MOODY'S
INVESTORS SERVICE

Rating Action: Moody's confirms Ba1 ratings of four Russian integrated oil and gas companies; negative outlook

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London, 26 April 2016 -- Moody's Investors Service (Moody's) has confirmed at Ba1 the corporate family ratings (CFRs) of four integrated oil & gas companies -- Gazprom, PJSC; Gazprom Neft PJSC; OJSC Oil Company Rosneft; Lukoil, PJSC -- and one independent exploration and production (E&P) company -- OAO Novatek. The outlook on all the ratings is negative.

These actions conclude the rating reviews initiated by Moody's on 22 January 2016. A full list of the companies and rating actions appears below.

"Our decision to confirm the ratings of Russian oil and gas majors reflects our view that they will be able to maintain solid credit metrics in a "lower-for-longer" oil price environment helped by rouble weakness and a favourable tax system. However, their ratings will remain constrained at Ba1 by the sovereign rating and outlook," says Denis Perevezentsev, a Moody's Vice President -- Senior Credit Officer.

On 22 January 2016, Moody's placed the ratings of 32 integrated oil, E&P, and OFS companies in the EMEA region on review for downgrade. This reflected the substantial drop of oil prices and the continued oversupply in the global oil markets. Moody's also lowered its oil price estimates on 21 January 2016 and now forecasts that Brent oil price will average $33 per barrel of oil equivalent (boe) in 2016 and $38/boe in 2017 (Moody's base case scenario), with a slow recovery for oil prices over the next several years. The drop in oil prices and weak natural gas prices have caused a fundamental change in the energy industry and significantly hampered the sector's ability to generate cash flow. Moody's believes that this environment will continue for several years.

RATINGS RATIONALE

Today's confirmations primarily reflect (1) the favourable taxation system that is tied to oil prices such that when they fall oil and gas companies pay less tax, which in turn lifts the pressure on their credit metrics; (2) their low production costs and the rouble depreciation, which makes average realised prices sustainable in rouble terms and supports companies' profitability metrics; (3) companies' high portion of rouble-denominated operating and capital expenditure, which contains cost inflation; (4) the importance of the oil and gas industry for the Russian economy; and (5) Moody's assessment of high government support for government-related issuers (GRIs) -- Gazprom and Rosneft.

However, Russian oil and gas companies' ratings remain constrained by the sovereign rating and outlook.

RATIONALE FOR NEGATIVE OUTLOOK

The negative outlook on the ratings is in line with the negative outlook for the sovereign rating and reflects the fact that a potential further downgrade of Russia's sovereign rating may lead to downgrade of the companies' ratings.

-- CONFIRMATION OF GAZPROM'S Ba1 CFR and Ba1-PD PDR

Moody's confirmed the Ba1 CFR and Ba1-PD probability of default rating (PDR) of Gazprom, PJSC (Gazprom) and the Ba1 instruments ratings of its subsidiaries Gaz Capital S.A. and OOO Gazprom Capital with a negative outlook.

To determine Gazprom's debt rating and CFR, Moody's applies GRI rating methodology, according to which the CFR is driven by the combination of (1) Gazprom's baseline credit assessment (BCA) of ba1; (2) the Ba1 local-currency debt rating of the Russian government with negative outlook; (3) the high dependence between the state and the company; and (4) Moody's assumptions of a high level of support from the state in case of need.

The rating reflects (1) the world's largest natural gas reserves, at 17% of global and 72% of Russian gas reserves; (2) its unique business profile as Russia's largest producer and monopoly exporter of gas, and owner and operator of the world's largest gas transportation and storage system; (3) its market position as Europe's largest gas supplier; (4) its strong financial metrics and free cash flow generation, underpinned by contracted foreign-currency-denominated revenues and modest leverage; and (5) the economic, political and reputational importance of the company to the Russian state.

Despite its sizeable capex programme and contracting domestic gas sales, Moody's expects that Gazprom's financial metrics will remain fairly robust in 2016-17. This view is underpinned by Gazprom's strong position in the European gas market, in which it is likely to maintain its market share. Also, Gazprom's gas supply to Europe accounts for one third of Europe's total consumption volume and represents more than a half of the company's gas revenues. Gazprom's activity in the European gas market hinges on long-term contracts with oil-pegged prices based on the take-or-pay commitment.

