

Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

February 10, 2004

Standard Oil

Summary and Recommendation

ExxonMobil (XOM) at a McDep Ratio of 0.95 is an attractive stock to own in our opinion helping make the case for all of our buy recommendations at lower McDep Ratios. Cash flow multiples implied by the value of energy resources in the denominator of the McDep Ratio are on the same standard for ExxonMobil and its four mega cap peers. Our valuation of producer/refiners and independent producers implies a discount to the ExxonMobil standard that appears increasingly inappropriate in the rising commodity price environment we now seem to be facing. That suggests our valuation may be understated for buy recommendations including large cap independents **Burlington Resources (BR)**, **Anadarko (APC)** and **Encana (ECA)** and small cap **Encore Acquisition (EAC)**.

Cash Flow Multiple Correlates with Reserve Life

Variations in cash flow multiple correlate with adjusted reserve life for natural gas and oil producers. The degree of variation explained is 80% or more for large independent producers. The correlation coefficient is about 50% for the six mega cap producers even before taking account of non-producing, or downstream operations. The correlation is lower for producer/refiners suggesting extra potential in non-North American companies in that group.

Assessed Multiples Higher than Market Multiples

Those relationships apply to the cash flow multiple determined by the market (EV/Ebitda). We draw on adjusted reserve life in assessing cash flow multiples (PV/Ebitda). Applying an assessed multiple to next twelve months cash flow is our main technique for estimating present value when we don't have a more detailed discounted cash flow analysis. Estimates of one-year cash flow incorporate latest one-year futures prices. Dividing market cap and debt by unlevered present value yields the McDep Ratio.

While both assessed multiples and market multiples depend on adjusted reserves/production, assessed multiples are higher than market multiples. We justify the difference on the belief that we are in a rising commodity price environment for the next several years.

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Mega Cap Premium in Valuation Multiples

Mega caps are valued more than one multiple higher than producer/refiners or independent producers. The current median EV/Ebitda and PV/Ebitda multiples are 7.0, 5.7, 5.2 and 8.3, 6.6, 6.5 respectively (see Table 1-2). The assessments of producer/refiners and independent producers are internally consistent, but could be at higher multiples leading to lower McDep Ratios if we further applied the Exxon standard.

Essentially we are applying an Exxon standard at the mega cap high end. Our currently assessed multiple applied to cash flow estimates taking account of latest results gets us to a McDep Ratio less than 1.0 for ExxonMobil. The four other mega caps are assessed consistent with the Exxon standard.

Perhaps a mega cap premium is justified by lower risk. That might also mean that an energy portfolio concentrated entirely on mega caps would earn a lower return. We advocate an energy portfolio with a mega cap anchor, but disproportionately weighted to non-mega caps.

Kurt H. Wulff, CFA

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Table 1-1
Energy Producers
Rank by McDep Ratio: Market Cap and Debt to Present Value

