FITCH AFFIRMS MOL AT 'BBB-'; OUTLOOK NEGATIVE

Fitch Ratings-Warsaw/London-01 July 2015: Fitch Ratings has affirmed MOL Hungarian Oil and Gas Company Plc's (MOL) Long-term Issuer Default Rating (IDR) at 'BBB-'. The Outlook is Negative. A full list of MOL's ratings is at the end of this commentary.

The Negative Outlook reflects pressures on the company's operations from the challenging upstream environment and uncertainties over management rights in its Croatian subsidiary INA - Industrija nafte d.d. (INA). The Outlook also takes into account potential risks associated with planned inorganic growth in the upstream segment, which may bring the leverage metrics above our guidance depending on the size and timing of possible transactions as well as their contribution to EBITDA.

MOL's ratings are supported by the company's vertical business integration with operations in upstream, refining, fuel retail and petrochemical segments, and by its relatively strong financial profile. MOL's funds from operations (FFO) adjusted net leverage increased to 2.3x in 2014 from 1.4x in 2013, and Fitch expects that it will remain within our rating guidance, i.e. below 2.5x on a sustained basis, despite MOL's capex and M&A plans.

KEY RATING DRIVERS
INA Uncertainty
Tensions between the Croatian government and MOL over the corporate governance structure of INA intensified in 2013, but so far with limited consequences for the financial profile and operations of both companies. INA accounted for 23% of MOL's consolidated EBITDA in 2014 and 36% of its hydrocarbon production. Fitch treats the potential loss of management control over INA arising from the conflict between the Croatian government and MOL as an event risk with probable negative credit implications. Pressure on MOL's ratings may also arise if INA's performance deteriorates further due to unfavourable regulatory changes imposed by the Croatian government.

Our base case scenario assumes the parties will be able to negotiate a settlement to the dispute. We consider an alternative scenario, where MOL sells its stake in INA and invests the proceeds to substitute lost revenue and EBITDA to be neutral for the ratings, but this would also depend on the credit profile of the acquired assets.

Upstream Decline Reversed, Challenges Remain
Over the past few years, MOL's oil and gas production has been falling, mainly due to a natural production decline in Hungary and Croatia, and withdrawal from Syria. In 2014, MOL's output amounted to 97.5 thousand barrels per day (mbpd), down 6% yoy and 32% lower than in 2010. The company's efforts to arrest the production decline paid off in 3Q14 when the negative production dynamics were reversed. In 1Q15 the company's upstream production stayed at 103.3mbpd, and we expect it will grow over the next few years as MOL's Kurdistan and North Sea production assets ramp up. The company's key challenges with regard to the upstream segment are relatively high capex, political risks in Kurdistan, significant breakeven production costs in the North Sea and high level of depletion of brownfields.

Kurdistan and North Sea
The unrest and political instability in Iraq have had a limited impact on MOL's operations in Kurdistan, unlike the decrease in oil prices in 2H14, which lowered profitability of production and complicated recovery of funds from the government of Kurdistan. MOL expects to ramp-up its oil and gas production from Shaikan and Akri-Bijeel fields to around 10mbpd in 2017. This may increase to 20mbpd if the company moves forward with plans to further develop its fields in Kurdistan. We believe that the volatile operating environment in Iraq coupled with depressed oil prices and delayed

payments to field operators from the government of Kurdistan pose risks to further growth of output from these assets.

North Sea is a challenging petroleum region with falling production, ageing infrastructure and relatively high production and development costs. It means that incremental production, including from the fields currently developed by MOL, will only be possible with significant capital investment. MOL entered the UK Continental Shelf through deals announced in 2014, and we believe that the profitability of these assets is contingent on Brent prices recovering to USD75-USD80/bbl.

Strong Downstream Performance
MOL's current cost of supply EBITDA increased 31% yoy to HUF205.2bn in 2014 due to favourable petrochemical and refining margins and good results of the retail segment. Downstream business continued to perform well in 1Q15 as petrochemical and refining margins and demand for fuels in Europe are strong.

We view positively MOL's downstream segment with its complex refining assets in Hungary and Slovakia integrated with petrochemical and retail operations. The company successfully completed a USD500m downstream improvement programme in 2014 and recently announced a new programme expected to bring USD500m of incremental EBITDA split into growth projects (USD150m, including mainly contribution from butadiene and LDPE4 units planned to be completed in 2015) and efficiency improvements. We believe MOL will be largely able to achieve the expected improvements. However, downstream segment results will continue to be reliant on European and global refining margin environment.

Favourable European Refining Environment
European refining margins started to recover in July 2014 after Brent began its fall from USD112/bbl. In 1Q15 the north-west European refining margin averaged USD7.6/bbl, up from USD4.1/bbl in 1Q14 and USD5.9/bbl in 4Q14. Healthy fuel demand in recent months exceeded market expectations and supported margins, though this was partly driven by temporary factors including opportunistic trading. Overcapacity and strong competition from refiners in oil producing countries may put pressure on European margins later this year.

