

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

Operating results

Second quarter 2016 vs. second quarter 2015

The company's net loss for the second quarter of 2016 was \$181 million or \$0.21 per share on a diluted basis, compared to net income of \$120 million or \$0.14 per share for the same period last year. Wildfires in northern Alberta significantly impacted results in the quarter, reducing net income by about \$170 million.

Upstream recorded a net loss in the second quarter of \$290 million, compared to a net loss of \$174 million in the same period of 2015. Results in the second quarter of 2016 reflected lower realizations of about \$500 million, the impact of the northern Alberta wildfires on Syncrude and Kearl operations of about \$155 million and higher depreciation expense of about \$50 million. These factors were partially offset by higher Kearl and Cold Lake volumes of about \$105 million, the impact of a weaker Canadian dollar of about \$65 million and the favourable impact of lower royalties of about \$50 million. Earnings in the second quarter of 2015 reflected the impact associated with increased Alberta corporate income taxes of about \$327 million.

West Texas Intermediate (WTI) averaged US\$45.64 per barrel in the second quarter of 2016, down from US\$57.90 per barrel in the same quarter of 2015. Western Canada Select (WCS) averaged US\$32.36 per barrel and US\$46.41 per barrel respectively for the same periods. The WTI / WCS differential widened to 29 percent in the second quarter of 2016, from 20 percent in the same period of 2015.

During the second quarter of 2016, the Canadian dollar weakened relative to the U.S. dollar versus the same period of 2015. The Canadian dollar averaged US\$0.78 in the second quarter of 2016, a decrease of US\$0.03 from the second quarter of 2015.

Imperial's average Canadian dollar realizations for bitumen and synthetic crudes declined essentially in line with the North American benchmarks, adjusted for changes in the exchange rate and transportation costs. Bitumen realizations averaged \$29.45 per barrel for the second quarter of 2016, a decrease of \$19.71 per barrel versus the second quarter of 2015. Synthetic crude realizations averaged \$58.58 per barrel, a decrease of \$16.62 per barrel for the same period of 2015.

Gross production of Cold Lake bitumen averaged 163,000 barrels per day in the second quarter, up from 161,000 barrels in the same period last year. Incremental volumes from Nabiye offset cycle timing in the base operation.

Gross production of Kearl bitumen averaged 155,000 barrels per day in the second quarter (110,000 barrels Imperial's share) up from 130,000 barrels per day (92,000 barrels Imperial's share) during the second quarter of 2015. Kearl production was reduced in the current quarter by 64,000 barrels per day (45,000 Imperial's share) due to the Alberta wildfires and planned maintenance activities.

The company's share of gross production from Syncrude averaged 18,000 barrels per day, compared to 52,000 barrels in the second quarter of 2015. Syncrude production was reduced in the current quarter by 54,000 barrels per day due to the Alberta wildfires and planned maintenance activities.

Downstream net income was \$71 million in the second quarter, compared to \$215 million in the same period of 2015. Earnings decreased mainly due to the impact of higher refinery turnarounds of about \$115 million and lower industry margins of about \$45 million.

Refinery throughput averaged 246,000 barrels per day, compared to 373,000 barrels in the second quarter of 2015. The decrease was mainly associated with planned turnaround activity at the Strathcona and Nanticoke refineries. Excluding the impact of the planned turnarounds, capacity utilization averaged 97 percent.

Petroleum product sales were 470,000 barrels per day, compared to 478,000 barrels per day in the second quarter of 2015.

Chemical net income was \$55 million in the second quarter, compared to \$69 million in the same quarter of 2015.

Net income effects from Corporate and Other were negative \$17 million in the second quarter, compared to positive \$10 million in the same period of 2015.

Six months 2016 vs. six months 2015

Net loss in the first six months of 2016 was \$282 million, or \$0.33 per share on a diluted basis, versus net income of \$541 million or \$0.64 per share for the first six months of 2015.

Upstream recorded a net loss of \$738 million for the first six months of 2016, compared to a net loss of \$363 million for the same period last year. The loss in 2016 reflected lower realizations of about \$870 million, the impact of the northern Alberta wildfires on Syncrude and Kearnl operations of about \$155 million and higher depreciation expense of about \$105 million. These factors were partially offset by the impact of a weaker Canadian dollar of about \$135 million, higher Kearnl and Cold Lake volumes of about \$130 million, the favourable impact of lower royalties of about \$80 million and lower energy cost of about \$60 million. Earnings in the second quarter of 2015 reflected the impact associated with increased Alberta corporate income taxes of about \$327 million.