The company's leverage as measured by Moody's-adjusted debt/EBITDA stood at 1.7x as of 30 September 2015. Deteriorating EBITDA and operating cash flows amid falling gas prices, potentially resulting in negative free cash flows in 2016, could increase leverage as measured by Moody's-adjusted leverage to 1.8x over the next 12-18 months. Gazprom is not subject to US and EU financial sanctions and retains good access to international capital markets having executed successful notes placements in 2015 and 2016.

Headquartered in Moscow, Gazprom is one of the world's largest integrated oil and gas companies. It is focused on the exploration, production and refining of gas and oil (via its subsidiary Gazprom Neft PJSC (Ba1, negative), as well as the transportation and distribution of gas to domestic, former Soviet Union (FSU) and European markets. Gazprom also owns and operates the Unified Gas Supply System in Russia, which is the world's largest gas transportation, storage and processing system, comprising nearly 170,700 kilometres of high-pressure trunk pipelines and 26 underground gas storage facilities, and is the leading exporter of gas to Western Europe. For the first nine months of 2015, Gazprom reported sales of RUB4.2 trillion and EBITDA of RUB1.4 trillion.

-- CONFIRMATION OF GAZPROM NEFT'S Ba1 CFR and Ba1-PD PDR

Moody's confirmed the Ba1 CFR and Ba1-PD PDR of Gazprom Neft PJSC (Gazprom Neft) and the Ba1 instruments ratings of its subsidiary GPN Capital S.A. with a negative outlook. The ratings reflect (1) the large scale of the company's reserves and operations; (2) its strong operating and financial performance; (3) its track record of production growth and robust reserves replacement; and (4) the close and beneficial linkages between Gazprom Neft and its parent Gazprom.

In 2015, the company grew its total proved hydrocarbon reserves, including shares in joint operations and joint ventures, by 5% to 11,268 million barrels of oil equivalent (mmboe). The company's hydrocarbon production including its share in joint ventures increased by 20.3% to 79.7 million tonnes (mt) in 2015 on continued production growth at joint ventures and sustained production at major fields. Lower oil and oil products prices on international markets were offset by higher sales volumes and prices at domestic market, resulting in net 2.1% sales decline. The company's refining throughput is fairly stable.

Higher production volumes and higher realised prices in the domestic market allowed the company to grow Moody's-adjusted EBITDA to RUB410 billion in 2015 compared with RUB371 billion in 2014. Capital expenditure increased by 29% to RUB349 billion in 2015 from RUB271 billion in 2014, resulting in negative Moody's-adjusted free cash flows of RUB95 billion in 2015.

Moody's expects that capex will remain at an elevated level resulting in negative free cash flows in 2016-17 as the company continues to actively invest in upstream operations and forges ahead with planned production ramp up. Moody's expects that Gazprom Neft's production will continue growing mainly owing to greenfield developments. Despite negative free cash flows, Moody's expects that Gazprom Neft's Moody's-adjusted leverage will remain at around 2.0x in 2016-17.

Gazprom Neft refines 77% of its oil production and sells more than half of its refining output via its own distribution network. The scale of the company's downstream assets and their proximity to its main producing fields in West Siberia highlight Gazprom Neft's high level of integration.

Gazprom Neft was included in the US and EU sanctions lists, which effectively cut off the company's access to long-term external financing in the Western financial and capital markets, as well as its ability to continue cooperating with Western partners on complex development projects. As a result, Moody's expects that Gazprom Neft will source liquidity from its strong operating cash flows as well as from (1) Russian banks (primarily state-owned); and (2) the issuance of rouble-denominated exchange bonds.

Headquartered in St. Petersburg, Gazprom Neft is Russia's fourth-largest vertically integrated oil and gas company by production levels. Gazprom Neft is 95.68% owned by Gazprom. For 2015, Gazprom Neft's revenue amounted to RUB1.7 trillion and its Moody's-adjusted EBITDA to RUB410 billion.

