Treasury Key Issues Report
1Q 2014

Financial Markets

Global Markets

KEY MARKET INDICATORS

		Prev Qtr 31/12/2013	End of Q1 31/03/2014	Change on Qtr
Equities	S&P 500	1848.4	1872.3	1.3 %
	FTSE 100	6749.1	6598.4	-2.2 %
	BP London	488.1	480.0	-1.6 %
	BP US	48.6	48.1	-1.0 %
Govt Bond Yields	US Treasury 10Y	3.03	2.72	-31 bp
	US 3mth Libor (L)	0.25	0.23	-2 bp
	Germany Bund 10Y	1.93	1.57	-36 bp
	Japan 10Y	0.74	0.64	-10 bp
Credit Profile	S&P	A	A	Nil
	Moodys	A2	A2	Nil
	BP 10Y bond spread	L+83	L+79	-4 bp
Currencies	EUR/USD	1.3743	1.3769	0.2 %
	GBP/USD	1.6557	1.6662	0.6 %
	USD/EGP	6.9475	6.9701	0.3 %
	USD/RUB	32.870	35.173	7.0 %
Commodities	Brent Crude Oil Future (ICE)	109.9	107.8	-2.0 %
	WTI Crude Oil Future (NYMEX)	98.0	101.6	3.7 %
	Nat Gas Future (NYMEX)	4.10	4.37	6.7 %

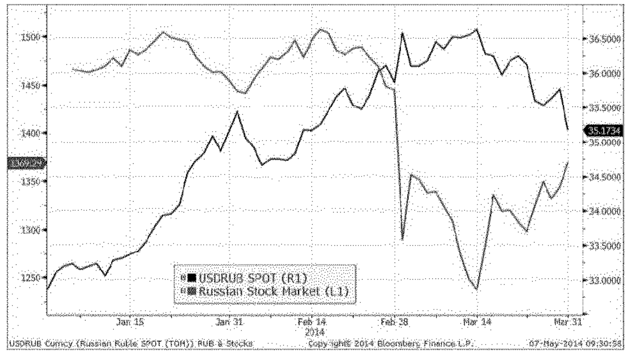
The financial markets have been very volatile in Q1 with tail risks in the EM "fragile five", the Crimea crisis, fears of a Chinese hard landing and severe winter storms affecting economic activity in the US. Global growth in Q1 has been soft mainly driven by weak growth in US and China. However the bright spots in Q1 were strong growth in the UK and reasonable growth in Europe with peripherals showing signs of recovery. Inflation globally is edging lower and with the absence of strong growth there is increasing risk that inflation will remain soft for a considerable period of time.

The US Federal Reserve continued to taper its asset purchases now running at $55bn per month and is expected to finish their asset purchase programme in the autumn. The Fed and the BoE shifted from a quantitative to qualitative forward guidance with the unemployment rate moving closer to their threshold for triggering rate hikes.

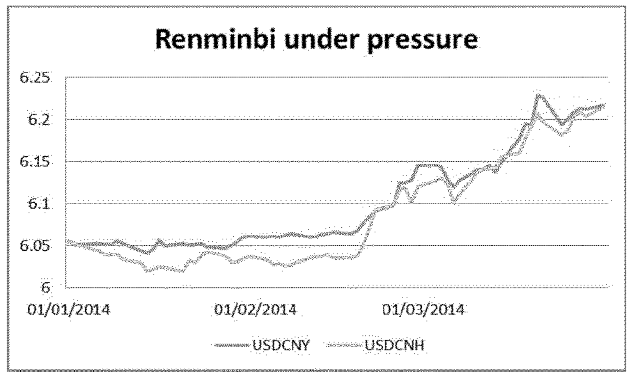
In the Euro area the ECB once again ignored the weak inflation by keeping monetary policy unchanged. The ECB still believes that the medium term inflation expectations are firmly anchored and there is no threat of deflation.

The "fragile five" currencies initially weekend at the start of year as the markets were concerned about money leaving EM and moving into DM on the back of rising rates in DM. However, we have seen a reversal of the initial sell off with EM currencies strengthening in March as investors were less worried about a US rates tightening cycle and were happy to be long "carry" as growth still remains soft in DM.

Russian currency and assets have been under pressure after Russia's President Vladimir Putin was granted permission by the Federation Council to send troops to Crimea, and Crimea held a referendum which resulted in 96% voting in favour of joining Russia. The Russian central bank surprised that market by raising rates by 150bps in an unscheduled meeting to curb currency weakness. Russia has avoided direct economic sanctions from the West following its ratification of the results of the Crimea referendum.



