

Rating: Buy
 S&P 500: 1168

Occidental Petroleum

Raise Net Present Value to \$87 a Share

<i>Symbol</i>	OXY	<i>Ebitda Next Twelve Months ending 3/31/06 (US\$mm)</i>	6,500
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	12
<i>Price (US\$/sh)</i>	56.95	<i>Natural Gas and Oil Production/Ebitda (%)</i>	88
<i>Pricing Date</i>	1/25/05	<i>Adjusted Reserves/Production NTM</i>	11.3
<i>Shares (mm)</i>	406	<i>EV/Ebitda</i>	4.5
<i>Market Capitalization (US\$mm)</i>	23,100	<i>PV/Ebitda</i>	6.4
<i>Debt (US\$mm)</i>	6,200	<i>Undeveloped Reserves (%)</i>	21
<i>Enterprise Value (EV) (US\$mm)</i>	29,300	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	29.00
<i>Present Value (PV) (US\$mm)</i>	41,500	<i>Present Value Proven Reserves(US\$/boe)</i>	14.80
<i>Net Present Value (US\$/share)</i>	87	<i>Present Value Proven Reserves(US\$/mcf)</i>	2.47
<i>Debt/Present Value</i>	0.15	<i>Earnings Next Twelve Months (US\$/sh)</i>	7.22
<i>McDep Ratio - EV/PV</i>	0.71	<i>Price/Earnings Next Twelve Months</i>	8
<i>Dividend Yield (%/year)</i>	1.9	<i>Indicated Annual Dividend (US\$/sh)</i>	1.10

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 a Buy rating on the common shares of Occidental Petroleum (OXY), a leading oil producer with more than half of production in the U.S. We increase our estimate of net present value to \$87 a share from \$75. The change is in line with an increase in our standard industry assumption of \$40 a barrel constant real oil price, up from \$35. Just reported fourth quarter 2004 cash flow was strong despite oil price and natural gas price that increased less than industry benchmarks. Once a high-debt stock that disappointed investors, Oxy has transformed to a low-debt stock with a more promising business mix. We see 50% stock price appreciation potential in a year or two to net present value where the stock would then offer a continuing return of 11% per year at \$40 oil and normal risk.

Present Value Estimate Previewed in Sensitivity Illustration

Estimated net present value of \$87 a share was the amount consistent with a constant real oil price of \$40 a barrel when we detailed a sensitivity analysis a few months ago (see *Stock Idea, Occidental Petroleum – Oil Rich*, August 23, 2004). What has changed since then is that we now believe that \$40 a barrel constant real oil price is the most likely long-term oil price rather than \$35 previously. On January 26, 2005, that caused us to select the present value calculated for \$40 oil for Oxy and other oil and gas producers.

By our estimates, Oxy's present value of oil resources is exceeded only by **PetroChina (PTR)**, **Lukoil (LUKOY)** and **ConocoPhillips (COP)** in addition to the five mega cap energy companies (see table Global Oil Cash Flow and Present Value). When present value is expressed as a multiple of annual cash flow the resulting ratio correlates with adjusted reserve life.

Oil resources account for 73% of the company's value (see table Functional Cash Flow and Present Value). Natural gas is concentrated in North America and is growing overseas. Downstream is a holdover from the company's diversification into chemicals. We have been

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classifying the company as an independent producer on the presumption that the downstream businesses would eventually be sold.

Volume Rising

Management expects that the company will be producing 600 thousand barrels oil equivalent daily (mboed) by year end 2005. That exit rate implies a yearly average of perhaps 580 mboed. Our projection of 534 mboed becomes 560 mboed including non-consolidated volumes on which management provides less detail (see table Next Twelve Months Operating and Financial Estimates). If actual volumes are higher than projected, it would give us some cushion to absorb any unfavorable surprises.

