Rating: Buy
S&P 500: 1190

Canadian Oil Sands Trust
After Hubbert's Peak

Symbol	COSWF	*Ebitda Next Twelve Months ending 12/31/05 (US$mm)*	730
Rating	Buy	*North American Natural Gas/Ebitda (%)*	-8
Price (US$/un)	49.63	*Natural Gas and Oil Production/Ebitda (%)*	100
Pricing Date	12/2/04	*Adjusted Reserves/Production NTM*	20.0
Units (mm)	91	*EV/Ebitda*	8.3
Market Capitalization (US$mm)	4,520	*PV/Ebitda*	11.1
Debt (US$mm)	1,530	*Undeveloped Reserves (%)*	10
Enterprise Value (EV) (US$mm)	6,050	*Natural Gas and Oil Ebitda (US$/boe)*	23.09
Present Value (PV) (US$mm)	8,090	*Present Value Proven Reserves(US$/boe)*	7.56
Net Present Value (US$/unit)	72	*Present Value Proven Reserves(US$/mcfe)*	1.26
Debt/Present Value	0.19	*Earnings Next Twelve Months (US$/un)*	4.74
McDep Ratio - EV/PV	0.75	*Price/Earnings Next Twelve Months*	10
Dividend Yield (%/year)	3.4	*Indicated Annual Dividend (US$/un)*	1.67

Note: Estimated cash flow and earnings tied to one-year futures prices for oil.
Reported results may vary widely from estimates. Estimated present value per share revised only infrequently.

Summary and Recommendation

We continue to recommend current purchase of the units of **Canadian Oil Sands Trust** for rising cash distributions up to and after Hubbert's Peak is reached for conventional world oil production. The trust distributes income to unitholders at a rate that may triple by 2007 and last indefinitely. Within a half year spending on a 40% capacity expansion will likely be finished. Within a year and a half operations are expected to reach the expanded level. During that time the stock has 35% appreciation potential to estimated present value of US$72 a unit. The estimate assumes a constant real oil price of $35 a barrel while the current average futures price for the next six years is $39. Beyond that the stock has characteristics of a top candidate for a potential ten-fold return in ten years including a product with appreciating value, volume growth with long-life sustainability, industry leading partners and low fees.

Hubbert's Peak

By now most energy investors have heard of M. King Hubbert, a Shell geophysicist, who predicted the peak in U.S. oil production by applying a statistical theory. A popular 2001 book by disciple, Kenneth S. Deffeyes, revives interest in the theory. Hubbert's formula appears to boil down to the idea that when half the oil in a basin is produced, the rate of production can no longer increase. It has peaked, if you will. The critical judgment then becomes how much oil is there in the basin or area of interest.

U.S. production may have peaked around 1970, but there was still a lot more oil to produce. In fact the dollar value of U.S. production may not have peaked yet to this day. Nonetheless, the rate of U.S. oil production never went higher. We developed Alaska, we intensified secondary and tertiary recovery, but we never matched the old volume peak. Hubbert's judgment on the amount of oil in the U.S. apparently was substantiated.

When we look north to Alberta we see a new oil resource as large as or larger than the conventional oil resource in the U.S. Production of Alberta's oil sands is only beginning. It is too early to talk of Hubbert's Peak for oil sands.

The more controversial discussion these days is the timing of Hubbert's Peak in the rest of the world. The subject was addressed in two recent weeks in *Barron's*. In the November 29 issue, oil banker Matt Simmons plays the unpopular Hubbert role by challenging the myth of Saudi Arabian reserves and production. In the November 15 issue, veteran oil analyst Charlie Maxwell essentially concludes that Hubbert's Peak would arrive for consuming country production in the next five years and for Organization of Petroleum Exporting Country (OPEC) production in the next decade.

Our interpretation is that price, the "invisible hand" of economics, will reflect a resolution of demand and supply necessarily. We expect the price that solves the demand/supply equation to be rewarding for investors in Canadian Oil Sands Trust among other natural gas and oil producers.

Absence of Hedging Boosts Next Twelve Months Financial Results

The expiration of crude oil price hedging at year end extends the benefits of oil price increases to all of the trust's volume in 2005 from half of volume in 2004. That is the major change affecting near term results (see table, Next Twelve Months Operating and Financial Estimates). Hedging is reducing oil revenue by some 17% in 2004.

