

Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

September 27, 2005

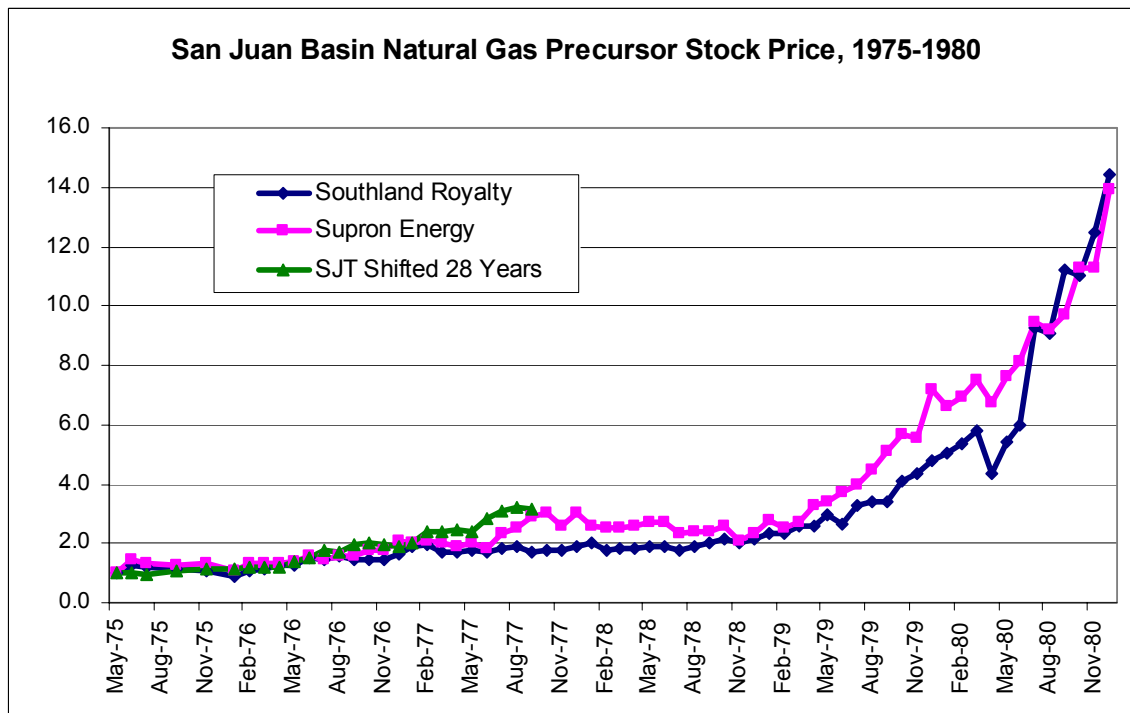
You Ain't Seen Nothin Yet

Summary and Recommendation

The natural gas investment trend may have further to run judging by history. Instinctively, traders are tempted to take profits after nice gains and the likelihood that the worst hurricane news may be behind us. Yet, a pure producer, like **San Juan Basin Royalty Trust (SJT)**, for example, may be in the third year of a five-year gain of 14-fold by analogy with predecessors 28 years ago. Though we cannot promise a repeat of history we can emphasize that natural gas remains underpriced compared to oil, coal or any other fuel considering its clean characteristics. That is particularly true overseas in rapidly growing China and resource-rich Russia.

Natural Gas Stock Precursors Southland Royalty and Supron Energy

To refresh our historical perspective on natural gas producer stocks we check our old DLJ research. Southland Royalty owned the properties that became San Juan Basin Royalty Trust in November 1980. Supron Energy was essentially a pure play on San Juan Basin natural gas. From May 1975 to December 1980 the stocks appreciated 14 times (see chart [San Juan Basin Natural Gas Precursor Stock Price, 1975-1980](#)).



