

Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

December 7, 2004

Canadian Income

Summary and Recommendation

Reinstating our coverage of **Enerplus Resources Fund (ERF)** and **Pengrowth Energy Trust (PGH)** we see reasonable value and attractive income from Canadian oil and gas production. The two entities are among the oldest and largest of the Canadian “royalty trusts”. Compared to U.S. counterpart, **San Juan Basin Royalty Trust (SJT)**, ERF and PGH offer similar current income, shorter reserve life and moderate financial risk/leverage. ERF and PGH offer 58% and 44% natural gas exposure compared to larger, long-life, Buy-recommended **Canadian Oil Sands Trust (COSWF)** that is concentrated on oil. Listed on the New York Stock Exchange, ERF and PGH have attracted a majority of non-Canadian ownership further reflected in a premium of more than 25% for Pengrowth’s A units that can be owned by non-Canadians over the B units that can be owned only by Canadians.

Thirst for Income

ERF and PGH join the Income group in our valuation tables with McDep Ratios of 1.20 and 1.31, respectively, ranking them in the middle of peers (see table Rank by McDep Ratio). We made no change to our previous estimates of net present value per unit, the main subjective estimate that influences McDep Ratio. ERF and PGH have cash flow multiples at the low end of the range in line with their shorter adjusted reserve life (see table Rank by EV/Ebitda).

ERF and PGH stand out for their Next Twelve Months Distribution Yields of 10.0% and 11.5%, respectively, two of the highest three of stocks in our regular coverage. The thirst for income in a low interest rate environment is so strong that much of the mature oil and gas production in Canada has been converted to royalty trust form. That thirst may be part of the explanation for the higher valuation reflected in McDep Ratios for ERF and PGH compared to Buy-rated Canadian producers like **Encana (ECA)**, **Petro-Canada (PCZ)**, **Imperial (IMO)** and **Suncor (SU)**.

Untapped U.S. Market for Resource Income Investments

A funny thing has happened since Pengrowth split its units into two classes a few months ago. The move positions the trust to limit its non-Canadian ownership to less than 50% as may be required by a 2007 deadline that may be imposed by the Canadian Federal Government. The non-Canadian A units have advanced to more than a 25% premium to

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the Canadian B units. The NYSE listed PGH units trade at the A price converted to U.S. dollars.

The premium for U.S. units fits the idea that the small Canadian market is relatively well-supplied with royalty trust income while the large U.S. market is not. The recent stock price action is in contrast to fears earlier in the year that U.S. holders might be forced to sell at an awkward time in order to bring ownership ratios in line with possible government restrictions.

The McDep Ratio for Pengrowth is calculated on the price for the PGH or the A units. On a 60/40 weighted basis for the approximate A/B makeup, the McDep Ratio might be about the same 1.20 as for ERF.

Get Paid While You Wait

The trusts, ERF and PGH, have become steady income payers maintaining a discretionary distribution that does not change much from month to month normally. Income investors can draw solace from a continuing distribution that may be steadier than the daily commodity price quote.

Trends Imply a Worthwhile Wait

Futures prices are a clue to a moving consensus of where we may be headed. Despite recent near month price declines it looks like an energy future with higher value for oil and gas is gradually gaining more adherents. Expectations expressed in average futures price for the next six years continue to rise as evidenced by the current quote being above the 40-week average (see chart [Six-Year Commodity Price Meter](#)).

Six-year futures are indicative of present value of future cash flow while one-year futures are indicative of next twelve months cash flow (see chart [Six-Year and One-Year Natural Gas and Oil Futures](#)). Stock prices appear to be lagging futures.

For recent single-stock research, see [Index of Stock Ideas](#). All of the analyses have been sent to regular clients. Single stock analyses on a number of stocks ranging from eleven to twenty-three are available as independent research to customers of five Wall Street investment banks.

