Report of the President

In 2017, despite the gradual recovery of the oil and gas industry, the company still faced tough challenges like volatility in oil prices, increased competition in the refined oil market, widened peak-trough gap in natural gas demand, especially the arduous task of securing winter gas supplies. Leveraging its integrated strengths, the company took a well-planned and coordinated approach to coping with the changing market, optimizing production operations, cutting cost and boosting efficiency to achieve steady increase in outputs and healthy growth in earnings. The company reported RMB 2,340.3 billion in total revenue and RMB 53.3 billion in total profit for the year.

In 2017, we made remarkable achievements in all business segments:

Domestic E&P business saw transformation in development mode with lower costs and rising profitability. With an emphasis on high-quality reserves, the company optimized exploration deployment and focused its technical and financial resources on high-efficiency exploration, making a number of major discoveries in the Junggar, Tarim and Sichuan basins and proving a series of high-quality and sizable producible reserves in the Ordors, Songliao and Bohai Bay basins. The full-year additions to proven oil and gas in place were 659.45 million tons and 569.8 billion cubic meters respectively, providing a solid ground for stabilizing oil production and ramping up gas output. Our efficiency-centered development activities aimed to optimize the development schemes and production structure and stably implemented a range of key capacity projects including the Mahu project at Xinjiang Oilfield and the Halahatang project in the Tarim Basin. We produced 102.54 million tons of crude oil throughout the year. Taking advantage of growing demand for natural gas, the company adopted a dynamic approach to gas production based on seasonal consumption patterns and tapped the potential of production capacity to ensure ample supply, registered a full year gas output up to more than 100 billion cubic meters. In particular, unconventional gas production such as shale gas and coalbed methane continued to increase.

The lifting costs per unit for oil and gas continued to decrease on a comparable basis, as a result of a series of measures for improving reserve management, cutting inefficient capacity, saving land with well clustering, increasing recoverable reserves through fine reservoir description and enhancing recovery through subdivision waterflooding, etc.

Refining and chemicals business achieved record-high earnings by optimizing operation and adjusting products mix. The company ensured the long-term, high-utilization operation of its integrated refining-petrochemical complexes and high-performing facilities by optimizing the allocation of crude oil resources and producing more chemicals. In 2017, we processed 152.45 million tons of crude, and produced 103.51 million tons of refined products and 5.76 million tons of ethylene, up 3.6%, 4.2% and 3.1% respectively. The upgrading of products mix and products quality led to a lower diesel-gasoline ratio of 1.28 and an increase of 10.2 percentage points in high-value refined products. The supply schedules for the National VI Standard-compliant gasoline and diesel in "2+26 Cities" were completed on time. Chemicals marketing kept optimizing resource allocation and logistics and promoting new products, selling 27.98 million tons of chemical products throughout the year. We made headway in a range of key projects. The refining facility was successfully commissioned at Yunnan Petrochemical; upgrading and expansion project proceeded smoothly at Huabei Petrochemical and Liaoyang Petrochemical; and a number of alkylation projects for gasoline upgrading advanced steadily. Refining and chemicals business remained an important source of revenue for the company, with 20 technical and financial indictors better than those in 2016.

Oil products sales continued to grow with marketing capabilities increased gradually. The company's full-year oil products sales reached 114.16 million tons, up 1% year-on-year, as a result of coordinating production and marketing activities, addressing regional imbalances, increasing exports, promoting integrated marketing and boosting the sales of high-value oil products such as premium gasoline and jet fuels. A series of marketing initiatives were launched, including third-party billing and retail apps, theme sales joint promotion and integrated marketing of oil products, fuel cards, non-fuel products and lubricants. Our marketing network was further expanded with a growing number of newly established, leased and joint-venture service stations.

Natural gas and pipelines business ensured growing supply and steady profitability. Given a sharp increase in natural gas demand, the company coordinated and balanced the transportation, allocation and marketing of domestically produced gas, pipeline gas imports and LNG to keep the market well-supplied. The company sold 151.8 billion cubic meters of natural gas domestically in 2017, up 15.5% year-on-year. The management on natural gas sales and purchase contracts was strengthened. The first online auction of 1 billion cubic meter of natural gas was made. An integrated natural gas sales framework was taken shape, based on sale and purchase contracts, prepayment system and online/offline transactions. Oil and gas pipeline operations stayed safe and efficient through centralized planning, scheduling and control. Key projects saw solid progress. Construction of the northern section of the Eastern Route of the Russia-China Gas Pipeline was in full swing; the Myanmar-China Crude Pipeline, the Second Russia-China Crude Pipeline, the Fourth Shaanxi-Beijing Gas Pipeline, Zhongwei-Jingbian spur line of the Third West-East Gas Pipeline and Yunnan Refined Products Pipeline were put into operation on schedule.

