RATING ACTION COMMENTARY

Fitch Assigns Leviathan Bond Ltd's Proposed Notes 'BB(EXP)' Expected Rating; Stable Outlook

Mon 27 Jul, 2020 - 10:05 AM ET

Fitch Ratings - London - 27 Jul 2020: Fitch Ratings has assigned Leviathan Bond Ltd's proposed notes of USD2.25 billion due between 2023 and 2030 an expected rating of 'BB(EXP)'. The Outlook is Stable.

The final rating is contingent upon the receipt by Fitch of final documents conforming to information already received as well as the final pricing and financial close on the proposed notes.

RATING RATIONALE

The rating reflects the project's high quality reserves, the use of commercially proven technology and strong operating set-up with Noble Energy Mediterranean Ltd (Noble Energy) providing the day-to-day operating services. At the same time, the offtake base limits the rating as the two largest offtakers, Dolphinus Holdings Limited (Dolphinus) in Egypt and National Electricity Production Company (NEPCO) in Jordan, which is backed by the Government of

Jordan, are viewed as having below investment grade credit standing. The Israeli offtake is diversified and we view the risk of contract renewal as low.

The project debt is structured as staggered bullet maturities, which are expected to be partially refinanced. This allows for some deleveraging over time, but exposes the project to a degree of refinancing risk, although there is a cash reserving mechanism.

KEY RATING DRIVERS

Diversified Offtake Base, Exposure To Lower-rated Counterparties: Revenue Risk - Midrange

The project benefits from a diversified offtake structure with long-term contracts with offtakers in Jordan and Egypt as well as currently 12 companies in Israel. The export volumes make up more than half of Leviathan gas sales and imply a reliance on the offtakers in Jordan and Egypt to perform on their payment obligations.

Leviathan's 15-year Gas Sales and Purchase Agreement (GSPA) with the Jordanian NEPCO is for an annual contracted quantity of 3BCM. NEPCO is the national electricity company of the Hashemite Kingdom of Jordan (BB-/Stable) and is wholly owned by the Jordanian Government. NEPCO is the sole carrier of electric power in the country. We view Leviathan's gas as strategically important to Jordan as the country does not have any domestic sources of energy other than renewables and is otherwise reliant on the import of relatively expensive LNG. Leviathan's piped natural gas is therefore important to the country's economic development, as reflected in the government's guarantee of NEPCO's obligations to Leviathan.

The project also has a 15-year GSPA with Dolphinus in place for the export increasing gradually to 4.7BCM per year to Egypt. Dolphinus is the local marketing company acting as the intermediary between Leviathan and the ultimate offtaker, the Egyptian Natural Gas Holding Company (EGAS, not rated). The GSPA expressly allows for the export of Leviathan gas as LNG in addition to domestic use. This provides a strong incentive for Egypt to make full use of the contractual volumes even as it develops its domestic gas fields in the Eastern Mediterranean.

Furthermore, East GAS together with Delek Drilling and Noble Energy acquired a 39% stake in the Eastern Mediterranean Gas Pipeline (EMG), which also gives it the exclusive right to transport gas through the EMG pipeline from Israel to Egypt. This demonstrates Egypt's intention to continue a long-term relationship with Leviathan.

We view the Israeli GSPAs as systemic in nature as the gas supply in Israel is currently limited to Tamar and Leviathan and Karish/ Tannin from 2021. Gas demand of the Israeli economy is forecast to grow significantly in the medium term with the gasification of the transport system and replacement of coal-fired power plants.

The project's volume risk is limited through the long-term nature of most offtake contracts, and the take-or-pay requirements under the GSPAs. The contracts also allow for additional sales in excess of contractual volumes if Leviathan has capacity to meet nominations.

The gas sales prices are based on various pricing formulas, including linkages to the electricity production tariff determined by the Public Utility Authority-Electricity for most GSPAs in Israel and the Brent barrel price for the NEPCO and Dolphinus GSPAs. This exposes the project to price risk, which is limited by the provision of floor prices set in the individual contract.

Experienced Operator: Operating Risk - Midrange

The operation of gas & oil facilities is at the higher end of complexity within the infrastructure space, but the project benefits from the presence of Noble Energy as an experienced operator of gas fields in the Eastern Mediterranean region with demonstrated performance on Tamar and the Yam Thetys/ Mari-B fields.

