

Management's discussion and analysis of financial condition and results of operations

Operating results

First quarter 2017 vs. first quarter 2016

The company's net income for the first quarter of 2017 was \$333 million or \$0.39 per-share on a diluted basis, an increase of \$434 million compared to the net loss of \$101 million or \$(0.12) per-share for the same period last year.

Upstream recorded a net loss in the first quarter of \$86 million, compared to a net loss of \$448 million in the same period of 2016. Earnings in the first quarter of 2017 reflect the impact of higher Canadian crude oil realizations of about \$600 million, partially offset by higher royalties of about \$80 million, lower volumes of about \$70 million and higher operating expenses of about \$50 million primarily due to higher energy costs.

West Texas Intermediate (WTI) averaged US\$51.78 per barrel in the first quarter of 2017, up from US\$33.63 per barrel in the same quarter of 2016. Western Canada Select (WCS) averaged US\$37.26 per barrel and US\$19.30 per barrel respectively for the same periods. The WTI / WCS differential narrowed to 28 percent in the first quarter of 2017, from 43 percent in the same period of 2016.

The Canadian dollar averaged US\$0.76 in the first quarter of 2017, an increase of US\$0.03 from the first quarter of 2016.

Imperial's average Canadian dollar realizations for bitumen and synthetic crudes increased essentially in line with the North American benchmarks, adjusted for changes in exchange rates and transportation costs. Bitumen realizations averaged \$36.21 per barrel for the first quarter of 2017, an increase of \$24.29 per barrel versus the first quarter of 2016. Synthetic crude realizations averaged \$67.79 per barrel, an increase of \$21.47 per barrel for the same period of 2016.

Gross production of Cold Lake bitumen averaged 158,000 barrels per day in the first quarter, compared to 165,000 barrels per day in the same period last year, mainly due to the timing of steam cycles.

Gross production of Kearl bitumen averaged 182,000 barrels per day in the first quarter (129,000 barrels Imperial's share) compared to 194,000 barrels per day (138,000 barrels Imperial's share) during the first quarter of 2016. Lower production was the result of planned and unplanned maintenance activities.

The company's share of gross production from Syncrude averaged 66,000 barrels per day, compared to 80,000 barrels per day in the first quarter of 2016. Syncrude production was reduced by about 14,000 barrels per day mainly due to a fire at the Syncrude Mildred Lake upgrader.

Downstream net income was \$380 million in the first quarter, compared to \$320 million in the same period of 2016. Earnings increased mainly due to a gain of \$151 million from the sale of a surplus property, partially offset by lower marketing margins of approximately \$60 million.

Refinery throughput averaged 398,000 barrels per day, unchanged from the same period in 2016.

Petroleum product sales were 486,000 barrels per day, up from 469,000 barrels per day in the first quarter of 2016. Sales growth was primarily driven by the company's focus on securing long-term supply agreements.

Chemical net income was \$45 million in the first quarter, compared to \$49 million in the same quarter of 2016.

Net income effects from Corporate and Other were negative \$6 million in the first quarter, compared to negative \$22 million in the same period of 2016.

Liquidity and capital resources

Cash flow generated from operating activities was \$354 million in the first quarter, compared with \$49 million in the corresponding period in 2016, reflecting higher earnings.

Investing activities generated net cash of \$61 million in the first quarter, compared with \$358 million used in the same period of 2016, reflecting lower additions to property, plant and equipment and higher proceeds from asset sales.

Cash used in financing activities was \$134 million in the first quarter, compared with cash from financing activities of \$261 million in the first quarter of 2016. Dividends paid in the first quarter of 2017 were \$127 million. The per-share dividend paid in the first quarter was \$0.15, up from \$0.14 in the same period of 2016.

The company's cash balance was \$672 million at March 31, 2017, versus \$155 million at the end of the first quarter of 2016.

The company has entered into additional long-term pipeline transportation agreements to ship crude oil and products. These agreements, which have a total commitment of about \$2 billion, will support the company's plans for long-term growth. The company expects to fulfill these commitments in the normal course of business.

Recently issued accounting standards

In May 2014, the Financial Accounting Standards Board (FASB) issued a new standard, *Revenue from Contracts with Customers*. The standard establishes a single revenue recognition model for all contracts with customers, eliminates industry specific requirements and expands disclosure requirements. The standard is required to be adopted beginning January 1, 2018. The company expects to adopt the standard using the modified retrospective method, under which prior years' results are not restated, but supplemental information on the impact of the new standard is provided for in the 2018 results. Imperial continues to evaluate other areas of the standard. The impact from the standard is not expected to have a material effect on the company's financial statements.

In February 2016, the FASB issued a new standard, *Leases*. The standard requires all leases with an initial term greater than one year be recorded on the balance sheet as a lease asset and lease liability. The standard is required to be adopted beginning January 1, 2019. Imperial is evaluating the standard and its effect on the company's financial statements and plans to adopt it in 2019.

In March 2017, the FASB issued an Accounting Standards Update, 2017-07, Compensation – Retirement Benefits (Topic 715): *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The update requires the service cost component of net benefit costs to be reported in the same line in the income statement as other compensation costs and the other components of net benefit costs to be presented separately from the service cost component. Additionally, only the service cost component of net benefit costs will be eligible for capitalization. The update is required to be adopted beginning January 1, 2018. Imperial is evaluating the standard and its effect on the company's financial statements.

Forward-looking statements

Statements in this report regarding future events or conditions are forward-looking statements. Actual future financial and operating results could differ materially due to the impact of market conditions, changes in law or governmental policy, changes in operating conditions and costs, changes in project schedules, operating performance, demand for oil and gas, commercial negotiations or other technical and economic factors.

Quantitative and qualitative disclosures about market risk

Information about market risks for the three months ended March 31, 2017, does not differ materially from that discussed on page 22 of the company's annual report on Form 10-K for the year ended December 31, 2016.