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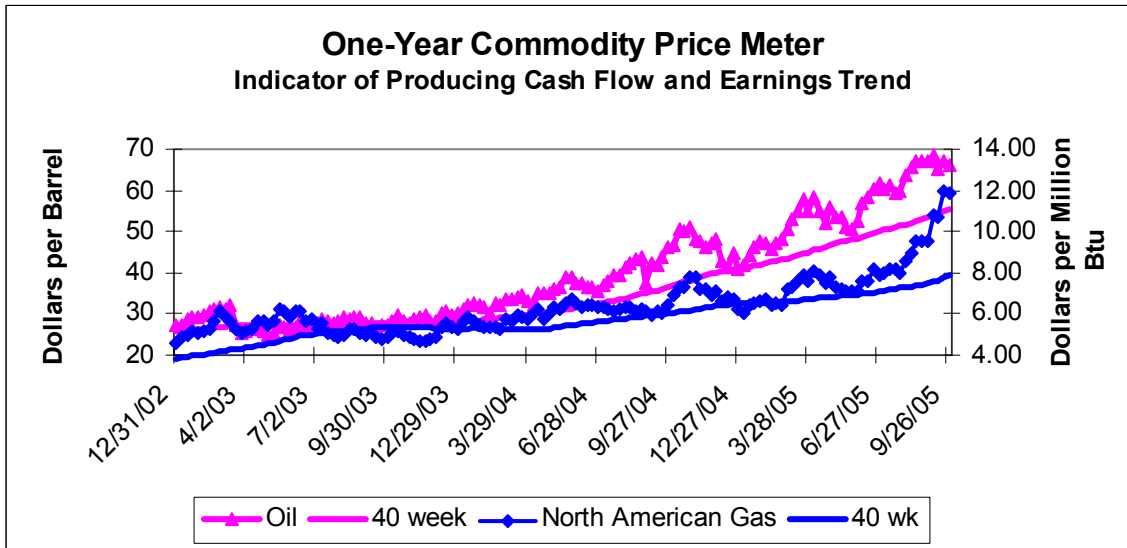
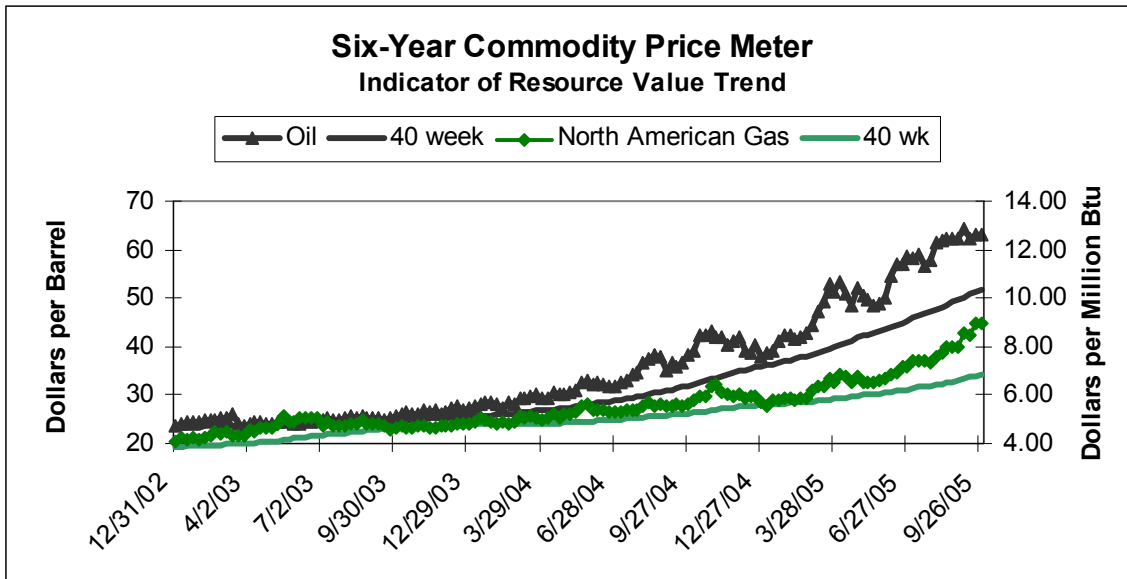
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Superimposed on the chart we add the distribution-adjusted, indexed price of SJT from May 2003 to September 2005 by plotting it forward from May 1975. The 28 year time difference matches the period from the stock market low of 1974 to the stock market low of 2002.

