Fitch Ratings

Corporates
Energy (Oil & Gas)
Russian Federation

PAO Novatek

Ratings

Rating Type	Rating	Outlook	Last Rating Action
Long-Term IDR	BBB	Stable	Affirmed 9 Jul 2020
Long-Term Local-Currency IDR	BBB	Stable	Affirmed 9 Jul 2020

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The rating reflects PAO Novatek's strong integrated business profile, enhanced operations after the full ramp-up of the company's transformational Yamal LNG (YLNG) project, strong cash flow generation and large low-cost reserve base. Novatek managed to keep low leverage through the cycle, despite substantial capex for the completion of its large-scale YLNG project.

Fitch Ratings expects leverage metrics will increase but remain within the rating guidance in the next four years, as investments in Arctic LNG 2 will be financed from the proceeds of the sale of a 40% stake in the project, an equity injection from partners and project finance.

Novatek is the largest independent gas producer in Russia with 820 thousand barrels of oil equivalent per day (kboe/d) of total hydrocarbon production (excluding joint ventures) with assets concentrated within the Russian Arctic Circle. The company's rating also takes into account its exposure to the operating environment in Russia.

Key Rating Drivers

LNG to Drive Growth: Novatek's YLNG project has enhanced its business profile and propelled the company from a niche Russian natural gas producer into a global liquefied natural gas (LNG) company with a 5% share of the global LNG market. Novatek has an ambitious target to increase its LNG production from 19 million tonnes (mt) to 40mt in 2026, with the start-up of all Arctic LNG 2 trains, before a further increase to 57mt-70mt by 2030 through additional LNG projects.

We believe Novatek's vast reserve base, with a proven reserves (1P) reserve life of 27.5 years, low lifting costs, expertise with launching YLNG and strategy towards LNG infrastructure, should support this target.

Arctic LNG-2 Progress: The final investment decision (FID) on Novatek's second LNG project with 19.8mt of capacity was taken in September 2019. Novatek has a 60% stake. Total SA (AA-/Stable), Novatek's minority shareholder, China National Petroleum Corporation (A+/Stable), China National Offshore Oil Corporation and the consortium of Mitsui & Co and Japan Oil, Gas and Metals National Corporation each acquired a 10% stake.

The launch of the three LNG trains is scheduled from late 2023 to 2026. We estimate capex of USD21.3 billion, which is more than 30% cheaper than YLNG on a per-tonne basis and achieved by placing the plant on gravity-based structures, and a higher degree of localisation. We estimate that the project is 19% complete to date.

Arctic LNG-2 Financing: The management views a 50%/50% debt/equity ratio as the most likely financing structure, equivalent to a maximum of around USD11 billion of project-finance debt. We conservatively assume a higher share of equity in our forecast as the final funding scheme is yet to be agreed.

We anticipate that Novatek's share of investments in the project will be predominantly covered by proceeds from the sale of 40% equity stakes to its partners. These proceeds include a cash consideration of around USD5.2 billion and have a contingent part that relates to train launches. Each project partner provides a long-term LNG offtake in proportion to its respective ownership interest.

Applicable Criteria

Corporate Rating Criteria (May 2020)

Corporates Notching and Recovery Ratings Criteria (October 2019)

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Future LNG Ventures: The next LNG project is a smaller Obskiy LNG project with two trains of 2.5mt capacity, which will be based on Novatek's in-house liquefaction technology similar to the fourth train of YLNG. Due to a supply glut we anticipate in the global gas market, Novatek is considering delaying the FID and commissioning of Obskiy LNG by one year to 2024. However, this should not affect its long-term target.

The company's future LNG projects will benefit from efforts to optimise logistics across the Northern Sea Route, as construction of LNG hubs in Kamchatka and Murmansk will reduce transportation expenses.

Uncertainty in Financial Profile: We expect that funds from operations (FFO) net leverage will remain comfortably below our guidance for a negative rating action in 2020-2023. The company's internal policy targets a net debt/EBITDA ratio of 1.0x on a through-the-cycle basis.

The pipeline of new LNG projects adds some uncertainty to the company's credit profile due to their potentially large scale, not-yet-finalised financial arrangements and medium-term pressure on the global gas market. Novatek has historically financed its project capex through the sale of stakes to partners. However, if the company decides to provide shareholder loans as bridge funding for future projects, this could have a temporary negative impact on its credit metrics. Novatek's intensified capex programme and increased dividend pay-out will lead to negative free cash flow (FCF) in the medium term.

Increased Capex: Novatek has significantly increased its investment in LNG-related projects and infrastructure, as well as in exploration and drilling aimed at stabilising its domestic production, since 2019. Its initial capex guidance in 2020 indicated a further increase. However, the company cut this figure by 20% to RUB200 billion due to pandemic-related challenges.

The updated capex is still higher than in 2019, primarily stemming from a large budget for LNG projects, while it has curtailed investment in oil production. We anticipate that capex will remain relatively high for at least the next three to four years.

YLNG is Resilient to Volatility: Despite low spot gas prices and subdued gas demand, we believe that the project's performance will be resilient due to a pricing mechanism in offtake contracts that cover 95% of sales and low-cost base. We assess YLNG's operational break-even natural gas price at around USD3/million British thermal units (MMBtu). This is above the current spot price but oil linkage in offtake contracts creates a higher-than-average sales price.

We therefore expect that YLNG will be able to service its bank debt with no support from Novatek, although cash flows to shareholders are likely to be lower than previously projected. The start-up of the fourth train, which will be purely priced on a spot basis, has been delayed until end-2020.

Although Novatek does not consolidate YLNG on its balance sheet and we also treat it on a deconsolidated basis, its financial profile will benefit from the repayment of shareholder loans and, later on, dividends. We expect that annual cash flows from YLNG to Novatek would exceed USD600 million under normal market conditions. In a hypothetical scenario when YLNG is proportionally consolidated into Novatek's financials, which is not our rating case, its FFO net leverage would be around 3x in the next three years, above the guidance for a negative rating action.