There is also a good alignment of interest with Delek Drilling through Noble Energy's participation as a partner in the Leviathan lease. Furthermore, the joint operating agreement clearly outlines the responsibilities of the parties.

The project uses commercially proven technology and a relatively high level of equipment redundancy. The project further benefits from the lessons learned on Tamar, which reduces outage risk.

Cost budgets are agreed between the operator and the Leviathan partners under the joint operation agreement, which should ensure good cost control. However, the project remains exposed to the risk of cost overruns.

Sufficient Resources, High Quality Reservoir: Supply Risk - Stronger

The technical advisor views Leviathan as a high quality gas reservoir with relatively strong drive mechanism that should result in the reservoir pressure to remain high, even as gas volumes reduce, as well as reducing the need for well drilling.

The reservoir is expected to produce 322 BCM in the 1P scenario, and 376 BCM in the 2P scenario as of June 2020. In the Fitch Rating Case (1P) the reservoir is expected to produce until 2064 without any further discoveries. Additional existing gas volumes currently classified as contingent (1C and 2C) will be added to the 1P and 2P reserves once additional wells are approved for drilling and the volumes become commercial, but no credit has been given to those volumes under the Fitch Rating Case.

New Assets, Expansion Outside Project Parameter: Infrastructure Development and Renewal - Midrange

Similarly to most other oil & gas fields, the operation of Leviathan will require investments to sustain production and address the operational issues that can be expected to arise in such complex ventures. Fitch believes the operator's experience means the field's operational and development requirements. will be appropriately managed and anticipated.

We do not expect that the project will have to raise additional finance to fund large capex requirements in our Fitch Rating Case. The works relating to the Phase 1B capacity extension involving the drilling of four additional wells are excluded from this financing.

Some Refinancing Risk: Debt Structure - Midrange

We assess Debt Structure as Midrange due to the senior secured nature of the debt, the absence of exposure to variable interest rates, swaps or other derivatives, which we view as stronger features, and significant exposure to refinancing risk, which is a weaker feature.

The cash flow servicing and securing the debt relate to the share (45.34%) of ownership interest that Delek Drilling has in the Leviathan gas field. This structure results in lower control over operationscompared with the standard project structure and is considered a weakness. We view the structure positively based on the strong alignment of interest between the partners and Noble Energy as operator and the clear provisions of the joint operating agreement.

Funds for debt service flow through accounts in the names of the Delek Drilling, which are separated from other company cash flows and pledged to the lenders. The debt issuance through a special purpose vehicle passes the issuance proceeds on to Delek and debt service is reliant on the back-to-back agreement with Delek Drilling on the basis of its pledge of the Leviathan working interest. As a listed company, Delek Drilling is, in our view, sufficiently insulated from any potential financial pressure at Delek Group Ltd. Moreover, Israeli bankruptcy law is protective of lenders' rights.

It is the intention of Leviathan Bond Ltd to raise USD2.25 billion. The bond documentation allows for total indebtedness of up to USD2.5 billion. The senior secured notes comprise staggered bullet maturities that allow the project to deleverage over time, but also provide the company with flexibility to refinance certain amounts over the project's long remaining operating term, in particular if larger reserves are confirmed and additional capex is required. The reserve accounts (the USD100 million debt payment fund funded from issuance proceeds and the principal reserve fund funded through cash trapping of up to USD150 million starting 12 months prior to a maturity) support debt service and allow for moderate deleveraging, justifying a Midrange assessment overall.

PEER GROUP

The closest peers in Fitch's portfolio are Dolphin Energy Ltd (DEL; A+/Stable) and Ras Laffan Natural Gas Company II & 3 (Rasgas; AA-/Stable). Both are large-scale natural gas producing projects in Qatar and benefit from a strong offtaker base and high resiliency to price declines given their low cost bases. In case of Rasgas, we also factor in its status as an integral part of Qatar's oil & gas industry. Initially both projects also had some bullet maturities, but these could be redeemed out of cash flow. Consequently the projects are rated well above Leviathan.

Financial Profile

We deem the project life cover ratio (PLCR), as a measure of debt service coverage, and net debt to EBITDA, as a measure of leverage, to be the most relevant financial metrics. The PLCR increases over time reflecting the long debt-free tail. The minimum FRC PLCR of 1.75x occurs in 2030. Net debt to EBITDA is gradually reducing.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- An upgrade is deemed unlikely at this stage. The project is exposed to lower rated counterparties.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- PLCR for the remaining operating life below 1.4x.

