Pearson 2023 Full Year Results

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Pearson 2023 Full Year Results

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Good morning everyone and welcome to Pearson's 2023 Preliminary Results. Today we will host a presentation followed by a Q&A session. There'll be two ways to submit your questions. If you'd like to ask your question personally, please use the numbers that are displayed on screen. These lines will be open following the main presentation. Alternatively, please type your questions into the questions tab at the top right of the screen and we will address them in turn at the end. And with that, I will hand over to Omar.

Good morning, everyone. I am Omar Abbosh. It is good to be here with you today for my inaugural results presentation. I am proud to be here representing Pearson and its people who are so committed to helping learners around the world. First off, I will make some introductory comments sharing my early impressions of Pearson. Next, Sally Johnson, who's here with me in London, will take us through our business unit financials for 2023. Then I will conclude the presentation part with our 2024 strategic priorities, and after that, we will open up for questions where we are joined by Art Valentine, Gio Giovannelli, and Tom Ap Simon from our leadership team.

Financials

Let me begin with our financials. It has been yet another year of strong operational and financial performance for Pearson. Once again, we have surpassed initial expectations with underlying sales growth of 5% and operating profit up 31% to 573 million pounds. 2023 also saw significant margin expansion from 12% in 2022 to 16% this year. This is the strongest margin Pearson has seen since 2013.

Our cash position is excellent with a 74% increase in free cashflow and 102% operating cash conversion. As a sign of our continued confidence in the cashflow growth of Pearson, I am pleased to announce an extension of our share buyback by an incremental 200 million pounds. These results reflect exciting progress across our whole business, and I want to call out the especially strong financial contributions from Assessments and Qualifications and English Language Learning.

Overall, this out-turn puts us in good stead moving forward and helps us invest in further growth opportunities that will ensure we drive continued shareholder value expansion in the coming years. As you know, I joined Pearson eight weeks ago. Let me tell you what I have been up to. I spent over 90 hours with leaders from across the businesses and corporate functions in hourly one-on-one sessions. I have also had in-depth conversations with over two dozen customers and spent time with each of my leadership teams' own management teams to hear their perspectives on many aspects of our business, and also so that I can dig into our operations.

I spent time with several of our investors as well as other participants in our markets such as private equity owners of educational and learning assets. The simple reason for this work is to establish priorities and their associated actions. These growth-oriented priorities address strategic operational product, people related and cultural topics. I'd like to share a handful of observations from my first weeks at Pearson. The headline is that I believe Pearson is a rare type of company with the ability to deliver long-term sustainable growth while also pursuing a purpose that genuinely helps the lives of millions of people around the world.

How do we do this? Well, at Pearson we do three things. We create and curate world-class learning and assessment content. We distribute that content digitally and through physical materials to millions of users globally, and we help individuals, employers, and institutions build and verify skills. So underpinning these three activities is the trust that the Pearson brand carries. I found that customers around the world, often in high stake settings rely on the products and services that we provide and really place a great deal of trust in what we do.

The Foundation for our Continued Momentum to Drive Profit Growth

This is the trust in the quality of the content and assessments, trust in the efficacy of the learning and trust in the reliability of the outcomes. This leads to deep and long-lasting relationships with many of them giving us unrivalled competitive advantage in the market. We have incredibly mission-driven people at Pearson and they fuel our purpose and culture. For sure, our employees are experts in their various fields, but what really stood out to me in my many conversations is how deeply they truly care about helping other human beings make progress in their lives. Those of you who've studied culture will understand how hard that is to manufacture.

I am pleased to see that we are well on the way to embedding digital and technology capabilities into the DNA of our company. More than 80% of our products and services are now digital or include digital components, and this is true for our Pearson Test of English delivery view assessments, our Higher Ed courseware, and most recently, in a first for the UK, in our GCSE qualifications. We have about 3000 technologists working across the business to continually improve end customer experiences with the application of digital and AI in our products and services.

Finally, we are sitting on vast data sets that have tremendous value in the development of next generation AI models. In 2023, these included 230,000 tutoring sessions, 347 billion total user engagement points across Higher Ed, 1.2 billion student interactions at our Connections Academy, 1.4 billion exam items at VUE where we deliver 20.7 million exams, 366 million unique data points across our Q Interactive Clinical platform and around 260 billion data points for Mondly.

First Impressions

On top of this, in Workforce Skills, we analyse 8 to 12 million job ads per month across the US, UK, Australia, and Canada, and map each job ad to an occupation and the skills found in our skills ontology. In summary, our brand trust, customer relationships, trusted IP mission-driven people and culture, technology assets and products, plus these huge data sets provide the foundation for our continued momentum to drive profit growth into the future.

Three Reasons I Joined the Company

To close off this introduction, my early time here has increased my conviction in the three reasons that I chose to join Pearson as CEO. Firstly, Pearson is a strong company, one that is performing consistently well and has good growth optionality for the future. Today's results are a continuation of our recent growth track record and our consistent performance, which underpin my confidence.

Second, I was drawn to Pearson by its unique and compelling purpose. Our ability to help people on their learning journey quite literally changes their lives. We have countless examples of this which we will share more of. We truly help people live the life they imagine - precious few other companies can claim this.

