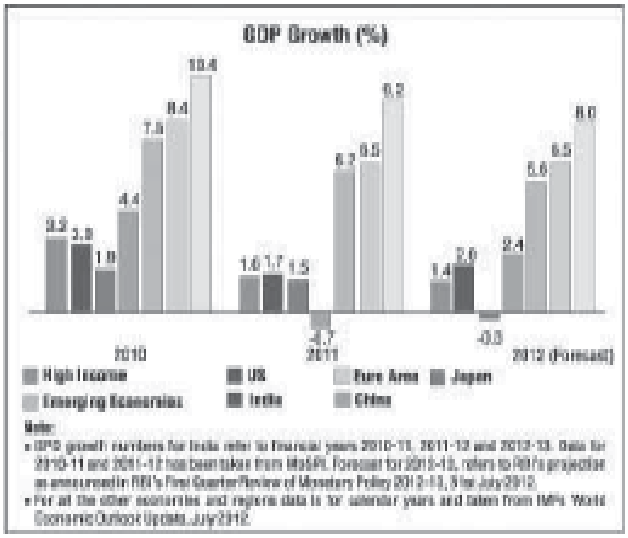
MANAGEMENT'S DISCUSSION & ANALYSIS

(Forming part of the Directors' Report for the year ended 31st March 2012)

ECONOMIC OVERVIEW & OUTLOOK

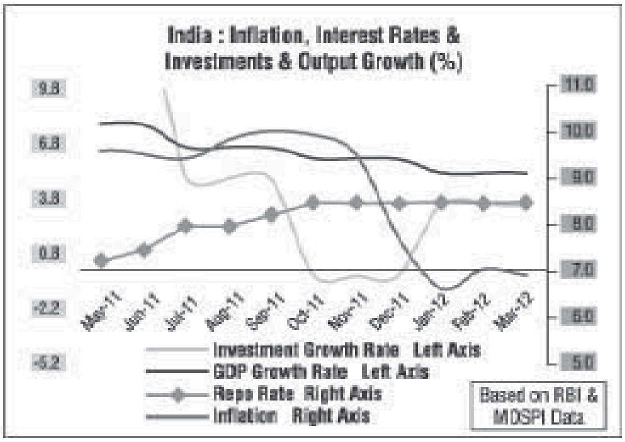
The overall economic environment was challenging as the intensification of sovereign debt crisis in the European Union (EU) and slowing of growth in the emerging economies undermined the global growth prospects.



During the year, global economy was hit by the deterioration of the sovereign debt conditions in Europe and the turbulence in the oil market. In particular, it was the European Union (EU) region, which experienced significant weakening of economic activity, with a fall in output in the last quarter of 2011. The emerging economies, which had been leading the recovery, also experienced deceleration in growth. As of now the overall economic environment continues to be fragile.

Indian economy confronted a mix of challenges emanating both from the domestic and external fronts resulting in slowing down of growth.

While India continues to be among the fastest growing economies, there was a marked slowdown in its growth momentum. In 2011-12 India's GDP growth rate slowed down to 6.5 per cent from 8.4 per cent in 2010-11.



For the Indian economy, both external and domestic channels worked adversely. Lower external demand and the slump in capital flows emanating from the weak global financial conditions resulted in the widening of the economy's current account deficit and depreciation of Rupee vis-à-vis the US Dollar. Forex reserves took a more than US$10 bn hit, falling from US$ 305 bn at the beginning of 2011-12 to US$ 294.4 bn at the end of it.

On the domestic front, the persistence of the high inflation rate and the tight monetary stance to curb inflation had a dampening impact on demand, especially the investment demand. Sectorally, it was the industrial sector, especially the manufacturing sector that experienced a slowdown in the growth momentum. The deteriorating fiscal situation during the year due to overshooting of the subsidies leading to a higher deficit than the target fixed by the Government also added to the dampening of investments in the country.

Looking ahead, how effectively India tackles its twin (Current Account & Fiscal) deficit problem will be critical to the macroeconomic stability and growth of the economy.

