



Imperial Oil Limited
1986
Annual Report

The No Trouble Gasoline

Cleans dirty carburetors
as you drive.



Gasoline
The No Trouble
MEMI

(Cover) A highlight of 1986 was the successful introduction of the company's No Trouble gasoline. Actor Les Yeo was featured in an award-winning television commercial that helped launch the engine-cleaning gasoline. Favorable customer response to the product was one reason for the growth in sales of Esso brand gasoline in 1986.

For the first time in the company's history, Calgary (below), host city for the 1988 Winter Olympics, will be the site of Imperial's upcoming annual meeting of shareholders. The meeting will be held in the Calgary Convention Centre on April 23, 1987.





Imperial Oil Limited, one of Canada's largest companies, manages most of its operations through three major segments.

Esso Resources Canada Limited, a wholly owned subsidiary based in Calgary, is the country's largest producer of crude oil; it also produces significant quantities of natural gas and coal.

Esso Petroleum Canada, a division of Imperial, operates five refineries across the country and has a major share of the Canadian market for petroleum products.

Esso Chemical Canada, another division, produces and markets a wide variety of fertilizers and petrochemicals.

In addition, the company has substantial interests in the mining and building material industries.

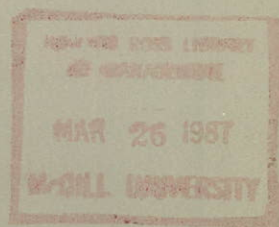


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Investor information

For more information about Imperial, please
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Toronto, Canada M5W 1K3

Financial highlights

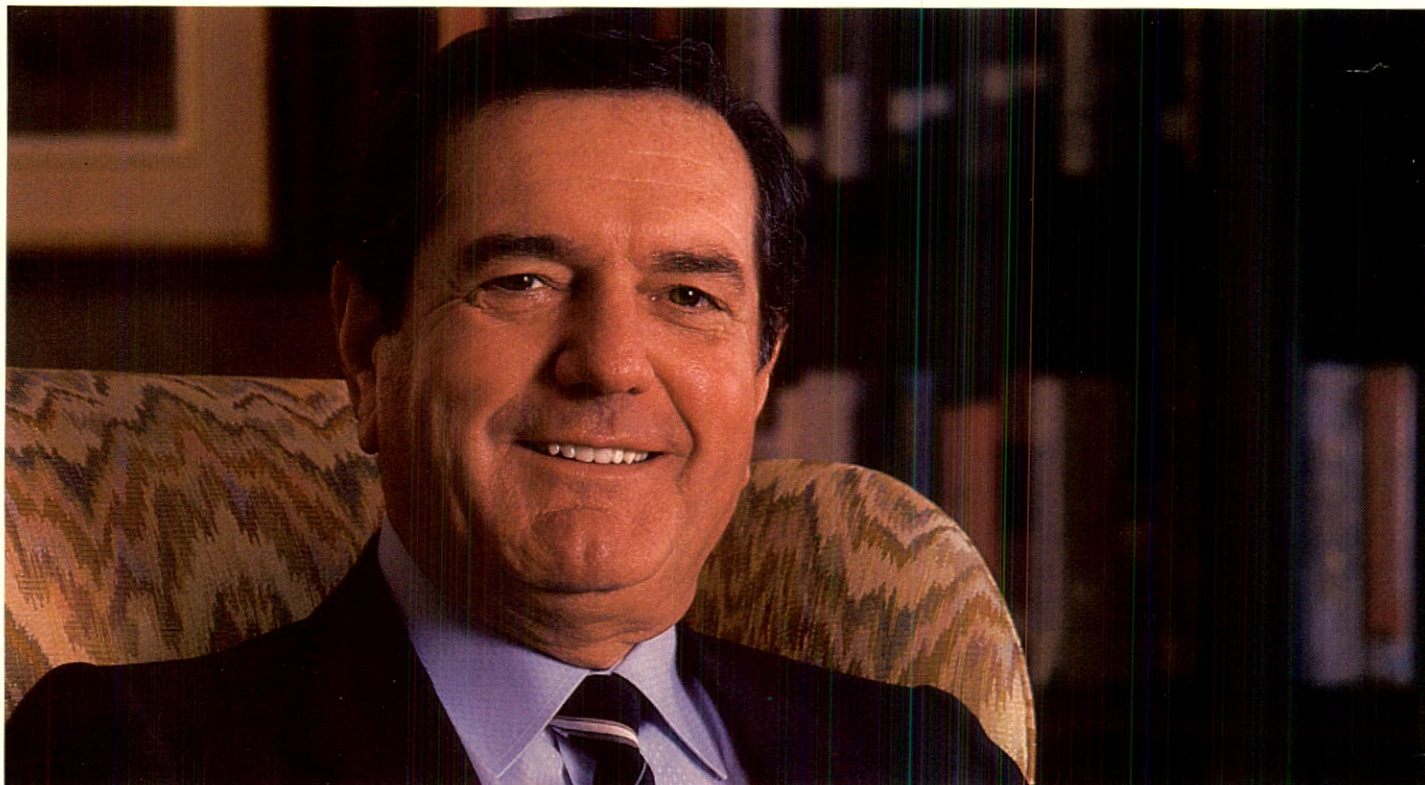
	1984	1985	1986
	millions of dollars		
Earnings			
From operations	520	694	440
After unusual items	520	644	285
	millions of dollars		
Total funds provided from operating activities	708	1004	1067
	millions of dollars		
Capital and exploration expenditures	679	1158	648
	percentages		
Return on average capital employed (before unusual items)	8.4	10.0	6.3
Return on average shareholders' equity	11.8	13.4	5.6
	dollars		
Per-share information			
Earnings from operations	3.24	4.27	2.69
Earnings after unusual items	3.24	3.97	1.74
Total funds provided from operating activities	4.41	6.19	6.52
Dividends	1.45	1.65	1.60

Operating earnings per share

Falling crude-oil prices result in lower operating earnings per share.

	dollars
82	1.89
83	2.12
84	3.24
85	4.27
86	2.69

Letter to shareholders



Arden R. Haynes,
chairman, president
and chief executive
officer

Even though Imperial's earnings were substantially reduced in 1986, as a result of external market forces, I am satisfied that your management's prompt response to those forces minimized their impact and strengthened the company overall.

Decisive actions – described elsewhere in this report – were taken early in the year to ameliorate the impact of sharply lower oil prices on natural resource earnings and to improve the profitability of Imperial's petroleum product and chemical businesses.

Successful though these measures were, 1986 was a very difficult year for the oil industry, and your company did not emerge unscathed. Imperial's earnings from operations declined by 37 percent to \$440 million.

Shareholders should find reassurance, however, in the fact that Imperial emerged from 1986 in sound financial shape. The calibre of a company can be gauged not only from how successfully it takes advantage of the opportunities that present themselves in good times but from how it responds to adversity. In this respect, Imperial's record speaks for itself. It has not only prospered in good times and survived in bad ones for more than a century but has grown to become one of Canada's largest and most successful corporations.

The basic reason for this, I believe, is to be found in the values to which the company has adhered throughout its existence. Imperial has always been dedicated to providing its customers with quality products at fair prices, maintaining the highest ethical standards in all its business dealings, fostering the long-term interest of its shareholders and rewarding its employees well and treating them equitably. In my view, these values are the essential ingredients of a successful business enterprise.

Maintaining these values was of paramount importance to the company in 1986 as it responded to the changing business environment. For example, in the interest of our shareholders the temptation to reduce quarterly dividends in the face of sharply lower earnings was resisted. And when it became clear that circumstances left the company no option but to reduce the number of employees, that reduction was achieved almost totally through innovative voluntary programs that were well received throughout the company. Such decisions incur a financial cost but reflect the values and beliefs to which Imperial subscribes, in the conviction that they serve the company's longer-term interests. I am sure that they will continue to serve us well in the future.

That future remains clouded, especially so far as international oil prices are concerned. Recent attempts by OPEC to reestablish control of the market have resulted in some upward movement of prices, but it is too early to determine whether this trend will be sustained or even whether the current levels will be maintained. It is still a time for prudence and caution, and the company's actions will continue to be based on the fundamentals of market supply and demand.

There remains a considerable surplus of crude oil in world markets, and the current period of adjustment could prove to be a protracted one. In the longer run, however, given that the world continues to use more oil than it finds, the outlook is for tightening supplies and higher prices.

The prospects for petroleum products are more promising than they were but still uncertain. The recent history of this business has been characterized by falling demand, resulting in over-supply and intense price competition. But if demand recovers in Canada, as it has in the United States, the supply/demand equilibrium could be reflected in more satisfactory profit margins.

Chemicals present a mixed outlook. The growth in demand for our major petrochemical products outstripped the growth in the Canadian economy in 1986, and so long as economic growth continues prospects for petrochemical sales are good. The future for fertilizers is clouded by

uncertainty over agricultural production in areas of the world that previously depended on food imports. The implications of this are not yet fully understood, but future large grain surpluses could dampen fertilizer demand and maintain pressure on prices.

The future, therefore, will not be without its problems. But neither will it be lacking in opportunities, and Imperial is as ready to take advantage of those as it possibly can be.

Your company today is a leaner, more productive and more flexible organization than it was even a year ago. Savings have been achieved in all areas. The increased efficiencies that have resulted from staff reductions and a major corporate reorganization have not only minimized the impact of adverse market conditions but will allow the company to derive maximum earnings benefit from any future improvements in revenues.

As the 1986 earnings figures indicate, Imperial's petroleum product and chemical operations are better geared to a highly competitive environment and to shifting market conditions. The company possesses an excellent inventory of natural resource opportunities. Several of these are large projects that Imperial is uniquely suited to develop. The company has strong financial reserves. And, most important, it is staffed by people who, in their dedication and superb skills, I believe to be second to none in the industry.

In short, Imperial is in good health. Your management, guided by the beliefs and values that have served so well in the past, is committed to its future growth and prosperity.



Arden R. Haynes,
chairman, president
and chief executive
officer

February 20, 1987

Review of operations



Robert B. Peterson,
executive vice-president
and chief operating
officer

Nineteen eighty-six was a year of major adjustment for Imperial, as the company responded to the impact of significantly lower crude-oil prices on its natural resource activities and the continuing need to improve the profitability of its petroleum product and chemical operations.

During the course of the year, business plans were revised, capital-spending programs curtailed, operating costs cut, debt obligations and interest costs trimmed, the size of the work force reduced and many parts of the organization restructured to better fit a difficult new business environment for the petroleum industry.

Imperial's earnings from operations were \$440 million, a drop of \$254 million, or 37 percent, from 1985. The decline was caused mainly by the nearly 50-percent reduction in average crude-oil prices that occurred during the year. That drop was offset in part by increased oil production and improved earnings from petroleum product operations.

The company's return on average capital employed, before unusual items, was 6.3 percent in 1986, down from 10 percent in 1985.

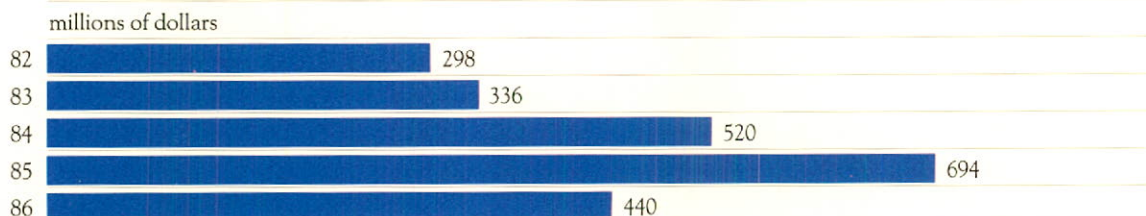
Capital and exploration expenditures amounted to \$648 million in 1986, compared with the record \$1.2 billion spent in 1985.

The company made major investments in additional stages of bitumen recovery at Cold Lake, in enhanced oil recovery and in programs to make its

retail outlets more appealing to customers and to improve the efficiency of its refineries.

Total earnings from operations

Improved results from petroleum product and chemical operations partially offset the impact of lower crude-oil prices.



Expenses cut by \$91 million

Operating, administrative and marketing expenses were trimmed by \$91 million from the previous year.

The size of the company's work force was reduced by about 16 percent during 1986, mainly through two voluntary programs, one that offered eligible employees enhanced pension benefits if they chose to take early retirement and another that offered employees lump-sum payments if they left the company. In addition, a major restructuring of the petroleum product and chemical segments occurred during the year.

The staff reduction programs and associated reorganizations gave rise to a \$90-million unusual charge to 1986 operating earnings. A second unusual expense item of \$65 million, associated with the retirement of a (U.S.) \$200-million debenture issue, brought total 1986 earnings after unusual items to \$285 million – down from \$644 million in 1985.

Notwithstanding the challenging environment, the company achieved several important operating highlights in 1986.

In natural resources, net production of hydrocarbon liquids increased 36 percent, and five million cubic metres (31.5 million barrels) were added to proven oil reserves. It was the fifth successive year in which additions to crude-oil reserves exceeded production.

In the petroleum product business, the year was marked by the successful introduction of a new engine-cleaning gasoline.

Imperial was an official sponsor of and a major supplier to Expo 86, the highly successful world exposition held in Vancouver. One of Expo's most popular exhibits was the Esso Roundhouse, which took a whimsical look at transportation through the ages. The historic railway roundhouse was restored by Imperial and will remain as a permanent part of Vancouver's heritage.



Safety
performance best
in the company's
history

In terms of safety performance, 1986 was the best year in the company's history. All operating segments set new records for employee safety, as the number of incidents fell by a quarter.

The company also continued to improve environmental protection in all its operations. Expenditures on facilities and equipment to protect the environment were \$38 million during 1986, bringing total expenditures over the past five years to \$270 million.

Imperial's prompt response to the sharp change in the business environment has placed the company in a good position to improve future profitability, particularly as the climate for the petroleum industry begins to improve. Imperial will continue to emphasize the safe, efficient and reliable operation of its facilities and to select an appropriate mix of investments suited to business conditions and forecasts.

Natural resources

Earnings from natural resource operations were \$196 million in 1986, down from \$542 million in 1985. Return on average capital employed was 5.9 percent, compared with 19.6 percent the previous year. The drop in earnings, mainly attributable to lower crude-oil prices, was partially offset by a 36-percent increase in net production of hydrocarbon liquids.

Earnings were also improved by government actions to reduce the tax burden on oil and gas production. The actions included the elimination of

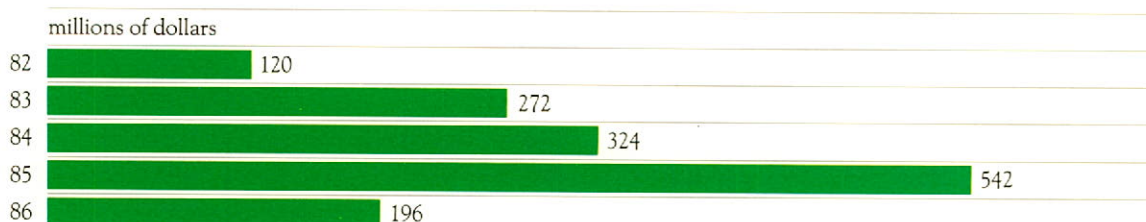
	1984	1985	1986
	millions of dollars		
Financial statistics			
Earnings	324	542	196
Revenues	1740	2255	1680
Capital employed at December 31	2423	3106	3522
Return on average capital employed (percent)	14.3	19.6	5.9
	thousands of m ³ /d		
Operating statistics			
Crude oil and natural-gas liquids (NGL) – net production			
Conventional	10.6	12.7	15.0
Cold Lake	2.7	4.4	9.5
Syncrude	3.3	4.5	5.2
NGL	1.5	1.4	1.6
Total crude oil and NGL produced	18.1	23.0	31.3
	millions of m ³ /d		
Natural gas – net production	4.8	4.0	4.3
	millions of tonnes annually		
Thermal coal production	1.3	1.0	0.9
	millions of m ³		
Net reserves of crude oil and NGL	171.8	208.1	213.1
	billions of m ³		
Net reserves of natural gas	36.2	40.6	41.4

One cubic metre (m³) is equal to approximately 6.3 barrels or 35.3 cubic feet.

One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

Earnings from natural resources

Natural resource earnings decline as crude-oil prices fall.



the federal Petroleum and Gas Revenue Tax and the reduction of some provincial royalties. Those changes increased the company's profit by about \$29 million during 1986 and will have a further favorable influence in 1987, when their impact will be felt over the entire year.

The company is pursuing three main strategies in its natural resource operations. The first is to reduce costs and maximize the value of production. The second is to invest selectively in projects that remain attractive at prevailing prices. And the third is to maintain and enhance longer-term development options at minimum current cost.

Esso Resources responded to falling oil prices by implementing a wide range of efficiency measures. The number of people in the organization was trimmed by about 19 percent, and costs were reduced in virtually every area of the operation.