Thirdly, our world is at an inflection point with AI. The next decade will be all about the application of AI in business, in our communities and in our individual lives. The opportunities to use AI as a tool for better learning while driving growth in our business are immense. We are well positioned to take advantage of this future. So in summary, Pearson is strong, has an incredible mission in the world that our people are utterly committed to and is positioned to be a winner in AI. Let me hand over to Sally here.

Sally Johnson

Chief Financial Officer, Pearson

Financial Review and Outlook

Thank you, Omar, and hello everybody. I am going to come on and talk about guidance in a moment, but first, I want to reflect on the strength of our 2023 results. We exceeded the profit expectations that we had at the beginning of the year by 30 million pounds, increasing profit by 31%. We secured 120 million pounds of cost savings, which alongside the margin from sales growth increased our margin from 12 to 16% and we have generated an operating cash conversion of 102%, increasing free cash flow by 74% despite one-time reorganisation costs, which will fall away in 2024.

It is this continued financial progress that underpins our confidence that we will be able to deliver another good year in 2024 and that we are on track to meet our 2025 guidance.

Adjusted earnings per share increased 12% to 58.2p reflecting the strong increase in operating profit and reduced share count from our share buyback. This was partially offset by interest and tax given the one-off provision benefits we had last year. Net debt increased slightly with strong operating cash utilised by the acquisition of PDRI and dividends alongside the share buyback.

Balance Sheet

Our balance sheet remains strong, providing us with a firm platform from which to invest for future growth whilst continuing to distribute cash to shareholders through our dividend policy and where appropriate, through ad hoc buybacks. Given our strong 2023 results and our confidence in the future, the board are proposing a 6% increase in the final dividend for a full year dividend of 22.7p.

In 2023, we delivered underlying group sales growth of 5%, excluding OPM.

By division Assessments and Qualifications grew 7% driven by a 10% growth in VUE, particularly in the IT and healthcare sectors. We saw good growth across US Student Assessments, Clinical and UK and International Qualifications due to new contract wins, government funding and price increases.

Virtual Learning decreased 20% for the full year, primarily due to the expected decrease in OPM. Virtual schools declined 2% for the full year with lower enrolments due to COVID normalisation in the 2022/2023 academic year and the loss of a larger public school in the 2023/ 2024 academic year. This was partially offset by an improvement in funding.

Higher Education was down 3% for the year, in line with our expectations. In the US, sales declines were driven by a loss of adoptions to non-mainstream publishers in the first half of the year, as well as pricing mix. There was strong growth in Inclusive Access with 22% sales growth, and we also delivered 2% growth in platform units.

English Language Learning delivered outstanding growth of 30%. All three segments delivered with PTE the standout contributor. Test volumes were up 49% against the backdrop of favourable migration policy in Australia and market share gains in India.

Workforce Skills grew 11% for the full year with solid performances in both Vocational Qualifications and Workforce Solutions. Strategically, we won several contracts in VUE aided by our acquisition of PDRI. We extended our onscreen exams and we drove growth in our digital platform in Clinical. Our renewal rate in VUE remains strong at 94%, down slightly from last year due to one particular factor.

In Virtual Schools, we launched our careers pathway program in five schools with more to come in 2024. This important initiative builds synergies with our workforce focused businesses and supports future enrolment growth. It will also enhance the consumer's experience in a business where we already have a really high NPS score of 67, and we are also pleased to have recently secured new schools in the States impacting the 2023/ 2024 and 2024/2025 academic years, providing us with a strong base for future growth.

In Higher Education, we improved our technology support leading to better NPS score amongst faculty. Our new go-to market strategy has led to higher retention rates and new adoptions. We launched generative AI study tools with select titles for Pearson+ and Mastering, and we will extend this for Fall 2024 to more than 40 titles. Pearson+ subscriptions passed the one million milestone and we monetised Channels for the first time.

In English Language Learning we won recognition for PTE in Canada for both student direct stream and immigration purposes.

In Workforce, we want a contract to provide BTEC to the Jordanian Ministry of Education and we are seeing success across digital credentialing and strategic workforce planning solutions where we have several new contract wins, including Cleveland Clinic and ServiceNow.

Summary

So in summary, we are winning contracts and investing in our range of products to drive sustainable profitable growth. Group profit grew 31% on an underlying basis to 573 million pounds with significant margin progression increasing 4% to 16%. This was driven by delivery of 120 million pounds of cost efficiencies and operating leverage on sales growth partially offset by increased inflation and investment at a divisional level.

Assessments and Qualifications grew its margin to 22% through operating leverage on sales and margin and OPEX efficiencies, partially offset by inflation. Virtual Learning margins increased to 12% due to cost efficiencies and the disposal of POLS. Higher Education margins increased to 13% with the 2023 cost efficiencies weighted towards this division and offsetting the decline in sales and inflation. English Language Learning margins grew to 11% through operating leverage on sales, partially offset by increased investment and inflation. And Workforce Skills was loss making as we continued to invest in the business with a focus on delivering modular personalised offerings to our pipeline of clients, leveraging our powerful technology stack.

Free Cashflow Generation

Our free cashflow generation is one of the key strengths of our business model. We have maintained a sharp focus on increasing free cashflow as we continue to invest behind opportunities to drive future growth that will support returns for shareholders. We had a strong cash performance with cash conversion of 102%, and operating cashflow of 587 million pounds. This was driven by the trading performance, great cash collections and reduced investment spend in Higher Education connected to the cost efficiency program.