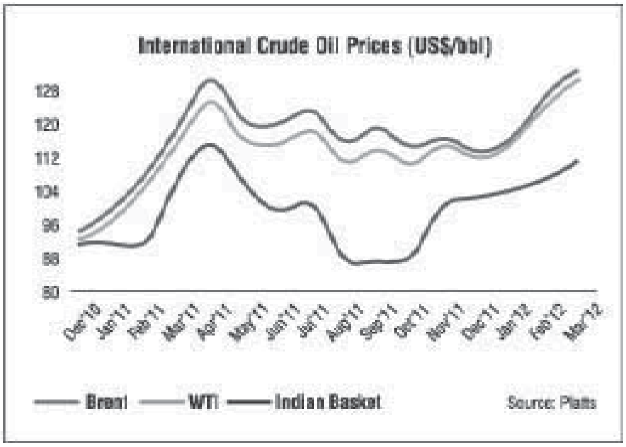
INDUSTRY STRUCTURE & DEVELOPMENTS

Energy Scene

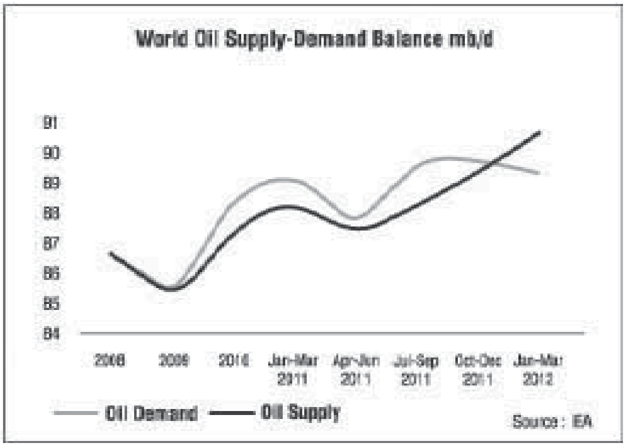
During 2011, global energy consumption grew by 2.5 per cent, decelerating from 5.1 per cent recorded in 2010 on account of weakened economic activity. On the supply side, disruptions in oil supply and high crude oil prices on one hand constrained the market, while high growth in production of natural gas in North America contributed to buoyancy in the energy supplies. Emerging economies continued to account for all of the net growth in energy consumption, while demand in the advanced economies fell for the third time in the last four years. Fossil fuels dominate the global energy mix and within the fossil fuels group it is oil with overall share of 33 per cent in the energy basket that dominates as world's largest energy source. Renewable energy's share in the global energy is small at about 2 per cent, but the sector is expected to continue growing at high rates through the long term.

Oil Market-International

With geo-political tensions rocking the oil market, prices were on an ascent despite slowing growth in demand.

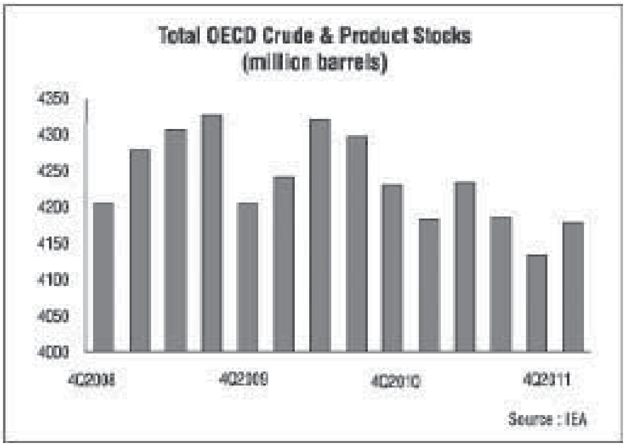


Prices: The year 2011-12 began with Brent above the US$120/bbl mark. Moderation was witnessed in crude oil prices during the year. However, by January 2012, prices again started rising steeply, resulting in Brent prices above US$ 120/bbl at the end of the year. Consequently, the average price of Brent in 2011-12 remained high at US$115/bbl as compared to US$87/bbl in 2010-11.



Supply-Demand Balance: It was the supply-demand mismatch witnessed during the year that, among other things, manifested in the high crude oil prices. Crude oil production rose marginally to 88.4 mb/d in 2011 from 87.3 mb/d in 2010. While oil demand growth was weak, it rose to 89.1 mb/d in 2011 from 88.3 mb/d in 2010. With growth rate plummeting to 0.9 per cent in 2011 from 3.2 per cent in 2010, production still fell short of demand.

Stocks: The draw down on the stocks including drawdown in government held stocks in countries belonging to the Organization for Economic Cooperation and Development (OECD) last summer, resulted in lowering of OECD stocks at the end of 2011 to an all time low since 2008.