Natural Gas Production Stabilising: Novatek's natural gas production started to decline in 2016 as it began depleting some of its key producing fields. The commissioning of the North Russkoye cluster, which will produce 14 billion cubic metres (bcm) of gas at plateau, as well as small-scale acquisitions should help mitigate the production decline. We expect Novatek's natural gas production, including a share in associates but excluding YLNG, to remain above 60bcm in the medium term, compared with a peak of 68bcm in 2015. This should be sufficient to meet Novatek's domestic gas sales commitments.

Domestic sales of gas have historically provided lower profitability than the liquids business but stable revenue and cash flows.

LNG Challenges: The ramp-up of new LNG facilities, slowing Chinese demand growth and the warm winter of 2019-2020 in the Northern Hemisphere put LNG prices under pressure even before the pandemic. Lockdowns have exacerbated the imbalance between LNG supply and demand. Despite near-term challenges, we expect that LNG demand will grow considerably in the long term and its role in the global energy mix will continue to increase, particularly in the context of the low-carbon transition.

Moreover, many final investment decisions for new projects are being postponed in the current low price environment, potentially resulting in the market switching to a deficit after 2022-2023.

Sanctions Are Manageable: Novatek has been included on the Sectoral Sanctions List by the US Office of Foreign Asset Control, which prohibits US companies and banks from providing new finance of longer than 60 days to named companies and their subsidiaries. This has effectively barred Novatek from US capital markets and we believe it may make access to other western markets difficult. We estimate that the company should be able to repay its upcoming debt maturities largely from internally generated funds, or it could resort to domestic borrowings if needed.

State Supportive Towards the Arctic: Novatek's existing and potential projects, including YLNG and Arctic LNG 2, are aligned with Russia's strategic aspirations, such as the diversification of energy exports through LNG and the development of the Arctic territories. The government has provided substantial tax breaks to YLNG, helped to build infrastructure and partially funded the project through the National Welfare Fund.

The state will also fund infrastructure construction for Arctic LNG 2, which justifies our expectation that the state will continue supporting Novatek's other projects in the Arctic through tax incentives and infrastructure investments.

Fitch has chosen to affirm and withdraw Novatek's senior unsecured rating because Fitch no longer considers it relevant for Fitch's coverage.

Financial Summary

(RUBm)	Dec 2017	Dec 2018	Dec 2019	Dec 2020F	Dec 2021F	Dec 2022F
Gross revenue	583,186	831,758	862,803	648,953	720,506	818,146
Operating EBITDA (before income from associates)	198,326	258,920	250,788	147,854	186,608	207,846
FCF margin (%)	15.7	5.5	2.7	-23.8	-10.0	-1.2
FFO interest coverage (x)	17.1	25.6	31.1	17.8	16.5	13.3
FFO net leverage (x)	0.6	0.5	0.1	0.2	1.2	1.5

Source: Fitch Ratings, Fitch Solutions

Rating Derivation Relative to Peers

Novatek is Russia's major LNG and domestic natural gas producer with sizable exposure to liquids. Novatek's upstream production volumes in 2019 was 820 thousand barrels per day (kbpd) by subsidiaries and 1,556kbpd including equity affiliates and joint ventures. Its EBITDA in 2019 was USD2.3 billion.

This compares with the production levels of the following Russian oil majors in 2019 (all excluding equity affiliates): 1,359kbpd by PJSC Gazprom Neft (BBB/Stable); 2,318kbpd by PJSC Lukoil (BBB+/Stable), 598kbpd by PJSC Tatneft (BBB-/Stable); and 10,248kbpd by PJSC Gazprom (BBB/Stable, with an 'a-' Standalone Credit Profile). Novatek compares favourably with US peers Marathon Oil Corporation (BBB/Negative), Devon Energy Corporation (BBB/Stable) and Noble Energy Inc. (BBB/Rating Watch Positive), which have half the production volumes of Novatek.

However, Novatek has much lower EBITDA than its Russian peers Gazprom Neft (USD8.2 billion), Tatneft (USD4.1 billion) and Lukoil (USD14 billion) and lower profitability on a per boe basis compared with domestic and foreign peers. This is because it primarily focuses on domestic sales of natural gas (on a subsidiary level), which is less profitable than liquids.

Novatek has one of the highest reserve life metrics domestically, at 27.5 years based on 1P reserves, which is a very strong reserve estimate compared with the median of 11 years amongst US peers in this rating category. All Novatek's reserves are concentrated in the Yamal region of Russia, meaning the company is subject to higher-than-average risks pertaining to the Russian operating environment.

Novatek's leverage is low compared to Russian and international peers, with only Lukoil and Tatneft having lower leverage. We believe that Novatek will be able to maintain its conservative leverage profile in the next three to four years.

Navigator Peer Comparison

Issuer		Business profile						Financial profile		
	IDR/Outlook	Operating Environment	Management and Corporate Governance	Diversification	Proved Reserves	Cash Flow Cycle	Production Size	Profitability	Financial Structure	Financial Flexibility
Apache Corporation	BB+/Sta	aa	bbb	bbb	bb+	bbb-	bbb	bbb-	bb+	bbb-
Devon Energy Corporation	BBB/Sta	aa	a-	bbb	bbb	bbb	bbb+	bbb	bbb+	bbb+
PJSC Gazprom	BBB/Sta	bb	bb+	a	aa+	bbb	aa+	a+	a+	a-
Marathon Oil Corporation	BBB/Neg	aa	bbb	bbb	bb+	bbb	bbb	bbb-	bbb+	bbb+
Noble Energy Inc.	BBB/RWP	aa	bbb	bbb	bbb	bbb	bbb	bbb-	bbb+	bbb+
PAO Novatek	BBB/Sta	bb-	bbb	bbb+	aa	bbb	a	bbb	aa	bbb+
PJSC Gazprom Neft	BBB/Sta	bb-	bbb	a	aa	bbb	a	a-	a	bbb-
PJSC Lukoil	BBB+/Sta	bb	bbb	a	aa	a	aa-	a	aa	a+
PJSC Tatneft	BBB-/Sta	bb	bb	bbb-	aa	bbb	bbb+	bbb+	aa	bbb+