- Repeated or extended payment delays of NEPCO or Dolphinus, a marked deterioration of the political situation in the region or similar sustained external shocks that would threaten Leviathan's ability to continue gas exports to Jordan or Egypt.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579].

TRANSACTION SUMMARY

The project is a refinancing/monetisation of the sponsors' interest in the Leviathan gas reservoir. The Leviathan gas field is owned by Delek Drilling LP (45.34%), Noble Energy (39.7%) and Ratio Oil (15%). The stakes owned by Noble Energy and Ratio Oil are not subject to this refinancing.

The gas field was discovered in 2010 and reached first gas in 2019 on time and below budget. Phase 1A consists of 1,200MMscfd production capacity. The gas reservoir is located offshore Israel in the Eastern Mediterranean Sea, approximately 120km west of Haifa. The gas extracted from the wells is gathered at the field in a subsea manifold and delivered to an offshore fixed platform via 115km gathering flowlines. Gas to the domestic and export markets is transported from the platform via a pipeline to the Israel Natural Gas Lines onshore grid. Other gas exports may occur via additional pipelines connected to the fixed platform.

FINANCIAL ANALYSIS

Fitch Base Case: We assume a 2P production profile in Fitch's Base Case, Fitch's base case Brent price forecasts. For the gas price assume a price of USD4.7/mcf for 2020 for any uncontracted volumes. In the long term, we assume USD5.5/mcf for uncontracted volumes in line with the international hub prices.

We further apply a 5% stress on opex and capex. Interest rates for the refinance debt are increased between 25bp-100bp based on the debt term compared with current expected interest rates. We reflect Fitch's sovereign inflation assumptions.

Fitch Rating Case: In the Fitch Rating Case, we assume the 1P production profile, Fitch's stressed Brent price forecasts and a gas price of USD4.3/mcf for 2020 for any uncontracted volumes. In the long term we assume USD5.0/mcf for uncontracted volumes.

We further increase the stress on opex and capex to 10% reflecting a realistic downside scenario. Interest rates for the refinance debt and inflation rates are assumed in line with the Fitch base case.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

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.

RATING ACTIONS

ENTITY/DEBT	RATING		
Leviathan Bond Ltd			
• Leviathan Bond Ltd/Debt/1	LT	BB(EXP) Rating Outlook Stable	Expected Rating

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Infrastructure and Project Finance Rating Criteria (pub. 24 Mar 2020) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Third-party Model (24 March 2020)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

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Endorsement Policy

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Leviathan Bond Ltd	-

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Energy and Natural Resources Infrastructure and Project Finance Middle East

Asia-Pacific Europe Israel

MOODY'S
INVESTORS SERVICE

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

27 Jul 2020

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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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569 .

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

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Research Update:

Leviathan Bond Ltd.'s Proposed $2.25 Billion Senior Secured Notes Rated Preliminary 'BB-', Outlook Stable

July 27, 2020

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Rating Action Overview

- Leviathan Bond Ltd. (or the project) expects to issue up to $2.25 billion in senior secured notes in four bullet series with final maturities in 2023, 2025, 2027, and 2030.
- On July 27, 2020, S&P Global Ratings assigned its preliminary 'BB-' issue-level rating to the proposed notes. We also assigned a preliminary recovery rating of '1' to the notes.
- The preliminary rating incorporates a Sponsor Loan that Leviathan Bond will provide to Delek Drilling Limited Partnership (Delek Drilling), which is a 45.3% joint leaseholder of the Leviathan field that will generate the revenue for the repayment of the notes. The proceeds of the issuance will refinance Delek Drilling's $1.75 billion debt it raised for the field's deployment debt, fund a $100 million debt repayment fund, repayment of $300 million secured corporate debt and for general corporate purposes.
- The stable outlook reflects our expectation that the project will produce and sell approximately up to 12 billion cubic meter (BCM) annually, leading to a debt service coverage ratio (DSCR) of more than 3.0x in the next 24 months.

