

Rating: Buy  
S&P 500: 1178

## Imperial Oil Limited The Unpromoters

<i>Symbol</i>	IMO	<i>Ebitda Next Twelve Months ending 9/30/06 (US\$mm)</i>	4,600
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	26
<i>Price (US\$/sh)</i>	82.64	<i>Natural Gas and Oil Production/Ebitda (%)</i>	75
<i>Pricing Date</i>	10/20/05	<i>Adjusted Reserves/Production NTM</i>	11.5
<i>Shares (mm)</i>	341	<i>EV/Ebitda</i>	6.8
<i>Market Capitalization (US\$mm)</i>	28,100	<i>PV/Ebitda</i>	6.9
<i>Debt (US\$mm)</i>	3,200	<i>Undeveloped Reserves (%)</i>	24
<i>Enterprise Value (EV) (US\$mm)</i>	31,300	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	32.20
<i>Present Value (PV) (US\$mm)</i>	31,800	<i>Present Value Proven Reserves(US\$/boe)</i>	17.04
<i>Net Present Value (US\$/share)</i>	84	<i>Present Value Proven Reserves(US\$/mcfe)</i>	2.84
<i>Debt/Present Value</i>	0.10	<i>Earnings Next Twelve Months (US\$/sh)</i>	7.27
<i>McDep Ratio - EV/PV</i>	0.99	<i>Price/Earnings Next Twelve Months</i>	11
<i>Dividend Yield (%/year)</i>	1.0	<i>Indicated Annual Dividend (US\$/sh)</i>	0.82

Note: Estimated cash flow and earnings tied to one-year futures prices for oil, natural gas and refinery crack.

Reported results may vary widely from estimates. Estimated present value per share revised only infrequently.

### Summary and Recommendation

Buy-recommended **Imperial Oil (IMO)** has solid prospects though it may not have the lowest McDep Ratio among its peers. Current industry conditions are more favorable than the expectations in our estimate of net present value of \$84 a share. At the same time projections that take account of recent quarterly results and reserves reported earlier fall short of justifying the present value estimate by the correlation with 30 companies. Valuable Arctic natural gas and a new oil sands plant are not explicitly counted in our value. Like the management of 70% owner, **Exxon Mobil (XOM)**, IMO management talks down oil industry profit prospects. No point in encouraging tax collectors and competitors. Down 30% from its recent high price, Canada's energy blue chip seems likely to reward investors again. Financial risk is low.

### Oil Price and Refining Crack above Long-Term Expectations

Six-year futures for oil are well above the \$50 a barrel expectation in our present value analysis (see table Oil and Gas Commodity and Stock Price). And Imperial's stock price is about in line with estimated present value as attested by a McDep Ratio near 1.0.

### Proven Reserves Understate Resource Potential

Estimated net present value of \$84 a share appears to be about \$6 higher than the amount indicated by the correlation of projected cash flow and reserve life for 30 companies (see table Functional Cash Flow and Present Value). Imperial's natural gas reserve life looks too low to be realistic. In addition trillions of cubic feet of Arctic resources are not included. The company is taking a hard line that the increasing share of resource value that the natives understandably want to claim should come from a redistribution of government take, not from operating company profits. The stakes are too important for the parties not to come to an accommodation.

Please see disclosures on the final page.

**Oil and Gas Commodity and Stock Price**  
**Thursday, October 20, 2005**

	<u>Units</u>	<u>Futures Price</u>		<u>McDep Ratio</u>
		<u>Six-Year</u>	<u>One-Year</u>	<u>Denominator</u>
<b>Crude Oil</b>	\$/barrel	56.28	60.16	50
<b>Natural Gas</b>	\$/million btu	8.48	11.58	10
<b>Oil Refining</b>	\$/barrel		13.26	10
				<u>Median</u>
	<u>Stocks</u>			<u>McDep Ratio</u>
	<b>Producer/Refiner</b>			0.78
	<b>Imperial Oil</b>			0.99

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

**Imperial Oil Limited**  
**Functional Cash Flow and Present Value**

	<u>NTM Ebitda</u>	<u>Adjusted</u>	<u>PV/</u>	<u>Present</u>	
	<u>(US\$mm)</u>	<u>R/P</u>	<u>Ebitda</u>	<u>Value</u>	
				<u>(US\$mm)</u>	
North American Natural Gas	1,169	4.2	3.4	4,000	13%
Syncrude	901	20.0	11.2	10,100	32%
Oil - Conventional and Cold Lake	1,371	12.3	7.1	9,700	31%
Downstream	1,142		7.0	8,000	25%
	4,584	11.5	6.9	31,800	100%
Debt (US\$mm)				3,200	
Net Present Value (US\$mm)				28,600	
Shares (mm)				341	
Net Present Value (US\$/sh)				84	
Over (-)/ Under (+) Correlation (US\$/sh)					(6)

**Kearl Oil Sands Project Not Counted Yet**

The company expects approval soon for plans to construct an oil sands plant beginning in 2007 and producing in 2010. The project has potential present value in the billions of dollars. It strikes us that the timetable is highly optimistic considering the backlog of similar projects underway. Nonetheless most of the high quality land to support the projects of the future is already under lease and Imperial's position is valuable.