Solid Financial Profile
MOL has shown the ability and willingness to maintain relatively conservative financial ratios through a reduction in capex in the face of operational headwinds. Funds from operations (FFO) adjusted net leverage totalled 2.3x in 2014, up from 1.4x in 2014. The increase was mainly a result of higher inorganic spending, but also depressed operating cash flows due to a negative inventory effect recorded by MOL's refining segment in 2H14 as oil prices dropped. This was a common feature for MOL's peers in 2H14 given the speed of oil decline. We expect that MOL's net leverage will remain within our rating guidance in 2015-2019.

Capex To Fall in 2015
The company had planned to increase capex by 70% in 2014-2016 compared with 2011-2013, with half of the total spending directed to the upstream segment. As oil prices declined in 2H2014, MOL reduced its 2015 capex guidance by 35% to USD1.5bn. We understand the ambitious capex plans are set to continue past 2015, provided oil prices start to recover. However, according to our base case scenario, MOL will still be able to maintain FFO net adjusted leverage below 2.5x over the rating horizon. Importantly, capex reduction in 2015 may also point to some flexibility in investment spending in case of worse than expected market conditions.

MOL also made several small to medium-size acquisitions in 2014 and YTD15 (upstream assets in the UK and Norwegian North Sea and a retail network from Eni SpA) and plans further M&A spending in the medium term. Exceptionally good refining and petrochemical segment environment in 1H15 coupled with planned capex reduction may give MOL the necessary headroom for M&A spending, while keeping leverage within our target range. However, financial flexibility is lower due to the fall in oil prices and an increase in leverage in 2014, which partly explains the Negative Outlook on MOL's ratings. According to our forecasts, acquisitions of up to USD0.5bn would allow MOL to maintain leverage within our guidance assuming also no contribution to EBITDA from acquired assets.

Exposure to Hungary
MOL's business demonstrates only limited exposure to Hungarian economy. Fitch believes that MOL's two main profit drivers - crude oil prices and crack spreads on refined products - are affected by global factors rather than the domestic economy. MOL's foreign currency ratings are higher than that of the Hungarian sovereign (BB+/Positive) but below Hungary's Country Ceiling of 'BBB.' In line with Fitch's criteria, 'Rating Non-Financial Corporates Above the Country Ceiling', if the company's standalone rating rises above 'BBB', its foreign currency IDR would be capped by the Country Ceiling.

Fitch revised Hungary's Outlook to Positive from Stable in May 2015 (see 'Fitch Revises Hungary's Outlook to Positive; Affirms at 'BB+'', dated 22 May 2015) citing an improvement in macroeconomic metrics. Although this has no direct impact on MOL's ratings, we view a stronger sovereign rating as positive for MOL as it reduces the risks of non-standard measures to be introduced by the government (e.g. special taxes), while GDP growth provides a good basis for an increase in fuel sales, which may benefit MOL's financial results.

KEY ASSUMPTIONS:
- Fitch oil price deck (USD55/bbl in 2015, USD65 in 2016, USD75 in 2017 and USD80 thereafter)
- Upstream production: 105mbpd in 2015 as guided by MOL; +5% yoy in 2016-17
- Strong European refining margins throughout 2015; downstream profitability in 2016 onwards supported by the company's improvement programme
- Capex around USD1.5bn in 2015; around USD1.9bn in 2016-17, USD1.5bn thereafter
- Dividends around USD150-200m in 2015-19

RATING SENSITIVITIES
Negative: Future developments that could, individually or collectively, lead to negative rating action include:
- FFO-adjusted net leverage above 2.5x on a through-the-cycle basis
- Large acquisition of non-producing upstream assets
- Upstream production significantly below Fitch's expectations (105mbpd in 2015; +5% yoy in 2016)
- Negative impact on MOL's financial profile from the dispute regarding its management rights in INA

Positive: Potential upside for the rating is limited by the company's Negative Outlook. Future developments that could, individually or collectively, lead to the Outlook being revised to Stable include:
- FFO-adjusted net leverage below 2.5x on a through-the-cycle basis
- Upstream production rising in line with Fitch's expectations
- Resolution of the INA dispute

LIQUIDITY AND DEBT STRUCTURE
Strong Liquidity
At end-March 2015, MOL had available liquidity comprising HUF149bn (USD534m) cash and USD3.0bn undrawn committed long-term facilities against debt maturing in one year of HUF480bn (USD1.7bn).

FULL LIST OF RATING ACTIONS
MOL Hungarian Oil and Gas Company plc:

Long-term foreign and local currency IDRs: affirmed at 'BBB-'; Outlook Negative
Short-term foreign and local currency IDRs: affirmed at 'F3'
Senior unsecured rating: affirmed at 'BBB-'

MOL Group Finance SA:
Senior unsecured rating: affirmed at 'BBB-'

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Additional information is available at www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

Applicable Criteria
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage (pub. 28 May 2014)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749393