

Year Ended December 31	Average rate
2010	\$1.54
2009	\$1.57
2008	\$1.84
2007	\$2.01
2006	\$1.84

#### Risk factors

*You should carefully consider the risk factors described below, as well as the other information included in this Annual Report. Our business, financial condition or results from operations could be materially adversely affected by any or all of these risks, or by other risks that we presently cannot identify.*

***Our education, business information and book publishing businesses will be impacted by the rate of and state of technological change, including the digital evolution and other disruptive technologies.***

A common trend facing all our businesses is the digitization of content and proliferation of distribution channels, either over the internet, or via other electronic means, replacing traditional print formats. The digital migration brings the need for change in product distribution, consumers' perception of value and the publisher's position between retailers and authors, which affects managing stock levels. The trend to e-books has created contraction in the consumer books retail market which increases the risk of bankruptcy of a major retail customer; this could disrupt short-term product supply to the market as well as could result in a large debt write off.

We face competitive threats both from large media players and from smaller businesses, online and mobile portals and news redistributors operating in the digital arena and providing alternative sources of news and information. New distribution channels, e.g. digital format, the internet, online retailers, growing delivery platforms (e.g. e-readers), combined with the concentration of retailer power pose both threats and opportunities to our traditional consumer publishing models, potentially impacting both sales volumes and pricing.

If we do not adapt rapidly to these changes we may lose business to 'faster' more 'agile' competitors, who increasingly are non-traditional competitors, i.e. technology companies, making their identification all the more difficult. We may be required to invest significant resources to further adapt to the changing competitive environment.

***Investment returns outside our traditional core US and UK markets may be lower than anticipated.***

To take advantage of international growth opportunities and to reduce our reliance on our core US and UK markets we are increasing our investments in a number of emerging markets, some of which are inherently more risky than our traditional markets. Political, regulatory, economic and legal systems in emerging markets may be less predictable than in countries with more developed institutional structures. Political, regulatory, economic, currency, reputational and corporate governance risks (including fraud) as well as unmanaged expansion are all factors which could limit our returns on investments made in these markets.

***Our US educational solutions and assessment businesses may be adversely affected by changes in state and local educational funding resulting from either general economic conditions, changes in government educational funding, programs, policy decisions, legislation at both at the federal and state level and/or changes in the state procurement processes.***

The results and growth of our US educational solutions and assessment businesses are dependent on the level of federal and state educational funding, which in turn is dependent on the robustness of state finances and the level of funding allocated to educational programs. State, local and municipal finances have been adversely affected by the US recession and the unknown timing of economic recovery. Funding pressures remain, with competition from low price and disruptive new business models and promotion of open source to keep costs down. The current challenging environment could impact our ability to collect on education-related debt.

Federal and/or state legislative changes can also affect the funding available for educational expenditure, which include the impact of education reform, such as the reauthorization of the Elementary and Secondary Education Act, the introduction of the Common Core and Race to the Top funding. Similarly changes in the state

procurement process for textbooks, learning material and student tests, particularly in the adoptions market can also affect our markets. For example, changes in curricula, delays in the timing of the adoptions and changes in the student testing process can all affect these programs and therefore the size of our market in any given year.

There are multiple competing demands for educational funds and there is no guarantee that states will fund new textbooks or testing programs, or that we will win this business.

***A control breakdown or service failure in our school assessment businesses could result in financial loss and reputational damage.***

There are inherent risks associated with our school assessment businesses, both in the US and the UK. A service failure caused by a breakdown in our testing and assessment processes could lead to a mis-grading of student tests and/or late delivery of test results to students and their schools. In either event we may be subject to legal claims, penalty charges under our contracts, non-renewal of contracts and/or the suspension or withdrawal of our accreditation to conduct tests. It is also possible that such events would result in adverse publicity, which may affect our ability to retain existing contracts and/or obtain new customers.

***Our reported earnings and cash flows may be adversely affected by changes in our pension costs and funding requirements.***

We operate a number of pension plans throughout the world, the principal ones being in the UK and the US. The major plans are self-administered with the plans' assets held independently of the Group. Regular valuations, conducted by independent qualified actuaries, are used to determine pension costs and funding requirements. As these assets are invested in the capital markets, which are often volatile, the plans may require additional funding from us, which could have an adverse impact on our results.