As previously discussed, the capital investment profile continues to change with CapEx reducing and focus shifting to investment in product development. The 186 million pound increase in operating cash has driven a 165 million increase in free cashflow. Free cashflow conversion of 93% is lower than the 102% operating cash conversion given one time reorganisation costs, which will fall away in 2024. I know many of you like to trace the detailed moving parts across the cashflow, and so you can find a reconciliation to the various disclosures in the prelims in the appendix of this presentation.

Looking at our balance sheet metrics, net debt increased slightly with strong operating cash utilised by the acquisition of PDRI and dividends alongside the share buyback. Leverage remains comfortable at one times net debt to EBITDA. And as a reminder, when we think about the application of our capital allocation policy, we calculate headroom against our most stringent rating agency metric, which is currently equivalent to a ratio of approximately two times. Return on capital was 10.3% compared to 8.7% in 2022, and we continue to be disciplined in our investments and rigorous about securing required returns.

Capital Allocation

Turning to capital allocation, we have got a disciplined capital allocation policy with a focus on maintaining a strong balance sheet investing both organically and inorganically, paying a progressive and sustainable dividend and returning surplus cash to shareholders. We have almost finished the 300-million-pound share buyback we announced last September, and today we are announcing its extension by 200 million pounds given the strength of our cashflow in 2023 and expectations for 2024. Administratively, this will commence as soon as possible.

Going forward, we will continue to apply our capital allocation policy, and through strong cash generation, we will continue to invest behind opportunities to drive further growth and create value for all our stakeholders.

Outlook

Moving to the 2024 outlook, we expect group underlying sales growth, adjusted operating profit and tax to be in line with current market expectations. Given our share buyback and its extension announced today, our interest charge will increase to circa 45 million pounds. We also continue to expect to achieve group sales growth of mid-single digits excluding OPM and the strategic review businesses across the 2022 to 2025 period with margins of 16 to 17% expected in 2025.

Divisional Expectations

Divisional expectations across that period remain the same, apart from Workforce where we expect double digit growth and in English, where we expect growth in the teens. Given the changing shape of the group, as you think about the role of FX and our guidance, you should now assume that a one cent move against the pound equates to around five million pounds of adjusted operating profit.

Growth Opportunities

I want to turn now to the considerable growth opportunities we have across the business. I will take each division in turn.

We continue to expect Assessments and Qualifications to grow sales at low to mid-single digits for 2024 with opportunities for increased growth beyond that. In Pearson VUE, we will finalise the successful integration of PDRI and expand into adjacent markets, accessing the technology cert prep market. We are going to expand our qualification business internationally and use our technology abilities to launch innovative future ready assessments.

Clinical offers us several opportunities as the market expands given macro trends. We will continue to invest in our digital intellectual property, which drives our competitive advantage and in adjacent opportunities such as the application in pharma clinical trials.

For Virtual Schools, we expect enrolments to be lower in the 2024 to 2025 academic year due to the loss of a major school in that period, and for annual sales to be down a similar level to 2023. We have recently secured those new schools in the States impacted by the 2023/2024 and 2024/2025 academic years, and whilst this will not be material for 2024, it will help the business to return to growth thereafter. The other factor driving growth will be the Career Pathways program with an additional 15 schools in 2024.

We expect Higher Education to return to top line growth in 2024 as we receive a full-year benefit from the implementation of our new go-to market strategy with continued momentum from Pearson + . We will also benefit from continued investment in our digital platforms, Channels and AI capabilities. We expect margins to improve further in Higher Ed with further cost efficiencies partially offset by above-the-line restructuring charges in 2024.

In English Language Learning, we continue to expect high single digit growth for 2024. We will see continued growth in the Pearson Test of English and in the institutional market through selling end-to-end solutions that combine courseware with assessments and certification. Mondly will grow through platform improvements and the introduction of Workplace English.

For Workforce Skills we will achieve high single digit growth as we drive further international expansion of our Vocational Qualifications and continue to make headway with our Workforce Solutions business.

Phasing and Cash

In terms of phasing, you'll remember the weighting of growth to H1 compared to H2 for the assessment businesses last year. This weighting will realign due to the comp as well as the timing of product releases. There will also be a weighting of growth to Q1 from Q2 in Virtual Schools due to the timing of funding and in Higher Ed, we expect H1 2024 to mirror H2 2023 and growth in H2 2024. Cash will continue to be a focus and we expect to achieve a 95 to 100% free cashflow conversion rate given that high operating cash conversion with no one-time reorganisation costs anticipated this year. We are assuming there is not a material divergence between the FX rate used to translate the P&L and cash flows.

Summary

So in summary, we have achieved financial expectations in 2023. We achieved 120 million pounds of cost savings, expanding margin by 4% to 16%. We are on track to meet expectations in 2024 and remain committed to our targets out to 2025. We have a strong balance sheet providing optionality and are extending our share buyback by 200 million pounds, and we have improved our free cashflow and expect 95 to 100% conversion in 2024. And with that, I will hand back to Omar to bring us to a close.

Closing Remarks

Omar Abbosh: Thank you, Sally. As you've heard, we have delivered strong, steady progress across the group, both in terms of our financial results and our business momentum. We fully intend to build on this track record of execution by continuing to deliver on the promises we make to learners, customers and shareholders. So for 2024, we are laying out three strategic priorities for the year.