Project Description And Key Credit Factors

The Leviathan field is an offshore gas field located in the eastern Mediterranean, discovered in 2010, and is the largest natural gas reserve in Israel. According to a reserve report prepared by the independent engineering consultant, Netherland, Sewell & Associates Inc. (NSAI), the field has proved developed producing reserves (1P) totaling 11,577.3 billion cubic feet (BCF) of gas and 20.8 million barrels (MMbbl) of condensate oil as of December 2019, when it started producing an annual capacity of 12 BCM.

The rights to explore and produce petroleum and gas in the Leviathan field were granted proportion to Delek Drilling (45.34%), to Noble Energy Mediterranean Ltd. (Noble Energy; 39.66%), and Ratio Oil Exploration (15.00%) under a production lease until February 2044, which may be

extended by up to an additional 20 years in case partners continue to produce from the Leviathan field. The operations and associated infrastructure are defined under a joint operating agreement (JOA) among the three parties in the respective proportion in the Leviathan lease. The operations of the field are performed by Noble Energy under the terms defined in the Leviathan lease and JOA.

Given these unique characteristics, we rate the project based on our "Principles Of Credit Ratings" methodology. In particular, we have assessed the cash flow coverage according to Delek Drilling's 45.34% working interest and the JOA. The latter defines that operating committee proposals need to reach at least a 60% approval by the vote of two non-affiliate partners. Whereas there's no majority control by any party, we view the risk of Delek Drilling having a non-controlling stake as mitigated by this voting procedure, because decisions can't be reached without its vote. As such, the repayment of the notes will consist on the pro-rata revenue stream from the sale of gas and condensate produced at the field. We also acknowledge the risk of having Delek Drilling as part of the project under the sponsor loan. But we don't limit the rating on the notes to the credit quality of Delek Drilling, because we see cross-default mitigation in the project's structure, and the risk of default under the JOA as remote at this stage.

The Leviathan field closed long-term gas sales purchase agreements (GSPA) under export contracts that account for around 60%-70% of sales, and the rest with energy producers in Israel totaling approximately 10 BCM per year (85% of production capacity) until around 2035. Currently, 55% of the Leviathan field gas sales in 2020 are expected to be for National Electric Power Co (Nepco) in Jordan and to Dolphinus Holdings in Egypt, and the rest in Israel.

Strengths

- The Leviathan field has minimal resource risk, with 1P reserves sufficient to cover production capacity for over 30 years, according to information provided under a reserve report prepared by NSAI.
- An experienced and global player will undertake the operations of the asset. Noble has been operating similar projects with an approximately 99.7% availability in the adjacent field (Tamar) since 2013, which we view as credit positive. This underlines our view of stable production and low operating cost (below 10% of revenues).

Risks

- Despite a high contracted revenue base, we expect the project will remain exposed to market risk, which introduces some cash flow volatility. About 85% of the gas sales benefits from long-term GSPA with minimum 'take-or-pay' volumes at fixed price, floor-price, and escalating price depending on Brent or the domestic electricity production tariff (depending on the type of agreement). Nevertheless, we could only assess the credit quality of 40% of the contracted capacity. For the 60% remainder, we assume that gas is sold in the merchant market throughout the project's life, making expected cash flows available for debt service more volatile throughout the debt's term.
- Each note series has a bullet payment for the respective maturities in 2023, 2025, 2027, and 2030, increasing the refinancing risk to the project. Refinancing risk is partly offset, in our view, by a principal reserve fund that starts to be funded 12 months before the maturity of each series, but is limited at $150 million and the very long reserve tail.
- Default by Delek Drilling under the JOA might cause an interruption of cash flows to the project,

if not cured. We asses this risk as remote, because our analysis of the base- and downside-case scenarios considers that Delek Drilling has already performed all required payments in respect of the current stage of development of the Leviathan Project and does not have any material outstanding liabilities.

Rating Action Rationale

The preliminary rating mainly reflects the operational risk in the exploration of a gas field and a low market risk exposure. As we cannot asses the creditworthiness of some of the offtakers, we assume that 60% of gas produced will be dispatched in the market, exposing the project to volume and price risk, and consequently to fluctuating cash flows.

Despite our view that the project will generate relatively predictable cash flow from the GSPA, we lack clear visibility on the quality of this cash flow, because around 60% of the offtakers (we exclude all volume sold to Dolphinus under its respective contract) are unrated or do not publicly share sufficient financial information in order for us fully assess. As such, we only consider the GSPA of 40% of the contracted capacity to the offtakers that we were able to assess its credit quality (including the portion sold to Nepco), and the remainder as exposed to market risk.