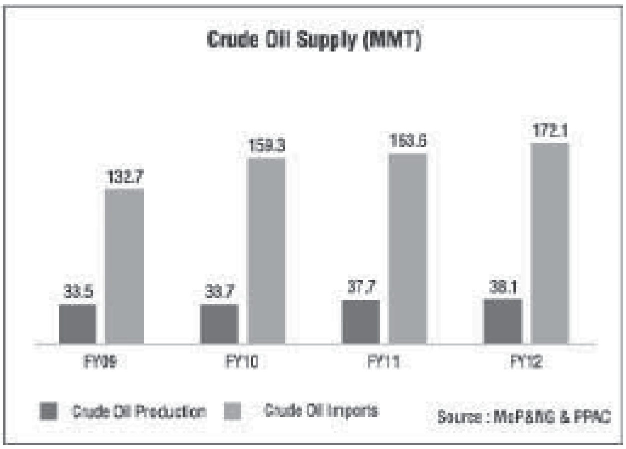
Geo-Politics: During the year, the spread of the 'Arab Spring' -wave of protests against the political establishment in the hydrocarbon rich Middle East and North Africa (MENA) region and the resultant potential & actual supply outages that rocked the oil market increased uncertainties and added pressure on price. Further, the imposition of sanctions on Iran by the US and EU and Iran's retaliatory indications of blocking the Strait of Hormuz increased supply-side fragility.

Oil Market-Domestic

The Indian market witnessed strong demand growth despite weakening economic activity. Deceleration in domestic crude oil production, rising international crude oil prices, depreciating Rupee and continuation of price control on major products to insulate consumers from the full impact of high International crude prices affected the financials of the sector.

Crude Oil Production: Domestic crude production witnessed marginal increase during the year. After growing at 11.9 per cent in 2010-11, crude oil production rose by meagre 1 per cent during 2011-12.

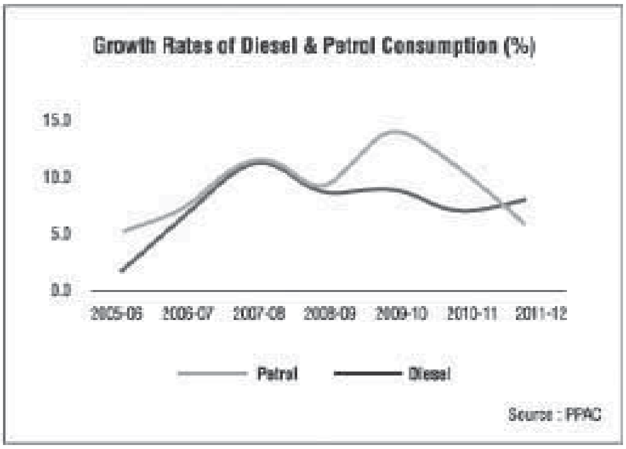
Crude Oil Imports: During the year, India imported around 172 MMT of crude oil representing a rise of 5.2 per cent from the previous year. In value terms, the rise was much more dramatic; India imported crude oil worth US$ 141.1 bn as against the value of US$100.1 bn in 2010-11.



Refineries Throughput: Indian Refineries recorded a throughput growth of 3.7 per cent. During the year, the sector's refining capacity expanded by around 20 MMTPA, making the total installed capacity reach the level of 213.2 MMTPA.

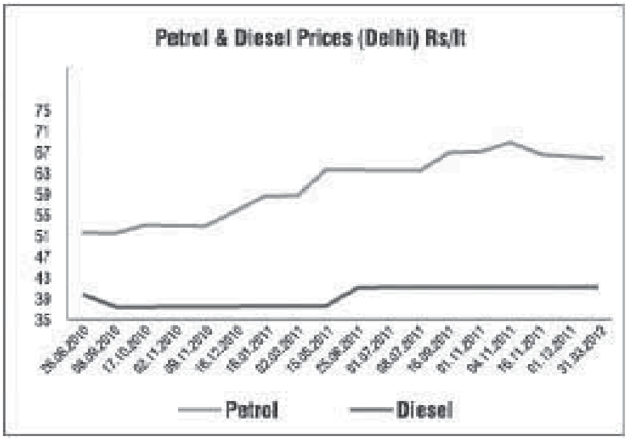
Product Consumption:

Petroleum products consumption (inclusive of imports) growth accelerated to 4.9 per cent from 2.3 per cent in the previous year. Transportation fuels were the front runners, with diesel growth outpacing petrol growth thereby breaking the trend of former trailing the latter. Consequent upon deregulation of MS and the rising crude oil prices, price differential between the two major transportation fuels widened significantly. Further, over the years the proportion of diesel



passenger cars has increased and this trend is expected to continue, reinforced by the fuel price differentials. In addition, the widening power requirement-availability gap in the country also explains a sizeable chunk of the growth in diesel consumption used for running power gensets.