Syncrude's unit
costs reduced by
15 percent

The Syncrude oil-sands project, in which the company holds a 25-percent share, made significant gains in operating efficiency. By producing a record amount of synthetic crude oil—averaging 20 600 cubic metres (130 000 barrels) a day during the year—and by reducing operating costs, Syncrude's employees were able to cut the plant's average unit operating costs by about 15 percent from the previous year.

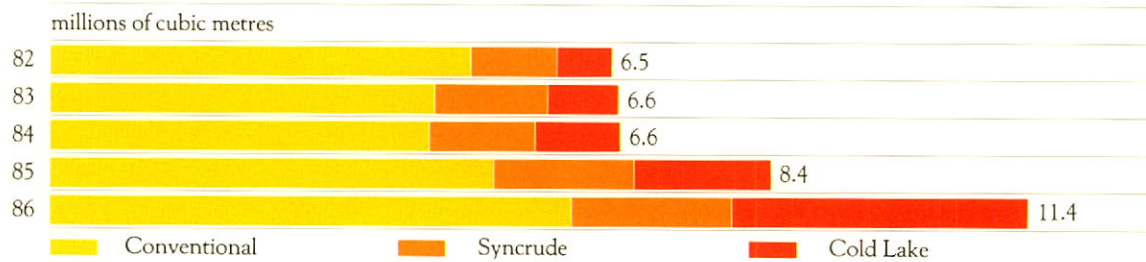
Bitumen production from the Cold Lake operation averaged 9500 cubic metres (60 000 barrels) a day in 1986, 117 percent higher than in 1985. There were two main reasons for the increase. One was the start-up in May of stages five and six of the project. In addition, the first four stages of the project, which went into operation during 1985, were producing oil for the entire year in 1986. At the end of the year, Cold Lake's output of bitumen was 11 500 cubic metres (72 300 barrels) a day.

The 18-percent increase in conventional oil production came largely from the Norman Wells oil-field expansion and the Judy Creek enhanced recovery project. Nineteen eighty-six was the first year both were in production for an entire 12 months.

Net production of natural gas increased slightly during the year, while production of coal declined, as the company withdrew from export markets for thermal coal.

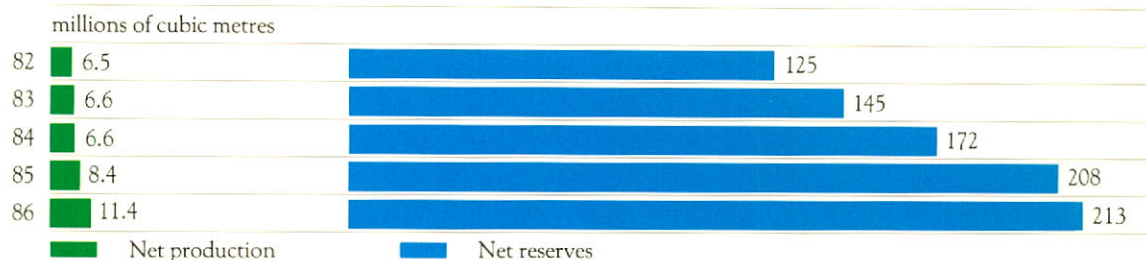
Net production of crude oil

Net production of crude oil increases 36 percent as Cold Lake bitumen production climbs, Syncrude achieves record output and conventional production grows by 18 percent.



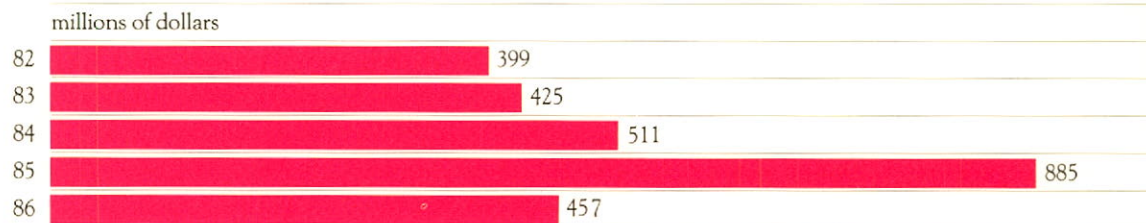
Net reserves and production of crude oil

Reserves grow for the fifth consecutive year and equal 19 years of current production.



Capital and exploration expenditures

Capital and exploration expenditures remain substantial even though crude-oil prices diminish opportunities for resource investment.



Capital and exploration expenditures exceed \$450 million

Esso Resources' capital and exploration expenditures totaled \$457 million in 1986.

The company was the most active driller in Canada during the year, participating in the drilling of a total of 553 exploration and development wells. While many of those wells resulted from development drilling at Cold Lake, a modest but successful program of exploration drilling was also undertaken in Western Canada.

In frontier exploration, Esso Resources fulfilled all the terms of six exploration agreements with the government of Canada related to drilling in the western Arctic. To meet drilling requirements under those 1982 agreements, Esso Resources entered a joint exploration program with a group of more than a dozen Canadian companies. In return for a part interest in any resulting discoveries, the group has paid most of the costs of drilling 29 wells over the past five years.

The five-year program provided further evidence of the production potential of the Mackenzie Delta/Beaufort Sea region. A total of 21 exploration wells and eight delineation wells were drilled. Most of the

Production and reserves the highest of any Canadian company

delineation wells were drilled as a follow-up to a shallow oil discovery made on the Tuktoyaktuk peninsula in 1985. They helped define the limits of the target structure and demonstrated that its geology and the quality of the hydrocarbons it contains are quite variable.

A two-year, two-well program was also completed in the Flemish Pass region of the Atlantic Ocean, about 400 kilometres east of St. John's, Nfld. Both wells were dry.

Despite this year's lower profits, the company holds a strong position and good prospects in the natural resource area. Imperial is Canada's largest oil producer, and its average net daily production of 31 300 cubic metres (197 000 barrels) of crude oil and natural-gas liquids in 1986 was the company's highest since 1974. Imperial's net proved reserves of crude oil increased by five million cubic metres (31.5 million barrels), or 2.4 percent, during the year, bringing them to a total of 213 million cubic metres (1.34 billion barrels) – also the largest of any Canadian company.

Looking to the future, we believe that it makes sense to base our plans on the assumption that oil prices will remain volatile during the next several years. At the same time, we are taking steps to retain our development options for the time when prices do improve.

Esso Resources continues to provide challenging job opportunities and to build heavy-oil expertise within the company by using its own employees rather than outside contractors to develop detailed engineering plans for future stages of its Cold Lake project. At the company's head office in Calgary, Doug Hall (right), Susan Wolfe and Brian Peterson use sophisticated computer equipment to support the engineering team, whose work will allow the company to embark on additional stages of the project when economic conditions permit.



Petroleum products

Earnings from petroleum products increased to \$174 million during 1986, from \$102 million the previous year. Return on average capital employed was 7.6 percent, better than it has been for several years but still below the average return for manufacturing industries.

The higher earnings resulted mainly from an improvement in margins on product sales, combined with lower operating expenses as Esso Petroleum reduced its work force by about 17 percent, restructured its organization and continued to improve its operating efficiency. Those measures were taken in response to an intensely competitive environment, particularly in central Canada.

Beginning in the fourth quarter of 1986, Imperial changed its method of accounting for inventories to the average-cost method, which provides a better matching of reported revenues and costs, particularly during periods of volatile prices. The new method has been used to restate the company's earnings for 1986 and prior years. That restatement resulted in an increase in 1986 earnings of \$4 million.

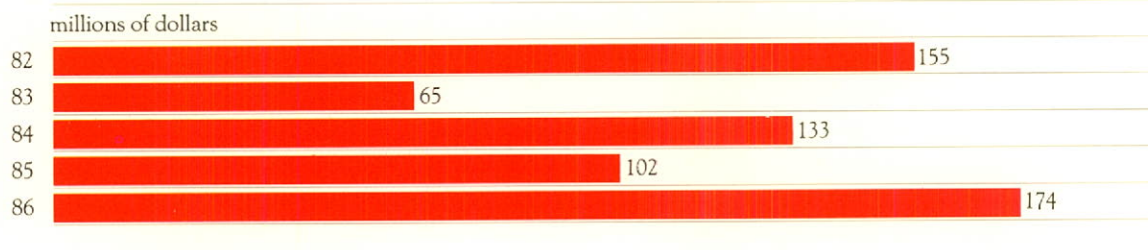
	1984	1985	1986
	millions of dollars		
Financial statistics (1)			
Earnings	133	102	174
Revenues	6816	7265	5772
Capital employed at December 31	2444	2589	2004
Return on average capital employed (percent)	5.3	4.1	7.6
Operating statistics			
Sales of petroleum products (thousands of m ³ /d)	53.0	54.1	52.7
Refinery utilization as a percentage of total capacity	88	83	80

One cubic metre (m³) is equal to approximately 6.3 barrels.

(1) Data for 1984 and 1985 have been restated to reflect the change in the method of inventory valuation described in note 1 to the audited financial statements.

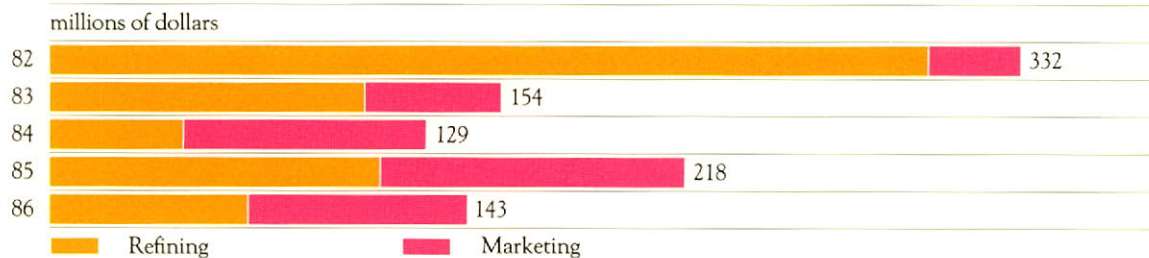
Earnings from petroleum products

Earnings increase, as a result of improved sales margins and lower operating costs, despite intense market competition.



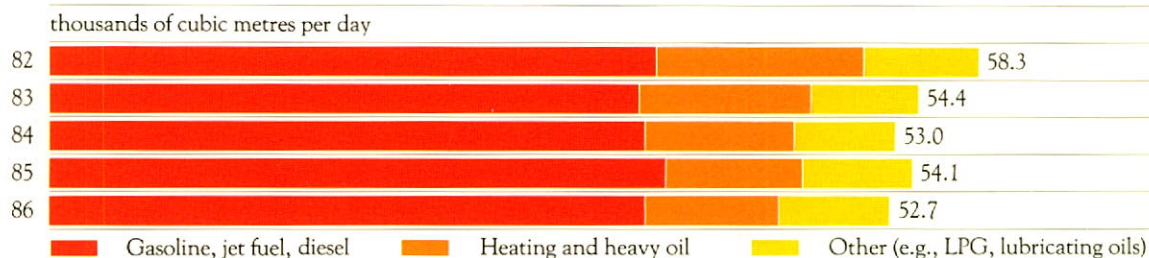
Capital expenditures

Petroleum product investment is directed to upgrading retail outlets and improving refinery efficiency.



Petroleum product sales

Total sales decline by almost three percent as the company withdraws from unprofitable business.



Demand for petroleum products stabilizes

Between 1980 and 1985, a combination of conservation, government incentives to reduce oil consumption and a severe recession caused Canadian demand for petroleum products to fall by about 23 percent. During 1986, total demand remained essentially unchanged from the previous year.

There were, however, sharp regional differences in demand in 1986. In Western Canada, downturns in the agricultural economy and the petroleum industry caused demand for petroleum products to fall by about 1.5 percent, while relatively buoyant economic conditions in central Canada caused product demand there to increase by one percent.

Esso Petroleum's total sales volume decreased by just under three percent during the year, primarily because the division withdrew selectively from unprofitable business. Exports constituted nearly 10 percent of the division's total sales during 1986 and are expected to be of equal importance during 1987.

No Trouble
gasoline
wins customer
acceptance

One of the highlights of the year was the highly successful introduction of the company's new No Trouble gasoline, which was launched in June, following an extensive research program. The gasoline contains new detergent additives that can clean fuel injectors and carburetors, thus improving engine performance. Customer acceptance of the new gasoline, coupled with other measures to improve marketing effectiveness, caused sales of Esso brand gasoline to grow more rapidly than industry sales.

Nineteen eighty-six also saw the release of the final report of the Restrictive Trade Practices Commission inquiry into the petroleum industry, after an exhaustive five-year investigation. It cost Imperial more than \$9 million to participate in the hearings and defend itself against the "rip-off" charges that were leveled at the industry when the inquiry was launched in the early 1980s.

The final report confirmed what the company and many others had been saying from the start. It found that the petroleum industry was, indeed, competitive and that there was no evidence of collusion in any sector.

Although petroleum product earnings increased during 1986, further improvement is needed to achieve adequate returns.

Esso Petroleum made important adjustments to its cost structure in 1986 and will continue to pursue vigorous programs to improve efficiency and customer service. Nevertheless, future growth in profitability will depend to a large extent on product margins in the marketplace.

Organizational changes at Esso Petroleum reflect the company's commitment to customer service and have greatly increased the responsibilities of individual employees. One such employee is Lawrence Richler (left), Esso Petroleum's retail area manager for Newfoundland, who gives retailer Gary Horwood high marks for the operation of his Churchill Park Esso station in St. John's.



Chemicals

Earnings from chemical operations were \$17 million, up from \$3 million in 1985. Return on average capital employed was 1.8 percent.

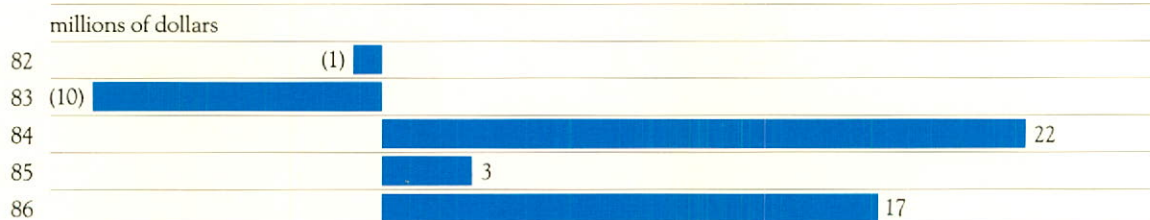
The Esso Chemical division, like other parts of the company, undertook a major organizational restructuring during the year. Its staff was reduced by about 16 percent and a large number of product lines were consolidated. Those actions have improved the division's competitive position by reducing fixed costs and by focusing greater attention on the quality of products and customer services.

	1984	1985	1986
	millions of dollars		
Financial statistics			
Earnings	22	3	17
Revenues			
Petrochemicals	479	478	480
Agricultural chemicals	328	327	300
Total revenues	807	805	780
Capital employed at December 31	1014	1008	947
Return on average capital employed (percent)	2.1	0.3	1.8
	thousands of tonnes per day		
Operating statistics			
Sales			
Petrochemicals	1.9	1.9	1.9
Agricultural chemicals	3.9	3.9	4.1

One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

Earnings from chemicals

Improved petrochemical performance accounts for encouraging increase in chemical earnings.

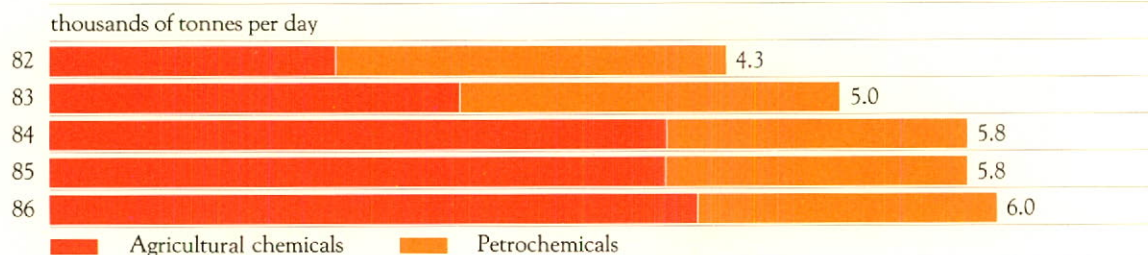


Esso Chemical underwent extensive organizational changes last year to reduce costs and improve the division's competitive position. At the Samia chemical research centre (clockwise from left), Bill Innes, who became president of Esso Chemical in 1986, discusses the changes with Donald Norris, Cathy McNair and John Young.



