

McDep Energy Income Producers

A Weekly Analysis of Royalty Trusts and Master Limited Partnerships

March 30, 2004

Canada's Budget 2004

Summary and Recommendation

Though royalty trusts attracted some unwanted attention when Canada's Department of Finance presented its budget on Tuesday, March 23, the proposals imply no change in our buy recommendation of **Canadian Oils Sands Trust (COSWF)**. Nor do we see any changes likely to affect the McDep Ratios we calculate for other Canadian royalty trusts in our coverage, **Pengrowth Energy Trust (PGH)**, **Enerplus Resources Fund (ERF)** and **Provident Energy Trust (PVX)**. The finance minister signals more careful attention to non-Canadian ownership that is not a problem now for COS. The possible taxing of capital gains for non-resident taxpayers seems of minor consequence, if any, to U.S. taxpayers for whom the 15% of distributions withheld by Canada can be largely recovered through the Foreign Tax Credit to U.S. taxes. Nonetheless, McDep Ratios increase for ERF and PVX as we omit explicit recognition of probable reserves as we did recently for PGH.

Revise Consideration of Probable Reserves

Until recently we included an amount of probable reserves suggested by ERF, PVX and PGH in our calculation of adjusted reserve life. We realize that proven-only reserves typically have a 90% or more probability of being exceeded. The concept was developed originally for lenders who needed high assurance of repayment. Equity investors, by definition, assume higher risks, presumably for higher returns. As a result, equity analysis takes account of enhancement of reserves beyond "lender" standards.

Now we are dealing with future potential more fully with revised cash flow multiple. The across-the-board revaluation on March 22 anticipated that current one-year natural gas and oil futures pointed to higher price for many years. When the new guide to cash flow multiple is applied against proven-only reserves it leads to attractive value for most producers. We remain conscious of differences in the quality of estimates of proven reserves and are open to modifying our interpretation when prospects seem justified.

Lower Present Value for Enerplus and Provident

After boosting present value for ERF and PVX in an across the board increase a week ago, we now lower present value for ERF and PVX. ERF's stock price implies reasonable value at a McDep Ratio near 1.00 while PVX's stock price implies borderline value at a McDep Ratio just under 1.20 (see table, [Rank by McDep Ratio](#)).

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ERF has a cash flow multiple near the median while PVX has a cash flow multiple less than the median (see table, Rank by EV/Ebitda). Cash flow multiple is not as complete a value indicator as the McDep Ratio. In the same table we print our assessed cash flow multiple (see column, *PV/Ebitda*). Our assessed cash flow multiple is somewhat below the median for ERF and well below the median for PVX.

The McDep Ratio also happens to be the ratio of the market cash flow multiple, *EV/Ebitda*, to the assessed cash flow multiple, *PV/Ebitda*. Explaining *PV/Ebitda* makes our rationale more transparent.

Adjusted reserve life is the most important determinant of assessed cash flow multiple. ERF has a ratio of proven producing plus half of proven non-producing reserves to next twelve months production of 9.3 years. That compares to PVX's adjusted reserve life of 4.0 years (see column, *Adjusted Reserves/Production NTM* in table, Determinants of Present Value).

Our starting point for assessed cash flow multiple is 2.5 plus 0.5 time adjusted reserve life. That implies a cash flow multiple for ERF of 7.2. There are two explanations for the higher assessed cash flow multiple of 7.9. Half the premium is qualitative and the other half reflects lower one-year commodity futures compared to those of March 22, 2004, when the formula was applied across the board.

Provident Energy Trust Augments Short Reserve Life with Processing Plant

PVX has a related business that reduces concentration on natural gas and oil production to 77% (see column, *NG & O Prod/Ebitda*). We assess the multiple on PVX's natural gas processing business at 8 times, near the amount paid in the acquisition of the properties last year. Management points out that the longer life of the processing business adds stability to its cash flow.

PVX's adjusted reserve life of only 4.0 years translates to a cash flow multiple of 4.5. The weighted average of 77% at 4.5 and 23% at 8.0 is 5.3. Our assessed multiple of 6.1 is the lowest we can use and still have a McDep Ratio no higher than 1.2, our arbitrary limit on the recent revaluation of producing properties. Perhaps we are missing some source of value in PVX.