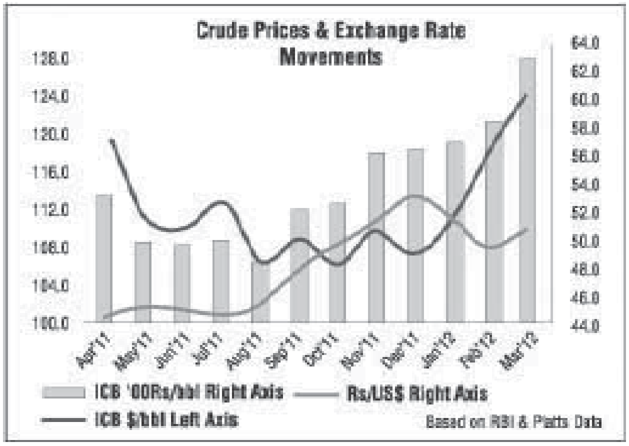
Product Imports & Exports: During the year, product imports fell to 14.9 MMT from 17.4 MMT in 2010-11, in value terms product imports fell to US$10.2 bn from US$ 12.1bn. Since 2001-02, India has been a net exporter of petroleum products. During the year, India exported 60.5 MMT as compared to 59.1 MMT of refined products with foreign exchange contribution of US$ 58.2 bn.



Financials:

For the downstream oil sector, while the physical production numbers were upbeat, the financials turned adverse.

On the cost side, the Oil Marketing Companies (OMCs) had to bear the double burden of rising international crude oil prices and sharp Rupee depreciation. Overall during 2011-12, Rupee depreciated from ₹ 44.60/ US$ on 31.03.2011 to ₹ 50.88/ US$ on 30.03.2012. Rupee experienced a sharp depreciation against the US Dollar between July-December 2011, while the international crude oil prices were sobering from their July peaks, thereby offset the prospects of easing of cost pressures. Between January-February 2012, the Rupee appreciated while international crude prices firmed up.



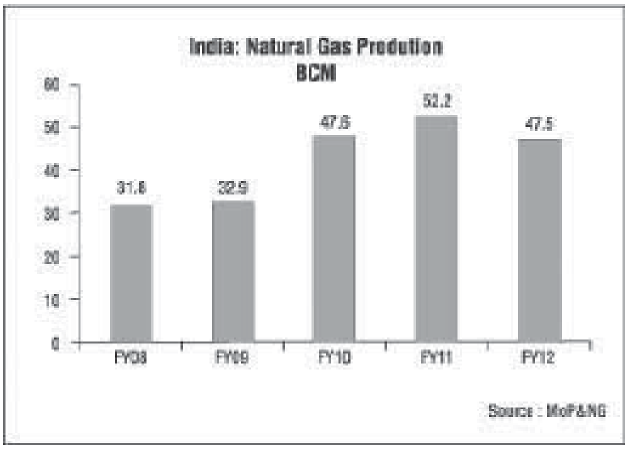
Natural Gas Sector

The Shale gas revolution in US has considerably enhanced gas supply prospects across the globe. While the global natural gas market was upbeat with scaling up of production, the domestic Indian market confronted issues such as dwindling domestic production from a large newly developed gas field and pricing dilemmas.

The dynamics of natural gas sector have changed significantly with the wave of shale gas in the US. During 2011, total marketed production of natural gas in the US grew by an estimated 7.9 per cent, registering the largest year-over-year volumetric increase in the history of US gas production. Henry Hub prices fell by 9 per cent from an average US$4.39/million Btu in 2010 to US$4.01/ million Btu in 2011.

In India, however, production from the country's gas bounty- KG Basin fell below the projections. During 2011-12, total natural gas production fell by 8.9 per cent on year-on-year basis, declining to 47.5 bcm from 52.2 bcm in 2010-11.

The improving global gas supply, however allowed the importing countries to access increased supplies of gas. In 2011, India emerged as Asia's third largest LNG buyer, with spot cargoes driving the market. The sector is set to witness sizeable investments in development of LNG import infrastructure. Development of domestic gas pipeline infrastructure both cross-country & city gas distribution is in full vigour in the country.



