

# ENERGY INVESTMENTS FOR THE FUTURE

An Excerpt From The 2005 Annual Report



# WORLDWIDE OPERATIONS

*At ConocoPhillips, our purpose is to use our pioneering spirit to responsibly deliver energy to the world.*

## Exploration and Production (E&P)

**Profile:** Explores for and produces crude oil, natural gas and natural gas liquids (NGL) on a worldwide basis. Also mines oil sands to upgrade to Syncrude. A key strategy is the development of legacy assets — very large oil and gas developments that can provide strong financial returns over long periods of time — through exploration, exploitation, redevelopments and acquisitions.

**Operations:** At year-end 2005, E&P held a combined 41.2 million net developed and undeveloped acres in 23 countries and produced hydrocarbons in 13, with proved reserves in three additional countries. Crude oil production in 2005 averaged 907,000 barrels per day (BD), gas production averaged 3.3 billion cubic feet per day, and natural gas liquids production averaged 91,000 BD. Key regional focus areas included the North Slope of Alaska; the Asia Pacific region, including Australia, offshore China and the Timor Sea; Canada; the Caspian Sea; the Middle East; Nigeria; the North Sea; Russia; the Lower 48 United States, including the Gulf of Mexico; and Venezuela.

## Refining and Marketing (R&M)

**Profile:** Refines crude oil, and markets and transports petroleum products. ConocoPhillips is the second-largest refiner in the United States and, of nongovernment-controlled companies, is the sixth-largest refiner in the world.

**Operations:** Refining — At year-end 2005, R&M owned 12 U.S. refineries, owned or had an interest in five European refineries, and had an interest in one refinery in Malaysia, totaling a combined net crude oil refining capacity of 2.61 million barrels of oil per day. Marketing — At year-end 2005, gasoline and distillates were sold through approximately 13,600 branded outlets in the United States, Europe and the Asia Pacific region. In the United States, products were marketed primarily under the Phillips 66, Conoco and 76 brands. In Europe and the Asia Pacific region, the company marketed primarily under the JET and ProJET brands. The company also marketed lubricants, commercial fuels, aviation fuels and liquid petroleum gas. ConocoPhillips' refined products sales were 3.3 million BD in 2005. The company also participated in joint ventures that support the specialty products business. Transportation — R&M owned or had an interest in about 29,000 miles of pipeline systems in the United States at year-end 2005.

## LUKOIL Investment

**Profile:** This segment consists of ConocoPhillips' investment in the ordinary shares of LUKOIL, an international, integrated oil and gas company headquartered in Russia. ConocoPhillips' investment was 16.1 percent as of Dec. 31, 2005.

**Operations:** At year-end 2005, LUKOIL had exploration, production, refining and marketing operations in about 30 countries.

## Midstream

**Profile:** Midstream consists of ConocoPhillips' 50 percent interest in Duke Energy Field Services, LLC (DEFS), as well as certain ConocoPhillips assets predominantly located in North America. Midstream gathers natural gas, extracts and sells the NGL, and sells the remaining (residue) gas to electrical utilities, industrial users and gas marketing companies.

**Operations:** At year-end 2005, DEFS' gathering and transmission systems included nearly 56,000 miles of pipelines, mainly in six of the major U.S. gas regions. DEFS also owned or operated 54 NGL extraction plants. Raw natural gas throughput averaged 5.9 billion cubic feet per day, and NGL extraction averaged 353,000 BD in 2005. In addition, ConocoPhillips owned or had an interest in four gas processing plants and four NGL fractionators at year-end 2005.

## Chemicals

**Profile:** ConocoPhillips participates in the chemicals sector through its 50 percent ownership of Chevron Phillips Chemical Company LLC (CPChem), a joint venture with Chevron. Major product lines included: olefins and polyolefins, including ethylene, polyethylene, normal alpha olefins and plastic pipe; aromatics and styrenics, including styrene, polystyrene, benzene, cyclohexane, paraxylene and K-Resin® styrene-butadiene copolymer; and specialty chemicals and proprietary plastics.

**Operations:** At year-end 2005, CPChem's 11 facilities in the United States were located in Louisiana, Mississippi, Ohio and Texas. The company also had nine polyethylene pipe, conduit and pipe fittings plants in eight states, and a petrochemical complex in Puerto Rico. Major international facilities were in Belgium, China, Saudi Arabia, Singapore, South Korea and Qatar. CPChem also had a plastic pipe plant in Mexico.