PVX may be eying the high valuation of U.S. income stocks concentrated on the pipeline and processing business rather than production. On that basis the acquisition of a mid stream business looks like a smart move. While we are wary of carrying that too far, PVX seems far from as highly valued as the largest U.S. master limited partnership.

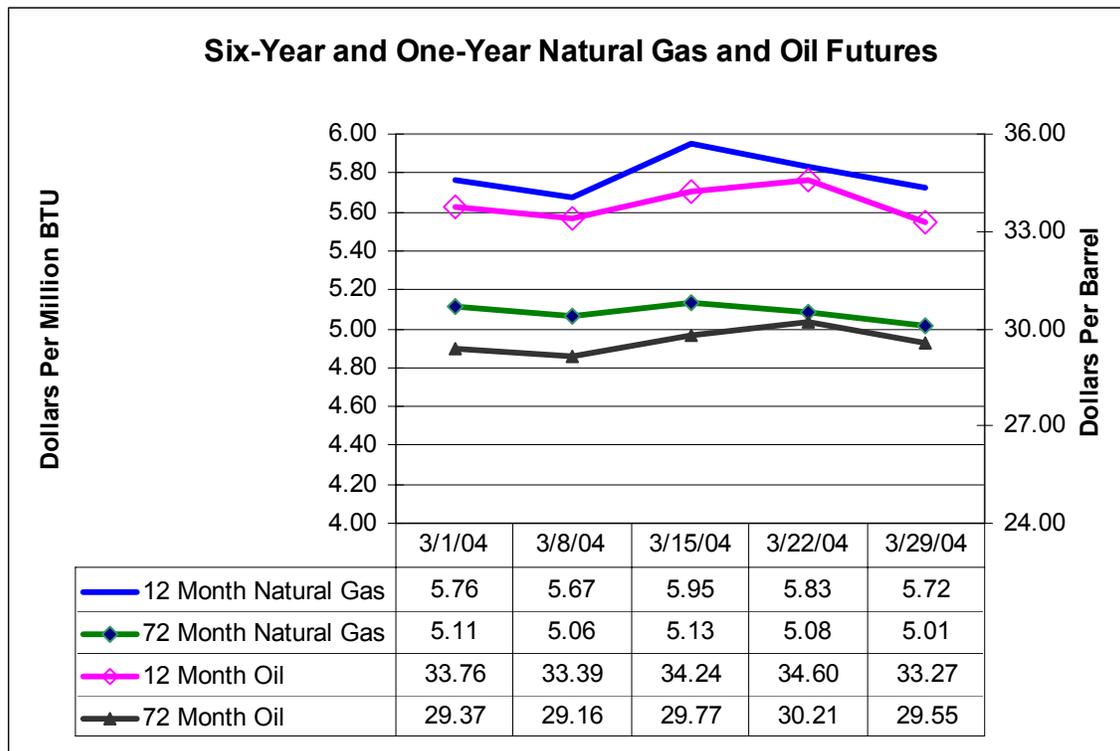
Kurt H. Wulff, CFA

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

	Symbol/ Rating	Price (\$/sh) 29-Mar 2004	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
Master Limited Partnerships and Canadian Royalty Trusts							
Kinder Morgan Energy Partners, L.P.	KMP s	44.00	140.1	6,160	14.00	0.48	2.11
Kinder Morgan Management, LLC	KMR s	41.00	48.6	1,990	14.00	0.48	2.00
Provident Energy Trust	PVX	8.07	85.0	690	6.20	0.36	1.19
Dorchester Minerals, L.P.	DMLP	18.15	27.0	490	17.00	-	1.07
Enerplus Resources Fund	ERF	28.72	90.4	2,600	28.00	0.13	1.02
Pengrowth Energy Trust	PGH	13.76	122.0	1,680	14.00	0.14	0.99
Canadian Oil Sands Trust (US\$)	COSWF B	32.97	86.9	2,870	62.00	0.19	0.62
<i>Total or Median</i>				<i>16,500</i>		<i>0.19</i>	<i>1.07</i>
U.S. Royalty Trusts							
Permian Basin RT (41%)	PBT	8.98	19.1	170	7.70	-	1.17
Sabine Royalty Trust	SBR	31.20	14.6	460	27.00	-	1.16
Hugoton Royalty Trust (46%)	HGT	21.12	18.4	390	22.00	-	0.96
San Juan Basin Royalty Trust	SJT B	20.24	46.6	940	22.00	-	0.92
Cross Timbers Royalty Trust	CRT	28.00	6.0	170	30.00	-	0.93
<i>Total or Median</i>				<i>2,100</i>		<i>-</i>	<i>0.96</i>