2024 Priorities

Firstly, we will deliver on our current 2024 market expectations for sales growth and operating profit with an intense focus on organic growth and execution. This is about building an ever stronger performance culture, sales disciplines, and customer experience orientation. Secondly, we are sharpening our focus on the enterprise market. This is a large multi-billion-dollar market with no dominant player presenting us with a good opportunity. My past experience with hundreds of companies' connections with dozens of enterprise CEOs, plus my recent various customer conversations have made it clear to me that Pearson has many of the capabilities that can help organisations with a challenge ahead of building an adaptable relevant workforce that is properly augmented by AI.

I'd like to thank Mike Howells for his leadership of the Workforce division, which has been at the centre of the capabilities we have built to date, and I look forward to welcoming Vishaal Gupta as the new president of Workforce Skills whose deep experience in enterprise sales leadership will be valuable to us in our next steps and making the most of this opportunity. Finally, we are increasing the intensity by which we infuse our products and services with a wide range of AI capabilities to ensure that we lead on innovation for our end consumers, for example, across Pearson + and our courseware platforms.

Everything that you've heard today points to a bright and exciting future for Pearson. What Pearson does matters to the world. So it is imperative that we use our strengths to continue building a company that drives value growth so that we can confidently pursue our purpose of adding life to a lifetime of learning and therefore benefiting the world. With that, Sally and I, along with Art, Gio and Tom, will be happy to take your questions. Operator, over to you.

Q&A

Operator: Thank you. To ask a question, please press star followed by one on your telephone keypads if you have dialled in on the phone lines today. We have the first question from Luke Holbrook of Morgan Stanley.

Omar Abbosh: Hi, Luke.

Luke Holbrook (Morgan Stanley): Yeah, good morning, everyone, and welcome, Omar. My first question is just on the buyback, how did you settle on 200 million as the right amount for the buyback? Why potentially not more, and I have just seen you put a press release saying that will go through till August. And then secondly, just on the Workforce Skills segment, it looks like you channelled in maybe 15 million pounds extra of investment than what the market was expecting through the second half of last year. Just interested to hear where that investment was channelled into and are we to expect any change or significant change in strategy following the new ahead of the segment? Thank you.

Omar Abbosh: Thank you very much, Luke. I will just say one little word and then I will hand over to Sally on the buyback. I think the message I'd like you to take is simply that our free cash flows are strong. We are confident that they will continue to be strong, and we just wanted to make sure that the market knows that we will continue to be very prudent, careful stewards of shareholder capital and that is it. But Sally, do you want to dig into that a little bit more?

Sally Johnson: Yeah, sure. I would not read too much into 200 versus 300. It is about half of the free cashflow that we are expecting to make this year. So we have got an operating free cashflow conversion that is really, really strong, and then in applying our capital allocation policy, we have decided to make that share buyback.

Omar Abbosh: And then on the Workforce Skills investment from last year.

Sally Johnson: Sure, we invested in Workforce Skills about what we were expecting to at the beginning of the year. I think probably in terms of that profit piece, it was the growth in sales where if you remember, we pivoted in the middle of the year from the approach that we had had to the more modular approach and therefore, the operating and leverage on sales was not quite what we had expected. But I think the thing that I want to underline here is that we are very excited about the growth that we have in Workforce Skills. The market opportunity is absolutely there and the growth that you see in the future will be strong with strong operating leverage coming as well. So this year or 2023 is really about that investment spend.

Operator: Thank you. We now have Sami Kassab with BNP Paribas.

Sally Johnson: Hey, Sami.

Sami Kassab (BNP Paribas): Thank you very much, and good morning, Omar. Good morning, Sally.

Sally Johnson: Morning.

Sami Kassab (BNP Paribas): I have three questions please. First, Omar, what are your current views in terms of the risks and opportunities in Virtual Schools, please, in the context of regulatory risk in particular. Secondly, what impact would you expect on the Higher Ed growth if the US Department of Ed was to go ahead and make inclusive access an opt-in rather than the current opt-out model? And lastly, given your strategy of investing to go into test prep at VUE, how do you expect margins at A&Q to develop in 2024 and 2025? Can they continue to expand or will they briefly decline as you increase investments there? Thank you.

Omar Abbosh: Thank you very much for those questions, Sami. It is good to hear you. I am going to go with the first two to Tom, and then the third one I will pick on Art. So Tom, do you want to comment on how we are seeing the risks and opportunities in Virtual Schools first please?

Thomas Ap Simon: Yeah, thank you, Sami. A few thoughts really from our perspective, if you take a step back, this is a business that is now 30% bigger in terms of students pre pandemic NPS is up, academic outcomes are up. Obviously, we have lost the two schools which have impacted growth. As Sally highlighted, we are thrilled with the two new school wins that we have got and we see that the underlying performance drivers in this space in terms of improved understanding of the space, better awareness of what virtual schools can do for students to continue to support the growth that we are seeing in the future. So we feel good about that.

In terms of Higher Education and the impact of the existing DOE discussions, obviously, it is something we are monitoring very carefully. Clearly, it is ongoing at the moment. Clearly, inclusive access is an important part of what we do from a business model perspective that we feel good about our underlying prospects and we will wait to see what happens. And regardless of that, those regulations are unlikely to come in until 2025 or 2026 depending on what happens with those. So we still feel good about our underlying opportunities to grow in Higher Education.