- Exploration Only
- Exploration and Production
- Production Only
- Refining
- Midstream
- Chemicals
- Retail Marketing\*

\*Retail Marketing is located in the following countries: Austria, Belgium, Czech Republic, Denmark, Finland, Germany, Hungary, Luxembourg, Malaysia, Norway, Poland, Slovakia, Sweden, Switzerland, Thailand, United Kingdom and the United States.

# LETTER TO SHAREHOLDERS

## The Relentless Challenge



J.J. Mulva, Chairman and Chief Executive Officer

### To Our Shareholders:

At ConocoPhillips, we welcome the relentless challenge of raising shareholder value. In 2005, we strived to meet that challenge by delivering good operating and financial performances, while investing in strong, value-building opportunities.

The company's net income in 2005 was \$13.5 billion, or \$9.55 per share, compared with net income of \$8.1 billion, or \$5.80 per share, in 2004. This solid financial performance, coupled with \$2.5 billion in debt reduction, boosted the company's adjusted return on capital employed (ROCE) to 32.1 percent\*, compared with 23.3 percent a year earlier.

In line with our objective to maintain regular dividend increases, we raised the quarterly dividend rate by 24 percent during the year. In addition, we completed a two-for-one stock split and made share repurchases totaling \$1.9 billion. The combination of larger dividends and stock appreciation provided shareholders with a total return of 36.7 percent. This was markedly higher than the returns of our peer companies, which are among the largest publicly owned and traded firms in the industry.

### Significant Investment Milestones

As the world's need for oil and natural gas continues to expand, ConocoPhillips is growing to meet that need with a portfolio of new energy investments. However, we recognize that our growth is sustainable only if we continue to deliver increasing value, along with providing greater energy supply. Therefore, our growth plans are highly disciplined and tightly focused on the goal of building a strong, diversified foundation of value-generating assets.

Several significant investment milestones were reached in 2005 and early 2006 including:

- Embarking on a \$4 billion to \$5 billion multi-year program to expand capacity and enhance processing capabilities in our U.S. refining system.

- Acquiring the 275,000-barrel-a-day Wilhelmshaven, Germany, refinery, which enhances our European and Atlantic refining position.
- Expanding the company's equity interest in LUKOIL and creating a significant venture in Russia with this large, international energy partner.
- Launching the development of a large liquefied natural gas (LNG) project supplying natural gas from Qatar, primarily to the United States.
- Completing a large LNG project in Australia to provide gas shipments under long-term contract to utilities in Japan.
- Returning to Libya after a 19-year absence, a move which adds to our reserves, increases production and offers substantial exploration potential.
- Increasing ConocoPhillips' ownership in Duke Energy Field Services, LLC (DEFS), one of the largest natural gas processors and marketers in the United States.
- Initiating the process to acquire Burlington Resources, a leading explorer and producer of natural gas in North America.

These investments are clear manifestations of our strategy to direct our cash flow toward growing our asset base and strengthening our competitive position for the long term. We're confident that the outcome will position us for even stronger cash flows and earnings for the future.

### Burlington Resources Acquisition

The acquisition of Burlington Resources will add depth to our overall production, reserves and exploration portfolio and will increase our production base in Organization for Economic Co-operation and Development countries.

When Burlington's assets are integrated with ConocoPhillips', our company will be a leading gas producer and supplier in North

America. Burlington is a major gas explorer and producer in the United States and Canada, with reserves of more than 2 billion barrels of oil equivalent (BOE) and production of about 475,000 BOE per day, of which some 80 percent is natural gas and gas liquids.

Burlington's near-term production profile is robust and growing, plus Burlington possesses an extensive inventory of prospects and significant land positions in the most promising basins in North America, primarily onshore. With this access to high-quality, long-life reserves, the acquisition enhances our production growth from both conventional and unconventional gas resources.

Specifically, our portfolio will be bolstered by opportunities to enhance production and gain operating synergies in the San Juan Basin of the United States and by an expanded presence and better utilization of our assets in Western Canada. In addition to growth possibilities, these assets also provide significant cash generation potential well into the future.

