

Rating: Buy  
S&P 500: 1285

## **Anadarko Petroleum Corporation**

### **Long Life, Low Stock Price**

<i>Symbol</i>	APC	<i>Ebitda Next Twelve Months ending 12/31/06 (US\$mm)</i>	6,100
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	53
<i>Price (US\$/sh)</i>	109.03	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	1/30/06	<i>Adjusted Reserves/Production NTM</i>	12.5
<i>Shares (mm)</i>	238	<i>EV/Ebitda</i>	5.0
<i>Market Capitalization (US\$mm)</i>	25,900	<i>PV/Ebitda</i>	6.2
<i>Debt (US\$mm)</i>	4,400	<i>Undeveloped Reserves (%)</i>	36
<i>Enterprise Value (EV) (US\$mm)</i>	30,400	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	39.19
<i>Present Value (PV) (US\$mm)</i>	37,700	<i>Present Value Proven Reserves(US\$/boe)</i>	15.92
<i>Net Present Value (US\$/share)</i>	140	<i>Present Value Proven Reserves(US\$/mcfe)</i>	2.65
<i>Debt/Present Value</i>	0.12	<i>Earnings Next Twelve Months (US\$/sh)</i>	11.11
<i>McDep Ratio - EV/PV</i>	0.80	<i>Price/Earnings Next Twelve Months</i>	10
<i>Dividend Yield (%/year)</i>	0.7	<i>Indicated Annual Dividend (US\$/sh)</i>	0.72

Note: Estimated cash flow and earnings tied to one-year futures prices for oil and natural gas.

Reported results may vary widely from estimates. Estimated present value per share revised only infrequently.

### **Summary and Recommendation**

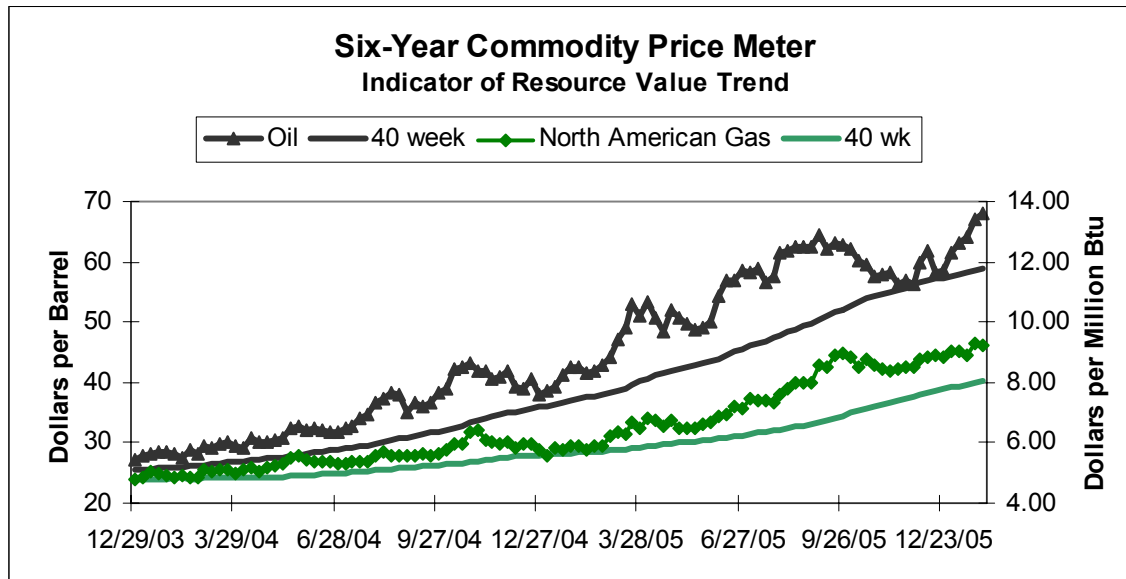
With another week before fourth quarter results are reported buy-recommended **Anadarko Petroleum (APC)** offers 28% appreciation potential to estimated net present value of \$140 a share that presumes a long-term oil price of \$50 a barrel. Futures investors price Light, Sweet Crude Oil at \$68 a barrel for the next six years. Among independent producer peers, APC's low McDep Ratio suggests that investors may not be giving the stock as much credit for long life as might be justified. Adjusted reserve life at 12.5 years is the longest in our large cap independent group. Concentrated primarily on natural gas, the company has deep water Gulf of Mexico potential that could be also be attractive to an acquirer.

### **McDep Ratio Relates Oil Price to Opportunity**

A McDep Ratio below 1.0 tells us that APC's market cap and debt, or enterprise value, is less than the estimated present value of its energy resources. The estimate has been increasing with six-year oil futures. Futures price momentum has been positive for more than three years as the current quote stays above the 40-week average (see chart [Six-Year Commodity Price Meter](#)). Six-year oil has tripled in the four years we have been calculating it on a weekly basis. We do not need further gains in oil price to make money in buy recommendations. Yet our vision of \$150 oil in 2010 implies additional scope to exceed common expectations.