	Symbol/ Rating	Price (\$/sh) 9-Feb 2004	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio	
Mega Cap								
Exxon Mobil Corporation	XOM	40.73	6,612	269,000	43.00	0.08	0.95	
Total S.A.	TOT	91.70	1,261	115,600	105.00	0.17	0.89	
BP plc	BP	48.40	3,682	178,000	60.00	0.13	0.83	
Royal Dutch/Shell	RD	B	47.53	3,389	161,000	60.00	0.18	0.83
ChevronTexaco Corporation	CVX	B	85.78	1,064	91,300	110.00	0.17	0.82
	<i>Total or Median</i>			815,000		0.17	0.83	
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S	59.90	124	7,430	14.00	0.80	1.64
Imperial Oil Limited (30%)	IMO		45.12	111	5,010	43.00	0.12	1.04
Murphy Oil Corporation	MUR		61.56	93	5,710	62.00	0.20	0.99
Valero Energy Corporation	VLO		53.60	120	6,430	55.00	0.42	0.99
ENI S.p.A.	E		96.22	755	72,700	108.00	0.17	0.91
Suncor Energy	SU		25.42	475	12,070	30.00	0.12	0.87
Petro-Canada	PCZ		45.55	265	12,070	54.00	0.12	0.86
ConocoPhillips	COP	B	66.17	680	45,000	88.00	0.33	0.83
Petroleo Brasileiro S. A.	PBR		30.63	1,096	33,600	40.00	0.28	0.83
PetroChina Company Ltd (10%)	PTR	B	51.66	176	9,080	65.00	0.09	0.81
Marathon Oil Corporation	MRO	B	32.54	311	10,110	47.00	0.27	0.78
Lukoil Oil Company	LUKOY	B	101.30	211	21,000	140.00	0.07	0.74
Norsk Hydro ASA	NHY	B	64.58	257	16,600	95.00	0.19	0.74
	<i>Total or Median</i>			257,000		0.19	0.86	
Independent Natural Gas and Oil								
Occidental Petroleum Corp.	OXY		44.11	391	17,300	50.00	0.26	0.91
Pogo Producing Company	PPP		42.30	64	2,710	50.00	0.10	0.86
Apache Corporation	APA		38.39	324	12,400	47.00	0.19	0.85
CNOOC Limited (19%)	CEO	B	40.78	78	3,180	48.00	-	0.85
XTO Energy Inc.	XTO	B	26.61	186	4,960	33.00	0.19	0.84
Canadian Natural Resources Limited	CNQ		50.93	137	6,980	72.00	0.33	0.80
Unocal Corporation	UCL		36.84	273	10,100	52.00	0.28	0.79
Pioneer Natural Resources Company	PXD		30.50	119	3,630	45.00	0.26	0.76
Encana Corporation	ECA	B	39.57	470	18,600	56.00	0.18	0.76
Anadarko Petroleum Corp.	APC	B	50.47	252	12,700	76.00	0.25	0.75
Burlington Resources	BR	B	54.50	198	10,800	80.00	0.21	0.75
Devon Energy	DVN		53.70	242	13,000	90.00	0.30	0.72
	<i>Total or Median</i>			116,000		0.23	0.80	
Service								
Baker Hughes Inc.	BHI		34.70	336	11,700	30.00	0.07	1.15
Halliburton Company	HAL		30.03	435	13,100	28.00	0.28	1.05
Schlumberger Ltd.	SLB		62.13	585	36,300	60.00	0.17	1.03
	<i>Total or Median</i>			61,000		0.17	1.05	

Buy/Sell rating after symbol: B - Buy, S - Sell

McDep Ratio = Market cap and Debt to present value of oil and gas and other businesses