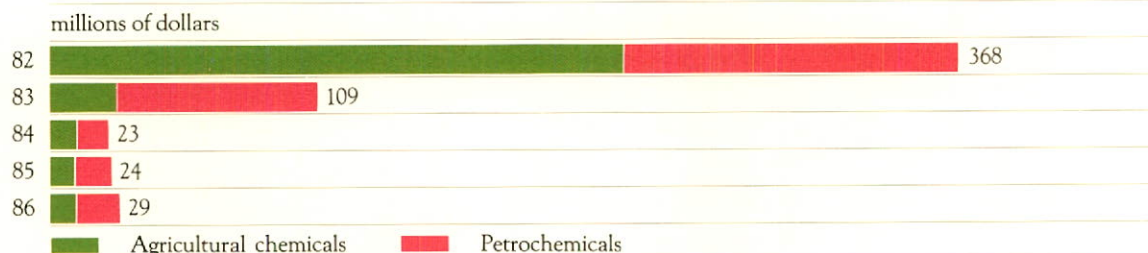
Sales volumes

Fertilizer sales increase by five percent; demand is strong for petrochemicals.



Capital expenditures

Investments remain relatively low as major projects completed in 1983 continue to meet market demands.



Petrochemical results improve sharply

The company's chemical business is made up of two distinctly different segments – petrochemicals and agricultural chemicals.

The petrochemical operation achieved a sharp turnaround from 1985. The main reason for the improvement was that margins on the sale of polyvinyl chloride and polyethylene resins were higher, as a result of lower feedstock and operating costs and improved manufacturing performance. Polyvinyl chloride resin is made into durable plastic products like vinyl pipe and siding, while polyethylene is made into grocery bags, stretch film and thousands of other products.

The company holds a strong position in domestic markets for other petrochemical products, such as solvents and chemical intermediates. Markets for those products are not growing as quickly as ones for plastic resins, but they continue to make a steady contribution to profitability.

The other segment of the business – agricultural chemicals – had a difficult year in 1986, as the agricultural economy of western North America continued to deteriorate.

Fertilizer demand hurt by falling grain prices

Falling grain prices have had a severe impact on demand for fertilizer in Western Canada and on international fertilizer prices. During 1986, total western Canadian demand for fertilizer declined for the first time since 1976. That set up a more intensely competitive situation in which profit margins on fertilizer sales in domestic and export markets were severely reduced.

Looking to the future, petrochemical earnings are expected to improve with steady economic growth. Improved profitability in the agricultural chemical business will depend largely on stability in international agricultural markets.

Building Products
achieves record
earnings

Other business operations

Building Products of Canada Limited, a wholly owned subsidiary of Imperial and a major manufacturer of high-quality construction materials for residential and commercial buildings, attained record sales and earnings in 1986, realizing a return on average capital employed of 14 percent.

Strong housing markets contributed to the increase in earnings, but the major portion came from gains in market share, improved sales of premium products, profitable penetration of the export market and reduced manufacturing costs in all product lines.

Building Products is one of the leading producers of fibreboard in North America. In December 1986, the company announced a 15-percent expansion of its Pont Rouge, Que., fibreboard plant in response to very strong demand in Canada and the United States.

Late in 1986, the installation of high-technology extrusion equipment in the company's vinyl-siding plant in Acton, Ont., was completed, resulting in a major improvement in the plant's efficiency.

Building Products has earned a strong reputation for responsiveness to customer needs. With its record of consistently improved earnings in recent years, it is well positioned for profitable growth.

Esso Minerals has
profitable year

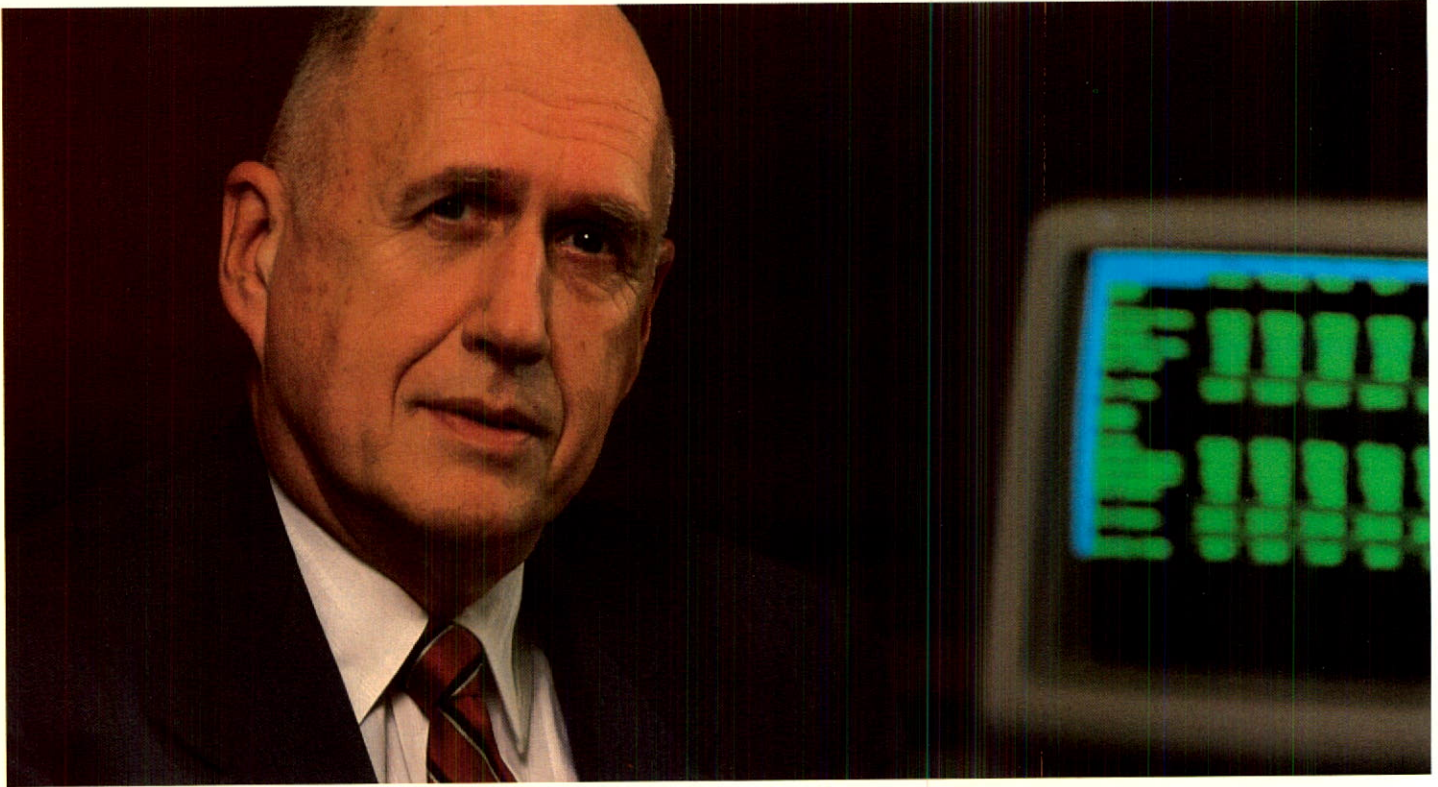
Esso Minerals Canada, a division of Esso Resources engaged in developing opportunities in base and precious metals, also had a good year in 1986. In late 1985, Esso Minerals purchased a 35-percent interest in Les Mines Selbaie, a mining complex located in the Abitibi region of northwestern Quebec. The operation currently produces copper, with precious metal by-products, from an underground mine and recently completed a \$130-million major open-pit expansion of a new ore body, where zinc and copper concentrates are now being commercially produced.

In 1986, the income from Selbaie and tax allowances associated with the development of the mine resulted in positive earnings for Esso Minerals, which continues to direct a Canada-wide exploration program.



Robert B. Peterson,
executive vice-president
and chief operating
officer

Financial review



William J. Young,
executive vice-president
and chief financial
officer

One of Imperial's fundamental principles over the years has been to enhance and protect the investments that shareholders and lenders have made in the company. Translated into a specific operating approach, that principle has meant, among other things, paying a regular and reliable dividend, which the company has done since the late 19th century – in fact, Imperial hasn't reduced its regular quarterly dividend since the beginning of the Second World War.

Another objective of the company has been to make it as easy as possible for investors to know what their money is buying by maintaining a policy of full disclosure of financial information and a simple capital structure. For example, Imperial has only two classes of shares, both common, that rank equally in terms of dividend payments and voting rights. (The only practical difference between its Class A and Class B shares is that one pays a cash dividend, the other a stock dividend.) The company's long-term debt consists of a relatively small number of debenture issues that are easy to keep track of since they are publicly traded.

However, the true cornerstone of Imperial's operating approach has been the maintenance of its financial strength, which has been particularly appropriate during the 1980s, when the operating environment for the petroleum industry has featured – in rapid succession – punitive new taxes,

record interest rates, a severe recession and, most recently, a sharp drop in oil prices.

Falling oil prices caused the company's return on average capital employed (ROCE) to fall to 6.3 percent in 1986, well below the ROCE of 12 to 13 percent that we believe is minimally appropriate given the inherent risks of the petroleum industry. One of the company's objectives is to achieve those higher returns within the next few years.

A key reason for believing that objective to be attainable is that Imperial has emerged from 1986 in excellent financial shape. And one of the principal ways it has accomplished that is by anticipating the impact that changes in earnings, investment plans and general economic conditions will have on the company's financial ratios – those standard measures, tested over time, that are commonly employed by the investment community to evaluate the financial position of a corporation.

A key ratio is interest coverage (chart 1), which essentially compares a company's before-tax earnings with the amount of interest it must pay during the year. That ratio indicates how many times a company's earnings, before interest has been deducted, will cover its current interest obligations. While Imperial's earnings dropped in 1986, they were still sufficient to cover interest payments about eight times, a healthy ratio by every commonly accepted standard.

1. Interest-
coverage ratio

Earnings continue to
exceed the company's
interest obligations by a
very wide margin.



Another way to measure a company's financial position is by comparing the amount of capital the owners, or shareholders, have invested in it with the amount lenders have provided (chart 2). As part of its strategy of maintaining financial strength, Imperial has relied mainly on cash generated by its business operations, rather than on borrowed money, to finance investment plans. As a result, debt makes up a relatively small part of the company's capital structure.

During 1986, Imperial reduced its long-term debt and interest costs even further by using cash reserves generated from operations to retire a (U.S.) \$200-million debenture issue that carried an interest rate of 15½ percent. Although the company had to pay a premium to retire the securities before

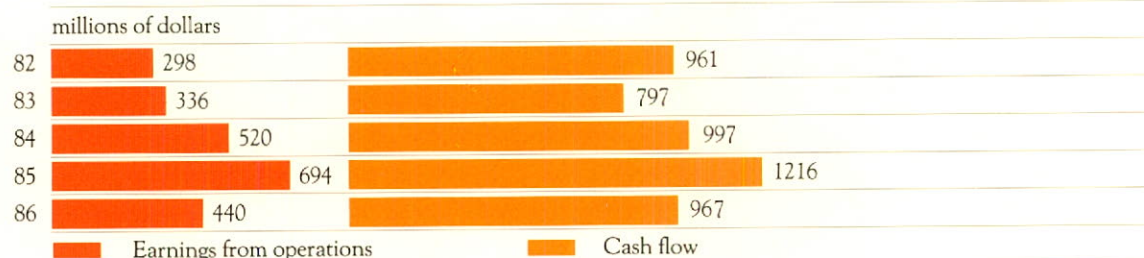
2. Debt compared with shareholders' ownership

Shareholders' ownership increases; company retires (U.S.) \$200-million debenture issue.



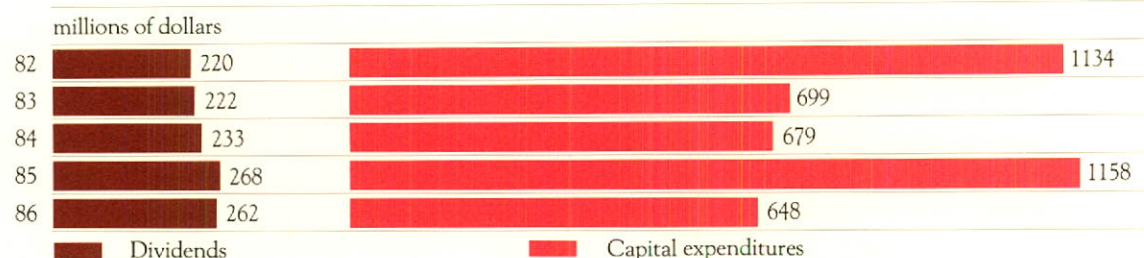
3. Cash flow compared with earnings from operations

Cash flow falls proportionately less than earnings as cash expenses decrease.



4. Principal uses of cash flow

Strong cash flow sustains dividend payments and capital spending, which has exceeded \$4 billion over the past five years.



their maturity date, the retirement will improve before-tax earnings by about \$15 million a year during the next several years.

Another way to measure a company's financial strength and resiliency is to look at operating results on a cash basis. This is commonly known as cash flow or funds flow. Broadly defined, cash flow is what remains from a company's revenues after it pays those taxes and expenses that require a current cash outlay.⁽¹⁾ (Certain expense items on an earnings statement—such as depreciation and deferred income taxes—don't require a current cash outlay.)

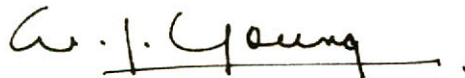
Many investment professionals consider cash flow to be as important as earnings in measuring corporate financial strength and capability, because it gives a more complete picture of a company's ability to repay debt, pay dividends and pursue growth opportunities. As shown in chart 3, Imperial's cash flow fell by about 20 percent in 1986, significantly less than the drop in its operating earnings. The reason is that although the company's revenues were lower, its cash expenses and taxes also decreased substantially.

(1) This amount appears as the first subtotal on the consolidated statement of changes in financial position, page 30.

Part of the company's cash flow has been used (chart 4) to pay dividends that, over the past five years, have totaled more than \$1 billion. Quarterly dividend payments were maintained during the difficult years of the recent recession and National Energy Program and increased when conditions improved in 1984. In 1985, when earnings reached a record level, the company declared an extra dividend. Despite the drop in earnings in 1986, the quarterly dividend payment was again maintained.

By far the greatest portion of the company's cash flow, however, has been put to work for shareholders in new investments that will enhance the earning power and asset value of their shares. Since 1982, more than \$4 billion has been invested in projects that have increased the company's oil production and reserves, such as Cold Lake, Judy Creek and Norman Wells, as well as in service-station improvement, refinery upgrading and new chemical plants. Investment over that five-year period totaled more than \$26 for each common share outstanding at the end of 1986.

Those investments have been made and dividends paid without in any way impairing the company's financial health and resiliency. Imperial has a simple capital structure that is easily understood, low debt, a strong cash position and the healthy financial ratios that the company believes will enhance and protect the investments of its shareholders in the years ahead.

A handwritten signature in black ink, reading "W. J. Young", followed by a horizontal line extending to the right.

William J. Young,
executive vice-president
and chief financial
officer

Financial section table of contents

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Glossary of terms

Average cost: a method of inventory valuation where the unit cost is a weighted average of the cost of the opening inventory and the cost of inventory produced or purchased, calculated on a monthly basis.

Deferred income taxes: the result of differences between income-tax legislation and conventional accounting treatments of certain revenues and expenses; the major difference results from substituting deductions permitted under income-tax legislation for depreciation and amortization expenses in respect of amounts capitalized in the financial statements (deferred income taxes are not a tax liability under the law).

Depreciation and amortization: the systematic allocation of the cost of assets to expense during the periods of their useful life.

Funds: the total of cash and marketable securities reduced by outstanding cheques and short-term notes payable.

Hedge: the purchase or sale of a forward-exchange contract for the specific purpose of eliminating or restricting the risk of foreign-exchange-rate fluctuations.

Net realizable value: the estimated selling price in the ordinary course of business less estimated costs of completion and sale.

Operating working capital: working capital (the excess of current assets over current liabilities) less funds.

Other operating revenues: revenues from the sale of products and services, other than the sale of crude oil, natural gas, petroleum products and chemicals; the main items are building materials, tires, batteries, auto parts, coal and other minerals.

Taxes and levies: Taxes consist of income taxes, both current and deferred; revenue taxes, which comprise the Petroleum and Gas Revenue Tax and the Incremental Oil Revenue Tax; and commodity, property and other taxes, which include fuel excise taxes and the federal sales tax. Levies consist of the Petroleum Compensation Charge and the Canadian Ownership Special Charge.

Write-down: the downward adjustment of the recorded value of an asset; normally this occurs when the recorded value is greater than the net realizable value.

