

Rating: Buy
S&P 500: 1184

Lukoil Oil Company National Treasure

<i>Symbol</i>	(LKOD)	LUKOY	<i>Ebitda Next Twelve Months ending 3/31/06 (US\$mm)</i>	12,100
<i>Rating</i>		Buy	<i>North American Natural Gas/Ebitda (%)</i>	0
<i>Price (US\$/sh)</i>		145.00	<i>Natural Gas and Oil Production/Ebitda (%)</i>	52
<i>Pricing Date</i>		4/6/05	<i>Adjusted Reserves/Production NTM</i>	20.0
<i>Shares (mm)</i>		209	<i>EV/Ebitda</i>	2.6
<i>Market Capitalization (US\$mm)</i>		30,200	<i>PV/Ebitda</i>	3.7
<i>Debt (US\$mm)</i>		1,500	<i>Undeveloped Reserves (%)</i>	40
<i>Enterprise Value (EV) (US\$mm)</i>		31,700	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	9.84
<i>Present Value (PV) (US\$mm)</i>		44,900	<i>Present Value Proven Reserves(US\$/boe)</i>	2.32
<i>Net Present Value (US\$/share)</i>		208	<i>Present Value Proven Reserves(US\$/mcf)</i>	0.39
<i>Debt/Present Value</i>		0.03	<i>Earnings Next Twelve Months (US\$/sh)</i>	32.53
<i>McDep Ratio - EV/PV</i>		0.71	<i>Price/Earnings Next Twelve Months</i>	4
<i>Dividend Yield (%/year)</i>		2.4	<i>Indicated Annual Dividend (US\$/sh)</i>	3.44

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 purchase of the American Depositary Receipts of **Lukoil Oil Company (LUKOY)** as a leading equity participation in the unfolding value of Russian oil and gas. The demise of competitor Yukos seems to have had the indirect effect of strengthening the market recognition of the value of Russian oil. Lukoil appears to have taken great pains to act in line with the strategic interests of the Russian government and is likely to be an appreciated private entity in the optimal development of Russian energy resources. The company claims that recent disclosure of final reserves for 2004 place it second only to ExxonMobil, a somewhat exaggerated assertion, but a valid indicator nonetheless that the company's potential exceeds its stock price. The stock would appreciate 43% to reach our estimated present value of \$208 a share.

No. 2 in Proven Reserves of Hydrocarbons?

Reporting 20.1 billion barrels equivalent of oil and gas reserves, Lukoil ranks just behind ExxonMobil at a reported 20.7 billions barrels (see table Oil Production, Reserves and Present Value). Though Lukoil's reserves are audited by U.S. engineer Miller and Lents, the estimates are made by Lukoil engineers according to the standards of the Society of Petroleum Engineers (SPE) rather than the cautious standards of the U.S. Securities and Exchange Commission. SEC-basis reserves may be half as much.

Lukoil's hydrocarbon reserves also include about 20% for natural gas that has little identifiable present value. That takes the Lukoil estimate down to about 40% of the ExxonMobil amount.

Finally, there is a steep excise tax on oil for export from Russia, and oil sold domestically draws a low price. As a result, Lukoil's estimated cash flow per barrel is less than 40% of that projected for XOM and its peers for the next twelve months. The last step helps explain a McDep Present Value estimate for Lukoil oil and gas reserves that is less than 16% of that for XOM.

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Oil Production, Reserves and Present Value

	<u>Lukoil</u>	<u>ExxonMobil</u>
Production, 2004		
Oil (mmb)	630	941
Natural Gas (bcf)	228	3598
Oil Equivalent (mmb)	668	1541
R/P - Proven Developed		
Oil	16.9	7.3
Natural Gas	21.7	10.6
Oil Equivalent	17.2	8.6
Reserves, Proven Developed		
Oil (mmb)	10.65	6.86
Natural Gas (bcf)	4.96	38.20
Oil Equivalent (mmb)	11.48	13.23
Reserves, Undeveloped (%)		
Oil	33	36
Natural Gas	80	36
Oil Equivalent	43	36
Reserves, Total		
Oil (mmb)	16.0	10.8
Natural Gas (bcf)	24.6	59.3
Oil Equivalent (mmb)	20.1	20.7
Cash Flows (\$billions)		
Future Cash Flows	308	551
Future Costs	171	163
Future Net Cash Flows (pre-inc tax)	137	388
Discounting at 10%/year	87	189
Discounted Cash Flow (pre-inc tax)	50	199
McDep Present Value (\$billions)	32	230

All of the factors that deflate Lukoil's reserves also point to the opportunity. When Russia needs more investment from its own companies it will likely reduce the excise tax. As the economy grows, the discount for locally sold crude oil will likely narrow. Russian natural gas reserves are likely to play an increasing role supplying the global demand for clean fuel. The SPE standard indicates more likely future production while the SEC standard indicates minimum expectations.

Futures Point to Cash Flow Gains

The outlook for future cash flow is up sharply from a few months ago as a result of recent oil price gains (see table Next Twelve Months Operations). Refining/marketing margins also appear unusually strong for the next twelve months.