Operating the Syncrude oil sands plant at nameplate capacity of 250,000 barrels daily is a continuous challenge. Last year at this time there was surprise maintenance. Currently there continues to be intensive construction activity in and around the operating equipment. Accordingly management has been cautious about projecting volume for the remainder of 2004 as well as in 2005. We take a similar stance while hoping to be surprised on the upside.

November volume, just in, at 242 thousand barrels daily, was better than expected. At the same time major maintenance is likely to reduce volumes in the first quarter of next year.

Our price projections are taken from the futures market and adjusted for Canadian currency. The backwardated pattern, as the futures traders refer to the declining trend of each future quarter, has been misleading for several years. Actual price has tended to be higher as each month gets adjusted upward with the passage of time.

Costs reflect management's guidance essentially. One exception is that our projection for Purchased Energy varies with the futures price of natural gas. The other differences are in our classification. For valuation purposes we calculate Ebitda as unlevered cash flow before non-operating items like oil price hedging. The trust reports levered cash flow after that and other items.

Table COS-2
Canadian Oil Sands Trust
Next Twelve Months Operating and Financial Estimates

	Q1 3/31/04	*Q2 6/30/04*	*Q3 9/30/04*	*Q4E 12/30/04*	***Year 2004E***	*Q1E 3/31/05*	*Q2E 6/30/05*	*Q3E 9/30/05*	*Q4E 12/31/05*	***Next Twelve Months 12/31/05***
Volume										
Syncrude (mmb)	23.0	20.8	22.4	21.0	**87.2**	20.8	20.8	22.4	23.2	**87.2**
Syncrude (mbd)	253	229	243	228	**238**	253	229	243	228	**239**
Days	91	91	92	92	**366**	90	91	92	92	**365**
Trust share (%)	34.9	37.2	35.7	35.5	**35.8**	35.5	35.5	35.5	35.5	**35.5**
Trust Oil (mmb)	8.04	7.75	7.97	7.45	**31.2**	7.38	7.40	7.93	8.23	**30.9**
Trust Oil (mbd)	88.3	85.1	86.6	81.0	**85.3**	89.8	81.3	86.2	81.0	**84.8**
Price										
WTI Cushing (US$/bbl)	35.23	38.34	43.89	49.69	**41.79**	43.43	43.23	42.42	42.69	**42.94**
Currency (US$/C$)	0.76	0.74	0.76	0.84	**0.78**	0.84	0.84	0.84	0.84	**0.84**
WTI Cushing (C$/bbl)	46.43	51.81	57.76	59.43	**53.86**	51.95	51.71	50.73	51.05	**51.36**
Differential	(0.70)	1.07	(1.32)	(1.35)	**(0.67)**	(1.18)	(1.18)	(1.16)	(1.16)	**(1.19)**
Trust Oil Price (C$/bbl)	45.73	52.88	56.44	58.07	**53.19**	50.76	50.53	49.58	49.89	**50.17**
Henry Hub Nat Gas (US$/m	5.64	6.10	5.75	7.15	**6.16**	6.83	6.30	6.37	6.65	**6.54**
Henry Hub Nat Gas (C$/mm	7.44	8.24	7.57	8.56	**7.94**	8.17	7.54	7.62	7.95	**7.82**
AECO Natural Gas (C$/GJ)	6.17	6.39	6.19	7.00	**6.44**	6.68	6.16	6.23	6.50	**6.39**
Revenue ($mm)										
Oil	367	410	450	433	**1,660**	375	374	393	411	**1,553**
Transportation & Marketing	(11)	(11)	(12)	(12)	**(46)**	(10)	(10)	(11)	(11)	**(42)**
Other	0	(0)	0	0	**1**		-	-	-	**-**
Total	357	398	438	421	**1,614**	365	364	383	400	**1,510**
Expense										
Production	105	114	133	110	**462**	116	116	116	116	**465**
Purchased Energy	31	33	31	36	**131**	34	31	32	33	**130**
Crown Royalties	4	4	4	4	**16**	4	4	4	4	**16**
Insurance	3	2	2	2	**8**	3	3	3	3	**10**
Administration	2	2	2	2	**8**	3	3	3	3	**10**
Taxes and Other	2	2	(9)	(1)	**(6)**	2	2	2	2	**8**
Total	146	156	163	153	**618**	161	158	159	160	**639**
Ebitda	211	242	275	269	**996**	204	205	224	239	**872**
Deprec., Deplet., & Amort.	46	41	44	45	**176**	44	44	48	49	**186**
Oil Hedging	41	59	82	95	**277**					**-**
Currency Hedging	(3)	(2)	(3)	(7)	**(15)**	(7)	(7)	(7)	(7)	**(27)**
Non-Production	11	11	11	11	**43**	22	22	22	22	**88**
Exchange on U.S. Debt	12	21	(62)		**(29)**					**-**
Future Income Tax	(21)	(9)	(7)		**(37)**					**-**
Ebit	125	121	210	125	**582**	144	146	161	175	**626**
Interest	22	23	24	25	**95**	27	27	27	27	**109**
Net Income ($mm)	103	98	186	100	**487**	117	118	134	147	**517**
Per Unit ($)	1.18	1.12	2.06	1.10	**5.46**	1.28	1.30	1.47	1.62	**5.67**
Units (millions)	87.5	87.6	90.0	91.1	**89.3**	91.1	91.1	91.1	91.1	**91.1**
Cash Flow ($mm)	140	151	161	145	**597**	161	163	181	197	**702**
Per Unit ($)	1.62	1.77	1.75	1.59	**6.68**	1.77	1.79	1.99	2.16	**7.71**
Ratios										
Production ($/bbl)	13.09	14.73	16.65	14.76	**14.81**	15.75	15.72	14.65	14.12	**15.03**
Purchased Energy ($/bbl)	3.83	4.25	3.95	4.77	**4.19**	4.60	4.24	3.99	4.01	**4.20**
Prod&Purch En ($/bbl)	16.93	18.98	20.60	19.53	**19.00**	20.35	19.96	18.65	18.13	**19.23**
Crown Royalties & Taxes	1%	1%	1%	1%	**1%**	1%	1%	1%	1%	**1%**
Other Expense ($/bbl)	0.24	0.25	(1.11)	(0.13)	**(0.19)**	0.27	0.27	0.25	0.24	**0.26**
Ebitda Margin	59%	61%	63%	64%	**62%**	56%	56%	58%	60%	**58%**
Deprec., D,& A ($/bbl)	5.72	5.29	5.52	6.00	**5.63**	6.00	6.00	6.00	6.00	**6.00**
Interest Rate (%/yr)	4.9	4.8								
Cash Flow ($/unit)	2.16	2.50	2.78	2.68	**10.11**	1.94	1.95	2.16	2.33	**8.37**
Distribution	0.50	0.50	0.50	0.50	**2.00**	0.50	0.50	0.50	0.50	**2.00**