Concerns of a hard landing in China increased after one of the wealth management products (WMP) defaulted on a bond coupon payment and the market started to fear that the credit markets would seize up, as further defaults were expected. Meanwhile both the onshore and offshore currency has been under pressure as the PBoC let the currency depreciate as part of their easing policy to boost growth and clear out speculative positions. The weakening of the Renminbi led to a speculator squaring up copper positions (used as carry trade by onshore speculators) which fell more than 13% in February. The PBoC also widened the USD-CNY daily trading band to +/- 2% from +/-1%.



US

Real GDP growth for Q4 was weaker than Q3 at 2.6% annualized, as much of Q3 gains were to due inventory build-up. Q1 GDP is expected to much lower, as the economic data in the US has been severely affected by the extreme winter weather. However, we have seen some improvement in the data in March and the market expects Q2 growth to be strong. The unemployment rate fell to 6.7% in Q1, now close to the Fed's threshold of 6.5%. Meanwhile, Inflation continues to be well below that Fed's target, but the market expects inflation to pick up in the 2H of this year as wages pick up.

Europe

The Euro-area posted another positive GDP print in Q4 at 0.3% QoQ and the market expects this positive growth trend to continue in 2014. However inflation fell sharply in Q1 to 0.5% YoY and many of the peripheral countries are already in deflation. Unemployment in the Euro area still remains high at 11.9% but we are seeing signs that the labour market is improving but this will be a slow and long process.

UK

The UK economy continued its strong recovery this year with 4Q GDP at 0.7% QoQ and 1Q GDP expected to be stronger. The survey data has softened a bit in Q1 but still remains high compared to the historical average. The unemployment rate continues to fall, currently at 7.2% and is expected to fall below 7.0% in the coming months. Meanwhile inflation has fallen sharply to 1.7% in Q1 and now is well below the BoE target of 2% and the expectations are that inflation will fall further in the coming months.

Egypt

GDP is expected to be 2.6% YoY in 2014 compared to 2.1% YoY in 2013, however inflation is expected to increase sharply to 10% and unemployment to remaining high at 14%.
The focus has turned to presidential elections that are scheduled to be held before the end of April, while parliamentary elections will be held in early summer. The Muslim Brotherhood is likely to boycott the political transition whilst the head of the Strong Egypt Party, Aboul Fotouh, will not run for election. The likelihood of Field Marshal al-Sisi running for presidential election and wining the vote is high.

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Group Activities

$m	1Q14	4Q13	3Q13	2Q13	1Q13
Gross Debt	53,249	48,192	50,284	46,990	46,425
Less FV of debt hedges	(633)	(477)	(734)	(460)	(1,083)
Cash	(27,358)	(22,520)	(29,499)	(28,313)	(27,679)
Net Debt	25,258	25,195	20,051	18,217	17,663
Net Debt Ratio	16.2%	16.2%	13.3%	12.3%	11.9%
Income Statement	**1Q14**	**4Q13**	**3Q13**	**2Q13**	**1Q13**
Interest Payable	250	261	279	258	278
Finance Costs	287	255	279	259	271
Qtr End Exchange Rates	**1Q14**	**4Q13**	**3Q13**	**2Q13**	**1Q13**
USD/GBP	1.66	1.65	1.61	1.52	1.51
USD/EUR	1.38	1.38	1.35	1.30	1.28

Financial Commentary

Reported net increased slightly to E4Q position at $25.3b (from $25.2b) with gearing remaining constant at 16.2%.

Note: Prior quarter comparatives have been updated from the original SEA published numbers to reflect the impacts of IFRS11 and IAS19 on 2013 reporting and the re-stated comparative numbers.

Treasury Credit Risk

Treasury's end 1Q14 credit risk exposures totalled $30.6bn, a $4.4bn increase from 4Q13 levels, primarily reflecting a $4.6bn increase in Treasury Cash to $23.4bn. Cash remains the largest component of Treasury's credit risk. Treasury's other credit exposures comprise foreign exchange and interest rate derivatives ($1.1bn MTM / $6.6bn PFE) and Treasury Working Capital ($0.6bn).