Consolidated statement of earnings

For the years	1984	1985	1986
	millions of dollars		
Revenues			
Crude oil (2)	830	548	249
Natural gas	185	148	149
Petroleum products (3)	6366	6761	5356
Chemicals	753	762	732
Other operating revenues	454	448	478
Interest and investment income (4)	167	137	100
Total revenues	8755	8804	7064
Expenses			
Exploration	63	85	116
Purchases of crude oil and products (3)	4073	4036	3030
Extracting, processing and manufacturing	1068	1187	1153
Marketing and administration	879	939	882
Interest (8)	126	126	104
Total expenses	6209	6373	5285
Revenues less expenses	2546	2431	1779
Depreciation and amortization	260	322	343
Earnings before taxes and levies	2286	2109	1436
Taxes and levies (5)	1766	1415	996
Earnings from operations	520	694	440
Unusual items (10)	—	(50)	(155)
Earnings after unusual items	520	644	285
	dollars		
Per-share information			
Earnings from operations (18)	3.24	4.27	2.69
Earnings after unusual items (18)	3.24	3.97	1.74
Dividends	1.45	1.65	1.60

The notes referred to on this and the following two pages are found in the Notes to the financial statements, pages 34 to 41.

The glossary of terms and the summary of accounting policies are found on pages 28 and 32 respectively.

Consolidated statement of changes in financial position

For the years	1984	1985	1986
	millions of dollars		
	inflows (outflows)		
Funds provided from operating activities			
Revenues less expenses other than exploration	2609	2516	1895
Current taxes and levies (5)	(1612)	(1300)	(928)
	997	1216	967
Work-force reduction programs (10)	—	—	(29)
Change in operating working capital	(56)	56	391
Dividends	(233)	(268)	(262)
Total funds provided from operating activities	708	1004	1067
Investment of funds			
Capital and exploration expenditures	(679)	(1158)	(648)
Proceeds from sale of property, plant and equipment	42	50	53
Other	(27)	(37)	5
Total investment of funds	(664)	(1145)	(590)
Inflow (outflow) of funds before external financing	44	(141)	477
External financing			
Long-term debt and other obligations, after repayments	(30)	7	19
Retirement of 15½ percent debentures (10)	—	—	(315)
Common shares issued (18)	74	76	23
Total external financing	44	83	(273)
Inflow (outflow) of funds	88	(58)	204
Increase (decrease) in funds by component			
Marketable securities	193	(130)	213
Outstanding cheques, less cash	(97)	62	(10)
Short-term notes	(8)	10	1
Total increase (decrease) in funds	88	(58)	204

The glossary of terms and the summary of accounting policies are found on pages 28 and 32 respectively.

Consolidated statement of financial position

As at December 31	1985	1986	change
			millions of dollars
Capital employed			
Working capital			
Current assets			
Marketable securities at cost, which approximates market value (19)	519	732	213
Accounts receivable (3)	984	664	(320)
Amounts receivable from Exxon Corporation and affiliates (17)	—	6	6
Inventories of crude oil and products	1294	819	(475)
Materials, supplies and prepaid expenses	143	135	(8)
Taxes recoverable	—	62	62
Total current assets	2940	2418	(522)
Current liabilities			
Outstanding cheques, less cash	66	76	10
Short-term notes	1	—	(1)
Accounts payable and accrued liabilities (3)	1100	766	(334)
Amounts owing to Exxon Corporation and affiliates (17)	49	—	(49)
Taxes payable	42	—	(42)
Dividends payable	68	65	(3)
Total current liabilities	1326	907	(419)
Total working capital	1614	1511	(103)
Investments and other long-term assets (7)	576	414	(162)
Property, plant and equipment at cost, less accumulated depreciation and amortization (6)	5680	5816	136
Total capital employed	7870	7741	(129)
Sources of capital employed			
Long-term debt and other obligations (9, 17)	1219	1034	(185)
Commitments and contingent liabilities (11)			
Deferred income taxes (5)	1607	1617	10
Shareholders' equity			
Common shares (18)	1400	1423	23
Earnings retained and used in the business			
At beginning of year	3268	3644	376
Earnings for the year	644	285	(359)
Dividends	(268)	(262)	6
At end of year	3644	3667	23
Total shareholders' equity	5044	5090	46
Total sources of capital employed	7870	7741	(129)

The summary of accounting policies, glossary of terms and notes are part of the financial statements.

Approved by the board

Arden R. Haynes

Chairman, president and
chief executive officer

A. J. Young

Executive vice-president and
chief financial officer

Auditors' report

Summary of significant accounting policies

To the shareholders of Imperial Oil Limited

We have examined the consolidated statements of earnings and changes in financial position of Imperial Oil Limited for each of the three years in the period ended December 31, 1986 and the consolidated statement of financial position as at December 31, 1985 and 1986. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the results of operations and changes in financial position of the company for each of the three years in the period ended December 31, 1986 and its financial position as at December 31, 1985 and 1986 in accordance with generally accepted accounting principles in Canada consistently applied.

Pricewaterhouse

Chartered Accountants
Toronto-Dominion Centre
Toronto, Ontario
February 23, 1987

Principles of consolidation

The consolidated financial statements include the accounts of Imperial Oil Limited and all its subsidiary companies. Intercompany accounts and transactions are eliminated. A list of subsidiary companies is shown on page 41.

A significant portion of the company's activities in natural resources is conducted jointly with other companies. The accounts reflect the company's proportionate interest in such activities.

Inventories

Inventories of crude oil at refineries and products are recorded at cost (primarily using the average-cost method). Crude oil in transit is valued at actual cost. The cost of these inventories is less than net realizable value.

Inventories of materials and supplies are recorded either at cost or net realizable value, whichever is lower.

Investments

The principal investments in companies other than subsidiaries are accounted for using the equity method. Imperial's share of the net assets of these companies is recorded in the consolidated statement of financial position as "investments." Imperial's share of the earnings after income taxes of these companies is included in the consolidated statement of earnings under the revenue line "interest and investment income."

Other investments are recorded at cost. The only income recorded by Imperial is the dividends from these investments.

The percentage owned by Imperial of each of its principal investments is shown on page 41. The amount at which all investments are recorded is shown in note 7 on page 36.

Property, plant and equipment

Property, plant and equipment, including related preoperational costs and design costs of major projects, are recorded at cost.

The company follows the successful-efforts method of accounting for costs of exploration and development activities. Costs of exploration acreage are capitalized and amortized over the period of exploration or until a discovery is

made. Costs of exploratory wells are capitalized until their economic status has been evaluated. Costs of exploratory wells found to be dry during the year or before the issuance of the annual financial statements are charged against earnings. All other exploration costs are charged against earnings as incurred. All costs of development wells and successful exploration wells are capitalized.

The costs of maintenance and repairs are charged to operating expenses. Improvements that increase the service capacity of an asset or prolong its service life beyond that contemplated in the established rates of depreciation are capitalized.

The cost of natural gas and natural gas liquids used as injectants in enhanced (tertiary) oil-recovery projects is capitalized as a development cost.

Investment tax credits, grants received under the Petroleum Incentives Program and other similar grants are treated as a reduction of the capitalized costs of the asset to which they apply.

Amortization of the capitalized costs of producing wells and leases, of the Syncrude project and Cold Lake plants and of operating mines are calculated using the unit-of-production method. Depreciation of other plant and equipment is calculated using the straight-line method, based on the estimated service life of the asset.

Gains or losses on assets sold or otherwise disposed of are included in the consolidated statement of earnings.

Retirement plans

The company's pension plans cover almost all employees. Pension-benefit obligations are determined annually by independent actuaries using the projected-unit-credit method. Valuation of assets is based on market values at December 31 of each year. The amounts contributed by the company to the plans are established according to accepted actuarial procedures. Prior to 1986, the amount funded was also the pension expense for the year. In 1986 the Canadian Institute of Chartered Accountants published new standards for accounting for pension plans. As a result, starting in 1986 the amount expensed is determined on the accrual basis, which reflects the service of employees for the year rather than the amount contributed by the company to the plans.

Consumer taxes and Crown royalties

Taxes levied on the consumer and collected by the company are excluded from the consolidated statement of earnings. These are primarily provincial taxes on motor fuels and the federal tax on exports of crude oil and petroleum products. Crown royalties are also excluded from the consolidated statement of earnings.

In order to encourage investment, the federal and provincial governments have reduced the amount of royalties payable during the early years of certain projects by allowing for the deduction of certain capital costs in determining the royalty. The result is an increase in the company's share of production, which is accounted for as additional income.

Translation of foreign currencies

Gains and losses on forward exchange contracts, which are effective hedges against specific foreign currency exposures, are offset against the associated gains and losses of the hedged item.

Long-term monetary liabilities payable in foreign currencies have been translated at the rates of exchange prevailing on December 31. Exchange gains and losses arising from the translation of long-term debt are amortized over the remaining term of the debt.

Interest costs

Interest costs are included in expenses as incurred.

Notes to the financial statements

1. Reporting changes

In 1986, the company changed its method of accounting for inventories of crude oil at refineries and products from the first-in, first-out method (FIFO) to the average-cost method. (Crude oil in transit continues to be valued at actual cost.) The average-cost method provides a better matching of costs and revenues, particularly in a period of changing crude oil prices. The adoption of the average-cost method has been applied retroactively and prior periods have been restated.

The effect on 1986 and prior years' earnings after unusual items, working capital and earnings per share was:

	Increase (decrease)		
	Earnings after unusual items	Working capital	Earnings per share
	(millions of dollars)		(dollars)
1986	4	1	.02
1985	10	(6)	.06
1984	(13)	(23)	(.08)
1983	4	1	.03
1982	9	(7)	.05

2. Crude-oil revenues

The company supplements its own production to meet its refining needs by buying crude oil and selling any unused quantities. Those sales, which amounted to \$990 million in 1986, are excluded from reported revenues and purchases (1985—\$1693 million; 1984—\$1354 million).

3. Petroleum product purchase/sale agreements

Purchase/sale agreements with other companies help the company meet its supply requirements while reducing transportation and other costs. Sales under those agreements are not included in "revenues," but are offset against the related purchases. In 1986 sales under those agreements amounted to \$819 million (1985—\$934 million; 1984—\$964 million). Accounts-receivable and accounts-payable balances with each company relating to such purchase/sale agreements have been offset.

4. Interest and investment income

	1984	1985	1986
	millions of dollars		
Interest on marketable securities and short-term deposits	65	69	47
Earnings (after income taxes) from equity investments	37	38	35
Other interest and investment income	65	30	18
Total interest and investment income	167	137	100
Dividends received from equity investments	21	22	22

5. Taxes and levies

	1984	1985	1986
	millions of dollars		
Current and deferred income taxes			
Federal	367	246	178
Provincial	111	78	75
Revenue taxes			
Petroleum and Gas Revenue Tax	150	125	7
Commodity, property and other taxes			
Federal sales tax	347	360	385
Fuel excise taxes	101	145	261
Property and other taxes	86	89	90
Levies (1)			
Petroleum Compensation Charge	473	321	—
Canadian Ownership Special Charge	131	51	—
Total taxes and levies	1766	1415	996
Less deferred income taxes	154	115	68
Current taxes and levies	1612	1300	928

(1) These charges expired June 1, 1985.

The operations of the company are complex and the related income and other tax interpretations, regulations and legislation are continually changing. As a result, there are usually some tax matters in question. The company believes the provision made for income and other taxes is adequate.

Summary of income-tax calculations	1984	1985	1986
	millions of dollars		
Earnings before taxes and levies	2286	2109	1436
Deduct:			
Taxes and levies, other than income taxes	1288	1091	743
Earnings from equity investments	37	38	35
Adjusted earnings	961	980	658
Basic corporate tax rate (percent)	47.8	47.1	50.2
Income taxes at basic rate	459	462	330
Additions to income taxes as a result of:			
Petroleum and Gas Revenue Tax, Crown royalties and other similar non-deductible payments to governments	215	156	58
	674	618	388
Reduction in income taxes as a result of:			
Resource allowance	121	120	81
Depletion allowance	42	85	18
Manufacturing and processing credit	9	6	16
Inventory allowance	19	21	3
Other (1)	5	62	17
Income taxes	478	324	253
Effective income-tax rate (percent)	49.7	33.1	38.4
Increases (decreases) in deferred income taxes resulting from timing differences			
Capital cost allowance	136	75	(13)
Successful drilling	36	35	57
Land-acquisition costs	(4)	(23)	(5)
Enhanced oil-recovery injectants	—	23	33
Other	(14)	5	(4)
Net increase in deferred income taxes (2)	154	115	68
Current income taxes (2)	324	209	185

(1) In 1985 the company sold interests in certain producing properties, with the right to reacquire them. These interests were reacquired in 1986. Due to deductions available for

these transactions, no additional income tax was payable. This item includes \$42 million in respect of these transactions in 1985 and \$10 million in 1986.

(2) Changes in income taxes as a result of unusual items recorded in 1985 and 1986 are not included.

6. Property, plant and equipment

	Cost		Accumulated depreciation and amortization	
	1985	1986	1985	1986
	millions of dollars			
Natural resources				
Exploration and production	2751	2903	908	1019
Heavy oil	1411	1524	169	216
Coal and other minerals	168	203	20	23
	4330	4630	1097	1258
Petroleum products	2557	2657	1127	1202
Chemicals	1091	1117	273	322
Other	306	313	107	119
Total property, plant and equipment	8284	8717	2604	2901
Less accumulated depreciation and amortization	2604	2901		
Net investment	5680	5816		

Notes to the financial statements

7. Investments and other long-term assets

Investments are primarily in companies engaged in pipeline transportation of crude oil and petroleum products.

Investments	1985	1986
	millions of dollars	
Recorded at equity value (a):		
With quoted market value (b)	186	200
Without quoted market value	22	22
Recorded at cost	5	5
Total investments	213	227
Long-term receivables	152	49
Other (c)	211	138
Total investments and other long-term assets	576	414

(a) The principal investments in companies other than subsidiaries are accounted for using the equity method. These principal investments are recorded at the original cost of the investment plus Imperial's share of earnings since the investment was made, less dividends received. Imperial's principal investments and ownership percentages are shown on page 41.

(b) This amount represents Imperial's investment in Interprovincial Pipe Line Limited. Imperial owns 8.597 million shares (22 percent) of Interprovincial; the original cost to Imperial was \$18 million. The market value of these shares at December 31, 1986, was \$344 million (1985—\$368 million).

(c) Included in this category is \$42 million, which is the unamortized cost of estimated future benefits associated with the company's health-care and life-insurance plans for retired employees. This item is being amortized over 17 years, starting in 1985. The plans are described further in note 15. As well, this category includes \$45 million, which represents the unamortized foreign-exchange loss arising on translation of long-term debt (1985—\$91 million).

8. Interest expense

	1984	1985	1986
	millions of dollars		
Long-term debt	107	107	84
Short-term notes	4	2	3
Capitalized leases	13	12	11
Other	2	5	6
Total interest expense	126	126	104

9. Long-term debt and other obligations

			1985	1986
year of issue	maturity date	rate of interest	millions of dollars	
Debentures				
1967	Jan. 2, 1987	6¾	10	—
1968	Jan. 2, 1988	7⅜	12	12
1969	Aug. 15, 1989	8½	9	7
1972	Feb. 15, 1992	7¾	17	17
1974	Aug. 15, 1994	10⅝	63	60
1975	Feb. 15, 1995	9¾	66	65
1979	Sept. 15, 2009			
	(1986—U.S. \$226 million;			
	1985—U.S. \$226 million)	9¾	316	312
1981	Dec. 1, 2011			
	(U.S. \$200 million)	15½	280	—
Total sinking-fund debentures			773	473
1983	Mar. 31, 1993	12	125	125
Total long-term debt (a)			898	598
Capitalized leases (a) (b)			84	70
Other obligations (c) (d) (e)			237	366
Total long-term debt and other obligations			1219	1034

(a) Payments of principal required during the next five years for:

	Sinking-fund debentures	Capitalized leases
	millions of dollars	
1987	13	5
1988	23	4
1989	18	3
1990	13	2
1991	13	1

(b) Imputed interest on capitalized leases will be \$45 million during the next five years and \$105 million over the remaining life of the leases.

(c) Other obligations at December 31, 1986, include \$61 million (1985 – \$75 million) related to take-or-pay gas contracts. Amounts received under these contracts for future delivery of natural gas are recorded as deferred revenue. These amounts are included in sales revenue when the gas is delivered.

(d) Other obligations at December 31, 1986, also include a \$58 million liability for the company's health-care and life-insurance plans for retired employees. These plans are described further in note 15.

(e) Other obligations at December 31, 1986, also include \$102 million, which represents the liability for future payments to employees retiring under the 1986 voluntary work-force reduction programs (see note 10).

Unused lines of credit with major Canadian banks totaled \$596 million at December 31, 1986 (1985 – \$597 million).