Cash Flow Multiple Low for Long-Life

Testing present value against the latest NTM cash flow projection results in a multiple, PV/Ebitda, of 11.1 times. In the current correlation of present value with reserve life for 28 stocks, the company's multiple could be considered high by 1.2 times above the level implied by the correlation.

A higher multiple for the trust than the correlation implies is reasonable because cash flow should soon increase when a 40% capacity expansion is expected to be fully complete by mid 2006. Another factor to keep in mind is that we have arbitrarily set the trust's adjusted reserve life to 20 years, the maximum we apply to any oil and gas property for purposes of the correlation. Syncrude reports proven reserves of 3.0 billion barrels with another 6.1 billion barrels of resources. Proven reserves amount to 23 years of supply at the rate of 350,000 barrels daily. With such a strong resource base, annual volume is likely to continue growing. Practically, we can say that current volume could last indefinitely.

Present Value by Discounted Cash Flow Analysis

The correlation is rigorous because of the combination of detail and number of companies that form our basis of analysis. Alternatively we go into more detail for each company by projecting cash flow for many years, not just the year ahead. Discounting those cash flows to the present further supports our estimate of present value of US$72 a unit (see table Present Value of Future Cash Flow).

Having erred temporarily in converting present value in Canadian dollars to net present value per unit in U.S. dollars we emphasize that the projections are in Canadian dollars. The valuation measures in the statistical summary at the top of the front page of this analysis are in U.S. dollars. Convert the estimate of C$9700 million present value of the trust's 35.5% share of the Syncrude venture to US$8100 million and we see that it matches present value for the trust in the statistical summary. Subtract debt of US$1830 and divide by 91.1 million units to get US$72 a unit.

