

Rating: Buy
 S&P 500: 1172

CNOOC Limited

Volume Gains Expected in 2005

<i>Symbol</i>	CEO	<i>Ebitda Next Twelve Months ending 12/31/05 (US\$mm)</i>	6,400
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	0
<i>Price (US\$/sh)</i>	56.18	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	3/22/05	<i>Adjusted Reserves/Production NTM</i>	9.1
<i>Shares (mm)</i>	411	<i>EV/Ebitda</i>	3.6
<i>Market Capitalization (US\$mm)</i>	23,100	<i>PV/Ebitda</i>	4.3
<i>Debt (US\$mm)</i>	0	<i>Undeveloped Reserves (%)</i>	53
<i>Enterprise Value (EV) (US\$mm)</i>	23,100	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	40.70
<i>Present Value (PV) (US\$mm)</i>	27,600	<i>Present Value Proven Reserves(US\$/boe)</i>	14.25
<i>Net Present Value (US\$/share)</i>	67	<i>Present Value Proven Reserves(US\$/mcfe)</i>	2.38
<i>Debt/Present Value</i>	0.00	<i>Earnings Next Twelve Months (US\$/sh)</i>	8.90
<i>McDep Ratio - EV/PV</i>	0.84	<i>Price/Earnings Next Twelve Months</i>	6
<i>Dividend Yield (%/year)</i>	3.2	<i>Indicated Annual Dividend (US\$/sh)</i>	1.79

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.

The Peoples Republic of China holds 81% of the outstanding shares.

Summary and Recommendation

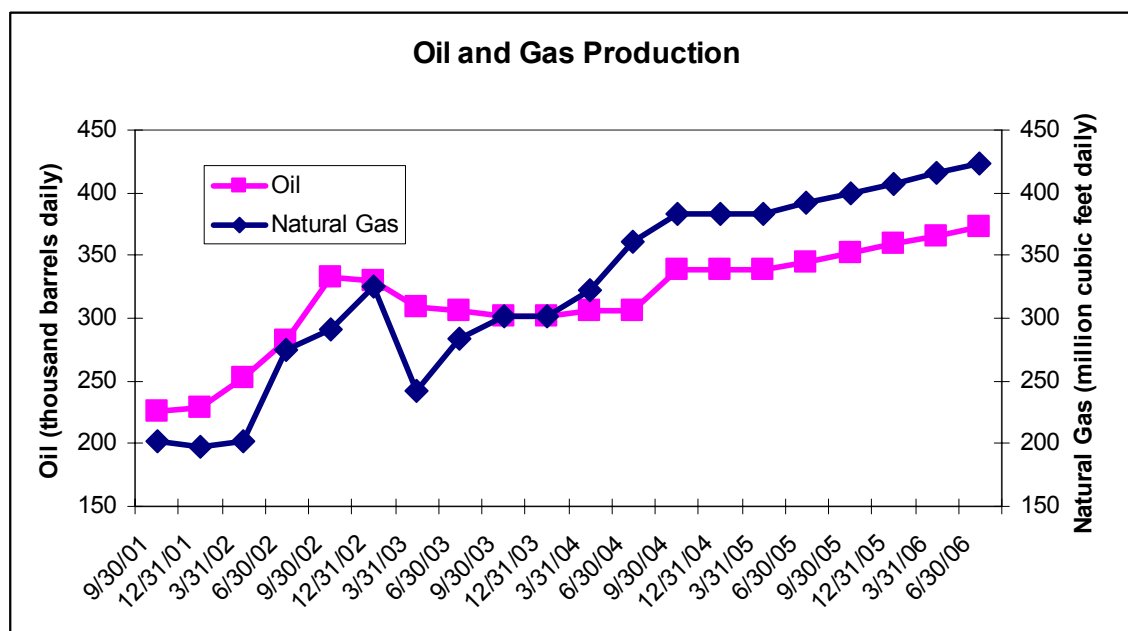
We continue to recommend current purchase of the American Depositary Shares of **CNOOC Limited (CEO)** the “independent producer” of China-domiciled oil and gas companies. Volume growth resumed in the second half of last year and is expected to continue through 2005. That strong trend combined with rising oil price generates projected cash flow for the next twelve months almost 50% higher than the amount we projected late last year. We raised our estimate of net present value on January 26, 2005 to \$67 a share from \$59 when we revised our estimate of long-term oil price to \$40 a barrel constant real from \$35. Now just two months later the average price of oil in the futures market for the next six years of \$53 a barrel implies even more present value. Business risk is partly shifted to partners including **ChevronTexaco (CVX)** and **ConocoPhillips (COP)** and financial risk is low as there is no net debt on the company’s balance sheet. Dividend yield of 3.3% may jump when the company reports final results for 2004 shortly.