No Strategic Storage for Natural Gas

The availability of government-owned emergency inventories kept crude oil within its normal price band despite the loss of all Gulf of Mexico oil production temporarily. Natural gas production has also been lost and can be made up only by substitution with oil at higher price. As a result the natural gas price trend has accelerated while the crude oil price trend continues at the same pace (see charts Six-Year Commodity Price Meter and One-Year Commodity Price Meter).

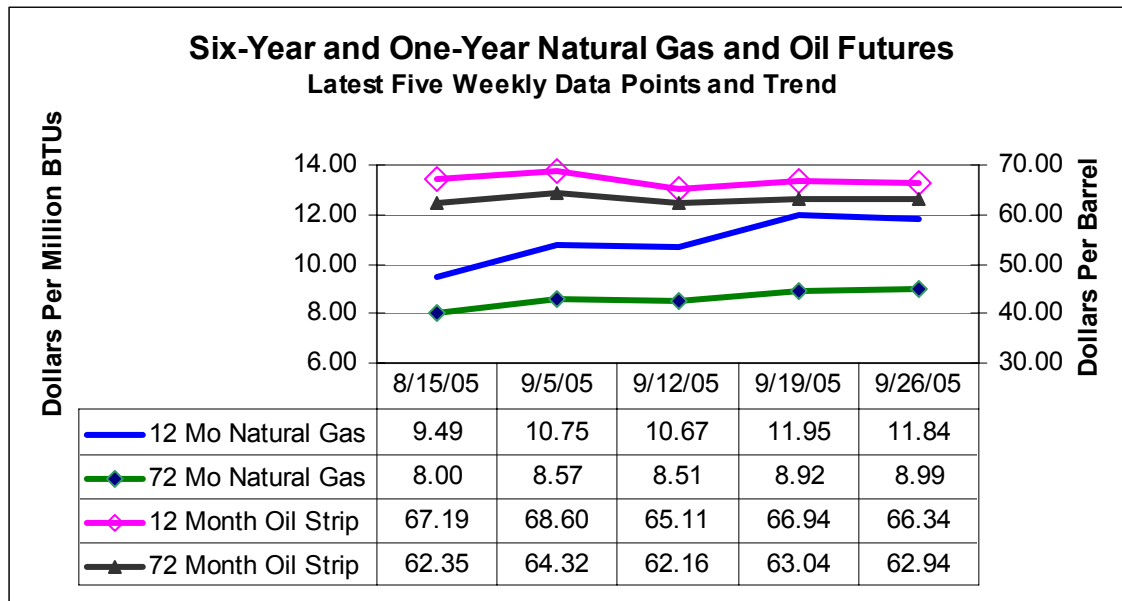


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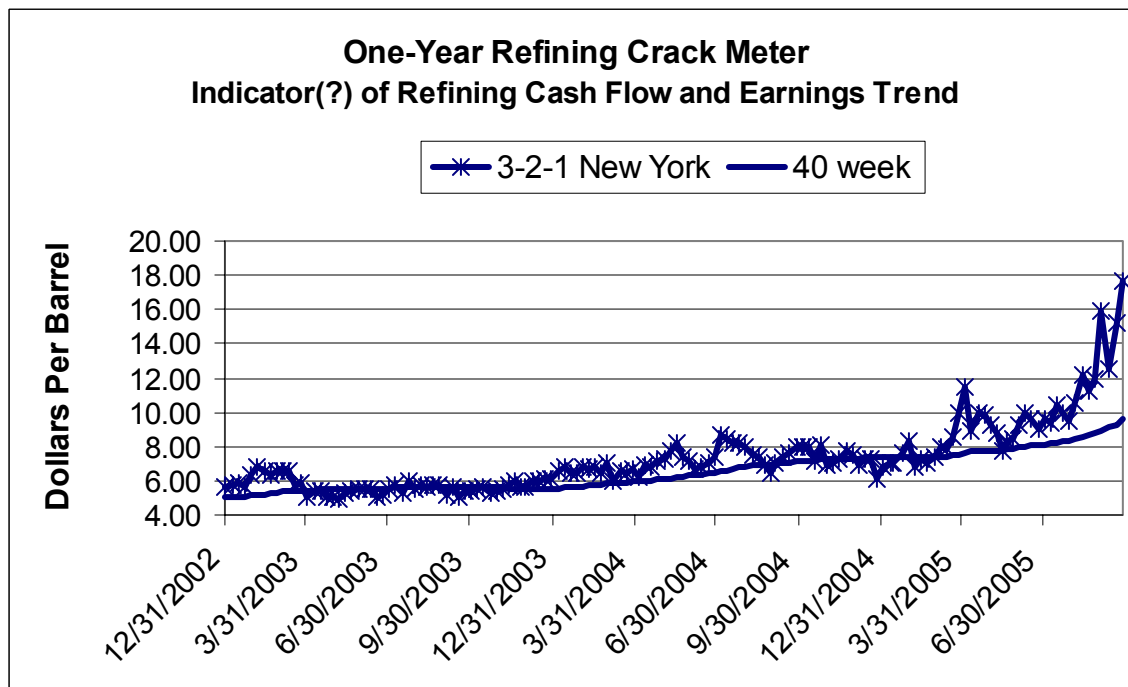
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Refining Crack Holds Strongly