10. Unusual items

	1984	1985	1986
	millions of dollars		
Deferral of producing profits	–	(45)	–
Granduc mine	–	(5)	–
Retirement of debentures	–	–	(65)
Work-force reduction programs	–	–	(90)
Total unusual items	–	(50)	(155)

Deferral of producing profits – The company's 1985 earnings were adjusted to reflect a one-time, noncash decrease of \$45 million, after income-tax credits of \$42 million, resulting from the June 1, 1985, deregulation of crude-oil pricing. Prior to June 1, the corporation was required to sell crude oil produced from Crown leases to the Alberta Petroleum Marketing Commission and recorded a sale at such time. This requirement has been removed. Consequently, the profit on company-produced crude oil used in the manufacture of petroleum products is deferred until the petroleum products are sold to the customer. This change had a one-time impact on earnings but had no effect on the company's cash flow.

Granduc mine – In late 1982 the company decided to wind down operations at the Granduc copper mine in British Columbia. An unusual item of \$40 million, after income-tax credits of \$26 million, was charged to earnings at that time to write the assets down to estimated net realizable value. The closure of the mine was completed in 1985 and the amount of the write-down was increased by \$5 million, after income-tax credits of \$3 million, mainly due to lower-than-anticipated copper prices during the wind-down period.

Retirement of debentures – During the second quarter of 1986, the company took steps to retire its (U.S.) \$200 million issue of 15 1/2 percent sinking fund debentures due December 1, 2011. The total cost of retiring the debt was (Canadian) \$315 million, which came from existing cash reserves. The premium paid for the retirement of the debentures, as well as a foreign-exchange loss arising from the transactions, resulted in a loss of \$65 million, or \$0.40 a share, after income-tax credits of \$10 million. This loss was recorded in the second quarter.

Work-force reduction programs – In March 1986 the company announced plans to reduce its work force, mainly through two voluntary programs that offered eligible employees enhanced pension benefits for early retirement and offered others lump-sum payments for leaving the company. The staff reduction and associated reorganization resulted in a charge to earnings in the second quarter of \$90 million after income-tax credits of \$81 million. Of this amount, \$29 million had been paid out by the end of 1986.

11. Commitments and contingent liabilities

The future liability for long-term contractual obligations and commitments, all arising in the normal course of business, does not significantly affect the company's consolidated financial position.

Pending lawsuits against the company would not, in the opinion of counsel, result in any financial liability that would significantly affect the company's consolidated financial position and earnings.

Notes to the financial statements

12. Business segments (1)

	Natural resources			Petroleum products			Chemicals		
	1984	1985	1986	1984	1985	1986	1984	1985	1986
Revenues									
Sales to customers	1094	758	487	6541	6919	5459	750	758	732
Intersegment sales	646	1497	1193	275	346	313	57	47	48
Total revenues	1740	2255	1680	6816	7265	5772	807	805	780
Earnings before taxes and levies	883	1016	319	1299	1048	1004	44	7	33
Taxes and levies	559	474	123	1166	946	830	22	4	16
Earnings from operations	324	542	196	133	102	174	22	3	17
Capital employed									
Segment assets	2937	3663	3708	3413	3531	2521	1062	1064	1006
Less current liabilities	514	557	186	969	942	517	48	56	59
Total capital employed	2423	3106	3522	2444	2589	2004	1014	1008	947
Depreciation and amortization	124	177	180	87	100	103	46	48	50
Capital and exploration expenditures	511	885	457	129	218	143	23	24	29

In the consolidated figures reported here, all intersegment transactions have been eliminated. The company operates its business in the segments described in the operating reviews.

The information in the table above is presented as though each segment were a separate business activity. Intersegment sales are made essentially at prevailing market prices.

13. Long-term incentive compensation plan

Monetary awards are granted to retain selected employees and reward them for high performance. The amounts of the awards are based on increases over time in the price of Class A convertible shares or in earnings per share, whichever is greater. Holders of the awards are not eligible to receive payments at the time the awards are granted; payments are deferred for periods of up to six years, depending on the type of award.

Estimated costs of the plan are amortized over its life. In 1986 the company charged \$20 million to earnings (1985—\$20 million; 1984—\$20 million).

14. Research and development costs

Research and development costs in 1986 were \$79 million (1985—\$79 million; 1984—\$63 million) before investment tax credits earned on these expenditures of \$12 million (1985—\$10 million; 1984—\$14 million). The net costs were included in expenses.

15. Annuitant health care and life insurance

The company shares the cost of certain health-care and life-insurance benefits for retired employees. Almost all of the company's employees may become eligible for those benefits when they retire from the company.

In 1985 the method used to charge costs against earnings was changed from a pay-as-you-go method to a method that recognizes a liability at retirement. Under the new method, estimated future benefits are now charged to earnings in the year an employee retires and the related liability is reduced by the annual cash costs of the benefits.

As a result of this change, a liability (included in "other obligations"—see note 9) has been recorded for employees who retired before 1985. This initial liability was not charged to earnings in 1985 but was deferred and is being charged to earnings over a 17-year period. This is described further in note 7(c). Total charges to earnings in 1986 amounted to \$19.4 million (1985—\$12.2 million; the 1984 amount under the pay-as-you-go method was \$5.7 million).

Other investments			Consolidated		
1984	1985	1986	1984	1985	1986
millions of dollars					
370	369	386	8755	8804	7064
15	18	19	—	—	—
385	387	405	8755	8804	7064
60	38	80	2286	2109	1436
19	(9)	27	1766	1415	996
41	47	53	520	694	440
1331	1150	1558	8678	9196	8648
(98)	(17)	290	1368	1326	907
1429	1167	1268	7310	7870	7741
3	(3)	10	260	322	343
16	31	19	679	1158	648

(1) Data for 1984 and 1985 have been restated to reflect the change in the method of inventory valuation described in note 1 to the audited financial statements.

16. Employee retirement plans

The pension plans cover almost all company employees and generally are based on length of service and on average earnings during the final three years of employment. The plans are funded by the company, based on actuarial valuation, the most recent being December 31, 1985. As well, the amounts include the company's share of the pension plans for the Syncrude joint venture.

Funded status at December 31	1984	1985	1986
millions of dollars			
Market value of assets	1057	1296	1319
Accumulated benefit obligation (1)	842	898	1067
Assets excess	215	398	252
Unearned benefit obligation (1)	308	328	222
(Unfunded liability) Surplus	(93)	70	30

The benefit obligation for 1986 is affected by the 1986 early-retirement program and an updating of the actuarial assumptions.

The surplus/unfunded liability is credited/charged to expense over the average remaining service life of employees, which is currently 17 years.

In addition, actuarially determined obligations to surviving spouses (which are paid directly by the company) amount to \$150 million at December 31, 1986.

Annual pension expense

In accordance with new accounting standards, the pension expense for 1986 is calculated on the accrual basis rather than the funding basis used in prior years. (See summary of significant accounting policies.)

	1984	1985	1986
millions of dollars			
Current service cost	—	—	33
Interest cost	—	—	5
Plan amendment amortization	—	—	1
Expense for 1984 and 1985 based on funding method	32	34	—
Pension expense before 1986 early-retirement program	32	34	39
Expense of 1986 early-retirement program (2)	—	—	109
Total pension plan expense	32	34	148

Assumptions

The measurement of the retirement obligation and expense involves making assumptions about economic and other factors over an extended future period. In order to aid in understanding the information provided above, the following provides the most significant assumptions and their impact.

	1984	1985	1986
Rate of return on the plan's assets (percent)	7.0	7.0	8.5
Salary escalation rate (percent)	5.0	5.0	6.0
millions of dollars			
Impact of a one percent increase in rate of return on total benefit obligation (1)			(160)
annual expense			(9)
Impact of a one percent increase in salary escalation on total benefit obligation (1)			22
annual expense			1

(1) The total benefit obligation is the amount the pension fund needs to have invested at the assumed rate of return (currently 8.5 percent) in order to be able to pay pensions for service rendered to date. This obligation has two parts. The accumulated benefit obligation is based on current salaries and the unearned benefit obligation is the estimated additional amount due to salary escalation by the time of retirement.

(2) This amount is part of the work-force reduction programs included in unusual items (note 10).

Notes to the financial statements

17. Transactions with Exxon Corporation and affiliated companies (Exxon)

The net amount of outflows by Imperial from transactions with Exxon was \$35 million in 1986. Transactions with Exxon resulted in a net outflow of \$244 million in 1985 and a net inflow of \$197 million in 1984. The terms of the transactions were competitive or as favorable as they would have been with unrelated parties. The transactions were to maintain supplies of crude oil, petroleum and petrochemical products to customers. Current amounts due from Exxon at December 31, 1986, were \$6 million (1985—\$49 million due to Exxon; 1984—\$15 million due from Exxon). "Other obligations," reported in note 9, include \$7 million due to Exxon at December 31, 1986 (1985—\$7 million; 1984—\$6 million).

In 1986, Exxon acquired 298 984 shares under the company's dividend reinvestment and share purchase plan described further in note 18 (1985—1 509 122 shares; 1984—1 323 071 shares). Exxon's ownership interest in Imperial at December 31, 1986, was 69.6 percent (1985—69.6 percent).

18. Common shares

	1984	1985	1986
	number of shares		
Authorized			
(Class A and B)	200 000 000	200 000 000	200 000 000
Issued			
at December 31 (a)			
Class A	158 496 912	161 879 023	162 505 798
Class B	3 078 171	1 301 915	1 140 174
Total	161 575 083	163 180 938	163 645 972
Transactions during the year:			
Dividend reinvestment and share purchase plan (b)			
Number of shares issued	1 777 917	1 545 879	422 621
	millions of dollars		
Amount	67.0	73.0	20.4
Class B stock dividends paid			
Number of shares issued	121 374	59 976	42 413
	millions of dollars		
Amount	4.7	3.0	1.9
Employee stock options (c)			
Number exercised	86 070	—	—
	millions of dollars		
Amount	2.2	—	—
	millions of dollars		
Fair Market value	3.2	—	—
Number outstanding at December 31	—	—	—

(a) Holders of both Class A and Class B shares have voting privileges. The shares are convertible on a share-for-share basis and rank equally in all respects. Holders of Class B shares receive a stock dividend of Class B shares with values substantially equivalent to the cash dividend on Class A shares.

(b) The plan enabled shareholders to reinvest their cash dividends in additional Class A shares at five percent less than the average market price. Shareholders could also invest between \$50 and \$5000 each calendar quarter in additional Class A or Class B shares at an average market price without paying brokerage or other fees. This plan was modified in 1986 and further information is provided on page 58.

(c) When the options were granted, fair market value ranged from \$28.00 to \$42.375 per share. All options expired on July 15, 1984.

Earnings per share are calculated on the monthly weighted average number of shares outstanding during the year (1986–163 611 000; 1985–162 320 000; 1984–160 376 000).

19. Marketable securities

The company's cash that is not immediately required for reinvestment in the business is invested primarily in Canadian marketable securities. These investments are comprised primarily of securities of the governments of Canada and the provinces, banks and other high-quality corporations.

20. United States accounting principles

The financial statements have been prepared in accordance with accounting principles generally accepted in Canada. A description of the differences between the accounting principles generally accepted in Canada and the United States as they apply to the company appears on page 54.

Supplemental information (unaudited)

Additional information for security holders is provided on pages 48 to 58.

Since the company uses capital markets in the United States, these pages include information that conforms with the financial reporting practices of that country.

The information reported on pages 48 to 51 is provided in accordance with the United States' Statement of Financial Accounting Standards No. 69, "Disclosures about Oil and Gas Producing Activities." This statement requires specific disclosure about oil and gas activities only; accordingly, the data exclude information about coal and mineral activities and certain corporate overhead expenses reported in the natural resource segment.

Subsidiaries and principal investments

Subsidiary companies (a)

Atlas Supply Company of Canada Limited
Beaverhill Resources Limited
Building Products of Canada Limited
Byron Creek Collieries (1983) Limited
Canada Wide Mines Ltd.
Champlain Oil Products Limited
Chinchaga Resources Limited
Devon Estates Limited
ESF Limited
Esso Chemical Alberta Limited
Esso of Canada Limited
Esso Resources Canada Limited
The Imperial Pipe Line Company, Limited
Maple Leaf Petroleum Limited
Metro Fuel Co. Ltd.
Nisku Products Pipe Line Company Limited
Northwest Company, Limited
107580 Canada Inc.
139675 Canada Ltd.
Pinpoint Retail Systems Inc.
Renown Building Materials Limited
Servacar Ltd.
Taglu Enterprises Limited
305120 Alberta Ltd.
Winnipeg Pipe Line Company Limited
(a) See page 32, Principles of consolidation.

Principal investments in other companies, not consolidated (b)

	Percentage of ownership
Alberta Products Pipe Line Ltd.	35.0
Interprovincial Pipe Line Limited	21.7
Montreal Pipe Line Limited	32.0
Rainbow Pipe Line Company, Ltd.	33.3
Tecumseh Gas Storage Limited	50.0
Williamsport Properties Limited	50.0

(b) See page 32, Investments.

Five-year summary

Financial*

Percentages and ratios

	1982	1983	1984	1985	1986
Return on average					
Capital employed (1)					
Before unusual items	5.8	6.1	8.4	10.0	6.3
After unusual items	5.4	5.4	8.4	9.4	4.3
Shareholders' equity	6.8	7.1	11.8	13.4	5.6
Debt as a percentage of					
Capital employed (2)	16.0	17.4	16.2	15.5	13.4
Debt plus shareholders' equity (2)	20.1	21.8	20.5	19.5	16.9
Interest coverage (3)	7.0	7.3	8.9	9.1	7.7
Reinvestment percentage (4)	154.6	106.2	93.8	114.0	55.3
Current ratio (5)	2.6	2.4	2.3	2.2	2.7

Definitions

(1) The return consists of the average capital employed divided into the sum of the earnings (before or after unusual items), the after-tax long-term-debt interest expense and the capitalized leases interest expense.

(2) Debt consists of long-term debt, capitalized leases and other obligations.

(3) Interest coverage is total interest expense divided into the sum of consolidated earnings from operations, total interest expense and consolidated income taxes on earnings from operations.

(4) Reinvestment percentage is the total investment of funds in the year divided by the total funds provided from operating activities.

(5) Current ratio is current assets divided by current liabilities.

Consolidated statement of earnings

	1982	1983	1984	1985	1986
	millions of dollars				
Revenues					
Crude oil	714	777	830	548	249
Natural gas	208	185	185	148	149
Petroleum products	6178	6231	6366	6761	5356
Chemicals	626	694	753	762	732
Other operating revenues	385	412	454	448	478
Interest and investment income	159	108	167	137	100
Total revenues	8270	8407	8755	8804	7064
Expenses					
Exploration	113	81	63	85	116
Purchases of crude oil and products	3710	4107	4073	4036	3030
Extracting, processing and manufacturing	1016	1056	1068	1187	1153
Marketing and administration	763	781	879	939	882
Interest	115	121	126	126	104
Total expenses	5717	6146	6209	6373	5285
Revenues less expenses	2553	2261	2546	2431	1779
Depreciation and amortization	219	235	260	322	343
Earnings before taxes and levies	2334	2026	2286	2109	1436
Taxes and levies	2036	1690	1766	1415	996
Earnings from operations	298	336	520	694	440
Unusual items	(22)	(42)	—	(50)	(155)
Earnings after unusual items	276	294	520	644	285

*Data for the years 1982 to 1985 have been restated to reflect the change in the method of inventory valuation described in note 1 to the audited financial statements.

