

Operating and Financial Review



The following review is divided into two parts. The Operating Review analyses the performance of the Group and each of the three divisions into which it is organised, looking at sales and operating profit, and highlighting significant factors that have contributed to the results. The Financial Review looks at Group interest, tax, earnings and cash flow, treasury management and accounting policies.

OPERATING REVIEW

A fuller discussion on the markets in which the Group operates and likely future developments can be found in the Business Reviews in the 1996 Annual Report.

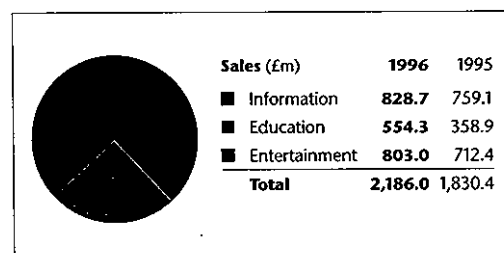
Group summary

Sales increased by £355.6m to £2,186.0m. Acquisitions during the year contributed £203.0m of sales, the most significant of which was the acquisition of HarperCollins Educational by Addison Wesley Longman which contributed £166.9m, or 8% of sales. Discontinued operations relate to the withdrawal of the Group from the UK regional newspaper business following the sale of Westminster Press in December 1996 for £305m. During the year Westminster Press contributed £137.1m in sales, £35.3m in operating profit and £35.6m in operating cash flow. Of total sales 38% relates to the Information Division, 25% to the Education Division and 37% to the Entertainment Division.

	1996 £m	1995 £m	Change %
Sales	2,186.0	1,830.4	19
Operating profit (continuing):			
Information	99.1	83.3	19
Education	68.1	31.8	114
Entertainment*	52.5	110.9	(53)
Investment Banking	40.8	39.9	2
Corporate expenses and other income	(14.5)	(28.3)	49
Continuing	246.0	237.6	4
Discontinued	35.3	22.0	60
Total*	281.3	259.6	8
Operating cash flow	219.0	146.5	49

*Excludes £100m charge for improper accounting at Penguin USA (see page 2).

Operating profit from continuing operations, excluding the £100m charge for improper accounting at Penguin USA, increased by £8.4m or 4%. Excluding both the £100m charge at Penguin USA and operating losses at Mindscape of £45.5m, total operating profits increased by 23%.



The change in operating profits in 1996, when compared with 1995, is due to a number of factors which are analysed in the table below. The increase in operating profits from acquisitions made in 1995 is primarily attributable to Grundy, acquired in May 1995, and Interactive Data Corporation, acquired in August 1995.

	Group excluding Mindscape £m	Mindscape £m	Group including Mindscape £m
1995 operating profit	266.5	(6.9)	259.6
Acquisitions in 1995	24.6	0.9	25.5
Acquisitions in 1996	45.5	–	45.5
Discontinued	8.4	–	8.4
Decrease BSKyB income	(30.1)	–	(30.1)
Channel 5 losses	(5.8)	–	(5.8)
Decrease restructuring	11.7	(5.4)	6.3
Other	(12.1)	(19.6)	(31.7)
Underlying increase	18.1	(14.5)	3.6
1996 pre improper accounting	326.8	(45.5)	281.3
% increase	23%		8%
Improper accounting	(100.0)	–	(100.0)
1996 operating profit	226.8	(45.5)	181.3

The increase from acquisitions made in 1996 relates primarily to HarperCollins Educational, acquired in April 1996. The increase attributable to the discontinued business relates to Westminster Press.

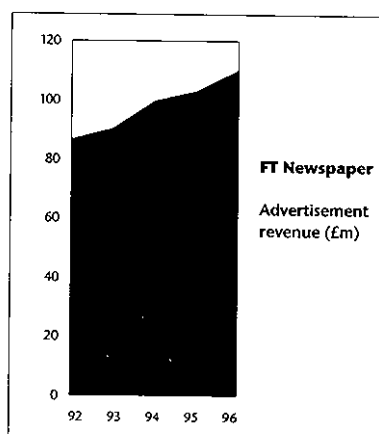
Following the disposal of its direct stake in BSKyB in 1995, the Group's income from this investment

is now derived from interest on its loan stock in BSB Holdings Ltd (BSBH). This amounted to £2.4m in 1996 compared with total income of £32.5m in 1995.

Other, excluding Mindscape, includes the increase in profits arising on the disposal of the Group's remaining interest in Cedar Fair (see 'Corporate expenses and other income'), losses on *Argent*, a French personal finance publication launched in January 1996 but closed in August 1996, and increased costs of the Shared Services initiative (see page 3). Excluding Mindscape, all three divisions contributed to the underlying increase in operating profit.

In 1996 Mindscape underwent substantial refocusing and restructuring of its operations. In addition, the accounting treatment in respect of royalty advances and development costs was changed to charge these costs earlier. Prior year figures have not been restated for the change in accounting treatment as the amounts involved are not material to the Group. Of the operating loss for the year of £45.5m, £11.2m relates to the write-off of abandoned product, £5.4m to restructuring costs and £7.4m to the change in accounting treatment.

On 13 February 1997 the Group announced that it had uncovered improper accounting at Penguin USA. The problems, dating back to 1991, relate to unauthorised discounts given to customers in return for early payments which had not been



correctly recognised in the accounts. This unauthorised practice has had little impact on ongoing sales and operating profits. The charge has been treated as a one-off item and therefore has been excluded from the calculation of adjusted earnings.

Interest payable of £29.5m was £5.6m higher than in 1995. The increase reflects the acquisitions made during the year, in particular the £369.2m acquisition of HarperCollins Educational in April 1996. In addition, a premium of £10.3m was paid on the redemption of the £25m (13.625%) 2007 Unsecured Loan Stock.

The taxation charge of £108.6m represents an effective rate of 30.4%. The effective rate on adjusted earnings of 28.8% is below the UK tax rate due mainly to consortium relief recognised following renegotiation with other partners in BSKyB/BSBH.

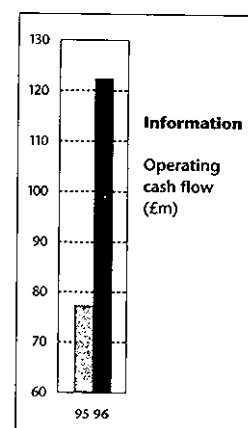
At the end of 1995 a decision was made to proceed with a major initiative to combine back office functions across the Group, and a provision for £16.7m was set up to cover restructuring costs. This provision will be utilised when the restructuring costs are incurred upon implementation, the main part of which is planned for 1998. During 1996 £6.9m was incurred on the Shared Services initiative, of which £1.9m was expensed and £5.0m was capitalised.

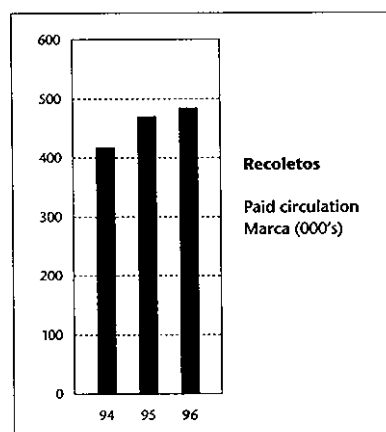
Information Division

	1996 £m	1995 £m	Change %
Sales	828.7	759.1	9
Operating profit (continuing):			
FT Newspaper	16.5	7.4	123
FT Information	17.3	11.4	52
Les Echos	(0.3)	3.2	-
Recoletos	34.9	37.8	(8)
Pearson Professional	18.6	11.5	62
The Economist	12.1	12.0	1
Westminster Press (discontinued)	35.3	22.0	60
Total	134.4	105.3	28
Operating cash flow	122.0	77.3	58
Operating margin	15%	12%	25

Financial Times Newspaper

Advertisement revenues grew by 7% overall and circulation revenues were up 8%, helped by a cover price rise in the UK and record overseas circulation. Average daily copy sales reached 299,000 in 1996 of which 42% were sold overseas. A new web site was opened in April and has already attracted over 250,000 registered users. Cost savings also played an important role in improving trading profits which increased by almost 50%. The closure of the East India Dock printing operation resulted in significant savings that were reinvested in the expanded network of print sites. The tenth such site, in Hong Kong, was opened in March 1996. Further significant cost savings were realised during 1996 resulting in an exceptional charge of £5.8m. Despite this exceptional charge,





operating profits before associates increased by 123%.

Financial Times Information

Sales from Financial Times Information's financial and business information services increased by 45% in 1996. This included the first full year of sales of £50.6m from Interactive Data Corporation, a leading supplier of price data in the capital and securities market, which was acquired in late 1995, and which contributed to strong results from the Asset Management business. Electronic Business Information and Research Products both increased revenue, but the benefit from this was offset by considerable development expenditure, particularly within Research Products. This investment will be continuing in 1997. Overall operating profit was up 52%, mainly reflecting the benefit from Interactive Data Corporation.

Les Echos Group

Overall advertising revenues for *Les Echos* fell by 2% in depressed advertising markets although financial advertising held up well and *Les Echos* improved its market share. Circulation grew by 5% and *Les Echos* is currently the only profitable French business paper. *Enjeux*, the monthly business magazine, increased revenues by 16% and significantly reduced its losses, and *Panorama du Medecin* is now operating profitably. *Argent*, a personal finance publication launched in January, was closed in August because news-stand sales were below initial assumptions. The loss on

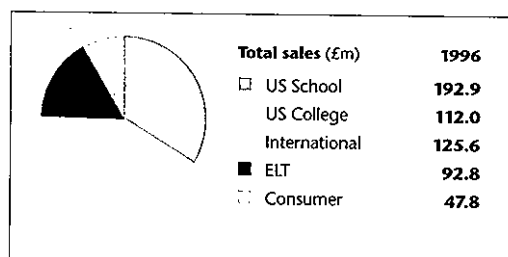
this venture led to the *Les Echos* group showing a small loss for the year; without *Argent*, it would have produced a profit 66% up on 1995.

Recoletos

Pearson increased its stake in Recoletos from 56.7% to 94.2% during 1996. At an average paid circulation of 486,000, the sports paper *Marca* is the most widely read newspaper in Spain and continues to grow. Advertising pages expanded by 15% as demand for space outstripped supply. Recoletos' margin, however, fell from 33% in 1995 to 27% in 1996, as investments were made in *Marca* to counteract competitor activity. Developments included a fantasy football league and club, which now has 1.3 million members, new printing centres in Spain and Holland, and regional editions. *Expansion* continued to be Spain's leading business newspaper, with circulation up 8% in 1996.

Pearson Professional

Sales increased by 8% overall, helped by strong performances from publishing in finance, energy and media. US sales for Churchill Livingstone, the health publishing business, were affected by the squeeze on physicians' incomes which is making trading conditions very difficult for wholesale publishers. Operating profits for Pearson Professional improved by 62% as the medical communications business in Japan, which was disrupted by the Kobe earthquake in 1995, was re-organised and as Pearson Professional focused on growing higher margin activities,



whilst reducing the cost base through efficiencies in its core businesses. Meanwhile, a small number of margin-enhancing acquisitions were made.

The Economist (50%)

The Economist had another excellent year. Pearson's share of profits amounted to £12.1m, slightly ahead of last year's record figure. Average circulation reached 640,385 by December 1996 compared to 621,201 in December 1995, an increase of 3%.

Education Division

The Education division consists of Addison Wesley Longman (AWL), Pearson's educational publishing business, which comprises five business units: US School, US College, International, English Language Teaching (ELT) and Consumer.

	1996 £m	1995 £m	Change %
Sales	554.3	358.9	54
Operating profit	68.1	31.8	114
Operating cash flow	28.3	6.8	316
Operating margin	12%	8%	50

AWL achieved sales of £554.3m in 1996, against £358.9m in 1995, an increase of 54%. £166.9m of sales or 85% of growth resulted from the acquisition of HarperCollins Educational Publishing, which chiefly impacted US School and US College publishing. The business, excluding HarperCollins Educational, also achieved a healthy organic growth of 9%.

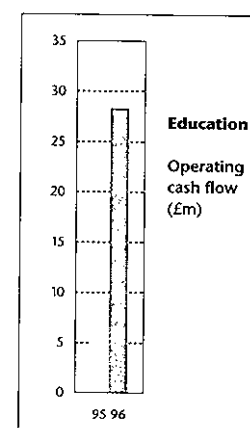
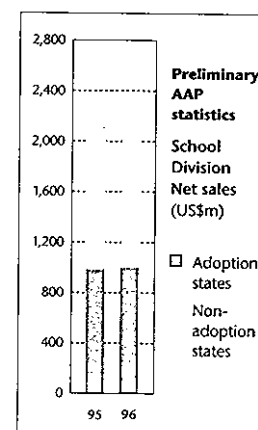
HarperCollins Educational was purchased at the beginning of April 1996 and has now been successfully integrated into Addison Wesley Longman. The operating profit of HarperCollins Educational of £45.1m, before restructuring costs of £15.0m, is not representative of a full 12 months performance as it excludes the loss making first quarter. However, this loss broadly equates to the charge for restructuring costs, and therefore the operating profit after restructuring costs is approximately equivalent to one full year's trading. The operating cash flow of £4.5m, on the other hand, has been reduced by restructuring expenditure and the exclusion of the first quarter, a strong period for collections, and is less than representative of a full year's cash flow.

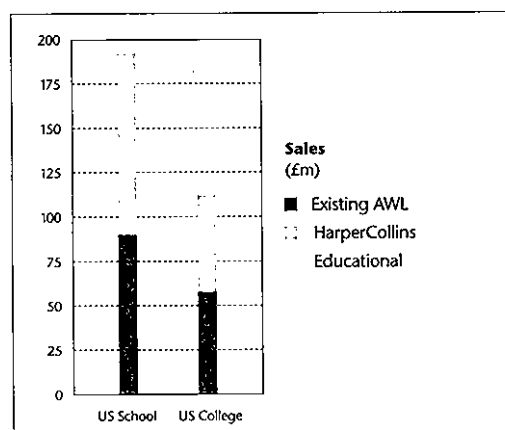
US School

Sales of £192.9m were £113.6m up on 1995, including £102.3m from HarperCollins Educational titles. Sales, excluding HarperCollins Educational, were also up by £11.3m or 14%, driven by growth in the school publishing market, by significant increases in sales of elementary maths and science products first published in 1995, and by the introduction of the Waterford Early Reading Program. Profit, excluding HarperCollins Educational, was higher than in 1995 and margins improved through reduced pre-publication cost amortisation.

US College

Sales in the US college market increased by 123% over 1995, to £112.0m. £54.0m of this was





attributable to HarperCollins Educational titles. Growth in sales elsewhere was also achieved, together with improved profits and margins through tight control on headcount and other discretionary expenses. This was partially offset by higher provisions for obsolescence.

International

The International business comprises all school and college products locally published and/or distributed outside the USA, including the UK. Sales for the business in 1996 were £125.6m, up by 29% over 1995 and all international areas contributed to the growth. Profits and margin percentages also rose. HarperCollins Educational accounted for incremental sales of £9.5m.

English Language Teaching (ELT)

Worldwide sales of ELT products were £92.8m, an increase of £11.1m or 13% over 1995. Most of this growth resulted from the first full year's results from Nelson titles, acquired in 1995. Profits improved over 1995 as a result of the Nelson contribution and reduced operating expenses.

Consumer Publishing

Sales for 1996 were £47.8m, representing growth of 11% over 1995. A major contributor was computer-related learning materials, where the increased importance of the Internet and associated programming languages such as JAVA helped to offset the decline in demand of Apple-related products. *Take Care of Yourself* continued

to sell well, reflecting the US focus on health care. Profit and margin for consumer publishing declined because of higher obsolescence reserves and an unfavourable movement in the mix towards higher cost product.

Entertainment Division

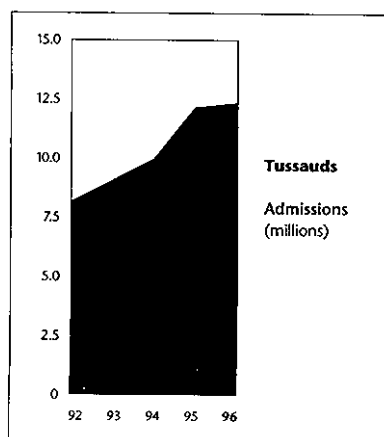
	1996 £m	1995 £m	Change %
Sales	803.0	712.4	13
Operating profit:			
Penguin*	31.0	33.6	(8)
Tussauds	22.2	18.3	21
Mindscape	(45.5)	(6.9)	-
Pearson New Entertainment	2.4	(0.1)	-
Pearson Television	42.4	66.0	(36)
Total*	52.5	110.9	(53)
Operating cash flow	56.5	56.2	1
Operating margin	5%	11%	(55)

*Excludes £100m charge for improper accounting at Penguin USA.

Penguin

Penguin acquired Putnam Berkley, one of the leading US publishers of best-selling fiction, for £201.0m in December 1996. The acquisition added £8.5m in sales during December. In addition to the operating loss of £1.1m, a charge of £4.4m was made to cover the cost of restructuring in 1997. Putnam Berkley also added £12.2m in operating cash flow in the period.

1996 sales of £380.2m were up by 3% on a highly successful 1995. A strong list of titles on both sides of the Atlantic contributed to the success.



Operating profit was down 8% overall, although most of this was due to the absence of any contribution from Eden Toys, which was sold at the end of 1995, and the inclusion of the Putnam Berkley loss mentioned above.

A charge of £100m has been made in 1996 to cover the cost of improper accounting at Penguin USA (see page 2).

Tussauds Group

Sales rose 10%, to £104.6m, compared with 1995. Admissions to the Group's attractions rose 3% to a record 12.3 million visitors. Madame Tussaud Scenerama in Amsterdam had a record year and saw admissions rise 13%, while in Spain, Port Aventura's second season produced a rise of 11% to over 3 million visits. Increases in visitor spending, notably at Alton Towers and Chessington World of Adventures, was the primary driver in 1996 producing record profits from the existing portfolio of locations.

The new Alton Towers hotel, which opened in the spring of 1996, enjoyed significantly higher occupancy and average room rates than expected in its maiden year. The Group's management contract with, and 40% stake in, Port Aventura contributed with profits of over £3.1m in 1996.

Mindscape

Mindscape's sales fell by 12% in 1996, to £50.3m, as new management focused on a smaller number of more successful software products in an

extremely difficult and competitive market.

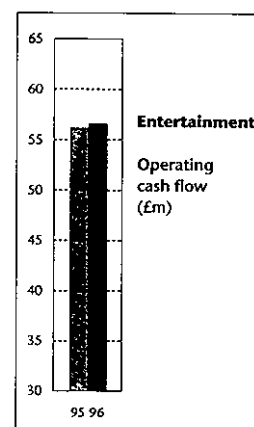
As foreshadowed at the Annual General Meeting of the Group in May 1996, the company reported an operating loss for the year of £45.5m compared with a loss of £6.9m in 1995. £24.0m of this loss was attributable to the costs associated with restructuring, write-offs of obsolete titles and a change in the accounting treatment of development expenditure, leaving a loss of £21.5m for the ongoing business.

Pearson New Entertainment

Sales at Pearson New Entertainment (PNE) grew sharply in 1996, up 26% to £63.6m on 1995. Of this sales growth, 40% came from a number of small acquisitions, on which the division spent £13.8m, and 60% from existing operations. Future Publishing, the UK's fifth largest magazine publisher, accounted for £53.7m of sales. PNE as a whole moved into profit in 1996, with over 60% of profit improvement coming from existing operations, again the remainder coming from acquisitions.

Pearson Television

Sales of £204.3m were up 45% on 1995. The international production business accounted for over 70% of sales revenues, benefiting from a full year's contribution from Grundy and the early impact of Alomo and Witzend acquired as part of SelecTV. Television distribution activities were boosted by ACI – also delivering its first full year's returns. Broadcasting operations in the UK and elsewhere continued to provide a valuable contribution, although results were mixed.



Operating profits for the television business increased by 37%, excluding Pearson's share of Channel 5 start-up costs of £5.8m in 1996, and income from BSkyB.

The Group has a 24% economic interest in Channel 5 and has decided to amortise its share of certain Channel 5 initial costs by the end of the 10 year licence period. The Group will equity account for its share of other profits and losses. As a result of this policy the charge to profits in 1996 was £5.8m out of a total investment of £23.8m.

In February 1997 Pearson Television sold its 10% interest in Television Broadcasts Limited for £111.1m, realising a profit of £6.3m.

Investment Banking

	1996 £m	1995 £m	Change %
Attributable profit	40.8	39.9	2

Lazard

Attributable profits amounted to £40.8m following high levels of Corporate Finance activity in the UK together with good performances from Asset Management and Asset Trading. Sustained levels of Corporate Finance activity in New York, as well as growth in Corporate Trading in bonds, equities, high yields and emerging markets and strong Asset Management results, led to another good performance.

Corporate expenses and other income

Corporate expenses and other income at £14.5m were £13.8m lower than in 1995.

This reflects two main factors. First, the increase in income from the sale of the balance of the Group's investment in Cedar Fair, the US theme park company, from £8.0m in 1995 to £15.4m in 1996. Second, the lower charge relating to the Shared Services initiative, down from £16.7m in 1995 to £1.9m in 1996.

FINANCIAL REVIEW

Exchange rates

The Group earns a significant proportion of its profits in overseas currencies. The currencies which have the greatest impact on the Group through the translation of overseas profits into sterling are the US dollar and the Spanish peseta (see treasury management below for a discussion on the hedging of capital employed and transactional cash flows).

The relevant exchange rates are as follows:

	£ versus US\$		£ versus peseta	
	1996	1995	1996	1995
Weighted average for operating profits	1.58	1.57	199.6	194.9
Year end rate	1.71	1.55	222.6	188.4

The strengthening of sterling towards the year end had a minimal impact on 1996 results, but if year end rates had prevailed throughout 1996, profit before tax would have been lower by an estimated £5m. If the loss at Mindscape is excluded, profit before tax would have been lower by £10m.

Interest

Net interest payable increased by £5.6m to £29.5m. In addition a £10.3m premium was paid to redeem the £25m (13.625%) Unsecured Loan Stock 2007 in April. The size of this premium reflected the entitlement of the holders of the Stock to receive a fixed rate of interest well in excess of current fixed rates for a further eleven years. Redeeming this Stock terminated the last remaining requirement for the Group to comply with a Trust Deed which had imposed limitations on borrowings that were inconsistent with (and potentially more restrictive than) all of the Group's other borrowing documents.

The principal reason for the increase in net interest payable was a £132m increase in average net debt to £430m in 1996. This increase reflected the effect of acquisitions made during 1996 (principally the purchase of HarperCollins Educational in April for £369m), as well as the effect of financing for a full year the £570m of businesses and investments which were acquired during 1995. These were, however, substantially offset by the interest benefit for a full year of the £560m proceeds of the September 1995 disposal of the Group's direct holding in BSKyB.

The effects of changes in interest rates were comparatively small. Lower US dollar interest rates had a small favourable impact on interest payable, which was partly offset by the effect of lower

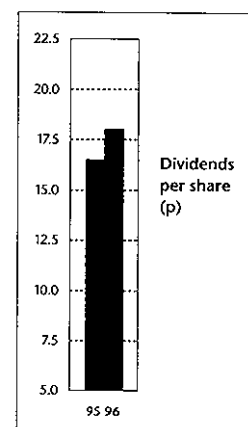
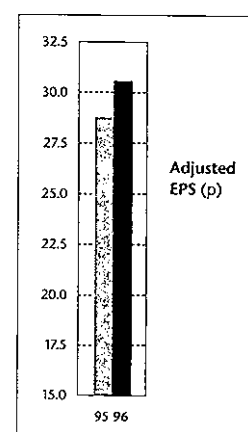
sterling interest rates on the interest receivable from sterling net cash.

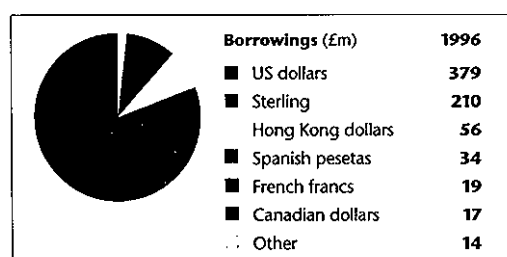
The Group's policy is to maintain its annual consolidated net interest cover ratio at a level between 5 and 9 times. For the 1996 financial year this ratio, after deducting the £100m charge for improper accounting at Penguin USA from operating profit, was 6.1 times.

Taxation

	1996 %	1995 %
UK tax rate	33.0	33.0
Effect of BSKyB/BSBH income	(3.5)	(3.8)
Other items	(0.7)	(1.7)
Tax rate reflected in adjusted earnings	28.8	27.5
Effect of profits/(losses) excluded from adjusted earnings	1.6	(2.1)
Tax rate reflected in earnings	30.4	25.4

The tax charge of £108.6m represents an effective rate of 30.4% compared with 25.4% in 1995. The 1995 rate was reduced by the release of £8.8m consortium relief to offset tax payable on BSBH income. The 1996 tax rate reflected in adjusted earnings has also been reduced by several one-off factors: the rate reflected in adjusted earnings has been reduced by £8.8m of consortium relief now recognised in the profit and loss account following renegotiation with the other partners in BSBH; there is no tax payable on the profit of £231.3m arising on the sale of Westminster Press; the Group has tax losses,





arising in the US, which have not been utilised or recognised in 1996 but are available to carry forward against taxable profits in future years. Accordingly the Group has decided not to recognise tax relief on the £100m charge for improper accounting at Penguin USA and has also written off to profit deferred tax assets totalling £36.6m.

A comprehensive worldwide tax review was carried out during 1996 aimed at further developing tax strategy and tax planning opportunities.

Minority interests

Minority interests decreased from £11.3m in 1995 to £7.7m in 1996 due to the acquisition of an additional stake in Recoletos taking the Group's holding to 94.2%.

Adjusted earnings and dividends

Adjusted earnings per equity share excludes the profits and losses on the sale of fixed assets and businesses, the loan stock redemption premium, the £100m charge for improper accounting at Penguin USA and the tax consequences of these items.

The weighted average number of shares in issue has increased from 554.4m in 1995 to 560.8m in 1996 due to the issue of shares under Executive and Save as you Earn share option schemes and the issue of shares on the acquisition of the additional stake in Recoletos.