Source: Fitch Ratings. **Importance** Higher Moderate Lower

Issuer		Business profile						Financial profile		
Name	IDR/Outlook	Operating Environment	Management and Corporate Governance	Diversification	Proved Reserves	Cash Flow Cycle	Production Size	Profitability	Financial Structure	Financial Flexibility
Apache Corporation	BB+/Sta	8.0	2.0	2.0	0.0	1.0	2.0	1.0	0.0	1.0
Devon Energy Corporation	BBB/Sta	6.0	2.0	0.0	0.0	0.0	1.0	0.0	1.0	1.0
PJSC Gazprom	BBB/Sta	-3.0	-2.0	3.0	7.0	0.0	7.0	4.0	4.0	2.0
Marathon Oil Corporation	BBB/Neg	6.0	0.0	0.0	-2.0	0.0	0.0	-1.0	1.0	1.0
Noble Energy Inc.	BBB/RWP	6.0	0.0	0.0	0.0	0.0	0.0	-1.0	1.0	1.0
PAO Novatek	BBB/Sta	-4.0	0.0	1.0	6.0	0.0	3.0	0.0	6.0	1.0
PJSC Gazprom Neft	BBB/Sta	-4.0	0.0	3.0	6.0	0.0	3.0	2.0	3.0	-1.0
PJSC Lukoil	BBB+/Sta	-4.0	-1.0	2.0	5.0	2.0	4.0	2.0	5.0	3.0
PJSC Tatneft	BBB-/Sta	-2.0	-2.0	0.0	7.0	1.0	2.0	2.0	7.0	2.0

Source: Fitch Ratings. Worse positioned than IDR In line with IDR Better positioned than IDR

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- A stronger business profile evidenced by funding arrangements and visible progress related to the implementation of Arctic LNG 2, along with an improvement in Russia's operating environment, provided that credit metrics remain conservative.

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- FFO net leverage above 2.5x on a sustained basis
- Intensification of western sanctions directly affecting Novatek or its LNG projects

Liquidity and Debt Structure

Comfortable Liquidity: At end-March 2020, Novatek had short-term debt equivalent to around RUB56 billion and which was fully covered by cash balances and short-term bank deposits of around RUB217 billion. Other sources of liquidity include undrawn long-term committed credit lines totalling RUB163 billion. We assume that Novatek will tap the capital market to partially fund its FCF deficit in 2021-2023. The company has strong access to domestic funding, including Russia's largest banks, but is barred from the US dollar debt market due to sanctions.

Guarantees Excluded: Novatek has provided around USD10 billion of completion and other non-financial guarantees to YLNG's creditors. We exclude these from Novatek's leverage as we view the risk of cash outflows under these guarantees as diminishing because the project was launched, reached full capacity and passed commercial and production tests in April 2020. Most guarantees will be released shortly or replaced by other smaller and more specific guarantees. We will assess Arctic LNG 2's guarantees once the terms and conditions are finalised.

ESG Considerations

The highest level of ESG credit relevance, if present, is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Liquidity and Debt Maturity Scenario with No Refinancing

(RUBm)	2020F	2021F	2022F
Available liquidity			
Beginning cash balance	136,992	185,636	69,263
Rating case FCF after acquisitions and divestitures	60,890	-71,859	-9,870
Total available liquidity (A)	**197,882**	**113,777**	**59,393**
Liquidity uses			
Debt maturities	-12,246	-44,514	-66,138
Total liquidity uses (B)	**-12,246**	**-44,514**	**-66,138**
Liquidity calculation			
Ending cash balance (A+B)	185,636	69,263	-6,745
Revolver availability	150,000	150,000	150,000
Ending liquidity	**335,636**	**219,263**	**143,255**
Liquidity score (x)	28.4	5.9	3.2

Source: Fitch Ratings, Fitch Solutions, PAO Novatek

Scheduled debt maturities	Original
(RUBm)	**31 December 2019**
2020	12,246
2021	44,514
2022	66,138
2023	4,305
2024	4,305
Thereafter	20,590
Total	**152,098**

Source: Fitch Ratings, Fitch Solutions, PAO Novatek

Key Assumptions

- Brent crude oil price: USD35/bbl in 2020, USD45/bbl in 2021, USD53/bbl in 2022 and USD55/bbl thereafter.
- USD/RUB: 70.4 in 2020, 68.9 in 2021, 68.0 in 2022 and 67.0 thereafter.
- A broadly stable tax environment in Russia.
- Stabilisation in natural gas and condensate production from consolidated subsidiaries in 2020 due to the launch of the North Russkoye cluster.
- Oil production declines due to OPEC+ agreement restrictions and a reduction in oil-related capex.
- Capex peaking at RUB200 billion in 2020 and moderating towards RUB110 billion from 2022.
- Novatek's investment in Arctic LNG 2 to be broadly covered by proceeds from equity stake sales to other partners.
- Dividend pay-outs in line with a dividend policy of more than 30% of adjusted net income.

