Treasury Key Issues Report
2Q 2010

Financial Markets

Global Markets

The first half of the year finished with growing concerns on the outlook for global growth and renewed anxiety around the EU sovereign crisis. Investors moved out of risky assets in a flight to quality that pushed 2-year US Treasury yields to levels below those seen during the credit crisis. Gold, seen as a safe haven in times of crisis, hit an all-time high of $1,242/oz. Equity markets, commodities and Emerging-market currencies fell as economic news pointed to a slowing Chinese economy and a stagnant US labour market. The S&P Index declined 12% on the quarter bringing losses for the year to 7.87%. Volatility in financial markets climbed to levels not seen since March 2009, as fears grew that Europe's debt crisis could spread around the world. The market was also unsettled by the technical glitch that affected the US equity markets on May 6th. The introduction of a €750bn rescue package for Europe managed to bring some stability to government bonds and the euro. Investors shifted their focus away from the possibility of a near-term government default to the ability of European governments to carry out the austerity measures and their impact on growth. The big news in the FX markets was the announcement by China to move to a more "flexible" exchange rate. The Chinese authorities will link the Renminbi to a basket of currencies with a 0.5% band for daily movements. The Renminbi appreciated by 0.50% against the dollar before the G-20 summit at the end of June. Fiscal consolidation, tougher financial regulation and foreign exchange flexibility were the key issues discussed at the G-20 meeting. However, no consensus was reached on these issues.

US

Economic data was below expectations during Q2, pointing to a slower pace of economic growth in the US. Investor sentiment was influenced by a housing market that slowed down as soon as government incentives expired and by a stagnant labour market. The Fed adopted a more cautious view of growth in the economy. Market expectations are that the first hike in short term rates will not be before mid 2011. The new Financial Regulation bill was approved by Congress and will now be debated in the Senate.

UK

The election and subsequent formation of a Conservative - Liberal Democrat coalition government dominated headlines during 2Q. The emergency budget released by the new Chancellor at the end of June provided support for the pound. It also persuaded rating agencies that the government was committed to address the structural nature of the deficit and that the UK should keep its AAA sovereign rating. The minutes from June's MPC meeting showed some concerns about rising inflation with one member voting to start hiking rates.

Europe

Fiscal problems in the Eurozone continued to be the focus of worldwide attention during Q2. Spreads between Southern European government bonds and German bonds reached new highs as concerns grew that the rescue package did not address the real structural issues within the EU. The euro depreciated almost 10% against the dollar on the quarter and inter-bank rates moved higher as some banks struggled to obtain dollar funding. However, the long term funding facility implemented by the ECB expired with no signs of distress and the Spanish government successfully auctioned EUR3.5bn of bonds.

Japan

Japan's former Finance Minister, Naoto Kan, became the new Prime Minister at the beginning of June. Kan has been an open supporter of a weaker yen and believes the Bank of Japan should be more aggressive in fighting deflation. The yen appreciated more than 6% against the dollar on the quarter as risk sentiment and liquidity became more important to markets than underlying fundamentals. The Tankan survey revealed a positive change in business sentiment among manufacturers in 2Q as exports gathered momentum.

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Financial Information

$m	2Q'10	1Q'10	4Q'09
Gross Debt	30,580	32,153	34,627
Less FV of debt hedges	(53)	(152)	(127)
Cash	(7,310)	(6,841)	(8,339)
Net Debt	23,217	25,160	26,161
Net Debt Ratio	21%	19%	20%
Income Statement	**2Q'10**	**1Q'10**	**4Q'09**
Interest Payable	192	194	195
Finance Costs	224	238	252
Qtr End Exchange Rates	**2Q'10**	**1Q'10**	**4Q'09**
USD/GBP	1.5058	1.5106	1.6010
USD/EUR	1.2177	1.3423	1.4300

Financial Commentary

Reported net debt decreased by $1.9bn in the quarter. Gearing increased to 21% taking into account the effect of provisioning for GoM. Net Debt and the Net Debt ratio are now shown including the offset of debt-related hedges.

Credit ratings

Following the cuts in our ratings post the Macondo incident, in September both Moodys and S&P took our ratings off creditwatch negative. Moodys confirmed our rating as A2 stable and S&P, A negative outlook. These changes reflected the success of killing the well and reduced uncertainty around the likely final liabilities. The size of the final liability and the wider impact on our US operations remain an overhang on the ratings. Fitch, who provide an unsolicited rating, also upgraded our rating to A stable.

Funding and Liquidity

After the dramatic widening of our CDS and secondary bond trading levels in June to distress levels, they fell rapidly from mid July with the improving newsflow before settling at levels around BBB.

The immediate actions in the aftermath of the Macondo incident were to buttress the Group's balance sheet and diversify our sources of liquidity:

- A sizeable cash buffer was maintained.
- In addition to our existing standby bank facilities of $5.25bn, we negotiated further committed unsecured bank facilities resulting in total banking facilities of close to $17bn.
- Pre oil export financing loans for Angola and Azerbaijan amounting to $4.75bn were put in place
- Secured financing was raised from Group equity holdings and IST working capital

As the newsflow improved again following the publication of the Bly report, bottom kill and ratings upgrades, our CDS and secondary levels continued to grind tighter. We returned to the conventional long term bond markets in late September/early October issuing $3.5bn in the US markets and €2bn in the Euromarkets. Both deals were heavily oversubscribed, enabling us to issue without any changes to BP's routine T&Cs and within secondary levels. The success of the issues has given further impetus to tightening in our CDS and secondary spreads.