Therefore, our base-case scenario assumes 60% of sales exposed to international market prices for gas, whereas Leviathan's contracts have floor prices. This scenario assumes a minimum annual DSCR of 1.45x in 2025 and an average of 1.74x until the end of the refinancing period, which we define as 2044, when the lease agreement matures.

We view positively the extensive experience that Noble Energy has in operating in the region, performing with over a 99% availability in the adjacent field (Tamar) since it started operations in 2013, while maintaining gas production costs in the first cost quartile. We estimate the project's gas production cost below $0.5 per million cubic feet (mcf) and annual operating expenditure (opex) around $80 million (Delek Drilling share).

The capital structure consists of several bullet maturities, partially synthesizing an amortizing repayment profile. To ensure that sufficient funds are available to meet each bullet maturity, 12 months ahead of each amortization date, free cash flow from the Revenue Account are reserved to a principal reserve fund that accumulates cash of up to $150 million. In our view, the long life of 1P provides a sufficient tail for refinancing of the notes. As such, the exposure to refinancing risk in 2023, 2025, 2027, and 2030 doesn't constrain the preliminary rating on the notes.

Finally, despite 30% of the project's gas sales to Jordan (B+/Stable/B), the rating on the latter doesn't limit the preliminary rating on the project. This is because Leviathan Bond comfortably passes a hypothetical sovereign stress scenario (the project's cash sources-to-uses ratio remains above 1.0x under the exercise due the low operating cost of the field, the bullet debt payments, and existence of debt reserve accounts). All payments are deposited in accounts in Israel, all cash is held offshore Jordan, compensating for the foreign-exchange conversion risk. We didn't apply the typical cash haircut, because all cash is held in Israel, invested under permitted investment-grade titles.

The rating on the notes is preliminary and the assignment of the final rating will depend on our receipt and satisfactory review of all final transaction documentation, while the interest rate on the notes would need to be in line with our expectations. Accordingly, the preliminary rating shouldn't be construed as evidence of the final rating. If we don't receive the final documentation within a reasonable timeframe, or if the final transaction departs from our assumptions, we reserve the right to withdraw or change the rating.

Outlook

The stable outlook reflects our assessment that Leviathan's operations shouldn't encounter substantial setbacks, and that the project has contracted a reasonable proportion of its production capacity at fixed price. Given the bullet nature of the notes, we expect the project to generate DSCRs above 3.0x in the next two years.

Downside scenario

We could lower the preliminary rating if the operations encounter production issues, resulting in lower uptime and higher operating cost, reducing minimum DSCR below 1.4x. In addition, we could revise our gas price assumption if conditions in the oil and gas industry continue to deteriorate, making it difficult for the project to sell its production capacity at favorable prices, leading to lower cash flows. We could also lower the rating if the credit quality of the offtakers deteriorate, in particular Jordan, which guarantees Nepco's GSPA.

Finally, a negative rating action could occur if the partners of the field were to engage in aggressive expansion commitments, which could reduce the net cash flows for the repayment of the notes, and result in extraordinary obligations to Delek Drilling pay its Participating Interest in related joint account expenses.

Upside scenario

We could raise the preliminary rating if the project sells its remaining capacity to counterparties of stronger creditworthiness, reducing its market risk exposure and enhancing the blended average credit quality of its revenue stream, which could reduce risks and even raise minimum DSCR above 1.5x.

Performance Update

The asset started operations in December 2019, and has presented an average uptime of 97%. We estimate stable operations going forward with uptime above 99%.