We continue to dynamically manage the Group's cash to bank credit events and Group liquidity requirements. Treasury Cash is invested in collateralised and uncollateralised bank deposits with highly rated banks, money market funds and diversified government and supranational cash investment securities. Across 1Q Treasury cash balances ranged from $15.8bn to $24.3bn.

There were two notable credit risk issues in the first quarter of 2014. Firstly the Russia Ukraine situation prompted a review of bank exposures in the region. The Group has limited direct exposure: $26m to Citibank in Russia (of which $2m equivalent is denominated in RUB) and $4m to VTB. Treasury is also monitoring for warning signals from international banks that are exposed to the region in case of an indirect exposure to Russia. Secondly Treasury is working with local cash managers to reduce the credit risk associated with approximately $120m decentralised cash held in Angola banks to fund capital investments.

Banks continue to report a challenging operating and regulatory environment, with profits mostly originating from cost control and credit improvements. Eurozone banking union, tapering and enhancing bank fundamentals are continuing themes for the first quarter.

Funding and Equity activities

Debt capital markets remained heavily bid in 1Q. The quarter represented the second and third largest ever quarterly issuance of investment grade corporate bonds in the US and Euro markets respectively. We took advantage of these positive market conditions to pre-fund, issuing a total of $6bn, made up of $2.5bn issued in the US markets, $2.7bn issued in euros, $0.6bn issued in CHF and a small offshore RMB bond specifically to finance the BP Zhuhai expansion. Pricing was at attractive levels. The issuance has helped bolster our strong liquidity position. At end 1Q 2014 net debt and the Group's cash balance were $25.3bn and $27.4bn respectively. We continued to repurchase stock during the quarter as part of the previously announced $8bn share buyback programme. By the end of the quarter $7.5bn worth of stock has been repurchased cumulatively ($2bn in 1Q 2014).

Pensions Funding

Both the UK and US pension funds remained around fully funded at the end of 1Q (102% for the UK fund, 99% for the US fund). This reflected continuing strong asset performance offset by pull back in Treasury and Gilt yields and a small increase in implied long run inflation in the UK. Forecast 2014 overall funding of $1.25bn remains consistent with 2013.

US Tax Exempt Bond Portfolio

The Treasury Executive Committee endorsed the post-2013 strategy for management of the ~$1 billion US tax exempt bond portfolio at a meeting in February. In accordance with the strategy, the upcoming $200 million mandatory tender in early June will be bought into BP inventory – given that tax exempt rates are not currently competitive with comparable taxable debt. This approach maintains the option to re-float this debt in the future when the interest rate environment may improve.

Segment Support

GENERAL

Major Claims Response Project

In conjunction with the Group Risk Team, BP Legal, and the Segments, the project to identify and engage any needed external expertise to assist BP in a major event resulting in significant third party claims against BP has nearly been completed. Final contractual negotiations are now underway with the two key suppliers. These engagements will allow for a quicker and more efficient response to claims if and when they occur. Completion of this project will also fulfil BP's obligations in many countries for a robust and complete crisis management plan, especially for oil spills.

Global Letters of Credit Portfolio

In Q1, we renewed $0.4bn of committed LC capacity to maintain target of c.$7.5bn. All committed facilities will be on a two year renewal schedule from mid-2014, significantly reducing renegotiation effort. The final two legacy uncommitted facilities have now been agreed to transfer to BP standard terms and conditions. Treasury maintains >$15bn in total LC capacity.

Group Insurance Companies

The Group Insurance companies continued to perform well in Q1 2014 due to good claims experience. Saturn Insurance Inc's premium has increased substantially since the inclusion of the US Terrorism (TRIA) and the primary Workers Compensation programs; in addition the Financial Assurance programs continue to expand steadily. Jupiter's major renewals are now in place; following an RFP AON has been appointed as actuary for review of non-life reserves, and a meeting regarding the credit rating of the group insurance companies was held with AM Best in March, the outcome of which should be available shortly.

Project Vulcan

In conjunction with S&OR and Jupiter Insurance Ltd, this project to develop a consistent fire hazard management review, rating and ranking methodology across key BP assets has progressed to the point where over 30 surveys will be scheduled in 2014. The rating/ranking models to undertake the survey work have also been completed along with good progress made on the development of a risk management information system.

UPSTREAM

Alaska

Treasury continues to work closely with the BP commercial team as the AKLNG project moves toward a Pre-FEED decision. Treasury engaged with the co-venturers financing team (BP, XOM, COP, and TransCanada), which presented an overview on financing and structuring considerations to the AK LNG Commercial Team as well as to representatives of AGDC and the State of Alaska on preliminary financing issues.