Beyond adding to production and reserves, Burlington also brings well-recognized technical expertise that, together with ConocoPhillips' existing upstream capabilities, will create a superior organization to capitalize on the expanded asset base. We do not anticipate that the \$33.9 billion acquisition will require asset sales within either ConocoPhillips or Burlington, nor should it change our organic growth plans for the company. We expect to achieve synergies and pretax cost savings of approximately \$375 million annually, after the operations of the two companies are fully integrated.

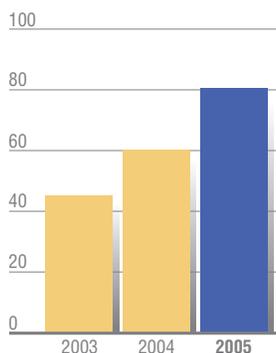
We anticipate immediate and future cash generation from this transaction that will aid in the rapid reduction of debt incurred for the acquisition and go toward the redeployment of cash into strategic areas of growth. Burlington shareholders will vote on the proposed transaction at a meeting on March 30, 2006.

#### LUKOIL Alliance

Our strategic alliance with LUKOIL, formed in 2004, continued to develop with positive results in 2005. We increased our equity ownership in this large, international oil and gas company to 16.1 percent during 2005, and we expect to increase our interest in 2006 to

#### Market Capitalization

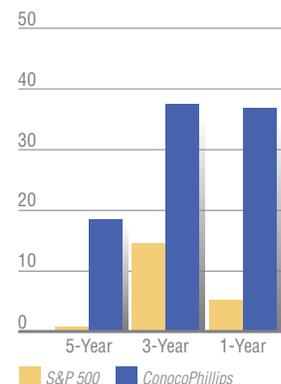
(Billions of Dollars)



ConocoPhillips' market capitalization was \$80.2 billion at the end of 2005, representing a 33 percent increase from 2004. The company had 1,378 million shares outstanding on Dec. 31, 2005, with a year-end closing price of \$58.18.

#### Total Shareholder Return

(Annual Average Return in Percent)



The company's total shareholder return for 2005 was 36.7 percent, highest among its peers. ConocoPhillips' return to shareholders over the three-year period was 37.2 percent and over a five-year period was 18.3 percent.

our contractual limit of 20 percent. Our LUKOIL investment contributed about 15 percent to ConocoPhillips' 2005 average daily oil and gas production and 5 percent to our average daily crude oil refining throughput.

Also under the alliance, we finalized a major E&P joint venture, Naryanmarneftegaz, with LUKOIL last year. We have a 30 percent interest in the project and equally share governance responsibilities. A crucial aspect of this project in northern Russia is the staffing of the venture with key personnel from the two companies and the sharing of technical expertise and best practices. By bringing together the strong Arctic experience of both companies, we believe we've created a powerful combination of technical resources to deal with the challenges of operating in the Far North and in other difficult environments.

We also are pursuing other international E&P and Refining and Marketing (R&M) opportunities with LUKOIL.

#### Increasing Value Through Investment

Our commitment to value-driven growth is exemplified by the fact that ConocoPhillips redeploys into its operating businesses a greater percentage of its cash flow than any of its peer companies. Over the last

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two years, approximately 70 percent of the company's cash provided by operating activities has been channeled back into growing the business, including expanding our equity positions in LUKOIL and DEFS.

Capital expenditures and investments in the business have risen from \$6.2 billion in 2003 to \$9.5 billion in 2004 and to \$11.6 billion last year. In 2006, we expect our capital spending to be approximately \$11.2 billion, which includes expenditures for our re-entry into Libya and the acquisition of the Wilhelmshaven refinery. Not included in this estimate are capital expenditures and investments related to Burlington Resources' assets after the acquisition is complete and discretionary expenditures to increase our equity interest in LUKOIL.

ConocoPhillips' investment plans reflect our belief in the importance of strong integration between E&P and R&M. Our E&P investments will be directed toward growing reserves and production in resource-rich regions, while R&M investments will be focused on increasing our refining capabilities and capacities to handle more E&P production of heavier, higher-sulfur crude oils.

We expect to invest \$4 billion to \$5 billion over the next several years at nine of our 12 U.S. refineries. These investments will allow us to increase our output of clean fuels by as much as 15 percent. This is roughly the equivalent of adding one world-scale refinery to our U.S. refining system.

