



Independent Stock Idea

October 29, 2008

rating: hold
s&p 500: 930

Encore Acquisition Company (EAC) Success with ExxonMobil in West Texas

<i>Symbol</i>	EAC	<i>Ebitda Next Twelve Months ending 9/30/09 (US\$mm)</i>	407
<i>Rating</i>	Hold	<i>North American Natural Gas/Ebitda (%)</i>	22
<i>Price (\$/sh)</i>	27.33	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	10/29/08	<i>Adjusted Reserves/Production NTM</i>	13.4
<i>Shares (mm)</i>	54	<i>EV/Ebitda</i>	7.3
<i>Market Capitalization (\$mm)</i>	1,460	<i>PV/Ebitda</i>	10.0
<i>Debt (\$mm)</i>	1,500	<i>Undeveloped Reserves (%)</i>	32
<i>Enterprise Value (EV) (\$mm)</i>	2,960	<i>Natural Gas and Oil Ebitda (\$/boe)</i>	28.10
<i>Present Value (PV) (\$mm)</i>	4,070	<i>Present Value Proven Reserves(\$/boe)</i>	17.60
<i>Net Present Value (\$/share)</i>	48	<i>Present Value Proven Reserves(\$/mcf)</i>	2.90
<i>Debt/Present Value</i>	0.37	<i>Earnings Next Twelve Months (US\$/sh)</i>	1.25
<i>McDep Ratio - EV/PV</i>	0.73	<i>Price/Earnings Next Twelve Months</i>	22
<i>Dividend Yield (%/year)</i>	0.0	<i>Indicated Annual Dividend (US\$/sh)</i>	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.			
Estimated present value presumes a long-term price for oil of US\$75 a barrel and natural gas, \$10 a million bu.			
For historical research on Encore since 2003 see http://www.mcdep.com/4eac.htm			

Summary and Recommendation

Hold-rated **Encore Acquisition Company (EAC)** offers unlevered appreciation potential of 37% to estimated net present value (NPV) of \$48 a share. On October 28 we reset NPV from \$75 a share on the basis of a long-term oil price assumption of \$75 a barrel, down from \$100. Patience may be necessary as EAC stock price remains below the 200-day average of \$48. Released today, third quarter results displayed strength in unlevered cash flow (Ebitda) driven by higher crude oil and natural gas prices. Futures prices now look lower for the next four quarters (see table Next Twelve Months Operating and Financial Estimates). Projected cash flow capitalized at unlevered multiples (PV/Ebitda) related to reserve life (Adjusted R/P) supports NPV (see table Functional Cash Flow and Present Value). A joint venture with **ExxonMobil (XOM)** in the Permian Basin of West Texas contributed noticeably to higher natural gas volume in the latest quarter. The financial terms are tough for EAC, but the quality of the resource is high. That project is helping the company get past the non-recurring reporting effect of acquisitions and divestitures in 2007 and to post a rising volume trend in 2008 (see chart Oil and Gas Production Volume).