Overseas operations continued to expand with robust growth in operating efficiency. Embracing the opportunities emerging under the Belt and Road Initiative, new projects including ADCO onshore in Abu Dhabi, South Pars in Iran, Peroba in Brazil were launched and a number of cooperation agreements were signed with energy companies from the United States, Russia, and Kazakhstan, etc. Based on comprehensive research and prioritization of prospects, new breakthroughs were made at Libra (Brazil), Amu Darya (Turkmenistan) and Andes (Ecuador), etc. Our newly added recoverable reserves amounted to 90.93 million tons of oil equivalent for the full year. Our full-year equity production hit a record high, including 68.80 million tons of crude oil and 25.5 billion cubic meters of natural gas, as a result of optimizing development plans, beefing up the development of high-value projects, accelerating drilling and operation of new wells, and boosting EOR efforts. In 2017, the company saw important achievements in its overseas projects, including the successful commissioning of the first phase of Yamal LNG in Russia, the first phase of the Shymkent Refinery upgrading project in Kazakhstan and the EGR project at the Saman-Depe Gas Field in Turkmenistan. Meanwhile, taking advantage of three overseas operation centers, our international trading business actively organized oil and gas imports, expanded oil products exports and increased sales of shared oil from overseas projects. In 2017, our trading volume was 470 million tons with turnover of USD 184.4 billion.

Service businesses made more market expansion efforts with performance continued to improve. The company's oilfield service business kept promoting general contracting and factory operation to boost speed and efficiency. We were awarded a number of major projects in Kuwait, Iraq and Venezuela. We participated in the offshore gas hydrate pilot project as the general contractor for the first time and achieved historic success, setting a new record in recovery duration and production volume. Giving full play to specialized advantages, our engineering construction business ensured the construction of key projects. We actively explored international market and won the contracts for the Amur Gas Processing Plant in Russia, integrated facilities at the Bab oilfield in UAE and Saudi Aramco's pipeline in Saudi Arabia, etc. In equipment manufacturing, the company sped up transformation to a service-oriented equipment manufacturer based on the "Manufacturing + Services" business mode. Our financial services continued to bolster the core business operations by integrating finance and production needs, promoting product and customer development, and deepening channel and service innovation.

Reform and innovation stimulated vitality and corporate management effectively improved. As the corporate reform continued to deepen, the company and its 151 subsidiaries underwent the transformation in ownership; the reform of overseas operation systems progressed well; the specialized restructuring of our engineering service sector was basically completed; China Petroleum Engineering Co., Ltd. (CPEC) and CNPC Capital Co., Ltd. were publicly listed; the pilot programs for promoting autonomy in management advanced steadily; internal oil and gas product and service pricing mechanisms were further straightened out; and the first batch of internal mining right transfer was conducted successfully. The company's operating efficiency improved significantly as a result of optimizing investment structure, curbing non-productive expenditure, implementing rigidly production and operation plans, cutting costs and boosting efficiency.

HSE management level was enhanced comprehensively and HSE situation was stable in general. The assessment of HSE management system continued to deepen; HSE standards were implemented across front-line sites and stations; risk management was stepped up for key areas and sensitive periods; inspections were conducted against HSE hazards, radioactive sources and hazardous chemicals; coal-fired boilers were phased out, gas-fired boilers were transformed and volatile organic compounds (VOCs) were effectively treated; and prevention and control on safety and security risks was heightened in overseas operations. HSE situation was stable in general .The company's full-year energy use was down by 880,000 tons of standard coal and water use down by 12.41 million cubic meters.

Technological innovation and IT application bolstered core business development. Important achievements were made in the development and application of some core technologies, including the techniques for exploration, evaluation and development of lithologic reservoirs, technical solutions for extracting shale gas from reservoirs within 3,500 meters; high-value oil products and synthetic materials; and the SCADA system for long-distance pipeline transportation, all of which have provided strong support for our core business development. ERP application integration was completed across the board; cloud technology platform was applied further; data sharing and integrated application capabilities were enhanced; digitization and intelligentization construction advanced steadily; and the application of IT-enabled systems played an increasingly notable role on business.

Looking ahead into 2018, we will implement the guideline of sound development across the board by further leveraging our integrated advantages, focusing more on the guiding role of market, resource allocation optimization and business risks prevention. With these efforts, we are confident to meet all our business objectives and score new achievements.

President