In early 2006, we expanded our international refining presence through acquisition of the Wilhelmshaven, Germany, refinery. This acquisition further enhances our position in Europe, strengthens our ability to supply products to key export markets and ties closely with our U.S. East Coast refineries. When additional investments are completed to increase its processing capabilities and complexity, the refinery will have the potential to handle production of lower-quality crudes, such as Russian-export blends.

The company also is looking at other ways to grow our European and Asian refining positions, while continuing to improve the integration of our refining capabilities with our crude oil production assets around the world.

ROCE continues to be an important yardstick for assessing the performance of our current operations and evaluating the worth of

prospective projects. Our R&M business consistently leads the peer companies on an adjusted ROCE basis, while our E&P business is very competitive with our peer group. As a result, ConocoPhillips' overall adjusted ROCE was among the highest in its peer group in 2005.

### **Business Environment and Outlook**

Higher oil and natural gas prices, along with improved refinery margins, were a major factor in the financial results of the petroleum industry in 2005. Prices and margins rose as global economic growth supported strong demand, while supply was disrupted by the U.S. Gulf of Mexico hurricanes. Oil and gas production capacity remained tight throughout the year, and many refineries ran at high utilization rates. Geopolitical concerns about supply security also continued to put upward pressure on prices.

In terms of the Gulf Coast hurricanes' impact on ConocoPhillips' operations, we were able to restore most of our affected operated oil and gas production relatively quickly. However, one partner-operated oil and gas field was down until near the end of the year, and two of our refineries were out of service for some time. Most affected was the 247,000-barrel-per-day Alliance refinery near New Orleans, which began partial operation in early 2006 and was expected to be in full operation around the end of the first quarter.

The exceptional performance of our employees before, during and after the Gulf Coast disasters is a testament to their dedication and service. Employees at dozens of affected facilities, large and small, safely performed complicated shutdown and restoration functions under difficult conditions. Many worked with tremendous perseverance despite personal losses and damage to their communities. Every effort was made to keep our customers supplied in the face of unprecedented circumstances. When relief efforts began, employees throughout the company, along with our retirees, came to the aid of displaced families and devastated communities with direct aid, as well as financial support.

Looking ahead, we expect global energy demand to continue climbing, assuming continued global economic growth. Production capacity is anticipated to be continuously stretched, and refineries

*ConocoPhillips is committed to being a part of the solution to the world's energy needs. We are intent on developing diverse, reliable resources of oil and natural gas around the globe. We are investing to expand the capacity and improve the capabilities of our infrastructure to process and transport energy. And we're serious in our efforts to pursue promising alternatives to supplement the traditional oil and gas resources that will be the mainstay of energy supply well into the future.*

are expected to run at levels well above those historically seen in the industry. Ongoing geopolitical concerns and heightened worries about weather-related disasters will contribute to price volatility. Overall, the outlook we see for the next several years is one of rising demand for our products and a continuation of prices above historical norms.

At the same time, higher costs and increasing competition will challenge us. The large number of multi-billion-dollar infrastructure projects now under development by our industry around the world is straining the supply of skilled personnel and driving up material costs. In addition, access to resources has become more limited and more costly, in part because new competitors, including newly privatized or invigorated national oil companies, have entered the world energy scene seeking development opportunities in resource-rich areas. Our strategic alliance with LUKOIL and our planned acquisition of Burlington Resources represent two responses to the challenges of increased competition and more restricted access opportunities.

Without question, the strong market for oil and gas had a marked effect on our 2005 performance. But it takes safe, consistently well-run operations to fully benefit from strong market conditions. We achieved that outcome in 2005, thanks to the hard work of our employees throughout the world.

#### The ConocoPhillips Culture

Although less than four years have passed since the merger that created our company, we believe a distinctive ConocoPhillips culture has been forged. We are a big company, and growing larger. But we strive to operate like the smaller companies from which we were

formed — quicker, more innovative and more agile than our larger competitors. We know it's important to keep that attitude and mode-of-operation in mind as we continue to grow.

ConocoPhillips is committed to being a part of the solution to the world's energy needs. We are intent on developing diverse, reliable resources of oil and natural gas around the globe. We are investing to expand the capacity and improve the capabilities of our infrastructure to process and transport energy. And we're serious in our efforts to pursue promising alternatives to supplement the traditional oil and gas resources that will be the mainstay of energy supply well into the future.

As a result of the growing scope, scale and capability of ConocoPhillips, we are able to take advantage of more opportunities today than we thought possible just two or three years ago. We intend to pursue these opportunities aggressively, but with a disciplined focus to assure they meet our foremost goal — raising shareholder value. This is our relentless challenge.