Anadarko's McDep Ratio ranks low among peer companies (see table [Rank by McDep Ratio](#)). Aside from the fundamental appreciation potential we outlined above, a McDep Ratio of 1.0 is an indication of takeover value. The McDep Ratio of buy-recommended **Burlington Resources (BR)**, increased to 1.0 immediately after buy-recommended **ConocoPhillips (COP)** announced its takeover offer.

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**Rank by McDep Ratio: Market Cap and Debt to Present Value**

	Symbol/ Rating	Price (\$/sh) 30-Jan 2006	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>							
CNOOC Limited (29%)	CEO B	86.31	119	10,290	84.00	0.00	1.03
XTO Energy Inc.	XTO B	49.45	370	18,300	48.00	0.20	1.02
Encana Corporation	ECA B	49.23	876	43,100	51.00	0.20	0.97
Devon Energy Corporation	DVN B	67.70	454	30,700	86.00	0.15	0.82
Occidental Petroleum Corp.	OXY B	94.47	432	40,800	120.00	0.12	0.81
Anadarko Petroleum Corp.	APC B	109.03	238	25,900	140.00	0.12	0.80
Burlington Resources	BR B	91.48	378	34,600	115.00	-	0.80
<i>Total or Median</i>				<i>204,000</i>		<i>0.12</i>	<i>0.82</i>

**Low Cash Flow Multiple**

Unlevered cash flow multiples in single digits attest to low valuation (see table [Rank by EV/Ebitda](#)). Cash flow estimated for the next twelve months, Ebitda NTM, reflects latest futures prices. Reserve life is measured as adjusted reserves divided by next twelve months production. APC's adjusted reserve life index of 12.5 years is the longest of large cap peers. While long-life ought to be worth a higher cash flow multiple, APC's unlevered multiple, EV/Ebitda, is the lowest.

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

	Symbol/ Rating		Price (\$/sh) 30-Jan 2006	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
XTO Energy Inc.	XTO	B	49.45	10.8	6.4	6.5	11	0.4
Encana Corporation	ECA	B	49.23	7.1	5.5	5.3	11	0.6
CNOOC Limited (29%)	CEO	B	86.31	9.2	5.0	5.1	9	2.7
Anadarko Petroleum Corp.	APC	B	109.03	12.5	6.2	5.0	10	0.7
Occidental Petroleum Corp.	OXY	B	94.47	11.3	5.6	4.6	8	1.5
Devon Energy Corporation	DVN	B	67.70	7.8	4.8	3.9	7	0.4
Burlington Resources	BR	B	91.48	-	-	-	-	-
	<i>Median</i>			9.2	5.5	5.0	9	0.6

**Natural Gas Concentration Blended with Deep Gulf Oil**

Each oil and gas stock has its own unique mix of energy resources (see table [Business Segments](#)). APC's concentration on natural gas is not as great as that of Burlington Resources, but its oil exposure could be appealing to a potential major company acquirer. Anadarko is in both of buy-recommended **Chevron (CVX)**'s recent discoveries in the deep Gulf of Mexico, Knotty Head and Big Foot.

**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)
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
Occidental Petroleum Corp.	OXY	B		14	1	75	11	59,000
Encana Corporation	ECA	B	Canada	83	-	17	-	55,600
Devon Energy Corporation	DVN	B		64	-	36	-	46,000
Anadarko Petroleum Corp.	APC	B		60	-	40	-	37,700
CNOOC Limited	CEO	B	China	-	12	88	-	34,600
XTO Energy Inc.	XTO	B		83	-	17	-	22,100
Burlington Resources	BR	B						
	<i>Median</i>			62	-	38	-	255,000

**Correlation Verifies Present Value in Real Time**

Our underlying quantitative method for estimating present value projects cash flows years into the future and brings them to the present by applying a real discount rate, currently 7% a year. Around that traditional discounted cash flow analysis (DCF) we deal with uncertainty on a qualitative basis. "Option value" to us, for example, is "upside potential". After awhile DCF analyses fall into a pattern where differences among companies depend mostly on first year cash flow and reserve life. Meanwhile input information is continually changing as companies make new disclosures, each on a different day or at a different hour and commodity prices fluctuate. We aggregate latest information into a correlation analysis that determines a real-time present value approximation. When that approximation deviates too much from our steady, official

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estimate of present value and we cannot justify the difference with company-specific explanation, we change the official estimate. Net present value indicated by the current correlation is about \$25 a share higher than our ongoing standard estimate for the company (see table Functional Cash Flow and Present Value).