Omar Abbosh: Thank you. Tom. And Art, do you want to comment on VUE and margins?

Arthur Valentine: Yes, absolutely. Sami, you are dead on. Entering more forcefully into that test preparation space, excuse me, and taking advantage of the traffic we already have coming to view to receive those certification tests is an important part of our growth pillars. The margin impact of that is contemplated already within the guidance that we are giving. So the strong performance of the business absolutely gives us the ability to achieve those growth plans while delivering on the margin guidance that Sally already gave before. So all good.

Omar Abbosh: Thank you, Art. Back to you, operator.

Operator: Thank you. We have the next question from Nick Dempsey of Barclays.

Sally Johnson: Hey, Nick.

Nick Dempsey (Barclays): Yeah, good morning, guys. So first of all, just in terms of your guidance on the return to growth in Higher Education, I think Sally said that the first half of 2024 we will perhaps be down in the same sort of bracket as second half 2023 minus 4%, and then first half in 2023 was 44% of the year. So I am kind of backing out that you need to grow at 4 to 5% in the second half of 2024 to get to your guidance. Can you just talk about what's giving you visibility on that? It has always been a market that is been quite hard to predict at this point of the year. Is it share? Is it price? Is it the AI elements? What's making you think you can grow four to 5% in the second half of 2024?

Second question, just want to look at the divisional organic growth verbal commentary for 24 for each division overall, we are guiding to in line with consensus, but each of the divisions is kind of the same or a bit worse than consensus as far as I understand it. Is there a bit of element of caution built into those verbal ranges for each division or am I missing something there? Then the third question, just Omar, are you happy with the portfolio as it stands or could disposals form any part of your strategy? And also, are you happy with how well invested the group is across all of the areas where you might be able to drive organic growth?

Omar Abbosh: Thank you very much, Nick. I think, Sally, those two first ones are a bit guidance oriented, so maybe you should take them.

Sally Johnson: Yeah, so I am going to take the middle one first and then I will touch on some of the elements of Higher Ed and turn over to Tom to talk about what he's seeing from a market point of view. And then we will come back to you for the last one. So in terms of divisional organic growth guidance, I am giving ranges, but we are really confident with hitting each of those and overall, I can't see your model, but really confident on hitting the group, which is about 4% organic growth revenue for 2024, and that is how we have modelled things for the year. So I do not think you are missing anything, but happy to follow up on the detail that you've got if that is helpful.

And then in terms of Higher Ed returning to growth and the phasing, probably a little bit less of a decline in the first half of the year than you quoted. I was kind of trying to give the shape of it rather than the actual numbers, but you are quite right. We will see growth in the second half of the year and the things that you call out are all contributory factors to that. So share growth, AI really important to that. But also the product enhancements that Tom and the team have been making, I am sure Tom will come and talk about the things that he's been doing in the sales team, price and element, but probably not a particularly strong one within that. So Tom, do you want to talk about what you are seeing in the market at the moment?

Thomas Ap Simon: Yeah, sure. As Sally I think highlighted, there is a broad range of factors. We know that enrolment stabilised in 2023 and grew slightly, up 1%, in the space that we were in. We know how we started the year in terms of January and February from a performance perspective, and we are pleased with that. Fundamentally, our performance in 2024 is driven by a lot of the things we did in 2023. So the new operating model we put in place with GMs driving performance in math, science, business and economics, all of those require slightly different strategies. We have got that in place now. We are very excited about the performance of the new sales team. We have done a lot of work around sales operations to really get a lot sharper there. But from a product perspective, last year we didn't have as an exciting a product lineup as we do this year.

So as we think about some of the investments we have made, for example, in interactive reading assignments, things like we have done with the AI study tools, we are seeing really good and really strong engagement from faculty in the market on those. And I am getting very regular feedback from the sales team on that. And then the other point I would make is that the K-12 adoption cycle, that is something we have reasonably good visibility into at this stage of the year. That is a more positive trend for us in 2024. So to summarise, the operating models in place, the sales team is betting down and doing a better job from an execution perspective. The product lineup is better and we have a firm view on the macro environment.

Omar Abbosh: Tom, thank you very much. And actually, Nick, I am going to just pile onto what some of what Tom said. So I have double clicked a bit with Tom and his team and what I can tell you is the sales operations precision in that team is very good. The folks there are really on their market. They understand exactly the dynamics, the competitive dynamics, the product dynamics, and exactly where customers are at. And under Tom's leadership, I feel very confident about where we are headed in Higher Ed.

On your other question that you asked me about portfolio and how we are investing across that portfolio, I will say a couple of things. there is incredible power in the breadth of capability that Pearson brings. So if you think about the world from a customer segment point of view, so the K-12, the Higher Ed, the workforce, individual citizens, our offers span all of those segments. If you think about it from a domain point of view in terms of creating content, learning-based content, assessment-based content, all the solutions and technologies that you need to provide to the delivery institutions of all that learning. Again, we have a lot of offers and capabilities and products that span those domain areas. And so, I am actually very happy with the breadth that we can bring because it can be a very forceful component of our strategy.

