: Monument Information Resources

# EET and the Mastering platform

effective educational technologies  
promoting two way learning around the globe

Mastering  
PHYSICS

- Incubated at MIT with NSF funding
- Commercial launch by Addison-Wesley in 2002
- Simulates the one-on-one relationship between student and tutor
- Proven to improve student performance on exams
- Access code purchase & student registration required

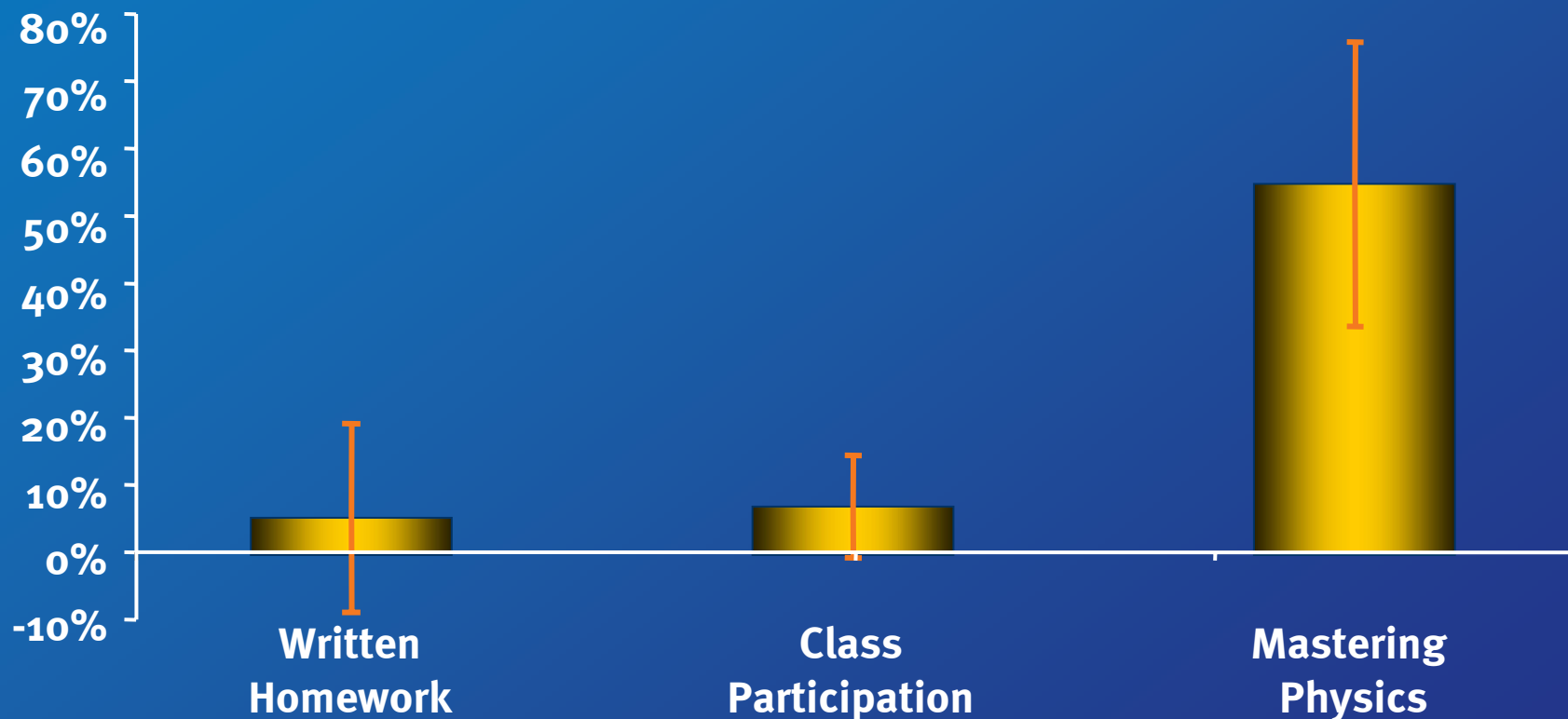


# **Mastering Chemistry video**

# Mastering Physics: Improving learning outcomes



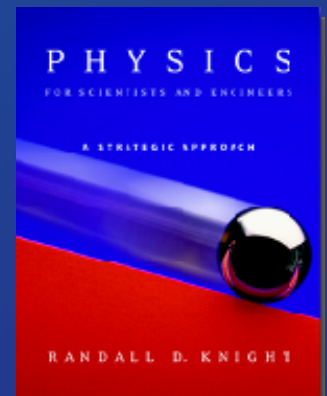
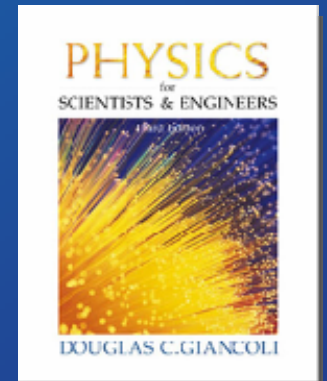
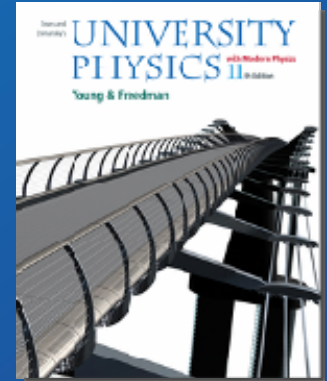
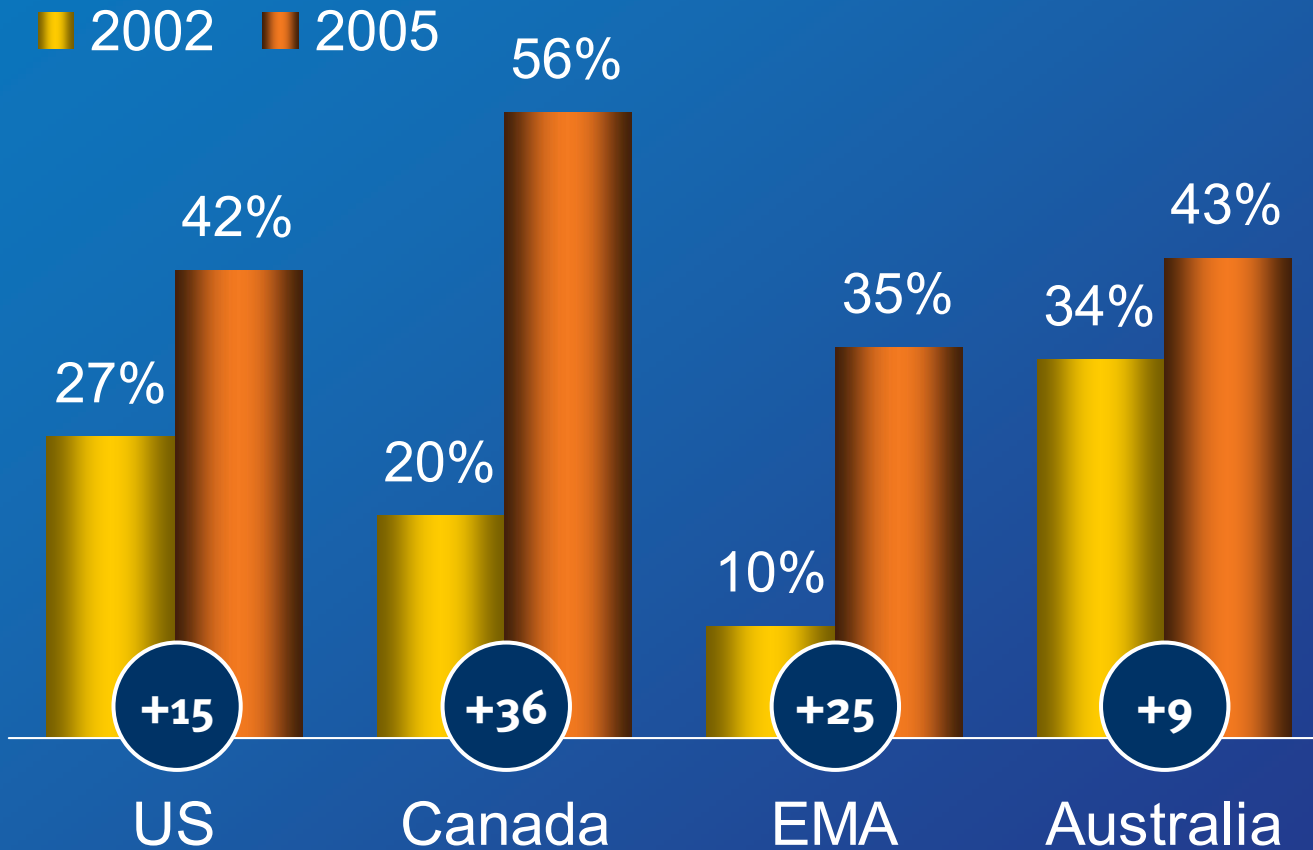
**NSF research:** % improvement in results



