

Rating Action: Moody's affirms TMK's ratings; changes the outlook to negative

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London, 15 December 2014 -- Moody's Investors Service, (Moody's) has today affirmed the B1 corporate family rating (CFR) of OAO TMK (TMK) and the rating of TMK Capital S.A., the issuer of senior unsecured loan participation notes issued for the sole purpose of financing loans to TMK. TMK's probability of default rating (PDR) is affirmed at B1-PD. The outlook is changed to negative from stable on all ratings.

RATINGS RATIONALE

The change in outlook is driven by falling oil prices, which make it more challenging for TMK to meet the credit metrics set for its current rating in the next 12 to 18 months. Brent oil price dropped by 41% to 66 \$/bbl in December 2014 from 112 \$/bbl in June 2014 on supply/demand imbalance owing to growing supply from North America, Libya and Nigeria. This imbalance will drive down oil country tubular goods (OCTG) prices and negatively affect oil drilling activity. This poses downside risk to 2015 financial results and might delay deleveraging. The company's leverage as measured by Moody's-adjusted total debt/EBITDA increased to 4.4x as of 30 September 2014 from 4.0x as of 31 December 2013, while Moody's-adjusted EBITDA margin fell to 13.7% in nine months 2014 from 15.0% in 2013. Geopolitical tensions between Russia and the EU/US over Ukraine, Russian oil and gas majors being subject to EU/US sanctions including a ban on the provision of financing and a ban on certain services necessary for deep-water oil exploration and production, arctic oil exploration or production and shale oil projects in Russia, create additional downside risks.

TMK's B1 corporate family rating (CFR) reflects exposure to the oil and gas sector, which can lead to wide swings in demand for OCTG and line pipes and cause volatility in TMK's profitability and leverage. In addition the rating is constrained by (1) a sharp decrease in oil prices during 2014, which might exert negative pressure on demand for OCTG and/or line pipes in Russia and US -- the company's key markets; (2) ruble devaluation during 2014, which will cause domestic deliveries' profitability to deteriorate unless prices are gradually adjusted as revenue in hard currency comprises less than 50% of the company's revenue; (3) volatility of steel prices; (4) TMK's high leverage; and (5) the company's liquidity profile with substantial maturities in 2015 and 2016 and high dependence on covenanted committed lines of credit.

However, the rating also captures TMK's (1) leading market position in Russia and US, especially in high margin seamless OCTG pipes; (2) geographical diversification, with meaningful production assets in North America and Europe; (3) favorable cost profile, which will be further supported by ruble devaluation partially counterbalancing the negative effect on revenue; (4) substantial unutilized credit facilities and Moody's assumption of continuing support from Russian state-owned and private banks; and (5) the company's efforts to increase the share of export sales, which will support its profitability metrics over longer-term.

Sharp ruble devaluation since the beginning of 2014 will have a moderately negative effect on the company's financial metrics. The company estimates that approximately 40% of revenue, 35% of operating expenses, 65% of debt and 50% of capex are denominated in foreign currency. Decreased dollar-denominated revenue in the domestic market will be partially counterbalanced by lower costs, while management's efforts to ramp up export deliveries and implement price hikes in the domestic market, mitigates the negative effect of ruble devaluation on EBITDA and cash flows.

RATING OUTLOOK

The negative rating outlook is in line with negative global outlooks for 2015 for the oil exploration and production, as well as drilling and oil field services sectors. Ruble volatility and the potentially negative effect of EU/US sanctions on the drilling programs of Russian oil and gas majors are additional drivers. Recovering oil prices, underpinning robust drilling activity and OCTG prices in Russia and US with leverage, as measured by Moody's-adjusted debt/EBITDA falling to below 4.0x, supported by ruble strengthening, might lead to a stabilisation of the outlook.

WHAT COULD CHANGE THE RATING UP/DOWN

The upgrade of the company's rating is unlikely given the negative outlook. However, TMK's rating could be upgraded if the company is able to (1) generate positive free cash flow; (2) reduce leverage as measured by

Moody's-adjusted debt/EBITDA to below 2.75x on a sustainable basis; and (3) maintain good liquidity.

A rating downgrade could be triggered by (1) a failure to generate positive free cash flow on a rolling 12-month basis; (2) leverage as measured by Moody's-adjusted debt/EBITDA exceeding 4.0x on a sustainable basis; (3) lack of recovery in oil prices and evidence of curtailments of drilling programs by oil and gas companies; and (4) liquidity profile deterioration.

PRINCIPAL METHODOLOGIES

The principal methodology used in these ratings was Global Steel Industry published in October 2012. Other methodologies used include Loss Given Default for Speculative-Grade Non-Financial Companies in the U.S., Canada and EMEA published in June 2009. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

OAQ TMK is Russia's largest producer - and one of the world's largest producers - of steel pipe products for the oil and gas industry, operating around 30 production sites across the US, Russia, Romania and Kazakhstan. The largest proportion of TMK's shipments comprises high-margin Oil Country Tubular Goods (OCTG), encompassing tubing, casing and drill pipes, complemented with line pipe, large-diameter pipe and industrial pipe also in the company's sales mix, including pipes with the entire range of premium connections. More than half of TMK's sales by volume, are of seamless pipe. In nine months 2014, TMK shipped approximately 3.2 million tonnes of steel pipes, including 1.9 million tonnes of seamless pipes. The company reported revenues of approximately \$4.5 billion and EBITDA of around \$0.6 billion over the same period. TMK's largest shareholder is Mr. Dmitriy Pumpyanskiy, who owns an approximate 70% stake in the company.

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