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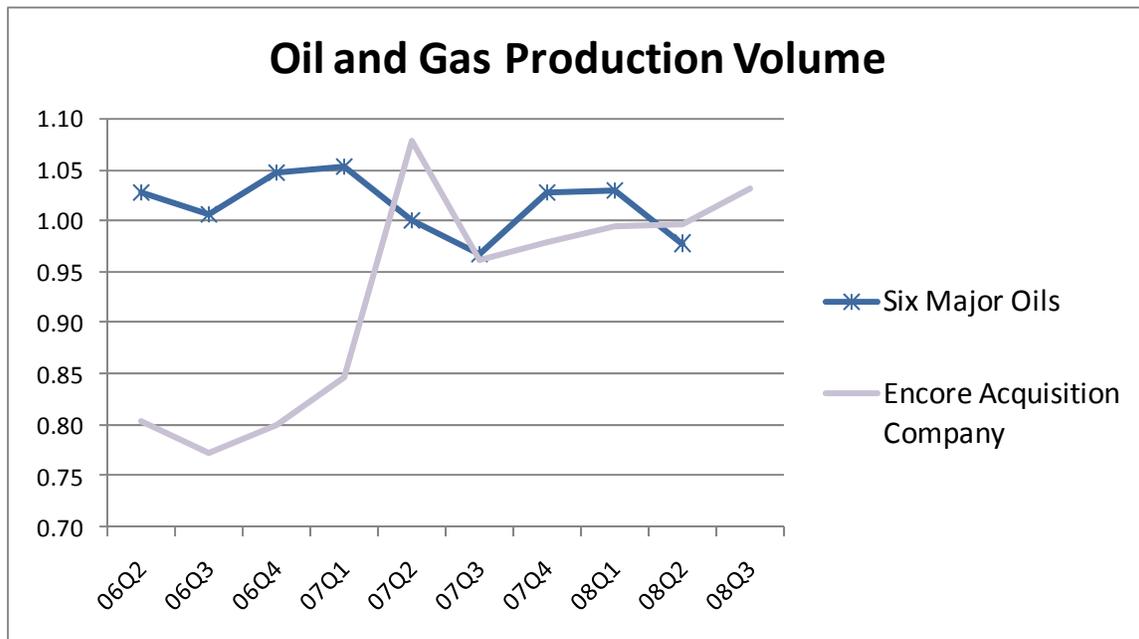
Encore Acquisition Company									
Next Twelve Months Operating and Financial Estimates									
									<i>Next</i>
	<i>Q3</i>	<i>Q2</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Twelve</i>
	<i>9/30/07</i>	<i>6/30/08</i>	<i>9/30/08</i>	<i>12/31/08</i>	<i>2008E</i>	<i>3/31/09</i>	<i>6/30/09</i>	<i>9/30/09</i>	<i>Months</i>
	<i>9/30/07</i>	<i>6/30/08</i>	<i>9/30/08</i>	<i>12/31/08</i>	<i>2008E</i>	<i>3/31/09</i>	<i>6/30/09</i>	<i>9/30/09</i>	<i>9/30/09</i>
Volume									
Natural Gas (mmcf)	57.9	67.1	75.8	75.8	70.7	75.8	75.8	75.8	75.8
Days	92	91	92	92	366	90	91	92	365
Oil (mbd)	27.3	27.0	27.0	27.0	27.12	27.0	27.0	27.0	26.98
Total (mb)	3,396	3,477	3,645	3,645	14,243	3,565	3,605	3,645	14,460
Total (mbd)	36.9	38.2	39.6	39.6	38.9	39.6	39.6	39.6	39.6
Price									
Henry Hub (\$/mmbtu)	6.16	10.93	10.25	6.65	8.96	6.65	6.67	6.97	6.73
Differential (\$/mmbtu)	0.07	(0.19)	0.68	0.44	0.22	0.67	0.67	0.70	0.62
EAC (\$/mcf)	6.09	11.12	9.57	6.21	8.74	5.99	6.00	6.28	6.12
WTI Cushing (\$/bbl)	75.48	123.97	117.99	67.52	101.86	64.23	65.80	67.22	66.19
Differential	12.00	7.33	9.78	5.59	7.94	5.32	5.45	5.57	5.47
EAC (\$/bbl)	63.48	116.64	108.21	61.92	93.91	58.91	60.35	61.65	60.72
Total (\$/bbl)	56.44	102.03	92.00	54.05	81.35	51.57	52.58	53.99	53.06
Revenue (\$mm)									
Natural Gas	32	68	67	43	226	41	41	44	169
Oil	159	287	269	154	932	143	148	153	598
Total	192	355	335	197	1,159	184	190	197	767
Expense									
	70	143	126	93	480	86	89	92	361
Ebitda									
	122	212	210	104	679	97	100	104	407
Exploration	9	12	13	13	43	13	13	13	52
Deprec., Deplet., & Amort.	49	51	58	58	217	57	58	58	231
Partnership, hedging, other	2		26		28	-	-		-
Ebit									
	62	149	113	46	404	40	43	46	175
Interest	24	16	18	18	71	18	18	18	72
Ebt									
	38	133	95	28	333	22	25	28	103
Income Tax	13	46	33	10	108	8	9	10	36
Net Income (\$mm)									
	25	86	62	18	224	15	16	18	67
Per Share (\$)	0.46	1.65	1.15	0.34	4.22	0.27	0.30	0.34	1.25
Shares (millions)									
	54	52	54	54	53	54	54	54	54
Ebitda Margin	64%	60%	63%	53%	59%	53%	53%	53%	53%
Tax rate	35%	35%	35%	35%	33%	35%	35%	35%	35%