Efforts will continue in 2Q14 in developing affordability analyses (from both BP and the other co-venturer perspectives) to help inform BP's commercial decision makers.

Canada Heavy Oil

Treasury provided assurance on the DFM for the next phase of development) in the Pike joint venture (50/50 JV with Devon Energy) which was reviewed and endorsed by the RCM in March 2014.

Global Deepwater Response Team

Treasury progressed with GDR a draft position paper on the Group's provision of financial responsibility / assurance. The GDR team is looking to communicate a BP preferred approach to financial responsibility in general, with the objective of allowing BP to consistently engage with governments, regulators and trade associations to help influence regulations and legislation. The draft position paper was well received by the GDR's Offshore Forum Working team in 1Q 2014, with Treasury looking to finalise the paper during 2Q 2014.

Gulf of Mexico Region

Treasury provided support and assurance for two exploration wells in GoM in the Hopkins and Bright areas respectively. Assurance was also provided for the exchange and cross assignment of Paleogene leases with Chevron in the Keathley Canyon and Garden Banks areas of GOM, a key alignment of leases needed to support BP's Paleogene strategy.

GoM midstream and Destin Pipeline (BP 2/3rd owner) are negotiating a Reimbursement Agreement (RA) for capital expenditure to improve flow assurance for the upstream. The proposed transaction triggered a TUA for asset-based LTCCs, with Treasury providing approval (by means of an SFN). Treasury also provided guidance on the creditworthiness clause in the RA, resisting the partner's request for a credit rating trigger.

Pan American Energy

Treasury continued to support BP's PAE shareholder team through assurance of the PAE 2014 Annual Plan and creation of the 2014 IJV Finance Plan. Treasury approved a 2014 programme SFN for up to $700m in new debt issuance subject to various boundary conditions contained in the IJV Finance Plan. This programmatic approach will simplify the ongoing approval process for PAE debt issuance, allowing the JV to be more nimble in the market while still meeting BP's assurance requirements.

Remediation Management

In response to a newly-enacted New Jersey state law, Treasury worked with Remediation Management to establish and pre-fund a required trust fund. Treasury developed a due diligence process and then formalised it into an SFN to ensure the creation of a trust was commensurate with the remedial activities undertaken and supported by the legal entity that held the relevant remediation liabilities. Despite tight deadlines, compliance with local regulation was ultimately achieved with good transparency of the trust's implications to the Group and the business.

Trinidad

Treasury and the Region are working on the funding of BPTT's Plan for the next 12 – 15 months with partner Repsol. This funding will likely be accomplished through an incremental shareholder loan of up to ~$1bn.

Shah Deniz Phase 2

Treasury continues to work with the AGT Region and IST Gas in optimising the financing strategies in the value chain. On BP's suggestion, the mandate of the TAP pipeline financial advisor has been reduced, simplifying the 2014 work scope.

Iraq IJV

Treasury is working closely with the Iraq Region in evaluating an option to form an Incorporated JV for Rumaila operations as a better reflection of the underlying commercial structure. Trapped cash and impact on economics and Group metrics are being assessed.

Egypt Exposure

A balanced approach to currency and receivables risk continues. Overall exposure continues to reduce with total receivables falling under $1bn as at end 1Q. Negotiations with banks are ongoing for currency conversion.

Tangguh LNG – International Commercial Banks and ADB loan Put Options

BP Berau Limited, the operator for Tangguh implemented the full repayment of the Tangguh Commercial Tranche loan ($820m) and ADB

Tranche loan ($270m) on 31 January 2014. The full repayments of these two loans are unavoidable in view of the failure of the Indonesian Government Oil & Gas regulator (SKK Migas) to approve BP's proposal for the re-pricing of the Commercial Tranche and ADB Tranche loans to current market rates. The loan repayments have been funded by three PSC contractors (BP, $616mm, CNOOC, $212m and Talisman, $46m) and the recovery of the repayments by these contractors commenced from end February 2014 following the execution of the special joint instruction with SKK Migas which instructed the Trustee to allocate certain Tangguh project revenues to repay the relevant parties. Full recovery of the loan repayments is expected within 2014.