J.J. Mulva  
Chairman and Chief Executive Officer  
March 1, 2006

#### RECONCILIATION TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

Return on Capital Employed Adjusted  
for Purchase Accounting

	Millions of Dollars Except as Indicated			
	2005		2004	
	GAAP ROCE	Adjusted for Purchase Accounting	GAAP ROCE	Adjusted for Purchase Accounting
Income from continuing operations	\$13,640	13,640	8,107	8,107
After-tax interest and minority interest	345	345	376	376
Alaska DD&A on asset step-up	—	124	—	124
Adjusted ROCE Income	\$13,985	14,109	8,483	8,607
Average capital employed	\$62,643	62,643	55,908	55,908
Purchase adjustments:				
Acquisition of ARCO Alaska	—	(1,889)	—	(2,069)
Acquisition of Tosco	—	(2,959)	—	(2,959)
ConocoPhillips merger	—	(13,833)	—	(13,895)
Adjusted Average Capital Employed	\$62,643	43,962	55,908	36,985
Return on Capital Employed	22.3%	32.1	15.2	23.3

# FINANCIAL HIGHLIGHTS

	Millions of Dollars Except as Indicated		
	2005	2004	% Change
<b>FINANCIAL</b>			
Total revenues and other income	\$ 183,364	136,916	34
Income from continuing operations	\$ 13,640	8,107	68
Net income	\$ 13,529	8,129	66
Per share of common stock — diluted*			
Income from continuing operations	\$ 9.63	5.79	66
Net income	\$ 9.55	5.80	65
Net cash provided by operating activities	\$ 17,628	11,959	47
Capital expenditures and investments	\$ 11,620	9,496	22
Total assets	\$ 106,999	92,861	15
Total debt	\$ 12,516	15,002	(17)
Minority interests	\$ 1,209	1,105	9
Common stockholders' equity	\$ 52,731	42,723	23
Percent of total debt to capital**	19%	26	(27)
Common stockholders' equity per share (book value)*	\$ 38.27	30.75	24
Cash dividends per common share	\$ 1.18	0.90	31
Closing stock price per common share*	\$ 58.18	43.42	34
Common shares outstanding at year-end (in thousands)*	1,377,849	1,389,547	(1)
Average common shares outstanding (in thousands)*			
Basic	1,393,371	1,381,568	1
Diluted	1,417,028	1,401,300	1
Employees at year-end (in thousands)	35.6	35.8	(1)

\*Per-share amounts and number of common shares outstanding in all periods reflect a two-for-one stock split effected as a 100 percent stock dividend on June 1, 2005.

\*\*Capital includes total debt, minority interests and stockholders' equity.

	2005	2004	% Change
<b>OPERATING*</b>			
U.S. crude oil production (MBD)	353	349	1
Worldwide crude oil production (MBD)	907	905	—
U.S. natural gas production (MMCFD)	1,381	1,388	(1)
Worldwide natural gas production (MMCFD)	3,270	3,317	(1)
Worldwide natural gas liquids production (MBD)	91	84	8
Worldwide Syncrude production (MBD)	19	21	(10)
LUKOIL Investment net production (MBOED)**	246	40	515
Worldwide production (MBOED)***	1,808	1,603	13
Natural gas liquids extracted — Midstream (MBD)	195	194	1
Refinery crude oil throughput (MBD)	2,420	2,455	(1)
Refinery utilization rate (%)	93	94	(1)
U.S. automotive gasoline sales (MBD)	1,374	1,356	1
U.S. distillates sales (MBD)	675	553	22
Worldwide petroleum products sales (MBD)	3,251	3,141	4
LUKOIL Investment refinery crude oil throughput (MBD)**	122	19	542

\*Includes ConocoPhillips' share of equity affiliates, except LUKOIL, unless otherwise indicated.

\*\*Represents ConocoPhillips' net share of its estimate of LUKOIL's production and processing.

\*\*\*Includes Syncrude and ConocoPhillips' estimated share of LUKOIL's production.

Certain disclosures in this Annual Report may be considered "forward-looking" statements. These are made pursuant to "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. The "Cautionary Statement" in Management's Discussion and Analysis on page 57 of the complete version of the 2005 Annual Report should be read in conjunction with such statements.