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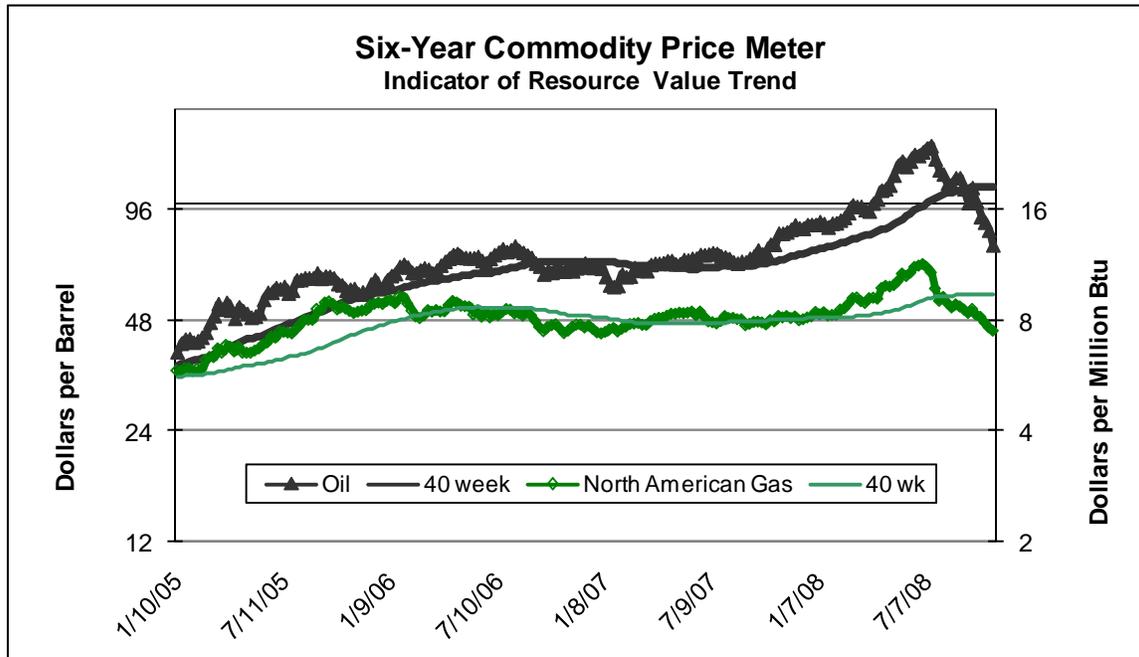
Encore Acquisition Company					
Functional Cash Flow and Present Value					
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Present</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>Value</i>	
				<i>(US\$mm)</i>	
North American Natural Gas	90	8.1	7.8	700	17%
Oil	317	15.9	10.6	3,370	83%
	407	13.4	10.0	4,070	100%
Debt (US\$mm)					1,500
Net Present Value (US\$mm)					2,570
Shares (mm)					54
Net Present Value - Standard Estimate (US\$/sh)					48
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					46





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