Kurt H. Wulff, CFA

Positive Canadian Income Development

Summary and Recommendation

Apparently the Canadian Federal Government backed off yesterday on imposing a 50% ceiling on non-Canadian ownership of income trusts. Minister of Finance Ralph Goodale approved a press release on budget issues that included the statement, "Further discussions will be pursued with the private sector concerning the appropriate Canadian tax treatment of non-residents investing in resource property through mutual funds." The 25% spread that opened in the trading of **Pengrowth (PGH)** units with restricted ownership appears to make a strong point that Canadians may be the losers in the application of the restrictions (see *Meter Reader* December 7, 2004). Presumably the spread will narrow for the Pengrowth units and the price of **Enerplus (ERF)** and Buy-recommended **Canadian Oil Sands Trust (COSWF)** may benefit from the changing situation.

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Oil and Gas Producers Rank by McDep Ratio: Market Cap and Debt to Present Value

	Symbol/ Rating		Price (\$/sh) 6-Dec 2004	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
Mega Cap								
Exxon Mobil Corporation	XOM	B3	50.14	6,508	326,000	50.00	0.07	1.00
BP plc	BP	B3	59.90	3,614	217,000	60.00	0.13	1.00
Shell Transport and Trading Co. plc	SC	B3	50.76	1,587	81,000	51.00	0.17	1.00
Total S.A.	TOT	B3	108.29	1,228	133,000	113.00	0.17	0.97
Royal Dutch Petroleum	RD	B1	57.15	2,021	116,000	60.00	0.17	0.96
ChevronTexaco Corporation	CVX	B1	52.81	2,126	112,000	62.50	0.13	0.86
<i>Total or Median</i>					985,000		0.15	0.98
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	68.40	125	8,530	20.00	0.74	1.63
Imperial Oil Limited (30%)	IMO	B3	59.28	107	6,330	58.00	0.10	1.02
Marathon Oil Corporation	MRO	B3	37.33	347	12,950	40.00	0.31	0.95
Norsk Hydro ASA	NHY	B1	79.95	254	20,320	90.00	0.18	0.91
Suncor Energy	SU	B3	33.36	460	15,350	38.00	0.13	0.89
ConocoPhillips	COP	B1	86.60	702	60,800	110.00	0.25	0.84
Petro-Canada	PCZ	B3	54.03	269	14,560	68.00	0.18	0.83
PetroChina Company Ltd (10%)	PTR	B2	54.64	176	9,610	82.00	0.06	0.69
Lukoil Oil Company	LUKOY	B2	120.25	209	25,000	208.00	0.06	0.60
<i>Total or Median</i>					173,000		0.18	0.89
Independent Natural Gas and Oil - Large Cap and Mid Cap								
CNOOC Limited (19%)	CEO	B2	54.91	78	4,290	59.00	-	0.93
XTO Energy Inc.	XTO	B1	33.38	272	9,090	38.00	0.19	0.90
Encana Corporation	ECA	B1	54.70	472	25,800	63.00	0.21	0.90
Unocal Corporation	UCL	B3	43.33	274	11,900	54.00	0.24	0.85
Occidental Petroleum Corp.	OXY	B3	56.51	403	22,800	75.00	0.17	0.80
Burlington Resources	BR	B1	43.51	395	17,200	58.00	0.14	0.78
Devon Energy Corporation	DVN	B3	39.55	500	19,800	55.00	0.22	0.78
Anadarko Petroleum Corp.	APC	B1	67.31	253	17,000	94.00	0.20	0.77
<i>Total or Median</i>					128,000		0.20	0.82
Independent Natural Gas and Oil - Small Cap								
Berry Petroleum Company	BRY	B2	46.39	22	1,040	43.00	0.06	1.08
Cimarex Energy Company	XEC	B2	37.57	43	1,610	38.00	0.00	0.99
Energy Partners Ltd.	EPL	B3	18.97	39	740	22.00	0.15	0.88
Encore Acquisition Company	EAC	B2	32.54	33	1,070	47.00	0.22	0.76
<i>Total or Median</i>					4,500		0.10	0.94
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	44.02	145	6,380	15.00	0.52	1.93
Kinder Morgan Management, LLC	KMR	S3	40.20	55	2,210	15.00	0.52	1.81
Pengrowth Energy Trust	PGH		19.95	136	2,710	14.00	0.26	1.31
Enerplus Resources Fund	ERF		34.81	104	3,620	28.00	0.19	1.20
San Juan Basin Royalty Trust	SJT	H	28.52	47	1,330	27.00	-	1.06
Canadian Oil Sands Trust (US\$)	COSWF	B1	51.88	91	4,730	72.00	0.19	0.77
<i>Total or Median</i>					21,000		0.23	1.25