**Rising Near Term Cash Flow**

Recent oil, natural gas and refined product price increase have only started to be reflected in the quarter just ended (see table Next Twelve Months Operations).

**Please see disclosures on the final page.**

**Imperial Oil Limited**  
**Next Twelve Months Operations**  
 (Canadian Dollars)

	<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>2004</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>
<b>Volume</b>											
Natural Gas (mmcf/d)	524	<b>500</b>	522	514	513	513	<b>515</b>	513	513	513	<b>513</b>
Oil (mbd)	242	<b>230</b>	233	235	209	208	<b>221</b>	208	207	207	<b>208</b>
Total gas & oil (bcf)	182	<b>688</b>	173	175	163	162	<b>673</b>	158	160	161	<b>642</b>
Total gas & oil (mbd))	329	<b>313</b>	320	321	295	294	<b>307</b>	293	293	292	<b>293</b>
<b>Price</b>											
Natural gas (\$/mcf)											
Henry Hub (\$/mmbtu)	7.10	<b>6.15</b>	6.27	6.76	8.56	13.39	<b>8.75</b>	13.49	10.36	10.30	<b>11.89</b>
Currency (US\$/C\$)	0.82	<b>0.77</b>	0.82	0.80	0.85	0.85	<b>0.83</b>	0.85	0.85	0.85	<b>0.85</b>
Henry Hub (C\$/mmbtu)	8.66	<b>7.98</b>	7.68	8.40	10.09	15.77	<b>10.54</b>	15.89	12.19	12.13	<b>14.00</b>
Canada (C\$/mcf)	7.12	<b>6.79</b>	7.02	7.71	8.80	13.76	<b>9.33</b>	13.86	10.64	10.58	<b>12.20</b>
Oil (\$/bbl)											
WTI Cushing	48.31	<b>41.44</b>	49.65	53.05	62.52	61.10	<b>56.58</b>	60.11	60.16	60.05	<b>60.35</b>
WTI Cushing (C\$/bbl)	58.94	<b>53.68</b>	60.85	65.99	73.66	71.95	<b>68.11</b>	70.78	70.84	70.71	<b>71.07</b>
Worldwide	43.85	<b>42.85</b>	45.43	49.85	63.00	61.54	<b>54.61</b>	57.62	57.64	57.51	<b>58.59</b>
Total gas & oil (\$/mcf)	7.26	<b>7.05</b>	7.43	8.15	10.01	11.27	<b>9.17</b>	10.84	9.91	9.88	<b>10.48</b>
NY Harbor 3-2-1 (\$/bbl)	5.72	<b>7.74</b>	6.17	10.59	16.70	12.24	<b>11.43</b>	13.37	14.57	13.69	<b>13.47</b>
<b>Revenue (\$mm)</b>											
Natural Gas	343	<b>1,242</b>	331	361	415	649	<b>1,756</b>	640	497	499	<b>2,285</b>
Oil	976	<b>3,603</b>	953	1,066	1,211	1,180	<b>4,410</b>	1,078	1,088	1,095	<b>4,441</b>
Other	4,793	<b>17,615</b>	4,674	5,375	6,084	6,084	<b>22,218</b>	6,084	6,084	6,084	<b>24,338</b>
Total	6,113	<b>22,460</b>	5,958	6,802	7,711	7,914	<b>28,385</b>	7,803	7,669	7,679	<b>31,064</b>
<b>Expense (\$mm)</b>											
Fixed	305	<b>975</b>	360	293	328	328	<b>1,309</b>	328	330	330	<b>1,009</b>
Variable	305	<b>975</b>	360	293	328	369	<b>1,350</b>	347	320	322	<b>916</b>
Other	4,463	<b>16,529</b>	4,390	5,172	5,771	6,445	<b>21,780</b>	6,423	6,398	6,400	<b>16,271</b>
<b>Ebitda (\$mm)</b>											
Exploration and Production	709	<b>2,895</b>	564	841	970	1,132	<b>3,507</b>	1,044	935	943	<b>4,053</b>
Other	331	<b>1,085</b>	284	203	313	336	<b>1,136</b>	336	336	336	<b>1,345</b>
Total Ebitda	1,040	<b>3,980</b>	847	1,044	1,283	1,469	<b>4,643</b>	1,380	1,271	1,279	<b>5,398</b>
Exploration	7	<b>59</b>	21	6	10	10	<b>47</b>	10	10	15	<b>45</b>
Deprec., Deplet., & Amort.	252	<b>904</b>	238	219	217	217	<b>891</b>	217	217	217	<b>868</b>
Other non cash	-	-	-	-	100	-	<b>100</b>	-	-	-	-
<b>Ebit</b>	781	<b>3,017</b>	588	819	956	1,242	<b>3,605</b>	1,153	1,044	1,047	<b>4,485</b>
Interest	1	<b>11</b>	2	6	-	-	<b>8</b>	-	-	-	-
<b>Ebt</b>	780	<b>3,006</b>	586	813	956	1,242	<b>3,597</b>	1,153	1,044	1,047	<b>4,485</b>
Income Tax	242	<b>968</b>	195	274	306	435	<b>1,210</b>	403	365	366	<b>1,570</b>
<b>Net Income (\$mm)</b>											
Exploration and Production	389	<b>1,487</b>	242	449	592	-	-	-	-	-	-
Other	186	<b>600</b>	146	93	183	-	-	-	-	-	-
Unallocated	(37)	<b>(49)</b>	3	(3)	(125)	-	-	-	-	-	-
Total	538	<b>2,038</b>	391	539	650	807	<b>2,387</b>	749	679	680	<b>2,915</b>
<b>Shares (millions)</b>	352	<b>357</b>	350	345	341	341	<b>343</b>	341	341	341	<b>341</b>
Earnings per share (\$)	1.53	<b>5.71</b>	1.12	1.56	1.91	2.37	<b>6.96</b>	2.20	1.99	2.00	<b>8.56</b>
Ebitda Margin (E&P)	54%	<b>60%</b>	44%	59%	60%	62%	<b>57%</b>	61%	59%	59%	<b>60%</b>
Tax Rate	31%	<b>32%</b>	33%	34%	32%	35%	<b>34%</b>	35%	35%	35%	<b>35%</b>