Key Policy Issues in Oil & Gas Sector

Direct Cash Transfers: The extant Government policy of subsidization of petroleum products continues to be major area of concern not only from the point of view of sustainability of the sector but also for the macroeconomic stability of the economy. The growing petroleum subsidy bill has contributed to the widening of fiscal deficit. Subsidization not only promotes excessive and inefficient consumption patterns, but also leads to the growing oil import bill of the country. Oil imports account for more than a third of India's total import bill and are a major reason behind the widened current account deficit, with which the country is grappling. Need for reform is paramount and while there is a growing appreciation of this fact concrete actions have yet to take shape. The Aadhaar-Unique Identification (UID) Scheme is being considered by the Government to provide the basic enabling fabric for rationalization of subsidization by moving from indirect subsidies to direct cash transfers to target beneficiaries.

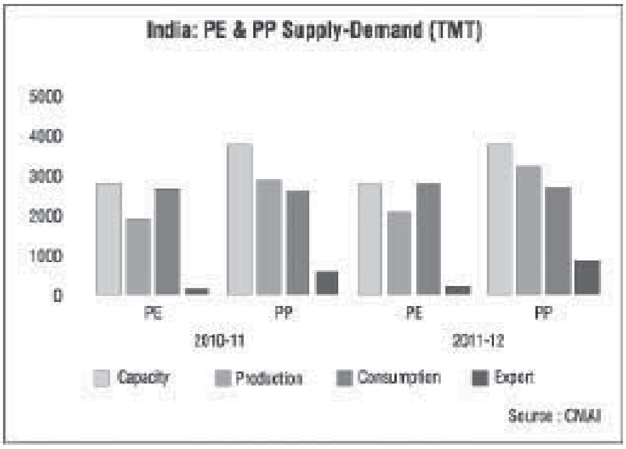
Auto Fuel Policy: The Government through the Auto Fuel Policy of 2003 had laid down the roadmap for implementation of environmentally compliant fuels.

In 2010, 13 cities went on BS IV petrol & diesel and the rest of the country on BS III. The Government plans to introduce BS IV fuels in 50 more cities by 2015. In line with that, during the year, OMCs added 7 more cities to the BS IV group with introduction of BS IV fuels.

Natural Gas Pricing: The natural gas pricing policy is also one of the vexed issues to which an answer is to be found to enable balanced and diversified investments. One of the issues debated was whether price pooling would serve the purpose. However, during the year the Inter Ministerial Committee set up by the Government on Policy for Pooling of Natural Gas Prices and Pool Operating Guidelines did not recommend pooling mechanism for natural gas at the overall level or on sectoral basis. The subject of appropriate natural gas pricing policy, therefore still hinges in various debates but perhaps time to decide on the same is running out.

Petrochemicals Sector

During the year, global petrochemicals sector was affected by high feedstock prices and slower growth in demand. Global Polyolefin's demand grew by 5 per cent in 2011-12 compared to 8.4 per cent the previous year. China continues to be the biggest consumer of Polyolefin products (about 40 per cent of global demand) and Middle East is the major supplier.



In the Indian Market, during 2011-12, the production of Poly Ethylene (PE) & Poly-Propylene (PP) grew by 7 per cent and 12 per cent while demand grew by 5.1 per cent and 2.9 per cent respectively thereby leading to increased exports. As a result petrochemical products registered a growth of 47 per cent during the year.

Sizeable capacity addition is lined up for the sector over the next few years. The high demand potential, given the low per capita petrochemicals consumption in India relative to other countries, even in the BRIC group is the driving force behind these investments.

OPPORTUNITIES AND CHALLENGES

India's long term growth prospects make the Indian market a front-runner of energy demand. At present, India's per capita energy consumption at 560 kgoe is less than a third of the world average of 1788 kgoe. With the rising growth, the per capita consumption levels have also to move up and in that context the wide difference between Indian and world average per capita consumption highlights the potential of the Indian Energy Sector. The Corporation being a major energy supplier in India, therefore finds itself placed in a very opportune position, filled with promising prospects of growth and innovation. Corporation's long-term vision of being the 'Energy of India' is based on this principal feature of the Indian market.

Core Business

Vehicular growth, urbanization, industrialization and the rising population of people with purchasing power, among other things will continue to drive the demand for refined petroleum products in the country, which augurs well for the Corporation as a leader in the downstream oil sector filled with ample growth opportunities.

Refining

Capacity Expansion: The Corporation has been scaling up its refinery capacity over the years. It is currently constructing a major green-field refinery project in Paradip.