B1 = Buy full unlevered position, B2 = Buy half unlevered position, B3 = Alternative buy

S2 = Short half unlevered position, S3 = Short quarter unlevered position

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

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Oil and Gas Producers

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

	Symbol/ Rating		Price (\$/sh) 6-Dec 2004	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
Mega Cap								
BP plc	BP	B3	59.90	9.9	7.6	7.6	16	2.8
Exxon Mobil Corporation	XOM	B3	50.14	11.1	6.9	6.9	13	2.2
Total S.A.	TOT	B3	108.29	9.6	6.7	6.4	12	3.0
Shell Transport and Trading Co. plc	SC	B3	50.76	8.1	5.8	5.8	11	2.5
Royal Dutch Petroleum	RD	B1	57.15	8.1	5.8	5.6	11	2.6
ChevronTexaco Corporation	CVX	B1	52.81	11.4	6.0	5.2	9	3.0
	<i>Median</i>			9.7	6.3	6.1	11	2.7
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	68.40		8.3	13.5	17	3.3
Suncor Energy	SU	B3	33.36	18.4	8.6	7.7	18	0.6
Imperial Oil Limited (30%)	IMO	B3	59.28	11.3	6.9	7.0	13	1.2
Marathon Oil Corporation	MRO	B3	37.33	7.8	6.2	5.9	12	3.0
Norsk Hydro ASA	NHY	B1	79.95	9.4	5.7	5.2	14	2.3
ConocoPhillips	COP	B1	86.60	11.9	6.0	5.1	8	2.0
Petro-Canada	PCZ	B3	54.03	7.6	6.0	5.0	10	0.9
PetroChina Company Ltd (10%)	PTR	B2	54.64	13.5	6.8	4.7	10	4.3
Lukoil Oil Company	LUKOY	B2	120.25	12.2	6.5	3.9	7	2.9
	<i>Median</i>			11.6	6.5	5.2	12	2.3
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B1	33.38	11.7	6.6	5.9	11	0.6
CNOOC Limited (19%)	CEO	B2	54.91	9.6	5.4	5.1	9	3.3
Occidental Petroleum Corp.	OXY	B3	56.51	11.2	6.3	5.0	9	1.9
Burlington Resources	BR	B1	43.51	9.9	6.0	4.7	10	0.8
Unocal Corporation	UCL	B3	43.33	8.9	5.5	4.7	10	1.8
Anadarko Petroleum Corp.	APC	B1	67.31	10.9	6.0	4.6	10	0.8
Encana Corporation	ECA	B1	54.70	6.4	4.9	4.4	10	0.7
Devon Energy Corporation	DVN	B3	39.55	6.6	5.1	4.0	8	1.0
	<i>Median</i>			9.7	5.7	4.7	10	0.9
Independent Natural Gas and Oil - Small Cap								
Berry Petroleum Company	BRY	B2	46.39	12.5	6.6	7.1	15	1.0
Encore Acquisition Company	EAC	B2	32.54	11.9	7.6	5.8	11	-
Cimarex Energy Company	XEC	B2	37.57	5.2	4.1	4.1	12	-
Energy Partners Ltd.	EPL	B3	18.97	4.9	4.1	3.6	13	-
	<i>Median</i>			8.6	5.4	5.0	12	-
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	44.02		8.0	15.4	20	6.6
Kinder Morgan Management, LLC	KMR	S3	40.20		8.0	14.4	19	7.3
Canadian Oil Sands Trust (US\$)	COSWF	B1	51.88	20.0	11.2	8.7	11	3.2
San Juan Basin Royalty Trust	SJT	H	28.52	12.5	8.2	8.6	10	10.4
Pengrowth Energy Trust	PGH		19.95	7.9	6.0	7.9	18	11.5
Enerplus Resources Fund	ERF		34.81	8.3	6.5	7.8	25	10.0
	<i>Median</i>			10.4	8.0	8.7	18	8.7