Pensions

The funding level of our funded pension plans remained under pressure in 3Q reflecting record lows in government bond yields. However, our main UK plan however remains overfunded at 102% and 101% funded for the June-September period which determines next year's funding. The US plan funding on an IAS19 basis is around 76% but above 80% on a smoothed PPA funding basis. Total 2010 contributions of $1bn are planned, in line with

2009. Around $750m has been contributed in 1H 2010.

Key Issues

GoM Incident Response

The Macondo well incident has required a broad-based and sustained Treasury response. Specifically we:

- Ensured timely responses to action requests from Incident Response teams (e.g. emergency checks, state grant payments);
- Responded to various information and / or adequate assurance requests from external parties (e.g. CME, FSA, EPA, surety bond providers);
- Undertook actions to manage the US tax exempt and gas prepaid bond portfolios in light of bondholder puts and yield volatility;
- Managed issues arising with existing guarantees (e.g. ratings triggers) and also from the businesses' need for ongoing credit support (e.g. provision of letters of credit / collateral);
- Supported multiple IST financing initiatives;
- Joined with M&A in coordinating the evaluation of options for the structuring of the $20bn oil spill trust / escrow fund; and
- Initiated support to a number of M&A efforts underpinning the Group's announced divestment agenda.

GoM Claims

Insurance Risk Solutions has assisted in the GoM oil spill response on several fronts: (i) instigating claims on our contractors' insurance policies where we have a right to do so, (ii) assisting with the claims handling process, (iii) providing oversight on claims for bodily injury and (iv) operationalising the claim on Jupiter, the BP Group captive insurer.

Counterparty Risk

Uncertainty in the credit markets regarding BP following the MC252 incident has caused some counterparties to review their credit appetite to the Group. Treasury is proactively working with IST, R&M and E&P to protect and manage the Group's liquidity position and to ensure counterparties receive accurate information about the Group's financial position.

Devon Acquisition

Treasury coordinated several actions in support of the 2Q closing of the GoM asset package. This included the execution of the Nansen sublease, the assignment of the West Sirius drilling rig, and the wire transfer of the final payment. In addition, Treasury is facilitating the planned replacement of the Independence Hub guarantee.

Structuring guidance was provided on the formation of the Canadian joint venture with Devon. In particular, advice was given on the Devon promissory note and guarantee.

Treasury continues to progress required closing actions for the Brazil asset package, notably final due diligence on leases and the provision of replacement guarantees.

M&A activity

Treasury continued to provide support for a number of portfolio actions. Apart from this, support has been provided for the Devon acquisition, the disposal of BBG, as well as a number of other EMEA Fuels Value Chain portfolio changes.

Alaska

Assurance was provided in support of the AtN put forth by the BP Alaska gas upstream team in its potential capacity as a shipper. Treasury advised upon likely credit support issues for any bid, including the inclusion of appropriate creditworthiness standards.

Trinidad

During 2Q, Treasury coordinated the payment of $13.8m (net BP) of dividends from Trinidad entities and a partial loan repayment (trapped cash release) from Trinidad A4 of $70m (net BP).

US Wind Financing

The Goshen II wind project financing ($283m gross) was closed in 2Q with a group of with a group of three initial banks. A fourth bank was brought in during the syndication process. This financing featured an innovative bridge loan for the ITC cash grant.

Progress continued to be made on the $330m Fowler II wind financing project. The funding proposal was negotiated with a club of banks and is now being taken to credit their committees. Closing is anticipated in 3Q.

During 2Q, Treasury also conducted a RFP for the $320m Cedar Creek II wind financing. A group of seven initial banks was selected to negotiate a club financing. The likely closing date of this transaction is in early 4Q.

Shipping

A review has been completed and presented to the Group Financial Risk Committee of BP's group-wide current and future shipping needs, setting out choices for financing the replenishment of the BP shipping fleet as existing leases terminate over the next 10 years. These choices have been framed in the context of Ship Financing Frameworks, current shipping and ship finance markets, the impact on group financial metrics and the potential impact of future lease accounting changes.

Decommissioning

External financial security of USD$210m was put in place as a result of our downgrade to cover decommissioning liabilities for the North Sea Miller field.

Insurance Optimisation

Contractor enrolment for the Texas City Refinery OCIP program was completed in 2Q. This programme, which eliminates indirect contractor insurance costs, is on target to deliver $14m+ in savings over the next 4 years. Revised forecasts for the Whiting OCIP are well in excess of original savings projections at $30m. We have continued to develop the concept for OCIP at Carson, with expected closure by year end. This approach is now becoming standard practice and is being expanded to other locations.

Feasibility analysis on the establishment of a new US based captive insurance company is ongoing.

Risk Mitigation

A programme to perform fire protection safety audits by Marsh Engineering has begun. Audits started in 2Q in Lubes and Eastern Hemisphere Refining. The objective of these audits is to identify and rank risk reduction measures at participating locations.

Remediation

Insurance solutions are being developed for the last two remaining mining sites. Further economies of scale are being considered by combining both sites into a single insurance market placing.

China Funding

BP businesses in China refinanced about $625m (gross) of loans at favourable terms during 2Q. Liquidity is expected to remain available for BP and its JV partners during the second half of the year.

China Onshore Bond

A cost benefit analysis of issuing an onshore RMB bond was completed. Local regulations are such that issuing an onshore bond would require the large scale restructuring of BP investments in China. Our analysis indicates that, at present, the costs of restructuring outweigh the benefits associated with interest cost savings.

EEM Policy

A policy paper reviewing the EEM policy of discounting fixed commitments at BP's cost of debt (dual discounting) was finalised, supporting the existing policy.