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Lukoil Oil Company
Next Twelve Months Operations

	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Next Twelve Months</i>
	<i>9/30/04</i>	<i>12/31/04</i>	<i>2004E</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>3/31/06</i>
Volume										
Oil (mmb)	159	159	630	156	158	159	159	632	156	632
Oil (mbd)	1,730	1,732	1,727	1,732	1,732	1,732	1,732	1,732	1,732	1,732
Price										
Oil (\$/bbl)										
WTI Cushing	43.89	48.30	41.44	49.44	56.85	59.03	59.25	56.14	58.11	58.31
Lukoil export	36.52	40.18	34.37	41.14	47.30	49.11	49.30	46.74	48.35	48.52
NY Harbor 3-2-1 (\$/bbl)	7.83	5.90	8.56	6.22	12.53	12.25	10.57	10.39	11.40	11.69
Revenue (\$mm)										
Oil	5,813	6,402	21,664	6,412	7,455	7,825	7,855	29,546	7,536	30,671
Other	4,009	4,009	13,179	4,009	4,009	4,009	4,009	16,038	4,009	16,038
Total	9,822	10,412	34,843	10,421	11,464	11,835	11,864	45,584	11,545	46,708
Expense										
Fixed	1,233	1,233	4,544	1,233	1,233	1,233	1,233	4,932	1,233	4,932
Variable	3,699	4,074	14,008	4,080	4,743	4,980	4,998	18,801	4,795	19,516
Other	2,677	2,841	8,686	2,825	2,525	2,534	2,584	10,468	2,556	10,199
Ebitda (\$mm)										
Exploration and Production	881	1,096	3,112	1,099	1,478	1,613	1,624	5,814	1,508	6,223
Other	1,332	1,168	4,493	1,184	1,484	1,476	1,425	5,570	1,453	5,839
Total Ebitda	2,213	2,264	7,605	2,283	2,962	3,089	3,049	11,383	2,961	12,061
Exploration	38	38	163	38	38	38	38	152	38	152
Deprec., Deplet., & Amort.	292	292	1,098	292	292	292	292	1,168	292	1,168
Ebit	1,883	1,934	6,344	1,953	2,632	2,759	2,719	10,063	2,631	10,741
Interest	77	77	297	77	77	77	77	308	77	308
Ebt	1,806	1,857	6,047	1,876	2,555	2,682	2,642	9,755	2,554	10,433
Income Tax	397	650	1,719	657	894	939	925	3,414	894	3,652
Net Income (\$mm)										
Exploration and Production	528	580	1,653	583	823	904	908	3,217	839	3,473
Other	871	618	2,640	628	826	827	797	3,077	809	3,258
Unallocated	10	9	34	9	12	13	13	47	12	50
Total	1,409	1,207	4,327	1,220	1,661	1,743	1,717	6,341	1,660	6,782
Shares (millions)	209	209	209	209	209	209	209	209	209	209
Per share (\$)	6.76	5.79	20.75	5.85	7.97	8.36	8.24	30.41	7.96	32.53
Ebitda Margin (E&P)	15%	17%	14%	17%	20%	21%	21%	20%	20%	20%
Tax Rate	22%	35%	28%	35%	35%	35%	35%	35%	35%	35%

The More Cash Flow Can Be Sustained, the More It Is Worth

Our estimate of present value of \$208 a share in place for about a year now implies particularly low multiples of near-term cash flow (see table Functional Cash Flow and Present Value).

Lukoil
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>	
Natural Gas					
Oil	6,200	20.0	5.1	31,900	71%
Downstream	5,900		2.2	13,000	29%
	12,100		3.7	44,900	100%
Debt (US\$mm)					1,500
Net Present Value (US\$mm)					43,400
Shares (mm)					209
Net Present Value (US\$/sh)					208

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Buy Oil and Gas Producers at Mid Decade

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 including LUKOY, in our opinion. Supporting improving prospects, the average futures prices of oil and gas for continuous delivery over the next six years are in a multi-year uptrend defined by the current quotes above the 40-week average. The recent benchmark oil average futures price for the next six years is more than \$53 a barrel. That is higher than the \$40 a barrel reflected in our current estimates of present value.

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

	<i>Symbol/</i>	<i>Rating</i>	<i>Price</i> <i>(\$/sh)</i> <i>6-Apr</i> <i>2005</i>	<i>Shares</i> <i>(mm)</i>	<i>Market</i> <i>Cap</i> <i>(\$mm)</i>	<i>Net</i> <i>Present</i> <i>Value</i> <i>(\$/sh)</i>	<i>Debt/</i> <i>Present</i> <i>Value</i>	<i>McDep</i> <i>Ratio</i>
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	76.39	125	9,550	20.00	0.74	1.74
Imperial Oil Limited (30%)	IMO	B	77.62	105	8,190	64.00	0.11	1.19
Marathon Oil Corporation	MRO	B	48.39	347	16,810	42.00	0.30	1.11
ConocoPhillips	COP	B	110.87	706	78,300	128.00	0.23	0.90
Petro-Canada	PCZ	B	59.29	264	15,660	70.00	0.18	0.87
Norsk Hydro ASA	NHY	B	83.59	252	21,090	101.00	0.16	0.85
Suncor Energy	SU	B	40.95	460	18,840	54.00	0.10	0.78
PetroChina Company Ltd (10%)	PTR	B	64.44	176	11,330	94.00	0.05	0.70
Lukoil Oil Company	LUKOY	B	145.00	209	30,000	208.00	0.03	0.71
<i>Total or Median</i>					<i>210,000</i>		<i>0.16</i>	<i>0.87</i>

Kurt H. Wulff, CFA

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