The outlook for oil refining is better than 28 years ago or one-year ago. The trend in the crack spread, a measure of refining cash flow, continues the definitive move above the 40-week average initiated earlier in 2005 (see chart [One-Year Refining Crack Meter](#)).



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Buy Natural Gas, Oil and Refining in the Stock Market

Current stock prices for natural gas and oil producers approximate a median McDep Ratio of 0.88 (see table [Rank by McDep Ratio](#)). A McDep Ratio of 1.0 presumes a 7% per year real return on constant real prices for oil of \$50 a barrel, natural gas of \$10 a million btu and refining crack of \$10 a barrel.

Stocks are ranked in descending order of McDep Ratio to suggest “buy low and sell high”. We recommend representation in each of the five groups from Mega Cap to Income with emphasis on low McDep Ratio stocks.

Next Twelve Months Cash Flow, Ebitda, changes weekly with futures prices for natural gas and oil in contrast to Present Value, the denominator of the McDep Ratio, which holds constant from week to week. As a result cash flow multiples may change more than McDep Ratios in the short term (see table [Rank by EV/Ebitda](#)). We regularly check the correlation of present value with cash flow multiple by business and expected life of production.

We encourage U.S. investors to concentrate disproportionately on stocks of companies headquartered in other countries (see table [Home Country and Business Segments](#)). That diversifies political risk and often offers more potential gain in resource value.

Finally, we recommend that investors be sure they are represented in the stocks of companies with strong natural gas concentration. Nor should that be at the expense of reasonable downstream exposure in other stocks.

Timely analyses are available on all recommended stocks (see table [Index of Recent Research](#)).