Financial Data

	Historical			Forecast		
(RUBm)	**Dec 2017**	**Dec 2018**	**Dec 2019**	**Dec 2020F**	**Dec 2021F**	**Dec 2022F**
Summary income statement						
Gross revenue	583,186	831,758	862,803	648,953	720,506	818,146
Revenue growth (%)	8.5	42.6	3.7	-24.8	11.0	13.6
Operating EBITDA (before income from associates)	198,326	258,920	250,788	147,854	186,608	207,846
Operating EBITDA margin (%)	34.0	31.1	29.1	22.8	25.9	25.4
Operating EBITDAR	198,416	259,096	251,568	148,634	187,388	208,626
Operating EBITDAR margin (%)	34.0	31.2	29.2	22.9	26.0	25.5
Operating EBIT	163,803	225,826	221,016	113,046	148,319	165,728
Operating EBIT margin (%)	28.1	27.2	25.6	17.4	20.6	20.3
Gross interest expense	-10,354	-9,176	-9,112	-7,586	-9,095	-13,185
Pretax income (including associate income/loss)	200,839	228,534	1,003,115	16,380	228,010	251,143
Summary balance sheet						
Readily available cash and equivalents	65,943	69,260	136,992	135,636	60,449	50,697
Total debt with equity credit	163,046	181,961	152,098	158,800	239,485	319,308
Total adjusted debt with equity credit	163,586	183,017	156,778	163,480	244,165	323,988
Net debt	97,103	112,701	15,106	23,164	179,036	268,611
Summary cash flow statement						
Operating EBITDA	198,326	258,920	250,788	147,854	186,608	207,846
Cash interest paid	-9,917	-8,056	-8,140	-7,586	-9,095	-13,185
Cash tax	-32,629	-47,127	-35,061	-21,294	-43,322	-47,717
Dividends received less dividends paid to minorities (inflow/(out)flow)	2,383	-11,568	29,292	5,766	3,689	11,702
Other items before FFO	1,209	6,138	8,210	2,596	2,882	3,273
Funds flow from operations	165,321	199,618	292,502	132,335	152,942	172,941
FFO margin (%)	28.3	24.0	33.9	20.4	21.2	21.1
Change in working capital	5,161	-11,393	-9,967	8,249	-4,972	-3,356
Cash flow from operations (Fitch defined)	170,482	188,225	282,535	140,584	147,970	169,585
Total non-operating/non-recurring cash flow	0	0	0			
Capital expenditure	-37,046	-90,205	-165,572			
Capital intensity (capex/revenue) (%)	6.4	10.8	19.2			
Common dividends	-42,075	-51,980	-93,468			
FCF	91,361	46,040	23,495			
Net acquisitions and divestitures	-19,558	-28,361	71,703			
Other investing and financing cash flow items	1,075	4,224	4,363	-58,948	-79,013	-77,705
Net debt proceeds	-53,794	-16,449	-2,176	6,702	80,685	79,823
Net equity proceeds	-1,442	-2,137	-1,865	-10,000	-5,000	-2,000
Total change in cash	17,642	3,317	95,520	-1,356	-75,187	-9,752
Leverage ratios						
Total net debt with equity credit/operating EBITDA (x)	0.5	0.5	0.1	0.2	0.9	1.2
Total adjusted debt/operating EBITDAR (x)	0.8	0.7	0.6	1.1	1.3	1.5
Total adjusted net debt/operating EBITDAR (x)	0.5	0.5	0.1	0.2	1.0	1.2
Total debt with equity credit/operating EBITDA (x)	0.8	0.7	0.5	1.0	1.3	1.5
FFO adjusted leverage (x)	1.0	0.9	0.6	1.2	1.6	1.8
FFO adjusted net leverage (x)	0.6	0.6	0.1	0.2	1.2	1.6
FFO leverage (x)	1.0	0.9	0.6	1.2	1.6	1.8
FFO net leverage (x)	0.6	0.5	0.1	0.2	1.2	1.5
Calculations for forecast publication						
Capex, dividends, acquisitions and other items before FCF	-98,679	-170,546	-187,337	-79,694	-219,828	-179,455
FCF after acquisitions and divestitures	71,803	17,679	95,198	60,890	-71,859	-9,870
FCF margin (after net acquisitions) (%)	12.3	2.1	11.0	9.4	-10.0	-1.2
Coverage ratios						
FFO interest coverage (x)	17.1	25.6	31.1	17.8	16.5	13.3
FFO fixed-charge coverage (x)	16.9	25.1	28.5	16.2	15.3	12.6
Operating EBITDAR/interest paid + rents (x)	20.1	30.1	31.5	18.5	19.4	15.8
Operating EBITDA/interest paid (x)	20.2	30.7	34.4	20.3	20.9	16.7
Additional metrics						
CFO-capex/total debt with equity credit (%)	81.8	53.9	76.9	-37.4	-5.0	18.7
CFO-capex/total net debt with equity credit (%)	137.4	87.0	774.3	-256.5	-6.7	22.2

Source: Fitch Ratings, Fitch Solutions.

How to Interpret the Forecast Presented

The forecast presented is based on Fitch Ratings' internally produced, conservative rating case forecast. It does not represent the forecast of the rated issuer. The forecast set out above is only one component used by Fitch Ratings to assign a rating or determine a rating outlook, and the information in the forecast reflects material but not exhaustive elements of Fitch Ratings' rating assumptions for the issuer's financial performance. As such, it cannot be used to establish a rating, and it should not be relied on for that purpose. Fitch Ratings' forecasts are constructed using a proprietary internal forecasting tool, which employs Fitch Ratings' own assumptions on operating and financial performance that may not reflect the assumptions that you would make. Fitch Ratings' own definitions of financial terms such as EBITDA, debt or free cash flow may differ from your own such definitions. Fitch Ratings may be granted access, from time to time, to confidential information on certain elements of the issuer's forward planning. Certain elements of such information may be omitted from this forecast, even where they are included in Fitch Ratings' own internal deliberations, where Fitch Ratings, at its sole discretion, considers the data may be potentially sensitive in a commercial, legal or regulatory context. The forecast (as with the entirety of this report) is produced strictly subject to the disclaimers set out at the end of this report. Fitch Ratings may update the forecast in future reports but assumes no responsibility to do so. Original financial statement data for historical periods is processed by Fitch Solutions on behalf of Fitch Ratings. Key financial adjustments and all financial forecasts credited to Fitch Ratings are generated by rating agency staff.