-- CONFIRMATION OF ROSNEFT'S Ba1 CFR and Ba1-PD PDR

Moody's confirmed the Ba1 CFR and Ba1-PD PDR of OJSC Oil Company Rosneft (Rosneft) and Rosneft International Holdings Limited and the Ba1 instruments ratings of Rosneft's subsidiaries Rosneft Finance S.A. and Rosneft International Finance Limited with a negative outlook.

To determine Rosneft's debt rating and CFR Moody's applies its GRI rating methodology, according to which the CFR is driven by a combination of (1) Rosneft's baseline credit assessment (BCA) of ba1; (2) the Ba1 local-currency debt rating of the Russian government with a negative outlook; (3) the high dependence between the state and the company; and (4) Moody's assumptions of a high level of support from the state in case of need.

Despite the government's plans to privatise 19.5% of Rosneft's shares, Moody's expects that the company will continue to enjoy high state support owing to its key economic role as one of the biggest tax payers in Russia and the biggest oil company in Russia (with the government continuing to retain controlling stake).

The rating reflects the company's strong business profile as one of the world's largest public oil and gas companies in terms of reserves and production. It also has substantial refining footprint. The company enjoys very strong state support, which was called upon at end-2014/early-2015 when the company issued more than RUB1 trillion of rouble-denominated bonds to refinance its upcoming maturities. This issuance came soon after the company appeared on US and EU sanctions lists, which effectively shuttered the company's access to international capital markets, as well as its ability to continue cooperating with western partners on complex development projects.

Moody's expects that Rosneft will source additional liquidity from its strong operating cash flows and cash balances as well as from (1) Chinese partners under prepayment crude supply contracts; (2) Russian banks (primarily state-owned); and (3) potential deals, announced in 2015-16, whereby it will sell assets.

Rosneft's proved hydrocarbon reserves amounted to 34 billion boe per Securities and Exchange Commission (SEC) classification and 43 billion boe per Petroleum Resources Management System (PRMS) classification as of 31 December 2015. In the Q4 2015, Rosneft's average hydrocarbon production amounted to 5.2 million boe per day. The production of natural and associated gas was 16.62 billion cubic meters in Q4 2015.

Moody's-adjusted debt includes about RUB1.9 trillion of prepayments from traders on long-term oil supply agreements, which the rating agency treats as a debt-like item, adding to financial debt. This elevates leverage, as measured by Moody's-adjusted debt/EBITDA, to about 5.3x as of 31 December 2015. The company used these prepayments as a liquidity buffer and also to reduce its financial debt.

Despite a sizeable capex programme, which Moody's estimates at about RUB600-RUB750 billion per year in 2016 and 2017, depending on prevailing oil prices, the rating agency expects that the company will be able to generate positive free cash flows in 2016-17. This will allow it to reduce Moody's-adjusted leverage to 3x-4x by end-2017. Sizeable cash and deposits balances of RUB1.3 trillion as of 31 December 2015, aided by operating cash flows estimated by Moody's at about RUB0.8-RUB1 trillion per year in 2016-17, will allow the company to fund its capex and repay its maturing financial debt.

Rosneft, in which the Russian state holds a 69.5% share via its fully owned agent OAO Rosneftegaz (not rated), is Russia's largest integrated oil and gas company. The company reported RUB5,150 billion of revenue and RUB1,245 billion of EBITDA in 2015.

-- CONFIRMATION OF LUKOIL'S Ba1 CFR and Ba1-PD PDR

Moody's confirmed the Ba1 CFR and Ba1-PD PDR of Lukoil, PJSC (Lukoil) and the Ba1 instruments ratings of its subsidiary LUKOIL International Finance B.V. with a negative outlook.

The rating reflects (1) the company's unique business profile as Russia's largest private company; (2) sustainable growth rates of both oil and gas production and successful reserve replacement; (3) evolving opportunities from ramping up production at key greenfield projects; and (4) its strong financial metrics, including low leverage.

