

Rating Action: Moody's assigns Ba3 rating to Leviathan Bond's senior secured notes, outlook stable

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First-time Rating

London, 27 July 2020 -- Moody's Investors Service (Moody's) has today assigned a Ba3 rating to \$2.25 billion proposed senior secured notes to be issued by Leviathan Bond Ltd. (Leviathan Bond). The outlook on the rating is stable. This is the first time Moody's has assigned a rating to Leviathan Bond.

Leviathan Bond is a special purpose vehicle and the notes are secured on Delek Drilling Limited Partnership's (Delek Drilling) 45.34% working interest in the Leviathan gas project in Israeli waters and associated assets.

RATINGS RATIONALE

The Ba3 rating reflects, as positives, the substantial gas reserves in the Leviathan gas reservoir, which had 1P proved reserves of 322.4 billion cubic meters as of 30 June 2020, and the minimal anticipated ongoing maintenance capital requirements to maintain stable production. It is the largest gas reserve in Israel (Government of Israel, A1 stable) and an important contributor to the country's energy security. Based on forecast production, the sponsor expects the field to have an operating life of over 30 years.

The rating further benefits from long-term offtake agreements covering a substantial share of production until 2030, including minimum take-or-pay quantities and floor prices that mitigate exposure to weak Brent oil prices. However, the value of these agreements is limited by the weak credit quality of the offtakers, the largest of which are the National Electric Power Company, owned by the Government of Jordan (B1 stable) and Dolphinus Holdings, a new entity formed to import gas to Egypt (Government of Egypt, B2 stable).

The Leviathan field faces intense competition from other Israeli gas suppliers, including the Tamar field, which creates risk of oversupply in the regional market despite growing demand in Israel as electricity generation transitions from coal to gas. If offtakers exercise volume reduction options included in these agreements, volumes and/or achieved prices may decline below levels Moody's currently anticipates.

The rating is also constrained by Leviathan Bond's significant and frequent refinancing requirements. Debt Reserve and Principal Reserve Funds are small relative to the outstanding debt and, in the case of the Principal Reserve Fund, unfunded until twelve months before each bond maturity. Moody's expects that Leviathan Bond will need to refinance a significant share of each maturity, and notes that management has significant discretion to maintain or increase leverage, subject to certain covenants and a cap of \$2.5 billion. The proposed financing terms include fewer creditor protections than many other rated project financing transactions. Specifically, there are limited creditor step in and remedy rights and a single financial ratio covenant that relies on a third-party consultant's estimate of future profits.

The rating also takes into consideration the reservoir's location in a region and country exhibiting significant geopolitical risk, and operational problems in the first seven months of production, although Moody's expects these to be manageable and notes that they have not resulted in any major outages to date. Delek Drilling and the operator, Noble Energy Mediterranean Ltd, a subsidiary of Noble Energy, Inc. (Baa3 RUR-UPG), have a strong track record at the neighbouring Tamar field (22% owned by Delek Drilling and financed through Delek & Avner (Tamar Bond) Ltd., Baa3 negative) and the former Mari B field.

Although the project's long production life is a credit positive, debt may decline slowly if management chooses to prioritise distributions, and leverage may remain high into the late 2030s, when uncertainty over global gas demand will increase.

RATIONALE FOR STABLE OUTLOOK

The stable outlook reflects Moody's expectation that Leviathan Bond will achieve improving financial metrics, in particular the ratio of Funds From Operations (FFO) to debt, based on Delek Drilling's share of the Leviathan project's cash flow, supported by a successful ramp-up to full production and progressive deleveraging.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

The ratings could be upgraded if Leviathan Bond achieved FFO/debt sustainably above 25%, or if the Leviathan partners entered into material new take-or-pay gas sale and purchase agreements with high-quality offtakers that improved cash flow visibility.

The ratings could be downgraded if FFO/debt appeared likely to fall below the mid-teens in percentage terms, if cash flow visibility deteriorated, if targeted production levels were not achieved or subsequently disrupted, or if appears that Leviathan Bond will be unable to refinance maturities in a timely fashion.

The principal methodology used in these ratings was Generic Project Finance Methodology published in November 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1194215. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

The Leviathan gas field is an operating deepwater field in the Eastern Mediterranean off the coast of Israel. In February 2014, the Leviathan partners were granted a production lease for a term of 30 years with a 20-year extension option. At 30 June 2020, the field had 322 billion cubic metres of proven (1P) gas reserves.

Leviathan Bond Ltd. is a special purpose vehicle established to issue bonds secured by a first priority fixed pledge of Delek Drilling's 45.34% working interest in the Leviathan gas project as well as certain associated assets. Recourse against Delek Drilling is limited to the collateral pledged by the sponsor.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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At least one ESG consideration was material to the credit rating action(s) announced and described above.

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