Month	Monthly uptime of Leviathan filed (%)
January 2020	92.6
February 2020	98.8
March 2020	94.4
April 2020	99.0
May 2020	98.7
June 2020	99.3

Source: Delek Drilling

Base Case

Assumptions

- Annual sales capacity of 12 BCM, 40% of which go to Nepco and some offtakers in Israel, and the remainder at our assumptions on Henry Hub prices as specified below, as we exclude the contracted conditions with the counterparties that we could not assess its respective credit quality (including Dolphinus in Egypt and other energy producers in Israel).
- Prices to rise in line with the combination of the production component of the electricity tariffs set by the Israeli Electricity Authority (EA) and Brent according to the terms of the GSPAs.
- S&P Natural Gas Henry Hub deck price: $2/MMBTU in 2020, $2.25/MMBTU in 2021, and $2.5/MMBTU starting in 2022, and Brent deck price: $30/bbl in 2020, $50/bbl in 2021 and $55/bbl starting in 2022, according to "S&P Global Ratings Cuts WTI And Brent Crude Oil Price Assumptions Amid Continued Near-Term Pressure," published March 19, 2020.
- A fixed interest rate of 6%-7% for the proposed notes.
- Operations and maintenance (O&M) costs in line with historical performance of the operator, adjusted to U.S. inflation, including variable cost of $0.5 per MCF and opex around $80 million per year for Delek Drilling share.
- U.S. CPI of 0.7% in 2020, 1.4% in 2021, 2.0% in 2022, and 1.8% in 2023 according to "Credit Conditions North America: Rolling Out The Recovery," published June 30, 2020.
- Budgeted remaining capex around $240 million (for the partners) until 2022 to finalize the ramp-up of the field. No expansion capex afterward.
- Refinancing of each bullet series at 200 basis points (bps) higher spread, with an amortizing loan until the end the lease agreement in 2044.

Key metrics

- Minimum DSCR of 1.45x in 2025 and average DSCR of 1.74x after the first bullet refinancing.

Downside Case

Assumptions

- 10% lower annual production.
- 10% lower gas market prices, and floor prices under the GSPA.
- 10% higher variable and fixed operating costs, including stress over insurance.
- Higher U.S. CPI by 100 bps, affecting costs.

Key metrics

- Minimum DSCR of 0.86x in 2025.

We factor into our downside-case scenario the project's ability to mitigate impacts on cash flows that could stem from operating risks, such as lower production, and higher operating and maintenance expenses. Cash flow could also fall due to external events such as Brent reference prices (subject to floor prices), inflation rates, and insurance costs, particularly because of the project's single-asset nature.

We assess the project's resilience in a stress case as neutral to the transaction, because Leviathan Bond would be able to maintain the timely debt service payments during four years before completely depleting the reserve provisions.

Operations phase stand-alone credit profile (SACP)

Our operations phase SACP reflects our view of the operating risk typical of a gas exploration field, which we view as relatively moderate ('4' in scale of '1' as lowest to '10' as highest). We incorporate our view the project's exposure to market risk and the offtaker's credit quality as a key factor for the preliminary rating on the debt.

We assess the operations phase SACP as 'bb-' based on:

- The project's operations phase business assessment (OPBA) as '8'.
- Minimal exposure to resource risk, because 1P reserves total 11,577.3 BCF of gas and 20.8 MMbbl of oil, sufficient to cover more than 30 years of production.
- Low market risk exposure. Even though the project has 85% of production contracted under long-term GSPA with minimum take-or-pay and at fixed price, we only assume contracted capacity for 40%, because we can't determine the credit quality of the cash flows stemming from 60% of these contracts.
- The downside resilience is supported by the $100 million debt payment fund amid exposure to refinancing risk on each of the bullet maturities. Whereas there's a principal reserve fund to accumulate funds to repay each maturity, it only starts to be seeded by the operating cash flows 12 months in advance of each maturity and it's limited to $150 million.
- As a result, the operations phase SACP is driven by minimum DSCR of 1.45x in 2025.

Counterparties

We view the offtakers of GSPA and the O&M operator of the project as material counterparties, but neutral to the preliminary rating.

On the revenue side, we calculated the blended average credit quality of the offtakers, which resulted in 'bb-'.

Our counterparty analysis of Nepco mirrors the ratings on its parent, Jordan (B+/Stable/B), because it provides a timely guarantee for the due payment of Nepco's obligations under the GSPA. We also included some of the Israeli offtakers, namely IPM Beer Tuvia Ltd., Paz Ashdod Refinery Ltd., Israel Chemicals Ltd. (BBB-/Stable), and Israel Electric Corp Ltd. (BBB/Stable).

We view Noble Energy Mediterranean (a wholly-owned subsidiary of Noble Energy) as an irreplaceable O&M counterparty. Despite the existence of other operators that could perform the same services, we view the unique characteristics of the lease agreement and JOA as tied to the obligations devoted to Noble Energy as the operator under these contracts. In addition, absent of O&M reserve account, we don't view financial flexibility for replacement.