Buy/Sell rating after symbol: B - Buy full unlevered position, s - short quarter unlevered position

McDep Ratio = Market cap and Debt to present value of oil and gas and other businesses

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Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

	Symbol/ Rating	Price (\$/sh) 29-Mar 2004	EV/ Sales NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)	PV/ Ebitda NTM
Master Limited Partnerships and Canadian Royalty Trusts							
Kinder Morgan Energy Partners, L.P.	KMP s	44.00	3.2	18.8	22	6.2	8.9
Kinder Morgan Management, LLC	KMR s	41.00	3.0	17.8	21	6.6	8.9
Dorchester Minerals, L.P.	DMLP	18.15	9.5	10.4	24	9.6	9.8
Canadian Oil Sands Trust (US\$)	COSWF B	32.97	4.3	8.2	13	4.6	13.3
Enerplus Resources Fund	ERF	28.72	5.4	8.1	20	11.2	7.9
Provident Energy Trust	PVX	8.07	5.1	7.3	25	13.6	6.1
Pengrowth Energy Trust	PGH	13.76	4.7	6.7	14	14.0	6.8
	<i>Median</i>		4.7	8.2	21	9.6	8.9
U.S. Royalty Trusts							
Cross Timbers Royalty Trust	CRT	28.00	8.4	11.7	12	8.3	12.6
Sabine Royalty Trust	SBR	31.20	10.1	10.5	10	9.6	9.0
Permian Basin RT (41%)	PBT	8.98	7.1	9.9	11	8.4	8.5
Hugoton RoyaltyTrust (46%)	HGT	21.12	6.5	8.6	10	9.6	9.0
San Juan Basin Royalty Trust	SJT B	20.24	6.6	8.0	10	9.9	8.7
	<i>Median</i>		7.1	9.9	10	9.6	9.0

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended March 31, 2005; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

Determinants of Present Value

	Symbol/ Rating	NG & O Prod/ Ebitda (%)	N. Am. Gas/ Ebitda (%)	Adjusted Reserves/ Production NTM	PV/ Ebitda NTM	NG&O Ebitda/ mcf	Natural Royalty (%)
Master Limited Partnerships and Canadian Royalty Trusts							
Provident Energy Trust	PVX	77	51	4.0	6.1	2.92	-
Pengrowth Energy Trust	PGH	100	39	7.7	6.8	2.34	-
Enerplus Resources Fund	ERF	100	58	9.3	7.9	3.01	-
Kinder Morgan Energy Partners, L.P.	KMP s	12	-	10.0	8.9		
Kinder Morgan Management, LLC	KMR s	12	-	10.0	8.9		
Dorchester Minerals, L.P.	DMLP	100	83	10.3	9.8	4.51	54
Canadian Oil Sands Trust (US\$)	COSWF B	100	(9)	20.0	13.3	2.69	-
	<i>Median</i>		39	10.0	8.9	2.92	
U.S. Royalty Trusts							
Sabine Royalty Trust	SBR	100	63	6.5	9.0	4.28	100
Permian Basin RT (41%)	PBT	100	44	9.0	8.5	3.14	24
San Juan Basin Royalty Trust	SJT B	100	99	11.7	8.7	3.47	-
Hugoton RoyaltyTrust (46%)	HGT	100	93	11.9	9.0	3.66	-
Cross Timbers Royalty Trust	CRT	100	75	12.7	12.6	3.83	85
	<i>Median</i>		75	11.7	9.0	3.66	

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