**Blue Chip Investment Quality**

Investors might make more money on lower McDep Ratio alternatives to Imperial (see table [Rank by McDep Ratio](#)). Yet the company that has been succeeding for a hundred years continues to deliver rewarding returns that might have been underestimated in the past. But let us not be too myopic about small valuation differences. The highest McDep Ratio stock in the peer group is valued twice as highly as Imperial on a McDep Ratio basis and four times Imperial on a net present value basis. Nor is that our imagination. On an enterprise value to cash flow basis the most highly valued stock is about 15 times, also twice the market valuation of Imperial.

**Please see disclosures on the final page.**

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

	<i>Symbol/</i>		<i>Price</i>		<i>Market</i>	<i>Net</i>	<i>Debt/</i>	
	<i>Rating</i>		<i>(\$/sh)</i>	<i>Shares</i>	<i>Cap</i>	<i>Present</i>	<i>Present</i>	<i>McDep</i>
			<i>20-Oct</i>	<i>(mm)</i>	<i>(\$mm)</i>	<i>Value</i>	<i>Value</i>	<i>Ratio</i>
			<i>2005</i>			<i>(\$/sh)</i>		
<b>Producer/Refiners - Large Cap and Mid Cap</b>								
Kinder Morgan, Inc.	KMI	S2	87.50	123	10,760	20.00	0.76	1.82
Imperial Oil Limited (30%)	IMO	B	82.64	102	8,440	84.00	0.10	0.99
Marathon Oil Corporation	MRO	B	56.28	367	20,650	65.00	0.27	0.90
Petro-Canada	PCZ	B	33.96	526	17,860	42.00	0.19	0.84
Lukoil Oil Company	LUKOY	B	51.40	830	43,000	65.00	0.03	0.80
Suncor Energy	SU	B	49.76	461	22,940	68.00	0.10	0.76
Norsk Hydro ASA	NHY	B	94.11	251	23,620	130.00	0.12	0.76
ConocoPhillips	COP	B	57.75	1,419	81,900	100.00	0.15	0.64
Gazprom (50%)	OGZPF	B	55.50	1,022	56,700	90.00	0.03	0.63
PetroChina Company Ltd (10%)	PTR	B	72.70	176	12,780	120.00	0.01	0.61
			<i>Total or Median</i>		<i>299,000</i>		<i>0.11</i>	<i>0.78</i>

Kurt H. Wulff, CFA

**Disclaimer:** This analysis was prepared by Kurt Wulff doing business as McDep Associates. The firm used sources and data believed to be reliable, but makes no representation as to their accuracy or completeness. This analysis is intended for informational purposes and is not a solicitation to buy or sell a security. Past performance is no guarantee of future results.

McDep does no investment banking business. McDep is not paid by covered companies including revenue from advertising, trading, consulting, subscriptions or research service. McDep shall not own more than 1% of outstanding stock in a covered company. No one at McDep is on the Board of Directors at a covered company nor is anyone at a covered company on the Board of Directors of McDep.

McDep or its employees may take positions in stocks the firm covers for research purposes. No trades in a subject stock shall be made within a week before or after a change in recommendation.

**Certification:** I, Kurt H. Wulff, certify that the views expressed in this research analysis accurately reflect my personal views about the subject securities and issuers. No part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research analysis.

**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 total return less than inflation.

**Please see disclosures on the final page.**