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Table 1-2

Energy Producers

Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

	Symbol/ Rating	Price (\$/sh) 9-Feb 2004	EV/ Sales NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)	PV/ Ebitda NTM	
Mega Cap								
Exxon Mobil Corporation	XOM	40.73	1.1	7.9	15	2.5	8.3	
Total S.A.	TOT	91.70	1.2	7.5	15	4.1	8.4	
BP plc	BP	48.40	0.9	7.0	14	3.2	8.4	
ChevronTexaco Corporation	CVX	B	85.78	0.9	6.4	12	3.4	7.9
Royal Dutch/Shell	RD	B	47.53	1.0	6.3	16	4.6	7.6
	<i>Median</i>		<i>1.0</i>	<i>7.0</i>	<i>15</i>	<i>3.4</i>	<i>8.3</i>	
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S	59.90	2.9	12.9	18	2.7	7.8
Imperial Oil Limited (30%)	IMO		45.12	1.4	7.9	16	1.5	7.5
Murphy Oil Corporation	MUR		61.56	1.6	7.6	19	1.3	7.7
Suncor Energy	SU		25.42	2.8	7.5	14	0.6	8.7
Valero Energy Corporation	VLO		53.60	0.3	6.5	10	0.9	6.6
ConocoPhillips	COP	B	66.17	0.7	6.2	10	2.6	7.4
ENI S.p.A.	E		96.22	1.5	5.7	12	4.9	6.3
Marathon Oil Corporation	MRO	B	32.54	0.4	5.3	10	3.1	6.8
PetroChina Company Ltd (10%)	PTR	B	51.66	2.6	4.8	10	4.0	5.9
Petro-Canada	PCZ		45.55	1.6	4.6	13	1.0	5.4
Norsk Hydro ASA	NHY	B	64.58	0.8	4.4	12	2.4	5.9
Petroleo Brasileiro S. A.	PBR		30.63	1.7	4.1	5	3.3	5.0
Lukoil Oil Company	LUKOY	B	101.30	1.0	4.1	6	2.5	5.5
	<i>Median</i>		<i>1.5</i>	<i>5.7</i>	<i>12</i>	<i>2.5</i>	<i>6.6</i>	
Independent Natural Gas and Oil								
CNOOC Limited (19%)	CEO	B	40.78	4.8	6.1	12	3.9	7.1
XTO Energy Inc.	XTO	B	26.61	4.3	5.7	10	0.2	6.7
Anadarko Petroleum Corp.	APC	B	50.47	3.7	5.5	11	1.1	7.4
Occidental Petroleum Corp.	OXY		44.11	2.5	5.4	9	2.4	5.9
Pioneer Natural Resources Company	PXD		30.50	3.8	5.3	14	-	6.9
Unocal Corporation	UCL		36.84	2.5	5.2	11	2.2	6.5
Encana Corporation	ECA	B	39.57	2.5	5.2	13	0.8	6.8
Apache Corporation	APA		38.39	3.4	4.9	10	0.6	5.7
Burlington Resources	BR	B	54.50	3.4	4.8	11	1.1	6.4
Canadian Natural Resources Limited	CNQ		50.93	3.3	4.6	10	0.9	5.8
Pogo Producing Company	PPP		42.30	2.6	3.7	9	0.5	4.3
Devon Energy	DVN		53.70	3.1	3.7	8	0.4	5.2
	<i>Median</i>		<i>3.3</i>	<i>5.2</i>	<i>10</i>	<i>0.8</i>	<i>6.5</i>	
Service								
Halliburton Company	HAL		30.03	1.1	12.8	27	1.7	12.1
Baker Hughes Inc.	BHI		34.70	2.3	12.6	32	1.3	11.0
Schlumberger Ltd.	SLB		62.13	3.1	11.0	38	1.2	10.7
	<i>Median</i>		<i>2.3</i>	<i>12.6</i>	<i>32</i>	<i>1.3</i>	<i>11.0</i>	

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended December 31, 2004; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Table 1-3
Energy Producers
Determinants of Present Value