The new capacity should be fully operational at 350,000 barrels daily in mid 2006. Some of the volume benefits of the expansion may be reflected after mid 2005.

After 2005 we assume a constant real oil price of US$35 a barrel for light, sweet crude oil. The expanded capacity will be producing Syncrude Sweet Premium. In 2007 we add a dollar a barrel to price to account for that premium.

Production costs are high currently partly due to construction, maintenance and operations below capacity. Management projects that those costs would decline to C$13.50 a barrel when the expanded capacity is running. Though we assume a constant real oil price we increase natural gas costs presuming that natural gas moves to a 20% premium to oil in ten years. Capital costs are from management's guidance for 2005 and 2006 including the amount expensed as non-production cost.

When historical capital costs are fully recovered the provincial royalty increases to 25% of cash flow. We start the full rate in 2008. There may be some unrecovered capital expense pre-2005 that would still be available to reduce royalty in 2008 as well.

When it becomes clear that royalties are about to jump there will be great incentive to begin the Phase 4 expansion. Some of the outlays being charged to the Phase 3 expansion now underway have the effect of making additional outlays in Phase 4 especially rewarding. While it seems premature to include Phase 4 in the model, its addition would further enhance present value at an oil price less than US$35 a barrel.

Canadian Oil Sands Trust
Present Value of Future Cash Flow

Present Value (US$): 8100 Discount rate (%/yr): 7.0

	Volume				Prod	Natural	Other &	Capital		Cash		Present
	Syncrude	Trust	Price	Revenue	Cost	Gas	NonOper	Exp.	Royalty	Flow	Disc	Value
Year	(mbd)	(mmb)	(US$/bbl)	(C$mm)	(C$/bbl)	(C$/bbl)	(C$/bbl)	(C$mm)	(C$mm)	(C$mm)	Factor	(C$mm)
Total 2005 through 2034; years ending on 12/31												
		1340	47.58	63738				6075	6978	22902	0.42	9700
2005	239	30.9	41.95	1553	15.03	4.20	2.27	797	16	75	0.97	72
2006	300	38.9	35.00	1797	14.00	3.59	2.27	238	18	769	0.90	695
2007	350	45.4	36.00	2157	13.50	3.77	2.27	180	22	1069	0.84	903
2008	350	45.4	36.00	2157	13.50	3.84	2.27	180	218	870	0.79	687
2009	350	45.4	36.00	2157	13.50	3.92	2.27	180	271	813	0.74	600
2010	350	45.4	36.00	2157	13.50	4.00	2.27	180	270	810	0.69	559
2011	350	45.4	36.00	2157	13.50	4.08	2.27	180	269	808	0.64	520
2012	350	45.4	36.00	2157	13.50	4.16	2.27	180	268	805	0.60	485
2013	350	45.4	36.00	2157	13.50	4.24	2.27	180	267	802	0.56	451
2014	350	45.4	36.00	2157	13.50	4.32	2.27	180	266	799	0.53	420
2015	350	45.4	36.00	2157	13.50	4.41	2.27	180	265	796	0.49	391
2016	350	45.4	36.00	2157	13.50	4.50	2.27	180	264	793	0.46	364
2017	350	45.4	36.00	2157	13.50	4.59	2.27	180	263	790	0.43	339
2018	350	45.4	36.00	2157	13.50	4.68	2.27	180	262	787	0.40	316
2019	350	45.4	36.00	2157	13.50	4.78	2.27	180	261	784	0.37	294
2020	350	45.4	36.00	2157	13.50	4.87	2.27	180	260	781	0.35	274
2021	350	45.4	36.00	2157	13.50	4.97	2.27	180	259	777	0.33	255
2022	350	45.4	36.00	2157	13.50	5.07	2.27	180	258	774	0.31	237
2023	350	45.4	36.00	2157	13.50	5.17	2.27	180	257	771	0.29	220
2024	350	45.4	36.00	2157	13.50	5.27	2.27	180	256	767	0.27	205
2025	350	45.4	36.00	2157	13.50	5.38	2.27	180	254	763	0.25	191
2026	350	45.4	36.00	2157	13.50	5.49	2.27	180	253	760	0.23	177
2027	350	45.4	36.00	2157	13.50	5.59	2.27	180	252	756	0.22	165
2028	350	45.4	36.00	2157	13.50	5.71	2.27	180	251	752	0.20	153
2029	350	45.4	36.00	2157	13.50	5.82	2.27	180	249	748	0.19	143
2030	350	45.4	36.00	2157	13.50	5.94	2.27	180	248	744	0.18	133
2031	350	45.4	36.00	2157	13.50	6.06	2.27	180	247	740	0.17	123
2032	350	45.4	36.00	2157	13.50	6.18	2.27	180	245	736	0.16	115
2033	350	45.4	36.00	2157	13.50	6.30	2.27	180	244	732	0.15	106
2034	350	45.4	36.00	2157	13.50	6.43	2.27	180	243	728	0.14	99