West Texas Intermediate averaged US\$39.78 per barrel in the first six months of 2016, down from US\$53.35 per barrel in the same period last year. Western Canada Select averaged US\$25.88 per barrel and US\$40.14 per barrel respectively for the same periods. The WTI / WCS differential widened to 35 percent in the first six months of 2016, from 25 percent in the same period of 2015.

During the first six months of 2016, the Canadian dollar weakened relative to the U.S. dollar versus the same period of 2015. The Canadian dollar averaged US\$0.75 in the first six months of 2016, a decrease of US\$0.06 from the same period of 2015.

Imperial's average Canadian dollar realizations for bitumen and synthetic crudes declined essentially in line with the North American benchmarks, adjusted for changes in the exchange rate and transportation costs. Bitumen realizations averaged \$20.76 per barrel for the first six months of 2016, a decrease of \$18.39 per barrel versus the same period of 2015. Synthetic crude realizations averaged \$48.59 per barrel, a decrease of \$15.30 per barrel for the same period of 2015.

Gross production of Cold Lake bitumen averaged 164,000 barrels per day in the first six months, up from 156,000 barrels from the same period last year, primarily due to Nabiye production.

Gross production of Kearnl bitumen averaged 175,000 barrels per day in the first six months of 2016 (124,000 barrels Imperial's share) up from 113,000 barrels per day (80,000 barrels Imperial's share). The increase was the result of the start-up of the expansion project and improved reliability of the initial development. Kearnl production was reduced by 32,000 barrels per day (23,000 Imperial's share) due to the Alberta wildfires and planned maintenance activities.

During the first six months of 2016, the company's share of gross production from Syncrude averaged 49,000 barrels per day, compared to 63,000 barrels from the same period of 2015. Syncrude production was reduced by 13,000 barrels per day due to the Alberta wildfires and planned maintenance activities.

Downstream net income was \$391 million, compared to \$780 million from the same period of 2015. Earnings decreased due to the impact of lower downstream margins of about \$480 million and higher refinery turnarounds of about \$115 million. These factors were partially offset by the impact of a weaker Canadian dollar of about \$130 million and lower fuels marketing operating costs of about \$50 million.

Refinery throughput averaged 323,000 barrels per day in the first six months of 2016, compared to 383,000 barrels in the same period of 2015. Capacity utilization decreased to 77 percent from 91 percent in the same period of 2015. The lower utilization reflected higher turnaround activity in 2016.

Petroleum product sales were 469,000 barrels per day in the first six months of 2016, compared to 476,000 barrels per day in the same period of 2015.

Chemical net income was \$104 million, compared to \$135 million in the same period of 2015.

For the first six months of 2016, net income effects from Corporate and Other were negative \$39 million, versus negative \$11 million in 2015.

Liquidity and capital resources

Cash flow generated from operating activities was \$443 million in the second quarter, compared with \$377 million in the corresponding period in 2015. Positive working capital effects offset the lower earnings.

Investing activities used net cash of \$297 million in the second quarter, compared with \$724 million in the same period of 2015, reflecting the completion of major upstream growth projects.

Cash used in financing activities was \$106 million in the second quarter, compared with cash from financing activities of \$315 million in the second quarter of 2015. Dividends paid in the second quarter of 2016 were \$118 million. The per-share dividend paid in the second quarter was \$0.14, up from \$0.13 in the same period of 2015.

The company's cash balance was \$195 million at June 30, 2016, versus \$28 million at the end of the second quarter of 2015.

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 will be adopted beginning January 1, 2018. Imperial is evaluating the standard and its 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 an 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.

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 six months ended June 30, 2016, 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, 2015 and Form 10-Q for the quarter ended March 31, 2016 except for the following:

Earnings Sensitivities

millions of Canadian dollars after tax

Seven cents decrease (increase) in the value of the Canadian dollar versus the U.S. dollar	+ (-)	590
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The sensitivity of net income to changes in the Canadian dollar versus the U.S. dollar increased from the first quarter of 2016 by about \$20 million (after tax) a year for each one-cent change, primarily due to the increase in bitumen prices and improved crack spreads.