Consolidated statement of changes in financial position

	1982	1983	1984	1985	1986
	millions of dollars inflows (outflows)				
Funds provided from operating activities					
Revenues less expenses					
other than exploration	2666	2342	2609	2516	1895
Current taxes and levies	(1705)	(1545)	(1612)	(1300)	(928)
	961	797	997	1216	967
Work-force reduction					
programs	—	—	—	—	(29)
Change in operating					
working capital	(9)	139	(56)	56	391
Dividends	(220)	(222)	(233)	(268)	(262)
Total funds					
provided from					
operating activities	732	714	708	1004	1067
Total investment of					
funds	(1132)	(758)	(664)	(1145)	(590)
Inflow (outflow) of funds					
before external					
financing	(400)	(44)	44	(141)	477
External financing					
Long-term debt and other					
obligations, after					
repayments	63	121	(30)	7	19
Retirement of 15½ percent					
debentures	—	—	—	—	(315)
Common shares issued	14	60	74	76	23
Total external financing	77	181	44	83	(273)
Inflow (outflow) of funds	(323)	137	88	(58)	204

Consolidated statement of financial position

	1982	1983	1984	1985	1986
	millions of dollars				
Capital employed					
Funds	285	422	510	452	656
Operating working capital	1398	1259	1315	1162	855
Investments and other					
long-term assets	286	450	511	576	414
Property, plant and					
equipment (net)	4446	4660	4974	5680	5816
Total capital employed	6415	6791	7310	7870	7741
Sources of capital employed					
Long-term debt					
and other obligations	1028	1180	1184	1219	1034
Deferred income taxes	1288	1380	1534	1607	1617
Shareholders' equity	4099	4231	4592	5044	5090
Total sources of					
capital employed	6415	6791	7310	7870	7741
Total assets	7456	7969	8678	9196	8648

**Capital and exploration expenditures
(after deducting incentives)**

	1982	1983	1984	1985	1986
	millions of dollars				
Natural resources					
Exploration	93	47	48	97	81
Production	206	246	209	315	187
Heavy oil	42	102	231	379	133
Coal and other minerals	58	30	23	94	56
Total natural resources	399	425	511	885	457
Petroleum products					
Marketing	31	46	83	106	75
Refining	301	108	46	112	68
Total petroleum					
products	332	154	129	218	143
Chemicals	368	109	23	24	29
Other investments	35	11	16	31	19
Total capital					
and exploration					
expenditures	1134	699	679	1158	648

Five-year summary

Financial*

Net payments to governments

	1982	1983	1984	1985	1986
	millions of dollars				
Taxes and levies					
Income taxes (1)	393	424	478	324	253
Revenue taxes	175	170	150	125	7
Commodity, property and other taxes	554	504	534	594	736
Levies (2)	914	592	604	372	—
Total taxes and levies	2036	1690	1766	1415	996
Add:					
Current taxes on unusual items	(6)	(15)	—	(3)	(33)
Consumer taxes collected on behalf of governments	618	608	967	1078	1119
Crown royalties	505	492	404	377	153
	3153	2775	3137	2867	2235
Less deferred income taxes	331	145	154	115	68
Total paid or payable to governments	2822	2630	2983	2752	2167
Receipts from governments					
Oil-import compensation (2)	422	149	105	57	—
Syncrude crude-oil price compensation (2)	117	86	83	60	—
Investment tax credits	20	24	44	71	99
Incentive programs	10	8	9	17	9
Total received or receivable from governments	569	267	241	205	108
Net payments to governments	2253	2363	2742	2547	2059
Net payments to					
Federal government	1139	1161	1610	1465	1201
Provincial governments	1058	1143	1067	1016	790
Local governments	56	59	65	66	68
Net payments to governments	2253	2363	2742	2547	2059

(1) Under a federal government program encouraging taxpayers to support Canadian scientific research, Imperial made payments to Canadian companies in lieu of income-tax payments to the government. Those payments provided the company with income-tax credits totaling \$393 million, which were applied to the payment of 1983 and 1984 income taxes reported above.

(2) Payments and receipts relating to these programs and charges expired on June 1, 1985.

Financial information by segment

	1982	1983	1984	1985	1986
	millions of dollars				
Revenues					
Natural resources	1484	1718	1740	2255	1680
Petroleum products	6638	6702	6816	7265	5772
Chemicals	682	742	807	805	780
Other investments	328	311	385	387	405
Intersegment sales	(862)	(1066)	(993)	(1908)	(1573)
Total revenues	8270	8407	8755	8804	7064
Earnings from operations					
Natural resources	120	272	324	542	196
Petroleum products	155	65	133	102	174
Chemicals	(1)	(10)	22	3	17
Other investments	24	9	41	47	53
Total earnings from operations	298	336	520	694	440
Capital employed					
Natural resources	2066	2094	2423	3106	3522
Petroleum products	2512	2553	2444	2589	2004
Chemicals	1030	1123	1014	1008	947
Other investments	807	1021	1429	1167	1268
Total capital employed	6415	6791	7310	7870	7741
Return on average capital employed					
	percent				
Natural resources	5.9	13.1	14.3	19.6	5.9
Petroleum products	6.3	2.6	5.3	4.1	7.6
Chemicals	(0.1)	(0.9)	2.1	0.3	1.8
Other investments	8.8	7.9	8.7	8.6	8.4
Return on average capital employed (after unusual items)	5.4	5.4	8.4	9.4	4.3

*Data for the years 1982 to 1985 have been restated to reflect the change in the method of inventory valuation described in note 1 to the audited financial statements.

Five-year summary

Operating

Wells drilled (1)	1982		1983		1984		1985		1986	
	gross	net	gross	net	gross	net	gross	net	gross	net
Western provinces										
Exploratory										
Conventional	36	11	41	18	34	17	55	25	27	10
Heavy oil	75	21	40	12	77	16	79	56	84	58
Development										
Conventional	34	13	114	56	362	117	397	137	299	85
Heavy oil	29	29	210	210	349	346	554	550	116	100
Northern areas and Atlantic offshore (2)										
Exploratory	5	1	9	3	10	2	13	4	14	7
Development	12	8	30	20	38	26	35	22	13	8
Other provinces										
Exploratory	—	—	1	—	—	—	—	—	—	—
Total wells drilled										
Exploratory	116	33	91	33	121	35	147	85	125	75
Development	75	50	354	286	749	489	986	709	428	193
Total wells in progress	60	52	16	8	30	17	40	14	21	10
Land holdings (1) millions of hectares										
Oil and gas										
Western provinces										
Conventional	5.3	1.3	2.5	0.9	2.4	0.9	2.3	0.9	2.3	0.9
Other	1.0	0.4	1.0	0.4	1.0	0.4	1.0	0.4	1.0	0.4
Northern areas (2)	9.8	3.9	10.5	3.8	9.6	3.5	8.7	2.6	5.0	1.4
Atlantic offshore	6.0	4.7	4.4	3.6	4.0	3.3	2.5	1.9	1.6	1.0
Other provinces (3)	1.8	0.4	1.9	0.4	1.9	0.4	1.9	0.4	—	—
Total oil and gas land holdings	23.9	10.7	20.3	9.1	18.9	8.5	16.4	6.2	9.9	3.7
Minerals										
Coal	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.3	0.3
Other minerals	0.6	0.5	0.5	0.3	0.3	0.1	0.6	0.3	0.7	0.4
Total minerals land holdings	1.1	1.0	1.0	0.8	0.7	0.5	1.0	0.7	1.0	0.7

One hectare equals about 2.5 acres.

(1) Gross includes the interests of others; net excludes the interests of others.

(2) Northern areas—the Arctic islands, the Yukon and the Northwest Territories, including the Beaufort Sea/Mackenzie Delta region—are often referred to as Canada Lands.

(3) This represents seismic options in the province of Quebec.

Five-year summary

Operating

	1982		1983		1984		1985		1986	
	gross	net	gross	net	gross	net	gross	net	gross	net
Proved reserves (1)										
Crude oil and natural-gas liquids (NGL) (millions of m ³)	167	125	190	145	222	172	265	208	270	213
Natural gas (billions of m ³)	52	38	50	37	51	36	55	41	56	41
Crude oil supply and utilization (thousands of m³/d)										
Crude oil production (1)										
Conventional	18.2	11.6	16.0	10.7	15.4	10.6	16.7	12.7	18.0	15.0
Cold Lake	1.8	1.7	2.3	2.1	2.9	2.7	4.5	4.4	9.7	9.5
Syncrude	3.4	2.8	4.4	3.7	3.4	3.3	5.1	4.5	5.2	5.2
Total crude oil production	23.4	16.1	22.7	16.5	21.7	16.6	26.3	21.6	32.9	29.7
Natural-gas liquids (NGL)	2.6	1.8	2.1	1.5	2.0	1.5	1.7	1.4	1.9	1.6
Total crude oil and NGL production	26.0	17.9	24.8	18.0	23.7	18.1	28.0	23.0	34.8	31.3
Net purchases from others										
Domestic	28.8		33.3		32.1		22.4		11.1	
Imported	11.5		8.8		7.8		9.4		10.5	
Total purchases and production	58.2		60.1		58.0		54.8		52.9	
Crude oil processed at company refineries										
Loco, B.C.	5.6		5.2		6.0		6.0		5.9	
Norman Wells, N.W.T.	0.5		0.5		0.5		0.5		0.5	
Strathcona, Alta.	21.1		21.9		24.8		20.4		19.4	
Sarnia, Ont.	14.1		14.9		16.3		17.2		16.4	
Montreal, Que. (2)	8.0		8.5		—		—		—	
Dartmouth, N.S.	8.9		9.1		10.4		10.7		10.7	
Total crude oil processed	58.2		60.1		58.0		54.8		52.9	
Refinery capacity at December 31	77.4		66.2		65.8		65.7		66.0	
Refinery utilization as a percentage of total capacity (2)	75		78		88		83		80	
Natural gas (millions of m³/d)										
Production (1)	7.3	5.4	6.9	5.2	6.6	4.8	5.5	4.0	5.3	4.3
Purchases	0.6		0.6		0.4		0.4		0.7	
Used in Cold Lake operations	—		—		—		(0.1)		(1.1)	
Sales	7.9		7.5		7.0		5.8		4.9	
Thermal coal production (millions of tonnes annually)	1.0		1.0		1.3		1.0		0.9	

One cubic metre (m³) is equal to approximately 6.3 barrels or 35.3 cubic feet. One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

(1) Gross reserves and production include only the amount directly owned, produced and sold by the company before deducting the shares of mineral owners or governments or both. Net reserves and production exclude these shares. (For a detailed breakdown of crude-oil and natural-gas reserves, see page 49.)

(2) The Montreal refinery ceased operations in October 1983. The calculation of capacity utilization for 1983 excludes the Montreal refinery.

Sales volumes	1982	1983	1984	1985	1986
Petroleum products (thousands of m ³ /d)(1)					
Gasolines	22.4	21.9	20.7	21.1	20.6
Jet fuels	4.3	3.7	4.5	4.9	5.0
Heating fuels	7.4	6.6	5.7	5.3	5.0
Diesel fuels	11.5	11.3	12.0	12.5	11.7
Heavy fuel oils	5.3	4.1	3.7	3.4	3.4
Liquid petroleum gas	4.2	3.4	3.1	3.3	3.6
Other products	3.2	3.4	3.3	3.6	3.4
Total petroleum products	58.3	54.4	53.0	54.1	52.7
Total domestic sales					
of petroleum products (percent)	94.6	92.8	91.1	90.4	90.2
Chemicals (thousands of tonnes per day)					
Petrochemicals	2.5	2.4	1.9	1.9	1.9
Agricultural chemicals	1.8	2.6	3.9	3.9	4.1
Average sale prices	1982	1983	1984	1985	1986
					dollars
Crude oil and NGL (per m ³)	151.90	189.55	192.43	197.48	90.88
Natural gas (per thousand m ³)	93.40	89.47	97.94	91.83	70.29

One cubic metre (m³) is equal to approximately 6.3 barrels or 35.3 cubic feet. One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

(1) Does not include sales made under purchase and sale agreements with other companies (see note 3 to the audited financial statements).

Employees

Number at December 31 (2)	15 476	14 732	14 331	14 834	12 516
Total payroll and benefits (millions of dollars)(3)	814	825	854	914	900
Payroll and benefits per employee (dollars)(4)	43 200	46 500	49 800	51 800	55 200

(2) The number of employees at December 31 includes only full-time company employees.

(3) This includes both the company's payroll and benefits as well as its share of the Syncrude joint-venture payroll and benefit costs.

(4) These are calculated by dividing the total payroll and benefits for full-time company employees by the monthly average number of full-time company employees.

Supplemental information

Oil and gas exploration and production activities

Capitalized costs	Oil and gas		Syncrude		Total	
	1985	1986	1985	1986	1985	1986
millions of dollars						
Property costs (1)						
Proved	137	142	—	—	137	142
Unproved	210	207	—	—	210	207
Producing assets	2462	2882	624	681	3086	3563
Support facilities	138	122	—	—	138	122
Incomplete construction	471	280	120	113	591	393
Total capitalized costs	3418	3633	744	794	4162	4427
Accumulated depreciation and amortization	978	1121	99	114	1077	1235
Net capitalized costs	2440	2512	645	680	3085	3192
Proportional interest in net capitalized costs of Interprovincial Pipe Line Limited	—	272	—	—	—	272
Costs incurred	1984	1985	1986	1984	1985	1986
millions of dollars						
Property costs	6	21	4	—	—	—
Exploration costs	42	76	77	—	—	—
Development costs	397	613	255	44	80	65
Results of operations						
Sales to customers	888	572	409	—	—	—
Intersegment sales	319	851	558	323	415	241
Total sales (2)	1207	1423	967	323	415	241
Production expenses	268	374	400	208	216	198
Exploration expenses	36	79	123	—	—	—
Depreciation and amortization	95	106	122	16	25	28
Petroleum and Gas Revenue Tax	140	106	7	10	19	—
Income taxes	383	308	126	32	55	(9)
Results of operations	285	450	189	57	100	24

(1) "Property costs" are payments for rights to explore for petroleum and natural gas. "Proved" represents areas where successful drilling has delineated a field capable of production. "Unproved" represents all other areas. Costs of incomplete construction include drilling and other costs relating to the discovery of commercial oil and gas reserves in the Beaufort Sea/Mackenzie Delta region.

(2) Sales of crude oil to consolidated affiliates are valued at market, using posted field prices. Sales of natural-gas liquids to consolidated affiliates are valued at amounts estimated to represent prices equivalent to those that could be obtained in a competitive, arm's-length transaction. Total sales exclude the sale of natural gas and natural-gas liquids purchased for resale.

Net reserves of crude oil and natural gas

Crude oil	Conventional and Cold Lake			Syncrude			Total		
	1984	1985	1986	1984	1985	1986	1984	1985	1986
	millions of m ³								
Net proved developed and undeveloped									
Beginning of year	116.4	144.5	169.6	28.5	27.3	38.5	144.9	171.8	208.1
Revisions of previous estimates and improved recovery	9.4	2.2	14.8	—	—	—	9.4	2.2	14.8
Purchase (sale) of reserves in place	—	(0.1)	0.1	—	—	—	—	(0.1)	0.1
Discoveries and extensions	24.1	29.7	1.5	—	12.9	—	24.1	42.6	1.5
Production	(5.4)	(6.7)	(9.5)	(1.2)	(1.7)	(1.9)	(6.6)	(8.4)	(11.4)
End of year	144.5	169.6	176.5	27.3	38.5	36.6	171.8	208.1	213.1
Net proved developed									
Beginning of year	81.0	84.3	136.0	28.5	27.3	34.7	109.5	111.6	170.7
End of year	84.3	136.0	173.0	27.3	34.7	31.8	111.6	170.7	204.8
Proportional interest in net proved developed and undeveloped crude-oil reserves of Interprovincial Pipe Line Limited	—	—	3.0	—	—	—	—	—	3.0

Natural gas	1984	1985	1986
	billions of m ³		
Net proved developed and undeveloped			
Beginning of year	36.8	36.2	40.6
Revisions of previous estimates and improved recovery	0.9	4.4	0.8
Purchase (sale) of reserves in place	—	—	0.9
Discoveries and extensions	0.2	1.5	0.7
Production	(1.7)	(1.5)	(1.6)
End of year	36.2	40.6	41.4
Net proved developed			
Beginning of year	31.9	31.1	33.2
End of year	31.1	33.2	33.7
Proportional interest in net proved developed and undeveloped natural-gas reserves of Interprovincial Pipe Line Limited	—	—	4.8

All reported reserves of crude oil and natural gas are located in Canada. Reserves of crude oil include condensate and natural-gas liquids. Conventional crude-oil and natural-gas reserve estimates are determined through analysis of geological and engineering data, which have demonstrated with reasonable certainty that these reserves are recoverable from known oil and gas fields under economic and operating conditions at December 31 of each year. The calculation of reserves of crude oil at Syncrude is based on the company's participating interest in the production permit granted in October 1979 and amended in January 1985 by the province of Alberta. Reserves of crude oil at Cold Lake are those reserves estimated to be recoverable from the existing experimental pilot plants and stages one to six of the Cold Lake production project.

The net proved reserves of conventional crude oil (excluding enhanced oil recovery projects in Alberta), oil from the Cold Lake pilots and natural gas are determined by deducting the mineral owners' or governments' share or both and are based on an estimate of the average royalty rate over the remaining production life. These royalty rates may vary with production and price.

Net reserves of Syncrude, stages one to six of the Cold Lake production project and enhanced oil recovery projects in Alberta are based on an estimate of the average royalty rate over the project's life. These royalty rates may vary with production, prices and costs.

Reserves related to stages one to six of the Cold Lake production project have been recognized as proved developed. Geological and engineering studies based on data gathered from about 1200 wells drilled for the six completed stages of the Cold Lake production project plus up to 12 years of pilot and production project operating performance resulted in an upward revision of 11.8 million cubic metres to Cold Lake proved reserves in 1986. At the end of 1986,

all reserves for Cold Lake operations were proved developed and amounted to 97.9 million cubic metres. Cold Lake reserves at the end of 1985 and 1984 were proved developed and undeveloped (1985–89.7 million cubic metres; 1984–62.7 million cubic metres).

Reserves data do not include crude oil and natural gas discovered in the Beaufort Sea/Mackenzie Delta and the Arctic islands or the reserves contained in the oil sands other than those attributable to Syncrude, the Cold Lake pilot area and stages one to six of the Cold Lake production project.

