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INVESTORS SERVICE

Rating Action: MOODY'S ASSIGNS Ba2 CORPORATE FAMILY RATING TO NOVATEK, OUTLOOK STABLE; MOODY'S INTERFAX RATING AGENCY ASSIGNS Aa2.ru LONG TERM NATIONAL SCALE RATING

Global Credit Research - 10 Feb 2006

First Time Rating

London, 10 February 2006 -- Moody's Investors Service has assigned a Ba2 Corporate Family Rating to OAO Novatek ("Novatek"). The outlook is stable. Concurrently, Moody's Interfax Rating Agency has assigned a Aa2.ru long term National Scale Rating (NSR) to the company. Moscow-based Moody's Interfax is majority-owned by Moody's Investors Service, a leading global rating agency. This is the first time that Moody's Investors Service has assigned credit ratings to Novatek.

According to Moody's and Moody's Interfax ("Moody's"), the Ba2 global scale Corporate Family Rating reflects Novatek's global default and loss expectation, while the Aa2.ru NSR reflects the standing of Novatek's credit quality relative to its domestic peers.

SUMMARY OF RATING RATIONALE

Moody's states that Novatek's ratings reflect (1) the group's substantial reserves, primarily natural gas, (2) very high operating and capital efficiency, (3) limited exposure to commodity price risk given low prices of domestic Russian gas, (4) strong growth prospects from increasing domestic demand and tighter supply, (5) Novatek's clear and transparent group structure, (6) the company's well-articulated and prudent financial policies, and (7) Moody's expectation that Novatek will maintain a robust financial profile going forward.

At the same time, Moody's adds that Novatek's ratings are currently constrained by (1) the group's high dependence on majority state-owned OJSC Gazprom for pipeline access, (2) the effective control of the Russian gas sector by Gazprom, (3) ongoing project and execution risk related to Novatek's high level of undeveloped reserves, (4) a certain degree of customer concentration risk and (5) wider geopolitical risks from operating solely in Russia.

DETAILED RATING RATIONALE

Novatek's ratings benefit from the significant scale associated with its reserve and production base, which position Novatek amongst the world's largest exploration & production (E&P) companies. Furthermore, Novatek's high operating and capital efficiency enable it to produce solid margins despite Russia's domestic gas prices being kept significantly below international averages, which in turn limits Novatek's risk exposure to volatile world crude oil prices. Consequently, Moody's believes that Novatek will be able to benefit from gradually rising domestic prices, which should be able to compensate for any cost inflation, and particularly as far as transport tariffs are concerned, which are outside the control of the company.

Novatek's ratings are also supported by the growing demand for natural gas in Russia, which faces increasingly tight supply due to Gazprom's focus on export markets and liquefied natural gas (LNG). Moody's believes that this growing gap between domestic supply and demand will be filled increasingly by independent domestically-focused gas companies (in addition to some of the integrated oil companies). Finally, Moody's adds that Novatek's ratings benefit from the group's clear and transparent group structure, strong corporate governance and relatively low privatisation risk, given that the group's core operating assets, which it fully owns, are all greenfield operations.

Moody's also states that Novatek's ratings are constrained by both fundamental risk factors and geopolitical influences, the latter of which presently limit Novatek's Ba2 rating by several notches below the company's fundamentally investment-grade credit profile. Overall, ratings are constrained by Novatek's high dependence on Gazprom, which holds the monopoly for gas transportation and exports. While Gazprom must ensure third-party access to the giant Unified Gas Supply System (UGSS), this is subject to the availability of capacity, which necessitates close co-ordination of Novatek's activities with Gazprom. Moody's adds that this risk is in large part mitigated by Novatek's cooperative working relationship with Gazprom over the past decade, and the benefits available to Gazprom from the presence of a reliable domestic partner, which allows Gazprom to focus its strategic attention on profitable exports. At the same time, Moody's would require evidence of continued unimpeded operations under more attractive domestic pricing conditions before Novatek's ratings could be raised closer to the company's fundamental credit quality. Ratings are also constrained by Novatek's high proportion of undeveloped reserves, which will require increased capital investments to come on stream, as well as some customer concentration risk, given that Novatek sells close to 60% of its gas to five key customers, most of which on short term contracts.

RATING OUTLOOK

Moody's states that Novatek's ratings are stable. To support the ratings, Moody's expects the company to produce growing positive free cash flow going forward, thereby implying that its growing capital investments and dividends can be funded from internal cash flow generation, while building up gradual cash balances. Moody's has factored some flexibility into the ratings and would expect retained cash flow (after maintenance investments) to total debt of at least 40% from what is expected to be at least 100% by year-end 2005. Accordingly, Novatek's ratings are currently strongly positioned. Moody's also expects Novatek to maintain secured debt as a percentage of total debt at no more than 15%, thereby eliminating the requirement to notch down any subsequent senior unsecured debt from the Corporate Family Rating.

Moody's views Novatek's ratings as strongly positioned within the Ba2 rating category, supported by the company's strong financial metrics and favourable business fundamentals. Ratings could experience upward pressure over the medium term, if Novatek is able to maintain its productive working relationship with Gazprom consistently, even under more attractive domestic market conditions, and upon coming closer to its 2010 production target of 45 billion cubic meters (bcm), primarily by developing its Yurkharovskoye field, while strongly outperforming above financial parameters. Moody's would also expect a larger overall number of longer term gas supply contracts with a somewhat more diversified customer base before ratings could benefit. At the same time, ratings could come under pressure, if Novatek were repeatedly unable to find transportation access to the UGSS for its gas or were otherwise impaired from undertaking its operations. Ratings could also come under pressure, if there was a material step change in financial policy, which would result in negative free cash flow and consistently higher debt;

nonetheless ratings do allow for some flexibility to increase investments or for higher shareholder returns, provided they are adopted in the context of above mentioned financial parameters.

ISSUER BACKGROUND

OAO Novatek, based in Moscow, is Russia's second largest gas company after state-controlled Gazprom, and the largest of the country's independent gas producers. In the first nine months ending 30 September 2005, Novatek reported sales volumes (including purchases) of 20.6 billion cubic meters (bcm) of natural gas all of which is sold domestically, 1.3 million tonnes (mt) of liquids (crude oil, stable gas condensates and LPG), and 560,000 tonnes of oil products. Total revenues in the first three quarters amounted to Rub. 28.6 billion (USD 995.5 million).

NATIONAL SCALE RATINGS

Moody's Interfax Rating Agency's National Scale Ratings (NSRs) are intended as relative measures of creditworthiness among debt issues and issuers within a country, enabling market participants to better differentiate relative risks. NSRs in Russia are designated by the ".ru" suffix. NSRs differ from global scale ratings, as assigned by Moody's Investors Service, in that they are not globally comparable to the full universe of Moody's rated entities, but only with other rated entities within the same country.

ABOUT MOODY's AND MOODY's INTERFAX

Moody's Interfax Rating Agency specialises in credit risk analysis in Russia and is 51% owned and controlled by Moody's Investors Service, a leading provider of credit ratings, research and analysis covering debt instruments and securities in the global capital markets. Moody's Investors Service is a subsidiary of Moody's Corporation (NYSE: MCO), which reported revenues of US$1.4 billion in 2004, employs approximately 2,500 people worldwide and maintains offices in 18 countries. Further information is available at www.moodys.com.

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