Lastly, the account bank will be the Tel Aviv branch of HSBC Bank PLC. The documented replacement language is not consistent with our financial counterparty criteria. However, our 'A+' rating on the counterparty assessed in line with our criteria applicable to bank branches doesn't currently pose a constraint to the preliminary rating on the notes.

Liquidity

- We assess the project's liquidity as neutral given a cash-funded $100 million debt repayment fund. Even though this is not a standard debt service reserve account, the resources are sufficient to cover more than one semi-annual interest payment of the all series of the notes.
- Additionally, the issuer accumulates cash one year ahead of any scheduled principal repayment, under a principal reserve fund, which it will use along with the debt payment fund and the cash flows to repay the bullet notes as they become due. The principal reserve fund is limited to a $150 million maximum amount.

The project is not subject to financial covenants, which could cause an event of default or an acceleration of the notes payment. The transaction structure has a forward-looking distribution lock-up test, based on 1.5x NPV10/net debt test (remaining net present value discounted at 10%, according to the reserve consultant report, however based on lower Brent prices). Whereas we typically expect lock-up mechanism within the next 12 months of operations to allow for seasonality and volatile cash flows and to effectively preserve additional cash to meet project liquidity needs, we view the proposed lock-up mechanism as neutral.

Rating Score Snapshot

Construction phase SACP (Senior Debt)

- Not under construction

Operations phase SACP (Senior Debt)

- Operations phase business assessment: 8 (on a scale of '1' [lowest risk] to '12' [highest risk])
- Preliminary SACP: bb-
- Downside impact on preliminary SACP: bb (no impact)
- Liquidity: Neutral
- Comparative analysis assessment: Neutral
- Adjusted preliminary operations phase SACP: bb-
- Operations counterparty ratings adjustment: bb-

- Financial counterparty ratings adjustment: A+ [1]
- Operations phase SACP: bb-

Modifiers (Senior Debt)

- Parent linkage: De-linked
- Structural protection: Neutral
- Sovereign rating limits: BB (not capped)
- Senior debt issue rating: BB- (prelim)

[1]HSBC Bank is the Trustee and the Account Agent.

Recovery Analysis

Key analytical assumptions

- S&P Global Ratings believes that lenders would achieve the greatest recovery amounts through reorganization of the project, rather than liquidation, given consistent demand for gas in the region.
- The preliminary '1' (95%) recovery rating indicates that we expect full recovery in this default scenario.
- We value the asset using the net present value of future cash flows of the field's expected remaining life through 2044, when the lease agreement end.

Simulated default assumptions

Simulated default year: 2023

- Our hypothetical default contemplates deterioration of the oil and gas industry in 2023, when the project is expected to refinance the first series of the new notes. The failure to place new notes would be the trigger point for a potential default.
- Our recovery forecast assumes there would continue to be a viable business model driver by the continued demand for gas in the region and the strength of the project's historically solid operations, supporting its ability to protect the existing GSPA.
- We discount the cash flow over the remaining life of the charter at a 15% rate (even though we typically discount at 10% based on the valuation method that follows the U.S. Securities and Exchange Commission guidance, we use a higher discount rate in this analysis, because 40% of volumes were assumed sold under contracted prices higher than the commodity benchmark and other commonly parameters used in the industry), and deduct 5% of administrative expenses to arrive at the net value.
- We add six-month pre-petition interest to the estimated debt at the time of default.

Simplified waterfall

- Debt outstanding at the hypothetical default (including pre-petition interest): $2.0 billion
- Estimated net value of the project: $2.3 billion
- Recovery expectations: Rounded to 100% (recovery rate of '1'- 95%).

Related Criteria

- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Criteria | Corporates | Project Finance: Project Finance Framework Methodology, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Project Finance Operations Methodology, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Project Finance Transaction Structure Methodology, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Key Credit Factors For Oil And Gas Project Financings, Sept. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, Oct. 24, 2013
- Criteria | Corporates | Project Finance: Project Finance Construction And Operations Counterparty Methodology, Dec. 20, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

New Rating	
Leviathan Bond Ltd.	
Senior Secured	BB-(prelim)/Stable
Recovery Rating	(prelim)1(95%)

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