Source : National Science Foundation

# Mastering Physics: Driving market share gains

## University (calculus-based) Physics





# Benefits of Mastering platform

## Students

- Adaptive, personalized, instantaneous feedback
- Flexible: work at your own pace/connect from anywhere
- Improved performance on exams

## Educators

- Automatically graded homework saves time
- Data and diagnostics pinpoint performance problems

## Pearson

- Driving sales and share gains
- Extending to Prentice Hall and other disciplines
- Ensuring scalability and performance

# Content+ across the curriculum



# PEARSON

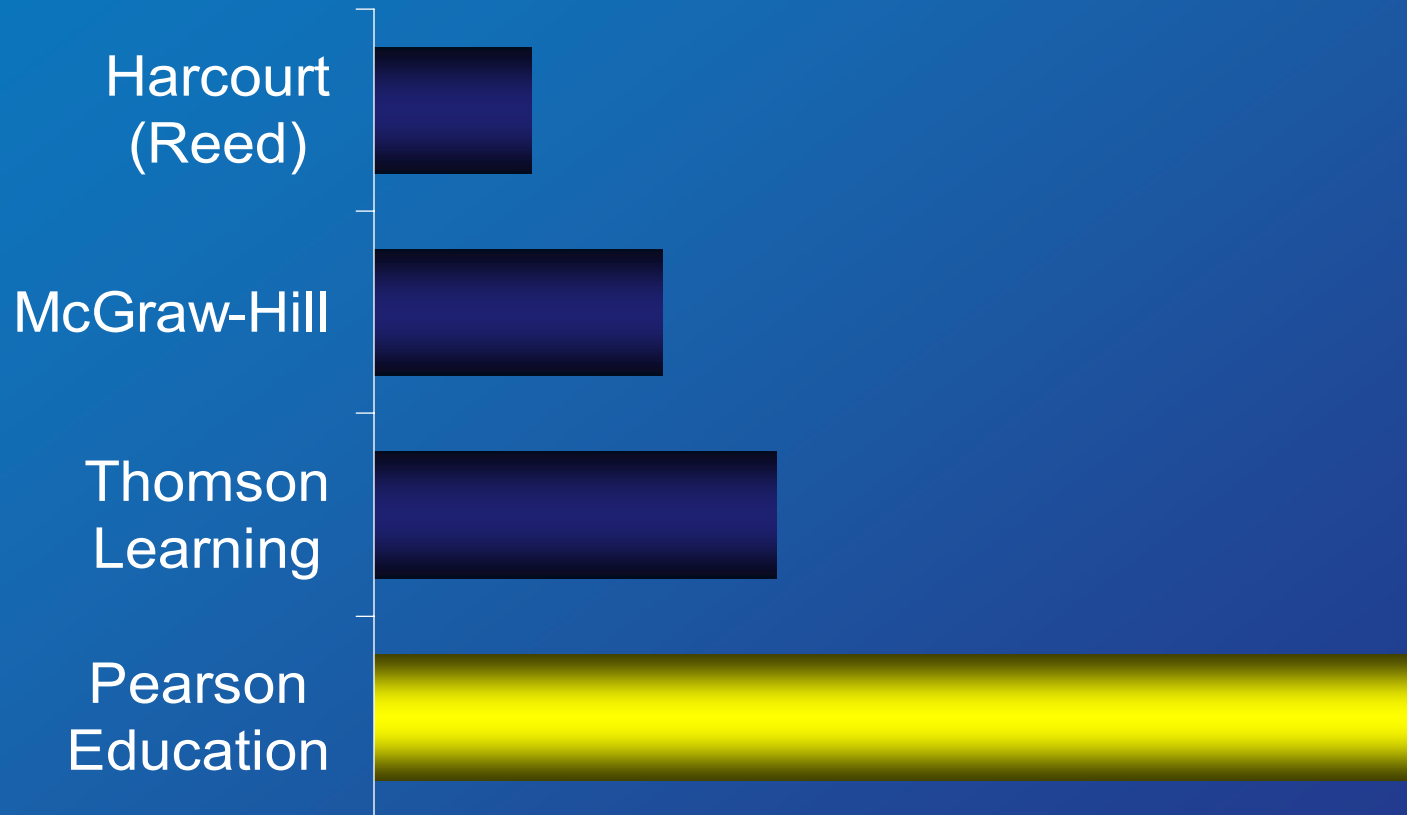


PBM PARAVIA BRUNO MONDADORI EDITORI

## **Paravia Bruno Mondadori (PBM): International Expansion**

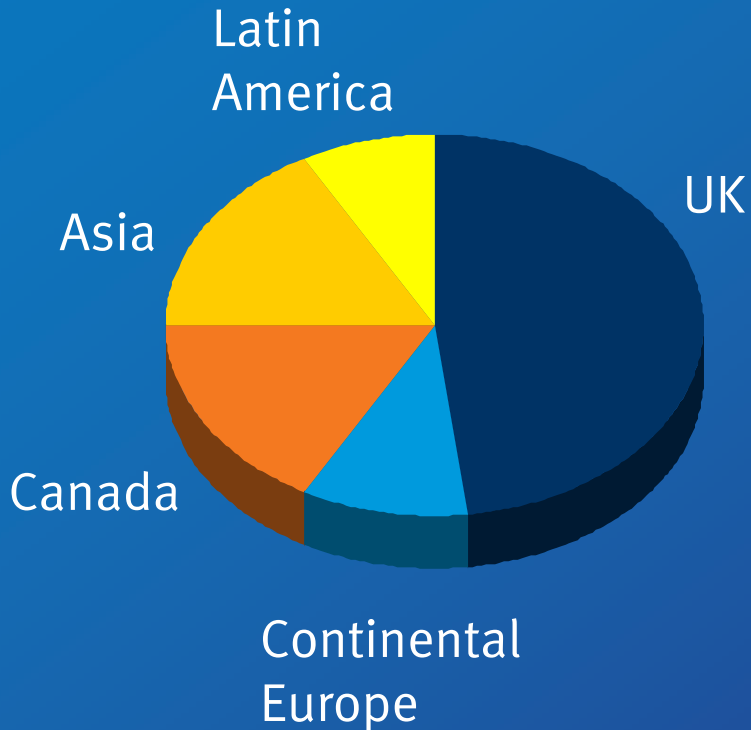
# Our international education business

Education revenues outside the US (2004)

