Rating: Buy
S&P 500: 1201

Encore Acquisition Company
Raise Net Present Value to $57 a Share

Symbol	EAC	*Ebitda Next Twelve Months ending 3/31/06 (US$mm)*	284
Rating	Buy	*North American Natural Gas/Ebitda (%)*	27
Price ($/sh)	38.34	*Natural Gas and Oil Production/Ebitda (%)*	100
Pricing Date	2/17/05	*Adjusted Reserves/Production NTM*	15.6
Shares (mm)	33	*EV/Ebitda*	5.9
Market Capitalization ($mm)	1,250	*PV/Ebitda*	8.1
Debt ($mm)	430	*Undeveloped Reserves (%)*	29
Enterprise Value (EV) ($mm)	1,680	*Natural Gas and Oil Ebitda ($/boe)*	29.80
Present Value (PV) ($mm)	2,290	*Present Value Proven Reserves($/boe)*	13.20
Net Present Value ($/share)	57	*Present Value Proven Reserves($/mcfe)*	2.20
Debt/Present Value	0.19	*Earnings Next Twelve Months (US$/sh)*	2.91
McDep Ratio - EV/PV	0.73	*Price/Earnings Next Twelve Months*	13
Dividend Yield (%/year)	0.0	*Indicated Annual Dividend (US$/sh)*	0.00

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

We continue to recommend current purchase of the common shares of **Encore Acquisition (EAC)** as a small cap oil producer with long life production. We raised our estimate of net present value for the independent producer to $57 a share from $47 on January 26, 2005 when we revised our estimate of long-term oil price to $40 a barrel constant real from $35. The new NPV matches the level previously calculated in a sensitivity illustration (see *Stock Idea*, Encore Acquisition Company, September 3, 2004). We see potential appreciation of 49% to our new estimate of net present value.

Cedar Creek Anticline Yielding More Volume

Encore's proven reserves in the Cedar Creek Anticline (CCA) of Montana and North Dakota account for two-thirds of corporate reserves. The essence of the opportunity is the potential increase in the recovery factor for CCA reserves. The upside is appealing because currently booked reserves of about the 114 mmb reflect a recovery factor of only 20% of original oil in place (ooip).

Conventional upside, as Encore calls it, would add 41 mmb while taking recovery factor to 22%. The techniques primarily involve more efficient horizontal wells that include some water injectors for secondary recovery.

Next Encore is tapping the Red River U4 formation with High Pressure Air Injection as a means of tertiary recovery. The RRU4 HPAI prospects have been proven for an area on the flanks of the CCA operated by private company, Continental Resources. RRU4 HPAI would add 57 mmb proven reserves to take recovery factor to 25%.

Finally because Encore's acreage is on the crest of the CCA rather than on the flanks, it may have additional HPAI potential in zones that are now producing on the crest, but not on the flanks. Another 144 mmb of potential reserves outside the RRU4 would take recovery factor to 32% that is still modest compared to most successful oil fields.

Concentrated on Long-Life Oil

Already the reserves booked on the CCA contribute to a long life for Encore's oil production that in turn supports higher present value as a multiple of cash flow (see table Functional Cash Flow and Present Value). The company's natural gas properties may contribute more growth initially as it takes time for the high pressure air injection to contribute new oil production.

Encore Acquisition Company
Functional Cash Flow and Present Value

	NTM Ebitda (US$mm)	*Adjusted R/P*	*PV/ Ebitda*	*Present Value (US$mm)*	
North American Natural Gas	76	11.9	8.6	650	28%
Oil	208	17.1	7.9	1,640	72%
	284	15.6	8.1	2,290	100%
Debt (US$mm)					430
Net Present Value (US$mm)					1,860
Shares (mm)					33
Net Present Value (US$/sh)					57

Management Expects 10% Volume Growth in 2005

Continued production in 2005 at the rate of the fourth quarter of 2004 implies total 2005 production 6% higher than 2004 (see table Next Twelve Months Operating and Financial Estimates). Management expects an increase of 8% to 12%. Such gains appear likely. In any event a long reserve life offers protection against unexpected sharp decline.

Commodity prices from the futures market imply gradual erosion of recent gains. Futures are usually backwardated, jargon for the pattern of decline. Futures may have a downward bias because traders have to make some money. Nonetheless we use futures in making our estimates because they are a widely quoted reference. Our own view is that actual prices are likely to be higher than futures most of the time over the next several years, but we can not rule out temporary periods of lower price.

The high rate of cash flow implies a low multiple of Enterprise Value to Ebitda near six times. The low multiple does not seem to reflect fully a reserve life more than fifteen years on our adjusted basis.