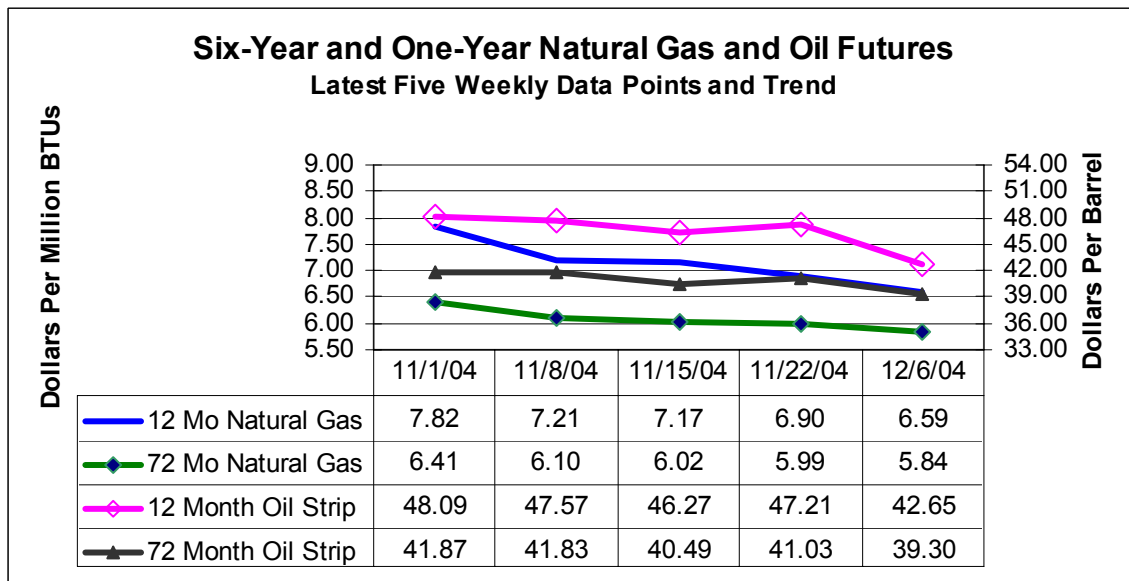
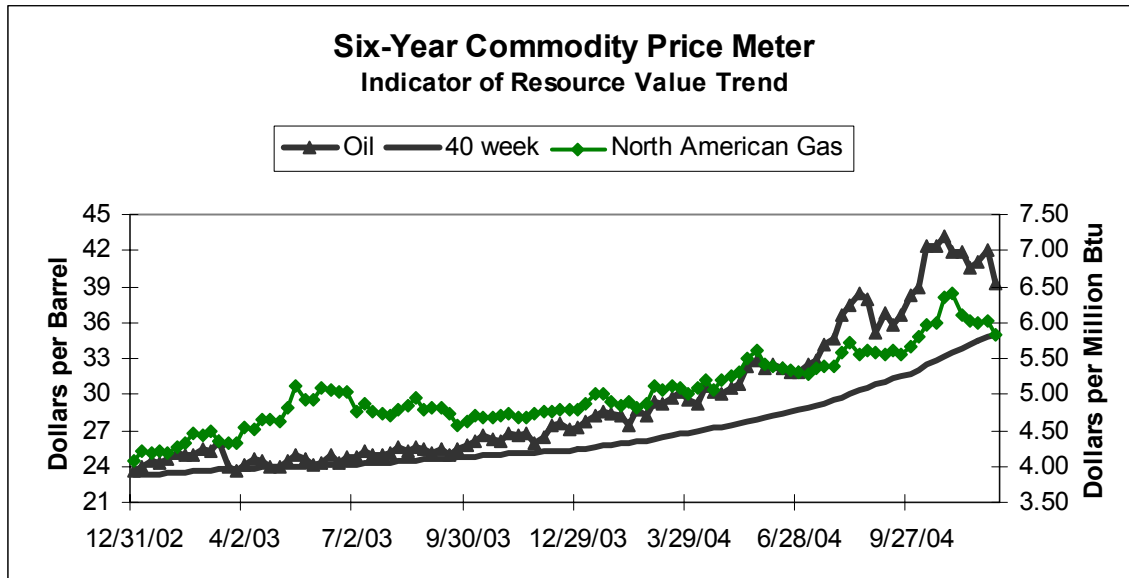
EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended December 31, 2005; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Index of Stock Ideas Recent Written Analyses