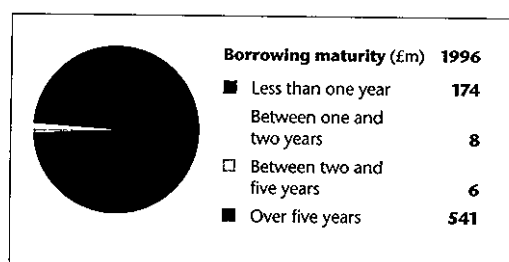
Adjusted earnings increased from £159.6m in 1995 to £171.5m in 1996; adjusted earnings per share increased by 1.8p from 28.8p to 30.6p in 1996.

An interim dividend of 6.9p per ordinary share was paid in November 1996. A final dividend of 11.1p per ordinary share is proposed giving a total dividend for the year of 18.0p, a 9% increase on 1995. Dividend cover decreased from 2.8 times in 1995 to 2.3 times in 1996 (1.7 times on adjusted earnings).

Cash flow

The table below summarises the Group's main cash flows and is in the format used by management to monitor Group cash flow. The main difference to the FRS1 cash flow presented on page 27 is that operating cash flow, the main measure used, is calculated after the deduction of capital expenditure.

	1996 £m	1995 £m
Operating activities	291.2	236.4
Net movement in fixed assets	(84.0)	(69.8)
Other	11.8	(20.1)
Operating cash flow	219.0	146.5
Interest, taxation and dividends	(213.3)	(196.8)
Funds from operations	5.7	(50.3)
Acquisitions, disposals and non operating activities	(409.2)	137.0
Net movement of funds	(403.5)	86.7
Net debt at the start of year	(63.4)	(146.4)
Exchange	36.5	(3.7)
Net debt at the end of year	(430.4)	(63.4)



Operating cash flow grew much more strongly than operating profit, as several of the factors that depressed profit performance had no bearing on the cash position. At £219.0m, operating cash flow was almost 50% higher than in 1995 and represented around 80% of operating profit, after adjusting for the Penguin charge and income from associates. The increase in operating cash flow is due to a number of factors. 1996 saw both profit and cash generation increase at Addison Wesley Longman, helped by a £4.5m operating cash inflow from the HarperCollins Educational acquisition. Overall, the Information Division improved cash collections and saw operating cash flow increase from £77.3m to £122.0m. Penguin benefited from the receipt of £12.2m following the acquisition of Putnam Berkley in December.

Capital expenditure reduced as the new hotel at Alton Towers became operational, but 1996 was absent the cash received in 1995 on the sale of Edinburgh Gate, the UK headquarters of Addison Wesley Longman, giving a net increase in the cash outflow relating to fixed assets.

Dividends paid increased by £5.0m reflecting both the larger number of shares in issue and the increase in the dividend amount per share.

The cash outflow due to acquisitions, disposals and non operating activities reflects the purchases of HarperCollins Educational for cash of £369.2m,

Putnam Berkley for £200.9m and Recoletos for £31.0m, offset in part by the disposal of Westminster Press for net cash of £297.0m.

Treasury management

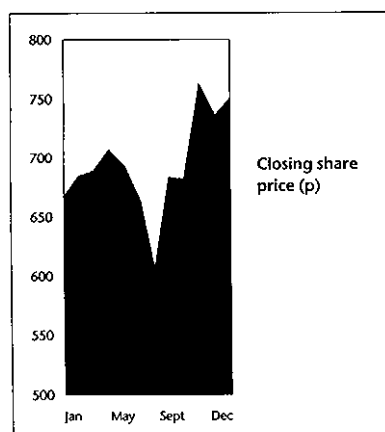
Treasury policy

The treasury activities of the Group are carried out in accordance with treasury policies which are approved by the board and implemented by the finance director. The treasury department is not operated as a profit centre and is subject to audit. A structure was put in place in 1996 whereby the finance director and a treasury committee of the board receive reports and review and comment upon the treasury policies of the Group.

Borrowings

The Group's policy is to manage the amount of its net debt (i.e. total borrowings less cash and liquid funds) and the level of interest cover in a manner which is consistent with the maintenance of its credit ratings at, or near, their current levels. The Group's current ratings from Standard & Poor's and Moody's are A and A2 respectively for long-term debt and A1 and P1 respectively for short-term debt. The Group's credit ratings for long-term debt were reduced from A+ and A1 respectively following the acquisition of Putnam Berkley in December 1996.

At 31 December 1996, total borrowings amounted to £729m, comprising £379m of US dollar borrowings and £210m of sterling



borrowings, with the remainder in a variety of other currencies.

The Group uses foreign currency debt to hedge a proportion of the value of its overseas assets. The aim is to reduce fluctuations in shareholders' funds resulting from changes in foreign exchange rates.

Net borrowings in a particular currency may be varied if there is some other element of risk for operational reasons, but the normal aim is to hedge around 20% of capital employed in each principal foreign currency.

Long-term financing requirements are met through sterling and US dollar debt issues in the capital markets. A guideline is in place whereby between 25% and 75% (with a norm of 50%) of core borrowings should come from non-bank sources. During 1996 a \$750m medium term note ('MTN') programme was set up in the United States, under which a \$250m 10 year MTN was issued in September 1996. The proceeds from this issue, which was swapped from fixed to floating rates, were used to repay short-term commercial paper borrowings.

The group aims to have a diversity of debt maturity dates to avoid a concentration of refinancing risk in any single period. The guideline is that the weighted average maturity of our core gross borrowings is between three and eight years. It currently stands at 7.2 years.

Short-term funding requirements are met through committed or uncommitted bank facilities and through the US commercial paper programme. At 31 December 1996, committed bank facilities amounted to £487m, of which £325m had a maturity of over five years. The general guideline is that available undrawn committed bank facilities should be above £200m.

Cash

At 31 December 1996, total cash and liquid funds amounted to £299m, consisting mainly of sterling and US dollars. Funds which are temporarily surplus to business requirements are invested in a range of money market instruments, including AAA-rated asset-backed securities, with a view to maximising after-tax returns while preserving liquidity and managing counterparty risk. In order to ensure that the portfolio is appropriately diversified, limits for individual issuers and assets are regularly reviewed, having regard inter alia to published credit ratings, and these limits are subject to approval by the finance director.

Interest rate management

Pearson's interest rate exposure arises principally in relation to sterling and the US dollar. Interest rate exposure is managed within parameters agreed by the board, with the principal policy guideline being that the interest rate on at least one third of core sterling and US dollar borrowings should be fixed or capped for around the next five years. Some of this is achieved by borrowing on a fixed rate basis, but in addition

the Group enters into interest rate swaps and forward rate agreements to modify the interest rate reset profile of its borrowing portfolio. At 31 December 1996, 43% of US dollar borrowings were fixed at a weighted average rate of 5.95% and 24% of sterling borrowings were fixed at a weighted average rate of 10.5%. In June 1997 the pro forma proportion of sterling borrowings on a fixed or capped basis will rise to 48%, taking into account the expiration of £50m of sterling interest rate swap contracts at that date. In broad terms, a 1% rise in US dollar interest rates would increase the net interest charge by £2m, while a 1% rise in sterling interest rates would increase the net interest charge by £1m.

Foreign exchange

Foreign currency transactional cash flows are normally hedged on the basis of rolling forecasts for periods of up to twelve months, but unremitted profits are not hedged. Cross border trading flows and other recurring items, such as dividends, giving rise to transactional foreign exchange exposure in the UK amounted to the equivalent of approximately £84m in 1996.

Accounting policies and standards

The accounting policies of the Group are shown on pages 29 and 30. These policies remain unchanged and have been applied consistently throughout the year.

During the year FRS1 (Revised 1996) 'Cash Flow Statements' was published by the Accounting Standards Board. The new format of presentation of the cash flow statement contained within the revised Standard has been adopted in these financial statements.

In addition, compliance with FRS8 'Related Party Disclosures' became mandatory during the year. Disclosure of related party transactions and balances is shown in note 28 to the Accounts.

Share price and market capitalisation

The share price ended the year at 749.5 pence, close to its high during the year of 760 pence and well above 1996's low of 601 pence. This represents an increase of 20% on the closing share price of 624 pence at the end of 1995 compared with an increase of nearly 12% in the FTSE 100 index and 25% in the FTSE Media index.

Based on the year end share price of 749.5 pence the market capitalisation of the Group was £4,280m.

Report of the Directors

The directors have pleasure in presenting their report to shareholders, together with the financial statements for the year to 31 December 1996 on pages 25 to 57. The principal activities of the Group are carried out in three main sectors: information, education and entertainment. More details of these and other activities, the development of the Group and its subsidiaries and likely future developments are given in the Operating and Financial Review on pages 1 to 13 and on pages 4 to 22 of the Annual Report. Sales and profits of the different sectors and geographical markets are given on pages 31 and 32 of this report.

Results and dividends

The profit for the financial year to 31 December 1996 was £240.5m (1995: £261.0m). The profit retained for the year was £137.8m (1995: £169.2m) and has been transferred to reserves. A final dividend of 11.1p per share is proposed for the year to 31 December 1996. This, together with the interim dividend already paid, makes a total for the year of 18.0p (1995: 16.5p). The final dividend will be paid on 6 June 1997 to shareholders on the register at the close of business on 11 April 1997, the record date.

Significant acquisitions and disposals

During the year, Pearson acquired HarperCollins Educational Publishers and Putnam Berkley in the USA and SelecTV plc in the UK, of which the Alomo and Witzend production businesses have been retained. Pearson also increased its holding in Recoletos from 56.7% to 94.2%. Further disclosure of these transactions can be found in note 23 to the accounts and on pages 1 to 13 of this report.

In December 1996, Pearson disposed of Westminster Press.

Transactions with related parties

For transactions with related parties which are reportable under FRS8, including the increase in Pearson's holding in Recoletos, please refer to note 28 to the accounts.

Post balance sheet events

In February 1997 Pearson acquired a 50% stake in Business Day and Financial Mail in South Africa for a consideration of £11.5m and sold its 10% stake in Television Broadcasts Ltd in Hong Kong for £111.1m.

In March Pearson agreed to sell its interests in the satellite and cable channels, UK Gold (20%) and UK Living (25%), to Flextech as part of joint venture agreements between Flextech and the BBC. The sale of these interests involves the payment by Flextech, between now and December 1998, of £7.8m representing the repayment of UK Living loan stock, and Pearson Television receiving 8.8m Flextech ordinary shares – a total consideration

of approximately £76m based on a Flextech share price of 772p. Following completion of the transaction, Pearson will own 5.6% of the enlarged share capital of Flextech.

Further details are given in note 31.

Corporate governance

The board has reviewed the Company's procedures in the light of the Code of Best Practice published by the Committee on Financial Aspects of Corporate Governance and, in the opinion of the directors, the Company fully complies with it and has done so throughout the year.

Internal financial control – the board of directors has overall responsibility for the Group's system of internal financial control which it exercises through an organisational structure with clearly defined levels of responsibility and authority and appropriate reporting procedures. This structure includes an audit committee, comprising three non-executive directors, 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.

On 13 February 1997 we announced the discovery of the breakdown of certain internal controls at Penguin USA, which allowed the unauthorised practice of offering discounts to certain customers in exchange for early payment of invoices. Swift action was taken to stop this irregular practice and to determine how and why the accounting irregularities, which are described in greater detail in the Finance Director's Review on pages 26 to 28 of the Annual Report, were not detected. A thorough review of the Group's control procedures is currently being undertaken in order to ensure, as far as possible, that such an event cannot recur. On the evidence presented so far, both the directors and the auditors believe that the systems and controls in the Group are generally of high quality. However, it must be recognised that no internal control system can provide absolute assurance against misstatement or loss.

The following are the main elements of the Group's control systems:

Financial reporting – there is a comprehensive budgeting system with an annual budget approved by the directors. Monthly 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. More detailed financial information, including balance sheets and cash flow statements, is provided quarterly.

Treasury management – the treasury department operates within board approved policies. 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 group finance director and quarterly summaries are prepared for the board.

Risk management – the identification of major business risks is carried out in conjunction with operating management and steps are taken to mitigate or eliminate these where possible. In addition the Group provides insurance cover either through its captive insurance subsidiary or externally depending on the scale of the risk in question.

Operating company systems – each operating company maintains financial controls and procedures appropriate to its own business environment and carries out local treasury activities, in both cases conforming to overall standards and guidelines.

Self assessment – each year relevant senior executives and chief executives of operating units are required to confirm in writing compliance with appropriate standards of internal financial control in their respective areas.

Internal audit – the Group has a centralised internal audit department with operations located both in the UK and the US, which reviews systems and procedures in all major operating companies and reports regularly to the audit committee.

Going concern – having reviewed the Group's liquid resources and borrowing facilities and the 1997 and 1998 cash flow forecasts contained in the Group budget for 1997, the directors believe that the Group has 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.

Auditors – the report of the auditors on corporate governance matters is set out on page 24.

Directors

The directors are shown in the Report of the Remuneration Committee on pages 17 to 23 together with details of their interests in ordinary shares and options of Pearson plc. Six directors will retire by rotation at the Annual General Meeting. Of these, David Veit, Reuben Mark and Gill Lewis, being eligible, will offer themselves for re-election for a further three years. In addition, Lord Blakenham, Frank Barlow and Mark Burrell retire by rotation but will not seek re-election. Sir Simon Hornby will

also retire at the end of the AGM. Marjorie Scardino, who was appointed to the board on 1 January 1997, retires from office in accordance with article 77 of the Company's articles of association and, being eligible, offers herself for re-appointment. For details of directors' service contracts, see page 18.

No director was materially interested in any contract of significance to the Company's business.

Nomination process for non-executive directors

The nomination and appointment of non-executive directors is included in the items reserved for the full board.

Insurance of officers of the Company

During the year to 31 December 1996 the Company continued to provide liability insurance for its officers.

Supplier payment policy

The Company aims to pay all of its suppliers within a reasonable period of their invoices being received and in any case within the supplier's own standard payment period. Operating companies are responsible for agreeing the terms and conditions under which business transactions with their suppliers are conducted.

Employment

The Group employs 20,745 people, of whom 10,851 are 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. This means that the sole criterion for selection and promotion is the individual's suitability for the position of employment offered, including consideration of disabled persons for employment, training, career development and promotion on the basis of their aptitudes and abilities.

Training and development – the Group is committed to the continuous improvement of employee performance by developing skills and expertise through training and development. Each operating company has developed its own in-house programmes and courses to meet the needs of its employees and its business. Pearson also encourages employees to develop their careers by taking up opportunities in other parts of the Group.

All-employee share option scheme – the Pearson plc 'Save As You Earn' Share Option Scheme, introduced for UK employees in 1982 and renewed in 1992, attracts a high level of interest and participation. The most recent grant was taken up by over 1,500 employees, and a cumulative total of more than 23.8 million

Report of the Directors

options over ordinary shares has been granted, of which about 6.1 million were outstanding at the end of the year.

Communications – communications with employees continue to be developed through the distribution of the Pearson magazine, the Chairman's Report to Employees, the introduction of an intranet and the Report to Members of the UK Pension Plan. The various operating companies also have their own channels such as briefing groups, videos, magazines and newsletters.

European Employee Forum – in 1996, Pearson established a European Employee Forum with elected representatives for each of the Pearson Group companies based in Europe. The Forum is intended to provide an arena for the exchange of relevant and appropriate information and the establishment of a constructive dialogue between management and employees on transnational issues which affect them.

Contributions for charitable and political purposes

In 1996, charitable donations in the UK amounted to £568,000 (1995: £792,000) and overseas to £240,000 (1995: £258,000). Political contributions of £25,000 were made to each of the Conservative Party and the Labour Party. A contribution of £10,000 was made to the Centre for Policy Studies. For further information, see page 23 of the Annual Report.

Share capital

Details of share issues are given in note 21.

At the Extraordinary General Meeting held on 3 May 1996, the Company was authorised, subject to certain conditions, to acquire up to 55.7 million of its ordinary shares by market purchase. This authority expires on the date of the forthcoming Annual General Meeting. Although circumstances have not merited using it and there are no plans at present to do so, shareholders are being asked to renew this authority.

At 17 March 1997, beneficial interests amounting to 3% or more of the issued ordinary share capital of the Company notified to the Company comprised:

	No. of Shares	%
Companies associated with		
Lazard Frères et Cie., Paris	48,129,727	8.42

Scrip dividend alternative

The Company operates a scrip dividend scheme under which a total of 868,318 new ordinary shares were issued in respect of the last two dividends in response to elections for shares instead of cash, made by around 5,000 shareholders on each occasion,

saving approximately £5.7m in cash and deferring approximately £1.4m of corporation tax. Details of the scrip dividend alternative for the final dividend for 1996 will be sent out to shareholders on 28 April 1997.

Close company status

The Company is not a close company within the terms of the Income and Corporation Taxes Act 1988.

Capital expenditure

The analysis of capital expenditure and details of capital commitments are shown in note 10.

Annual General Meeting

The notice convening the Annual General Meeting to be held at 12 noon on Friday, 2 May 1997 is contained in the enclosed circular.

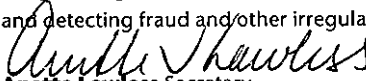
Registered auditors

In accordance with sections 384 and 390A of the Companies Act 1985 (the Act) resolutions proposing the re-appointment of Price Waterhouse as auditors to the Company, at a level of remuneration to be agreed by the directors, will be put to the shareholders at the Annual General Meeting, special notice having been given pursuant to sections 379 and 391A 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. In preparing those financial statements, the directors are required to select suitable accounting policies and apply them consistently and make judgements and estimates that are reasonable and prudent.

The directors must also state whether applicable accounting standards have been followed and disclose and explain any material departures in the financial statements which must be prepared on the going concern basis unless it is inappropriate to presume that the Group will continue in business. The directors are responsible for the maintenance of adequate accounting records in compliance with the Companies Act 1985, for safeguarding the assets of the Group, and for preventing and detecting fraud and other irregularities.


Anette Lawless Secretary

17 March 1997

Report of the Remuneration Committee

The committee, which is composed of non-executive directors, is chaired by Sir Simon Hornby. Other members in 1996 were Dennis Stevenson, Gill Lewis and Reuben Mark. In view of his forthcoming appointment as chairman, Dennis Stevenson ceased to be a member of the committee in December 1996.

The terms of reference of the committee are to decide the remuneration and benefits packages of the executive directors and approve the recommended remuneration and benefits packages of the chief executives of the main operating subsidiaries. The committee determines the annual guidelines for executive long-term incentive plans and recommends the awards to be made under these plans.

The committee also recommends the chairman's remuneration to the board for its decision.

The committee confirms that the Company has complied throughout the year with Section A and that it has taken into account Section B annexed to the Listing Rules of the Stock Exchange.

Remuneration policy for executive directors

The committee's policy is designed to attract, retain and motivate high calibre senior executives through pay and other arrangements which are competitive and represent best practice, while also relating reward to performance and aligning the interests of directors and senior management with the interests of shareholders.

The main components are base salary, an annual cash bonus plan, long-term incentives and pension benefits. In addition, the Company provides company car and health care benefits. The Company also provides housing for Marjorie Scardino, who is a US national. Further details of Marjorie Scardino's remuneration can be found below table 2 on page 19.

Base salary – the committee aims to set base salaries in the region of the upper quartile of the range paid to directors and executives in similar positions in comparable companies, in return for above-average performance. This policy was established five years ago when annual bonuses, which had previously been unlimited, were capped. The committee believes salaries should reflect the experience, responsibilities, effectiveness and market value of the individual executives concerned.

Annual bonus – under the annual bonus plan, bonuses of up to 50% of annual base salary can be earned by reference to performance against financial targets determined by the committee. The committee may also award individual discretionary bonuses. Annual bonuses do not form part of pensionable earnings.

In 1996, the bonus target for directors was related to the Company's adjusted earnings per share and operating cash flow, with the exception of David Bell and Greg Dyke, part of whose targets were related to the performance of their individual divisions.

Long-term incentives

The committee considers that long-term incentive plans align the personal interests of directors and executives with those of shareholders.

The operation of long-term incentive plans for executives is subject to on-going review by the committee taking into account legislative and regulatory developments, particularly with regard to the establishment of performance conditions and evolving best practice.

Share option schemes – the Company operates a UK Inland Revenue approved and two United States executive share option schemes. The UK scheme was amended in 1996 to allow unapproved options to be granted in addition to options granted within the new Inland Revenue limit of £30,000, but within the normal limit of four times earnings authorised by shareholders.

Executive options are granted to eligible executives under the 1988 Executive Share Option Scheme and the 1992 United States Executive Share Option Scheme based on guidelines established by the committee on the total number of options which may be granted, the frequency of awards and the progression towards these maxima.

A 'Save As You Earn' share option scheme is also open to all eligible employees in the UK.

Incentive share plan – the incentive share plan (the Plan), first introduced on the recommendation of the committee in 1993, is designed to reward executives of the Group in such a way that their total remuneration reflects the relative performance of the Company in terms of the total return received by shareholders over the medium to longer term.

Under the Plan, participants are conditionally awarded a certain number of Pearson shares which are held in an employee share trust for a specified period, currently three years. At the end of this period, the shares, together with the dividends on these shares, which are taken in the form of scrip and rolled up, can be released depending upon the extent to which previously determined performance conditions, both absolute and in relation to the *FTSE 100* index, are met. For existing awards the maximum release of shares is made if the total return to Pearson shareholders exceeds the equivalent average *FTSE 100* figure by 25% over the period. The performance criteria are reviewed from time to time to ensure that they remain appropriate. Details of directors' awards under the Plan are set out in table 6 on page 23 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.

Report of the Remuneration Committee

Service contracts

All executive directors have agreements which can be terminated by the Company on 12 months notice, although the earliest expiry date of Marjorie Scardino's employment is 31 December 1999. The committee considered that this initial fixed notice period was appropriate and necessary in order to attract her to the Company as its chief executive. In the event of early termination by the Company without cause of the service agreements of those directors appointed since January 1996, the contracts provide for liquidated damages to be payable, equivalent to 12 months base salary, benefits and a proportion of annual bonus. In the case of Marjorie Scardino, the amount of liquidated damages payable is equivalent to 15 months and 18 months base salary, benefits and a proportion of bonus should her employment be terminated without cause in the first or second year respectively. The committee feels that these provisions for liquidated damages are adequate, but not excessive, compensation for loss of office.

Non-executive directors' remuneration

Fees for non-executive directors' duties 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 re-imbursement for expenses incurred in connection with their directorship of the Company) and do not participate in the Company's share option schemes or incentive share plan.

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.

Pension benefits

Michael Blakenham, Frank Barlow, Mark Burrell and James Joll are members of the non-contributory Pearson Section of the Pearson Group Pension Plan, which is now closed to new membership.

They are entitled to pensions of two thirds of final base salary at the normal retirement age of 62 and like all other plan members may retire with company consent at age 60 without any early retirement reduction. In 1988 (on the formation of the Pearson Group Pension Plan) all former members of the S. Pearson & Son Pension Scheme, including Michael Blakenham, James Joll and Mark Burrell, received pension enhancements equivalent to 40% of accrued service to 1 August 1988. The combined pension benefits are within Inland Revenue limits.

The Company contributed a total of £97,965 in matching the additional voluntary contributions (AVCs) made by the above directors.

The pensions of James Joll and Frank Barlow are augmented with effect from their retirement dates of 31 December 1996 (James Joll) and 2 May 1997 (Frank Barlow). The costs of these augmentations are £250,000 for James Joll and £253,333 for Frank Barlow.

David Veit's pension arrangements are based in the United States and \$239,967 was allocated in respect of his pension plan in 1996.

David Bell, John Makinson and Greg Dyke are members of the Final Pay Section of the Pearson Group Pension Plan, which has 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 transferred service from the Financial Times. Both John Makinson and Greg Dyke are subject to the pensions earnings cap introduced by the Finance Act 1989. 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 scheme).

John Makinson and Greg Dyke are entitled to supplements of 31.1% and 50% of annual base salary respectively to compensate them for pension benefits which cannot be provided from the plan because of the pensions cap regulations.

All the 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 3 on page 20 of this report.

Table 1

Directors' emoluments:	1996 £000's	1995 £000's	1994 £000's	1993 £000's	1992 £000's	1991 £000's	1990 £000's
Base salaries	1,996	1,383	1,270	1,186	1,057	1,007	953
Bonus	173	—	635	593	55	60	—
Three year incentive share plan	—	1,687	—	—	—	—	—
Other emoluments	945	287	353	392	292	251	224
Fees to non-executive directors	210	224	212	219	141	124	122
Total	3,324	3,581	2,470	2,390	1,545	1,442	1,299

Other emoluments comprised any pension contributions and augmentations, compensation for early termination of contract and company car and health care benefits.

The shares awarded in 1993 under the Company's three year incentive share plan were released on 8 August 1996. The share price on 8 August was lower than the price reported in the 1995 Directors' Report and Accounts. However, this decrease was not deemed to be material.

Table 2

Remuneration of the directors:

Excluding contributions to approved pension funds and compensation for early termination of contract, directors' remuneration was as follows:

Name:	1996 Salary/fees £000's	Bonus £000's	Other £000's	3-year ISP £000's	1996 Total £000's	1995 Salary/fees £000's	Bonus £000's	Other £000's	3-year ISP £000's	1995 Total* £000's
Executive directors:										
Michael Blakenham	315	—	38	—	353	300	—	37	413	750
Frank Barlow	380	—	41	—	421	330	—	40	413	783
David Bell†	179	12	10	—	201	—	—	—	—	—
Mark Burrell	207	—	42	—	249	200	—	42	287	529
Greg Dyke†	183	100	108	—	391	—	—	—	—	—
James Joll	250	—	38	—	288	230	—	37	287	554
John Makinson†	179	61	16	—	256	—	—	—	—	—
David Veit	303	—	10	—	313	323	—	11	287	621
Non-executive directors:										
Michel David-Weill	25	—	—	—	25	25	—	—	—	25
Pehr Gyllenhammar	25	—	—	—	25	30	—	—	—	30
Jean-Claude Haas†	11	—	—	—	11	32	—	—	—	32
Sir Simon Hornby	25	—	—	—	25	25	—	—	—	25
Gill Lewis	25	—	—	—	25	30	—	—	—	30
Reuben Mark	32	—	—	—	32	32	—	—	—	32
Vernon Sankey	25	—	—	—	25	25	—	—	—	25
Dennis Stevenson	25	—	—	—	25	25	—	—	—	25
David Verey†	17	—	—	—	17	—	—	—	—	—

*The incentive share plan release relating to the three-year period 1993–1995 is included in the total 1995 remuneration figure.