Daily Volume Growth Resumes

Earlier in the month, management laid out expectations for some 19% growth in oil and gas volume in 2005. The company has always had attractive growth prospects despite a temporary lull in 2003 (see chart [Oil and Gas Production](#)).

The impact on revenue is magnified when we take account of latest futures prices for oil (see table [Next Twelve Months Operations](#)). Chinese companies appear to be benefiting to the full extent of international oil price and that is more important today. A low natural gas price, presumably imposed by the government, helps to speed consumer adoption of the clean fuel. Once adopted there should be no turning back as producers will need international prices to support optimal supply development of natural gas.

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CNOOC Limited											
Next Twelve Months Operations											
	Q3	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Year	Q1E	Q2E	Next Twelve Months
	9/30/04	12/31/04	2004E	3/31/05	6/30/05	9/30/05	12/31/05	2005E	3/31/06	6/30/06	6/30/06
Volume											
Natural gas (bcf)	35	35	133	35	36	37	37	144	37	39	150
Natural Gas (mmcf/d)	384	384	363	384	391	399	407	395	415	424	411
Days	92	92	366	90	91	92	92	365	90	91	365
Oil (mmb)	31	31	118	30	31	32	33	127	33	34	132
Oil (mbd)	338	338	322	338	345	352	359	348	366	373	362
Total gas & oil (bcf)	222	222	844	217	224	231	235	907	235	242	944
Total gas & oil (mbd)	402	402	383	402	410	418	427	414	435	444	431
Price											
Natural gas (\$/mcf)			141					151			157
Henry Hub (\$/mmbtu)	5.75	7.10	6.15	6.27	7.46	7.65	8.04	7.35	8.53	7.12	7.84
Company	2.87	2.87	2.87	2.87	2.87	2.87	2.87	2.87	2.87	2.87	2.87
Oil (\$/bbl)											
WTI Cushing	43.89	48.30	41.44	49.69	57.35	58.50	58.09	55.91	57.20	56.38	57.54
Company	40.28	44.32	37.51	45.60	52.63	53.68	53.30	51.39	52.49	51.74	52.79
Total gas & oil (\$/mcf)	6.10	6.67	5.70	6.85	7.83	7.98	7.93	7.66	7.81	7.71	7.86
Revenue (\$mm)											
Natural Gas	101	101	381	99	102	105	108	414	107	111	431
Oil	1,253	1,378	4,427	1,387	1,651	1,737	1,759	6,535	1,729	1,757	6,982
Other											
Total	1,354	1,480	4,808	1,487	1,754	1,842	1,867	6,949	1,836	1,868	7,413

Higher revenue translates mostly to higher cash flow as the company has a high Ebitda margin (see table Next Twelve Months Financial Results).

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CNOOC Limited
Next Twelve Months Financial Estimates