	Symbol/ Rating		NG & O Prod/ Ebitda (%)	N. Am. Gas/ Ebitda (%)	Adjusted Reserves/ Prod NTM	PV/ Ebitda NTM	NG&O Ebitda/ mcf	McDep Ratio 9-Feb 2004
Mega Cap								
Royal Dutch/Shell	RD	B	75	5	8.5	7.6	2.95	0.83
Total S.A.	TOT		76	1	9.3	8.4	2.67	0.89
BP plc	BP		78	12	10.3	8.4	2.99	0.83
ChevronTexaco Corporation	CVX	B	81	12	10.4	7.9	2.55	0.82
Exxon Mobil Corporation	XOM		70	10	10.9	8.3	2.78	0.95
		<i>Median</i>	76	10	10.3	8.3	2.78	0.83
Producer/Refiners - Large Cap and Mid Cap								
Valero Energy Corporation	VLO		-	-		6.6		0.99
Petro-Canada	PCZ		82	23	7.2	5.4	2.11	0.86
Murphy Oil Corporation	MUR		92	29	7.3	7.7	3.33	0.99
Marathon Oil Corporation	MRO	B	69	23	8.7	6.8	2.58	0.78
Norsk Hydro ASA	NHY	B	66	-	8.9	5.9	1.03	0.74
Petroleo Brasileiro S. A.	PBR		93	-	9.9	5.0	2.43	0.83
ENI S.p.A.	E		53	-	9.9	6.3	2.41	0.91
Imperial Oil Limited (30%)	IMO		71	18	10.2	7.5	2.23	1.04
ConocoPhillips	COP	B	67	13	11.2	7.4	2.27	0.83
PetroChina Company Ltd (10%)	PTR	B	78	-	16.0	5.9	3.96	0.81
Suncor Energy	SU		93	9	19.0	8.7	2.95	0.87
Lukoil Oil Company	LUKOY	B	46	-	20.0	5.5	0.74	0.74
Kinder Morgan, Inc.	KMI	S	6	-		7.8		1.64
		<i>Median</i>	69	-	9.9	6.6	2.41	0.86
Independent Natural Gas and Oil								
Pogo Producing Company	PPP		100	35	5.8	4.3	3.32	0.86
Canadian Natural Resources Limited	CNQ		100	50	7.2	5.8	2.47	0.80
Devon Energy	DVN		100	61	7.4	5.2	3.96	0.72
Apache Corporation	APA		100	45	8.1	5.7	3.42	0.85
Unocal Corporation	UCL		100	34	8.4	6.5	3.12	0.79
Encana Corporation	ECA	B	98	71	9.0	6.8	2.62	0.76
XTO Energy Inc.	XTO	B	100	88	9.5	6.7	3.73	0.84
Burlington Resources	BR	B	100	71	10.3	6.4	3.14	0.75
Pioneer Natural Resources Company	PXD		100	65	10.3	6.9	2.93	0.76
CNOOC Limited (19%)	CEO	B	100	-	10.7	7.1	3.57	0.85
Anadarko Petroleum Corp.	APC	B	100	56	10.9	7.4	2.98	0.75
Occidental Petroleum Corp.	OXY		90	18	10.9	5.9	3.55	0.91
		<i>Median</i>	100	53	9.3	6.5	3.23	0.80

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Table 2-1
Independent Natural Gas and Oil Producers - Small Cap
Rank by McDep Ratio: Market Cap and Debt to Present Value

	<i>Symbol/ Rating</i>	<i>Price (\$/sh) 9-Feb 2004</i>	<i>Shares (mm)</i>	<i>Market Cap (\$mm)</i>	<i>Net Present Value (\$/sh)</i>	<i>Debt/ Present Value</i>	<i>McDep Ratio</i>	
Short Life								
Spinnaker Exploration Company	SKE	35.60	33.9	1,210	28.00	0.08	1.25	
Southwestern Energy Company	SWN	20.51	36.0	740	21.00	0.28	0.98	
Newfield Exploration Company	NFX	48.52	56.0	2,720	52.00	0.24	0.95	
Western Gas Resources	WGR	46.35	37.0	1,720	50.00	0.17	0.94	
Energy Partners Ltd.	EPL	13.86	36.9	511	15.00	0.19	0.94	
Stone Energy Company	SGY	43.10	26.6	1,150	58.00	0.23	0.80	
Chesapeake Energy Corporation	CHK	12.34	220	2,710	18.00	0.35	0.79	
Denbury Resources Inc.	DNR	14.45	55.7	810	20.00	0.25	0.79	
Westport Resources Corporation	WRC	30.20	68.0	2,050	42.00	0.22	0.78	
Range Resources Corporation	RRC	10.15	57.0	580	15.00	0.32	0.78	
Cimarex Energy Company	XEC	B	26.05	42.0	1,090	35.00	0.00	0.74
St. Mary Land and Exploration Company	SM	28.68	29.0	830	43.00	0.12	0.71	
The Houston Exploraton Company	THX	36.36	31.0	1,130	55.00	0.13	0.70	
Forest Oil Corporation	FST	25.96	49.0	1,270	45.00	0.30	0.70	
	<i>Total or Median</i>			<i>18,500</i>		<i>0.23</i>	<i>0.79</i>	
Long Life								
Ultra Petroleum Corp.	UPL	22.95	78.0	1,790	16.00	0.08	1.40	
Unit Corporation	UNT	25.80	43.7	1,130	22.00	0.02	1.17	
Penn Virginia Corporation	PVA	54.78	9.1	500	56.00	0.17	0.98	
Quicksilver Resources Inc.	KWK	34.98	23.0	810	37.00	0.25	0.96	
Berry Petroleum Company	BRY	19.07	22.1	421	22.00	0.12	0.88	
Swift Energy Company	SFY	16.94	27.4	460	22.00	0.37	0.86	
Whiting Petroleum Corporation	WLL	19.42	18.7	360	25.00	0.27	0.84	
Encore Acquisition Corp.	EAC	B	25.50	30.3	773	33.00	0.13	0.80
Evergreen Resources, Inc.	EVG	32.50	44.0	1,430	42.00	0.12	0.80	
Magnum Hunter Resources, Inc.	MHR	8.77	68.0	600	15.00	0.38	0.74	
Vintage Petroleum, Inc.	VPI	12.68	63.0	800	27.00	0.32	0.64	
	<i>Total or Median</i>			<i>9,100</i>		<i>0.17</i>	<i>0.86</i>	
Micro Cap								
Abraxas Petroleum Corporation	ABP	2.67	35.8	96	1.00	0.84	1.28	
Purcell Energy, Ltd. (US\$)	PEL.TO	2.07	48.0	99	2.80	0.27	0.81	