†David Bell, Greg Dyke and John Makinson were appointed to the board on 15 March 1996. David Verey became a non-executive director on 3 May 1996. Jean-Claude Haas retired from the board on 3 May 1996. In the case of David Bell, Greg Dyke and John Makinson, the emoluments shown relate to the ten-month period from March to December 1996, with the exception of bonus, which relates to the full year.

A sum of £250,000 was paid to James Joll as compensation for early termination of his contract, which had a three-year notice period. In addition his pension was augmented with effect from his retirement date at a capital cost of £250,000.

Marjorie Scardino joined the board and became chief executive on 1 January 1997, at a base salary of £396,500, although for pension and bonus purposes, her salary is deemed to be £425,000 (so as to include an element of the housing benefit referred to below). She received a joining bonus of £130,000 in consideration of the loss of potential benefits with her previous employer. She participates in the annual bonus plan and the incentive share plan, under which she will be conditionally awarded shares to the value of £300,000 in 1997, £200,000 in 1998 and £200,000 in 1999. Housing is provided at an initial annual cost to the Company of £60,500 and she receives a pension supplement of 25% of salary to provide for benefits in excess of the pensions earnings cap.

Dennis Stevenson will receive annual fees of £240,000 on becoming chairman on 2 May 1997. He will also participate in the incentive share plan, under which he will be conditionally awarded shares to the value of £300,000 upon appointment and £200,000 one year later, each vesting over five years. Dennis Stevenson's fees for 1996 were paid to SRU Limited.

Frank Barlow was the highest paid director in 1996. His total remuneration, including pension contributions, amounted to £421,346. The chairman's total remuneration, including pension contributions, amounted to £352,979.

Report of the Remuneration Committee

Table 3

	Years of pensionable service	Accrued pension		Increase in accrued pension over the period
		31.12.95* £000's pa	31.12.96 £000's pa	£000's pa
Directors' pensions:				
Michael Blakenham	31	231.1	248.7	17.6
Frank Barlow	29	216.9	250.1	33.2
David Bell	24	91.6	95.6	4.0
Mark Burrell	34	157.4	166.3	8.9
Greg Dyke	2	1.2	2.3	1.1
James Joll	17	185.0	205.6	20.6
John Makinson	3	5.7	7.1	1.4
David Veit	35	116.8	128.2	11.4

*Or date of director's appointment, if later.

The accrued pension figures in the above table relate only to the normal entitlements (excluding the effect of augmentations and supplements paid to 'capped' directors) from the Pearson Group Pension Plan in respect of each of the directors other than David Veit, whose pension arrangements are based in the United States.

For further information relating to pensions generally, please refer to page 18 of this report.

Table 4

Interests of directors were:	Ordinary shares		Options – Ordinary shares		Incentive share plan ‡ – Ordinary shares		Maximum number of shares in lieu of adjustment on Royal Doulton Demerger
	31.12.96*	1.1.96**	31.12.96*	1.1.96**	31.12.96*	1.1.96**	
Michael Blakenham	138,214	101,580	417,454	417,454	31,926	72,919	12,908
(non beneficial)	129,040	129,040	–	–	–	–	–
Frank Barlow	38,750	6,939	419,794	419,794	25,107	72,919	11,235
David Bell	9,303	8,348	111,156	85,469	6,790	6,620	628
Mark Burrell	791,674	1,032,504	283,339	282,799	15,222	50,276	9,840
(non beneficial)	65,040	65,040	–	–	–	–	–
Michel David-Weill†	48,129,727	48,129,727	–	–	–	–	–
Greg Dyke	–	–	106,900	73,300	6,790	6,620	–
Pehr Gyllenhammar	–	–	–	–	–	–	–
Jean-Claude Haas	29,537	29,537	–	–	–	–	–
Sir Simon Hornby	4,000	4,000	–	–	–	–	–
James Joll	25,494	2,093	155,846	155,847	9,160	50,276	4,541
Gill Lewis	–	–	–	–	–	–	–
John Makinson	1,000	–	103,784	68,000	–	–	–
Reuben Mark	7,600	7,600	–	–	–	–	–
Vernon Sankey	–	–	–	–	–	–	–
Dennis Stevenson	38,000	8,000	–	–	–	–	–
David Veit	253,602	107,712	245,380	348,869	31,892	50,276	–
David Verey	–	–	–	–	–	–	–

†Mr David-Weill's interests include 48,088,523 ordinary shares owned by companies associated with Lazard Frères et Cie., Paris.

*Or date of retirement, if earlier.

**Or date of appointment, if later.

‡A full explanation of this plan is given on page 17. The number of shares shown represents the maximum number of shares, plus accumulated scrip dividend shares, comprised in the original award which may be transferred to the individual concerned.

Executive directors of the Company, as possible beneficiaries, are also deemed to be interested in the Pearson Employee Share Trust, the trustee of which held 149,933 Pearson ordinary shares of 25p each at 31 December 1996 and 148,395 ordinary shares at 17 March 1997, the latest practicable date prior to the printing of this report.

Marjorie Scardino was appointed to the board with effect from 1 January 1997, at which date she had no interests in Pearson securities. On 16 January 1997, she acquired 10,000 ordinary shares of 25p each in the Company. Also on 16 January 1997, John Makinson acquired a further 2,000 ordinary shares of 25p each, taking his total holding to 3,000 shares.

Report of the Remuneration Committee

Table 5

Movements in directors' interests in share options	Date of Grant	Options held at 1.1.96	Exercise price (pence)†	Options granted	Options exercised	Market price* on day of exercise	Options held at 31.12.96
Michael Blakenham	21.04.89	150,000	353	–	–	–	150,000
UK Executive	24.04.90	220,000	329	–	–	–	220,000
	06.05.94	4,300	635	–	–	–	4,300
	20.04.95	39,400	545	–	–	–	39,400
SAYE	04.10.91	3,754	299	–	–	–	3,754
		417,454					417,454
Frank Barlow	21.04.89	100,000	353	–	–	–	100,000
UK Executive	24.04.90	220,000	329	–	–	–	220,000
	06.05.94	63,900	635	–	–	–	63,900
	20.04.95	29,800	545	–	–	–	29,800
SAYE	04.10.91	3,754	299	–	–	–	3,754
	08.10.92	1,549	242	–	–	–	1,549
	19.05.95	791	436	–	–	–	791
		419,794					419,794
David Bell	06.05.94	50,000	635	–	–	–	50,000
UK Executive	24.04.95	29,300	545	–	–	–	29,300
	08.08.96	–	654	26,500	–	–	26,500
SAYE	12.10.90	1,409	265	–	1,409	728	–
	04.10.91	1,250	299	–	–	–	1,250
	08.10.92	2,324	242	–	–	–	2,324
	19.05.95	1,186	436	–	–	–	1,186
	23.05.96	–	578	596	–	–	596
		85,469					111,156
Mark Burrell	21.04.89	100,000	353	–	–	–	100,000
UK Executive	24.04.90	180,000	329	–	–	–	180,000
SAYE	04.10.91	1,250	299	–	1,250	711	–
	08.10.92	1,549	242	–	–	–	1,549
	23.05.96	–	578	1,790	–	–	1,790
		282,799					283,339
Greg Dyke	20.04.95	73,300	545	–	–	–	73,300
UK Executive	08.08.96	–	654	33,600	–	–	33,600
		73,300					106,900
James Joll	24.04.90	120,000	329	–	1	717	119,999
UK Executive	06.05.94	2,400	635	–	–	–	2,400
	20.04.95	25,700	545	–	–	–	25,700
SAYE	08.10.92	7,747	242	–	–	–	7,747
		155,847					155,846

Table 5 continued

Movements in directors' interests in share options	Date of Grant	Options held at 1.1.96	Exercise price (pence)†	Options granted	Options exercised	Market price* on day of exercise	Options held at 31.12.96
John Makinson	06.05.94	50,000	635	–	–	–	50,000
UK Executive	20.04.95	18,000	545	–	–	–	18,000
	08.08.96	–	654	32,800	–	–	32,800
SAYE	23.05.96	–	578	2,984	–	–	2,984
		68,000					103,784
David Veit	21.04.89	103,489	341	–	103,489	661	–
US Executive	24.04.90	103,489	317	–	–	–	103,489
	11.05.90	82,791	334	–	–	–	82,791
	20.04.95	59,100	545	–	–	–	59,100
		348,869					245,380

†The exercise prices have been rounded down to the nearest whole penny for ease of reference.

*Mid-market quotation at close of business on the date of exercise, rounded down to the nearest whole penny.

No options lapsed during the year. The mid-market price of the shares at 31 December 1996 was 749p and the range during 1996 was 601p to 760p.

Outstanding UK executive options become exercisable on the third anniversary of the grant and lapse if they remain unexercised after the tenth.

Outstanding US executive options granted before May 1990 became exercisable on the third anniversary of the grant and lapse if they remain unexercised after the seventh. Options granted from May 1990 onwards become exercisable on the third anniversary of the grant and lapse if they remain unexercised after the tenth.

SAYE options become exercisable on the fifth or seventh anniversary of the grant and lapse if not exercised within six months of that anniversary.

In all the above cases, special rules apply if a director ceases to be employed by the Company.

Table 6

Movements in directors' interests under the incentive share plan	No. of shares outstanding at 1.1.96*	Maximum conditional awards in 1996 including scrip dividend on Plan shares†	No. of shares vested and released	No. of shares lapsed	Market price on date of release	No. of shares outstanding at 31.12.96
Michael Blakenham	72,919	19,139	60,132	–	648p	31,926
Frank Barlow	72,919	12,320	60,132	–	648p	25,107
David Bell	6,620	170	–	–	–	6,790
Mark Burrell	50,276	6,705	41,759	–	648p	15,222
Greg Dyke	6,620	170	–	–	–	6,790
James Joll	50,276	643	41,759	–	648p	9,160
John Makinson	–	–	–	–	–	–
David Veit	50,276	23,375	41,759	–	648p	31,892

*Or the date of appointment, if later.

†The award as stated is the maximum number of shares which may vest, subject to various performance conditions as described on page 17 being fulfilled.

Report of the Auditors on Corporate Governance Matters

To the Directors of Pearson plc

In addition to our audit of the financial statements we have reviewed your statements in the Directors' Report on pages 14 and 15 concerning the Group's compliance with the paragraphs of the Cadbury Code of Best Practice specified for our review by the London Stock Exchange and the adoption of the going concern basis in preparing the financial statements. The objective of our review is to draw attention to non-compliance with Listing Rules 12.43(j) and 12.43(v), if not otherwise disclosed.

Basis of opinion

We carried out our review having regard to guidance issued by the Auditing Practices Board. That guidance does not require us to perform the additional work necessary to, and we do not, express any opinion on the effectiveness of either the Group's system of internal financial control or corporate governance procedures nor on the ability of the Group to continue in operational existence.

Opinion

In our opinion, your statements on internal financial control and on going concern on pages 14 and 15 have provided the disclosures required by the Listing Rules referred to above and are consistent with the information which came to our attention as a result of our audit work on the financial statements.

In our opinion, based on enquiry of certain directors and officers of the Company and examination of relevant documents, your statement on page 14 appropriately reflects the Group's compliance with the other aspects of the Code specified for our review by Listing Rule 12.43(j).

Price Waterhouse

Chartered Accountants
London, 17 March 1997

Report of the Auditors to the Members of Pearson plc

We have audited the financial statements on pages 25 to 57 (including the additional disclosures on pages 17 to 23 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 and the accounting policies set out on pages 29 and 30.

Respective responsibilities of Directors and Auditors

As described on page 16, the Company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of 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 1996 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.

Price Waterhouse

Chartered Accountants and Registered Auditors
London, 17 March 1997

Consolidated Profit and Loss Account

for the year ended 31 December 1996

		1996			1995		
	Notes	Operating activities £m	Other items £m	Total £m	Operating activities £m	Other items £m	Total £m
Sales							
Continuing operations		1,845.9	–	1,845.9	1,687.1	–	1,687.1
Acquisitions		203.0	–	203.0	–	–	–
		2,048.9	–	2,048.9	1,687.1	–	1,687.1
Discontinued operations		137.1	–	137.1	143.3	–	143.3
Total sales	2	2,186.0	–	2,186.0	1,830.4	–	1,830.4
Cost of sales	3	(1,064.1)	–	(1,064.1)	(939.7)	–	(939.7)
Gross profit		1,121.9	–	1,121.9	890.7	–	890.7
Net operating expenses – normal	3	(853.3)	–	(853.3)	(627.7)	–	(627.7)
– exceptional	3	(40.4)	(100.0)	(140.4)	(46.7)	–	(46.7)
Net income from partnerships and associated undertakings	11	53.1	–	53.1	43.3	–	43.3
Operating profit							
Continuing operations		219.9	(100.0)	119.9	237.6	–	237.6
Acquisitions		26.1	–	26.1	–	–	–
		246.0	(100.0)	146.0	237.6	–	237.6
Discontinued operations		35.3	–	35.3	22.0	–	22.0
Total operating profit	2	281.3	(100.0)	181.3	259.6	–	259.6
Continuing operations:							
Profit/(loss) on sale of fixed assets	4	–	(14.1)	(14.1)	–	123.4	123.4
Profit/(loss) on sale of businesses	5	–	(1.9)	(1.9)	–	6.0	6.0
Discontinued operations:							
Profit on sale of Westminster Press	5	–	231.3	231.3	–	–	–
Profit before interest		281.3	115.3	396.6	259.6	129.4	389.0
Net interest payable	6	(29.5)	–	(29.5)	(23.9)	–	(23.9)
Loan stock redemption premium	6	–	(10.3)	(10.3)	–	–	–
Profit before taxation		251.8	105.0	356.8	235.7	129.4	365.1
Taxation	7	(72.6)	(36.0)	(108.6)	(64.8)	(28.0)	(92.8)
Profit after taxation		179.2	69.0	248.2	170.9	101.4	272.3
Equity minority interests		(7.7)	–	(7.7)	(11.3)	–	(11.3)
Profit for the financial year		171.5	69.0	240.5	159.6	101.4	261.0
Dividends on equity shares	8	(102.7)	–	(102.7)	(91.8)	–	(91.8)
Profit retained	22	68.8	69.0	137.8	67.8	101.4	169.2
Adjusted earnings/							
total earnings per equity share		30.6p	12.3p	42.9p	28.8p	18.3p	47.1p
Dividends per equity share		18.0p	–	18.0p	16.5p	–	16.5p
Average number of shares (millions)		560.8	560.8	560.8	554.4	554.4	554.4

In order to show results from operating activities an adjusted earnings per equity share has been calculated which excludes profits on the sale of fixed assets and businesses (see notes 4 and 5), the loan stock redemption premium (see note 6), the £100m charge for improper accounting at Penguin USA (see note 2) and the tax consequences of these items.

Consolidated Balance Sheet

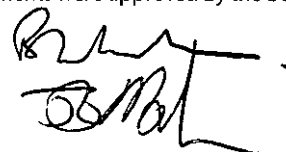
as at 31 December 1996

	Notes	1996 £m	1995 £m
Fixed assets			
Tangible assets	10	484.0	530.1
Investments:			
Partnerships and associated undertakings	11	182.6	167.3
Other	12	242.0	228.2
		908.6	925.6
Current assets			
Stocks	13	360.7	289.9
Debtors	14	669.8	672.0
Investments	15	7.9	8.3
Cash and liquid funds	16	299.0	672.0
		1,337.4	1,642.2
Creditors – amounts falling due within one year:			
Short-term borrowing	17	(174.2)	(261.0)
Other creditors	18	(919.8)	(826.7)
		(1,094.0)	(1,087.7)
Net current assets		243.4	554.5
Total assets less current liabilities		1,152.0	1,480.1
Creditors – amounts falling due after more than one year:			
Medium and long-term borrowing	17	(555.2)	(474.4)
Other creditors	18	(15.1)	(15.9)
		(570.3)	(490.3)
Deferred taxation	19	(30.3)	(0.6)
Other provisions for liabilities and charges	20	(159.1)	(133.8)
Net assets		392.3	855.4
Capital and reserves			
Called up share capital	21	142.8	139.1
Share premium account	22	129.5	48.7
Revaluation reserve	22	5.4	6.9
Other reserves	22	1.2	1.4
Profit and loss account	22	109.7	637.1
Equity shareholders' funds		388.6	833.2
Equity minority interests		3.7	22.2
		392.3	855.4

The financial statements were approved by the board of directors on 17 March 1997 and signed on its behalf by

Blakenham

J Makinson



Consolidated Statement of Cash Flows

for the year ended 31 December 1996

		1996	1995
	Notes	£m	restated £m
Net cash inflow from operating activities	25	291.2	236.4
Interest received		45.6	37.7
Interest paid		(76.0)	(67.7)
Dividends paid to minority interests		(6.1)	(10.8)
Returns on investments and servicing of finance		(36.5)	(40.8)
Taxation		(80.8)	(69.7)
Purchase of tangible fixed assets		(89.8)	(100.2)
Sale of tangible fixed assets		13.2	40.2
Purchase of investments		(33.5)	(132.1)
Sale of investments		53.7	633.9
Capital expenditure and financial investment		(56.4)	441.8
Purchase of subsidiary undertakings		(697.9)	(359.8)
Net cash acquired with subsidiary undertakings		4.5	8.6
Purchase of associated undertakings		(36.0)	(57.1)
Sale of businesses		307.2	3.9
Net cash disposed with subsidiary undertakings		(5.5)	(1.1)
Acquisitions and disposals	23/24	(427.7)	(405.5)
Equity dividends paid		(96.0)	(86.3)
Cash (outflow)/inflow before management of liquid resources and financing		(406.2)	75.9
Disposal/(purchase) of asset backed securities		204.1	(172.7)
Liquid resources acquired		(65.1)	(304.3)
Liquid resources disposed		212.4	252.0
Management of liquid resources	25	351.4	(225.0)
Issue of equity share capital		14.1	11.8
Loan stock redemption premium		(10.3)	-
Capital element of finance lease rentals		(1.1)	(1.7)
US medium term notes – repayable 1999		157.8	-
Net movement in other borrowings		(138.9)	256.6
Financing		21.6	266.7
(Decrease)/increase in cash in the year	25	(33.2)	117.6

Statement of Total Recognised Gains and Losses

for the year ended 31 December 1996

	1996 £m	1995 £m
Profit for the financial year	240.5	261.0
Other net gains and losses recognised in reserves:		
Unrealised surplus on revaluations	–	2.0
Exchange translation effect on:		
Profit for the financial year	(0.4)	1.8
Foreign currency net assets	(35.5)	5.7
	(35.9)	9.5
Total recognised gains and losses relating to the year	204.6	270.5

Note of Historical Cost Profits and Losses

for the year ended 31 December 1996

	1996 £m	1995 £m
Reported profit before taxation	356.8	365.1
Realisation of fixed investment revaluations	–	458.3
Realisation of property revaluations	(1.2)	0.9
Historical cost profit on ordinary activities before taxation	355.6	824.3
Deferred tax on fixed investment revaluations	–	(150.8)
Historical cost profit retained after taxation, equity minority interests and dividends	136.6	477.6

Reconciliation of Movements in Equity Shareholders' Funds

for the year ended 31 December 1996

	1996 £m	1995 £m
Profit for the financial year	240.5	261.0
Dividends on equity shares	(102.7)	(91.8)
	137.8	169.2
Other net recognised gains and losses relating to the year (see above)	(35.9)	9.5
Goodwill arising	(632.4)	(393.4)
Goodwill written back	1.4	–
Shares issued	84.5	11.8
Net movement for the year	(444.6)	(202.9)
Equity shareholders' funds at beginning of year	833.2	1,036.1
Equity shareholders' funds at end of year	388.6	833.2

Notes to the Accounts

1 Accounting policies

Accounting policies have been consistently applied. FRS 1 (Revised 1996) 'Cash Flow Statements' has been adopted early and comparative figures, including associated notes, have been restated. FRS 8 'Related Party Disclosures' has been adopted. Comparative figures in the profit and loss account have been restated to reflect the revised presentation of results. Balance sheet presentation has been restated to show advance corporation tax recoverable in debtors rather than in deferred taxation.

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

- (i) 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.
- (ii) Goodwill – Goodwill, being either the net excess of the cost of shares in subsidiary undertakings, partnerships and associated undertakings over the value attributable to their net tangible assets on acquisition or the cost of other goodwill by purchase, is deducted from reserves in the year of acquisition. On disposal or closure, goodwill previously charged to reserves is written back and the profit or loss is adjusted accordingly.
- (iii) Partnerships and associated undertakings – The profit of the Group includes the Group's share of the profit of partnerships and associated undertakings, and the consolidated balance sheet includes the Group's interest in partnerships and associated undertakings 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 amounts invoiced during the period, net of valued added tax and other sales taxes, and excluding trade discounts, to external customers and associated undertakings for the provision of goods and services.

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 affecting these translations are the US dollar and the Spanish peseta. The weighted average rates for the year against sterling were \$1.58 and Pts 199.6 (1995: \$1.57 and Pts 194.9) and the year end rates were \$1.71 and Pts 222.6 (1995: \$1.55 and Pts 188.4).

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 working lives of the employees concerned.

G Channel 5

The Group's share of certain Channel 5 initial 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.

Notes to the Accounts

1 Accounting policies continued

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 10.

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 written off 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, after deducting progress payments. Stocks and work in progress include direct costs incurred in the development of product prior to its publication which are amortised over their estimated economic lives not exceeding four years.

L 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. Deferred taxation relief is accounted for in full on long-term timing differences in respect of provisions for unfunded retirement benefits.

M Capital instruments

Capital instruments are included at cost, adjusted for discount accretion or premium amortisation where the intention is to hold them to maturity. Interest receivable thereon and the premium or discount where relevant is taken to the profit and loss account so as to produce a constant rate of return over the period to the date of expected redemption.

Forward foreign exchange contracts and other off-balance sheet instruments are valued at the market prices prevailing at the balance sheet date. Borrowing is classified according to the maturity date of the respective individual holdings.

N 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.

O Retained profits of overseas subsidiary and associated undertakings

No provision is made for any additional taxation, less double taxation relief, which would arise on the remittance of profits retained.

Notes to the Accounts

2(a) Analysis of sales and operating profit

Business sectors	Sales		Operating profit			
	1996 £m	1995 £m	Before exceptional items	After exceptional items	Before exceptional items	After exceptional items
			1996 £m	1996 £m	1995 £m	1995 £m
Information	691.6	615.8	108.3	99.1	95.0	83.3
Education	554.3	358.9	83.7	68.1	33.9	31.8
Entertainment	803.0	712.4	65.1	(47.5)	116.7	110.9
Investment Banking	—	—	40.8	40.8	39.9	39.9
Corporate expenses less other income	—	—	(12.3)	(14.5)	(6.9)	(28.3)
Continuing operations	2,048.9	1,687.1	285.6	146.0	278.6	237.6
Discontinued operations	137.1	143.3	36.1	35.3	27.7	22.0
	2,186.0	1,830.4	321.7	181.3	306.3	259.6
Geographical markets supplied						
UK	601.4	544.0	90.7	80.7	112.9	89.1
Continental Europe	419.4	351.6	73.4	71.5	72.1	69.9
North America	798.3	591.4	96.6	(30.5)	76.1	63.2
Asia Pacific	185.2	163.0	20.6	20.0	11.3	9.2
Rest of World	44.6	37.1	4.3	4.3	6.2	6.2
Continuing operations	2,048.9	1,687.1	285.6	146.0	278.6	237.6
Discontinued operations	137.1	143.3	36.1	35.3	27.7	22.0
	2,186.0	1,830.4	321.7	181.3	306.3	259.6

Exceptional items comprise restructuring costs for both 1995 and 1996 (see below) and the £100m charge to profits in 1996 arising from improper accounting at Penguin USA. Entertainment profits in 1996 include BSkyB/BSBH income of £2.4m (1995: £32.5m).

Discontinued operations relate to the withdrawal of the Group from the UK regional newspaper business upon its disposal of Westminster Press in December 1996. Prior year figures have been restated to separately identify discontinued operations.

Analyses of the profits of partnerships and associated undertakings are shown in note 11.

Restructuring costs	1996 £m	1995 £m
Post acquisition:		
HarperCollins Educational	15.0	—
Putnam Berkley	4.4	—
Grundy	—	2.0
Mindscape	5.4	—
Shared Services initiative	—	16.7
Financial Times cost cutting measures (including the closure of the Financial Times printing facility at East India Dock in 1995)	5.8	7.9
Cost cutting measures at Westminster Press	0.8	5.7
Other	9.0	14.4
	40.4	46.7

Notes to the Accounts

2(a) Analysis of sales and operating profit continued

The table on page 31 shows sales and operating profit analysed by the destination to which products and services are supplied. The table below analyses sales by the geographic region from which the products and services originate. Inter-regional sales are those made between the Group companies in different regions.

Geographical source of sales	— Total by source —		— Inter-regional —		— Sales —	
	1996 £m	1995 £m	1996 £m	1995 £m	1996 £m	1995 £m
Continuing operations:						
UK	822.7	754.2	(51.2)	(51.6)	771.5	702.6
Continental Europe	330.2	284.6	(9.0)	(11.8)	321.2	272.8
North America	820.8	599.1	(20.0)	(12.6)	800.8	586.5
Asia Pacific	149.0	123.3	(4.4)	(5.6)	144.6	117.7
Rest of World	10.9	7.5	(0.1)	—	10.8	7.5
	2,133.6	1,768.7	(84.7)	(81.6)	2,048.9	1,687.1

2(b) Analysis of capital employed

Business Sectors	— Capital employed —	
	1996 £m	1995 £m
Information	142.7	156.6
Education	354.3	260.9
Entertainment	454.5	470.2
Investment Banking	113.9	122.1
Corporate expenses less other income	(53.3)	(22.1)
Continuing operations	1,012.1	987.7
Discontinued operations	—	65.5
	1,012.1	1,053.2
Location of capital employed		
UK	342.4	299.8
Continental Europe	106.6	105.8
North America	411.4	423.6
Asia Pacific	144.2	150.6
Rest of World	7.5	7.9
Continuing operations	1,012.1	987.7
Discontinued operations	—	65.5
	1,012.1	1,053.2
Reconciliation of capital employed to net assets		
	1996 £m	1995 £m
Capital employed	1,012.1	1,053.2
Less: deferred taxation	(30.3)	(0.6)
other provisions	(159.1)	(133.8)
net debt	(430.4)	(63.4)
Net assets	392.3	855.4

Notes to the Accounts

3 Analysis of consolidated profit and loss account

	Continuing	Discontinued	Total	Continuing	Discontinued	Total
	1996	1996	1996	1995	1995	1995
	£m	£m	£m	£m	£m	£m
Cost of sales	(982.0)	(82.1)	(1,064.1)	(850.4)	(89.3)	(939.7)
Distribution costs	(114.3)	(12.5)	(126.8)	(105.9)	(16.9)	(122.8)
Administration and other expenses	(932.6)	(8.9)	(941.5)	(641.2)	(17.6)	(658.8)
Other operating income (see below)	72.9	1.7	74.6	104.7	2.5	107.2
Net operating expenses	(974.0)	(19.7)	(993.7)	(642.4)	(32.0)	(674.4)
Analysed as:						
Net operating expenses – normal	(834.4)	(18.9)	(853.3)	(601.4)	(26.3)	(627.7)
– exceptional expense	(139.6)	(0.8)	(140.4)	(41.0)	(5.7)	(46.7)
Net operating expenses	(974.0)	(19.7)	(993.7)	(642.4)	(32.0)	(674.4)

The following amounts relating to acquisitions included in the 1996 totals are: cost of sales £88.2m and net operating expenses of £88.7m. The exceptional expense of £140.4m is included in administration and other expenses in 1996 which comprises restructuring costs and the £100m Penguin USA charge for improper accounting (see note 2).