Distribution May Triple by 2007

The trust normally distributes all of its cash flow after debt obligations and capital expenditures. In tax-efficient fashion, the trust avoids double taxation as the distribution is virtually free of corporate tax. Government does get its fair share through a royalty to the Province of Alberta that

applies after capital expenditures are recovered. Nonetheless the potential cash generation and income distribution is quite attractive particularly in the oil price environment we envision.

We have often repeated our thesis that the distribution could triple from the current level in a few years. The current distribution is about C$180 million a year. The DCF model illustrates cash flow of almost C$800 million in 2006 all of which could be distributed. As a result, a quadrupling is in the realm of reason with oil at US$35 a barrel.

Now that the Phase 3 expansion is in its final stages it may be time to think of a higher dividend sooner. Putting ourselves in management's shoes we might expect management to wait until after the first of the year to see where oil price settles after hedges expire and how first quarter maintenance proceeds. Management might also reckon that there is some construction debt to be paid down first.

We see that the ratio of debt to present value at 0.19 times is not high by industry standards. A reasonable payout for a trust might be the equity portion of cash flow or 0.81 times Ebitda. That would be more than a tripling now. Thus, it is just the inherent conservativeness of management that keeps us from saying the distribution is likely to triple next year.

Strategic Advantages

Among the points we have emphasized is the quality of the participants in the Syncrude Joint Venture led by **ExxonMobil (XOM)** through its 70% owned affiliate **Imperial Oil (IMO)**. Investors in the trust also have the advantage that no manager or general partner extracts a disproportionate share of the rewards.

More recently we have pointed out the logic of IMO/XOM increasing their interest in the trust from 25% toward 60% by acquiring units of the trust. Of course we have no sign from IMO/XOM that such a transaction is being contemplated.

Of the three oil sands mining plants in operation, the Syncrude plant produces the highest quality crude oil product on site. As a result, oil sands profitability is high on a per barrel basis and least susceptible to deterioration when industry spreads widen between light oil and heavy oil. That has happened in recent months and is a continuing concern in the Canadian heavy oil industry. The root of the issue is that it is easier to add new heavy oil producing capacity than to add the upgrading capacity that makes the heavy oil marketable. In fact, Canadian Oil Sands unitholders have suffered with the difficulties in constructing the new upgrader for Syncrude.

Past construction problems for Syncrude as well as for the Shell and Suncor plants have a silver lining in that they discourage competition. Syncrude's problems seem to be in hand as the construction reports in recent months have shown progress slightly ahead of a revised schedule and cost slightly under a revised budget. A year ago the picture was the opposite and the situation was addressed early in 2004. Moreover all of Syncrude's equipment, made largely of steel, has been purchased and delivered ahead of steel price increases since then.

Finally, it may be that Hubbert's Peak has already been reached worldwide for light oil. That suggests a sustained rewarding price for light oil of the kind that Syncrude produces.

Kurt H. Wulff, CFA

Research Methodology/Ratings Description: McDep Associates is an independent research originator focused on oil and gas stocks exclusively. The firm applies the thirty years of experience of its analyst to estimate a present value of the oil and gas resources and other businesses of covered companies. That value is compared with a company's stock market capitalization and debt. Stocks with low market cap and debt relative to present value tend to outperform stocks with high market cap and debt relative to present value. Buy recommendations are expected to deliver a total return better than 7% per year above inflation. Hold recommendations assume the attributes of the underlying business are reflected in the current price of the stock. Sell recommendations are expected to deliver a negative total return less than 7% per year including the effects of inflation.

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