Alignment to Demand Pattern: Besides, capacity augmentation, investments are required to be made for matching the changing demand patterns, compliance to tighter regulations and for optimization and maximization of margins. Across the globe the demand pattern is shifting towards middle distillates. In India also with the rising per capita vehicle ownership, transportation fuels and middle distillates are likely to account for the bulk of the demand growth and this calls for investments in aligning the Corporation's product mix with the changing demand pattern.

Gross Refinery Margins: Imported crude oil forms a major raw material for the Corporation's refineries. The Corporation has been working towards diversification of its crude basket and in the process sourcing heavier and opportunity crudes with a view to improve margins. Efforts are also on to upgrade the bottom of the barrel by introducing new residue upgradation technologies viz. by setting up of Hydrocrackers, Delayed Cokers and revamping of Resid Fluid Catalytic Cracker (RFCCs) etc. Another thrust area is reduction in energy consumption and operating cost in our refineries and other locations. It is noteworthy that there has been sustained improvement in the energy conservation management at refineries.

Marketing & Distribution

Expanding marketing and distribution network is one of the pillars of success in keeping the Corporation's market leadership. Sizeable investments are called for expanding the marketing & distribution infrastructure. Pipelines, as a means of transportation, standout as the cheapest and the most environmentally benign mode of supplying the product. Plans are afoot to connect more and more primary distribution points viz. depots and terminals through pipelines from supply sources.

The Corporation places strong emphasis on supply of quality products and ensuring customer satisfaction by improving its delivery of not only quality products but also quality services. In this pursuit, it is the Corporation's endeavour to automate entire distribution chain and terminal/depot facilities. Simultaneously through supply chain optimization, efforts for making infrastructure development efficient & effective are a priority area for the Corporation.

Within the domestic demand segment, the rural segment is one which presents significant growth opportunities. The renewed thrust of the Government towards the basic energy needs of the Below Poverty Line (BPL) families through focused schemes such as Rajiv Gandhi Gramin LPG Vitaran Yojana (RGGLVY) is unleashing the potential of this sector. As per the Government's "Vision-2015"adopted for the LPG sector, target of overall 75% LPG population coverage has been fixed. However to ensure that growth of LPG usage is evenly spread, Oil Marketing Companies are opening distributorships under RGGLVY in rural/low potential areas in all States/Union Territories so as to achieve target growth of at least 50% LPG population coverage in each district and at least 60% overall LPG coverage in each State by 2015.

Business Integration

Beyond its core business, the Corporation has been straddling across the energy value chain in line with its vision. The Corporation's endeavour is to emerge as an integrated energy company providing clean and sustainable energy solutions to its customers.

Petrochemicals

IndianOil has become a major player in the field of Petrochemicals & Polymers within a short span of few years. It stands as a testimony to the technical and marketing prowess of IndianOil. With the coming on stream of the Naphtha Cracker unit in Panipat and entry of IndianOil in the polymers market, IndianOil's petrochemicals product-market matrix has expanded manifolds. As a long-term strategy IndianOil is committed to deliver high-end petrochemical products. In the immediate future, challenge is to achieve consistent stabilized operations in our Naphtha Cracker Unit and strike the balance between volume growth and margin retention.

Gas

The Corporation's gas business has been growing steadily. With the increase in the availability of sourcing avenues in the last few years, and the growing demand for gas, the growth opportunities for the Corporation's gas business have increased manifold. Empowered by its vast experience of constructing and maintaining oil pipelines, the Corporation has made initial forays in the development of cross country gas pipelines in partnership with other State/ Central entities.

Exploration & Production

Today, the Corporation has a portfolio of 22 blocks. Discoveries have been made in three overseas and two domestic blocks. The success story of shale gas driven by the breakthroughs in hydraulic fracturing and horizontal drilling in the United States in the recent past has raised hopes across the world regarding the merit of exploring unconventional energy sources. The Corporation views unconventional oil & gas as an area of considerable prospects. To hone up its skills the Corporation is currently engaged in an exercise to enhance its capabilities in the upstream exploration and production area.