Buy/Sell rating after symbol: B - Buy, S - Sell

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Table 2-2

Independent Natural Gas and Oil Producers - Small Cap

Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

		<i>Price</i> <i>(\$/sh)</i>	<i>EV/</i>	<i>EV/</i>	<i>Divd or</i>	<i>PV/</i>
<i>Symbol/</i>		<i>9-Feb</i>	<i>Sales</i>	<i>Ebitda</i>	<i>P/E</i>	<i>NTM</i>
<i>Rating</i>		<i>2004</i>	<i>NTM</i>	<i>NTM</i>	<i>NTM</i>	<i>Ebitda</i>
					<i>(%)</i>	<i>NTM</i>
Short Life						
Western Gas Resources	WGR	46.35	0.8	9.1	19	- 9.7
Spinnaker Exploration Company	SKE	35.60	5.3	6.0	18	- 4.8
Southwestern Energy Company	SWN	20.51	3.2	5.8	11	- 5.9
Energy Partners Ltd.	EPL	13.86	2.9	4.7	22	- 5.0
Denbury Resources Inc.	DNR	14.45	3.2	4.6	8	- 5.9
Stone Energy Company	SGY	43.10	3.2	4.5	10	- 5.6
Newfield Exploration Company	NFX	48.52	3.1	4.4	11	- 4.7
Chesapeake Energy Corporation	CHK	12.34	3.4	4.4	8	1.0 5.5
Westport Resources Corporation	WRC	30.20	3.3	4.3	11	- 5.5
Range Resources Corporation	RRC	10.15	3.3	4.2	8	0.4 5.4
Cimarex Energy Company	XEC	B 26.05	3.2	4.1	10	- 5.5
Forest Oil Corporation	FST	25.96	3.0	4.1	7	- 5.9
St. Mary Land and Exploration Company	SM	28.68	2.7	4.1	11	0.3 5.7
The Houston Exploraton Company	THX	36.36	2.5	3.0	7	- 4.2
	<i>Median</i>		<i>3.2</i>	<i>4.4</i>	<i>11</i>	<i>- 5.5</i>
Long Life						
Ultra Petroleum Corp.	UPL	22.95	12.7	16.6	29	- 11.9
Quicksilver Resources Inc.	KWK	34.98	6.0	9.2	18	- 9.6
Unit Corporation	UNT	25.80	3.5	8.0	19	- 6.9
Berry Petroleum Company	BRY	19.07	3.6	7.8	16	2.3 8.8
Evergreen Resources, Inc.	EVG	32.50	5.5	7.5	12	- 9.3
Penn Virginia Corporation	PVA	54.78	3.5	6.3	14	1.6 6.4
Swift Energy Company	SFY	16.94	3.9	6.0	16	- 7.0
Encore Acquisition Corp.	EAC	B 25.50	3.8	5.3	11	- 6.6
Magnum Hunter Resources, Inc.	MHR	8.77	3.2	5.1	11	- 6.9
Whiting Petroleum Corporation	WLL	19.42	3.1	5.1	11	- 6.1
Vintage Petroleum, Inc.	VPI	12.68	2.3	4.1	10	1.4 6.4
	<i>Median</i>		<i>3.6</i>	<i>6.3</i>	<i>14</i>	<i>- 6.9</i>
Micro Cap						
Abraxas Petroleum Corporation	ABP	2.67	9.2	15.2		- 11.9
Purcell Energy, Ltd. (US\$)	PEL.TO	2.07	3.9	5.4	11	- 6.6