The company's proved reserves at 1 January 2016 fell to 16,558 million barrels of oil equivalent (mmboe) from 17,585 mmboe as of 1 January 2015, with production (890 mmboe) in 2015 and negative reserve revisions (643 mmboe) in the same year exceeding reserve additions (506 mmboe). Moody's positively notes that the company continues to expand reserves and production outside of Russia, with the West Qurna-2 project in Iraq contributing significantly to positive reserves revision in 2016. The project's contribution to total production also rose to about 10% in 2015 (versus 5.7% in 2014) offsetting declining production at Lukoil's mature fields in Western Siberia. This boost in production at West Qurna-2 allowed the company to increase 2015 oil and condensate production to 2,052 thousand barrels of oil equivalent per day (boepd) compared with 1,992 thousand boepd in 2014, even as production in Western Siberia declined.

Lukoil's leverage as measured by Moody's-adjusted debt/EBITDA stood at 1.0x as of 31 December 2015, compared with 0.9x as of 31 December 2014, which is low versus both Russian and global oil and gas sector peers. The company was free cash flow positive in 2015, which, alongside its disciplined control over operating expenses and capex, allows it to pay substantial dividends. Moody's expects that under its base case oil price scenario, the company will generate about RUB700 billion of operating cash flows in 2016 and RUB800 billion in 2017, which will allow it to fund about RUB600 billion of annual capex in 2016-17, pay dividends and still remain free cash flow positive. Moody's estimates that the company will be able to maintain its leverage, as measured by Moody's-adjusted debt/EBITDA, at about 1.0x in 2016-17.

Lukoil is a private company and is not among the Russian entities affected by US and EU financial sanctions. However, Lukoil is subject to US sanctions banning the provision of goods, services and technology for certain deep-water (greater than 500 feet), Artic offshore, or shale projects that have the potential to produce oil, encompassing license requirements for exports involving certain projects. Lukoil is also subject to similar EU sanctions, which limit the provision of services required for technologically challenging oil exploration and production projects and apply to all such projects in Russia. However, Lukoil is not currently impacted by these sanctions as its production in Western Siberia is mostly conventional and its offshore projects in the North Caspian Sea are at water depths of approximately 20 meters. As such, they do not qualify as deep-water (500 feet equals about 150 m) as indicated by the US sanctions.

Lukoil is Russia's third-largest vertically integrated oil & gas company. The company reported revenue of RUB5,749 billion and adjusted EBITDA of RUB946 billion in 2015.

-- CONFIRMATION OF NOVATEK'S Ba1 CFR and Ba1-PD PDR

Moody's confirmed the Ba1 CFR and Ba1-PD PDR of OAO Novatek (Novatek) and the Ba1 instruments ratings of its subsidiary Novatek Finance Limited with a negative outlook.

The rating reflects the company's (1) vast conventional low cost reserves; (2) integrated business model with a high share of processed value added products; (3) track record of strong production growth in gas and liquids (gas condensate and oil); (4) strong domestic market position in gas; (5) strong financial metrics and fairly low leverage; and (6) execution and financing risks related to the development of Yamal LNG project, which have somewhat abated recently.

Novatek has 31 E&P licences located mainly above the Arctic Circle in the West Siberian Yamalo-Nenets Autonomous District of Russia, with total proven SEC reserves growing by 1.4% to 12.8 billion boe as of 31 December 2015 from 2014. The company carries out the commercial production of natural gas, gas condensate and crude oil at 13 fields, including the company's flagship Yurkharovskoye and East-Tarkosalinskoye oil and gas condensate fields, with E&P production licences valid until 2034 and 2043, respectively. These fields contributed 53% and 13% of the company's total gas production in 2015.

Helped by the growing production of gas and liquids at its joint ventures, the company grew gas production to 68 billion cubic meters (bcm) in 2015 from 62 bcm in 2014 while growing liquids production by 51% to 9.1 million tonnes in 2015 from 6 million tonnes in 2014. Production of gas and liquids at the company's joint ventures with Gazprom Neft, SeverEnergia (not rated), of which the company owns 53.3% (ownership will be reduced to parity during 2016) and Northgas (not rated), of which the company owns 50%, as well as oil production from Yarudeyskoye oil field developed by joint venture Yargeo, of which the company owns 51%, launched in December 2015 and ramped up to full capacity by the end 2015, will continue contributing to growing gas and liquids volumes in 2016.