	1996	1995
	£m	£m
Other operating income		
Income from other investments:		
Listed	2.9	2.3
Unlisted	8.5	8.5
BSkyB dividend	–	5.2
BSBH loan stock interest	2.4	27.3
Other operating income (mainly royalties, rights and commission income)	60.8	63.9
	74.6	107.2
Profit before taxation is arrived at after charging:		
Depreciation	63.2	61.5
Operating lease rentals:		
Plant and machinery	16.5	13.8
Properties	32.7	29.3
Auditors' remuneration:		
Audit (Company £0.1m; 1995: £0.1m)	1.6	2.2
Non-audit – UK (Company £nil; 1995: £nil)	0.4	0.9
– Other	0.2	0.7

Notes to the Accounts

4 Profit/(loss) on sale of fixed assets

	1996 £m	1995 £m
Continuing operations:		
Loss on fixed assets at East India Dock	(8.0)	(24.9)
Net (loss)/profit on other investments and property interests	(6.1)	5.6
Sale of direct investment in BSkyB and redemption of BSBH loan stock	–	133.3
Sale of investment in Yorkshire-Tyne Tees Television (YTTV)	–	9.4
	(14.1)	123.4

5 Profit/(loss) on sale of businesses

	1996 £m	1995 £m
Continuing operations:		
Other	(1.9)	6.0
Discontinued operations:		
Sale of Westminster Press (see note 24)	231.3	–

6 Net interest payable

	1996 £m	1995 £m
Interest payable:		
On borrowing repayable wholly within five years not by instalments	(18.4)	(18.0)
On borrowing repayable wholly or partly after five years	(52.2)	(51.3)
Partnerships and associated undertakings	(0.3)	–
Finance lease charges	(0.1)	(0.2)
Interest capitalised	0.2	2.0
	(70.8)	(67.5)
Interest receivable:		
On deposits and liquid funds	38.8	41.1
Amortisation of swap proceeds (see note 18)	2.5	2.5
Net interest payable	(29.5)	(23.9)
Interest cover	x6	x11

1995 interest payable has been restated to reflect the interest on the 9.5% Euro-sterling Bonds 2004 in borrowing repayable wholly or partly after five years rather than wholly within five years.

Interest cover is calculated by dividing net interest payable into operating profit.

A £10.3m premium was paid on the redemption of the £25m (13.625%) 2007 Unsecured Loan Stock.

Notes to the Accounts

7 Taxation

	1996 £m	1995 £m
Taxation on profit on ordinary activities		
United Kingdom:		
Corporation tax at 33%	46.8	217.1
Deferred taxation	(5.5)	(156.1)
BSkyB consortium relief	(8.8)	(8.8)
Double taxation relief	(2.2)	(3.4)
Partnerships and associated undertakings	10.2	10.6
Tax on franked investment income	0.2	1.8
Overseas:		
Overseas tax	25.3	32.6
Deferred taxation	41.2	(3.6)
Partnerships and associated undertakings	1.4	2.6
	108.6	92.8
Tax rate reconciliation	1996 %	1995 %
UK tax rate	33.0	33.0
Effect of BSKyB/BSBH income	(3.5)	(3.8)
Other items	(0.7)	(1.7)
Tax rate reflected in adjusted earnings	28.8	27.5
Effect of profits/(losses) excluded from adjusted earnings	1.6	(2.1)
Tax rate reflected in earnings	30.4	25.4

The 1996 tax rate has been affected by several significant factors:

- The rate reflected in adjusted earnings has been reduced by £8.8m of consortium relief now recognised in the profit and loss account following renegotiation with the other partners in BSBH.
- There is no tax payable on the profit of £231.3m arising on the sale of Westminster Press.
- The Group has tax losses, arising in the US, which have not been utilised or recognised in 1996 but are available to carry forward against taxable profits in future years. Accordingly the Group has decided not to recognise tax relief on the £100m charge for improper accounting at Penguin USA and has also written off to profit deferred tax assets totalling £36.6m.

The 1995 tax rate was reduced by two significant factors:

- Consortium relief of £8.8m was released to offset tax payable on BSBH income.
- The disposal of YTTV resulted in a write back of a deferred tax provision of £4.5m.

8 Dividends

	1996 pence per share	1996 £m	1995 pence per share	1995 £m
Interim paid	6.9	39.4	6.325	35.1
Final proposed	11.1	63.3	10.175	56.7
Dividends per equity share	18.0	102.7	16.5	91.8

Notes to the Accounts

9 Employee information

The details of the emoluments of the directors of Pearson plc are shown on pages 17 to 23 and form part of these audited financial statements.

Staff costs	1996 £m	1995 £m
Wages and salaries	454.1	408.3
Social security costs	47.5	45.1
Post-retirement costs	6.1	8.9
	507.7	462.3

Discontinued operations total staff costs were £38.7m (1995: £50.7m).

Average number employed 1996	UK	USA	Other	Total
Information	3,078	903	1,786	5,767
Education	823	2,352	1,348	4,523
Entertainment	4,272	1,607	1,080	6,959
Other	114	19	1	134
Continuing operations	8,287	4,881	4,215	17,383

Average number employed 1995	UK	USA	Other	Total
Information	3,072	592	1,669	5,333
Education	787	1,651	1,247	3,685
Entertainment	4,179	1,738	960	6,877
Other	91	19	3	113
Continuing operations	8,129	4,000	3,879	16,008

Discontinued operations employed on average 2,564 (1995: 3,414) in the UK (Information sector).

Post-retirement costs	1996 £m	1995 £m
Defined benefit pension schemes:		
UK Group plan:		
Regular pension cost	12.6	13.1
Amortisation of surplus	(17.1)	(13.1)
Net pension credit	(4.5)	–
Other defined benefit pension schemes	5.0	3.9
Defined contribution pension schemes	4.4	3.8
Medical benefits	1.2	1.2
	6.1	8.9

Notes to the Accounts

9 Employee information continued

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's finances. 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 non-UK defined contribution schemes.

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 below. The principal assumptions used are also shown in the table below. The net assets of the UK Group plan at 31 December 1996 are included in the pension plan accounts at £848m (unaudited).

	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 £4.5m (1995: £nil).

The total market value of the assets of the non UK defined benefit schemes (mainly in the United States), valued this year, was £40.3m (1995: £38.0m).

Other post-retirement benefits

The principal assumptions affecting the provision for other post retirement benefits were: medical inflation rates of between 5.5% and 10.0% and a discount rate of 7.25%.

Notes to the Accounts

10 Tangible fixed assets

	Freehold and leasehold property £m	Plant and equipment £m	Assets in course of construction £m	Total £m
Cost or as valued				
At 31 December 1995	324.5	487.3	29.9	841.7
Exchange differences	(10.3)	(16.9)	(1.4)	(28.6)
Reclassifications	9.0	10.9	(19.9)	—
Permanent diminution in value	(4.4)	(5.0)	—	(9.4)
Owned by subsidiary undertakings acquired	14.7	9.7	—	24.4
Capital expenditure	14.0	65.7	10.4	90.1
Capitalised interest	0.2	—	—	0.2
Disposals	(5.2)	(22.5)	—	(27.7)
Owned by subsidiary undertakings disposed	(30.2)	(70.2)	(0.9)	(101.3)
At 31 December 1996	312.3	459.0	18.1	789.4
Depreciation				
At 31 December 1995	60.1	251.5	—	311.6
Exchange differences	(2.4)	(9.8)	—	(12.2)
Permanent diminution in value	(0.2)	—	—	(0.2)
Provided in the year	10.0	53.2	—	63.2
Subsidiary undertakings acquired	2.4	4.0	—	6.4
Disposals	(0.5)	(15.7)	—	(16.2)
Owned by subsidiary undertakings disposed	(6.0)	(41.2)	—	(47.2)
At 31 December 1996	63.4	242.0	—	305.4
Net book value				
At 31 December 1995	264.4	235.8	29.9	530.1
At 31 December 1996	248.9	217.0	18.1	484.0

Freehold and leasehold property

Net book value includes: short leases of £23.1m (1995: £17.8m) and long leases of £4.8m (1995: £17.4m). On an original cost basis, cost would have been included at £319.4m, and accumulated depreciation at £54.1m. The net book value included at valuation is £8.0m.

Permanent diminution in value

Freehold and leasehold property and plant and equipment include £8.4m and £5.0m respectively of assets held for sale. Of the charge for permanent diminution in value, £8.0m (1995: £36.6m and £11.7m in depreciation) in cost relates to the loss on assets at East India Dock. At 31 December 1996 the provision for permanent diminution in value amounted to £66.0m in cost and £11.9m in depreciation.

Depreciation

Except for £70.7m of land, 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.

Capital commitments

The Group had capital commitments for fixed assets, including finance leases, amounting to £126.7m at 31 December 1996. This represented £22.0m already under contract and £104.7m authorised but not yet contracted.

Other notes

The net book value of Group tangible fixed assets includes £1.8m in respect of assets held under finance leases. Depreciation on these assets charged in 1995 was £1.0m. The net book value of Group tangible fixed assets includes £4.2m in respect of capitalised interest.

Notes to the Accounts

11 Partnerships and associated undertakings

	Valuations		Book values	
	1996 £m	1995 £m	1996 £m	1995 £m
Analysis				
Partnership interests	200.0	200.0	113.9	122.1
Unlisted associated undertakings	122.6	104.7	3.9	(4.1)
Loans	64.8	49.3	64.8	49.3
	387.4	354.0	182.6	167.3

Principal associated undertakings are listed on page 57. The valuations of unlisted partnerships and associated undertakings are at directors' valuations as at 31 December 1996. If realised at these values there would be an estimated liability for taxation, at year end rates, of £42.9m. The Group had no capital commitments to subscribe for further capital and loan stock.

	Equity £m	Share of loans £m	Reserves £m	Total £m
Summary of movements				
At 31 December 1995	97.9	49.3	20.1	167.3
Exchange differences	(7.8)	(2.2)	(8.9)	(18.9)
Additions	11.8	24.2	—	36.0
Goodwill written off	(0.6)	—	—	(0.6)
Transfer from fixed asset investments	—	(6.5)	5.0	(1.5)
Retained profit for the year	—	—	0.5	0.5
Provision for losses and diminution in value	(0.2)	—	—	(0.2)
At 31 December 1996	101.1	64.8	16.7	182.6

	Profit		Net assets	
	1996 £m	1995 £m	1996 £m	1995 £m
Analysis of partnerships and associated undertakings				
Business sectors				
Information	10.9	10.9	(7.1)	(13.8)
Education	3.0	4.2	5.1	6.4
Entertainment	(1.6)	(11.7)	70.7	52.6
Investment Banking	40.8	39.9	113.9	122.1
	53.1	43.3	182.6	167.3

Geographical markets supplied and location of net assets

UK	20.6	18.6	103.9	85.1
Continental Europe	12.9	7.1	38.1	35.7
North America	17.2	14.0	36.7	42.0
Rest of World	2.4	3.6	3.9	4.5
	53.1	43.3	182.6	167.3

Reconciliation to retained profit

	1996 £m
Net income from partnerships and associated undertakings	53.1
UK taxation	(10.2)
Overseas taxation	(1.4)
Distributions receivable in respect of the year from partnership interests	(34.2)
Dividends (including tax credits) from unlisted associated undertakings	(6.8)
Retained profit for the year	0.5

Notes to the Accounts

11 Partnerships and associated undertakings continued

Interests in Lazard Partners Limited Partnership and the three Lazard Houses

	Net assets	
	1996	1995 restated*
	£m	£m
A summary of the aggregate net tangible assets at 31 December is as follows:		
Total assets	8,013	5,573
Total liabilities	(7,632)	(5,179)
Net tangible assets	381	394
Attributable to Pearson	114	122

During 1995 Lazard Frères & Co. became a New York Limited Liability Company and Pearson's indirect general partnership interest with unlimited liability interest is now restricted to Lazard Frères et Cie and Maison Lazard et Cie held directly and indirectly through Lazard Partners Limited Partnership. 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 £831m (1995: £863m). Pearson also holds direct interests in Lazard Frères & Co.

Interests in the Lazard Houses	Country of incorporation of registration	Beneficial interest %	Class of share	Share capital million
Lazard Partners Limited Partnership (which, with direct interests in the US and French partnerships gives the following interests in the Lazard Houses):	USA	50		Partnership
Lazard Brothers & Co., Ltd	England	37.2	Ord £1	25.3
		80	Def £1	5.0
		50	Sw Fr 1	0.4
Lazard Frères & Co., 'LLC'	USA	11.6		Limited Liability Company
Lazard Frères et Cie } Maison Lazard et Cie }	France	9.6		Partnership

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 inter-house 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, in 1996 the members, directors or partners in a particular Lazard House received a greater 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 income (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 Pools profit share and the Pearson adjustment) is divided in accordance with the respective capital interests of the original partners (Pearson plc ~ 50%).

*Following the introduction of the open gilt repo market on 2 January 1996, there has been a shift in Lazard Brothers & Co. Ltd money markets business from gilt stock borrowing to gilt repo contracts which has led to an increase in the balance sheet footings and a restatement of the 1995 comparatives on the balance sheet to show the cash loan elements of stock loans gross, when previously they were shown net.

Interest in The Economist Newspaper Ltd

The net liabilities of The Economist Newspaper Ltd as at 31 March 1996 were £33.3m (1995: net assets £26.5m); profit before taxation amounted to £24.0m (1995: £19.8m).

Notes to the Accounts

12 Other fixed asset investments

	Valuations		Book values	
	1996 £m	1995 £m	1996 £m	1995 £m
Listed abroad	111.8	112.2	100.2	110.6
Unlisted	355.0	266.8	141.8	117.6
	466.8	379.0	242.0	228.2

Subsequent to the year end, Pearson's 10% equity share investment in Television Broadcasts Limited (TVB) was sold for £111.1m (see note 31). If all investments were realised at valuation there would be no liability for taxation. Details of the principal investments in which the Group held more than 10% of the equity share capital are shown on page 57.

Summary of movements	BSBH £m	TVB £m	Other £m	Total £m
At 31 December 1995	67.2	109.2	51.8	228.2
Exchange differences	—	(10.2)	(3.0)	(13.2)
Additions	26.5	—	6.0	32.5
Owned by subsidiary undertakings acquired	—	—	30.2	30.2
Transfer to partnerships and associated undertakings	—	—	1.5	1.5
Provisions for permanent diminution in value and losses	—	—	(6.4)	(6.4)
Disposals and redemptions	—	—	(30.8)	(30.8)
Book value at 31 December 1996	93.7	99.0	49.3	242.0
Valuation at 31 December 1996	280.0	111.1	75.7	466.8

13 Stocks

	1996 £m	1995 £m
Raw materials	22.3	29.4
Work in progress	79.6	72.6
Finished stock	258.8	187.9
	360.7	289.9

The replacement cost of stocks and work in progress is not materially different from book value.

14 Debtors

	1996 £m	1995 £m
Amounts falling due within one year		
Trade debtors	382.3	408.7
Partnerships and associated undertakings	14.1	8.3
Other debtors	179.8	158.2
Prepayments and accrued income	53.5	61.2
	629.7	636.4
Amounts falling due after one year		
Other debtors	23.8	21.1
Prepayments and accrued income	0.4	0.3
ACT recoverable	15.9	14.2
	40.1	35.6
	669.8	672.0

The Pearson Employee Share Trust holds 149,933 (1995: 293,800) Pearson plc ordinary shares with a market value of £1.1m (1995: £1.8m) inclusive of accumulated scrip dividend shares. Amounts included within other debtors for own shares are £0.6m (1995: £0.4m).

Notes to the Accounts

15 Current asset investments

	Valuations		Book values	
	1996 £m	1995 £m	1996 £m	1995 £m
Listed abroad	–	16.1	–	–
Unlisted	7.9	9.8	7.9	8.3
	7.9	25.9	7.9	8.3

Listed investment valuations are at middle market quotation and unlisted investments are at directors' valuations. If all investments were realised at valuation there would be no liability for taxation.

Details of the principal investments in which the Group held more than 10% of the equity share capital are shown on page 57.

Summary of movements	£m
At 31 December 1995	8.3
Exchange differences	(0.7)
Additions	1.0
Disposals	(0.7)
At 31 December 1996	7.9

16 Cash and liquid funds

	Group		Company	
	1996 £m	1995 £m	1996 £m	1995 £m
Cash, bank current accounts and overnight deposits	138.8	155.5	24.5	54.3
Certificates of deposit and commercial paper	6.0	63.9	–	50.4
Money market fund units	–	8.4	–	8.4
UK government securities	1.0	22.6	–	21.6
Listed sterling asset backed floating rate notes	45.9	156.5	15.3	105.2
Listed US dollar asset backed floating rate notes	42.1	139.7	42.1	139.8
Other listed securities	–	60.1	–	50.1
Term bank deposits	51.2	49.7	1.4	40.4
Other	14.0	15.6	14.0	15.5
	299.0	672.0	97.3	485.7
Listed securities, dealt on recognised Stock Exchanges, included above:				
Cost	89.0	378.9	57.4	316.7
Market value	89.0	378.8	57.4	316.6

Notes to the Accounts

17 Borrowings

	Group		Company	
	1996	1995	1996	1995
	£m	£m	£m	£m
Borrowing summary (by maturity)				
Short term				
Loans or instalments due within one year	8.5	12.1	3.0	7.3
Bank loans, overdrafts and commercial paper	165.7	248.9	167.3	282.0
Total due within one year	174.2	261.0	170.3	289.3
Medium and long term				
Loans or instalments thereof repayable:				
From one to two years	7.8	0.1	—	—
From two to five years	6.3	24.5	4.8	14.4
After five years not by instalments	541.1	449.8	184.3	224.8
Total due after more than one year	555.2	474.4	189.1	239.2
Total borrowing	729.4	735.4	359.4	528.5

In the absence of enforceable contracts from the relevant lenders to refinance current advances as they fall due, at the balance sheet date £84.3 of debt currently classified from two to five years and after five years would be repayable within one year.

	Group	
	1996	1995
	£m	£m
Borrowing summary (by currency)		
US dollars	379.3	340.5
Sterling	210.2	239.1
Hong Kong dollars	56.1	61.3
Spanish pesetas	33.7	36.2
French francs	19.1	24.0
Canadian dollars	16.5	19.2
Other currencies	14.5	15.1
	729.4	735.4

	Group		Company	
	1996	1995	1996	1995
	£m	£m	£m	£m
Borrowing summary (by instrument)				
Secured				
Bank loans and overdrafts	0.1	0.1	—	—
Unsecured				
10.5% Euro-sterling Bonds 2008	100.0	100.0	100.0	100.0
13.625% fixed rate loan stock 2007 (see note 6)	—	25.0	—	25.0
9.5% Euro-sterling Bonds 2004	113.2	124.9	—	—
10.75% Euro-sterling Bonds 2002	100.0	100.0	—	—
Other unsecured borrowings	8.5	12.8	3.0	7.8
Unsecured bank loans and overdrafts, commercial paper and medium term notes	407.6	372.6	256.4	395.7
Total borrowing	729.4	735.4	359.4	528.5

Notes to the Accounts

17 Borrowings continued

Forward foreign exchange contracts

Foreign currency transactional cash flows are hedged using forward foreign exchange contracts. At 31 December 1996, the UK Group had contracted to exchange the equivalent of £22m and the estimated mark-to-market loss on these contracts at 31 December 1996 was £0.8m. In addition, the UK Group enters into foreign exchange swaps in order to hedge surplus cash invested in US dollars back into sterling. At 31 December 1996, £50m of these contracts were held with a mark-to-market gain of £1.2m.

Interest rate hedging transactions	Notional principal £m	Weighted average rate %	Mark-to market value £m
Swaps in force at 31 December 1996			
US dollars: converting fixed debt to floating	146	7.23	6
US dollars: converting floating debt to fixed	156	5.77	2
Sterling: converting fixed debt to floating	150	7.86	4
Converting fixed sterling debt to floating US dollars	113	10.41	11
			23

Of the total mark-to-market gain on the above transactions of £23m, £17m arises from transactions that hedge debt issues for their entire lives. There is a mark-to-market loss on those issues of £32m included in the footnote below.

The following shows the amount of these contracts which are in force at the end of each year.

	1996 £m	1997 £m	1998 £m	1999 £m
US dollars: converting fixed debt to floating	146	146	146	146
US dollars: converting floating debt to fixed	156	135	117	117
Sterling: converting fixed debt to floating	150	100	100	100
Converting fixed sterling debt to floating US dollars	113	113	113	113

During the year, a cap setting a maximum cost of 9% on \$50m of variable US dollar borrowings for the period 1998 to 2001 was terminated.

As a result of the above transactions, the interest rate exposure of the borrowings of the Group at 31 December 1996 was as follows:

	Total gross borrowing £m	Fixed rate £m	Floating rate £m
Sterling	210	50	160
US dollars	379	164	215
Other currencies	140	–	140
	729	214	515

Of this total, £541m relates to long-term borrowings with a maturity of over five years. The current value of this debt at 31 December 1996, considering only the movements in risk-free interest rates, is £573m. The difference between the current and book values of these borrowings is partially offset by the mark-to-market gain on the related swaps detailed above.

Notes to the Accounts

18 Other creditors

	1996 £m	1995 £m
Amounts falling due within one year		
Trade creditors	288.2	222.6
Taxation	232.3	245.6
Social security and other taxes	26.7	27.5
Other creditors	72.4	89.5
Accruals and deferred income	230.5	177.2
Obligations under finance leases	0.8	1.5
Payments received on account	5.1	3.6
Dividends	63.8	59.2
	919.8	826.7
Amounts falling due after one year		
Obligations under finance leases	0.6	1.1
Other creditors	3.2	1.0
Accruals and deferred income	11.3	13.8
	15.1	15.9

Accruals and deferred income includes £12.6m (1995: £15.1m) 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. £10.2m is due after one year, within which the amount falling due after five years is £0.2m.

19 Deferred taxation

Summary of movements		£m
At 31 December 1995		0.6
Exchange differences		2.7
Subsidiary undertakings acquired/disposed		(6.8)
Net charge for the year		35.7
Transfer to current taxation		(1.9)
At 31 December 1996		30.3
Deferred taxation derives from	1996 £m	1995 £m
Capital allowances	21.6	27.6
Revalued assets	1.1	1.1
Other timing differences	7.6	(28.1)
	30.3	0.6
Deferred taxation not provided		
Relating to revalued assets and timing differences	7.2	13.0
Relating to gains subject to rollover relief	18.9	20.1
	26.1	33.1

Notes to the Accounts

20 Other provisions for liabilities and charges

	Post-retirement £m	Other £m	Total £m
At 31 December 1995	32.8	101.0	133.8
Exchange differences	(3.5)	(10.5)	(14.0)
Subsidiary undertakings acquired/disposed	6.7	24.9	31.6
Deferred consideration arising on acquisitions	–	12.9	12.9
Transfers	(0.2)	(4.0)	(4.2)
Released	(5.8)	(4.3)	(10.1)
Provided	11.9	45.4	57.3
Utilised	(6.8)	(41.4)	(48.2)
At 31 December 1996	35.1	124.0	159.1

Post-retirement provisions are in respect of pensions, £21.9m and post-retirement medical benefits, £13.2m. Other provisions are mainly in respect of future costs relating to the purchase of subsidiary and associated undertakings £57.4m, litigation £3.5m, reorganisations and redundancies £37.5m, disposals and closures £1.6m, and lease commitments £12.5m. Amounts utilised include £9.3m, and amounts released £2.1m, in respect of provisions relating to subsidiary undertakings acquired.

21 Share capital of Pearson plc

Authorised	Number (000's)	£m
Ordinary shares of 25p each	816,000	204.0
	816,000	204.0
Called up and allotted		
Ordinary shares of 25p each fully paid 31 December 1995	556,164	139.1
Issued on acquisition of Recoletos	11,314	2.8
Issued under share option and employee share schemes	2,655	0.7
Issued under scrip dividend scheme	868	0.2
At 31 December 1996	571,001	142.8

Ordinary shares issued on the acquisition of the increased shareholding in Recoletos were issued for aggregate consideration of £70.4m based on a share price of 622.6p per share.

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 FRS 4. The consideration received in respect of shares issued during the year was £84.5m (1995: £11.8m).

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 97,839 under the 'Save As You Earn' scheme and 51,603 under the Executive schemes.

Notes to the Accounts

21 Share capital of Pearson plc continued

Options outstanding at 31 December 1996	When granted	Number of shares ('000's)	Original subscription price (pence)	Exercise period
'Save As You Earn' share option schemes	1989	129	301	1994-1997
	1990	453	265	1995-1998
	1991	640	299	1996-1999
	1992	2,103	242	1997-2000
	1994	833	509	1999-2002
	1995	1,043	436	2000-2003
	1996	883	578	2001-2004
Executive share option schemes	1988	66	342	1991-1998
	1989	405	341-376	1992-1999
	1990	1,045	307-334	1993-2000
	1991	245	364-377	1994-2001
	1992	684	327-379	1995-2002
	1993	150	396-410	1996-2003
	1994	1,779	629-635	1997-2004
	1995	1,683	545-606	1998-2005
	1996	1,769	654-682	1999-2006
		13,910		

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

22 Reserves

Summary of movements	Share premium account £m	Revaluation reserve £m	Other reserves £m	Profit and loss account £m	Total £m
At 31 December 1995	48.7	6.9	1.4	637.1	694.1
Exchange differences	-	(0.3)	(0.2)	(35.4)	(35.9)
Premium on issue of 3.5m equity shares	13.2	-	-	-	13.2
Premium arising on equity shares issued on Recoletos acquisition	67.6	-	-	-	67.6
Goodwill arising (see note 23)	-	-	-	(632.4)	(632.4)
Goodwill written back (see note 24)	-	-	-	1.4	1.4
Realisation of revaluation reserve	-	(1.2)	-	1.2	-
Profit retained for the year	-	-	-	137.8	137.8
At 31 December 1996	129.5	5.4	1.2	109.7	245.8
Analysed as:					
Partnerships and associated undertakings	-	0.2	1.2	15.3	16.7
Group excluding partnerships and associated undertakings	129.5	5.2	-	94.4	229.1

The cumulative net goodwill written off is £1,896.4m.