It is our policy to ensure that each pension plan is adequately funded, over time, to meet its ongoing and future liabilities. Our earnings and cash flows may be adversely affected by the need to provide additional funding to eliminate pension fund deficits in our defined benefit plans. Our greatest exposure relates to our UK defined benefit pension plan, which is valued once every three years. Pension fund deficits may arise because of inadequate investment returns, increased member life expectancy, changes in actuarial assumptions and changes in pension regulations, including accounting rules and minimum funding requirements.

***Our intellectual property and proprietary rights may not be adequately protected under current laws in some jurisdictions and that may adversely affect our results and our ability to grow.***

Our products and services largely comprise intellectual property delivered through a variety of media, including newspapers, books, the internet and other growing delivery platforms. We rely on trademark, copyright and other intellectual property laws to establish and protect our proprietary rights in these products and services.

We cannot be sure that our proprietary rights will not be challenged, invalidated or circumvented. Our intellectual property rights in countries such as the US and the UK, jurisdictions covering the largest proportion of our operations, are well established. However, we also conduct business in other countries where the extent of effective legal protection for intellectual property rights is uncertain, and this uncertainty could affect our future growth. Moreover, despite trademark and copyright protection, third parties may copy, infringe or otherwise profit from our proprietary rights without our authorization.

These unauthorized activities may be more easily facilitated by the internet. The lack of internet-specific legislation relating to trademark and copyright protection creates an additional challenge for us in protecting our proprietary rights relating to our online business processes and other digital technology rights. The loss or diminution in value of these proprietary rights or our intellectual property could have a material adverse effect on our business and financial performance.

In that regard, Google reached a tentative settlement in 2008 with the Author's Guild and the Association of American Publishers over Google's plans to copy the full text of all books ever published without permission of the copyright owners, including Pearson. The agreement was revised in 2009 to narrow the definition of books covered under the settlement agreement to those registered with the US Copyright Office by January 2009 or published in Australia, UK, Canada or US. Subject to final court approvals, the settlement would allow copyright owners of

books covered by it to control the online display of those books by Google, with a sharing of revenues derived from that display. The amended settlement agreement has yet to be approved.

***A major data privacy breach may cause reputational damage to our brands and financial loss.***

Across our businesses we hold large volumes of personal data including that of employees, customers and, in our assessment businesses, students and citizens. Individuals may try to gain unauthorized access to our data in order to misappropriate such information for potentially fraudulent purposes. As the techniques used to gain unauthorized access change frequently, we may be unable to anticipate or protect against the threat of breaches. Failure to adequately protect personal data could lead to penalties, significant remediation costs, reputational damage, potential cancellation of some existing contracts and inability to compete for future business.

***Operational disruption to our business caused by our third party providers, a major disaster and/or external threats could restrict our ability to supply products and services to our customers.***

Across all our businesses, we manage complex operational and logistical arrangements including distribution centers, data centers and large office facilities as well as relationships with third party print sites. We have also outsourced some support functions, including information technology, to third party providers. The failure of third parties to whom we have outsourced business functions could adversely affect our reputation and financial condition. Failure to recover from a major disaster, (e.g. fire, flood etc) at a key facility or the disruption of supply from a key third party vendor or partner (e.g. due to bankruptcy) could restrict our ability to service our customers. Similarly external threats, such as a flu pandemic, terrorist attacks, strikes, weather etc, could all affect our business and employees, disrupting our daily business activities.

***Changes in students' buying and distribution behaviour put downward pressure on price.***

Students are seeking cheaper sources of content, e.g. online discounters, file sharing, use of pirated copies, and rentals, along with open source. This change in behaviour, along with the move from professor-centric decision-making, puts downward pressure on textbook prices in our major markets.

***Our professional services and school assessment businesses involve complex contractual relationships with both government agencies and commercial customers for the provision of various testing services. Our financial results, growth prospects and/or reputation may be adversely affected if these contracts and relationships are poorly managed.***

These businesses are characterized by multi-million pound sterling contracts spread over several years. As in any contracting business, there are inherent risks associated with the bidding process, start-up, operational performance and contract compliance (including penalty clauses) which could adversely affect our financial performance and/or reputation. Failure to retain these contracts at the end of the contract term could adversely impact our future revenue growth. At Edexcel, our UK Examination board and testing business, any change in UK Government policy to examination marking (e.g. price capping) could have a significant impact on our present business model.