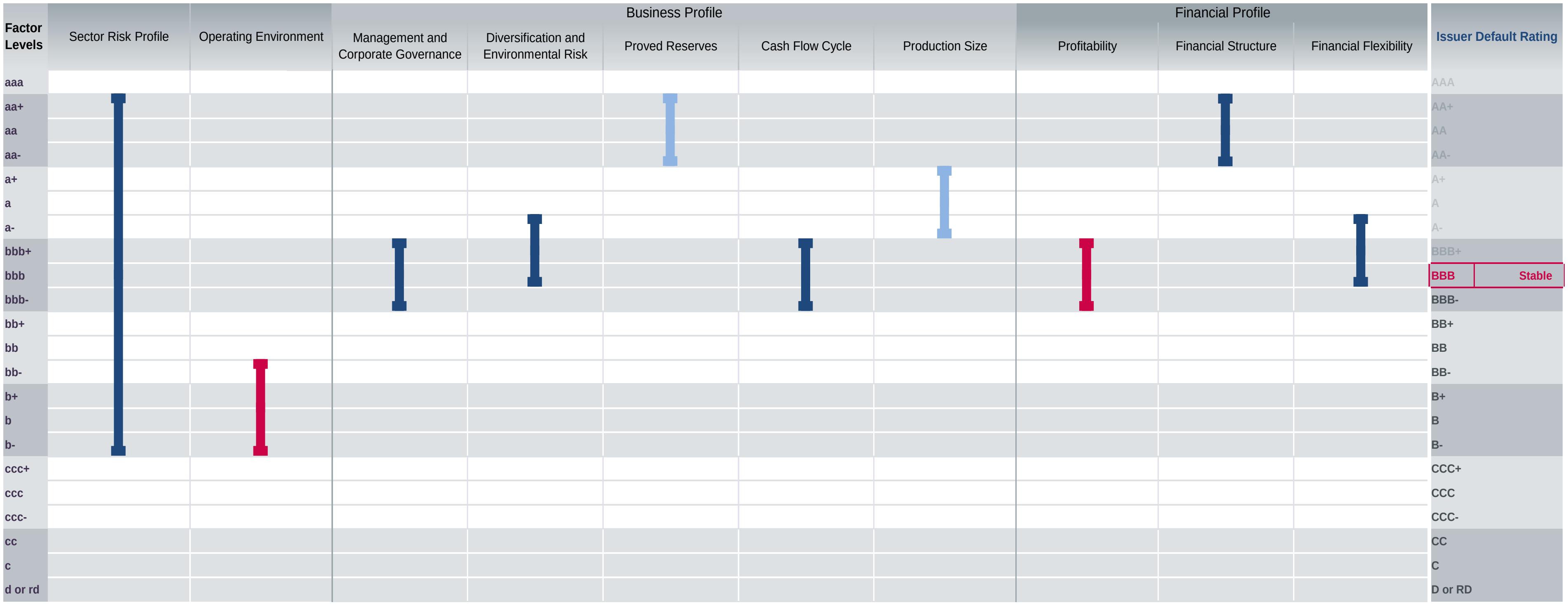
Ratings Navigator

FitchRatings

PAO Novatek

ESG Relevance:

Corporates Ratings Navigator
Oil & Gas Production



Bar Chart Legend:			
Vertical Bars = Range of Rating Factor		Bar Arrows = Rating Factor Outlook	
Bar Colours = Relative Importance		⇧	Positive
■	Higher Importance	⇩	Negative
■	Average Importance	⇳	Evolving
■	Lower Importance	□	Stable

FitchRatings

PAO Novatek

Corporates Ratings Navigator
Oil & Gas Production

Operating Environment

Band	Sub-Factor	Score	Description
bb	Economic Environment	bbb	Average combination of countries where economic value is created and where assets are located.
bb-	Financial Access	bb	Below average combination of issuer specific funding characteristics and of the strength of the relevant local financial market.
	Systemic Governance	b	Systemic governance (eg rule of law, corruption; government effectiveness) of the issuer's country of incorporation consistent with 'b'.
b-			
ccc+			

Management and Corporate Governance

Band	Sub-Factor	Score	Description
a-	Management Strategy	a	Coherent strategy and good track record in implementation.
bbb+	Governance Structure	bb	Board effectiveness questionable with few independent directors. "Key man" risk from dominant CEO or shareholder.
bbb	Group Structure	bbb	Some group complexity leading to somewhat less transparent accounting statements. No significant related-party transactions.
bbb-	Financial Transparency	a	High quality and timely financial reporting.
bb+			

Diversification and Environmental Risk

Band	Sub-Factor	Score	Description
a	Diversification	bbb	Upstream E&P companies with diverse projects or smaller integrated. Less vulnerable to price volatility; still subject to cost overruns and production delays.
a-	Environmental Risk	bbb	Moderate exposure to environmental regulations and/or material but manageable remediation costs relative to projected cash flows.
bbb+			
bbb			
bbb-			

Proved Reserves

Band	Sub-Factor	Score	Description
aaa	Reserve Base (boe)	aa	>4 billion
aa+			
aa			
aa-			
a+			

Cash Flow Cycle

Band	Sub-Factor	Score	Description
a-	Free Cash Flow	bbb	Neutral across the cycle.
bbb+			
bbb			
bbb-			
bb+			

Production Size

Band	Sub-Factor	Score	Description
aa-	Production (thousand boe/day)	a	700 - 2,000
a+			
a			
a-			
bbb+			

Profitability

Band	Sub-Factor	Score	Description
a-	FFO ($)	bb	$1.5 billion
bbb+	Capex/CFO (%)	aa	67%
bbb			
bbb-			
bb+			

Financial Structure

Band	Sub-Factor	Score	Description
aaa	FFO Leverage	aa	1.2x
aa+	FFO Net Leverage	aa	1.0x
aa	Total Debt With Equity Credit/Op. EBITDA	aa	1.0x
aa-			
a+			

