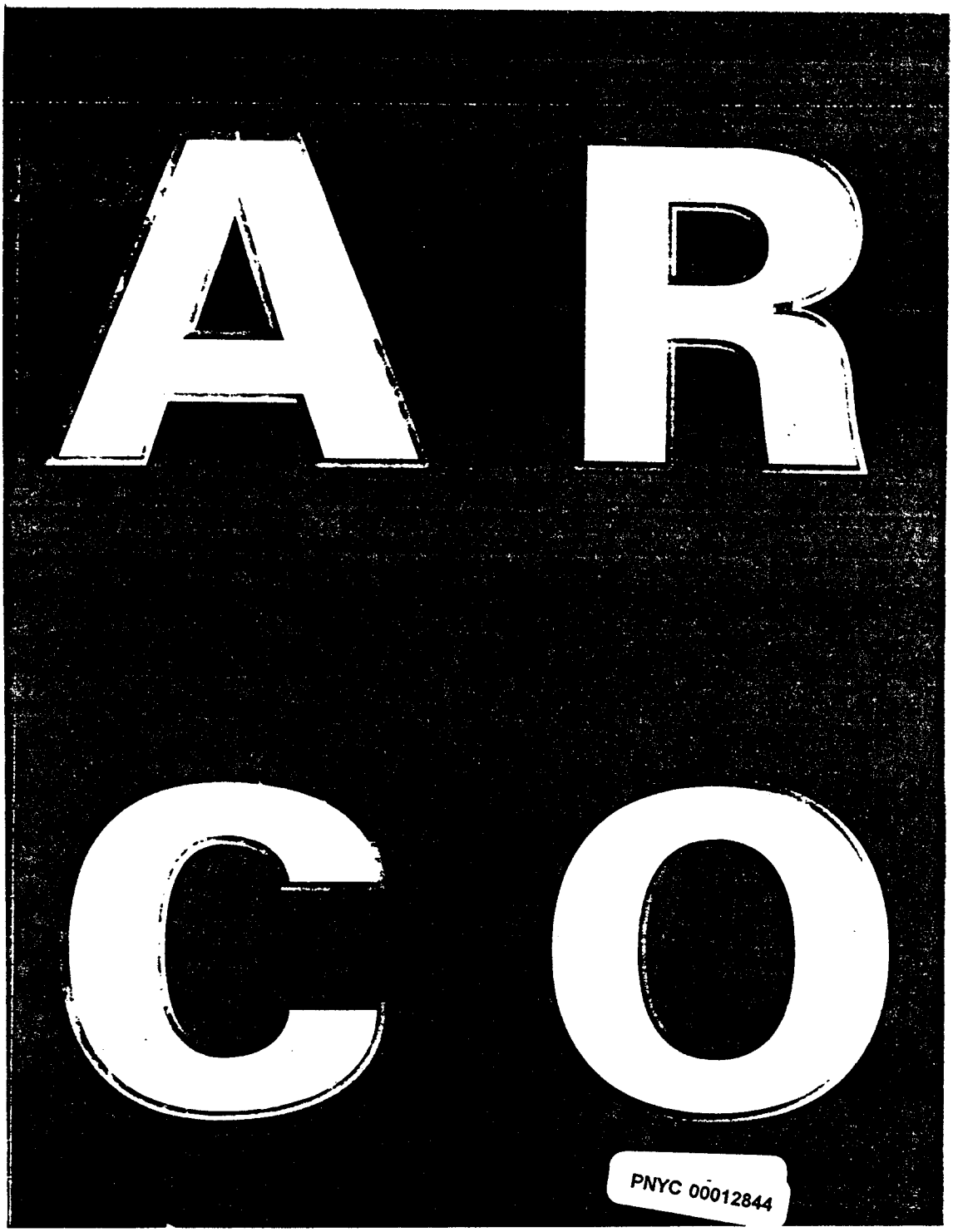
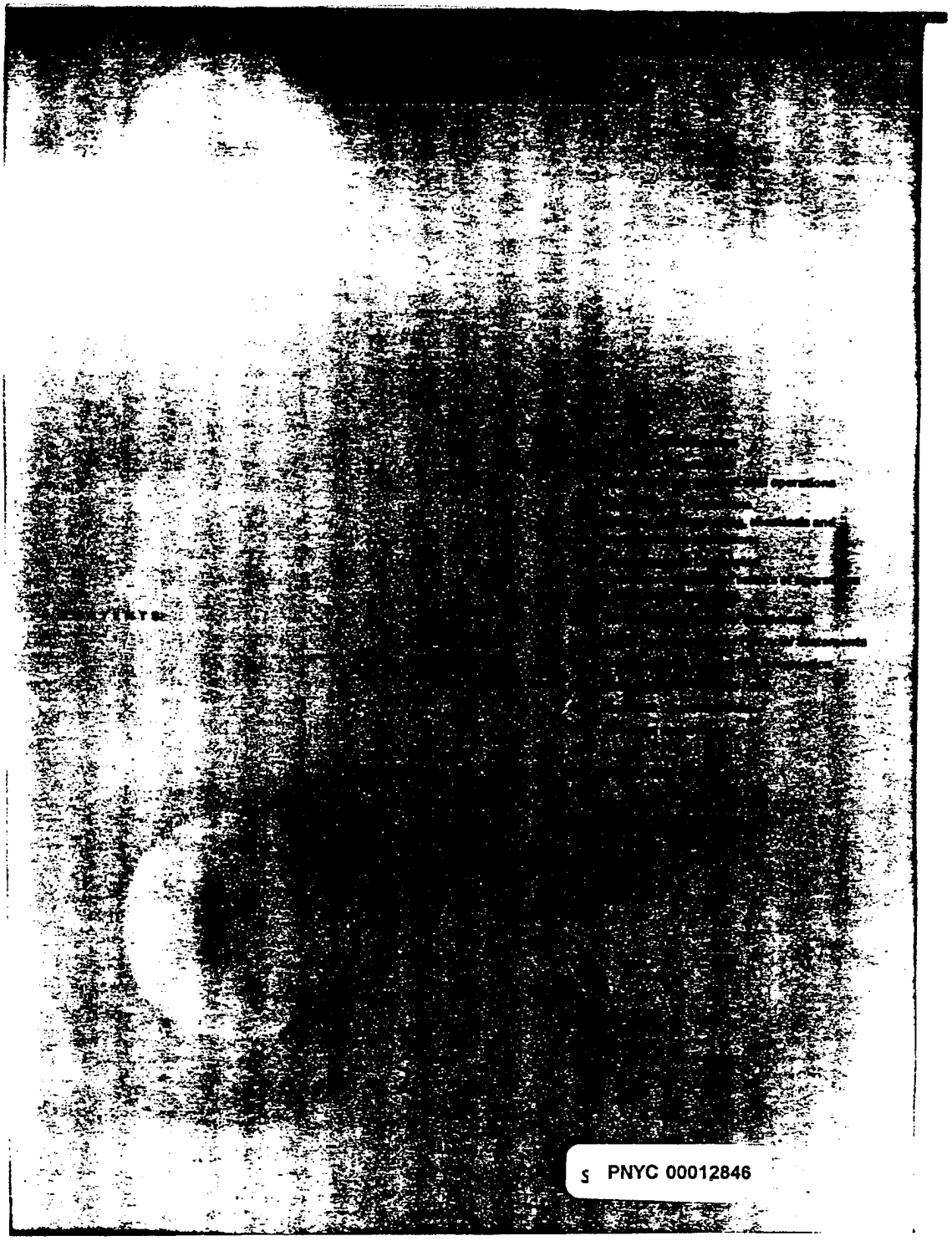