Tangguh LNG Train 3 Expansion Project

Treasury, together with the project Financial Advisor (Societe Generale), has developed a preliminary strategy and successfully engaged Tangguh partners on the external financing plan for Tangguh Train 3 expansion project's onshore LNG capex (estimated $5 to 6bn including financing costs during construction) based on a modified Trustee Borrowing Scheme structure approved last year by the Government of Indonesia. The key focus in 1Q 2014 was to present and discuss the preliminary financing strategy with the government oil and gas regulator (SKK Migas). Approval of the financing strategy was planned to be one of the internal minimum conditions of satisfaction required by the Project before the progressing to the milestone of awarding of the onshore FEED contract (planned in April 2014). However, the negotiation process with SKK Migas has been slow in view of the cautious decision making process and management changes at SKK Migas and the difficult environment especially in view of the general and presidential election processes in Indonesia over the coming months. Treasury and the Business is therefore evaluating the option to delink the financial strategy, which may now take longer to agree and then implement, from the onshore FEED process and currently developing a contingency plan to mitigate any delay in financial close (targeted for mid-2015) which may include securing bridge financing cash calls from partners until external financing is in place.

Deepwater Horizon Insurance Litigation

In BP's continuing legal effort to recover insurance proceeds from liability insurance policies placed by Transocean, a briefing was submitted to the Texas Supreme Court in March. We expect this Court to issue its opinion in a timely manner, possibly by year end. Potential recoveries by BP under those policies are in excess of $500 million.

DOWNSTREAM

EOR Fuels Value Chain

Treasury continued to work with EOR FVC on the Growth Through Equity (GTE) project, including development of a JV financing plan. Treasury support for Project Blackhawk was kicked off in 1Q 2014 with an anticipated review by the RCM at its June 2014 meeting.

Byaco Funding

Treasury secured the USD27.2m working capital line from HSBC with no shareholder support for BARACO, a 50% BP-owned Petrochemical JV in Nanjing, China. The financing for BYACO was challenging given the current chemical industry down cycle which has put pressure on operating cash and the limited market liquidity in China. Despite these, Treasury managed to secure the additional clean working capital line for BYACO and is working on finalizing the documentation.

Dim Sum Bond #3 for BP Zhuhai

Towards the end of February, BP successfully raised another CNH1bn (~$164m), 5-year notes at 3.65% in a competitive market with another A-rated MNC (Caterpillar) accessing 2 year money. The order book was >3x oversubscribed against the backdrop of a slump in RMB/USD rate. The bond proceeds were remitted into BP Zhuhai in China in the form of shareholder loans for 10 years. The decision to bring forward the shareholder loans was jointly agreed with the Petrochemicals SPU and CFO organisation to mitigate the risk of BP being unable to launch a bond or attractively access the market and also liquidity risks within China. This bond issuance is expected to deliver close to $5m of interest savings p.a. which would otherwise have to be paid to external banks.

IST

GTEL

Treasury conducted a holistic review of the Freeport LNG transaction during 1Q, providing additional context on the Group's overall level of commitment in developing a LNG export value chain onshore US. Together with the GTEL team, Treasury set the foundations for further monitoring of the transaction's impact on the Group balance sheet as each component of the value chain is committed.

Treasury also drew upon its experience in the recent Shah Deniz 2 export pipeline selection process to facilitate the sharing of lessons learned with the GTEL team as they may pertain to selecting a preferred pipeline route into the Freeport Terminal.

IST Americas

Treasury collaborated with NAGP (in accordance with the recently updated URP policy) in securing joint IST-Treasury approval of a significant programme ATN which targets the securing of US gas supply for some of the Freeport LNG requirements.

Treasury also provided assurance on a number of GOA transactions reviewed at the IST Commitments Committee including those accessing Treasury Unique Authorities such as material operating and finance leases and potential corporate guarantees outside of the IST delegated authority for guarantees.

Project Thunder

Treasury continues support IST on a Rosneft prepayment facility by mandating a small group of BP relationship banks as Lead Arrangers. Discussions are still being progressed.

Advanced economic evaluation for IST

The Investment Evaluation Policy team has been working with IST practitioners to refine the application of BP's economic evaluation methodology) to complex IST transactions. The changes include clarification of the treatment of "low-risk" cash flows, a more refined approach to credit counterparty risk, the introduction of downside cash sensitivities and recognition of "renegotiation" risks.

SHIPPING

BP Shipping Financing Strategy

Treasury led the development of a financing strategy for BP Shipping's acquisition of 24 oil tankers and 6 LNG tankers, evaluating net present cost, risk, optionality, and impact on accounting metrics including capex.