

Rating: Buy
S&P 500: 1207

CNOOC Limited

Low Price for Natural Gas

<i>Symbol</i>	CEO	<i>Ebitda Next Twelve Months ending 9/30/06 (US\$mm)</i>	6,500
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	0
<i>Price (US\$/sh)</i>	65.70	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	10/31/05	<i>Adjusted Reserves/Production NTM</i>	9.4
<i>Shares (mm)</i>	411	<i>EV/Ebitda</i>	4.2
<i>Market Capitalization (US\$mm)</i>	27,000	<i>PV/Ebitda</i>	5.3
<i>Debt (US\$mm)</i>	300	<i>Undeveloped Reserves (%)</i>	46
<i>Enterprise Value (EV) (US\$mm)</i>	27,400	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	40.22
<i>Present Value (PV) (US\$mm)</i>	34,900	<i>Present Value Proven Reserves(US\$/boe)</i>	17.59
<i>Net Present Value (US\$/share)</i>	84	<i>Present Value Proven Reserves(US\$/mcf)</i>	2.93
<i>Debt/Present Value</i>	0.01	<i>Earnings Next Twelve Months (US\$/sh)</i>	8.96
<i>McDep Ratio - EV/PV</i>	0.78	<i>Price/Earnings Next Twelve Months</i>	7
<i>Dividend Yield (%/year)</i>	3.5	<i>Indicated Annual Dividend (US\$/sh)</i>	2.32

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 71% of the outstanding shares.

Summary and Recommendation

Buy-recommended **CNOOC Limited (CEO)** offers 28% appreciation potential to estimated net present value of \$84 a share. Taking account of latest quarterly results, our correlation of 30 companies indicates net present value about \$2 a share lower than estimated. The simplified correlation overlooks the advantage CEO enjoys as international companies assume the exploratory risk on offshore China acreage blocks. Growing volumes of natural gas have catch up price potential because the reported price around \$3 a million btu is less than a third of our long-term expectation for North American production.

Cash Flow and Reserve Life Point to Present Value

McDep analysis presumes that fundamental value is measured by the projection of cash flows far into the future and discounting them to the present at a rate of return, currently 7% a year before inflation. Next Twelve Months (NTM) cash flow represents the volumes and costs that form the base for future projections. Reserve life index tells how long cash flow will last. NTM cash flow and reserve life are the two main variables in our correlation by function for about 30 companies. Net present value indicated by the current combined correlation is about \$2 a share lower than our ongoing standard estimate for the company (see table Functional Cash Flow and Present Value).

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CNOOC Limited
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>	
Natural Gas	400	17.3	10.8	4,300	12%
Oil	6,100	7.9	5.0	30,500	88%
	6,500	9.4	5.4	34,800	100%
Debt (US\$mm)					300
Net Present Value (US\$mm)					34,500
Shares (mm)					411
Net Present Value (US\$/sh)					84
Over (-)/ Under (+) Correlation (US\$/sh)					(2)

Cash Flow by Quarter Depends on Latest Results and Futures Prices

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.

Industry Conditions Support Long-Term Price Expectation

Present value estimates that form the denominator of the McDep Ratio and change only occasionally for all companies, most recently in early August, are tied to expected constant real long-term prices. Recent futures price for oil delivered over the next six years at \$58 a barrel exceeds our long-term expectation of \$50. One-year futures for natural gas exceed our long-term expectation while six-year futures for natural gas also have appreciation potential, in our opinion.

Oil and Gas Commodity and Stock Price
Monday, October 31, 2005

	<i>Units</i>	<i>Futures Price</i>		<i>McDep Ratio</i>
		<i>Six-Year</i>	<i>One-Year</i>	<i>Denominator</i>
Crude Oil	\$/barrel	57.99	60.98	50
Natural Gas	\$/million btu	8.46	11.08	10
	<i>Stocks</i>			<i>Median</i>
	Independent Producer - Large Cap			0.78
	CEO			0.78

Source: McDep Associates, Bloomberg, New York Mercantile Exchange, Yahoo and company disclosures

