Our performance: 2012 financial overview continued

Statutory results

Our statutory results show a decrease of £603m in operating profit to £515m, from £1,118m in 2011, reflecting the absence in 2012 of the £412m profit on the sale of FTSE International in 2011 and the £113m closure-related costs on Pearson in Practice in 2012. Basic earnings per share similarly fell to 40.5p in 2012, down from 119.6p in 2011.

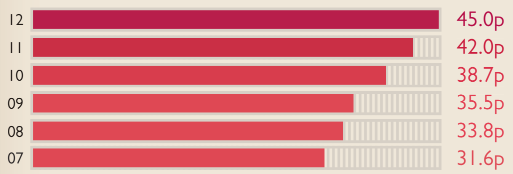
Balance sheet

Our net debt increased to £918m (£499m in 2011) reflecting acquisition investment of £759m and sustained organic investment in our business, partly offset by cash generation. Since 2000, Pearson's net debt/EBITDA ratio has fallen from 3.9x to 0.9x and our interest cover has increased from 3.1x to 18.0x.

Dividend

The board is proposing a dividend increase of 7% to 45.0p, subject to shareholder approval. 2012 will be Pearson's 21st straight year of increasing our dividend above the rate of inflation. Over the past ten years we have increased our dividend at a compound annual rate of 7%, returning more than £2.5bn to shareholders. We have a progressive dividend policy: we intend to sustain our dividend cover at around 2.0x over the long term, increasing our dividend more in line with earnings growth.

Dividend per share paid in fiscal year Pence



Outlook: 2013

We expect the external environment to remain challenging for our developed world and publishing businesses in 2013 owing to a combination of cyclical and structural factors: pressures on education budgets and college enrolments; retail consolidation; the shift in our business model from print sales to digital subscriptions; changing consumer behaviour and a dynamic competitive landscape. In general, we expect market conditions to remain favourable for our businesses in developing economies and education software and services.

In order to reshape the company to take advantage of significant growth opportunities, we will expense approximately £150m of restructuring costs in 2013 (the restructuring cost will be approximately £100m net of cost savings achieved in the year). This investment has two objectives:

1. to accelerate our transition from print to digital business models and from developed to developing economies; and
2. to separate Penguin activities from Pearson central services and operations, and to reduce fixed cost infrastructure in Pearson, in preparation for the Penguin Random House merger.

We expect this transformation programme to generate approximately £100m of annual cost savings from 2014. In 2014, we intend to reinvest the £100m of cost savings in the organic development of our fast-growing digital, services and emerging markets businesses and further restructuring, including the Penguin Random House integration. We expect these businesses to contribute to faster organic growth, improving margins and improved cash flow and capital intensity from 2015. The precise phasing of restructuring costs and benefits will depend on timing of completion of the Penguin Random House combination, which remains subject to regulatory approval and which we expect to complete in the second half of 2013.

At this early stage in the year we expect Pearson 2013 operating profits and adjusted EPS to be broadly level with 2012 before expensing these restructuring costs (compared to 2012 adjusted EPS of 82.6p under revised IAS 19 which we will adopt in 2013) and including Penguin for the full year.

This guidance is struck at the 2012 average exchange rate of £1:$1.59 and reflects the following outlook:

Education

In Education, we expect to achieve modest revenue growth in 2013 with margins similar to 2012.

North America

In North America, we anticipate modest growth with challenging cyclical and structural market conditions in publishing offset by growth in digital and services.

International

We expect our International education business to show good growth. Austerity measures will continue to affect education spending in much of the developed world and we expect a slower year for UK examinations and qualifications. However, we see significant opportunity in emerging markets in Asia, Latin America, the Middle East and Sub-Saharan Africa – which together accounted for 45% of our International education revenues in 2012.

Professional

Our Professional education business will reflect the closure of our UK professional training business and continued growth from our professional certification business.

FT Group

We expect the FT Group to benefit from continued growth in digital and subscription revenues in 2013 but advertising to remain weak and volatile with profits reflecting further actions to accelerate the shift from print to digital. Mergermarket will benefit from its high subscription renewal rates, with market activity likely to boost its core product offerings.

Penguin

As previously announced, subject to regulatory approval, we expect Penguin's combination with Random House to be completed in the second half of 2013. We believe that the combined organisation will have a stronger platform and greater resources to invest in rich content, new digital publishing models and high-growth emerging markets. The organisation will generate synergies from shared resources such as warehousing, distribution, printing and central functions. We expect market conditions to remain similar to 2012 with a tough environment in the physical bookstore channel but helped by good growth in digital.

Interest and tax

In 2013, our net interest charge to adjusted earnings will exclude pension income and charges following the adoption of IAS 19 revised and be similar to the £65m reported in 2012 on a comparable basis. We anticipate our P&L tax charge against adjusted earnings to be in the 23–25% range with our cash tax rates around the same level.

Exchange rates

Pearson generates approximately 60% of its sales in the US. A five cent move in the average £:$ exchange rate for the full year (which in 2012 was £1:$1.59) has an impact of approximately 1.4p on adjusted earnings per share.