Moody's expects that Novatek will maintain its strong financial metrics in 2016-17 with leverage (as measured by Moody's-adjusted debt/EBITDA) of around 1.5x in 2016-17. The company's solid operating cash flows will be sufficient to fund sharply reduced capex requirements, repay debt and pay dividends. Moody's expects free cash flows after dividends in 2016 at about RUB40 billion potentially growing to RUB70 billion in 2017 under Moody's base case oil price scenario, provided the company does not extend substantial financing to its joint venture Yamal LNG from 2016.

Novatek is subject to a US ban on the provision of financing for, and other dealings in, new debt with a maturity of longer than 90 days and all activities related to new debt, which does not impact the company's existing debt or equity instruments. Novatek is not subject to the US technological sanctions, comprising a ban on the provision of goods, services and technology for certain deep-water (greater than 500 feet), Arctic offshore, or shale projects that have the potential to produce oil, encompassing also licence requirements for exports involving certain projects. For that reason, Yamal LNG has not experienced meaningful difficulties, apart from some delays in closing external financing owing to these financial restrictions, while the project continues to receive equipment from foreign suppliers, including from the US.

Headquartered in Moscow, Novatek is Russia's largest independent gas producer and second-largest gas company in Russia, after state-controlled Gazprom. In 2015, Novatek reported RUB475 billion in revenue and normalized EBITDA of RUB215 billion.

PRINCIPAL METHODOLOGY

The principal methodology used in rating Gazprom, PJSC, Gaz Capital S.A., OOO Gazprom Capital, OJSC Oil Company Rosneft, Rosneft International Finance Limited, Rosneft International Holdings Limited and Rosneft Finance S.A. was Global Integrated Oil & Gas Industry published in April 2014. Other methodologies used include the Government-Related Issuers methodology published in October 2014.

The principal methodologies used in rating OAO Novatek and Novatek Finance Limited was Global Independent Exploration and Production Industry published in December 2011.

The principal methodologies used in rating Lukoil, PJSC, LUKOIL International Finance B.V., Gazprom Neft PJSC and GPN Capital S.A. was Global Integrated Oil & Gas Industry published in April 2014.

Please see the Ratings Methodologies page on www.moodys.com for a copy of these methodologies.

List of affected ratings:

Confirmations:

..Issuer: Gazprom, PJSC

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: Gaz Capital S.A.

....Senior Unsecured Medium-Term Note Program, Confirmed at (P)Ba1

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

....Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: OOO Gazprom Capital

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: Gazprom Neft PJSC

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: GPN Capital S.A.

....BACKED Senior Unsecured Medium-Term Note Program, Confirmed at (P)Ba1

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: OJSC Oil Company Rosneft

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: Rosneft Finance S.A.

....BACKED Senior Unsecured Medium-Term Note Program, Confirmed at (P)Ba1

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: Rosneft International Finance Limited

....BACKED Senior Unsecured Medium-Term Note Program, Confirmed at (P)Ba1

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: Rosneft International Holdings Limited

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: Lukoil, PJSC

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: LUKOIL International Finance B.V.

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

..Issuer: OAO Novatek

.... Probability of Default Rating, Confirmed at Ba1-PD

.... Corporate Family Rating, Confirmed at Ba1

..Issuer: Novatek Finance Limited

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

....Senior Unsecured Regular Bond/Debenture, Confirmed at Ba1

Outlook Actions:

..Issuer: Gazprom, PJSC

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Gaz Capital S.A.

....Outlook, Changed To Negative From Rating Under Review

..Issuer: OOO Gazprom Capital

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Gazprom Neft PJSC

....Outlook, Changed To Negative From Rating Under Review

..Issuer: GPN Capital S.A.

....Outlook, Changed To Negative From Rating Under Review

..Issuer: OJSC Oil Company Rosneft

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Rosneft Finance S.A.

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Rosneft International Finance Limited

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Rosneft International Holdings Limited

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Lukoil, PJSC

....Outlook, Changed To Negative From Rating Under Review

..Issuer: LUKOIL International Finance B.V.

....Outlook, Changed To Negative From Rating Under Review

..Issuer: OAO Novatek

....Outlook, Changed To Negative From Rating Under Review

..Issuer: Novatek Finance Limited

....Outlook, Changed To Negative From Rating Under Review

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