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended December 31, 2004; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Table 2-3
Independent Natural Gas and Oil Producers - Small Cap
Determinants of Present Value

	Symbol/ Rating	NG & O Prod/ Ebitda (%)	N. Am. Gas/ Ebitda (%)	Adjusted Reserves/ Prod NTM	PV/ Ebitda NTM	NG&O Ebitda/ mcf	McDep Ratio 9-Feb 2004	
Short Life								
Spinnaker Exploration Company	SKE	100	82	4.3	4.8	4.72	1.25	
Newfield Exploration Company	NFX	100	85	5.2	4.7	3.68	0.95	
The Houston Exploraton Company	THX	100	94	5.2	4.2	4.41	0.70	
Energy Partners Ltd.	EPL	100	64	5.5	5.0	3.13	0.94	
Cimarex Energy Company	XEC	B	100	78	6.2	5.5	3.91	0.74
St. Mary Land and Exploration Company	SM	100	67	6.8	5.7	3.21	0.71	
Stone Energy Company	SGY	100	67	7.1	5.6	3.82	0.80	
Chesapeake Energy Corporation	CHK	100	90	7.8	5.5	3.92	0.79	
Westport Resources Corporation	WRC	100	73	7.8	5.5	4.00	0.78	
Western Gas Resources	WGR	61	61	7.9	9.7	2.57	0.94	
Forest Oil Corporation	FST	100	77	7.9	5.9	3.66	0.70	
Southwestern Energy Company	SWN	89	74	8.4	5.9	3.63	0.98	
Range Resources Corporation	RRC	100	79	8.6	5.4	3.96	0.78	
Denbury Resources Inc.	DNR	100	51	8.9	5.9	3.52	0.79	
	<i>Median</i>		75	7.4	5.5	3.75	0.79	
Long Life								
Penn Virginia Corporation	PVA	77	63	9.4	6.4	2.14	0.98	
Unit Corporation	UNT	62	55	9.5	6.9	3.69	1.17	
Magnum Hunter Resources, Inc.	MHR	100	70	10.0	6.9	3.22	0.74	
Whiting Petroleum Corporation	WLL	100	59	10.2	6.1	2.87	0.84	
Swift Energy Company	SFY	100	32	11.1	7.0	2.55	0.86	
Encore Acquisition Corp.	EAC	B	100	21	12.0	6.6	3.51	0.80
Ultra Petroleum Corp.	UPL	100	96	14.5	11.9	3.54	1.40	
Berry Petroleum Company	BRY	100	-	14.6	8.8	1.73	0.88	
Vintage Petroleum, Inc.	VPI	100	31	15.9	6.4	2.41	0.64	
Evergreen Resources, Inc.	EVG	100	100	17.2	9.3	3.78	0.80	
Quicksilver Resources Inc.	KWK	100	87	18.5	9.6	3.02	0.96	
	<i>Median</i>		59	12.0	6.9	3.02	0.86	
Micro Cap								
Purcell Energy, Ltd. (US\$)	PEL.TO	100	79	6.4	6.6	1.80	0.81	
Abraxas Petroleum Corporation	ABP	100	78	11.7	11.9	2.55	1.28	

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