Encore Acquisition Company
Next Twelve Months Operating and Financial Estimates

	Q3 9/30/04	*Q4 12/31/04*	***Year 2004***	*Q1E 3/31/05*	*Q2E 6/30/05*	*Q3E 9/30/05*	*Q4E 12/31/05*	***Year 2005E***	*Q1E 3/31/06*	***Next Twelve Months 3/31/06***
Volume										
Natural Gas (mmcfd)	44.2	46.7	**38.5**	46.7	46.7	46.7	46.7	**46.7**	46.7	**46.7**
Oil (mbd)	18.42	18.32	**18.25**	18.32	18.32	18.32	18.32	**18.32**	18.32	**18.32**
Total (mbd)	25.8	26.1	**24.7**	26.1	26.1	26.1	26.1	**26.1**	26.1	**26.1**
Price										
Henry Hub ($/mmbtu)	5.75	7.10	**6.15**	6.14	6.10	6.27	6.66	**6.29**	7.16	**6.55**
Differential ($/mmbtu)	0.45	0.41	**0.39**	0.41	0.35	0.36	0.38	**0.36**	0.38	**0.38**
EAC ($/mcf)	5.30	6.69	**5.76**	5.79	5.75	5.91	6.28	**5.93**	6.75	**6.17**
WTI Cushing ($/bbl)	43.89	48.30	**41.44**	47.12	48.56	48.01	46.92	**47.65**	45.84	**47.33**
Differential	3.48	4.45	**3.19**	4.45	4.47	4.42	4.32	**4.39**	4.32	**4.35**
EAC ($/bbl)	40.41	43.85	**38.25**	42.78	44.09	43.59	42.60	**43.26**	41.62	**42.98**
Total ($/bbl)	37.95	42.74	**37.29**	40.38	41.22	41.16	41.13	**40.98**	41.28	**41.20**
Revenue ($mm)										
Natural Gas	22	29	**81**	24	24	25	27	**101**	28	**105**
Oil	68	74	**255**	71	73	73	72	**289**	69	**287**
Total	90	103	**336**	95	98	99	99	**390**	97	**392**
Expense										
Lease operating	13	13	**47**	13	13	13	13	**52**	13	**52**
Production taxes	8	9	**30**	9	9	9	9	**35**	9	**35**
General and administrative	4	5	**17**	5	5	5	5	**21**	5	**21**
Total	25	28	**94**	27	27	27	27	**109**	27	**109**
Ebitda	65	75	**242**	68	71	71	71	**282**	70	**284**
Exploration	0	2	**4**	1	1	1	1	**4**	1	**4**
Deprec., Deplet., & Amort.	13	15	**49**	16	16	16	16	**65**	16	**65**
Hedging and other	13	11	**39**	11	12	11	11	**45**	12	**46**
Ebit	39	47	**150**	41	43	45	44	**172**	42	**173**
Interest	6	7	**23**	7	7	7	7	**27**	7	**27**
Ebt	32	40	**126**	34	36	38	37	**145**	35	**146**
Income Tax	11	14	**44**	12	13	13	13	**51**	12	**51**
Net Income ($mm)	21	26	**82**	22	23	25	24	**95**	23	**95**
Per Share ($)	0.64	0.80	**2.57**	0.67	0.71	0.75	0.75	**2.89**	0.70	**2.91**
Shares (millions)	33	33	**32**	33	33	33	33	**33**	33	**33**
Lease operating ($/bbl)	5.31	5.58	**5.24**	5.50	5.50	5.50	5.50	**5.50**	5.50	**5.50**
Production taxes (%rev)	9.0	9.0	**9.0**	9.0	9.0	9.0	9.0	**9.0**	9.0	**9.0**
General and admin ($/bbl)	1.78	2.20	**1.87**	2.25	2.23	2.20	2.20	**2.22**	2.25	**2.22**
Deprec., D,& A ($/bbl)	5.38	6.36	**5.39**	6.80	6.80	6.80	6.80	**6.80**	6.80	**6.80**
Ebitda Margin	72%	73%	**72%**	72%	72%	72%	72%	**72%**	72%	**72%**
Tax rate	35%	35%	**35%**	35%	35%	35%	35%	**35%**	35%	**35%**

Encore Founder a Serial Value Creator

Mr. Jon Brumley, the founder of Encore, has a long, distinguished career guiding or creating five successful public oil and gas stocks before founding his latest venture. He was the driving force as president of Southland Royalty when its stock multiplied in the 1970s, the founder of **San Juan Basin Royalty Trust (SJT)** and **Permian Basin Royalty Trust (PBT)** in 1980, **Cross Timbers Royalty Trust (CRT)** in 1992 and **XTO Energy (XTO)** which first went public in 1993.

Buy Oil and Gas Producers at Mid Decade

Encore stock appears undervalued in an attractive group for investment (see table Rank by McDep Ratio). Three to five-fold gain potential for oil and gas price over the next 5 to 13 years justifies investment in recommended oil and gas producers, in our opinion. Supporting improving prospects, the average futures price of oil for continuous delivery over the next six years is in a multi-year uptrend as defined by the current quotes above the 40-week average. The current benchmark oil average futures price for the next six years is about $42 a barrel.

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

	Symbol/	Rating	Price ($/sh) 17-Feb 2005	Shares (mm)	Market Cap ($mm)	Net Present Value ($/sh)	Debt/ Present Value	McDep Ratio
Independent Natural Gas and Oil - Small Cap								
Berry Petroleum Company	BRY	B	55.57	22	1,240	50.00	0.05	1.10
Energy Partners Ltd.	EPL	B	24.43	39	960	24.00	0.24	1.01
Cimarex Energy Company	XEC	B	37.34	43	1,600	44.00	0.00	0.85
Encore Acquisition Company	EAC	B	38.34	33	1,250	57.00	0.19	0.73
Total or Median					*5,100*		*0.12*	*0.93*

B = Buy, S2 = Short half unlevered position, S3 = Short quarter unlevered position
McDep Ratio = **M**arket **c**ap and **De**bt to **p**resent value of oil and gas and other businesses

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Please see disclosures on the final page.