	<i>H1</i>	<i>H2E</i>	<i>Year</i>	<i>H1E</i>	<i>H2E</i>	<i>Year</i>	<i>H1E</i>	<i>Next Twelve Months</i>
	<i>6/30/04</i>	<i>12/31/04</i>	<i>2004E</i>	<i>6/30/05</i>	<i>12/31/05</i>	<i>2005E</i>	<i>6/30/06</i>	<i>6/30/06</i>
Revenue (mmRMB)								
Natural Gas (from Q table)	1,474	1,675	3,149	1,664	1,760	3,423	1,801	3,561
Oil (from Q table)	14,840	21,744	36,584	25,114	28,894	54,007	28,808	57,701
Other	(129)	(129)	(258)	(129)	(129)	(258)	(129)	(258)
Total	16,028	23,290	39,318	26,649	30,525	57,173	30,480	61,004
Expense								
Fixed	1,452	1,452	2,903	1,452	1,452	2,903	1,452	2,903
Variable	1,452	2,084	3,535	2,383	2,727	5,110	2,723	5,451
Other	-	-	-	-	-	-	-	-
Ebitda	13,411	19,884	33,295	22,943	26,474	49,418	26,434	52,908
Exploration	551	551	1,102	551	551	1,102	551	1,102
Deprec., Deplet., & Amort.	2,648	2,648	5,296	2,648	2,648	5,296	2,648	5,296
Ebit	10,212	16,685	26,897	19,744	23,275	43,020	23,235	46,510
Interest	-	-	-	-	-	-	-	-
Ebt	10,212	16,685	26,897	19,744	23,275	43,020	23,235	46,510
Income Tax	3,221	5,840	9,061	6,911	8,146	15,057	8,132	16,279
Net Income	6,991	10,845	17,836	12,834	15,129	27,963	15,103	30,232
Shares (millions)	41,124	41,124	41,124	41,124	41,124	41,124	41,124	41,124
Per share (RMB)	0.17	0.26	0.43	0.31	0.37	0.68	0.37	0.74
Ebitda Margin	84%	85%	85%	86%	87%	86%	87%	87%
Tax Rate	32%	35%	34%	35%	35%	35%	35%	35%

Present Value Reflects Low Cash Flow Multiple

Oil accounts for 88% of estimated present value as we estimate now (see table Functional Cash Flow and Present Value). The cash flow multiple of only four times for oil is only slightly low for the adjusted reserve life of 7.5 years. When reported, 2004 reserves are likely to be higher and could justify a higher multiple if there is no change in expected production volume. Management cites the respected U.S. engineering firm Ryder Scott in disclosing its reserves of specific new fields.

CNOOC Limited
Functional Cash Flow and Present Value

	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Present</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>Value</i>	
				<i>(US\$mm)</i>	
Natural Gas	370	17.3	8.9	3,300	12%
Oil	6,030	7.5	4.0	24,300	88%
	6,400	9.1	4.3	27,600	100%
Debt (US\$mm)					-
Net Present Value (US\$mm)					27,600
Shares (mm)					411
Net Present Value (US\$/sh)					67

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Buy Oil and Gas Producers at Mid Decade

Measured by McDep Ratio, CEO stock appears undervalued along with peers (see table Rank by McDep Ratio). A McDep Ratio of 1.0 means that stock price and debt equal present value estimated on the basis of a long-term price of oil of \$40 a barrel. The current benchmark oil average futures price for the next six years is about \$53 a barrel. If the past repeats, we see three to five-fold gain potential for oil and gas price over the next 5 to 13 years.

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

	<i>Symbol/</i>		<i>Price</i>		<i>Market</i>	<i>Net</i>		
			<i>(\$/sh)</i>	<i>Shares</i>	<i>Cap</i>	<i>Present</i>	<i>Debt/</i>	
	<i>Rating</i>	<i>22-Mar</i>	<i>2005</i>	<i>(mm)</i>	<i>(\$mm)</i>	<i>Value</i>	<i>Present</i>	<i>McDep</i>
						<i>(\$/sh)</i>	<i>Value</i>	<i>Ratio</i>
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	33.00	349	11,530	33.80	0.17	0.98
Unocal Corporation	UCL	B	60.74	271	16,500	65.00	0.21	0.95
Encana Corporation	ECA	B	68.20	471	32,100	77.00	0.16	0.90
Occidental Petroleum Corp.	OXY	B	71.17	406	28,900	87.00	0.15	0.85
CNOOC Limited (19%)	CEO	B	56.18	78	4,390	67.00	-	0.84
Devon Energy Corporation	DVN	B	46.81	500	23,400	63.00	0.16	0.78
Burlington Resources	BR	B	49.82	391	19,500	67.00	0.12	0.77
Anadarko Petroleum Corp.	APC	B	75.34	246	18,500	113.00	0.14	0.71
<i>Total or Median</i>					<i>155,000</i>		<i>0.15</i>	<i>0.84</i>

Kurt H. Wulff, CFA

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