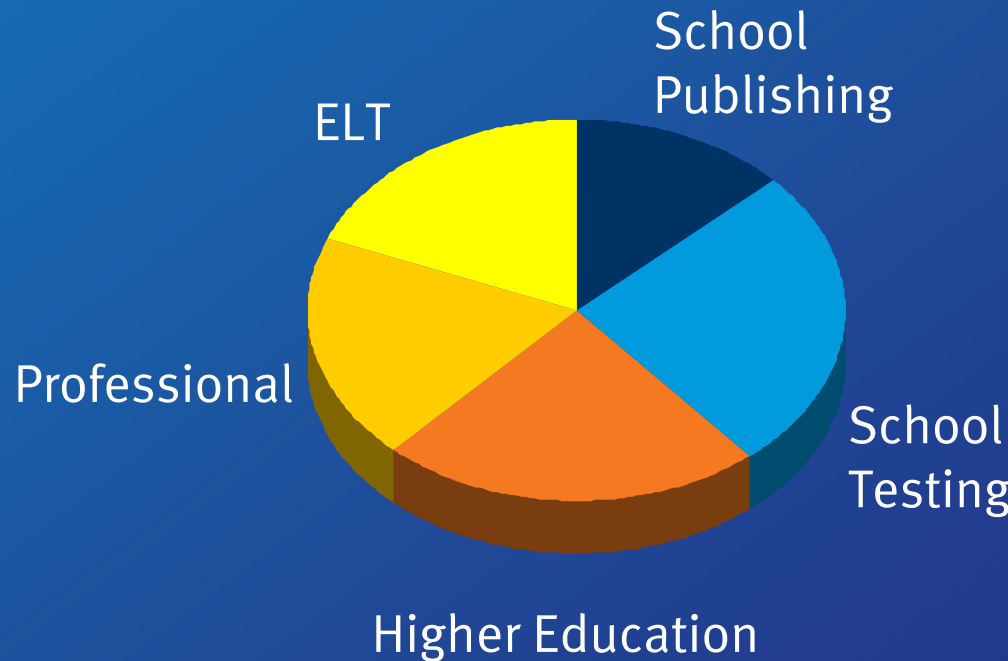


# Pearson Education International

## By region



## By product



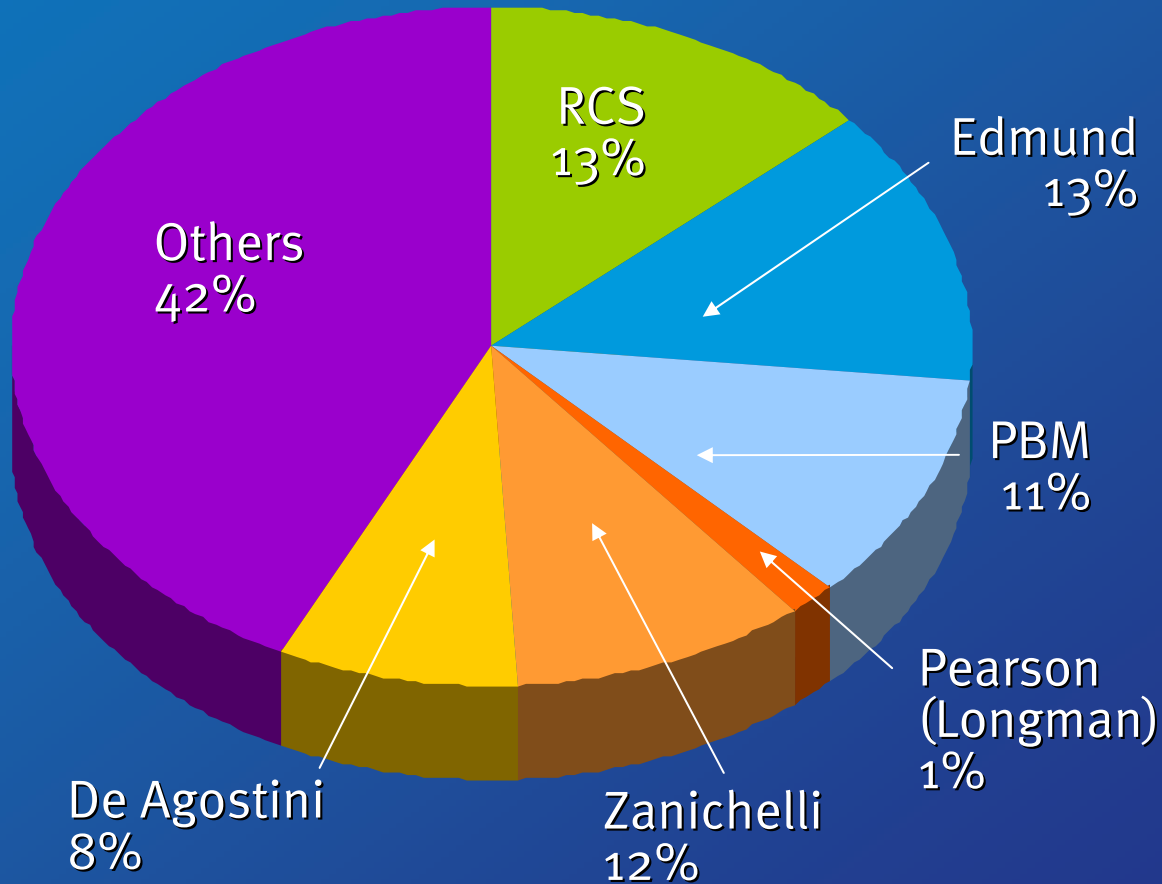
**2005 Sales: \$1.4 Billion**  
**Revenue Growth: 15%**

# Paravia Bruno Mondadori (PBM)

- €620M K-12 market
- 3rd largest full curriculum education publisher in Italy with c.11% market share
- Key brands include: Ed. Scholastiche Bruno Mondadori, Paravia, Archimede Edizioni and Lang Edizioni
- Teacher adoption/parental purchase model

# Large and fragmented market

Market share, 2005A (%)



# Opportunities for PBM with Pearson

- Strong front-list for '07-'09 adoption cycle
- Pearson adds value in technology, testing, and publishing expertise
- Pearson ELT benefits from a strong sales network
- Potential for consolidation opportunities



# Managing integration

- Experienced integration teams
  - Simon & Schuster integration
  - Alignment of US Higher Education with International
  - Systems and technology expertise
- Good cultural fit

# Summary

- Bolt-on acquisitions leverage scale and synergies
- Attractive market characteristics
  - size, pricing, transparency
- Leverage Pearson's unique strengths
- Connect ELT with cross-curriculum publishing

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New York Media Conference**

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