Kurt H. Wulff, CFA

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

	Symbol/ Rating		Price (\$/sh) 26-Sep 2005	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
Mega Cap								
BP plc	BP	B	71.31	3,545	253,000	82.00	0.10	0.88
Exxon Mobil Corporation	XOM	B	64.68	6,370	412,000	74.00	0.04	0.88
Total S.A.	TOT	B	136.28	1,182	161,000	160.00	0.12	0.87
Royal Dutch Shell plc	RDS-A	B	65.44	3,372	221,000	84.00	0.09	0.80
Chevron Corporation	CVX	B	64.29	2,256	145,000	90.00	0.12	0.75
<i>Total or Median</i>					<i>1,192,000</i>		<i>0.10</i>	<i>0.87</i>
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	94.26	123	11,600	20.00	0.76	1.90
Imperial Oil Limited (30%)	IMO	B	113.79	104	11,780	84.00	0.09	1.32
Marathon Oil Corporation	MRO	B	69.59	367	25,540	65.00	0.27	1.05
Petro-Canada	PCZ	B	42.36	526	22,280	42.00	0.19	1.01
Suncor Energy	SU	B	59.45	461	27,410	68.00	0.10	0.89
Norsk Hydro ASA	NHY	B	111.54	251	28,000	130.00	0.12	0.88
Lukoil Oil Company	LUKOY	B	56.45	830	47,000	65.00	0.03	0.87
ConocoPhillips	COP	B	69.32	1,419	98,400	100.00	0.15	0.74
Gazprom (50%)	OGZPF	B	61.70	1,022	63,000	90.00	0.03	0.70
PetroChina Company Ltd (10%)	PTR	B	81.75	176	14,370	120.00	0.01	0.68
<i>Total or Median</i>					<i>349,000</i>		<i>0.11</i>	<i>0.88</i>
Independent Natural Gas and Oil - Large Cap and Mid Cap								
Encana Corporation	ECA	B	56.09	892	50,000	51.00	0.16	1.08
Burlington Resources	BR	B	79.30	385	30,500	86.00	0.09	0.93
XTO Energy Inc.	XTO	B	43.77	372	16,290	48.00	0.17	0.93
CNOOC Limited (29%)	CEO	B	71.89	119	8,570	84.00	0.01	0.86
Devon Energy Corporation	DVN	B	66.43	471	31,300	86.00	0.15	0.81
Occidental Petroleum Corp.	OXY	B	87.33	406	35,500	120.00	0.11	0.76
Anadarko Petroleum Corp.	APC	B	96.24	238	22,900	140.00	0.11	0.72
<i>Total or Median</i>					<i>544,000</i>		<i>0.11</i>	<i>0.87</i>
Independent Natural Gas and Oil - Small Cap								
Berry Petroleum Company	BRY	B	64.89	23	1,460	65.00	0.10	1.00
Energy Partners Ltd.	EPL	B	30.67	41	1,240	38.00	0.17	0.84
Encore Acquisition Company	EAC	B	38.11	49	1,880	50.00	0.17	0.80
Cimarex Energy Company	XEC	B	43.70	85	3,710	64.00	0.12	0.72
<i>Total or Median</i>					<i>8,300</i>		<i>0.15</i>	<i>0.82</i>
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	52.33	157	8,220	15.00	0.55	2.11
Kinder Morgan Management, LLC	KMR	S3	49.40	56	2,750	15.00	0.55	2.03
Pengrowth Energy Trust	PGH		24.95	157	3,910	20.00	0.17	1.21
San Juan Basin Royalty Trust	SJT		47.15	47	2,200	40.00	-	1.18
Penn West Energy Trust	PWTFF	B	29.32	174	5,090	28.00	0.16	1.04
Enerplus Resources Fund	ERF		43.51	105	4,560	42.00	0.13	1.03
Canadian Oil Sands Trust (US\$)	COSWF	B	105.63	93	9,810	136.00	0.12	0.80
<i>Total or Median</i>					<i>36,500</i>		<i>0.16</i>	<i>1.18</i>

B = 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) 26-Sep 2005	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
Mega Cap								
Exxon Mobil Corporation	XOM	B	64.68	11.5	6.7	5.9	10	1.8
BP plc	BP	B	71.31	9.4	6.2	5.5	9	3.0
Total S.A.	TOT	B	136.28	9.2	5.9	5.2	9	2.4
Royal Dutch Shell plc	RDS-A	B	65.44	7.2	5.4	4.4	8	3.4
Chevron Corporation	CVX	B	64.29	9.3	5.7	4.3	7	2.8
	<i>Median</i>			9.3	5.9	5.2	9	2.8
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	94.26		8.1	15.5	22	3.2
Gazprom (50%)	OGZPF	B	61.70	22.0	12.8	8.9	18	0.6
Imperial Oil Limited (30%)	IMO	B	113.79	10.5	5.9	7.9	13	0.7
Suncor Energy	SU	B	59.45	18.1	8.6	7.7	16	0.3
Petro-Canada	PCZ	B	42.36	5.9	4.8	4.8	8	1.6
Marathon Oil Corporation	MRO	B	69.59	7.1	4.4	4.7	7	1.6
Norsk Hydro ASA	NHY	B	111.54	8.2	5.3	4.6	10	2.8
ConocoPhillips	COP	B	69.32	11.2	5.6	4.1	6	1.8
PetroChina Company Ltd (10%)	PTR	B	81.75	13.9	5.7	3.9	8	4.6
Lukoil Oil Company	LUKOY	B	56.45	19.8	4.4	3.8	6	1.7
	<i>Median</i>			11.2	5.7	4.7	9	1.7
Independent Natural Gas and Oil - Large Cap and Mid Cap								
Encana Corporation	ECA	B	56.09	7.2	5.0	5.4	10	1.1
Burlington Resources	BR	B	79.30	9.9	5.4	5.0	10	0.5
XTO Energy Inc.	XTO	B	43.77	11.3	5.2	4.8	8	0.5
Occidental Petroleum Corp.	OXY	B	87.33	11.3	5.6	4.3	7	1.4
CNOOC Limited (29%)	CEO	B	71.89	9.4	5.0	4.3	7	3.2
Anadarko Petroleum Corp.	APC	B	96.24	12.5	5.5	4.0	7	0.7
Devon Energy Corporation	DVN	B	66.43	7.3	3.8	3.1	5	0.5
	<i>Median</i>			10.6	5.3	4.5	8	0.9
Independent Natural Gas and Oil - Small Cap								
Encore Acquisition Company	EAC	B	38.11	14.7	6.4	5.1	11	-
Berry Petroleum Company	BRP	B	64.89	11.0	5.1	5.1	13	1.0
Cimarex Energy Company	XEC	B	43.70	7.5	4.0	2.9	6	-
Energy Partners Ltd.	EPL	B	30.67	5.1	3.1	2.6	6	-
	<i>Median</i>			9.2	4.6	4.0	9	-
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	52.33		8.2	17.4	28	6.0
Kinder Morgan Management, LLC	KMR	S3	49.40		8.2	16.7	27	6.3
San Juan Basin Royalty Trust	SJT		47.15	12.0	7.4	8.7	9	10.8
Canadian Oil Sands Trust (USS)	COSWF	B	105.63	20.0	9.7	7.8	8	1.6
Pengrowth Energy Trust	PGH		24.95	7.6	5.1	6.2	9	9.5
Enerplus Resources Fund	ERF		43.51	9.8	5.3	5.4	8	8.4
Penn West Energy Trust	PWTFF	B	29.32	8.0	4.2	4.3	6	9.1
	<i>Median</i>			9.8	7.4	7.8	9	8.4

