Exchange rate information

The following table sets forth, for the periods indicated, information concerning the noon buying rate for sterling, expressed in dollars per pound sterling. The average rate is calculated by using the average of the noon buying rates in The City of New York on each day during a monthly period and on the last day of each month during an annual period. On December 31, 2009 the noon buying rate for cable transfers and foreign currencies as certified by the Federal Reserve Bank of New York for customs purposes for sterling was £1.00 = $1.62. On February 28, 2010 the noon buying rate for sterling was £1.00 = $1.52.

Month	High	Low
February 2010	$ 1.60	$ 1.52
January 2010	$ 1.64	$ 1.59
December 2009	$ 1.66	$ 1.59
November 2009	$ 1.68	$ 1.64
October 2009	$ 1.66	$ 1.59
September 2009	$ 1.67	$ 1.59

Year Ended December 31	Average rate
2009	$1.57
2008	$1.84
2007	$2.01
2006	$1.84
2005	$1.81

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.

Global economic conditions may adversely impact our financial performance.

As the current economic environment remains dynamic and challenging, the risk of weak trading conditions continues in 2010 which could adversely impact our financial performance. The effect of a continued deterioration in the global economy will vary across our different businesses and will depend on the depth, length and severity of any economic downturn. Specific economic risks by business are described more fully in the other risk factors below.

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 funding, at a cost level that was sustainable for the business. Were this to occur, the inability to raise funding would likely lead to a curtailment in investment and growth plans, potential asset disposals (if possible), reduction or elimination in the dividend and in an extreme case a need to restructure the Group's debt, business model and terms of trade. In such event, the value of the Group's equity could not be assured.

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 and legislation (both at the federal and state level), and/or changes in the state procurement process.

The results and growth of our US educational solutions and assessment businesses is 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. In response to budget shortfalls, states and districts may reduce educational spending as they seek cost savings to mitigate budget deficits. The American Recovery and Reinvestment Act provided additional federal funding for education; the potential impact of this new money on our markets remains uncertain.

Federal and/or state legislative changes can also affect the funding available for educational expenditure, which include changes in assessment policy, the reauthorization of the Elementary and Secondary Education Act, along with the movement to a common core of skills and knowledge. 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.

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 2009, translated at 2008 average rates, would have been £4,984m or 11% 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”.

Pearson currently generates approximately 60% of its sales in US dollars and each 5¢ change in the average £:$ exchange rate for the full year (which in 2009 was £1:$1.57) has a translation impact of approximately 1.3p on reported earnings per share and affect shareholders’ funds by approximately £120m.

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 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.

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 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.

The plan trustees and the company finalised the latest triennial valuation for funding purposes (as at January 1, 2009) on March 22, 2010.

We operate in a highly competitive environment that is subject to rapid change and we must continue to invest and adapt to remain competitive.

Our education, business information and book publishing businesses all operate in highly competitive markets, which are constantly changing in response to competition, technological innovations and other factors. We may be required to invest significant resources to further adapt to the changing competitive environment. 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. 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.

Illustrations of the competitive threats we face at present include:

— Students seeking cheaper sources of content, e.g. online discounters, file sharing, use of pirated copies, used books or re-imported textbooks, along with the open source initiative are causing us to lose sales and putting downward pressure on textbook prices in our major markets.

— Competition from major publishers, technology companies and other educational material and service providers, including not for profit organizations, in our US educational solutions and assessment businesses.

— Penguin: 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.

— FT: 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.

- People: the investments we make in our employees, combined with our employment policies and practices, we believe are critical factors enabling us to recruit and retain the very best people in our business sectors.
- Financial Systems and Processes: we are embarking on a substantial transformation programme based around shared and common processes and services, 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. We cannot be certain that we will realise the anticipated savings in full.

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. 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.

At Penguin, changes in product distribution channel and/or customer bankruptcy may restrict our ability to grow and affect our profitability.

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.

Penguin’s financial performance could also be negatively affected by the bankruptcy of a major retail customer which disrupts short-term product supply to the market as well as results in a large debt write off. The economic slowdown has increased this risk in the short term.

Reductions in advertising revenues and/or circulation will adversely affect the profitability of our newspaper business.

Our newspaper business has diversified its revenue streams but remains dependent on advertising income. The business has high operational gearing; relatively small changes in revenue, positive or negative, have a disproportionate effect on profitability. Any downturn in corporate and financial advertising spend due to the economic slowdown will negatively impact the results of the *Financial Times* newspaper. The outlook for advertising markets, which remain subject to macroeconomic conditions, is not clear and visibility is low.

Our customers can increasingly access their information through different channels and from alternative suppliers. This allows our newspaper businesses to distribute and monetize their content in new ways. Our ability to offer a range of content channels provides some protection against the risk of decline of any one format. For example, we might see a decline in print circulation in our more mature markets as readers migrate online or via mobile platforms, although we see further opportunities for growth in our less mature markets. However, if the migration of readers to new digital formats occurs more quickly than we expect, this is likely to adversely affect print advertising and our newspaper’s profitability.

Operational disruption to our business caused by 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. 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.

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.

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 2009 we acquired Wall Street English, China's leading provider of premium English language training to adults, for £101m. In South Africa, the company received regulatory approval for the acquisition of the majority stake in Maskew Miller Longman (MML) which we intend to integrate with Heinemann South Africa.

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.

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.

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 Interactive Data and 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. The failure to recruit and retain staff with relevant skills may constrain our ability to grow as we combine traditional publishing products with online and service offerings.