Now, the other thing about the portfolio is that our business units give us incredible clear line of sight of accountability. We have a very good match of responsibility and authority in each of our business units with clear, strong, intensive regime on each of the management teams so that people know what they are solving for and they know what they are on the hook for. And I like that as well. I like the clarity there, but if you ask me to think going forward, I will share with you a couple of my philosophies.

Of course, as a management team, you'd expect us to leave no stone unturned. We are going to look at all strategic options and we will do that all the time. And if great opportunities arise, we will jump on them. But my focus is growth, and I specifically believe in focus to scale. You can get more growth when you are incredibly focused. So the way I look at the portfolio all the time is to say, are we really focused in the areas where the profit pools are moving and are we having a good enough insight into our market so that we really put our energy and our resource where it ought to be for the future. Back to you, operator.

Operator: Thank you. We now have a question from Tom Singlehurst of Citi. Hey, Tom, the line is open.

Tom Singlehurst (Citi): Yeah, good morning. Thank you for taking the questions. A couple if it is okay on English Language Learning. I know we have only got the ramp up of the non-student part of the Canada contract from the beginning of this year, but can you just talk at a high level how you think about the risk associated with the geopolitics of migration and scope reductions in quotas for immigration in markets like Canada and how that follows through to PTE? It would be great if you can just talk about that a little bit.

Second question on the AI study tools, that program that you initiated at the beginning of this academic year fairly looks like it is going quite well, it is expanding rapidly. I am interested in whether that is primarily a tool to just drive engagement and then bring with it adoption share and more usage or whether it is something that could drive meaningful revenue in the short term or medium term. And then final question on I suppose political risk. Sammy mentioned regulatory risk in Virtual Schools, which I am not sure there is, but at the same time, the point with all of your activities to a degree is that makers can choose to interfere as they perhaps might do with inclusive access. How should we think about that risk running into an election year? Thank you.

Omar Abbosh: That is great, Tom. Thank you very much. On the first question, I am going to go straight to Gio and then we will pick up on AI next. So Gio, could you pick that one up please?

Gio Giovannelli: Yeah, sure. Thank you, Tom. The high stakes assessments remain an exciting opportunity for us. The policy changes that you are referring to in 2024, we see them as a one-off normalisation of inflows of students and migrants after the exceptional intakes that we had post pandemic and that we had anticipated. But first of all, the impact and the timing of that normalisation depends on further regulation and could take time. Second, there is a long-term growth in this segment that will continue because students and migrants contribute meaningfully to these country's economies.

Just for example, a recent survey that we published in a couple of weeks, Australia says that 72% of PTE test takers are employed in high skilled jobs and they make 38% more money than the country's median salary. So you can understand the impact of that. Now, a couple of factors to understand the impacts. Number one, people usually need to take the test before they apply to a visa, so there is not a linear correlation between the number of visas available and the tests that are taken.

The second thing is these policy changes may result in actually an increased level of proficiency required to get a visa, and this would mean that people have to test more time to get to the English level required, and so that would turn into increased number of tests. The other thing to take into account, we have been growing share over the last three years, and we think there is still opportunity to grow share even if the market doesn't grow as much as in the past. And the reason for that is we believe we give an end-to-end experience to our customer, in this case is the test taker, which is superior to competition in terms of the way you find the test, the way you book it, the way you take it all in one go, and the way you are assessed fairly and without bias, and then the way you get your test results very quickly and the way you can use them. they are basically accepted everywhere in the world.

Now, the other and last point is that we have unlocked other growth opportunities in the PTE space and we believe we can continue to do that. So in summary, those factors that you mentioned are real, but we feel confident about the growth that we have, the high single digit in 2024. And just to bear in mind, more than half of the revenue that we have in the division is outside of the high stakes assessments. And in that space, we have been growing double digit every year consistently as we have in PTE in the last three years. So we think we have a track record and a team that knows how to innovate and to execute in there. Thank you, Tom.

Omar Abbosh: Gio, thank you very much. And Tom, I just want to emphasise a little bit what Gio was saying there is that of course we are incredibly aware of the macro trends of what's happening in the world of migration, but even when the trend in is trending downwards, that doesn't mean the demand for migration is trending downward and it is the demand for migration that drives the test takers. And so, that is something that I think you should be cognisant of. Okay. On the AI topic, Tom, I'd like to come to you with this question of engagement versus monetisation that Tom is asking us here. Maybe talk about us a little bit from your courseware perspective, but also from Pearson + as well, please.

Thomas Ap Simon: Yeah, absolutely. I think the point I would make here is that we are incredibly excited by the engagement we are seeing with these tools today, both in Pearson + and in our courseware products. We had a meeting with some customers a week ago, and the feedback from the customers as they saw the new study tool was that they were blown away because it allows them to teach differently.

So as you think about the fact that in any sort of higher education institution today, there is a lot of time that faculty are spending on getting the basics right with students and helping them understand. What we are increasingly seeing is that the role of faculty is changing. So this gives them more of an opportunity to move from a provider of the basic instruction to starting to facilitate critical thinking differently is changing the role of faculty and we are helping them do that.

So it is changing the way they think about content, it is changing the way in terms of how they think about working with content. And it is essentially benefiting from our rich data sets, aligning that to our AI driven study tools and providing really exciting additional supports and outcomes for students. Now, I think we are only in the foothills of what we can do with all of this, and so I am incredibly excited about how we leverage this technology through every element of our higher education ecosystem.