***We operate in markets which are dependent on Information Technology (IT) systems and technological change.***

All our businesses, to a greater or lesser extent, are dependent on information technology. We either provide software and/or internet services to our customers or we use complex IT systems and products to support our business activities, particularly in business information publishing, back-office processing and infrastructure. We face several technological risks associated with software product development and service delivery in our educational businesses, information technology security (including virus and hacker attacks), e-commerce, enterprise resource planning system implementations and upgrades. Although plans and procedures are in place to reduce such risks, our businesses could be adversely affected if our systems and infrastructure experience a significant failure or interruption.

***Failure to generate anticipated revenue growth, synergies and/or cost savings from acquisitions could lead to goodwill and intangible asset impairments.***

We continually acquire and dispose of businesses to achieve our strategic objectives. In 2010 we acquired Melorio plc, Medley Global Advisors LLC, Sistema Educacional Brasileiro, Wall Street Institute Education Sarl, America's Choice Inc and several other small acquisitions, and we sold our interest in Interactive Data. Acquired goodwill and intangible assets could be impaired if we are unable to generate the anticipated revenue growth, synergies and/or cost savings associated with these or other acquisitions.

***Expected benefits from our finance transformation programme initiatives may not be realised.***

We have entered into a substantial finance transformation programme based around shared and common processes and services, including the outsourcing of financial transaction processing, which is expected to result in significant cost savings in future years. The programme may take longer than planned, cost more than planned, and may cause disruption to our business. There is no assurance that the full extent of the anticipated benefits will be realised in the timeline envisaged.

***Changes in our tax position can significantly affect our reported earnings and cash flows.***

Changes in corporate tax rates and/or other relevant tax laws in the UK and/or the US could have a material impact on our future reported tax rate and/or our future tax payments.

***We generate a substantial proportion of our revenue in foreign currencies particularly the US dollar, and foreign exchange rate fluctuations could adversely affect our earnings and the strength of our balance sheet.***

As with any international business our earnings can be materially affected by exchange rate movements. We are particularly exposed to movements in the US dollar to sterling exchange rate as approximately 60% of our revenue is generated in US dollars. Sales for 2010, translated at 2009 average rates, would have been £128m or 2% lower.

This is primarily a currency translation risk that only arises on consolidation and is the result of translating entities into sterling for reporting purposes (i.e. non-cash flow item), and not a trading risk (i.e. cash flow item) as our foreign currency trading cash flows in individual operating companies are relatively limited. See "Item 5. Operating and Financial Review and Prospects – General Overview, Exchange rate fluctuations".

Each 5¢ change in the average £:\$ exchange rate for the full year (which in 2010 was £1:\$1.54) has a translation impact of approximately 1.3p on reported earnings per share and affect shareholders' funds by approximately £115m.

***The inherent volatility of advertising could adversely affect the profitability of our newspaper business.***

Advertising revenue is susceptible to fluctuations in economic cycles. Certain of our products, such as the *Financial Times* newspaper, are more advertising-driven than our other products. Consequently, these products are more affected by decreases in advertising revenue. As the internet continues to grow as a global medium for information, communication and commerce, advertisers are increasingly shifting advertising dollars from print to online media. Any downturn in corporate and financial advertising spend due to the economic slowdown will negatively impact the results.

***A significant deterioration in Group profitability and/or cash flow caused by a severe economic depression could reduce our liquidity and/or impair our financial ratios, and trigger a need to raise additional funds from the capital markets and/or renegotiate our banking covenants.***

A prolonged and severe economic depression could significantly reduce the Group's revenues, profitability and cash flows as customers would be unable to purchase products and services in the expected quantities and/or pay for them within normal agreed terms. A liquidity shortfall may delay certain development initiatives or may expose the Group to a need to negotiate further funding. If there was a steep decline in operating profit the Group might breach its banking covenants, creating (or exacerbating) a need for further funding (or a renegotiation of the terms of the bank credit agreement) to maintain operations. The current fragile state of the credit markets could expose the Group to a risk that it could neither re-negotiate its existing banking facilities, nor raise enough new