ARCO
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ARCO, the Atlantic Richfield Company, is a worldwide, integrated hydrocarbons corporation with operations and subsidiaries encompassing all aspects of the oil and gas business: exploration, production and marketing of crude oil, natural gas and natural gas liquids, and refining, marketing and transportation of petroleum products. ARCO also mines and markets coal and has interests in two petrochemical companies. Its earliest predecessor, The Atlantic Refining Company, was founded on July 1, 1866.



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HIGHLIGHTS

Millions, except per share amounts	1994	1993	1992
FINANCIAL			
Total revenues	$17,199	$19,183	$19,248
Net income before accounting changes	$ 919	$ 269	$ 1,193
Net income	$ 919	$ 269	$ 801
Net income per share	$ 5.63	$ 1.66	$ 4.96
Dividends	$ 885	$ 879	$ 873
Dividends per share of common stock	$ 5.50	$ 5.50	$ 5.50
Additions to fixed assets	$ 1,658	$ 2,070	$ 2,278
Total assets	$24,563	$23,894	$24,256
Return on stockholders' equity*	14.8%	4.2%	17.6%
Return on capital employed*	9.4%	5.1%	11.4%
RESERVES			
Petroleum liquids — million barrels:			
U.S.	2,246	2,259	2,517
International	222	206	211
Natural gas — billion cubic feet:			
U.S.	4,615	4,725	5,185
International	3,493	3,280	3,117
Coal — million tons recoverable:			
U.S.	1,279	1,296	1,236
International	227	214	232
OPERATIONS			
Oil and Gas production — net			
Liquids — barrels per day:			
U.S.	591,300	604,700	660,500
International	72,800	79,700	77,700
Natural gas — million cubic feet per day:			
U.S.	960	911	1,202
International	511	321	240
Coal shipments — thousand tons:			
U.S.	38,322	37,499	30,634
International	11,235	10,246	9,158
Refining and Marketing — barrels per day:			
Refinery crude runs	408,300	425,800	425,100
Petroleum product sales (U.S.)	477,900	481,500	479,500
Chemical sales — millions of pounds:			
Propylene oxide and derivatives	3,699	3,356	3,055
Styrene monomer and derivatives	2,496	2,084	1,434

*Calculated based on net income before accounting changes

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[redacted]

1994 was a strong year for ARCO. Financial results improved in spite of lower crude oil prices, lower natural gas prices and a weaker U.S. West Coast refining and marketing environment. At the same time, ARCO's chemical interests had improved earnings as a result of a stronger U.S. economy.