Financial Flexibility

Band	Sub-Factor	Score	Description
a	Financial Discipline	a	Clear commitment to maintain a conservative policy with only modest deviations allowed.
a-	Liquidity	bbb	One year liquidity ratio above 1.25x. Well-spread maturity schedule of debt but funding may be less diversified.
bbb+	FFO Interest Coverage	aa	12.0x
bbb	FX Exposure	bbb	Some FX exposure on profitability and/or debt/cash flow match. Effective hedging in place.
bbb-	Op. EBITDA/Interest Paid	aa	15.0x

Credit-Relevant ESG Derivation

PAO Novatek has 12 ESG potential rating drivers

- Emissions from OGP production
- Energy use in OGP operations
- Water management (e.g. usage levels, recycling capacity)
- Waste and material handling; operations proximity to environmentally sensitive areas
- Hydrocarbon reserves exposure to present/future regulation and environmental costs
- Operations proximity to areas of conflict or indigenous lands

Showing top 6 issues

			Overall ESG
key driver	0	issues	5
driver	0	issues	4
potential driver	12	issues	3
not a rating driver	1	issues	2
	1	issues	1

For further details on Credit-Relevant ESG scoring, see page 3.

How to Read This Page: The left column shows the three-notch band assessment for the overall Factor, illustrated by a bar. The right column breaks down the Factor into Sub-Factors, with a description appropriate for each Sub-Factor and its corresponding category.

FitchRatings

PAO Novatek

Corporates Ratings Navigator
Oil & Gas Production

Credit-Relevant ESG Derivation

PAO Novatek has 12 ESG potential rating drivers

- PAO Novatek has exposure to emissions regulatory risk but this has very low impact on the rating.
- PAO Novatek has exposure to energy productivity risk but this has very low impact on the rating.
- PAO Novatek has exposure to water management risk but this has very low impact on the rating.
- PAO Novatek has exposure to waste and impact management risk but this has very low impact on the rating.
- PAO Novatek has exposure to extreme weather events but this has very low impact on the rating.
- PAO Novatek has exposure to land rights/conflicts risk but this has very low impact on the rating.

Showing top 6 issues

			Overall ESG Scale
key driver	0	issues	5
driver	0	issues	4
potential driver	12	issues	3
not a rating driver	1	issues	2
	1	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference
GHG Emissions & Air Quality	3	Emissions from OGP production	Diversification and Environmental Risk; Profitability
Energy Management	3	Energy use in OGP operations	Diversification and Environmental Risk; Profitability
Water & Wastewater Management	3	Water management (e.g. usage levels, recycling capacity)	Diversification and Environmental Risk; Profitability
Waste & Hazardous Materials Management; Ecological Impacts	3	Waste and material handling; operations proximity to environmentally sensitive areas	Diversification and Environmental Risk; Profitability
Exposure to Environmental Impacts	3	Hydrocarbon reserves exposure to present/future regulation and environmental costs	Diversification and Environmental Risk; Profitability; Financial Flexibility

E Scale: 5, 4, 3, 2, 1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	3	Operations proximity to areas of conflict or indigenous lands	Diversification and Environmental Risk; Profitability; Financial Flexibility
Customer Welfare - Fair Messaging, Privacy & Data Security	1	n.a.	n.a.
Labor Relations & Practices	3	Impact of labor negotiations and employee (dis)satisfaction	Profitability; Financial Structure; Financial Flexibility
Employee Wellbeing	2	Worker safety and accident prevention	Diversification and Environmental Risk; Profitability; Financial Flexibility
Exposure to Social Impacts	3	Social resistance to major projects or operations that leads to delays and cost increases	Production Size; Profitability; Financial Structure; Financial Flexibility

S Scale: 5, 4, 3, 2, 1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference
Management Strategy	3	Strategy development and implementation	Management and Corporate Governance
Governance Structure	3	Board independence and effectiveness; ownership concentration	Management and Corporate Governance
Group Structure	3	Complexity, transparency and related-party transactions	Management and Corporate Governance
Financial Transparency	3	Quality and timing of financial disclosure	Management and Corporate Governance

G Scale: 5, 4, 3, 2, 1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies the some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

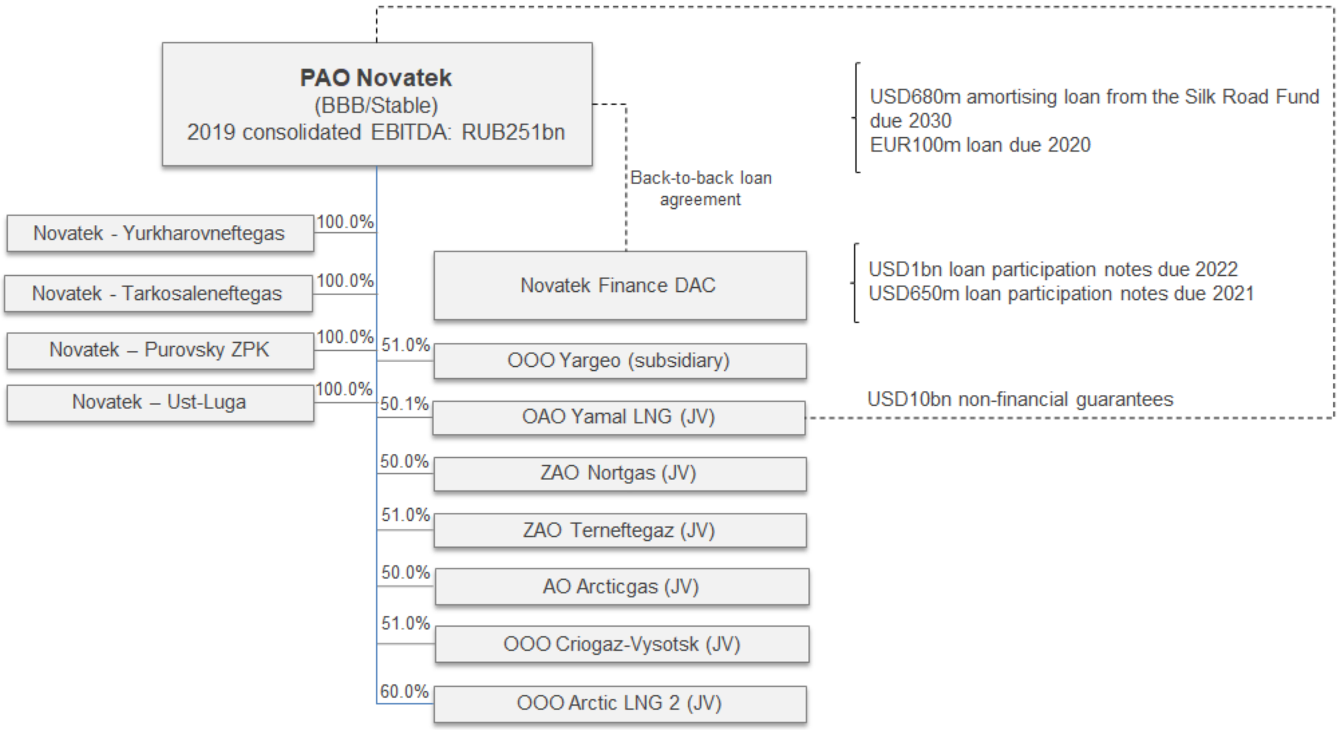
Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Priniciples for Responsible Investing (PRI) and the Sustainability Accounting Standards Board(SASB).