CNOOC Limited
Next Twelve Months Operations

	<i>Q4</i>	<i>Year</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Next Twelve Months</i>
	<i>12/31/04</i>	<i>2004E</i>	<i>3/31/05</i>	<i>6/30/05</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>9/30/06</i>
Volume											
Natural gas (bcf)	36	133	31	34	38	38	141	38	40	41	157
Natural Gas (mmcf)	389	364	348	369	410	418	387	427	435	444	431
Days	92	366	90	91	92	92	365	90	91	92	365
Oil (mmb)	30	117	32	32	33	33	130	33	34	35	137
Oil (mbd)	326	319	352	357	356	363	357	370	378	385	374
Total gas & oil (bcf)	216	835	221	229	234	239	923	238	246	254	977
Total gas & oil (mbd)	391	380	410	419	424	433	421	441	450	459	446
Price											
Natural gas (\$/mcf)		139					154				163
Henry Hub (\$/mmbtu)	7.10	6.15	6.27	6.76	8.56	12.79	8.59	12.53	10.32	10.33	11.49
Company	2.43	2.75	2.69	2.95	2.94	2.94	2.89	2.94	2.94	2.94	2.94
Oil (\$/bbl)											
WTI Cushing	48.31	41.44	49.65	53.05	62.52	60.65	56.47	60.72	61.21	61.27	60.96
Company	36.37	35.41	40.91	43.91	52.40	50.83	47.09	50.89	51.30	51.35	51.10
Total gas & oil (\$/mcf)	5.46	5.39	6.23	6.68	7.80	7.58	7.09	7.59	7.65	7.65	7.62
Revenue (\$mm)											
Natural Gas	87	367	84	99	111	113	407	113	116	120	462
Oil	1,091	4,139	1,296	1,427	1,716	1,698	6,137	1,696	1,764	1,820	6,979
Other											
Total	1,178	4,506	1,380	1,526	1,827	1,811	6,544	1,809	1,880	1,940	7,441

CNOOC Limited
Next Twelve Months Financial Estimates

	<i>H2</i>	<i>Year</i>	<i>H1</i>	<i>H2E</i>	<i>Year</i>	<i>H1E</i>	<i>H2E</i>	<i>Next Twelve Months</i>
	<i>12/31/04</i>	<i>2004</i>	<i>6/30/05</i>	<i>12/31/05</i>	<i>2005E</i>	<i>6/30/06</i>	<i>12/31/06</i>	<i>12/31/06</i>
Revenue (mmRMB)								
Natural Gas (from Q table)	1,556	3,030	1,478	1,807	3,284	1,849	1,849	3,656
Oil (from Q table)	19,368	34,208	21,956	27,535	49,491	27,904	27,904	55,439
Other	(66)	(352)	1,300	1,300	2,599	1,300	1,300	2,599
Total	20,858	36,886	24,734	30,641	55,375	31,053	31,053	61,694
Expense								
Fixed	2,297	3,749	1,484	2,297	3,781	2,297	2,297	4,595
Variable	2,297	3,749	1,484	1,858	3,341	1,884	1,884	3,741
Ebitda	16,329	29,740	20,467	25,186	45,653	25,572	25,572	50,758
Exploration	765	1,316	611	611	1,222	611	611	1,222
Deprec., Deplet., & Amort.	2,807	5,455	2,787	2,787	5,574	2,787	2,787	5,574
Ebit	12,757	22,969	17,069	21,788	38,857	22,174	22,174	43,962
Interest	-	-	-	-	-	-	-	-
Ebt	12,757	22,969	17,069	21,788	38,857	22,174	22,174	43,962
Income Tax	3,710	6,931	5,143	7,626	12,769	7,761	7,761	15,387
Net Income	9,047	16,038	11,926	14,162	26,088	14,413	14,413	28,576
Shares (millions)	41,124	41,124	41,124	41,124	41,124	41,124	41,124	41,124
Per share (RMB)	0.22	0.39	0.29	0.34	0.63	0.35	0.35	0.69
Ebitda Margin	78%	81%	83%	82%	82%	82%	82%	82%
Tax Rate	29%	30%	30%	35%	33%	35%	35%	35%

Buy Independent Natural Gas and Oil Producers

Energy is necessary for world economic growth and clean energy provides a better quality of life. Independent natural gas and oil producers are among the leading global suppliers of clean energy. Headquartered in China, Canada and the U.S., buy recommendations also offer political

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diversification. McDep Ratios that compare Enterprise Value with Present Value of energy and other businesses imply that the stock market undervalues the fundamental prospects. Stocks are ranked in descending order of McDep Ratio connoting “buy low, sell high” (see table Rank by McDep Ratio).

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

	<i>Symbol/</i>	<i>Rating</i>	<i>Price</i> <i>(\$/sh)</i>	<i>Shares</i>	<i>Market</i>	<i>Net</i>	<i>Debt/</i>	<i>McDep</i>
			<i>31-Oct</i>	<i>(mm)</i>	<i>Cap</i>	<i>Value</i>	<i>Present</i>	<i>Ratio</i>
			<i>2005</i>		<i>(\$mm)</i>	<i>(\$/sh)</i>	<i>Value</i>	
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	43.46	370	16,080	48.00	0.20	0.92
Encana Corporation	ECA	B	45.91	876	40,200	51.00	0.20	0.92
Burlington Resources	BR	B	72.20	381	27,500	86.00	0.09	0.85
CNOOC Limited (29%)	CEO	B	65.70	119	7,840	84.00	0.01	0.78
Devon Energy Corporation	DVN	B	60.38	471	28,400	86.00	0.15	0.75
Occidental Petroleum Corp.	OXY	B	78.88	404	31,900	120.00	0.11	0.70
Anadarko Petroleum Corp.	APC	B	90.71	238	21,600	140.00	0.12	0.69
	<i>Total or Median</i>				<i>174,000</i>		<i>0.12</i>	<i>0.78</i>

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