Alternative Energy Space

The Corporation's commitment to sustainable development and its vision of being the 'Energy of India' have motivated its initiatives into the renewable energy sources such as Bio-fuels, Wind, Solar & Nuclear Power. These newer businesses are set to witness high growth rates and open new vistas of providing sustainable energy solutions. Conducive policy framework is critical to the success of renewable energy ventures. In this context, the Government's National Action on Climate Change is expected to play the role of a key catalyst in making renewable energy investment attractive and rewarding. The Corporation's R&D Centre has set up a multi-feed fluidized bed gasification pilot plant with various analytical and characterisation facilities to give impetus to alternative energy research. For development of large scale photo catalytic process for hydrogen production, IndianOil's R&D Centre has entered into an MoU with Institute of Technology, BHU.

Research & Development

The Corporation places significant thrust on knowledge and research based growth. Especially, in the present scenario of high international crude oil prices and the price control in domestic market, where margins are under pressure, investment in proprietary research in lubricants, petrochemicals, catalyst, gas & refinery operations and product offerings is viewed as a thrust area for the Corporation. The Corporation appreciates the importance of R&D as a key competitive advantage driver for its new businesses, especially, petrochemicals and alternative energy and has been working in building a base for knowledge based growth in these areas.

RISKS & CONCERNS

As India's major player in the downstream petroleum industry, your Corporation faces some key risks from geo-political troubles, forex market fluctuations, hardening of interest rates and domestic pricing policies.

High Debt level: Corporation has to resort to borrowings from the market to bridge the gap arising out of incurrence of under-recoveries on sale of major products viz., HSD, LPG Domestic and SKO(PDS). The under-recovery on these products is a consequence of pricing policies of the Government under which these products are sold at a subsidized rate i.e. the gap between the price chargeable and the price actually charged. There is considerable time between incurrence of under-recoveries and cash compensation provided by Government which requires borrowing from the market for meeting the working capital requirement.

Besides above, prevalence of high crude oil and petroleum product prices requires additional borrowings to cover the increased working capital. Depreciation of the Rupee against USD also causes increase in amount of borrowings.

Geo-Politics: The escalation of geo-political tensions as witnessed during the year, not only adversely affects prices but also risks smooth supplies of crude oil.

Rupee Depreciation: The weakening of the Rupee against the Dollar during the year escalated crude oil costs. Exchange rate movements continue to be a serious area of concern for the Corporation given its high and growing import dependency.

Environment Clearances: Delay in receipt of Environment / Forest clearances for some of projects has been an area of concern that can result in cost and time overruns.

Entry Tax on Crude Oil in Uttar Pradesh: The Uttar Pradesh government's decision to impose a 5 per cent entry tax (with retrospective effect) on the crude oil supplied to the Corporation's Mathura Refinery is a serious area of concern for the Corporation. The burden of entry tax not only places considerable financial burden on the Corporation but also adversely affects the profitability of the refinery as well as of the Corporation.

High Domestic Inflation: In the context of high domestic inflation, passing of high international crude oil prices to the consumers becomes an area of risk. Should the inflation levels in the economy remain high it could act as a major deterrent to move to market determined petroleum product prices. The confluence of high domestic inflation and high international crude oil prices therefore poses considerable business challenge to the sector.

Safety & Security: For the Corporation's pan India refinery, marketing & pipeline infrastructure, safety and security is a priority concern at all times and at all locations. Given the hazardous nature of products handled, the Corporation is fully committed to compliance to all guidelines with respect to health, safety& environment.

FINANCIAL REVIEW

Turnover

The turnover of the Corporation (inclusive of excise duty) for the year 2011-12 was ₹ 4,09,957 crore as compared to ₹ 3,28,652 crore in the previous year. The total sales of products (including gas and petrochemicals) for 2011-12 was 75.66 MMT as against 72.92 MMT during 2010-11.

Profit Before Tax

The Corporation has earned a Profit Before Tax of ₹ 3,754 crore in 2011-12 as compared to ₹ 9,096 crore in 2010-11.

Provision for Taxation

An amount of (₹ 201) crore has been provided towards income tax for 2011-12 considering the applicable income tax rates as against ₹ 1,651 crore provided during 2010-11.

SEGMENTWISE PERFORMANCE

(₹ in Crore)

	Sale of Petroleum Products	Sale of Petrochemicals	Other Businesses	Eliminations	Total
External Revenue	3,82,966	11,174	40,369	-	4,34,509
Inter Segment Revenue	7,506	49	3,618	(11,173)	-
Total Revenue	**3,90,472**	**11,223**	**43,987**	**(11,173)**	**4,34,509**
Operating Profit	16,918	(210)	76	-	**16,784**

Notes:

A. Segment Revenue comprises Turnover (Net of Excise Duties), Subsidy & Grants received from Government of India and Other Operating Income.