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

Simplified Group Structure Diagram



Source: Fitch Ratings, Fitch Solutions, PAO Novatek, as of 31 December 2019

Peer Financial Summary

Company	IDR	Financial statement date	Operating EBITDA (before income from associates) (USDm)	Funds flow from operations (USDm)	Free cash flow (USDm)	FFO Leverage (x)	FFO Net Leverage (x)
PAO Novatek	BBB						
	BBB	2019	3,877	4,522	363	0.6	0.1
	BBB	2018	4,111	3,170	731	0.9	0.5
	BBB	2017	3,402	2,836	1,567	1.0	0.6
PJSC Lukoil	BBB+						
	BBB+	2019	18,247	16,826	6,502	0.4	-0.1
	BBB+	2018	17,702	14,259	5,023	0.6	0.0
	BBB+	2017	13,969	13,129	1,143	0.8	0.3
PJSC Tatneft	BBB-						
	BBB-	2019	4,985	4,052	-637	0.4	-0.1
	BBB-	2018	5,027	4,236	812	0.6	0.0
	BBB-	2017	3,480	2,876	-438	0.8	0.3
Apache Corporation	BB+						
	BBB	2019	4,036	2,552	-742	2.9	2.9
	BBB	2018	4,795	3,206	-721	2.3	2.2
	BBB	2017	3,686	2,334	-799	3.2	2.5
Marathon Oil Corporation	BBB						
	BBB	2019	3,191	2,881	37	1.8	1.5
	BBB	2018	3,564	3,189	312	1.6	1.2
	BBB	2017	2,616	2,015	-15	2.3	2.1
PJSC Gazprom	BBB						
	BBB	2019	29,478	27,763	-5,036	2.1	1.4
	BBB-	2018	43,361	37,922	5,411	1.6	0.9
	BBB-	2017	26,825	20,837	-2,853	2.6	1.7
PJSC Gazprom Neft	BBB						
	BBB	2019	9,309	9,174	-1,214	1.2	0.9
	BBB-	2018	9,937	8,642	1,565	1.5	1.1
	BBB-	2017	7,544	6,441	357	1.9	1.6
Noble Energy Inc.	BBB						
	BBB	2019	2,418	1,883	-865	3.5	3.3
	BBB-	2018	2,789	2,192	-1,202	2.7	2.4
	BBB-	2017	2,526	1,846	-916	3.1	2.8
Devon Energy Corporation	BBB						
	BBB	2019	2,453	2,092	13	1.8	1.2
	BBB+	2018	2,965	1,987	104	2.5	1.5
	BBB+	2017	3,618	2,798	-274	3.4	2.6

Source: Fitch Ratings, Fitch Solutions.