Notes to the Accounts

23 Acquisitions

On 1 April 1996 the Group acquired HarperCollins Educational and, on 1 December 1996, Putnam Berkley. During the year the Group increased its shareholding in Recoletos from 56.7% at 31 December 1995 to 94.2%. All acquisitions have been consolidated applying acquisition accounting principles.

Acquisition analysis of subsidiary undertakings and businesses	Harper Collins Educational £m	Putnam Berkley £m	Recoletos £m	Other £m	1996 Total £m	1995 Total £m
Tangible fixed assets	6.0	9.9	–	2.1	18.0	4.3
Investments	–	–	–	30.2	30.2	–
Associated undertakings	–	–	–	–	–	2.8
Stocks	86.4	21.8	–	3.3	111.5	5.1
Debtors	12.4	67.8	–	11.1	91.3	45.9
Creditors	(29.4)	(60.4)	–	(16.4)	(106.2)	(43.9)
Provisions	(27.3)	(3.3)	–	(2.0)	(32.6)	(1.0)
Deferred taxation	–	–	–	0.3	0.3	9.2
Equity minority interests	–	–	19.6	0.7	20.3	(0.9)
Net cash/(borrowing) acquired	–	(0.2)	–	4.7	4.5	8.6
Net assets acquired at fair value	48.1	35.6	19.6	34.0	137.3	30.1
Fair value of consideration:						
Cash	(369.2)	(200.9)	(31.0)	(84.6)	(685.7)	(348.6)
Shares issued	–	–	(70.4)	–	(70.4)	–
Deferred cash consideration	–	0.7	(7.9)	(5.7)	(12.9)	(28.2)
Costs accrued	–	(0.8)	–	(0.4)	(1.2)	–
Net prior year adjustments	–	–	–	1.1	1.1	(1.4)
Total consideration	(369.2)	(201.0)	(109.3)	(89.6)	(769.1)	(378.2)
Goodwill arising	321.1	165.4	89.7	55.6	631.8	348.1

Shares issued consisted of 11,313,908 ordinary shares (see note 21).

Acquisition goodwill and fair values	Harper Collins Educational £m	Putnam Berkley £m	Recoletos £m	Other £m	Total £m
Acquisition cost	369.2	201.0	109.3	89.6	769.1
Book value of net tangible assets acquired	253.7	65.7	19.6	12.5	351.5
Fair value adjustments	(205.6)	(30.1)	–	21.5	(214.2)
Fair value to the Group	48.1	35.6	19.6	34.0	137.3
Goodwill arising written off to reserves	321.1	165.4	89.7	55.6	631.8

Other fair value adjustments comprise the revaluation of the investment in Meridian following the acquisition of SelecTV of £22.7m and other sundry adjustments of £(1.2)m.

Notes to the Accounts

23 Acquisitions continued

	Note	Book value £m	Accounting policy alignment £m	Revaluations and other adjustments £m	Fair value £m
HarperCollins Educational					
Tangible fixed assets		5.5	–	0.5	6.0
Stocks	a	240.9	(124.7)	(29.8)	86.4
Debtors	b	38.4	(18.9)	(7.1)	12.4
Creditors	c	(25.4)	–	(4.0)	(29.4)
Provisions	d	(5.7)	–	(21.6)	(27.3)
Net assets acquired		253.7	(143.6)	(62.0)	48.1

Provisional fair value adjustments:

Accounting policy alignment

- a) Pre-publication expenditure for still to be published and published books has been reduced by £124.7m to comply with the Pearson accounting policy which capitalises fewer internal costs and also amortises this expenditure over a shorter time period.
- b) The reserve for returns has been increased by £3.9m, and £15.0m of capitalised promotion and complimentary product cost has been written off in line with Pearson accounting policy.

Revaluations and other adjustments

- a) Inventory has been written down by £15.0m to net realisable value. A further adjustment of £14.8m has been made to write pre-publication expenditure down to net realisable value.
- b) The reserve against debtors has been increased by £0.8m to reflect potential bad debts; the reserve for royalty advances has been increased by £3.6m to reflect net realisable value; capitalised software costs amounting to £2.7m have been written down to their net realisable value.
- c) Additional accruals have been made for sundry liabilities identified at the time of purchase.
- d) A provision has been recognised for onerous property related liabilities.

	Note	Book value £m	Accounting policy alignment £m	Revaluations and other adjustments £m	Fair value £m
Putnam Berkley					
Tangible fixed assets		10.1	–	(0.2)	9.9
Stocks		21.8	–	–	21.8
Debtors	a	81.6	(5.4)	(8.4)	67.8
Creditors	b	(47.6)	–	(12.8)	(60.4)
Provisions	c	–	–	(3.3)	(3.3)
Net cash acquired		(0.2)	–	–	(0.2)
Net assets acquired		65.7	(5.4)	(24.7)	35.6

Provisional fair value adjustments:

Accounting policy alignment

- a) To establish a backlist reserve for returns in line with existing Pearson accounting policy.

Revaluations and other adjustments

- a) A provision of £7.1m has been made against irrecoverable royalty advances and the reserve against debtors has been increased by £1.3m to reflect potential bad debts.
- b) A provision of £9.3m has been established against irrecoverable royalty advances, committed prior to purchase, and £3.5m has been provided for sundry liabilities identified at the time of purchase.
- c) A provision has been recognised for onerous property related liabilities.

Notes to the Accounts

23 Acquisitions continued

	1 July 1995 to 31 March 1996 £m	Year to 30 June 1995 £m
HarperCollins Educational financial information		
Profit and loss		
Sales	107.7	204.1
Gross profit	52.4	104.0
Operating profit	–	32.9

The above results are shown using the accounting policies of HarperCollins Educational prior to acquisition. Profit before taxation and taxation numbers are not available, as the taxation of HarperCollins Educational was accounted for as part of a larger group. Accordingly no statement of total recognised gains and losses is presented. Operating profit for the period 1 July 1995 to 31 March 1996 is not available.

The profit after tax of Putnam Berkley from 1 July 1996, the beginning of its financial year, to 1 December 1996, the effective date of acquisition was £8.2m (1996 financial year £12.8m). These results are based on the accounting policies of Putnam Berkley prior to acquisition.

	Cost £m	Net assets acquired £m	Goodwill £m
Total goodwill arising on acquisitions			
Subsidiary undertakings and businesses (see page 48)	769.1	137.3	631.8
Associated undertakings	36.0	35.4	0.6
	805.1	172.7	632.4
Cash flow from acquisitions			
		1996 £m	1995 £m
Cash – current year acquisitions (see page 48)		685.7	348.6
Deferred payments for prior year acquisitions and other items		12.2	11.2
Net cash outflow		697.9	359.8

Contributions to the cash flow from acquisitions in 1996 are as follows: net cash inflow from operating activities £18.7m, returns on investments and servicing of finance £(20.5)m, taxation £nil; and investing activities £30.1m.

Notes to the Accounts

24 Disposals

	Westminster Press £m	Other £m	1996 Total £m	1995 £m
Disposals of subsidiary undertakings and businesses				
Tangible fixed assets	(53.7)	(0.4)	(54.1)	(0.7)
Goodwill written back	–	(1.4)	(1.4)	–
Stocks	(1.9)	–	(1.9)	(6.4)
Debtors	(24.5)	(0.4)	(24.9)	(4.2)
Creditors and taxation	6.9	0.5	7.4	3.6
Provisions	1.0	–	1.0	(0.2)
Deferred tax	6.5	–	6.5	–
Net cash	(5.0)	(0.5)	(5.5)	(1.1)
Net assets	(70.7)	(2.2)	(72.9)	(9.0)
Proceeds	305.0	0.8	305.8	15.0
Costs paid	(3.0)	(0.5)	(3.5)	–
Profit/(loss) on sale	231.3	(1.9)	229.4	6.0
Cash flow:				
Cash – current year disposals			302.3	3.9
Deferred receipts from prior year disposals			4.9	–
			307.2	3.9

Contributions to the cash flow from disposals in 1996 are as follows:

Net cash inflow from operating activities £38.4m, returns on investments and servicing of finance £(0.8)m, taxation £(14.1)m and capital expenditure and financial investment £7.5m.

25 Notes to consolidated statement of cash flows

a) Reconciliation of operating profit to net cash inflow from operating activities	Continuing 1996 £m	Discontinued 1996 £m	Total 1996 £m	Continuing 1995 £m	Discontinued 1995 £m	Total 1995 £m
Operating profit	146.0	35.3	181.3	237.6	22.0	259.6
Depreciation charges	56.8	6.4	63.2	54.7	6.8	61.5
Share of profit of partnerships and associated undertakings	(53.1)	–	(53.1)	(43.3)	–	(43.3)
Dividends from partnerships and associated undertakings	33.5	–	33.5	30.7	–	30.7
Decrease/(increase) in stocks	4.6	1.9	6.5	(34.6)	(1.9)	(36.5)
Decrease/(increase) in debtors	21.8	(1.0)	20.8	(80.3)	(0.2)	(80.5)
Increase/(decrease) in creditors	59.9	1.0	60.9	20.2	(2.0)	18.2
(Decrease)/increase in operating provisions	1.6	(3.5)	(1.9)	29.2	(0.2)	29.0
Exchange adjustments	(7.7)	–	(7.7)	2.8	–	2.8
Other	(10.6)	(1.7)	(12.3)	(5.1)	–	(5.1)
Net cash inflow from operating activities*	252.8	38.4	291.2	211.9	24.5	236.4
Purchase of fixed assets and finance leases	(85.9)	(5.0)	(90.9)	(97.6)	(4.3)	(101.9)
Sale of operating tangible fixed assets	6.5	0.4	6.9	31.6	0.5	32.1
Other	10.0	1.8	11.8	(20.1)	–	(20.1)
Operating cash flow	183.4	35.6	219.0	125.8	20.7	146.5

*Cash inflow for 1996 includes a £20.9m outflow relating to exceptional items charged in 1996 and a £12.5m outflow relating to exceptional items charged in prior years.

Notes to the Accounts

25 Notes to consolidated statement of cash flows continued

	Cash at bank and in hand £m	Overdrafts £m	Sub total £m	Current asset investments £m	Debt due within one year £m	Debt due after one year £m	Total £m
b) Analysis of net debt							
At 31 December 1995	155.5	(50.7)	104.8	516.5	(210.3)	(474.4)	(63.4)
Exchange differences	(8.2)	6.8	(1.4)	(4.9)	19.6	23.2	36.5
Net cash flow	(8.5)	(24.7)	(33.2)	(351.4)	85.1	(104.0)	(403.5)
At 31 December 1996	138.8	(68.6)	70.2	160.2	(105.6)	(555.2)	(430.4)
At 31 December 1994	75.8	(85.3)	(9.5)	290.8	(70.5)	(357.2)	(146.4)
Exchange differences	(0.3)	(3.0)	(3.3)	—	(0.3)	(0.1)	(3.7)
Net cash flow	80.0	37.6	117.6	225.0	(139.5)	(117.1)	86.0
Deferred cash flow	—	—	—	0.7	—	—	0.7
At 31 December 1995	155.5	(50.7)	104.8	516.5	(210.3)	(474.4)	(63.4)
c) Reconciliation of net cash flow to movement in net debt						1996	1995
						£m	£m
(Increase)/decrease in net debt from cash flows						(33.2)	117.6
(Increase)/decrease in net debt from management of liquid resources						(351.4)	225.7*
(Increase)/decrease in net debt from other borrowings						(18.9)	(256.6)
Exchange differences						36.5	(3.7)
Movement in net debt in the year						(367.0)	83.0
Net debt at 1 January						(63.4)	(146.4)
Net debt at 31 December						(430.4)	(63.4)

*Net cash flow of £225.0m and deferred cash flow of £0.7m.

d) Tax paid

Tax paid includes £30.1m (1995: £2.5m of credits) relating to items excluded from operating profit.

26 Commitments under leases

At 31 December 1996, the Group had commitments under leases, other than finance leases, to make payments in 1997 as follows:

	Land and buildings £m	Other £m
For leases expiring:		
In 1997	5.2	0.6
Between 1998 and 2001	9.1	8.3
Thereafter	19.7	6.8
	34.0	15.7

27 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 subsidiary and associated undertakings. In addition there are contingent liabilities of the Group in respect of legal claims and general partnership interests (see note 11). None of these claims is expected to result in a material gain or loss to the Group.

Notes to the Accounts

28 Related parties

Partnerships and associated undertakings

Loans and equity advanced to associated undertakings during the year and at the balance sheet date are shown in note 11. Amounts falling due from partnerships and associated undertakings are set out in note 14. Dividends received from partnerships and associated undertakings are set out in note 11. Details of individually significant transactions are shown below.

Troll Communications Inc

The Group has a 44% interest in the equity of Troll Communications Inc. During the year £2.5m in interest income was received on the subordinated debt and £1.4m dividend income was received on the preferred stock. As at 31 December 1996 £3.6m (1995: £1.4m) in interest was outstanding and £2.1m (1995: £0.8m) in dividend was outstanding.

Port Aventura SA

The Group has a 40% interest in the equity of Port Aventura SA. During the year £5.2m equity was provided. Management fees of £2.5m were earned during the year of which £1.0m (1995: £1.2m) 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 £4.6m equity was provided and £19.2m loans advanced.

It is intended that the Group will provide programming to Channel 5 Broadcasting Ltd, a wholly owned subsidiary of Channel 5 Television Group Ltd, and undertake transmission for Channel 5 Engineering Services Ltd, a subsidiary of Channel 5 Television Group Ltd. In 1996 the Group contracted to provide programming to the value of £24.0m for transmission in 1997 and beyond.

European Channel Management Ltd

The Group has a 45% interest in the redeemable unsecured loan stock of European Channel Management Ltd. During the year £4.1m loans were advanced. In addition the Group paid £3.1m during the year for £10.3m of start up tax losses.

UK Gold/UK Living

The Group has 20% and 25% economic interests respectively in the equity of UK Gold and UK Living. During the year the Group provided programmes and services to the value of £5.4m and £9.4m respectively to UK Gold and UK Living of which £1.4m and £0.4m were outstanding at the year end (see note 31).

Grundy associated undertakings

During the year the Group received £4.4m for management fees, format rights and royalties from a number of associated undertakings of Grundy Worldwide Ltd, of which £0.4m was outstanding at the year end. No individual transactions were material to the Group.

Lazard Partnership

Details of the ownership structure and profit sharing arrangements are set out in note 11.

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 1996 totalled £4.4m.

Recoletos

Transactions with directors and officers of the company are set out on page 15 of the Directors' Report.

In September 1996, Pearson purchased approximately 30% of the issued share capital of Recoletos Compañía Editorial SA (Recoletos) from five Recoletos directors (Juan Kindelan Jaquotot, Alejandro Kindelan Jaquotot, Jose Maria Garcia-Hoz Rosales, Luis Infante Brave and Jaime Castellanos Borreo). The consideration totalled £17.6m in cash and 11.3 million new Pearson ordinary shares. An agreement exists between the five Recoletos directors and Union Bank of Switzerland (UBS) whereby UBS will compensate the directors as shareholders if, by 5 October 1999, the Pearson share price is lower than 95% of the share price on 16 January 1997 (the date the transaction was entered into). Similarly the directors as shareholders will compensate UBS if the share price is greater than 111% of the share price on the date of the transaction. This can be settled in cash or Pearson shares.

Notes to the Accounts

29 Company balance sheet as at 31 December 1996

	Notes	1996 £m	1995 £m
Fixed assets			
Tangible assets		—	0.4
Investments:			
Subsidiary undertakings		1,798.4	1,742.9
		1,798.4	1,743.3
Current assets			
Debtors:			
Advance corporation tax recoverable		15.9	14.2
Subsidiary undertakings – due within one year		696.9	627.8
– due after one year		521.6	557.7
Other debtors		6.8	6.6
Prepayments and accrued income		5.6	10.7
Investments		0.7	0.7
Cash and liquid funds	16	97.3	485.7
		1,344.8	1,703.4
Creditors – amounts falling due within one year:			
Short term borrowing	17	(170.3)	(289.3)
Subsidiary undertakings		(958.7)	(1,394.8)
Taxation		(23.1)	(19.6)
Other creditors		(0.2)	(2.6)
Accruals and deferred income		(11.0)	(13.8)
Dividends		(63.3)	(56.7)
		(1,226.6)	(1,776.8)
Net current assets/(liabilities)		118.2	(73.4)
Total assets less current liabilities		1,916.6	1,669.9
Creditors – amounts falling due after more than one year:			
Medium and long term borrowing	17	(189.1)	(239.2)
Subsidiary undertakings		(225.0)	(225.0)
Accruals and deferred income		(10.2)	(13.5)
Deferred taxation		(0.6)	(3.8)
Other provisions for liabilities and charges		(10.5)	(2.0)
		(435.4)	(483.5)
Net assets		1,481.2	1,186.4
Capital and reserves			
Called up share capital	21	142.8	139.1
Share premium		129.5	48.7
Special reserve		397.2	397.2
Other reserves		50.1	50.1
Profit and loss account		761.6	551.3
Equity shareholders' funds		1,481.2	1,186.4

The financial statements were approved by the board of directors on 17 March 1997 and signed on its behalf by

Blakenham

J Makinson

[Handwritten signatures of Blakenham and J Makinson]

Notes to the Accounts

30 Notes to the company balance sheet

	1996 £m	1995 £m
Tangible fixed assets (leasehold property)		
Cost	0.6	0.6
Depreciation	(0.6)	(0.2)
Net book value	–	0.4

There were no capital commitments for fixed assets at 31 December 1996.

Investment in subsidiary undertakings	£m
At 31 December 1995	1,742.9
Acquisition from subsidiary undertaking	234.4
Disposals to subsidiary undertaking	(30.9)
Subscription for additional share capital in subsidiary undertaking	87.9
Repayment of capital by subsidiary undertaking	(211.0)
External disposal	(23.0)
Revaluations	(1.9)
At 31 December 1996	1,798.4

Shares are stated at cost less provisions for diminution in value or directors' 1969 valuations.

Deferred taxation	£m
Summary of movements	
At 31 December 1995	(3.8)
Charge for the year	3.2
At 31 December 1996	(0.6)

Deferred taxation derives from	1996 £m	1995 £m
Other timing differences	(0.6)	(3.8)

Current investments

The investments are unlisted, valued by the directors at book value and if realised at valuation there would be no liability for taxation on disposal.

Accruals and deferred income

Accruals and deferred income includes £12.6m (1995: £15.1m) 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. £10.2m is due after one year, within which the amount falling due after five years is £0.2m.

Notes to the Accounts

30 Notes to the company balance sheet continued

Reserves	Share premium account £m	Special reserve £m	Other reserves £m	Profit and loss account £m	Total £m
Summary of movements					
At 31 December 1995	48.7	397.2	50.1	551.3	1,047.3
Premium on issue of 3.5m equity shares	13.2	–	–	–	13.2
Premium arising on equity shares issued on Recoletos acquisition	67.6	–	–	–	67.6
Profit for the financial year	–	–	–	313.0	313.0
Dividends	–	–	–	(102.7)	(102.7)
At 31 December 1996	129.5	397.2	50.1	761.6	1,338.4

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.

31 Post balance sheet events

Disposal of investment in Television Broadcasts Limited

On 27 February 1997 Pearson sold its 10% interest in Television Broadcasts Limited ("TVB") for £111.1m. Pearson originally purchased this investment for £106.2m but the carrying value has subsequently been reduced as a result of exchange rate fluctuations. The profit on disposal, to be recognised in 1997, is £6.3m. In 1996 operating profit included £2.8m (1995: £0.7m) in respect of TVB dividends.

Acquisition of stake in South African business newspapers

On 1 February 1997 Pearson acquired a 50% stake in *Business Day* and *Financial Mail*, the leading daily and weekly financial and business publications in South Africa for £11.5m.

Flextech

On 17 March 1997 Pearson agreed to sell its interests in the satellite and cable channels, UK Gold (20%) and UK Living (25%), to Flextech as part of joint venture agreements between Flextech and the BBC. The sale of these interests involves the payment by Flextech, between now and December 1998, of £7.8m representing the repayment of UK Living loan stock, and Pearson Television receiving 8.8m Flextech ordinary shares – a total consideration of approximately £76m based on a Flextech share price of 772p. Following completion of the transaction, Pearson will own 5.6% of the enlarged share capital of Flextech.

Principal Subsidiary and Associated Undertakings and Investments

Subsidiary undertakings	Country of incorporation or registration	Business sector
The principal operating subsidiary undertakings 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.		
Financial Times Group Ltd*	England	Information
Interactive Data Corporation	USA	
Les Echos SA	France	
Recoletos Compañía Editorial SA (94.2%)	Spain	
Pearson Professional Ltd	England	
Addison-Wesley Publishing Co Inc	USA	Education
Addison Wesley Longman Ltd	England	
HarperCollins Educational Publishers	USA	
Penguin Putnam Inc	USA	Entertainment
The Penguin Publishing Co Ltd	England	
Mindscape Inc	USA	
Future Publishing Ltd	England	
Pearson Television Limited*	England	
Grundy Worldwide Limited	Australia	
Thames Television Ltd	England	
The Tussauds Group Ltd*	England	

	Country of incorporation or registration	Beneficial interest %	Class of share	Share capital £m	Accounting year end	
Associated undertakings						
Information						
The Economist Newspaper Ltd	England	50	Ord 5p	1.1	March	
		100	'B' 5p	}		0.1
		Nil	'A' 5p			
		Nil	Trust 5p			
Entertainment						
Port Aventura SA	Spain	40	Pts 10,000	52.8	December	
Troll Communications Inc	USA	44	Common equity	0.6	December	
Channel 5 Television Group Ltd	England	24	Ord 1p	–	December	
			Def 1p	–		
			Pref 1p	–		

Investments

The Group held 10% or more of the following:

Entertainment

Television Broadcasts Limited (sold February 1997)	Hong Kong	10.0	Ord HK 5c	1.8	December
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The principal partnerships are shown on page 40.

* Direct investment of Pearson plc

Five Year Summary

	1992 £m	1993 £m	1994 £m	1995 £m	1996 £m
Sales					
Continuing operations	1,022.3	1,193.8	1,413.3	1,687.1	2,048.9
Discontinued operations	613.4	676.3	136.8	143.3	137.1
	1,635.7	1,870.1	1,550.1	1,830.4	2,186.0
Profits					
Information	39.9	31.1	69.0	83.3	99.1
Education	42.5	55.8	51.2	31.8	68.1
Entertainment	41.6	62.2	129.5	110.9	(47.5)
Investment Banking	23.7	36.4	30.2	39.9	40.8
Corporate expenses less other income	(4.5)	(4.3)	(23.2)	(28.3)	(14.5)
Continuing operations	143.2	181.2	256.7	237.6	146.0
Discontinued operations	12.4	34.9	15.7	22.0	35.3
Operating profit	155.6	216.1	272.4	259.6	181.3
Profit/(loss) on disposals of businesses	–	(68.4)	15.2	6.0	229.4
Profit/(loss) on sales of fixed assets	8.8	4.4	26.4	123.4	(14.1)
Provision on investment in BSkyB	–	71.4	–	–	–
Profit before interest	164.4	223.5	314.0	389.0	396.6
Net interest payable	(13.6)	(14.9)	(16.2)	(23.9)	(29.5)
Loan stock redemption premium	–	–	–	–	(10.3)
Profit before taxation	150.8	208.6	297.8	365.1	356.8
Taxation	(44.4)	(60.3)	(74.3)	(92.8)	(108.6)
Profit after taxation	106.4	148.3	223.5	272.3	248.2
Equity minority interests	(1.1)	(0.3)	(0.6)	(11.3)	(7.7)
Profit for the financial year	105.3	148.0	222.9	261.0	240.5
Earnings per equity share	19.3p	27.0p	40.4p	47.1p	42.9p
Adjusted earnings per equity share†	17.3p	27.9p	34.1p	28.8p	30.6p
Dividends per equity share	12.0p	13.0p	15.0p	16.5p	18.0p

†Adjusted in accordance with page 25.