B. Other Business segment of the Corporation comprises; Sale of Imported Crude Oil, Sale of Gas, Oil & Gas Exploration Activities, Explosives & Cryogenic Business and Wind Mill & Solar Power Generation.

Profit After Tax

The Corporation has earned a Profit After Tax of ₹ 3,955 crore during the current financial year as compared to ₹ 7,445 crore in 2010-11.

Depreciation & Amortisation

Depreciation for the year 2011-12 was ₹ 4,542 crore as against ₹ 4,567 crore for the year 2010-11.

Finance Cost

Finance Cost Net of Interest income of the Corporation for the current year was ₹ 3,801 crore as against ₹ 1,121 crore during 2010-11.

Borrowings

The borrowings of the Corporation were ₹ 75,447 crore as on March 31, 2012 as compared to ₹ 52,734 crore as on March 31, 2011. The Total Debt to Equity ratio as on 31st March, 2012 worked out to 1.30:1 as against 0.95:1 as on 31st March, 2011.

Capital Expenditure

Gross Fixed Assets (including Capital Works in Progress) increased from Rs.1,02,418 crore as on 31.03.2011 to Rs.1,12,890 crore as on 31.03.2012. In addition, capital advances for LSTK projects have also gone up from Rs.3,367 crore in 2010-11 to Rs.8,082 crore in 2011-12.

Investments

Investments as on 31st March, 2012 were ₹ 18,678 crore as compared to ₹ 19,545 crore as on 31st March, 2011. The decrease in investments during the year is mainly due to sale of Government of India Special Oil Bonds. The aggregate market value of quoted investments as on 31st March, 2012, i.e., investments made in ONGC Ltd., GAIL(India) Ltd., Oil India Ltd., Chennai Petroleum Corporation Ltd., Petronet LNG Ltd. and Lanka IOC Plc., is ₹ 23,238 crore (as against the acquisition price of ₹ 3,828 crore).

Earnings Per Share

Earnings Per Share works out to ₹ 16.29 for the current year as compared to ₹ 30.67 in the previous year.

Earnings in Foreign Currency

During the year, the Corporation earned ₹ 19,829 crore in foreign currency as against ₹ 16,968 crore in 2010-11, which is mainly on account of export of petroleum products.

INTERNAL CONTROL SYSTEMS

The Corporation has a well established internal control system, which is commensurate with the size and nature of its business. Detailed manuals have been prepared on various aspects of the business activities, accounting policies and guidelines. The Board of Directors regularly monitors the performance of your Corporation. The Corporation has a full-fledged independent Internal Audit Department headed by an Executive Director (below Board level), who reports to the Chairman. The Internal Audit Department has mix of officers from finance and technical functions. The audit assignments are carried out as per the Annual audit programs approved by the Chairman and Audit Committee. The Internal Audit carries out extensive audits round the year covering each and every aspect of business activity so as to ensure accuracy, reliability and consistency of records, systems and procedures. An Audit Committee comprising entirely of Independent Directors reviews the recommendations and observations of the Internal Audit Department regularly.

HUMAN RESOURCES / INDUSTRIAL RELATIONS

Human capital is at the core of the success of any organization. The Corporation acquires the best talent in the country from leading institutes and universities. It has been working towards nurturing and retaining talent. In view of the rising competition in the domestic market, acquiring and retaining manpower is a challenge. In our new business areas of Petrochemicals, Gas and E&P, getting the right talent is pivotal to the future of these ventures.

The industrial relations climate in the Corporation remained harmonious, peaceful and cordial during the year. Employees' Participation has been ensured through information sharing with employees regularly seeking their support, suggestions and co-operation. IndianOil continues to align its HR strategies with organisational strategies. The employee strength of IndianOil as on 31st March, 2012 was 34,233 including 14,851 officers.

Information regarding Corporate Social Responsibility, Environmental Protection & Conservation, Technological Conservation, Renewable Energy Developments, Foreign Exchange Conservation has been included in the Director's Report and Annexure thereto.

CAUTIONARY STATEMENT

Statements in the Management's Discussion & Analysis describing the Company's focal objectives, expectations or anticipations may be forward looking within the meaning of applicable securities, laws and regulations. Actual results may differ materially from the expectations. Important factors that could influence the Company's operations include global and domestic demand and supply conditions affecting selling prices of products, input availability and prices, changes in Government regulations/ tax laws, economic developments within the country and factors such as litigation and industrial relations.