<u>Date</u>	<u>Symbol</u>	<u>Stock</u>	<u>Theme</u>
3-Dec	COSWF	Canadian Oil Sands Trust	After Hubbert's Peak
3-Dec	COP	ConocoPhillips	Connecting with Lukoil
29-Nov	XEC	Cimarex Energy Company	Timely Talent
26-Nov	XTO	XTO Energy Inc.	Twenty Per Cent per Year per Share
24-Nov	APC	Anadarko Petroleum Corporation	Asset Upgrade
22-Nov	EAC	Encore Acquisition Company	Opportunity in Hedging Impact
22-Nov	MTR	Mesa Royalty Trust	Hugoton Predictability, San Juan Surprise
17-Nov	TOT	Total S.A.	African Oil, European Refining
17-Nov	UCL	Unocal Corporation	Incremental Production in 2005
15-Nov	EPL	Energy Partners, Ltd.	Lowest Cash Flow Multiple
15-Nov	OXY	Occidental Petroleum Corporation	Still Cheap
12-Nov	CRT	Cross Timbers Royalty Trust	Low Risk, Long Life
9-Nov	* IMO	Imperial Oil Limited	Raise Present Value to US\$58 a Share
9-Nov	* DVN	Devon Energy Corporation	Large Cap Natural Gas
8-Nov	* BRY	Berry Petroleum Company	Smart Oil Contract
8-Nov	* PCZ	Petro-Canada	Looking for Long Life
5-Nov	* SJT	San Juan Basin Royalty Trust	High Winter Distributions Ahead
4-Nov	* ECA	EnCana Corporation	Bold Moves
3-Nov	* MRO	Marathon Oil Corporation	Lower Net Present Value to \$40 a Share
2-Nov	* XOM	Exxon Mobil Corporation	Raise Present Value to \$50 a Share
26-Oct	* KMP	Kinder Morgan Energy Partners, L.P.	Fallen Star
26-Oct	* KMI	Kinder Morgan Inc.	Fallen Star
26-Oct	* KMR	Kinder Morgan Management, LLC	Fallen Star
18-Oct	* NHY	Norsk Hydro ASA	High Cash Flow
11-Oct	* BR	Burlington Resources, Inc.	Natural Gas Sensitivity
11-Oct	* COSWF	Canadian Oil Sands Trust	Raise Present Value to US\$72 a Unit
11-Oct	* SJT	San Juan Basin Royalty Trust	Raise Present Value to \$27 a Unit
6-Oct	* COSWF	Canadian Oil Sands Trust	Ten Percent Holder Surfaces
5-Oct	* LUKOY	Lukoil Oil Company	SEC Standard Reduces Reserves
30-Sep	* COP	ConocoPhillips	Lukoil Investment Confirmed
30-Sep	* LUKOY	Lukoil Oil Company	ConocoPhillips Partner Confirmed
28-Sep	* RD	Royal Dutch Petroleum	Low Risk, Attractive Reward
28-Sep	* SC	Shell Transport & Trading Company, p.l.c.	Low Risk, Attractive Reward
20-Sep	* BP	BP p.l.c.	Betting on Putin
20-Sep	* LUKOY	Lukoil Oil Company	ConocoPhillips Partner
8-Sep	* CEO	CNOOC Ltd ADS	Higher Dividend, Higher Present Value
8-Sep	* PTR	PetroChina Company Limited	Dividend Raised, Present Value Trimmed
26-Aug	* BP	BP p.l.c.	Russia Distinction
16-Aug	* SU	Suncor Energy Inc.	A Boone and Charlie Favorite
4-Aug	* CVX	ChevronTexaco Corporation	Stock Price Lagging Oil Price

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