Five Year Summary

	1992	1993	1994	1995	1996
	£m	£m	£m	£m	£m
Capital employed					
Net assets	1,058.3	1,000.1	1,051.9	855.4	392.3
Deferred tax and other provisions	85.6	67.6	233.8	134.4	189.4
Net debt	121.3	1.3	146.4	63.4	430.4
Capital employed	1,265.2	1,069.0	1,432.1	1,053.2	1,012.1
Cumulative goodwill written off	670.7	700.2	1,042.5	1,437.8	1,896.4
Gearing					
Debt/equity	11%	N/A	14%	7%	110%
Debt/adjusted equity (including goodwill)	7%	N/A	7%	3%	19%
Interest cover	x11	x15	x17	x11	x6
Share statistics					
Equity shares – weighted average	545.5m	547.6m	551.6m	554.4m	560.8m
Share price – Year end	390p	608p	555p	624p	750p
– High	459p	614p	725p	684p	760p
– Low	302p	356p	554p	543p	601p
Average number employed					
Continuing operations	11,534	11,823	13,562	16,008	17,383
Discontinued operations	16,432	15,453	3,653	3,414	2,564
	27,966	27,276	17,215	19,422	19,947

Index to the Financial Statements

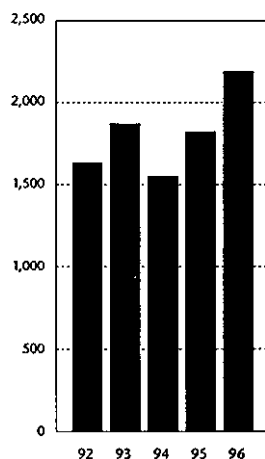
- Accounting policies pp29, 30
- Acquisitions pp48, 49, 50
- Adjusted earnings per share p25
- Auditors
 - Remuneration p33
 - Report to members p24
- Balance sheets
 - Company p54
 - Group p26
- Borrowings p43, 44
- Capital commitments p38
- Capital employed p32
- Capital expenditure p38
- Cash flow pp27, 51, 52
- Cash and liquid funds p42
- Contingent liabilities p53
- Creditors, other p45
- Debtors p41
- Deferred taxation p45
- Depreciation p38
- Disposals p51
- Dividends p35
- Earnings per share p25
- Employee information pp36, 37
- Fair value pp48, 49
- Forward exchange p44
- Five year summary pp58, 59
- Fixed assets, tangible p38
- Geographical analysis pp31, 32, 36, 39
- Goodwill pp48, 50
- Historical cost profits and losses p28
- Interest p34
- Interest rate hedging p44
- Investments pp41, 42
- Leases p52
- Net cash inflow from operating activities p51
- Net debt p52
- Other income p33
- Partnerships and associates pp39, 40
- Pensions pp36, 37
- Post balance sheet events p56
- Post-retirement costs pp36, 37
- Principal group companies p57
- Profit and loss account p25
- Provisions p46
- Recognised gains and losses p28
- Related parties p53
- Reserves p47
- Sales pp31,32
- Sector analysis pp31, 32, 36, 39
- Share capital and options pp46, 47
- Shareholders' funds p28
- Stocks p41
- Subsidiaries p57
- Taxation pp35, 45
- Treasury information pp43, 44

Pearson plc | an introduction

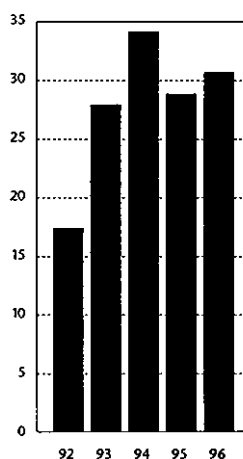
Pearson plc is an international media group with interests in publishing, television production, broadcasting, electronic and multi-media businesses. The Group focuses on three key markets worldwide: information, education and entertainment.

	1996	1995	Change
Sales	£2,186.0m	£1,830.4m	+19%
Operating profit before charge for improper accounting at Penguin USA*	£281.3m	£259.6m	+8%
Operating profit	£181.3m	£259.6m	-30%
Profit before tax	£356.8m	£365.1m	-2%
Earnings per share	42.9p	47.1p	-9%
Adjusted earnings per share	30.6p	28.8p	+6%
Dividends per share	18.0p	16.5p	+9%

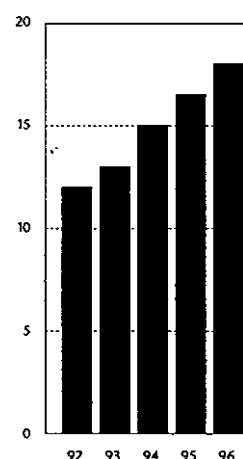
*See Finance Director's review



Sales (£m)



Adjusted earnings per share (p)



Dividends per share (p)

PEARSON

Pearson is an international media group with a diverse range of skills in newspaper, magazine and book publishing, on-line and software services, television and visitor attractions. The Group focuses these core skills, through separate business divisions, on three markets worldwide: information, education and entertainment. Pearson also has significant interests in investment banking.

Investment Banking

The Group has a 50% stake in Lazard Brothers, one of London's pre-eminent merchant banks, and interests in Lazard Frères of New York and Lazard Frères of Paris.



The **Information** division encompasses a wide portfolio of information services worldwide. Its printed products include national and international business newspapers, professional books, magazines and periodicals. It also provides electronic information services.

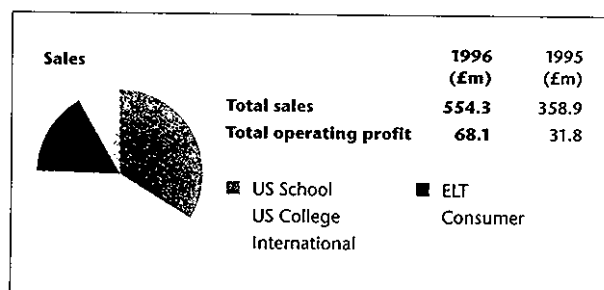
The **Entertainment** division produces, distributes and broadcasts television programmes, is a leading international trade book publisher, runs visitor attractions and produces consumer magazines, videos and software.

LEARN



J. Larry Jones

the business



With the addition of the HarperCollins Educational business in 1996, Addison Wesley Longman (AWL) is now one of the world's biggest educational publishers, with a significant share of the US market and a massive international presence. J. Larry Jones discusses the global market for high-quality educational resources.

Education, by its very nature, is a growth market. As economies develop around the world, governments, schools, colleges and individuals wish to invest increasing amounts in education for the future. AWL is in an excellent position to secure a significant share of the demand, and the acquisition of HarperCollins Educational in April has greatly extended our global franchise in educational publishing. There were compelling reasons for making this acquisition. The US educational publishing market is consolidating and those companies that will

EDUCATION



Addison
Wesley
Longman

Addison Wesley Longman (AWL) is a global educational publisher, selling books, multimedia and learning programmes in major academic disciplines to the primary, secondary, higher education and professional markets throughout the world. Its main imprints include Addison-Wesley, Longman, Scott Foresman·Addison Wesley and Benjamin Cummings. AWL is also the world's largest publisher of English language teaching (ELT) books and materials.



Operating Profit (£m)	1996	1995	%
Information	134.4	105.3	28
Education	68.1	31.8	114
Entertainment*	52.5	110.9	(53)
Investment Banking	40.8	39.9	2
Corporate Expenses	(14.5)	(28.3)	49
Total*	281.3	259.6	8

*Excludes £100m charge for improper accounting at Penguin USA

Financial Times Newspaper publishes the *Financial Times*, printed in ten centres covering Europe, North America and Asia.

Financial Times Information provides comprehensive electronic business and specialist financial information worldwide.

Les Echos is France's leading business daily newspaper and the flagship of a group which includes many other business and professional titles.

Recoletos is one of Spain's leading newspaper and magazine publishers. Its titles include the country's premier business daily and sports daily.

Pearson Professional publishes books, periodicals and screen-based services for professional communities worldwide.

Addison Wesley Longman publishes teaching products in many major markets in the US and throughout the world for elementary and secondary schools, colleges, and computer science and engineering professionals. AWL is also the world's largest publisher of American and British English language teaching materials.

Penguin publishes English language consumer books, fiction and non-fiction, in hardcover and paperback.

The Tussauds Group is the largest European operator of leading visitor attractions specialising in exhibitions and theme parks.

Pearson New Entertainment publishes special-interest consumer magazines, videos and related new media.

Mindscape develops and publishes consumer software for personal computers and video game systems.

Pearson Television is the UK's largest international television producer. It sells its formats worldwide and also has interests in distribution and broadcasting.

Chairman's | statement



The foundations of an international media company have been laid and 1996 saw Pearson building its strengths in the information, education and entertainment markets. In the Information division we increased the availability of the Financial Times newspaper in key world financial centres and developed further our electronic information services. In Education Addison Wesley Longman expanded through the acquisition of HarperCollins Educational Publishing, substantially increasing the range of our US educational products and reinforcing our position as a leading world educational publisher. In our Entertainment division the purchase of Putnam Berkley did very much the same for Penguin and Pearson Television consolidated its position as the UK's foremost international production company.

Our 1996 profits were badly hit by the results at Mindscape and the events at Penguin. Before taking into account the exceptional £100m charge in relation to unauthorised behaviour at Penguin USA (which is detailed in the Finance Director's Review) our operating profits for the year nonetheless increased by 8% and a 6% rise was achieved in adjusted earnings per share. These included the loss of £45m relating to Mindscape, which although large and disappointing, was nonetheless in line with what we forecast at the time of the last Annual General Meeting. Pearson has made a satisfactory start to the year with operating profits in line with expectations and I will report further to shareholders at the AGM in May. In the meantime your board is recommending a final

dividend of 11.1p, which would take the total dividend to 18p, representing a 9% increase for the year as a whole.

In addition to building on the strengths of the company, the other important development that has been taking place in the Group over the past year is the orderly transfer of executive power from one generation to another. David Bell, Greg Dyke and John Makinson became Pearson executive directors in March last year, Marjorie Scardino became chief executive in January this year and Dennis Stevenson will replace me as chairman after the AGM on 2 May. They will make a formidable team, with great individual skills, strong beliefs and the ability to create growing long term value for shareholders.

In wishing success to the new team I would also like to thank and acknowledge the achievements of the previous team of Frank Barlow, Mark Burrell, James Joll and David Veit, all of whom, with the exception of David who forms part of the new team, will have retired by the end of the AGM. I have worked with them on a daily basis since I became chairman of Pearson in September 1983. The market capitalisation of the company that September stood at £313m. At the time of writing (mid-March 1997) it stands at £4.4bn, the adjusted share price has multiplied by more than nine and a half times and Pearson shares have outperformed the FTSE All Share Index by over 100%. The FTSE 100 Index was started in January 1984. Since then 51 of the original companies have dropped out of the index and of the remainder only three companies have improved their ranking by more places than Pearson. In this period the nature of the company has been changed from that of a widespread conglomerate to a leading international media company. During the course of this change three additional successful public companies have been established in their own right, Fairey, Camco and Royal Doulton, and the value of the latter's shares distributed by scrip dividend to Pearson shareholders.

The philosophy of Pearson is to take a long term view; to take risk and sometimes substantial risk against a background of financial security; to deal fairly and honestly and to promote quality; and in doing so to create a company with a culture

which attracts and motivates entrepreneurial and talented people and makes it attractive for other companies to join.

Throughout this period the executives have been advised and encouraged by a strong group of internationally minded non-executive directors and I would like to thank them and the chief executives of the operating companies and everyone working in the Group for their enthusiasm and support throughout the good times and bad. In addition to immediate colleagues, of whom Frank Barlow has played an outstanding leadership role, I would also like to pay special tributes, as they leave the Group, to Peter Mayer who has over nineteen years taken Penguin from the position of a threatened UK paperback publisher to the international publishing house it is today, and to Sir Simon Hornby, who in addition to chairing the Remuneration Committee has been a valued contributor to the Pearson board for many years.

I want to conclude by emphasising that Pearson as a company has gone through a transformation. We are now well positioned with our leading international franchises to take advantage of the exciting prospects of the new media age, and as the pace of change quickens, I intend to enjoy watching the new management team do just that.



Michael Blakenham, Chairman

Managing Director's review



Pearson, as an international media group, is now organised into three business divisions. David Bell is responsible for the Information division worldwide, and J Larry Jones directs all our Education activities. David Veit co-ordinates our Entertainment businesses, with the exception of Pearson Television, which is run by Greg Dyke. This year, for the first time, in the divisional review on pages 9-21 of this annual report, each of them writes personally about the key issues and events of 1996 as he sees them.

Results

The majority of Pearson's operating companies continued to make significant progress during the year. Sales increased by 19% and exceeded £2bn for the first time. We reported an operating profit of £181m but this was after taking a charge of £100m in relation to improper accounting at Penguin USA. Setting this and the operating losses at Mindscape aside, profits increased by 23%.

A global strategy for Information

The Information division had a good year in 1996, expanding sales to £829m from £759m in 1995, and also generated excellent growth in operating profits. The division is establishing its strategic direction for the future, a position to be built firmly on the brand values associated with the *Financial Times* newspaper. In publishing, whether in newspapers or in professional areas, there is great potential for international growth.

In electronic information, key opportunities lie in supplying the expanding demand for high-quality financial and business information.

The Information portfolio will therefore be focused on markets where the division can build a significant international position. Consequently, Westminster Press, one of the UK's largest regional newspaper groups and a valued member of the Group for many years, no longer fitted this strategy, and its sale was completed in 1996.

All the Information division's companies saw a steady advance in sales in 1996. Growth in the UK economy created an uplift in financial and trade advertising, and the FT and Pearson Professional both increased their operating profit. Despite the difficult economic climate in France, *Les Echos* also improved its trading profitability, although this performance was



Peter Mayer and Michael Lynton

outweighed by the closure costs of our personal finance magazine *Argent*. In Spain, *Recoletos* continued to perform well, and we made further investment for its future. *Financial Times Information* enjoyed a strong contribution from *Interactive Data Corporation* which, in its first full year as part of Pearson, benefited from the rapid growth of mutual funds in the US.

Now a world-scale player in Education

The major event of the year was the acquisition in April of HarperCollins Educational Publishing, part of the HarperCollins publishing group. This has increased Pearson's turnover in Education from £359m in 1995 to £554m in 1996, making it one of the world's top three educational publishers, and positioned it for further global development.

Profit for the combined business in 1996 was £68m compared with £32m in 1995. This is a good result during a year when management was heavily absorbed in a major integration exercise – the second in two years, following the merger of Addison-Wesley and Longman. Substantial operational efficiencies should be achieved from 1997, with the most significant benefits of the acquisition becoming apparent as we near 2000 and new, larger publishing programmes are launched.

In the US school market, the Scott Foresman • Addison Wesley School Publishing Group has seen significant increases in the sales of its maths programme. The US college business continued

to expand and international higher education is also growing healthily. The English language teaching (ELT) market remains buoyant. *AWL* is number one in the world in ELT, a market where continuing growth is expected for the foreseeable future.

New international talent in Entertainment

The Entertainment division achieved a 13% increase in sales in 1996 to £803m compared to £712m in 1995. 1996 has been a year of international expansion for Pearson Television, with particular success in developing and selling worldwide the Grundy programme formats acquired in 1995. As part of the acquisition of *SelectTV*, we acquired the *Alomo* and *Witzend* programme makers, and all Pearson's television production activities were brought together at a single location in Central London in March 1997.

In consumer books, *Penguin USA*'s strong publishing programme produced a good result, and *Penguin UK* achieved a healthy profit recovery. The acquisition of *Putnam Berkley* brings together two of the most successful trade publishers in the US and makes *Penguin* the second largest English language trade book publisher in the world.

At the end of 1996, we bade farewell to Peter Mayer, who had been chief executive of the *Penguin Group* since 1978 and who had



Marjorie Scardino and Frank Barlow

built it from a loss-making British company to one of the leading international publishing houses. He was succeeded by Michael Lynton, who joins Penguin from Hollywood Pictures and Disney Publishing, bringing us the benefit of experience with one of the world's leading consumer brands.

The Tussauds Group produced a year of solid profit growth from its visitor attractions, against increased competition in the UK market, and continued to apply its management skills worldwide. Excellent performances came from Port Aventura in Spain, which has now completed a second successful year; Madame Tussaud Scenerama in Amsterdam; and the new Alton Towers Hotel, opened in March.

Pearson New Entertainment (PNE), which produces magazines, videos and other media for 'boys of all ages', also advanced into profit in 1996. Future Publishing had an outstanding year, concluding with a welcome recovery in the computer and video games magazine market.

Following an extremely difficult year in 1995, our software publishing company, Mindscape, has been reorganised and refocused in 1996 under its new chief executive, John Moore.

Excellent prospects for the future

When this Annual Report is published, I will have retired as Managing Director after

nearly 30 years with Pearson, seven as its managing director. The past few years have been personally very fulfilling and particularly momentous for the company. Pearson has been transformed from a broadly-based conglomerate to a coherent and increasingly cohesive media group.

I feel confident that the Group is now in a position to go from strength to strength, gaining further benefits from greater integration and global development of its portfolio. The prospects for 1997 are excellent, and I wish my successor Marjorie Scardino and her team every success in continuing Pearson's progress.

A handwritten signature in dark ink, reading 'Frank Barlow'.

Frank Barlow, Managing Director



Financial Times Newspapers publishes the *Financial Times*, widely regarded as one of the world's great newspapers, and a journal of record for the business community. It is printed in ten centres across the world.

Recoletos is one of Spain's leading newspaper and magazine publishers. Its titles include *Expansión*, the country's premier business daily, *Marca*, the leading sports newspaper and *Diario Medico*, a daily newspaper for doctors.

information

GROUPE

Les Echos Group is France's leading business daily newspaper and the flagship of a group which also includes amongst its many titles a monthly business magazine, *Enjeux les Echos*, and a twice-weekly medical newspaper, *Panorama du Médecin*.



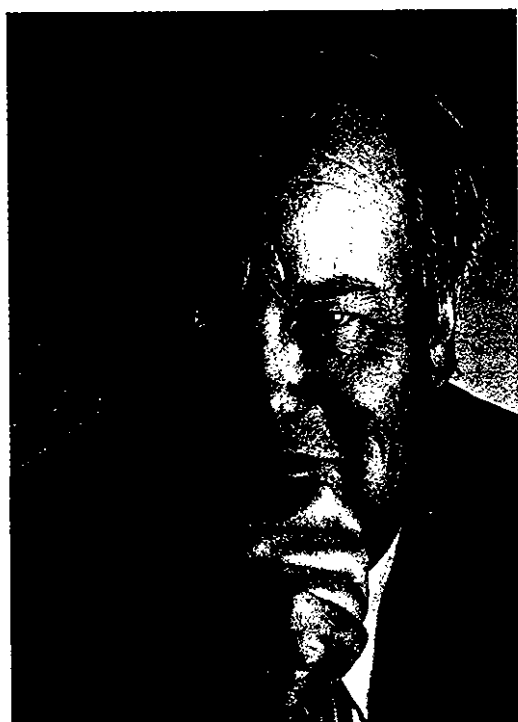
Financial Times Information provides electronic business and specialist financial information to the asset management, investment research and general business information markets worldwide.

Pearson Professional publishes books, periodicals, reports and screen-based services for professional communities worldwide, under brand names which include the *Financial Times*, *Pitman Publishing* and *Churchill Livingstone*.



Sales		1996 (£m)	1995 (£m)
	Total sales	828.7	759.1
	Operating profit:		
	■ FT Newspaper	28.6	19.4
	■ FT Information	17.3	11.4
	■ Les Echos	(0.3)	3.2
	■ Recoletos	34.9	37.8
	■ Pearson Professional	18.6	11.5
	Westminster Press	35.3	22.0
	Total	134.4	105.3

THE INFORMATION revolution



David Bell

The value of the worldwide information market – encompassing both the printed word and electronic media – is estimated at nearly £40 billion. Over the next ten years, it should double, driven by changes in technology. David Bell talks about Pearson's position and prospects.

We are in the midst of a global revolution in electronic data, as open systems like the Internet, or more localised 'intranets', provide access to all on an equal basis. This is opening up huge opportunities to sell business and financial information, and we are seeing value shift from the technology itself

energy, healthcare, media and telecommunications, advertising and marketing industries. During 1996, six specialist companies were acquired in these fields. Pitman Publishing has established itself as Europe's leading provider of management development materials in a range of paper-based and screen formats.

Two excellent pieces of news from Les Echos in the French specialist publishing field were the rapid growth in market share of *Enjeux les Echos* to become the second-ranking business magazine in the country and the turnaround of *Panorama du Médecin*, our specialist magazine for doctors.

Information in depth – the electronic media

The *Financial Times* and other business titles give Pearson a highly visible presence as a quality information provider across diverse geographical markets and professional sectors. They also help to generate interest in the wide range of on-line information services which benefit from association with the *Financial Times* brand. There is much talk of electronic data overtaking the written word, but in reality the world needs both; they occupy different, but equally important, positions in the information hierarchy.

Our electronic information services, whether text or number-based, are designed to provide selected data to specific users, with the emphasis on our unrivalled quality, authority and reliability. In the past year, we have invested substantially in database development and acquisition. *Financial Times Information* is co-operating with Dow Jones and Knight-Ridder Information to build a global news database, which will be the most comprehensive global collection of news available. In Asia, we acquired Asia Intelligence Wire, the region's leading on-line news and business database, and opened a new data collection centre in Manila.

KR KNIGHT-RIDDER
INFORMATION

DOW JONES

Financial Times Information is leading the team who are working together to build the world's largest, truly international database.

FT
FINANCIAL TIMES
Information



The Register Group, the advertising and marketing information division of Pearson Professional, acquired SHOTS Ltd which publishes a bi-monthly video and magazine for the international advertising community.

Added value through quality of content

Pearson now has one of the best financial data sets in the world. Success, however, depends on quality as much as quantity. Raw data means nothing until it is refined and presented in a form which meets the needs of its recipients. In the written word, this means excellence of comment and analysis for which the *Financial Times* and our other publications are already renowned. In electronic media, we are building a similar reputation providing timely, accurate, value-added data for the end-user.

For example, this year *Financial Times Information* signed a global strategic agreement with Verity to co-develop a new generation of on-line information products, including the re-engineering of *FT Profile*, the on-line market leader in English-language business information in Europe. This will enable not only text, but also audio and video, to be available worldwide, on demand. The Register Group, part of Pearson Professional, has developed a new, highly automated system to monitor television and press advertising across Europe. Most important of all, we have embarked on a major new development which will integrate all our databases and make them easily accessible, whether via the Internet or a dial-up phone line. The project has already excited interest worldwide.

The information business, like any other, succeeds by managing its assets effectively. Pearson, over the past few years, has extended the powerful position of the *Financial Times* brand into the global arena; we have invested in high-quality information databases and high-technology delivery systems; and we have developed and honed our ability to add value to information. We know where and how to focus our efforts, and expect to see the benefit of that knowledge coming through in sustained, profitable future growth.

to the content of the information it delivers – in which Pearson excels. Ours has become a universal industry, as information requirements around the world converge. Fund managers everywhere, for example, need the same timely access to dependable pricing data; business people in Asia, like those in the UK, want to wake up to the world's leading financial newspaper. During the past few years, Pearson has substantially strengthened its position in

ion

this exciting global market and we are developing a portfolio of information services for management communities worldwide.

The power of the printed word

The *Financial Times* itself serves the world's key financial centres: it is published in ten centres in eight countries



Mastering Management began as a 20-part weekly supplement in the *Financial Times*. Circulation of the newspaper increased dramatically and it has had a similar impact on the 13 other newspapers, including *Les Echos* and *Expansión*, in which *Mastering Management* has been published worldwide. Now it has gone on to become a book published by Pitman Publishing (a division of Pearson Professional) which sold 10,000 copies in the first six weeks.

CLUB FANTASTICO MARCA

Recoletos continues to capitalise on the success of the leading Spanish sports newspaper *Marca* with the introduction of Club Fantastico – a readers' club – which in its first year already has over 1,300,000 members.

worldwide. For reliability, authority and integrity in financial publishing, its reputation is unsurpassed. Overseas circulation continues to grow – the paper attracts more than half of its circulation revenue and approaching half of its advertising revenue from outside the UK. The FT is now read by over a million people in over 140 countries worldwide.

The *Financial Times* Web site, <http://www.FT.com>, demonstrates the FT's commitment to electronic publishing and the delivery of business news, comment and analysis around the world in a variety of formats. The Web site combines articles from the newspaper with material specially prepared and updated by a team of dedicated journalists. New users are registering to use the site at a rate of over 1,000 per day.

As well as being a global financial newspaper, the *Financial Times* is the UK's major national business newspaper. Its sisters are *Les Echos*, which has remained one of very few profitable national newspapers in the difficult French market; and *Expansión*, part of Recoletos, the market leader in Spain for both circulation and advertising. This year we invested in both, increasing our holding in Recoletos to an effective 94% and installing new presses for *Les Echos*. The three papers benefit from sharing content – as, for example, in the highly successful *Mastering Management* series. Beyond Europe, we extended our services to Spanish language markets by taking a preliminary stake in *El Diario*, a leading Chilean business newspaper. In February 1997 we acquired a 50% interest in *Business Day* and *Financial Mail*, the leading daily and weekly financial and business publications in South Africa.

While our national daily papers paint the broader business picture, we also provide a range of information products and services to more focused business communities. Pearson Professional publishes data, comment and analysis, in the form of newsletters, management reports, journals, magazines, directories and screen-based products, for the legal community and for specialists in the finance,

compete successfully into the next century need to offer their customers a broad range of products and secure economies of scale in selling, distribution and administration. The acquisition achieves this critical mass: AWL now has enviable, highly ranked positions in both the US school and college markets. It has, equally, enhanced our credibility and will ensure we can continue to attract the best authors and editorial talent for the future.

The process of integrating the HarperCollins operation has been remarkably smooth and our customers are already benefiting from the combination. New key executives in Corporate Services, School, and Higher Education, as well as our ongoing strong management team, have provided the experience and leadership to guide the company successfully through the integration and to maintain business performance. This has been a tremendous achievement by all concerned, and is a major reason for this year's much improved results.



1996 was a particularly strong year for the merged Scott Foresman-Addison-Wesley science lines. Strong state adoption sales secured the lead market position for two elementary science programmes: *Destinations in Science* and *Discover the Wonder*. In the secondary school market, both the new fourth edition of Addison-Wesley *Chemistry* and the new third edition of *Conceptual Physics* had record revenues and are outstanding market leaders.

A major player in US school publishing

The acquisition has had its most immediate effect on our school publishing programme in the US. It brings into our portfolio the highly respected Scott Foresman business, which includes titles in reading, language arts, mathematics and science. The school sales force can now add many popular, established programmes like *Discover the Wonder*, *Literature and Integrated Studies* and *Celebrate Reading!* to its bookbag.

Having this extended range will assist AWL in achieving a more even revenue stream throughout the US school book adoption cycle. Under this system, about half the states,

after evaluating many offerings, select titles from which their schools must choose for the next five to seven years. The HarperCollins acquisition is well timed to take advantage of opportunities offered by the cycle; a number of major subject adoptions are forthcoming in 1998 and 1999, with another important adoption year in 2001. Success in securing places on the adoption lists, particularly in significant markets like California, Florida and Texas, will depend on the excellence of our publishing. Our priority, now that the integration with HarperCollins is complete, is for our editorial teams to ensure that Scott Foresman-Addison Wesley books and other teaching materials fully meet – or exceed – the requirements of students, teachers and school boards.

Apart from mainstream book publishing, this year we have extended our school product by offering the *Waterford Early Reading Program*, a software-based programme for children in pre-school through grade two. We are very pleased with the results of this innovative programme to date.

New initiatives – home education, Electronic Commerce Center, expansion in Asia

Home education is an increasingly important market as families seek to supplement their children's formal studies with out-of-school learning activities, and there is increasingly an overlap between educational and consumer publishing. To respond to this market, we acquired BrightIdeas, a company that sells directly to parents, helping them to choose appropriate software to supplement their children's formal educational curriculum. Other products and methods to reach this market are in the pipeline.