So not only do we have some of the tools in place for students this year, we are also building additional functionality into the platform from an instructor perspective as we think about how they create assignments. So we are using the AI to help them set up their assignments differently and think differently about how and where they curate assessments content to provide incredibly rich learning experiences for our students.

So we are incredibly excited about what we are doing. As you mentioned Tom, it'll be driving increased product usage, increased adoptions in the near term. And then obviously as we are thinking about our broader ambition and vision, we are very clear that everything we have to do in the higher education landscape and indeed across the company be heavily driven by bringing AI into our ecosystem and benefiting from that in terms of the additional hyper-personalisation it can bring to students, it meets students where they need to be and everyone learns differently.

And that is the power of AI, that it can help meet everyone where they are and provide that personalised learning. And what's also just funny on an anecdotal note, it can help anyone at two o'clock in the morning and all of our faculty, whenever they are talking about this, they always reference 2:00 AM as the time that somehow students are learning and that the AI study tools come into their own. So 2:00 AM is the new hour to be doing your homework.

Omar Abbosh: An always on tutor. Thank you, Tom. So you heard this concept of more telemetry in the product, capturing more data points for us that allow us to do more AB testing to constantly enrich the product. So yes, for sure, it will help with engagement, keeping people on our platform for longer. But as you can get the hint there from Tom, the more we are focused on real world problems like helping an educator understand exactly where a student's struggling, the more we can monetise as well. And you can expect to see more of that in the future. And then the last one there, Tom, on policymakers in Virtual Schools, how would you like us to think about that one?

Thomas Ap Simon: Yeah, look, I think Tom, as you pointed out, whether it is Higher Education or it is virtual schools, there is ongoing regulatory challenges across the whole education space. that is frankly one of the beauties of Pearson because we understand this incredibly deeply, whether it is in assessment, whether it is in K-12 from a virtual school's perspective, whether it is in higher education, it takes deep expertise to navigate all of the different things we do on a day-to-day basis. We have a really strong network of lobbyists both at the federal level and at the state level. We are monitoring these things all the time as part and parcel of life, and we do our best to be very proactive and think about this 12, 24, 36 months in advance. Of course, in a federal election year, there is always a chance of a bit more things happening in DC.

The obvious point I'd make about the K-12 market is that all of that is really driven at the state level. So there is going to be less that you see at the state level driven by DC compared to what you see at the set of the federal level. So we feel fairly good about what we are seeing at the moment in terms of our visibility into the market. As I said, we monitor this all very closely. We just have regular discussions with lobbyists on a weekly, monthly basis and whatever we are tracking, we are tracking, but we feel good about life at the moment.

Omar Abbosh: And then the last point I'd add on that, Tom, is that when you meet Lauren and the team who run Virtual Schools, their proximity to the market, their proximity to the state officials is incredibly helpful. And I think our being incredibly local actually is incredibly defensible position for us. Actually, I feel strong about it and I think it is easy to forget across this huge US marketplace. Only two national players, one of them is Pearson now. It was getting a bit confusing there with Tom talking to Tom. But anyway, I think I have figured it out. But operator, back to you please.

Operator: Thank you. We now have Adam Berlin of UBS on the line.

Adam Berlin (UBS): Hi, good morning. Hi, everyone. Three questions from me, please. The first question is for Tom Ap Simon. In Sally's presentation, she talked about some adoption wins. Can you just give us the examples? You may have to anonymise them, but can you just talk through one or two examples of where you won the adoption and why? And if you can make the examples around the big introductory courses – and we could get a sense of what's getting people to change to Pearson and how big that could be.

Second question is on English, I think you just said that only half of the revenue is from high stakes exams. Did you mean half the Pearson Test of English revenue or half of the whole of English revenue? And when you are talking about this growth highest single digit, what are you assuming about Australia and Canada? Do you think Australia volumes can still grow given the comps and the change in policy in 2024 and find a question for Omar on, I am just really interested in your view on the workforce solutions product that Pearson have built. Do you think it is fit for purpose and just needs to be deployed in the market, or do you think that based on the conversation you've be having, there is a bit of product development work to do until it is really ready for the market? Thanks.

Omar Abbosh: Thank you so much. Tom, you go first.

Thomas Ap Simon: Cool. So really like the question. So a good example is in one of our interactive calculus titles, and that is a new title that we have relaunched this year. It is a three-semester course. It is all video based as well as the e-text that you would expect. What we like about that product in particular and what's helped it win adoption so far is the integrated reading assignment. And this is where we bring the text and the formative assessment together so that you as a student or you as an instructor, it is all in one flow and that means that it is a read a little, do a little bit. So if you think about the pedagogical approach, we are then bringing the assessment together with the content right in one screen now as people are learning. that is a very powerful approach. And then aligned to that, it is the AI study tools as well.

So people have always appreciated the really outstanding pedagogical approaches that we have got that is now being backed up by more learning science driven AI tools to help as well as a different approach in terms of the way we scaffolded the product between the assessments as well as the e-text. That is a very powerful story that is really resonating strongly with faculty. And so I would say things like the interactive reading assignment as well as the study tools, but just opening up more conversations on campus, right? More and more faculty are curious and want to understand about what we can do here. And those two features in particular are really resonating in the market.