Net earnings for 1994 totaled $919 million, or $5.63 per share, which included an after-tax net gain from special items of $40 million. In 1993, we had earnings of $269 million, or $1.66 per share, after taking net special items charges of $545 million.

These results show that ARCO is beginning to reap the benefits of a lower overall cost structure and the changes we have made in our approach to doing business.

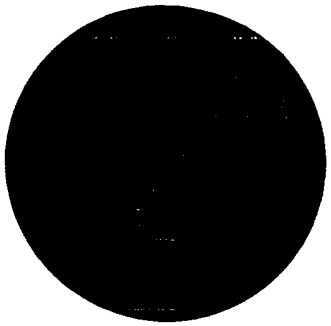
Restructuring has been an important part of the transition that ARCO has undergone in the past two years. While some of the benefits are yet to be realized in hard numbers, we can report savings in 1994 of $250 million after tax. We expect the savings will grow to $400 million annually as the full impact of reduced staffing levels and other changes is realized by 1996.

Although 1994 was a tough year in terms of challenging operating conditions and hard decisions, ARCO made important progress. Let us review some of the major accomplishments:

1994 ACCOMPLISHMENTS

- Our cost structure was lowered and capital spending plans were adjusted to improve cash flow and profitability, even in the lower price environment. This was achieved without sacrificing growth.
- Our U.S. natural gas company, Vastar Resources, Inc., completed an offering of 17 million shares of its common stock, which raised $480 million in the public capital markets. This was the last major step in the restructuring of ARCO's Lower 48 oil and gas operations which we started in 1993. Vastar is one of four discrete and self-supporting business units that we created to lower the cost of these operations and make them more competitive. Today, Vastar's cost structure is competitive with the most efficient "independents" in the oil and gas business.
- Significant advances were made in several major long-term projects which promise benefits for many years:
  - The Pagerungan and the Offshore Northwest Java Sea gas fields in Indonesia each completed their first full year of operation, as did the Orwell and Murdoch fields in the United Kingdom North Sea.
  - We completed the fabrication, sealift

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and installation of the second phase of the large-scale Gas Handling Expansion (GHX-2) at Prudhoe Bay on the North Slope of Alaska on schedule and under budget.

• Substantial progress was made in the construction and development of our first natural gas field in the South China Sea, where we expect to start production by early 1996.

• We completed the Los Angeles refinery modifications necessary to meet federal Clean Air Act requirements for gasoline and stationary emissions on schedule and under budget. At the same time, we introduced a new mid-grade gasoline to improve our product mix. We are also on track to meet the more demanding California gasoline specifications in 1996.

• The Gordonstone mine completed its first full year of operation, achieving a production level that establishes it as Australia's largest underground mine.

✔ Plans for upstream projects with substantial promise of future growth made progress:

• ARCO plans a large-scale enhanced oil recovery project at the Kuparuk River field on the North Slope of Alaska. This added 80 million barrels of reserves in 1994 and is expected to enhance production by 1997.

• In Ecuador, we submitted a development plan for our Villano oil field in the Oriente Basin and have added 75 million barrels of oil reserves for this field.

• A preliminary agreement to develop additional reserves in the Rhourde El Baguel field in Algeria was reached. Work on the final agreement is continuing in 1995. This project would use ARCO's special expertise in enhancing oil recovery by using miscible gas injection and could add nearly 250 million barrels of reserves over the project's life.

• We acquired operatorship and a 27.5% interest in an exploration and production sharing contract for part of the Qatar North Gas Field, among the world's largest. Discussions on development of the field and transportation facilities are underway while markets for the gas are being explored.

✔ During 1994, we added a total of 365 million barrels of oil equivalent reserves, replacing 106% of our 1994 oil and gas production.

✔ ARCO made an important overseas refining investment in 1994 by acquiring a 9.9% interest in China's Zhenhai Refining and Chemical Company Limited, which is south of Shanghai in the port of Ningbo. Additionally, we are studying coal mining and power generation ventures in China.

✔ ARCO Chemical Company entered into a long-term arrangement to market Rhone-Poulenc's production of toluene di-isocyanate (TDI), a key ingredient in polyurethanes.