The ability of customers to purchase our products and services via the worldwide web took a step closer in 1996, with the decision to establish an Electronic Commerce Center (ECC).

Through an innovative use of technology the *Waterford Early Reading Program* provides a proven way to enable all children to learn to read regardless of level of literacy. The program was developed by the Waterford Institute, a non-profit making educational research center.





The success of Michael Parkin's *Economics* has been driven by the joint commitment of author and publisher. In 1990, it was the most successful entry into the competitive US principles-of-economics textbook market in two decades. It is a market leader worldwide with bestselling adaptations in the UK, Australia, Canada and Mexico.

In addition to being a new source of business, the ECC will provide a new publishing platform for many of our groups and invaluable customer data for direct marketing. AWL already has a substantial presence in Hong Kong. Now we have established a beachhead in China, a vast new market, with offices in Shanghai and Beijing that will permit visibility for many of our publications. This exciting initiative sprang from the AWL China Development Group, made up of members from the International and English language teaching groups. They also initiated Korean co-publishing programmes in computer science and higher education and planned a reprint programme for developing countries.

A global franchise in higher education, technology and computer sciences/engineering

AWL's strong global franchise in higher education has been further strengthened by the HarperCollins College list, which includes titles such as *Psychology* by Wade and Tavis, the Lial/Hornsby/Miller maths series and *Economics* by Miller. Internationally, the higher education market is growing

Longman Malaysia launched the monthly newspaper *The Malaysian Student* in May. The newspaper, according to Datin Hajjah Aidah Ghani (representing the Deputy Director General of Education), "can play a significant role in helping to create a world-class youth for a 21st century Malaysia".



rapidly as the American education model exercises an increasing influence as far afield as Japan, Australia and, in some subjects, Europe and the UK. Our college products have shown themselves capable of travelling well, proving highly acceptable in different cultures and languages. Technology has an especially important place in higher education. This year, Addison Wesley Interactive (AWI) has published four new CD-ROM products that support interactive learning approaches to maths and science subjects. Through an arrangement with Netscape, a leading Internet software provider, we now offer students the ability to work seamlessly between AWI's multimedia products and worldwide web resources. It is a small, but important, step to ensure that AWL is ready for on-line teaching which, we believe, will inevitably follow interactive study as a force in education.

We are particularly strong around the world in computer sciences and engineering education which, in a technology-driven world, has created an important bridgehead for entering new international markets. In recognition of our publishing strengths in these subjects, we created the Computer and Engineering Publishing Group, whose charter is to publish a broad range of computer and engineering products, both print and new media, for the professional, academic and consumer markets. This concentrated focus will strengthen our acquisition, development and delivery capabilities, as well as taking advantage of scale and resources.

English language teaching – a world force

English is the mother tongue of some 370 million people and an official language for a further 250 million. It has been estimated that there are 350 million people in the world studying English, and that they spend nearly £1 billion on books and other published materials to help them. Whereas the traditional education market for English language teaching (ELT) in western Europe has matured, in the high-growth economies of the world, demand for English is accelerating. AWL is already strongly represented in Latin America and the tiger economies of south-east Asia and is well positioned to secure business in the huge Chinese market.

AWL offers a full range of innovative global programmes in both British and American English. We have the financial strength to develop new products and recoup the investment through worldwide sales. In particular, we have been highly successful in meeting the shift in demand from grammar-based learning to more sophisticated programmes centred on communication skills.

EXCITING YOUR
The
TUSSAUDS
Group
 IMAGINATION



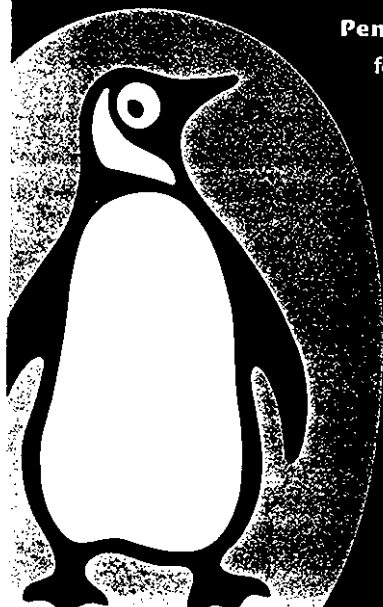
Pearson New Entertainment is a consumer entertainment company with a growing stake in the market for special interest magazines, news and information. It is the parent company of Future Publishing, the UK's third highest consumer magazine publisher.

entertainment

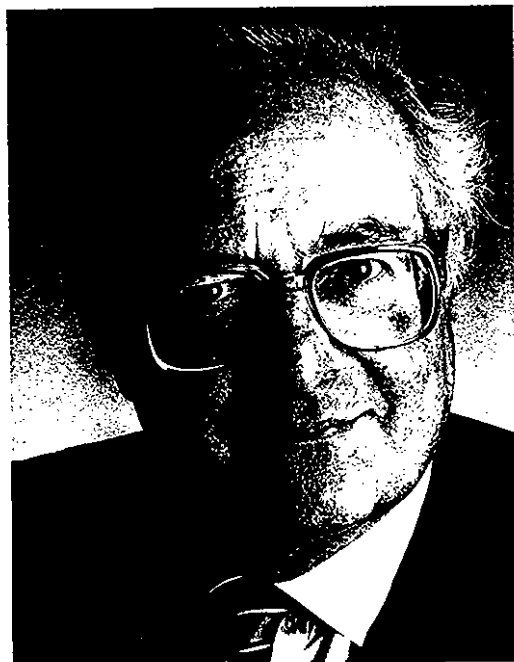
Pearson Television is the UK's largest international television producer, selling programmes and formats under Thames, Grundy, Alamo and Witzend and ACI brands. It also has interests in distribution and broadcasting, including a 24% stake in the UK's Channel 5.



Penguin Books is one of the world's foremost publishers of English-language consumer books, in both hardback and paperback. It owns a wide range of imprints and trademarks in addition to its own name, and also produces maps, audio books and other media products.



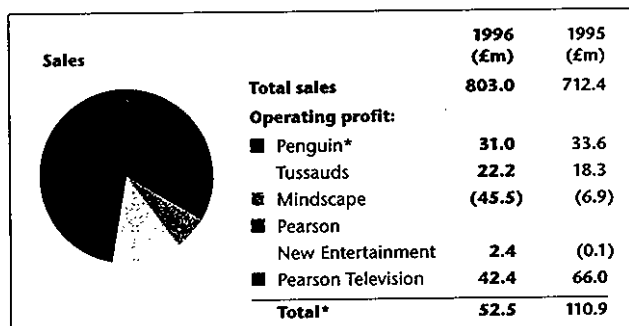
Mindscape develops and publishes consumer software for personal computers and video game systems, focusing primarily on entertainment, educational and reference titles.



David Veit

The world of consumer entertainment is fast-moving and demanding. Behind the entertainment value of a paperback novel or a TV serial, an exhibition or a theme park, a consumer magazine or a computer game, lies a great store of business skill and acumen. David Veit and Greg Dyke explain.

ENTERTAINING idea



*Excludes £100m charge for improper accounting at Penguin USA

Entertainment and leisure today are big business, global business – a company has to know where it is going and why. Pearson is clear about its products and markets, and has invested in top talent to direct its chosen businesses. Each of our businesses has, in different ways, successfully strengthened its management and strategy this year.

Penguin – a story of our times

Defying the predictions that television would eclipse book publishing, the consumer's appetite for a good read is growing. Competition for the attention of both adult and young readers is fierce, so even with a brand as powerful as Penguin, we must innovate constantly. In recent years we have produced some outstanding new publishing ideas, the pocket-sized Penguin 60s and serial partworks. This year, Stephen King's six-part thriller *The Green Mile* has been a runaway success on both sides of the Atlantic. So too have books which tie in with television dramatisations – especially the Jane Austen revival – and with children's films like *Babe*, *James and the Giant Peach*, and *Matilda*.



Greg Dyke

Dick Francis' *To the Hilt* was his best-selling novel ever for Penguin UK, and PD James' *Original Sin* was her strongest-selling novel yet. Other UK successes were Pat Barker's *Regeneration* trilogy, including her Booker Prize winner, *The Ghost Road*, and Fergal Keane's *Letter to Daniel*. In the US, hardback triumphs included Terry McMillan's *How Stella got her Groove Back* and Jacquelyn Mitchard's *The Deep End of the Ocean*, as well as the highly successful simultaneous

STEPHEN KING

THE GREEN MILE



THE WAIT IS OVER

The 6-part serial thriller is now complete
Available from WH Smith and all good book retailers
R.R.P. £1.99 each

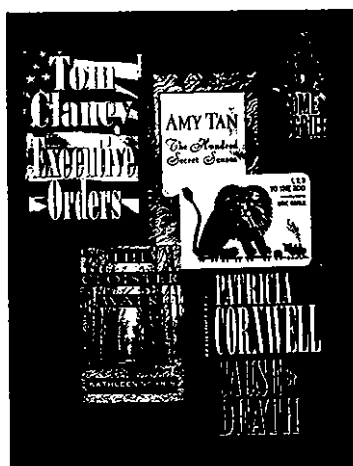
Penguin published Stephen King's latest thriller *The Green Mile* which was notable for two reasons: it was published in six monthly instalments and it was the first time that the author had been published by Penguin in the UK.

publication of Stephen King's *Desperation* and *The Regulators* (under his pseudonym Richard Bachman). Best-selling paperbacks were *The Road Ahead* by Bill Gates and *The Song of Solomon* by Toni Morrison.

Michael Lynton, who joined Penguin in October and took over as chief executive from Peter Mayer at the year end, will have the task of developing our publishing lists still further. Michael's first major contribution has been the acquisition of the US trade publisher Putnam Berkley, whose front list includes authors such as Tom Clancy, Patricia Cornwell, Dick Francis, Robin Cook, Amy Tan, Lawrence Sanders and Nora Roberts. Such names – each of whom produced a book included on the *New York Times* best-seller lists in 1996 – form a powerful fit with Penguin's renowned back list. The acquisition doubles Penguin's share of total US trade book sales, and makes us the second largest English language trade book publisher in the world.

Since the year end we have made an accounting provision of up to £100m (included in the 1996 figures) pending investigation of improper accounting at Penguin USA. This should not, however, detract from the trading performance in 1996.

In December Penguin acquired the US trade publisher, Putnam Berkley, for £200 million. Its authors include Amy Tan, Tom Clancy, Patricia Cornwell and, in the US only, Dick Francis.



International expertise in visitor attractions

Managing large-scale exhibitions and theme parks has become a specialised business involving a complex mix of planning, project management and operational skills. Tussauds owns and operates its enterprises in the UK, but our strategy is gradually shifting from capital-intensive investment in fixed assets towards contract-based projects. An example of our new approach to financing is for a proposed development at Stonehenge, in partnership with English Heritage, to attract Millennium Commission funding.

Alton Towers opened The Tussauds Group's first-ever hotel in March, since when it has achieved an outstanding 90% occupancy during the season. The Tussauds Group studios designed the themed areas to reflect the magic of the park itself.

This new direction is being driven by Tussauds' young, talented management – whose resources extend from a brilliant studio team to experts in people flow and visitor management. Their success in managing our existing portfolio of strong, branded visitor attractions is opening up wider opportunities for Tussauds. In the UK, we opened our first hotel at Alton Towers, which has had an outstanding year. We have proved our international capability as operators of the new Port Aventura theme park in Spain. Now, our skills in long-term planning and project management have resulted in negotiations with developers and investors as far afield as Thailand, where we are undertaking a feasibility study for a world-class theme park near Bangkok. Projects such as these make us increasingly aware of our potential as an attractive partner worldwide.

In exhibitions, of course, the Tussauds name needs no introduction. This year we have made excellent progress towards the opening of a new Madame Tussaud's on New York's 42nd Street, in the heart of this regenerated and dynamic part of the city. In Australia, plans are well advanced for a touring exhibition to be launched in autumn 1997. This innovative project is intended as a profitable enterprise in its own right, and a vehicle for raising awareness of The Tussauds Group as a whole.

SECRET GARDEN RESTAURANT



Market-first: a formula for success

Pearson New Entertainment (PNE) is a business defined by its market – hobbyists, enthusiasts, and especially 'boys of all ages'. This approach gives us the freedom to develop the business across media boundaries: from magazines, at present our principal medium, to video and software. Our Web site, FutureNet, is one of Europe's busiest on-line services. Future Publishing, which produces over 50 magazines on computing, music, crafts, sports and entertainment, has directed a formidable array of creative, editorial and commercial talent into meeting readers' and advertisers' aspirations. As just one example, *Official PlayStation Magazine*, launched only at the end of 1995, recorded massive growth in its first year, dwarfing competitors despite its premium cover price.

Future Publishing is the UK's fifth largest magazine publisher using the latest techniques to publish over 50 titles. These skills not only produce excellent magazines but have won Chris Stocker and Richard Davies a £500 first prize in a photographic competition open to all Pearson employees.



Future also acquired two specialist publishing groups, Music Maker and Litharne, a craft publisher. Meanwhile, PNE has continued to explore the potential for transferring its approach overseas, moving further into the Spanish and French markets.



Mindscape moves forward

After last year's difficulties, encountered throughout the industry, our software publishing company Mindscape has taken a more positive direction in 1996.

The management team has concentrated on developing and marketing proven products such as the successful 'evergreens' *Chessmaster 5000*, *Mavis Beacon Teaches Typing*, and a range of games like *Steel Panthers*, a contemporary wargame, *Azrael's Tear*, a state-of-the-art adventure game and *Warwind*, a critically acclaimed strategy game.

In the home creativity market, they have built on the success of *Printmaster Publishing Suite*, launching new products including the *Mindscape Student Reference Library* and *Mindscape Home Office Assistant* which received excellent reviews. We also launched a partnership with National Geographic which, as its first project, will deliver a compendium of the National Geographic magazine's images and stories going back more than 100 years.

The UK's largest international television production company

The television industry worldwide is changing fast. As the means of delivery proliferate through cable, satellite and now digital technology, shareholder value is gradually shifting from broadcasting to content. The winners will be those companies which make, own or have rights to successful formats and brands, and can exploit them worldwide. 1996 has been a year of just such international expansion for Pearson, as we have

concentrated on adapting formats from the Grundy, Thames, Alomo and Witzend libraries, to suit local markets. This year we have secured our leadership in the European daily serial market, launching new 'soaps' in Germany (where we now run four), Italy and Sweden. We are also gearing up to produce Britain's first five-day-a-week serial for Channel 5, the UK's last terrestrial channel, launched in March 1997. We have had great success in transferring game show formats across international boundaries. Two thirds of our profits and half of our revenues already come from outside the UK. We now aim to achieve the same international acceptability for re-formatted situation comedy programmes as we have in daily serial and light entertainment programming. Pearson's investments in distribution and broadcasting are also important, especially for their longer-term value as a means of distributing our own productions. We already sell programmes worldwide from the libraries owned by Thames, Grundy, Alomo and Witzend and ACI. In the UK, we have already sold £24m worth of new programming to Channel 5, in which Pearson has a 24% stake. The business plan for the new channel looks even more successful than it was when we submitted our bid, because since then the channel has been given an additional frequency, bringing in up to three million more viewers.



Pearson Television is making a daily drama called *Family Affairs* for Channel 5, the new terrestrial television franchise in the UK, as part of a package of programming which also includes an afternoon magazine programme, drama and several game shows.

INVESTMENT banking

Through its shareholding in Lazard Partners, Pearson has a 50% interest in Lazard Brothers, and a 9% stake in the partnership profits of Lazard Frères, Paris, and Lazard Frères, New York.

	1996	1995	Change
	£m	£m	%
Attributable profit	40.8	39.9	2

Together, the Lazard Houses occupy a unique position in the international merchant and investment banking community: a combination of three strong, indigenous operations each based in one of the world's principal capital markets. In 1996, Lazard Partners introduced a system which will enable each bank to share in the financial performance of all three, while preserving the Houses' independence and separate cultures. This will strengthen further the potential for cooperation and collaboration in their major business activities.

Corporate Finance/Mergers & Acquisitions

The essence of the Houses' work in corporate finance is to

advise some of the largest companies in the industrialised world, principally on acquisitions and mergers. Corporate finance is a dominant business for the Lazard Houses which, unlike many other merchant banks, have remained independent and focused on their corporate advisory business and have not integrated into large-scale equity distribution and market-making activities. This has enhanced Lazard's powerful reputation for working in close partnership with its clients, and for providing objective and highly professional advice. In 1996, all three Houses again produced very strong performances in their domestic and international corporate finance markets. Notable transactions for Lazard Brothers included the high-profile takeovers of Forte by Granada and BET by Rentokil, the flotation of British Energy and advice to the Council of Lloyd's of London on the Lloyd's reconstruction. Transactions by Lazard Frères, New York included the huge, US\$23bn acquisition by SBC Communications of Pacific Telesis and, in collaboration with Lazard Brothers, the US\$25bn negotiations between MCI and BT and the merger of Lucas and Varity. Lazard Frères, Paris advised on the first tranches of privatisation for both France Telecom and Aerospatiale.

Capital Markets

Since March 1995, the Lazard Houses have worked in partnership in capital markets, the business of issuing capital securities to investors. 1996, the first full year of this arrangement, was extremely successful, particularly as a result of business referred to the partnership by Corporate Finance partners. Over the year, the three Houses acted as lead, co-lead or joint lead manager to their clients on more than 50 managed offerings with a combined value in excess of US\$10bn.

Asset Management

The Lazard Houses manage funds for institutional investors, mutual funds and private investors. Together, the Houses had funds under management in excess of US\$50bn at the end of 1996. Lazard Frères, New York and Lazard Frères, Paris enjoyed a very successful year in asset management. Lazard Brothers made a good recovery after two difficult years, achieving sales of over £100m from the first year of its mutual funds business and launching a personal portfolio service for individuals investing over £20,000. Early in 1997 Lazard announced that the US and UK asset management operations would be combined into a new entity – Lazard Asset Management.

Pearson | and the community



Pearson is sponsoring an exhibition about Seurat's masterpiece, *The Bathers at Asnières*, at the National Gallery in London from 2 July to 28 September.

Corporate sponsorship

Pearson has sponsored 16 major art exhibitions since 1982, including, last year, an exhibition about the work of William Morris, the great Victorian designer, poet, businessman and radical. It was staged at the Victoria and Albert Museum in London to mark the centenary of Morris's death, and attracted well over 200,000 visitors – including 2,000 Pearson employees and shareholders.

In 1997 we will be sponsoring *Seurat and the Bathers*, which will run from July to September at the National Gallery in London. It will bring together for the first time the preparatory drawings and oil sketches for Seurat's masterpiece, *The Bathers at Asnières*.

The *Financial Times* sponsored a design competition for a new Millennium bridge across the river Thames, linking St Paul's Cathedral with the south bank development of the Globe Theatre and the new Tate Gallery of Modern Art at Bankside. The competition was won by a consortium including Foster and Partners.



Andy Anderson, deputy managing editor, *Financial Times*, is part of the staff who support reading schemes in local schools and also act as 'mentors' to individual pupils.

Charitable donations

Each year, Pearson aims to donate approximately one half of one per cent of the previous year's adjusted earnings to charitable causes. In 1996, we gave £808,000, again focusing on education and young people.

Approximately half our donations are made by operating companies, many of which take an active role in their local communities. For example, last year staff from the *Financial Times* and FT Information were involved in mentoring pupils from local schools; AWL supported the Victoria Hall Performing Arts Association in Harlow; and Mindscape employees helped provide Christmas gifts for underprivileged children through the Human Needs Center of Novato. Staff around the world ran, walked and biked to raise money for good causes, including charities to combat multiple sclerosis, AIDS, hunger and cancer.

At the centre, Pearson plc continued to support the Bodleian Library and helped a wide range of educational charities including the National Literacy Trust and the British Dyslexia Association.

The environment

Pearson no longer operates in industries where there is potential for serious industrial pollution. However, we recognise our responsibility to be aware of, and take steps to control and minimise, any damage our businesses may cause to the environment. For example, we buy paper, ink and packaging from renewable sources.

Board of Directors

Michael Blakenham



Frank Barlow



David Bell



Mark Burrell



Michel David-Weill



Greg Dyke



Pehr Gyllenhammar



Jean-Claude Haas



Sir Simon Hornby

Michael Blakenham Chairman aged 59, became a director of Pearson in 1971, chief executive in 1978 and chairman in 1983 and will retire at the AGM in May 1997. He is also chairman of MEPC plc and a director of a number of other companies.

Frank Barlow Managing Director until 31 December, aged 67, joined Pearson in 1968, where his many posts have included chief executive of Westminster Press, chief executive of the Financial Times and, since 1986, director of Pearson. He became managing director of Pearson in 1990 and will retire from the board after the 1997 AGM. He will continue to be a director of *The Economist* and chairman of Logica plc.

David Bell Information division aged 49, became an executive director of Pearson in March 1996, with responsibility for the Group's information businesses, having previously been chief executive of the Financial Times Group since 1993. He joined Pearson as a trainee journalist on the *Oxford Mail* and *Times* before moving to the *Financial Times* in 1972 where his career ranged from Washington correspondent to managing editor before leaving editorial in 1989 on his appointment as advertisement director.

Mark Burrell Development Director aged 60, joined Pearson in 1963 and was involved with the company's

industrial subsidiaries. In 1970 he joined Lazard Brothers. He has been a director of Pearson since 1977 and will retire at the AGM. He is also non-executive chairman of Royal Doulton plc.

Michel David-Weill aged 64, is chairman of Lazard Partners, deputy chairman of Lazard Brothers and chairman of Lazard Frères, New York and managing director of Lazard Frères, Paris. He is the longest serving non-executive director of Pearson having joined the board in 1970.

Greg Dyke Television aged 49, chairman and chief executive of Pearson Television since 1995. He became an executive director of Pearson plc, responsible for the Group's television interests, in March 1996. He is currently chairman of Channel 5 Broadcasting. He was previously the chief executive of London Weekend Television which he left in February 1994. He started in television as a journalist in 1977 (also with LWT) held senior executive positions with TV-am and TVS, (other companies within the ITV network) during the 1980s and was chairman of ITV for two years. He is also a former director of both ITN and Channel Four.

Pehr Gyllenhammar aged 61, is a senior adviser to Lazard Frères & Co LLC, New York and former chairman of AB Volvo. He has been a non-executive director of Pearson since 1983.

James Joll



Gill Lewis



John Makinson



Reuben Mark



Vernon Sankey



Marjorie Scardino



Dennis Stevenson



David Veit



David Verey

Jean-Claude Haas aged 71, retired at the AGM in 1996. He is a partner of Lazard Frères, Paris and is a non-executive managing director of Lazard Brothers. He was appointed a non-executive director of Pearson in 1990.

Sir Simon Hornby[†] aged 62, is a director of Lloyds Bank and the former chairman of W H Smith and Lloyds Abbey Life plc. He became a non-executive director of Pearson in 1978 and will retire at the AGM this year.

James Joll aged 60, retired as finance director in April 1996 and as an executive director of Pearson at the end of 1996. He joined Pearson in 1980 and became finance director in 1985. Prior to Pearson he was a director of NM Rothschild and Sons and before then a journalist at the *Financial Times*.

Gill Lewis[†] aged 53, became a non-executive director of Pearson in 1992. She is a director and managing partner of the consumer practice of Heidrick & Struggles in Europe.

John Makinson Finance Director aged 42, joined the board in March 1996 and succeeded James Joll as finance director on 1 April 1996. Prior to joining Pearson he was managing director of the *Financial Times*.

Reuben Mark[†] aged 58, is chairman and chief executive of Colgate-Palmolive Company. He became a non-executive director of Pearson in 1988.

Vernon Sankey^{*} aged 47, is chief executive of Reckitt & Colman plc which he joined in 1971. He became a non-executive director of Pearson in 1993.

Marjorie Scardino Chief Executive aged 50, became a director and chief executive on 1 January 1997. Marjorie Scardino trained and practised as a lawyer before publishing a weekly newspaper in the USA. In 1985 she joined The Economist as president of its North American operations and became its chief executive in 1993.

Dennis Stevenson^{*} Deputy Chairman aged 51, is chairman of GPA Group plc and of the Trustees of the Tate Gallery. He has been a non-executive director of Pearson since 1986. He became deputy chairman in October 1996 and will succeed Michael Blakenham as chairman after the AGM in May 1997.

David Veit aged 58, joined Lazard Brothers in 1961. He remained there until 1973, apart from a break of two years when he obtained an MBA at Stanford University. Over the past 20 years he has been the senior Pearson executive in the US, becoming a director in 1981 and president of Pearson Inc. in 1985. In March 1996 he assumed responsibility for Pearson's entertainment businesses (excluding television).

David Verey aged 46, joined Lazard Brothers in 1972 and became chairman in 1992. He was appointed an alternate director of Pearson in 1995 and became a non-executive director in 1996.

Anette Lawless FCIS Secretary, Pearson plc.

^{*} The Audit Committee, chaired by Vernon Sankey and made up entirely of non-executive directors, 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 audit committee to raise any matter of concern and to report the results of work directed by the committee. The committee itself reports to the full board of Pearson.

[†] The Remuneration Committee is chaired by Sir Simon Hornby and consists of non-executive directors. It meets regularly to decide the remuneration and benefits packages of the executive directors and approve the recommended remuneration and benefits packages of the chief executives of the main operating subsidiaries.

Finance Director's | review



This is my first report to shareholders as Pearson's finance director and it spans a period of exceptional activity for the company. While the past 12 months have presented their problems, the reorganisation of Mindscape and the discovery of improper accounting at Penguin USA being the most challenging, they have also yielded progress and opportunity. The underlying operating performance of many Pearson companies has markedly improved, we have narrowed our focus on media businesses which can deliver strong and secure growth, and we have a new management committed to making the business perform to the maximum of its potential.

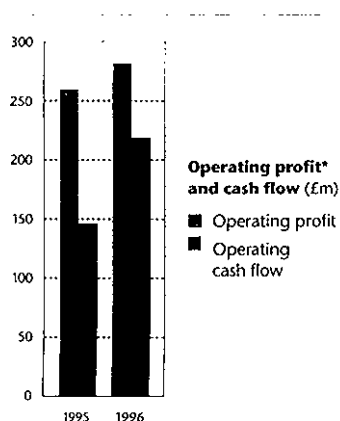
Operating performance

Pearson's sales exceeded £2bn for the first time last year, with acquisitions made over the past two years contributing the majority of the 19% increase over 1995 levels. The underlying sales growth of the Group remains disappointing and the generation of additional revenue from our established businesses is an important priority for this year and beyond.