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended September 30, 2006; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Oil and Gas Producers Home Country and Business Segments

	Symbol/ Rating		Non- U.S. Domicile	North Amer. Natural Gas (%)	Rest of World Natural Gas (%)	Oil Prod'n (%)	Down- stream (%)	Total Present Value (US\$mm)
Mega Cap								
Exxon Mobil Corporation	XOM	B		10	19	39	33	492,000
BP plc	BP	B	UK	10	12	44	34	324,000
Royal Dutch Shell plc	RDS-A	B	UK	4	22	29	45	313,000
Chevron Corporation	CVX	B		9	9	54	28	230,000
Total S.A.	TOT	B	France	-	27	38	35	215,000
			<i>Total or Median</i>	9	19	39	34	1,574,000
Producer/Refiners - Large Cap and Mid Cap								
PetroChina Company Ltd.	PTR	B	China	-	9	71	20	213,000
Gazprom	OGZPF	B	Russia		100			190,000
ConocoPhillips	COP	B		13	7	45	35	166,900
Lukoil Oil Company	LUKOY	B	Russia	-	-	62	38	55,700
Norsk Hydro ASA	NHY	B	Norway	-	27	38	35	37,300
Suncor Energy	SU	B	Canada	5	-	89	7	35,000
Marathon Oil Corporation	MRO	B		14	8	33	46	32,900
Imperial Oil Limited	IMO	B	Canada	13	-	62	25	31,900
Petro-Canada	PCZ	B	Canada	23	4	53	20	27,200
			<i>Median</i>	9	7	58	30	790,000
Independent Natural Gas and Oil - Large Cap and Mid Cap								
Occidental Petroleum Corp.	OXY	B		15	1	73	11	54,900
Encana Corporation	ECA	B	Canada	84	-	16	-	54,500
Devon Energy Corporation	DVN	B		62	-	38	-	47,500
Anadarko Petroleum Corp.	APC	B		60	-	40	-	37,500
Burlington Resources	BR	B		69	5	26	-	36,300
CNOOC Limited	CEO	B	China	-	12	88	-	34,800
XTO Energy Inc.	XTO	B		82	-	18	-	21,600
			<i>Median</i>	62	-	38	-	287,000
Independent Natural Gas and Oil - Small Cap								
Cimarex Energy Company	XEC	B		70	-	30	-	6,140
Encore Acquisition Company	EAC	B		27	-	73	-	2,990
Berry Petroleum Company	BRY	B		16	-	84	-	1,920
Energy Partners Ltd.	EPL	B		56	-	44	-	1,860
			<i>Median</i>	42	-	58	-	12,910
Income								
Canadian Oil Sands Trust (US\$)	COSWF	B	Canada	-	-	100	-	14,400
Penn West Energy Trust	PWTFF	B	Canada	43	-	57	-	5,800
Enerplus Resources Fund	ERF		Canada	61	-	39	-	5,080
Pengrowth Energy Trust	PGH		Canada	43	-	57	-	3,730
San Juan Basin Royalty Trust	SJT			100	-	-	-	1,860
			<i>Median</i>	43	-	57	-	30,900