Natural-gas reserves are calculated at a pressure of 101.325 kilopascals at 15 degrees Celsius.

Oil and gas producing activities

	1984	1985	1986
Present value of estimated future net cash flows discounted at 10 percent			
	millions of dollars		
Future cash flows (a)	31848	31862	18301
Future production and development costs	(10859)	(11109)	(10690)
Future Petroleum and Gas Revenue Tax (b)	(3605)	(389)	–
Future income taxes (c)	(9851)	(9532)	(3650)
Future net cash flows	7533	10832	3961
Discount of 10 percent for estimated timing of cash flows	(4285)	(5810)	(1933)
Discounted future net cash flows	3248	5022	2028
Proportional interest in discounted future net cash flows of Interprovincial Pipe Line Limited	–	–	182

The company does not agree that the calculation of the present value of future net cash flows from estimated production of proved reserves necessarily represents future cash flows or the fair market value of conventional oil and gas properties. The valuation does not include the value of exploratory properties and probable reserves and does not provide for the deduction of exploration expenses, amortization of land acquisition costs and depreciation of capitalized producing assets. It also does not include any potential changes in future prices for oil and gas and any potential changes in the cost of development and production. The valuation excludes the company's activities related to extraction and upgrading of crude oil from Syncrude. In the company's opinion, the method of calculating the data is not reliable and the values may not provide a basis for meaningful analysis. Imperial cautions readers about its use.

(a) Estimated future net cash flows are computed by applying the prices on December 31 of crude oil, including condensate and natural-gas liquids and natural gas to the estimated future production of proved oil and natural gas reserves.

(b) The Petroleum and Gas Revenue Tax was eliminated in 1986.

(c) Estimated future income taxes are computed by applying the current statutory income-tax rates to the estimated taxable income for each year. Taxable income is based on estimated future net revenues adjusted to take into account differences from standard accounting practices permitted under income-tax regulations in effect at the end of the year.

Summary of changes in present value of estimated future net cash flows	1984	1985	1986
	millions of dollars		
Balance at beginning of year	2312	3248	5022
Changes resulting from:			
Sales and transfers of oil and gas produced, net of production costs	(914)	(1163)	(687)
Net changes in prices, development costs and production costs (1)	258	(2351)	(6650)
Extensions, discoveries, additions and improved recovery, less related costs (2)	659	1815	98
Development costs incurred during the period	479	688	206
Revisions of previous quantity estimates (3)	266	1	351
Accretion of discount (4)	631	377	482
Net change in Petroleum and Gas Revenue Tax (5)	(248)	1149	342
Net change in income taxes (6)	(858)	(414)	2593
Change in production pattern (7)	663	1672	271
Net change	936	1774	(2994)
Balance at end of year	3248	5022	2028

(1) Net changes in prices and costs reflect the changes in prices for crude oil, natural gas and natural-gas liquids during each year and related increases in development and production costs.

(2) Increases in proved reserves resulting from extensions, discoveries, additions and improved recovery represent the present value of estimated future net revenues, less estimated future development and production costs.

(3) The 1986 increase was primarily due to an upward revision to Cold Lake and Redwater and from royalty-rate reductions partially offset by a downward revision to Judy Creek "B" Pool.

(4) Accretion of discount is due to an increase in the estimated present value because realization of future net cash flows occurs one year sooner.

(5) The net change in the Petroleum and Gas Revenue Tax is calculated by applying the tax rate to the estimated present value of future income from net operating revenue at the end of the year and deducting the amount similarly computed at the beginning of the year. This charge is considered a production tax and is shown as a reduction of net revenues. This tax was eliminated in 1986.

(6) The net change in income taxes is computed by applying current statutory tax rates to the estimated present value of future taxable income to be generated from proved reserves in production at the end of the year and deducting the amount similarly computed as of the beginning of the year.

(7) Changes in production patterns result primarily from revisions to the timing of future production.

Management discussion and analysis

Overview

Imperial's consolidated statements report the combined results of all the company's operations. The principal business segments are natural resources, petroleum products and chemicals. Each of those segments is managed by a president, who is responsible for the segment's operations and who reports to the company's chief executive officer through the executive vice-president and chief operating officer.

As discussed in note 1 to the audited financial statements, prior-period information has been restated to reflect a change in the method of inventory valuation. The financial highlights for 1986 as well as the two preceding years are as follows:

	1984	1985	1986
Earnings from operations (millions of dollars)	520	694	440
Earnings after unusual items (millions of dollars)	520	644	285
Capital and exploration expenditures (millions of dollars)	679	1158	648
Earnings per share (after unusual items) (dollars)	3.24	3.97	1.74
Dividends per share (dollars)	1.45	1.65	1.60

The unusual items are described in note 10 to the audited financial statements.

Segment Information

Natural resources

Earnings from natural resource operations in 1986 were \$196 million, a decrease of \$346 million from 1985 and \$128 million from 1984. Return on average capital employed was 5.9 percent, down from 19.6 percent in 1985 and 14.3 percent in 1984.

The decline in earnings from 1985 was caused mainly by the nearly 50-percent drop in Canadian crude-oil prices that occurred during 1986. As well, lower capital-expenditure-related income-tax and royalty credits, resulting from reduced capital expenditures in 1986 and the sale in 1985 of interests in certain crude-oil and natural-gas-producing properties (the company held the right to reacquire them, which it did in 1986), contributed to the reduction in 1986

earnings. These factors were partially offset by a 36-percent increase in the company's net production of crude oil and natural gas liquids, resulting primarily from increased production at the Cold Lake project and a full year of production at the Norman Wells oil-field expansion project. Other favorable factors were a reduction in royalties and the reduction and subsequent elimination of the Petroleum and Gas Revenue Tax.

Capital and exploration expenditures of \$457 million were 48 percent lower than the record expenditures of \$885 million in 1985 (1984—\$511 million). Expenditures to increase or maintain production at Cold Lake and Syn-crude were \$133 million (down \$246 million from 1985), which primarily reflects the completion of the first six stages of the Cold Lake production project (1984—\$231 million). Expenditures to increase or maintain conventional crude-oil production were \$187 million in 1986, down \$128 million from 1985 (1984—\$209 million)—the reduction was largely a response to the major decline in the prices of crude oil that occurred in 1986. Expenditures related to exploring for conventional oil and gas were \$81 million, \$16 million lower than 1985 (1984—\$48 million).

Petroleum products

The petroleum product operations earned \$174 million in 1986, an increase of \$72 million from 1985 and \$41 million from 1984. Return on average capital employed increased to 7.6 percent in 1986 (1985 — 4.1 percent; 1984—5.3 percent). The earnings increase in 1986 resulted primarily from improvements in the margins on petroleum product sales. As well, expenses were lower, mainly as a result of actions taken in the early part of 1986, including a staff reduction of about 17 percent to restructure and improve the efficiency of operations. Partially offsetting the increase in earnings was the elimination of the inventory allowance tax deduction and a three-percent reduction in product sales.

The decrease in product sales resulted from aggressive price competition, which prompted the company to withdraw selectively from business that became unprofitable.

Capital expenditures for marketing were \$75 million, a decrease of \$31 million from 1985, primarily due to a reduction in spending on the maintenance of existing facilities. As well, in 1986 a greater proportion of the service-station expenditures was spent on providing more customer services, such as car washes and convenience stores, in an effort to increase sales volumes (1984—\$83 million). Refining and pipeline capital expenditures were \$68 million in 1986, down from \$112 million in 1985, mainly as a result of the completion of a 1985 pipeline construction project (1984—\$46 million).

Chemicals

Earnings from chemical operations increased \$14 million to \$17 million in 1986, and were down from \$22 million in 1984. Return on average capital employed was 1.8 percent, up from 0.3 percent in 1985, and down from the 1984 return of 2.1 percent.

Petrochemicals achieved an earnings turnaround during 1986. Margins increased as a result of lower feedstock costs, cost reduction programs and improved plant performance. Sales volumes remained relatively constant over 1985 as declines in some businesses were offset by gains in polymers.

In agricultural chemicals, earnings decreased from 1985. Falling grain prices, driven by oversupply, have had a severe impact on international fertilizer prices and on the demand for fertilizer in Western Canada. Even though raw material and operating costs were lower and export sales volumes increased, this was not sufficient to offset the lower profit margins in both domestic and export markets.

Total capital expenditures were \$29 million in 1986, up \$5 million from 1985 (1984—\$23 million). The majority of the expenditures in 1986 were for the maintenance of existing facilities.

Liquidity and capital resources

Total funds provided from operating activities (after changes in operating working capital and payment of dividends by the company) were \$1.1 billion, an increase of \$63 million from 1985 (1984—\$708 million). This increase occurred in spite of a 37-percent decrease in earnings from operations. A significant decrease in operating working capital (mainly in accounts receivable and inventories), as a result of the almost 50-percent decrease in the prices of Canadian crude oil, more than offset the decrease in earnings from operations.

Capital and exploration expenditures were \$648 million in 1986, down from the record level of \$1.2 billion in 1985 (1984—\$679 million). The reduction occurred mainly in natural resource operations as a result of the sharp decline in Canadian crude-oil prices in 1986, which limited the company's investment opportunities.

During the second quarter of 1986, the company took steps to retire its (U.S.) \$200 million issue of 15½ percent sinking fund debentures due December 1, 2011. The total cost of retiring the debt was (Canadian) \$315 million, which came from existing cash reserves. The premium paid for the retirement of the debentures, as well as a foreign-exchange loss arising from the transactions, resulted in a loss of

\$65 million, or 40 cents a share (see note 10 to the audited financial statements on page 37). Debt compared to debt plus equity was 16.9 percent at December 31, 1986, down from 19.5 percent in 1985 and 20.5 percent in 1984.

In 1986, the company revised its dividend reinvestment and share purchase plan so that funds directed to the plan would be used to buy existing shares on a stock exchange rather than new shares from the company. In 1984 and 1985, \$67 million and \$73 million respectively had been raised through this plan (1986—\$20 million).

Funds available at the end of the year were \$656 million, compared with \$452 million in 1985 and \$510 million in 1984. In addition to these funds, the company's unused lines of credit with five Canadian banks amounted to \$596 million at December 31, 1986.

Outlook for 1987

In 1986 there was a precipitous drop in Canadian crude-oil prices. The company believes that it is prudent to manage its business on the assumption that low or volatile crude-oil prices could continue during the next several years. As well, the company wants to have the flexibility to pursue longer term growth opportunities should the investment climate improve. As a result, the company's current strategies will focus on maintaining its financial strength and improving near-term earnings performance through managed reductions in operating expenses and selective capital spending. The actions initiated by the company in 1986 to restructure and improve the efficiency of its operations are expected to continue to show benefits in 1987. The company expects to spend about \$750 million on capital and exploration expenditures in 1987.

Entering 1987, the company's financial position is strong. The company has large cash reserves, its debt to debt-plus-equity ratio is 16.9 percent (down from 19.5 percent in 1985), its interest-coverage ratio is healthy by every commonly accepted standard and its credit rating is strong.

Reported earnings are not adjusted for inflation and changes in prices. A report on the effects of inflation and changing prices appears on page 55.

Supplemental information

Presentation of financial statements

The financial statements of the company have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada. These principles conform in all material respects to those in the United States except for the following:

	1982	1983	1984	1985	1986
	millions of dollars				
Earnings as shown in financial statements	276	294	520	644	285
Increase (decrease) in net earnings due to:					
Capitalized interest (1)	21	21	24	10	(4)
Foreign exchange (2)	(10)	(4)	(19)	(15)	33
Subtotal (4)	287	311	525	639	314
Adjustment for amounts restated under Canadian GAAP	(9)	(4)	13	(10)	—
Earnings according to GAAP in the United States, before the cumulative effect of a change in accounting principles with regard to inventory valuation	278	307	538	629	314
Cumulative effect (3)	—	—	—	—	(3)
Net earnings according to GAAP in the United States	278	307	538	629	311
Earnings per share	(dollars)				
Under accounting principles of					
Canada	1.75	1.86	3.24	3.97	1.74
United States—before accounting principle change	1.77	1.94	3.35	3.88	1.92
United States—after accounting principle change	1.77	1.94	3.35	3.88	1.90
United States—after retroactive application (4)	1.82	1.96	3.27	3.94	1.92

(1) Interest expense related to major construction projects is not required to be capitalized in Canada, as it is in the United States.

(2) Long-term liabilities in foreign currencies have been translated at the rates of exchange prevailing on December 31. Exchange gains and losses arising on translation of long-term debt are amortized over the remaining term of the debt. In the United States the practice is to include the gains and losses arising from this translation in the earnings for the period in which they arise. In 1986, the retirement of a debt issue denominated in U.S. dollars resulted in a foreign-exchange loss under Canadian GAAP, but under the accounting practices of the United States this loss would have been recognized in prior years.

(3) A change in an accounting principle in Canada is to be applied retroactively and data of prior years are to be restated. In the United States, the cumulative effect of the accounting principle change on the amount of retained earnings at the beginning of the year in which the change is made is to be included in net income of that year. See note 1 in the notes to the audited financial statements for a description of the change.

(4) This is the pro forma effect of a change in accounting principle as if that change has been applied retroactively.

The Statement of Financial Standards No. 87, Employer's Accounting for Pensions, requires the recording of a liability and an offsetting intangible asset if the benefit obligation, excluding future service and compensation increases, exceeds the fair market value of the plan assets. The company's surviving spouse benefit plan is an unfunded plan. Accordingly, under United States GAAP, an amount of approximately \$90 million would be added to assets and liabilities in the consolidated statement of financial position. Although the following methods of disclosure in the financial statements differ between Canada and the United States, they do not affect the amounts shown as net earnings.

(a) Under U.S. GAAP the unusual items described in note 10 to the financial statements other than the retirement of debentures, would be reported in the consolidated statement of earnings before "earnings before taxes and levies" and would not be shown net of the applicable income taxes.

(b) Because of the tax structure for the Canadian oil and gas industry, the company reports all taxes and levies shown in note 5 as a separate item in the consolidated statement of earnings. The general practice in the United States is to disclose earnings before income taxes and to report income taxes as a separate item.

International Accounting Standards

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in Canada and conform in all material respects with International Accounting Standards.

Accounting for the effects of inflation and changing prices

Conventional accounting practices and published reports reflect financial results from prices and costs in effect at the time the transactions occurred.

Inflation-adjusted earnings provide insight into the performance of the company after stripping away the uncontrollable factors of inflation and changing prices, leaving earnings that are available to shareholders after providing for the preservation of the company's financial capital.

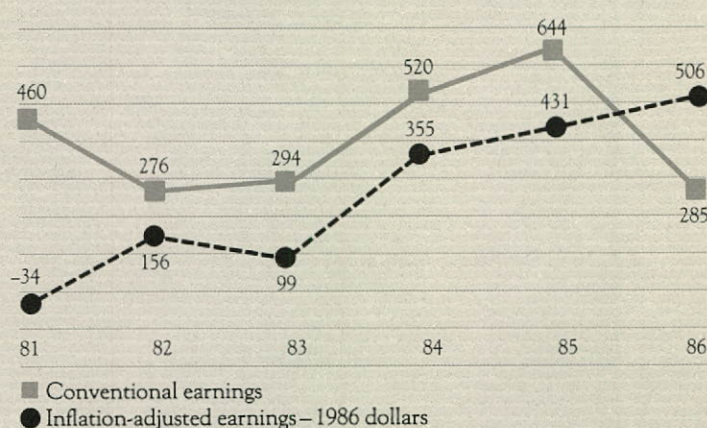
Comparative results for 1986

	Inflation-adjusted	
	Conventional	Imperial method (1)
	millions of dollars	
Revenues less expenses	1779	1779
Adjustment for cost of sales	—	540
Depreciation and amortization	(343)	(680)
Earnings before taxes and levies	1436	1639
Current taxes and levies	(928)	(928)
Deferred income taxes	(68)	(50)
Earnings from operations	440	661
Unusual items	(155)	(155)
Earnings after unusual items	285	506

(1) Adjustments have been rounded to the nearest \$10 million.

Inflation-adjusted earnings for 1986 are higher than reported by conventional accounting methods. The difference is due to three recurring items: cost of sales, depreciation and amortization, and deferred income taxes.

The cost of sales in 1986 is lower under inflation accounting because the fall in crude prices caused the current replacement cost of product sold to be less than the historical cost used in conventional accounting. Depreciation and amortization are higher under inflation accounting because they are based on the cost of the company's physical assets in current (inflated) dollars. Deferred taxes are lower under inflation accounting as the higher accounting depreciation results in a smaller difference from the tax depreciation.