Omar Abbosh: Thank you, Tom. Gio, please.

Gio Giovannelli: Yes, thank you, Adam. The first part of your question is when I referred to the half of the revenue, I meant that we do recognise that there is policy restrictions in many of the receiving countries, but let's bear in mind that the beauty of ELL is that it has a very diversified revenue base. One of the interesting things is that more than 50%, actually 52%, of our ELL revenue come from areas that are not high stakes assessment and have grown consistently. that is the institutional and the monthly business. So that business we expect to continue to grow, as well as, as I said, I will not repeat the dynamics on the high stakes test.

On the second part of your questions, whether Australia volume can still grow. I think as I said, these restrictions that have been announced haven't really introduced in specific regulation yet. So we need to see what the regulation could be. Second thing is people will still want to immigrate or work on study. Australia is a fantastic destination to go and live. We will publish research in two weeks that has specifically to do with Australia, and it is very exciting news coming up there. People will apply to the test before getting an admission to university or an immigration visa. So that will continue to happen.

And also, if the policy change is, say for example, that you need a higher PTE score or actually all the scores because that is the way it works, people will need to retake the test more time to get to the desired score. And so what ultimately will impact in the demand of test is not a linear correlation. And then the third thing is in Australia we have grown share consistently. We have a high share, but we believe there are still margins to grow further. So I think that the ultimate effect on Australia volumes for us is uncertain, but there are different factors that point in the right direction.

Omar Abbosh: Thank you, Gio. And then, Adam, on the last question on Workforce Solutions, what I can tell you is a customer at Cleveland Clinic that I spent time with could not stop waxing lyrical about how amazing Faethm is and how it is at the heart of their workforce strategic planning for the company right down at the micro, not just skill level, but task level in the business to really understand how they need to evolve their workforce in the future. And actually,he was challenging us to stay on the front foot of innovation the way we have been for years. So actually, I just love that interaction with them. And that is a customer who is really on the front end of where the world is going. And I feel very confident about that. Similarly, I spent time with a customer at one of the huge hyperscalers on the west coast in the US.

Again, this lady who's explaining to me why she's chosen Credly to deploy across the entire workforce of that big company and how it is a key part of their way of the development of their own people. And really understanding in a granular way how that motivates, how that inspires, and also how frankly people can credentialise themselves as they want to move up and get promotions and develop their careers. So I am extremely confident that a lot of the assets that we have under the hood are very pertinent to this marketplace. Now, as you think about product going forward, there is never a day where you suddenly say, stop. I am done with the product. Any good product company is constantly evolving the product to meet customer needs, adding new innovations to monetise and increase value. And you can expect Pearson to do that as well. Operator?

Operator: Thank you. If you would like to ask a question on the phone lines, I remind you to please press star followed by one on your telephone keypad, and I would now like to hand it back to Jo for the online platform questions.

Jo: Thank you. So well, we have got four questions from Lisa from Goldman Sachs, but I think we have probably covered two of them, Lisa. So I am going to go for the remaining two. First one, losses worsened for Workforce Skills in 2023. Can you comment on the profitability to expect in 2024 given the slower than expected top line growth of high single digit, what's driving the slow down to high single digit growth for the division are seeing weakness in corporate demand environment of your products and not gaining enough traction? And then the second question is on A&Q margins very strong in 2023. Can you sustain further improvement from here and what is the operating leverage of the business?

Omar Abbosh: Thanks, Jo. I think, Sally, then a few.

Sally Johnson: Sure. Hi, Lisa. Nice to hear from you. So the profitability in Workforce Skills, I think I covered the 2023 piece. So thinking about 2024, I think you'll see the operating leverage on that high single digit revenue dropping through, and then us coming into a, first of all profitability perspective. I think the thing to do though is to look further out in Workforce Skills where we expect to see further growth. At the moment, I am guiding for the businesses that we have got right now. I think as we think about what more we can do with those assets, we will see higher growth out into the future. And of course, the operating leverage on that will really start growing profits as we look out the future.

So I think that is a way to think of Workforce Skills in terms of the A&Q margin. In 2023, we have got the operating leverage on the top line. We have also got some cost efficiencies. And then, A&Q of course, also benefits from the fantastic growth that we have had with Pearson Test of English, because one of the great synergies that we have at Pearson is that we are using our VUE test centres to deliver those tests. So really brilliant margin from that team in 2023. As you heard from Art, that brilliant margin and that operating leverage means that we can afford to invest in the business and further growth into the future, but the operating leverage will still grow margins into the future as well. So your CFO can have her cake and eat it, which is brilliant. In terms of the operating leverage, the way I think of that business, it is slightly different depending on which segment you are looking at, but it is between 40% and 60% depending on which of the businesses you are looking at. Thanks for your question, Lisa.

Omar Abbosh: Thanks, Sally.

Sally Johnson: Thank you. And with that, I will hand back to Omar.

Omar Abbosh: Oh, okay. Well, just to say thank you, thanks so much for being with us, spending time with us. We know you are busy people, and we really appreciate you being focused on Pearson. I am personally looking forward to getting to know you all, hopefully meeting you over the next weeks and months. I have enjoyed my first eight weeks or so. I think it is two months next Friday. So yeah, thanks so much and see you all very soon. Thanks, everyone.

[END OF TRANSCRIPT]