**Anadarko Petroleum Corporation**  
**Functional Cash Flow and Present Value**

	<i>NTM Ebitda</i> <i>(US\$mm)</i>	<i>Adjusted</i> <i>R/P</i>	<i>PV/</i> <i>Ebitda</i>	<i>Present</i> <i>Value</i> <i>(US\$mm)</i>	
North American Natural Gas	3,230	12.9	7.0	22,500	60%
Oil	2,870	12.0	5.3	15,200	40%
	6,100	12.5	6.2	37,700	100%
Debt (US\$mm)					4,400
Net Present Value (US\$mm)					33,300
Shares (mm)					238
Net Present Value - Standard Estimate (US\$/sh)					140
Net Present Value - Approximation by Correlation (US\$/sh)					165

**Futures Prices and Company Disclosures Propel Estimated Cash Flow by Quarter**

Cash flow for the next year is projected from a base through the latest reported quarter (see table Next Twelve Months Operating and Financial Estimates). Company disclosures provide the clues for future volumes and costs as well as geographic and quality differences in price. Futures prices from the New York Mercantile Exchange determine industry benchmarks for the next year in our model.

Kurt H. Wulff, CFA

**Anadarko Petroleum Corporation**  
**Next Twelve Months Operating and Financial Estimates**

	<i>Q4</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Next Twelve Months</i>
	<i>12/31/04</i>	<i>9/30/05</i>	<i>12/31/05</i>	<i>2005E</i>	<i>3/31/06</i>	<i>6/30/06</i>	<i>9/30/06</i>	<i>12/31/06</i>	<i>12/31/06</i>
<b>Volume</b>									
Natural Gas (mmcf)	1,641	1,382	1,382	<b>1,413</b>	1,382	1,382	1,382	1,382	<b>1,382</b>
Oil (mbd)	223	196	196	<b>198</b>	196	196	196	196	<b>196</b>
Total gas & oil (bcf)	274	235	235	<b>950</b>	230	233	235	235	<b>934</b>
<b>Price</b>									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	7.10	8.56	13.00	<b>8.65</b>	10.04	9.54	9.77	10.72	<b>10.02</b>
Company (\$/mcf)	6.10	7.15	10.86	<b>7.45</b>	8.39	7.97	8.16	8.95	<b>8.61</b>
Oil (\$/bbl)									
WTI Cushing	48.31	62.52	60.02	<b>56.31</b>	67.44	69.57	70.44	70.76	<b>69.56</b>
Worldwide	42.15	48.51	46.57	<b>45.43</b>	52.33	53.98	54.66	54.91	<b>53.98</b>
Total gas & oil (\$/mcf)	6.52	7.69	9.61	<b>7.51</b>	8.67	8.57	8.72	9.19	<b>8.79</b>
<b>Revenue (\$mm)</b>									
Natural Gas	921	936	1,421	<b>3,840</b>	1,074	1,032	1,067	1,172	<b>4,344</b>
Oil	865	875	840	<b>3,287</b>	923	963	986	990	<b>3,862</b>
Other	(184)	(55)		<b>10</b>					<b>-</b>
Total	1,602	1,756	2,261	<b>7,137</b>	1,997	1,995	2,053	2,162	<b>8,206</b>
<b>Expense</b>									
Fixed	191	226	226	<b>859</b>	226	226	226	226	<b>906</b>
Variable	191	226	353	<b>985</b>	287	286	301	328	<b>1,201</b>
<b>Ebitda (\$mm)</b>	1,219	1,303	1,682	<b>5,293</b>	1,484	1,482	1,526	1,607	<b>6,099</b>
Deprec., Deplet., & Amort.	355	334	334	<b>1,325</b>	334	334	334	334	<b>1,336</b>
Hedging and other			97	<b>116</b>	115	122	126	132	<b>496</b>
<b>Ebit</b>	864	969	1,250	<b>3,851</b>	1,035	1,026	1,065	1,141	<b>4,267</b>
Interest	92	50	50	<b>202</b>	50	50	50	50	<b>200</b>
<b>Ebt</b>	772	919	1,200	<b>3,649</b>	985	976	1,015	1,091	<b>4,067</b>
Income Tax	270	322	420	<b>1,277</b>	345	342	355	382	<b>1,424</b>
<b>Net Income (\$mm)</b>	502	597	780	<b>2,372</b>	640	634	660	709	<b>2,644</b>
<b>Shares (millions)</b>	246	238	238	<b>238</b>	238	238	238	238	<b>238</b>
Per share (\$)	2.04	2.51	3.28	<b>9.96</b>	2.69	2.67	2.77	2.98	<b>11.11</b>
Ebitda Margin	76%	74%	74%	<b>74%</b>	74%	74%	74%	74%	<b>74%</b>
Tax Rate	35%	35%	35%	<b>35%</b>	35%	35%	35%	35%	<b>35%</b>

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