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Index of Recent Research

Stock Ideas

<u>Date</u>	<u>Symbol</u>	<u>Stock</u>	<u>Theme</u>
26-Sep	LUKOY	Lukoil Oil Company	Adapting to New Russia
22-Sep	MRO	Marathon Oil Corporation	Hurricane Watch
19-Sep	NHY	Norsk Hydro ASA	Acquiring U.S. Producer for \$2.45 Billion
16-Sep	XOM	Exxon Mobil Corporation	New Highs Ahead
15-Sep	OGZPF	Gazprom	The Ultimate Natural Gas Stock
9-Sep	APC	Anadarko Petroleum Corporation	Natural Gas Jumps
7-Sep	EPL	Energy Partners, Ltd.	Katrina Survivor
6-Sep	COP	ConocoPhillips	Refining and Natural Gas Event
30-Aug	* CEO	CNOOC Ltd	Independent Producer with Income
28-Aug	* PTR	PetroChina Company Limited	Income Stock
21-Aug	* PTR	PetroChina Company Limited	Understated Natural Gas Resources
18-Aug	* SJT	San Juan Basin Royalty Trust	Sharp Stock Price Drop
17-Aug	* CVX	Chevron Corporation	Astute Acquisition
16-Aug	* EPL	Energy Partners, Ltd.	Denali 2006
15-Aug	* XEC	Cimarex Energy Company	\$Billion Cash Flow for Small Cap NG Producer
11-Aug	* PWTF	Penn West Energy Trust	Undiscovered by U.S. Investors
11-Aug	* SU	Suncor Energy Inc.	Oil Price and Operating Reliability
11-Aug	* KMx	Kinder Morgan	Canada May Block KM-Terasen Deal
8-Aug	* TOT	Total S.A.	Oil Sands Oui!
3-Aug	* DVN	Devon Energy Corporation	Raise Net Present Value to \$86 a Share
2-Aug	*	26 Stocks - Single Issue Statistics	Raise Net Present Value to \$xx a Share
28-Jul	* EAC	Encore Acquisition Company	HPAI Incline
27-Jul	* BP	BP p.l.c.	Steady-State Growth
26-Jul	* OXY	Occidental Petroleum Corporation	Back in Libya
22-Jul	* PCZ	Petro-Canada	Approaching Par
22-Jul	* IMO	Imperial Oil Limited	Syncrude Boost
22-Jul	* COSWF	Canadian Oil Sands Trust	Distribution Capability Blossoming
20-Jul	* XTO	XTO Energy Inc.	Simpson Sense
14-Jul	* RD	Royal Dutch Petroleum	Frontier Challenge
6-Jul	* COSWF	Canadian Oil Sands Trust	Free (Cash Flow) at Last
31-May	* ECA	EnCana Corporation	Clean Fuel Supplier
31-May	* BR	Burlington Resources, Inc.	Clean Fuel Supplier
5-May	* BRY	Berry Petroleum Company	Oil in the Kitty Litter

Meter Reader - A Weekly Analysis

27-Sep		You Ain't Seen Nothin Yet
20-Sep	*	Startling Gains for Natural Gas
13-Sep	*	Big Bucks for Big Oil
6-Sep	*	Refining and Natural Gas Event
16-Aug	*	Energy Policy Act of 2005
9-Aug	*	Comparables
2-Aug	*	Raise Present Value for \$50 Oil

* Archived on www.mcdep.com

Also see

U.S. Natural Gas Royalty Trusts - A Weekly Analysis, and Single-Trust Analyses

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