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In early 1995, our transportation operation formed a partnership with another oil company that will provide significant pipeline capacity to meet increasing market demand for transporting offshore crude oil from the Gulf of Mexico to the midcontinent area. We expect this venture to be fully operational by early 1996.

For the longer term, we are looking at a range of projects which are outside of our core businesses, including those that would use our large gas resources, such as power generation in China and Indonesia. We are also studying a potentially major oil production and upgrading project in Venezuela.

FIVE KEY GOALS

The 1994 accomplishments represent important steps toward five key goals that we share at ARCO. These goals were reflected in every action we took in 1994 and those we will pursue in 1995 and beyond:

1. Return ARCO to a leading position among its peers in Total Return to Stockholders. Our 1994 total return to stockholders was 2.0%. This compared with the Standard & Poor's industry index, which was 1.3%, while our peer group average was 6.1%. We took action in 1994 that will begin restoring ARCO to a leading position within the industry.

2. Provide a solid, long-term future for the company through a portfolio of projects that offer increased earnings potential.

Upstream, we will continue to access new reserves at economic rates of return through a balanced program that includes exploration, development or redevelopment projects, and acquisitions, particularly those near existing operations.

Downstream, we are investing to capitalize on our leadership position in West Coast refining and marketing. The changing product composition requirements present new opportunities for us to enhance our high volume/low cost, high quality/low price position. ARCO Chemical will continue to invest in and expand its core businesses, allowing it to maintain its world leadership position.

3. Continue the transformation of ARCO from a predominantly domestic company to a global company.

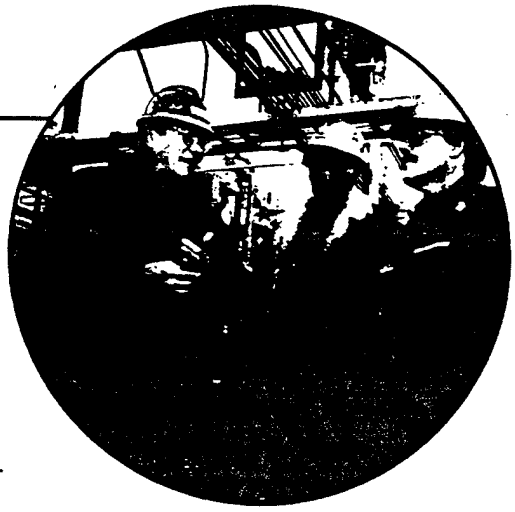
- Overseas revenues from all of our international upstream operations grew by 5% in 1994. We expect these revenues to continue growing and become a larger contributor to our operations.
- In addition to our upstream oil, gas and coal projects overseas, we expect strong growth from downstream projects, including chemicals, refining and marketing.

4. Develop and motivate a world-class work force.

- We recognize a *world-class* work force is a *world-class* asset and critical to our success.

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Mike Bowlin, left, talks with Crane Gas Plant Mechanic Carl Millam and Supervisor Alton Callihan during a visit to the West Texas natural gas processing facility. A positive example of ongoing attention to worker safety, the ARCO Permian plant has achieved more than 800,000 hours, or 18 years, worked without any lost time injuries.



• ARCO has a rich tradition in this regard; with the restructure behind us, we can reassert the importance of our people in light of a different competitive environment.

5. Maintain ARCO's traditional core values in terms of corporate citizenship, business ethics, and environment, health and safety.

• ARCO and its employees are widely recognized as excellent corporate citizens. In 1994, for one example, ARCO's Gordon Galloway received the China Friendship Award, by which the People's Republic of China recognized his (and ARCO's) contributions to both the social and economic improvement of its people. Gordon is president of ARCO China, Inc., which is developing that nation's first offshore natural gas field.

• ARCO's people use sensitive and innovative approaches to doing their jobs more effectively. In 1994, we received national recognition for the only environmental award among 10 "Innovations in State and Local Government" awards, given jointly by the Ford Foundation and Harvard's John F. Kennedy School of Government. This award came two years after an ARCO oil field became the 6,000-acre Coles Levee Ecosystem Preserve in a unique partnership between the California Fish and Game Department and ARCO Western Energy. ARCO continues to produce from the field while managing the preserve and earning land use credits for other projects.

SUBSTANTIAL CAPITAL COMMITMENT

To achieve these goals, we will commit substantial capital annually and maintain flexibility for "opportunity" projects. For 1995, we have budgeted $1.9 billion, of which $1.2 billion will be devoted to upstream projects and exploration. In 1994, we spent $1.65 billion on capital projects with $1 billion spent on upstream activities.

We believe ARCO is in a very strong position, with a new lower cost structure, a growing production profile and a portfolio of promising projects. We are looking forward to a positive future.

Lodwrick M. Cook
Chairman of the Board

Mike R. Bowlin
President, Chief Executive Officer and
Chief Operating Officer

February 27, 1995

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