Reconciliation of Key Financial Metrics

(RUBm, as reported)	31 Dec 19
Income Statement Summary	
Operating EBITDA	250,788
+ Recurring Dividends Paid to Non-controlling Interest	-16,758
+ Recurring Dividends Received from Associates	46,050
+ Additional Analyst Adjustment for Recurring I/S Minorities and Associates	0
= Operating EBITDA After Associates and Minorities (k)	**280,080**
+ Operating Lease Expense Treated as Capitalised (h)	**780**
= Operating EBITDAR after Associates and Minorities (j)	**280,860**
Debt and Cash Summary	
Total Debt with Equity Credit (l)	**152,098**
+ Lease-Equivalent Debt	4,680
+ Other Off-Balance-Sheet Debt (p)	0
= Total Adjusted Debt with Equity Credit (a)	**156,778**
Readily Available Cash [Fitch-Defined]	136,992
+ Readily Available Marketable Securities [Fitch-Defined]	0
= Readily Available Cash & Equivalents (o)	**136,992**
Total Adjusted Net Debt (b)	**19,786**
Cash Flow Summary	
Preferred Dividends (Paid) (f)	**0**
Interest Received	47,413
+ Interest (Paid) (d)	**-8,140**
= Net Finance Charge (e)	**39,273**
FFO (c)	**292,502**
+ Change in Working Capital [Fitch-Defined]	-9,967
= Cash Flow from Operations [CFO] (n)	**282,535**
Capital Expenditures (m)	**-165,572**
Multiple applied to Capitalised Leases	**6.0**
Gross Leverage	
Total Adjusted Debt / Op. EBITDAR* [x] (a/j)	**0.6**
FFO Adjusted Gross Leverage [x] (a/(c-e+h-f))	**0.6**
Total Adjusted Debt/(FFO - Net Finance Charge + Capitalised Leases - Pref. Div. Paid)	
FFO Leverage [x] ((l+p)/(c-e+h-f))	**0.6**
(Total Debt + Other Debt)/(FFO - Net Finance Charge - Pref. Div. Paid)	
Total Debt With Equity Credit / Op. EBITDA* [x] (l/k)	**0.5**
CFO-Capex/Total Debt with Equity Credit (%)	**76.9%**
Net Leverage	
Total Adjusted Net Debt / Op. EBITDAR* [x] (b/j)	**0.1**
FFO Adjusted Net Leverage [x] (b/(c-e+h-f))	**0.1**
Total Adjusted Net Debt/(FFO - Net Finance Charge + Capitalised Leases - Pref. Div. Paid)	
FFO Net Leverage [x] ((l+p-o)/(c-e+h-f))	**0.1**
Total Adjusted Net Debt/(FFO - Net Finance Charge - Pref. Div. Paid)	
Total Net Debt / (CFO - Capex) [x] ((l-o)/(n+m))	**0.1**
CFO-Capex/Total Net Debt with Equity Credit (%)	**774.3%**
Coverage	
Op. EBITDAR / (Interest Paid + Lease Expense)* [x] (j/-d+h)	**31.5**
Op. EBITDA / Interest Paid* [x] (k/(-d))	**34.4**
FFO Fixed-Charge Coverage [x] ((c+e+h-f)/(-d+h-f))	**28.5**
(FFO + Net Finance Charge + Capit. Leases - Pref. Div Paid) / (Gross Int. Paid + Capit. Leases - Pref. Div. Paid)	
FFO Gross Interest Coverage [x] ((c+e-f)/(-d-f))	**31.1**
(FFO + Net Finance Charge - Pref. Div Paid) / (Gross Int. Paid - Pref. Div. Paid)	
* EBITDA/R after Dividends to Associates and Minorities	

Source: Fitch Ratings, Fitch Solutions, PAO Novatek

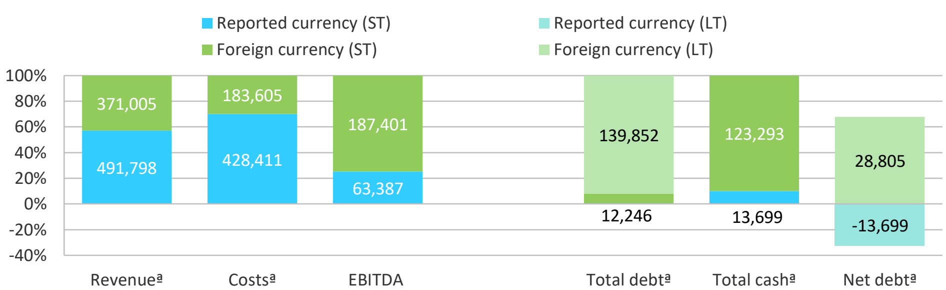
Fitch Adjustment Reconciliation

(RUBm)	Reported Values 31 Dec 19	Sum of Fitch Adjustments	Cash Adjustment	CORP - Lease Treatment	Other Adjustment	Adjusted Values
Income Statement Summary						
Revenue	862,803	0				862,803
Operating EBITDAR	220,028	31,540		-3,002	34,542	251,568
Operating EBITDAR after Associates and Minorities	249,320	31,540		-3,002	34,542	280,860
Operating Lease Expense	780	0				780
Operating EBITDA	219,248	31,540		-3,002	34,542	250,788
Operating EBITDA after Associates and Minorities	248,540	31,540		-3,002	34,542	280,080
Operating EBIT	187,018	33,998		-544	34,542	221,016
Debt and Cash Summary						
Total Debt With Equity Credit	152,098	0				152,098
Total Adjusted Debt With Equity Credit	152,098	4,680		4,680		156,778
Lease-Equivalent Debt	0	4,680		4,680		4,680
Other Off-Balance Sheet Debt	0	0				0
Readily Available Cash & Equivalents	53,240	83,752	83,752			136,992
Not Readily Available Cash & Equivalents	0	0				0
Cash Flow Summary						
Preferred Dividends (Paid)	0	0				0
Interest Received	47,413	0				47,413
Interest (Paid)	-8,140	0				-8,140
FFO	292,502	0				292,502
Change in Working Capital [Fitch-Defined]	-9,967	0				-9,967
Cash Flow from Operations [CFO]	282,535	0				282,535
Non-Operating/Non-Recurring Cash Flow	0	0				0
Capital (Expenditures)	-165,572	0				-165,572
Common Dividends (Paid)	-93,468	0				-93,468
FCF	23,495	0				23,495
Gross Leverage						
Total Adjusted Debt / Op. EBITDAR* [x]	0.6					0.6
FFO Adjusted Leverage [x]	0.6					0.6
FFO Leverage [x]	0.6					0.6
Total Debt With Equity Credit / Op. EBITDA* [x]	0.6					0.5
CFO-Capex/Total Debt with Equity Credit (%)	76.9%					76.9%
Net Leverage						
Total Adjusted Net Debt / Op. EBITDAR* [x]	0.4					0.1
FFO Adjusted Net Leverage [x]	0.4					0.1
FFO Net Leverage [x]	0.4					0.1
Total Net Debt / (CFO - Capex) [x]	0.8					0.1
CFO-Capex/Total Net Debt with Equity Credit (%)	118.3%					774.3%
Coverage						
Op. EBITDAR / (Interest Paid + Lease Expense)* [x]	28.0					31.5
Op. EBITDA / Interest Paid* [x]	30.5					34.4
FFO Fixed-Charge Coverage [x]	28.5					28.5
FFO Interest Coverage [x]	31.1					31.1

Source: Fitch Ratings, Fitch Solutions, PAO Novatek

FX Screener

(RUBm)



[a] Post-hedge, absolute figures displayed are Fitch's analytical estimates, based on publicly available information
Source: Fitch Ratings

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.