We reported an operating profit for 1996 of £181m but this was after taking a charge of £100m in relation to the improper accounting at Penguin. I discuss this issue in more detail later but, in considering the Group's operating profit, it is important to remember that the 1996 charge was to cover problems dating back to 1991 and had little impact on Penguin's ongoing sales or profits. This charge has been treated as a one-off item and

therefore excluded from the calculation of adjusted earnings. If the Penguin item is set aside, profit before interest emerges at £281m, which compares favourably with the 1995 figure of £260m. Even this comparison needs to be made with care, however, as 1996 suffered the damaging impact of significant non-trading losses from Mindscape, as well as start-up costs at Channel 5 and the absence of income from the shares in BSkyB which we sold in September 1995. Conversely, we saw the benefit of acquisitions made in each of the past two years and experienced a lower overall level of restructuring costs. If allowance is made for all these factors, underlying operating profits were £18m higher than in 1995.

The net interest charge increased from £24m to £30m during the year, reflecting the higher average level of debt which resulted from acquisition



*Excludes £100m charge for improper accounting at Penguin USA

activity in 1996. Despite this increase, net interest was covered almost 10 times by operating profit before the Penguin charge. The profit before tax of £357m was, by coincidence, very similar to the previous year's level. This figure was boosted, however, by the book profit of £231m on the sale of Westminster Press and does not provide a useful guide to our underlying performance.

The tax rate attributable to our adjusted earnings was again held below 30% and we believe that this remains a realistic target for the next several years given the significant level of tax losses available to the Group in the USA. Over the past year we have undertaken a thorough review of Pearson's tax structure and this review will be helpful to us in realising our tax rate objectives.

Adjusted earnings per share for the year were 30.6 pence, an increase of 6% on the previous year's number. The recommended dividend was increased at a slightly faster rate of 9% to 18 pence, reducing adjusted earnings cover fractionally to 1.7 times. While earnings cover is a useful indicator of a company's distribution capacity, we need to focus strongly in future on the generation of sufficient cash from the business, after payment of interest and tax, to meet our responsibilities to shareholders. The proposed 1996 dividend was fully funded on that basis although we would aim over time to strengthen the cash cover for the payment.

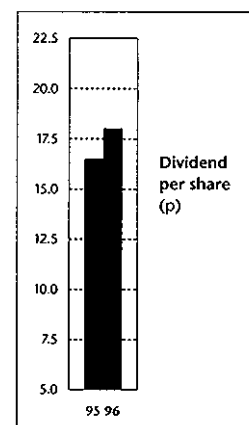
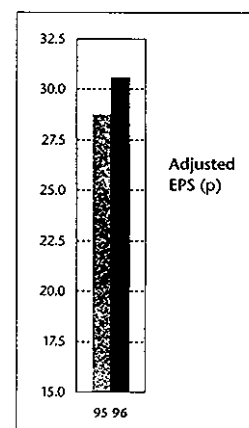
Operating cash flow grew much more strongly than operating profit last year, as several of the factors

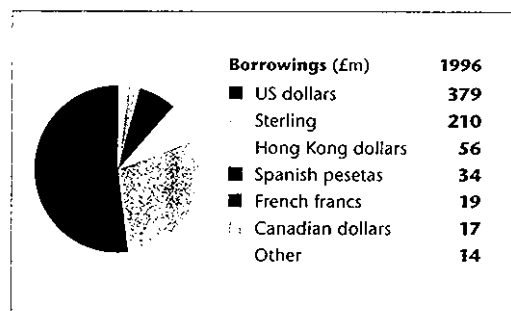
that depressed our profit performance had no bearing on our cash position. At £219m, operating cash flow was almost 50% higher than in the previous year and represented around 80% of operating profit, adjusting for the Penguin charge and for income from associates. We will be giving this ratio more weight in future as we strive to improve further the underlying cash performance of the Group.

Portfolio changes

The balance sheet reflects the changes in the portfolio over the course of the year. In total we spent £769m on acquisitions, the most significant being HarperCollins Educational, for which we paid £369m in April, and Putnam Berkley, which was acquired in December for £201m. The goodwill which arose on these acquisitions has been charged directly to reserves, in line with our normal practice. This was the principal reason for the fall in total shareholders' funds from £855m to £392m.

Almost half of our acquisition spending was financed by the sale of Westminster Press for £305m. The balance was funded by an increase in our net debt from £63m at the end of 1995 to £430m at the 1996 balance sheet date. Since the year end we have reduced our borrowing by £111m through the sale of our 10% investment in TVB, the Hong Kong broadcaster. We are examining other minority investments which the Group holds, to establish whether the capital could be more productively redeployed in managed businesses. The acquisition of two





sizeable US publishing companies, together with the disposal of the regional newspaper business in the UK, combined to increase the proportion of the Group's total capital employed in the US, as well as the sales and profits generated by those assets. We reflected that change in the shape of our dollar balance sheet through the creation of a \$750m medium term note (MTN) programme in the US debt market. We have so far issued \$250m of this programme, which provides us with a flexible and cost-effective source of dollar capital for the future.

Financial strategy

The MTN issue formed an element of a comprehensive review of Pearson's financial strategy which we undertook last year. One outcome was the creation of a Treasury Committee, comprising the finance director and two other members of the Pearson board, to consider treasury policies and controls on a regular basis.

In June last year we appointed Price Waterhouse as our new worldwide auditors. Since their appointment they have been working actively with the finance function throughout Pearson to reassess our risk exposures and to consider ways of refining our approach to performance measurement.

Improper accounting at Penguin USA

This work has been given an added urgency by the discovery of improper accounting practices at Penguin USA. The losses which have been reflected in the 1996 figures stemmed from an unauthorised practice of offering discounts to certain customers

in exchange for early payment of invoices.

This practice was concealed through an extremely intricate pattern of misleading accounting entries. As far as we can judge, and our investigation into the matter is not complete, this was an isolated incident involving a very small number of people. Nonetheless, we have initiated an urgent analysis of Pearson systems, procedures and controls, the importance of which has been communicated to everyone in the Group.

The future

This analysis is being undertaken in conjunction with an important project to improve back office services across our publishing companies. The Shared Services Project is expected to yield considerable cost savings, as well as an improvement in the quality of information and service, by combining transactional activities – such as payroll and the processing of purchase orders – which can more efficiently be conducted under one roof.

The Shared Services Project, like much else that we are studying at Pearson with a fresh eye, will not show an instant return on investment. We are mindful of the need to generate the profits and cash which, year by year, will fund a rising stream of dividends to our shareholders. But, at the same time, we cannot afford to neglect the financial investment needed to make Pearson a truly competitive media company in the next century.

John Makinson, Finance Director

Summary Directors' Report

Important note

The summary financial statements on pages 32 to 35 of this document do not contain sufficient information to allow for a full understanding of the results of the Group and of the state of affairs of the Group. For further information, the full Annual Accounts, the Directors' Report and the Auditors' Report on those accounts, should be consulted. If you have not received the Directors' Report and Accounts, but wish to do so, please return the request for these which is attached to your proxy form for the Annual General Meeting. If however, you are happy to receive this Annual Report only (which does include summary financial statements) you need take no action.

Summary directors' report

The full Directors' Report is set out on pages 14 to 16 of the Directors' Report and Accounts.

Business review and future development

The principal activities of the Group are carried out in three main sectors: information, education and entertainment. More details of these and other activities, the development of the Group and likely future developments are set out on pages 4 to 28 of this Annual Report and in the Operating and Financial Review on pages 1 to 13 in the Directors' Report and Accounts.

Post balance sheet events

In February 1997 Pearson acquired a 50% stake in *Business Day* and *Financial Mail* in South Africa for a consideration of £11.5m and sold its 10% stake in Television Broadcasts Ltd in Hong Kong for £111.1m. In March Pearson agreed to sell its interests in the satellite and cable channels, UK Gold (20%) and UK Living (25%), to Flextech as part of joint venture agreements between Flextech and the BBC. The sale of these interests involves the payment by Flextech, between now and December 1998, of £7.8m representing the repayment of UK Living loan stock, and Pearson Television receiving 8.8m Flextech ordinary shares – a total consideration of approximately £76m based on a Flextech share price of 772p. Following completion of the transaction, Pearson will own 5.6% of the enlarged share capital of Flextech.

Further details are given on page 56 of the Directors' Report and Accounts.

Directors

Information about the directors of the Company is set out on pages 24 and 25 of this document and an extract of the Report of the Remuneration Committee containing details of directors' emoluments and share interests is set out on pages 30 and 31. Six directors will retire by rotation at the Annual General Meeting.

Of these David Veit, Reuben Mark and Gill Lewis, being eligible, will offer themselves for re-election for a further three years. In addition, Lord Blakenham, Frank Barlow and Mark Burrell retire by rotation but will not seek re-election. Sir Simon Hornby will also retire at the end of the Annual General Meeting. Marjorie Scardino, who was appointed to the board on 1 January 1997, retires from office in accordance with article 77 of the Company's articles of association and, being eligible, offers herself for re-appointment.

No director was materially interested in any contract of significance to the Company's business.

Full details of these and related matters are set out on pages 14 to 16 of the Directors' Report and Accounts.

Report of the auditors

The report of the auditors on the annual accounts of the Group for the year ended 31 December 1996 was unqualified and did not contain a statement under either s.237(2) or s.237(3) of the Companies Act 1985.

Dividend

A final dividend of 11.1p per share is proposed for the year to 31 December 1996. This, with the interim already paid, makes a total for the year of 18.0p. The final dividend will be paid on 6 June 1997 to shareholders on the register at the close of business on 11 April 1997 (the record date).

The Company operates a scrip dividend scheme. Details of the scrip dividend alternative will be posted to shareholders on 28 April 1997.

If you would like further information about the scheme please contact our Registrar whose address and telephone number are on page 36.

Annual General Meeting

The notice convening the Annual General Meeting to be held on Friday 2 May 1997 is contained in the enclosed circular.


Anette Lawless, Secretary

17 March 1997

Extracts from the Report of the Remuneration Committee

Remuneration policy for executive directors

The committee's policy is designed to attract, retain and motivate high calibre senior executives through pay and other arrangements which are competitive and represent best practice, while also relating reward to performance and aligning the interests of directors and senior management with the interests of shareholders. The main components are base salary, an annual cash bonus plan, long-term incentives and pension benefits. In addition, the Company provides company car and health care benefits. The Company also provides housing for Marjorie Scardino who is a US national. Further details of Marjorie Scardino's remuneration can be found below the following table. The full Remuneration Committee Report is set out on pages 17 to 23 of the Directors' Report and Accounts.

Excluding contributions to approved pension funds, and compensation for early termination of contract, directors remuneration was as follows:

Name	1996 Salary/fees £000's	Bonus £000's	Other £000's	3-year ISP £000's	1996 Total £000's	1995 Salary/fees £000's	Bonus £000's	Other £000's	3-year ISP £000's	1995 Total* £000's
Executive directors										
Michael Blakenham	315	—	38	—	353	300	—	37	413	750
Frank Barlow	380	—	41	—	421	330	—	40	413	783
David Bell†	179	12	10	—	201	—	—	—	—	—
Mark Burrell	207	—	42	—	249	200	—	42	287	529
Greg Dyke†	183	100	108	—	391	—	—	—	—	—
James Joll	250	—	38	—	288	230	—	37	287	554
John Makinson†	179	61	16	—	256	—	—	—	—	—
David Veit	303	—	10	—	313	323	—	11	287	621
Non-executive directors										
Michel David-Weill	25	—	—	—	25	25	—	—	—	25
Pehr Gyllenhammar	25	—	—	—	25	30	—	—	—	30
Jean-Claude Haas†	11	—	—	—	11	32	—	—	—	32
Sir Simon Hornby	25	—	—	—	25	25	—	—	—	25
Gill Lewis	25	—	—	—	25	30	—	—	—	30
Reuben Mark	32	—	—	—	32	32	—	—	—	32
Vernon Sankey	25	—	—	—	25	25	—	—	—	25
Dennis Stevenson	25	—	—	—	25	25	—	—	—	25
David Verey†	17	—	—	—	17	—	—	—	—	—

* The incentive share plan release relating to the three-year period 1993-1995 is included in the total 1995 remuneration figure.

† David Bell, Greg Dyke and John Makinson were appointed to the board on 15 March 1996. David Verey became a non-executive director on 3 May 1996. Jean-Claude Haas retired from the board on 3 May 1996. In the case of David Bell, Greg Dyke and John Makinson, the emoluments shown relate to the ten-month period from March to December 1996, with the exception of bonus, which relates to the full year.

A sum of £250,000 was paid to James Joll as compensation for early termination of his contract, which had a three-year notice period. In addition his pension was augmented with effect from his retirement date at a capital cost of £250,000.

Marjorie Scardino joined the board and became chief executive on 1 January 1997, at a base salary of £396,500, although for pension and bonus purposes, her salary is deemed to be £425,000 (so as to include an element of the housing benefit referred to below). She received a joining bonus of £130,000 in consideration of the loss of potential benefits with her previous employer. She participates in the annual bonus plan and the incentive share plan, under which she will be conditionally awarded shares to the value of £300,000 in 1997, £200,000 in 1998 and £200,000 in 1999. Housing is provided at an initial annual cost to the Company of £60,500 and she receives a pension supplement of 25% of salary to provide for benefits in excess of the pensions earnings cap.

Dennis Stevenson will receive annual fees of £240,000 on becoming chairman on 2 May 1997. He will also participate in the incentive share plan, under which he will be conditionally awarded shares to the value of £300,000 upon appointment and £200,000 one year later, each vesting over five years. Dennis Stevenson's fees for 1996 were paid to SRU Limited.

Frank Barlow was the highest paid director in 1996. His total remuneration, including pension contributions, amounted to £421,346. The chairman's total remuneration, including pension contributions, amounted to £352,979.

Extracts from the Report of the Remuneration Committee

Interests of directors were:	Ordinary shares		Options – Ordinary shares		Incentive share plan ‡ – Ordinary shares		Maximum number of shares in lieu of adjustment on Royal Doulton demerger
	31.12.96*	1.1.96**	31.12.96*	1.1.96**	31.12.96*	1.1.96**	
Michael Blakenham	138,214	101,580	417,454	417,454	31,926	72,919	12,908
(non-beneficial)	129,040	129,040	–	–	–	–	–
Frank Barlow	38,750	6,939	419,794	419,794	25,107	72,919	11,235
David Bell	9,303	8,348	111,156	85,469	6,790	6,620	628
Mark Burrell	791,674	1,032,504	283,339	282,799	15,222	50,276	9,840
(non-beneficial)	65,040	65,040	–	–	–	–	–
Michel David-Weill†	48,129,727	48,129,727	–	–	–	–	–
Greg Dyke	–	–	106,900	73,300	6,790	6,620	–
Pehr Gyllenhammar	–	–	–	–	–	–	–
Jean-Claude Haas	29,537	29,537	–	–	–	–	–
Sir Simon Hornby	4,000	4,000	–	–	–	–	–
James Joll	25,494	2,093	155,846	155,847	9,160	50,276	4,541
Gill Lewis	–	–	–	–	–	–	–
John Makinson	1,000	–	103,784	68,000	–	–	–
Reuben Mark	7,600	7,600	–	–	–	–	–
Vernon Sankey	–	–	–	–	–	–	–
Dennis Stevenson	38,000	8,000	–	–	–	–	–
David Veit	253,602	107,712	245,380	348,869	31,892	50,276	–
David Verey	–	–	–	–	–	–	–

† Mr David-Weill's interests include 48,088,523 ordinary shares owned by companies associated with Lazard Frères et Cie., Paris.

* Or date of retirement, if earlier.

** Or date of appointment, if later.

‡ A full explanation of this plan is given on page 17 of the Directors' Report and Accounts. The number of shares shown represents the maximum number of shares, plus accumulated scrip dividend shares, comprised in the original award which may be transferred to the individual concerned.

Executive directors of the Company, as possible beneficiaries, are also deemed to be interested in the Pearson Employee Share Trust, the trustee of which held 149,933 Pearson ordinary shares of 25p each at 31 December 1996 and 148,395 ordinary shares at 17 March 1997, the latest practicable date prior to the printing of this report.

Marjorie Scardino was appointed to the board with effect from 1 January 1997, at which date she had no interests in Pearson securities. On 16 January 1997, she acquired 10,000 ordinary shares of 25p each in the Company. Also on 16 January 1997, John Makinson acquired a further 2,000 ordinary shares of 25p each, taking his total holding to 3,000 shares.

Consolidated Profit and Loss Account

for the year ended 31 December 1996

	1996			1995		
	Operating activities £m	Other items £m	Total £m	Operating activities £m	Other items £m	Total £m
Sales						
Continuing operations	1,845.9	—	1,845.9	1,687.1	—	1,687.1
Acquisitions	203.0	—	203.0	—	—	—
	2,048.9	—	2,048.9	1,687.1	—	1,687.1
Discontinued operations	137.1	—	137.1	143.3	—	143.3
Total sales	2,186.0	—	2,186.0	1,830.4	—	1,830.4
Cost of sales	(1,064.1)	—	(1,064.1)	(939.7)	—	(939.7)
Gross profit	1,121.9	—	1,121.9	890.7	—	890.7
Net operating expenses – normal	(853.3)	—	(853.3)	(627.7)	—	(627.7)
– exceptional	(40.4)	(100.0)	(140.4)	(46.7)	—	(46.7)
Net income from partnerships and associated undertakings	53.1	—	53.1	43.3	—	43.3
Operating profit						
Continuing operations	219.9	(100.0)	119.9	237.6	—	237.6
Acquisitions	26.1	—	26.1	—	—	—
	246.0	(100.0)	146.0	237.6	—	237.6
Discontinued operations	35.3	—	35.3	22.0	—	22.0
Total operating profit	281.3	(100.0)	181.3	259.6	—	259.6
Continuing operations:						
Profit/(loss) on sale of fixed assets	—	(14.1)	(14.1)	—	123.4	123.4
Profit/(loss) on sale of businesses	—	(1.9)	(1.9)	—	6.0	6.0
Discontinued operations:						
Profit on sale of Westminster Press	—	231.3	231.3	—	—	—
Profit before interest	281.3	115.3	396.6	259.6	129.4	389.0
Net interest payable	(29.5)	—	(29.5)	(23.9)	—	(23.9)
Loan stock redemption premium	—	(10.3)	(10.3)	—	—	—
Profit before taxation	251.8	105.0	356.8	235.7	129.4	365.1
Taxation	(72.6)	(36.0)	(108.6)	(64.8)	(28.0)	(92.8)
Profit after taxation	179.2	69.0	248.2	170.9	101.4	272.3
Equity minority interests	(7.7)	—	(7.7)	(11.3)	—	(11.3)
Profit for the financial year	171.5	69.0	240.5	159.6	101.4	261.0
Dividends on equity shares	(102.7)	—	(102.7)	(91.8)	—	(91.8)
Profit retained	68.8	69.0	137.8	67.8	101.4	169.2
Adjusted earnings/total earnings per equity share	30.6p	12.3p	42.9p	28.8p	18.3p	47.1p
Dividends per equity share	18.0p	—	18.0p	16.5p	—	16.5p
Average number of shares (millions)	560.8	560.8	560.8	554.4	554.4	554.4

In order to show results from operating activities an adjusted earnings per equity share has been calculated which excludes profits on the sale of fixed assets and businesses, the loan stock redemption premium, the £100m charge for improper accounting at Penguin USA and the tax consequences of these items.

Summary Cash Flow Statement

for the year ended 31 December 1996

	1996 £m	1995 £m
Net cash inflow from operating activities	291.2	236.4
Returns on investments and servicing of finance	(36.5)	(40.8)
Taxation	(80.8)	(69.7)
Capital expenditure and financial investment	(56.4)	441.8
Acquisitions and disposals	(427.7)	(405.5)
Equity dividends paid	(96.0)	(86.3)
Cash (outflow)/inflow before management of liquid resources and financing	(406.2)	75.9
Management of liquid resources	351.4	(225.0)
Financing	21.6	266.7
(Decrease)/increase in cash in the year	(33.2)	117.6

Summary Reconciliation of Net Cash Flow to Movement in Net Debt

for the year ended 31 December 1996

	1996 £m	1995 £m
Change in net debt resulting from cash flows	(33.2)	117.6
Change in net debt from management of liquid resources	(351.4)	225.7
Change in net debt from other borrowings	(18.9)	(256.6)
Exchange differences	36.5	(3.7)
Movement in net debt in the year	(367.0)	83.0
Net debt at 1 January	(63.4)	(146.4)
Net debt at 31 December	(430.4)	(63.4)

Summary Consolidated Balance Sheet

as at 31 December 1996

	1996 £m	1995 £m
Fixed assets	908.6	925.6
Current assets	1,337.4	1,642.2
Creditors due within one year	(1,094.0)	(1,087.7)
Net current assets	243.4	554.5
Total assets less current liabilities	1,152.0	1,480.1
Creditors due after more than one year	(570.3)	(490.3)
Provisions for liabilities and charges	(189.4)	(134.4)
Net assets	392.3	855.4
Capital and reserves	388.6	833.2
Equity minority interests	3.7	22.2
	392.3	855.4

This summary financial statement was approved by the board of directors on 17 March 1997 and signed on its behalf by

Blakenham



J Makinson



Statement by the Auditors to the Members of Pearson plc

We have examined the summary financial statement set out on pages 32 to 34.

Respective Responsibilities of Directors and Auditors

The summary financial statement is the responsibility of the directors. Our responsibility is to report to you our opinion on its preparation and consistency with the annual financial statements and Directors' Report.

Basis of Opinion

We conducted our work in accordance with Auditing Guideline "The auditors' statement on the summary financial statement" adopted by the Auditing Practices Board.

Opinion

In our opinion the summary financial statement is consistent with the annual financial statements and the Directors' Report of Pearson plc for the year ended 31 December 1996 and complies with the requirements of section 251 of the Companies Act 1985 and the regulations made thereunder, applicable to summary financial statements.

Price Waterhouse

Chartered Accountants and Registered Auditors
Southwark Towers,
London SE1 9SY
17 March 1997

Five Year Summary

	1992	1993	1994	1995	1996
	£m	£m	£m	£m	£m
Sales					
Continuing operations	1,022.3	1,193.8	1,413.3	1,687.1	2,048.9
Discontinued operations	613.4	676.3	136.8	143.3	137.1
	1,635.7	1,870.1	1,550.1	1,830.4	2,186.0
Profits					
Information	39.9	31.1	69.0	83.3	99.1
Education	42.5	55.8	51.2	31.8	68.1
Entertainment	41.6	62.2	129.5	110.9	(47.5)
Investment Banking	23.7	36.4	30.2	39.9	40.8
Corporate expenses less other income	(4.5)	(4.3)	(23.2)	(28.3)	(14.5)
Continuing operations	143.2	181.2	256.7	237.6	146.0
Discontinued operations	12.4	34.9	15.7	22.0	35.3
Operating profit	155.6	216.1	272.4	259.6	181.3
Profit/(loss) on sale of businesses	–	(68.4)	15.2	6.0	229.4
Profit/(loss) on sale of fixed assets	8.8	4.4	26.4	123.4	(14.1)
Provision on investment in BSKyB	–	71.4	–	–	–
Profit before interest	164.4	223.5	314.0	389.0	396.6
Net interest payable	(13.6)	(14.9)	(16.2)	(23.9)	(29.5)
Loan stock redemption premium	–	–	–	–	(10.3)
Profit before taxation	150.8	208.6	297.8	365.1	356.8
Taxation	(44.4)	(60.3)	(74.3)	(92.8)	(108.6)
Profit after taxation	106.4	148.3	223.5	272.3	248.2
Equity minority interests	(1.1)	(0.3)	(0.6)	(11.3)	(7.7)
Profit for the financial year	105.3	148.0	222.9	261.0	240.5
Earnings per equity share	19.3p	27.0p	40.4p	47.1p	42.9p
Adjusted earnings per equity share[†]	17.3p	27.9p	34.1p	28.8p	30.6p
Dividends per equity share	12.0p	13.0p	15.0p	16.5p	18.0p

[†] Adjusted to eliminate the distortions caused by including abnormal items in accordance with page 25 of the Directors' Report and Accounts.

Shareholder Information

Registered office and telephone

3 Burlington Gardens, London W1X 1LE
Telephone no: 0171 411 2000, Fax no: 0171 411 2390
email: firstname.lastname@pearson.com
Registered number 53723 (England)

Web site

Pearson has a Web site which is regularly updated with information about the Company and our operating companies. The address is: <http://www.pearson.com>

Financial calendar for 1997

Ex-dividend date:	Monday 7 April
Record date:	Friday 11 April
Despatch of scrip dividend information:	Monday 28 April
Annual General Meeting:	Friday 2 May
Last date for scrip election:	Tuesday 20 May
Share entitlement under scrip dividend posted:	Thursday 5 June
Payment date for dividend:	Friday 6 June
Interim results:	Monday 5 August

Payment of dividends to mandated accounts

Where shareholders have given instruction for payment to be made direct into a bank or building society account, this is done through the Bankers Automated Clearing System (BACS), with the associated tax voucher showing the tax credit attributable to the dividend payment sent direct to the shareholder at the address shown on our register. If you wish the tax voucher to be sent to another address, please inform our Registrar.

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 s. 272(3) of the Taxation of Chargeable Gains Act 1992 and as derived from The 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)

Pearson operates a Corporate PEP and a Single Company PEP. Both are open to existing and prospective shareholders in Pearson. For further information, please 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 0836 433620. Calls are charged at 40p per minute cheap rate and 50p per minute at all other times, inclusive of VAT.

American Depositary 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 Company shareholder meetings. For further information, please contact the Bank of New York at the above address.

CREST

Last year we advised shareholders that we would be joining CREST. We have now entered the CREST system. Under the new system those shareholders who wish to do so can retain their share certificates.

Pearson employee magazine

Pearson produces a magazine for all its employees, which is also available to shareholders. It deals with people and events within the Group. If you wish to receive copies of the magazine when it is published, please return the enclosed form to the Registrars.

Advisers

Registrar:	Lloyds Bank Plc, Lloyds Bank Registrars, The Causeway, Worthing, West Sussex BN99 6DA.
Auditors:	Price Waterhouse
Broker:	Cazenove & Co
Bankers:	Midland Bank plc National Westminster Bank Plc
Solicitors:	Freshfields Herbert Smith
Financial Advisers:	Lazard Brothers & Co., Limited J. Henry Schroder & Co. Limited

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Entertainment

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