Inflation-adjusted earnings were consistently lower from 1981 to 1985, revealing a different pattern from earnings reported under conventional accounting methods. In 1981, the impact of the economic recession and the National Energy Program was more severe than was apparent from conventional results. The 1982 adjusted results show that the company was recovering, which was not evident until later years under conventional accounting.

The substantial drop in oil prices in 1986 is reflected differently between conventional and inflation-adjusted results. Conventional earnings decreased from 1985 as sales revenues dropped more than the cost of sales, which was affected by approximately three months of inventories valued at historical cost. However, adjusted earnings increased as cost of sales included the one-time drop in current replacement costs, which was more than the drop in revenues.

The Canadian Institute of Chartered Accountants introduced recommendations for "reporting the effects of changing prices" in 1982. It is encouraging experimentation to arrive at the best method of reporting the impact of inflation. Imperial feels the CICA approach is unnecessarily complex and subjective and has chosen to account for the effects of inflation on a basis that is easier to interpret and communicate.

Imperial supports the reporting of inflation-adjusted financial results and believes it is important for the accounting model to evolve so that it communicates objective, understandable information to all users of financial statements.

Shareholder and investor information*

Share ownership, trading and performance					
	1982	1983	1984	1985	1986
Share ownership, Class A and B					
Average number outstanding, weighted monthly (thousands)	157 328	158 472	160 376	162 320	163 611
Number of shares outstanding at December 31 (thousands)	157 760	159 590	161 575	163 181	163 646
Shares held in Canada at December 31 (percent)	26.0	26.8	26.9	25.3	22.5
Number of shareholders at December 31 (1)					
Total shareholders	44 691	41 571	37 237	33 664	31 164
Registered in Canada	39 289	36 926	32 995	29 800	27 485
Shares traded, Class A (thousands)	21 187	19 516	23 604	24 905	38 899
Share prices, Class A					dollars
High	33 $\frac{1}{4}$	41 $\frac{1}{4}$	45 $\frac{1}{2}$	55	51 $\frac{7}{8}$
Low	19 $\frac{5}{8}$	26 $\frac{1}{2}$	33 $\frac{3}{8}$	39 $\frac{7}{8}$	34 $\frac{3}{4}$
Close at December 31	28 $\frac{3}{4}$	37 $\frac{1}{8}$	42 $\frac{3}{8}$	51	51 $\frac{1}{4}$
Earnings per share					
From operations	1.89	2.12	3.24	4.27	2.69
After unusual items	1.75	1.86	3.24	3.97	1.74
Return on average shareholders' equity (percent)	6.8	7.1	11.8	13.4	5.6
Price/earnings ratio, Class A at December 31	15.2	17.5	13.1	11.9	19.1
Dividends					
Total paid (millions of dollars) (2)	220	222	233	268	262
Per share (dollars) (2)					
Cash	1.40	1.40	1.45	1.65	1.60
Stock	1.40	1.40	1.45	1.65	1.60
As a percentage of earnings after unusual items	80	75	45	42	92

(1) Imperial is an affiliate of Exxon Corporation, which owns 69.6 percent of the company's shares.

*Data for the years 1982 to 1985 have been restated to reflect the change in the method of inventory valuation described in note 1 to the audited financial statements.

Shareholders	Shareholders			
	of record at	Registered (percent)		
	Dec. 31, 1986	Canada	Foreign	Total
Class A	30 597	88.3	11.7	100
Class B	721	79.5	20.5	100

The total number of shareholders does not equal the total number of shareholders of record, because some shareholders hold both Class A and Class B shares.

(2) The 1986 fourth-quarter dividend declared on November 17, 1986, was paid on January 1, 1987.

Imperial's shares are listed on the Montreal, Toronto and Vancouver stock exchanges and are admitted to unlisted trading on the American Stock Exchange. The high and low prices for Class A shares are based on trading on the Toronto Stock Exchange and the American Stock Exchange. The number of shares traded is based on transactions on all the above exchanges. Class B shares generally trade at the same price as Class A shares.

The average number of outstanding shares included in the calculation of earnings per share is weighted on a monthly basis. As a result, the sum of the quarterly earnings per share does not necessarily equal the yearly earnings per share.

Quarterly financial and stock-trading data	1985				1986			
	three months ended				three months ended			
	Mar. 31	June 30	Sept. 30	Dec. 31	Mar. 31	June 30	Sept. 30	Dec. 31
	millions of dollars							
Financial data								
Operating revenues	2089	2249	2107	2222	1869	1787	1666	1642
Investment and other income	38	34	30	35	26	27	22	25
Total revenues	2127	2283	2137	2257	1895	1814	1688	1667
Expenses, including taxes and levies (1)	1991	2124	1979	2016	1757	1716	1612	1539
Earnings from operations (2)	136	159	158	241	138	98	76	128
Unusual items	—	—	(45)	(5)	—	(155)	—	—
Earnings after unusual items (2)	136	159	113	236	138	(57)	76	128

(1) Previously reported expenses including taxes and levies have been adjusted as described in note 1 to the audited financial statements. These adjustments, included above, are as follows:

(6)	(7)	(6)	9	(42)	(5)	27	—
-----	-----	-----	---	------	-----	----	---

(2) Previously reported earnings from operations and earnings after unusual items have been adjusted as described in note 1 to the audited financial statements. These adjustments, included above, are as follows:

6	7	6	(9)	42	5	(27)	—
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Quarterly financial and stock-trading data	1985				1986			
	three months ended				three months ended			
	Mar. 31	June 30	Sept. 30	Dec. 31	Mar. 31	June 30	Sept. 30	Dec. 31
	dollars							
Per-share information								
Earnings from operations	0.85	0.98	0.96	1.48	0.84	0.60	0.46	0.78
Earnings after unusual items	0.85	0.98	0.69	1.45	0.84	(0.34)	0.46	0.78
Dividends (declared quarterly)	0.40	0.40	0.40	0.45	0.40	0.40	0.40	0.40
Share prices (3)								
Toronto Stock Exchange								
High	52 ⁵ / ₈	55	53 ⁷ / ₈	55	51 ⁷ / ₈	46 ³ / ₄	47 ³ / ₈	51 ³ / ₄
Low	39 ⁷ / ₈	47 ³ / ₈	48	49 ⁵ / ₈	42 ¹ / ₄	37 ⁷ / ₈	34 ³ / ₄	44 ¹ / ₂
Close	52	48 ¹ / ₄	50 ⁵ / ₈	51	46 ⁷ / ₈	38	45 ⁷ / ₈	51 ¹ / ₄
American Stock Exchange (\$U.S.)								
High	38 ¹ / ₂	40 ¹ / ₄	39 ¹ / ₂	39 ³ / ₄	37	33 ⁷ / ₈	34 ¹ / ₄	37 ³ / ₈
Low	30 ¹ / ₄	34 ⁵ / ₈	35 ¹ / ₈	36	29 ¹ / ₄	27	25 ¹ / ₈	32
Close	38 ¹ / ₈	35 ³ / ₈	36 ⁷ / ₈	36 ¹ / ₂	33 ⁵ / ₈	27 ¹ / ₂	33 ¹ / ₄	37 ¹ / ₈
Shares traded (thousands)	7886	5909	4694	6416	8534	8363	12 584	9418

(3) Share prices were obtained from stock exchange records.

Shareholder and investor information

The company's head office mailing address is:

Imperial Oil Limited
111 St. Clair Avenue West
Toronto, Canada M5W 1K3

If you wish to transfer your Imperial Oil shares

you may contact the head office of Imperial Oil or the principal offices of our cotransfer agent, Montreal Trust Company, in St. John's, Charlottetown, Halifax, Saint John, Montreal, Toronto, Winnipeg, Regina, Calgary and Vancouver; or the Bank of New York, New York.

If you changed your address

please notify the company in writing and mail the notification to the investor relations division at the above address.

Shareholder and investor inquiries

Additional information about the company can be obtained by contacting the investor relations division.

For information about shares and dividends, please phone (416) 968-5076.

To obtain additional information on the company's operating performance and projects, including Form 10-K filed with the United States Securities and Exchange Commission, write to the investor relations manager at the above address or phone (416) 968-8145.

Where Imperial's shares trade

Imperial's shares trade on the Toronto, Montreal and Vancouver stock exchanges as well as on the American Stock Exchange in New York. The symbol on these exchanges for Imperial's Class A shares is "IMO A" and for its Class B shares, "IMO B."

Dividend reinvestment and share purchase plan

In October 1982 the company introduced its dividend reinvestment and share purchase plan. The plan enabled shareholders to reinvest their cash dividends in additional Class A shares at five percent less than the average market price. Shareholders could also invest between \$50 and \$5000 per calendar quarter in additional Class A or Class B shares at the average market price, without paying brokerage or other fees.

Imperial revised its dividend reinvestment and share purchase plan on January 23, 1986. The dividend reinvestment plan was changed to eliminate the five-percent discount on shares purchased with cash dividends. As well, funds directed to the dividend reinvestment and share purchase plan are used to buy existing shares on a stock exchange, rather than new shares from the company.

General summary of tax consequences affecting foreign security holders

Cash dividends paid to shareholders resident outside Canada—in the United States, the United Kingdom, France, Switzerland and most countries with which Canada has an income-tax convention—are usually subject to Canadian nonresident withholding tax of 15 percent. Class B stock dividends paid to nonresident holders of Class B shares are subject to the same Canadian nonresident withholding tax as cash dividends.

There is no Canadian tax on gains from selling shares or debt instruments owned by nonresidents not carrying on business in Canada.

Interest paid to nonresidents with whom the company deals at arm's length on the company's outstanding debentures issued before June 24, 1975, is subject to withholding tax. Interest paid on debentures issued subsequent to that date is not subject to withholding tax.

No estate taxes or succession duties are imposed by the government of Canada or provincial governments.

Version française des rapports

Pour obtenir en français les rapports de la Compagnie Pétrolière Impériale Ltée aux actionnaires, veuillez écrire à la division des Relations avec les investisseurs, Compagnie Pétrolière Impériale Ltée, 111 St. Clair Avenue West, Toronto, Canada M5W 1K3.

Senior management

Officers and vice-presidents of Imperial Oil

A. R. Haynes

Chairman of the board, president and chief executive officer

R. B. Peterson

Executive vice-president and chief operating officer

W. J. Young

Executive vice-president and chief financial officer

W. E. Beacom

Vice-president and comptroller

A. F. Gomm

Vice-president, operations planning and coordination

W. R. K. Innes

Vice-president, and president, Esso Chemical Canada

H. G. Jarvis

Vice-president and treasurer

R. E. Landry

Vice-president

R. J. Michaelides

Vice-president, public affairs, and general secretary

W. P. Moher

Vice-president, human resources and management development

G. L. Munro

Vice-president, information systems and technology

A. L. Peterson

Vice-president, general services

G. H. Thomson

Vice-president, and president, Esso Petroleum Canada

R. C. Walker

Vice-president and general counsel

W. D. West

Vice-president, tax

Principal operating management

Esso Resources Canada Limited

K. T. Koonce

President and chief executive officer

Esso Petroleum Canada

G. H. Thomson

President

Esso Chemical Canada

W. R. K. Innes

President

Board of directors

The directors schedule monthly meetings to consider and act on matters of significance to the corporation. These include financial and social performance, investment decisions, strategic plans, corporate policies and other matters on which the directors are legally required to act. There are 10 directors, and in 1986 their attendance at meetings of directors averaged 94 percent.

J. B. Buchanan is vice-chairman of British Columbia Packers Limited, a fishing and food-processing company. He is past chairman of the Fisheries Council of Canada, chairman of the Fisheries Council of British Columbia and is associated with a number of other business, community and health related organizations.

J. V. R. Cyr is president of Bell Canada Enterprises, Inc. and chairman of Bell Canada. He also holds a number of other directorships, is a member of the Canada/U.S. section of the Canadian Chamber of Commerce and is chairman of the Museum of Contemporary Art of Montreal. Mr. Cyr is also associated with several business, education, culture and health related organizations.

P. Des Marais II is chairman, president and chief executive officer of Carling O'Keefe Limited and president of Pierre Des Marais Inc., a large printing and lithography firm. Prior to his appointment at Carling O'Keefe Limited, he was chairman, president and chief executive officer of Canadair Limited. Mr. Des Marais was chairman of the executive committee of the Montreal Urban Community and has held senior positions with various business, community and educational organizations. He also holds a number of other corporate directorships and is a former mayor of the City of Outremont.

A. R. Haynes is chairman, president and chief executive officer of Imperial Oil Limited and is a director of The Royal Bank of Canada, the Power Corporation of Canada and the Moore Corporation Limited. He is cochairman of the University of Manitoba's development fund and chairman of the Diabetes Canada fundraising campaign. Mr. Haynes is a director of a number of cultural, educational and health related organizations and is chairman of the National Advisory Council for the World Energy Congress, to be held in Montreal in 1989.

K. T. Koonce is president and chief executive officer of Esso Resources Canada Limited, a wholly owned subsidiary of Imperial. He is a director of Exxon Production Research Company, a member of the board of governors and executive committee of the Canadian Petroleum Association, a member and former director of the Society of Petroleum Engineers and a member of the advisory council of the George R. Brown School of Engineering at Rice University in Houston, Texas. In 1987 Mr. Koonce will be general chairman of the Calgary United Way campaign.



M. Kovitz is president of Murko Investments Ltd., a private company. She is a member of the Order of Canada and chancellor emeritus of the University of Calgary and holds other directorships. Mrs. Kovitz has been actively associated with numerous community, health and educational organizations and is a member of the executive of the board of directors, Canadian Council of Christians and Jews, Western Region.

W. A. Macdonald is a partner with the firm of McMillan, Binch, barristers and solicitors. He is a recognized authority in the fields of taxation, government-business relations and other public policy and serves on the Ontario government sponsored Labor Management Study Group and on the C. D. Howe Institute Policy Analysis Committee. Mr. Macdonald is also a director of other corporations as well as a number of organizations concerned with health, culture and the arts.

R. B. Peterson is executive vice-president and chief operating officer of Imperial, chairman of Esso Resources and a director of Interprovincial Pipe Line Limited. Mr. Peterson is a member of the advisory council, school of business, Queen's University as well as a member of a number of professional associations.

G. H. Thomson is vice-president of Imperial and president of Esso Petroleum Canada. He is a director of Interprovincial Pipe Line Limited, past president of the Canadian Society for Chemical Engineering, a fellow of the Chemical Institute of Canada and a member of a number of other professional associations. Mr. Thomson is a director of Famous People Players, the Toronto-based theatre group for the mentally handicapped.

W. J. Young is executive vice-president and chief financial officer of Imperial. He is a director of Interprovincial Pipe Line Limited and Building Products of Canada Limited.



Board committees

Meetings of committees are usually scheduled on the same day as meetings of directors. Attendance at all committee meetings in 1986 averaged 91.5 percent.

Audit committee

W. A. Macdonald, *chairman*

The committee, composed of the five nonemployee directors and Mr. Peterson, reviews the company's financial statements, accounting practices and business and financial controls. It also recommends the appointment of auditors and reviews their fees. The shareholders' auditors, Price Waterhouse, attend and participate in all meetings. The committee met seven times in 1986.

Board compensation committee

P. Des Marais II, *chairman*

The committee, composed of the five nonemployee directors and Mr. Haynes, is responsible for decisions on the compensation of senior management above the level of vice-president. It also reviews policy on corporate compensation and the process by which future managers of the company are identified and selected. The committee met once in 1986.

Contributions committee

M. Kovitz, *chairman*

The committee, composed of the five nonemployee directors and Mr. Young, examines policies and programs related to the contribution program and recommends an annual budget for adoption by the board of directors. The company's contribution program is aimed at enhancing the quality of Canadian life through support for education, health, welfare, community services, sports and culture. The committee met four times in 1986.

Nominations committee

A. R. Haynes, *chairman*

The committee, composed of the five nonemployee directors and Mr. Haynes, recommends to the board of directors the slate of director candidates to be proposed for election by the shareholders at the annual meeting. It also recommends criteria for the selection and tenure of directors, specific director candidates and the successor to the chief executive officer when vacancies are expected. The committee met once in 1986.



Imperial Oil strives for excellence in all its activities. By competing aggressively, seeking new opportunities, providing quality and value in its products and services, maintaining a challenging and rewarding work environment and responding to community needs, the company serves its customers, shareholders and employees and contributes to Canada's economic growth.

Imperial markets a wide range of quality products, primarily under the Esso brand name, and pursues product innovation and processing advances through one of the country's largest research programs, which in 1986 committed \$68 million to research and development in Canada. The company has an active and long-standing program to identify and support Canadian suppliers and during 1986 purchased more than 80 percent of the goods and services it required from Canadian sources.

Imperial is the largest corporate contributor in Canada; in 1986 it donated more than \$6 million to Canadian education, health care, culture and sports.

NEW!

The No Trouble Gasoline

Cleans fouled fuel injectors
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Regular Leaded

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