Global Oil Cash Flow and Present Value

	<i>Ebitda</i>	<i>Adjstd</i>	<i>PV/</i>	<i>Present</i>
	<i>NTM</i>	<i>Resrvs/</i>	<i>Ebitda</i>	<i>Value</i>
	(\$mm)	<i>Prod</i>	<i>NTM</i>	(\$mm)
		<i>NTM</i>		
Exxon Mobil Corporation	25,160	10.2	6.9	173,000
PetroChina	21,100	12.7	6.6	139,800
BP plc	20,400	8.8	6.6	134,000
ChevronTexaco Corporation	16,040	11.1	6.6	105,800
Royal Dutch/Shell	19,990	6.6	5.1	101,000
Total S.A.	12,910	8.9	6.6	84,800
ConocoPhillips	8,300	12.0	5.9	49,100
Lukoil Oil Company	4,400	20.0	10.2	44,900
Occidental Petroleum Corp.	4,786	11.8	6.4	30,400
Suncor Energy	2,190	20.0	11.1	24,300
CNOOC	4,560	8.0	5.3	24,300
Imperial Oil	1,776	13.3	8.7	15,500
Encana Corporation	2,850	7.5	5.3	15,200
Anadarko Petroleum Corp.	2,440	11.6	6.2	15,100
Devon Energy Corporation	3,100	5.3	4.3	13,400
Norsk Hydro ASA	2,740	6.0	4.7	12,900
Petro-Canada	2,381	7.4	5.4	12,900
Unocal Corporation	1,920	8.7	5.5	10,500
Canadian Oil Sands Trust (USS)	880	20.0	11.5	10,100
Burlington Resources	1,520	9.9	5.8	8,800
Marathon Oil Corporation	1,330	8.8	6.1	8,100
XTO Energy Inc.	450	12.1	6.4	2,900
Encore Acquisition Company	212	11.7	7.7	1,640
San Juan Basin Royalty Trust	149	12.5	9.4	1,400
Berry Petroleum Company	183	12.5	6.4	1,180
Energy Partners Ltd.	103	7.5	5.1	530
Cimarex Energy Company	92	5.2	4.3	400

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Occidental Petroleum Corporation
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	792	9.5	7.2	5,700	14%
Overseas Natural Gas	85	9.1	7.0	600	1%
Oil	4,786	11.8	6.4	30,400	73%
Downstream	786		6.1	4,800	12%
	6,450	11.3	6.4	41,500	100%
Debt (US\$mm)					6,200
Net Present Value (US\$mm)					35,300
Shares (mm)					406
Net Present Value (US\$/sh)					87

It was only a mild surprise because we can see quotes every day, but Oxy's oil price realizations did not keep up with the industry benchmarks in the last quarter of the year. In Texas, the company produces primarily West Texas Sour that lagged the price increase in West Texas Intermediate the grade traded as Light Sweet Crude Oil in the commodity markets. Similarly the price for natural gas that Oxy produces from the Hugoton field in Kansas apparently lagged the Henry Hub price in Louisiana that is the benchmark for trading in the futures markets. As with volume we project a continuation of fourth quarter conditions for simplistic reasons knowing that the wider differential for natural gas, at least, should narrow.

Lower expenses kept reported cash flow at a high level. As a result, our projection for the Next Twelve Months remains as high as before latest disclosures.

Libya and Oxy Negotiating

Oxy's oil assets in Libya made it an important company in the 1960s. Libya expropriated the assets in the 1970s. Then the U.S. had sanctions against doing business with Libya through the 1990s. Now, Libya and American oil companies are negotiating a reentry. It is unlikely that Libya will be giving anything away, but Oxy may have a chance to reapply its technological skill to create value. If agreement is reached, possibly in 2005, it may be positive for Oxy stock though we put no explicit value on such a development.

Buy Oil and Gas Producers at Mid Decade

Measured by McDep Ratio, Oxy stock appears undervalued along with peers (see table of stocks ranked 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.

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Occidental Petroleum
Next Twelve Months Operating and Financial Estimates

	<i>Q3</i>	<i>Q4</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>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>3/31/06</i>
Volume										
Natural Gas (mmcf)										
U.S. (or North America)	488	499	508	499	499	499	499	499	499	499
Overseas (or Int'l)	161	145	131	145	145	145	145	145	145	145
Total	649	644	639	644	644	644	644	644	644	644
Oil (mbd)	431	427	436	427	427	427	427	427	427	427
Total gas & oil (mmb)	50	49	198	48	49	49	49	195	48	195
Total gas & oil (mbd)	539	534	541	534	534	534	534	534	534	534
Price										
Natural gas (\$/mcf)										
Henry Hub (\$/mmbtu)	5.75	7.10	6.15	6.40	6.40	6.47	6.80	6.52	7.26	6.73
U.S. (or North America)	5.87	5.65	5.35	5.10	5.09	5.15	5.41	5.19	5.78	5.36
Overseas (or Int'l)	1.57	1.53	1.70	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Total	4.80	4.72	4.60	4.40	4.40	4.44	4.65	4.47	4.93	4.60
Oil (\$/bbl)										
WTI Cushing	43.89	48.30	41.44	47.88	48.71	47.66	46.57	47.70	45.60	47.14
Worldwide	38.85	39.11	35.87	38.77	39.45	38.59	37.71	38.63	36.93	38.17
Total gas & oil (\$/bbl)	36.84	36.95	34.25	36.29	36.82	36.19	35.74	36.26	35.45	36.05
Revenue (\$mm)										
Natural Gas										
U.S. (or North America)	264	259	991	229	231	236	249	945	259	976
Overseas (or Int'l)	23	20	81	26	26	27	27	106	26	106
Total	287	280	1,073	255	258	263	275	1,051	286	1,082
Oil	1,541	1,536	5,707	1,490	1,533	1,516	1,481	6,020	1,419	5,949
Other	1,205	1,266	4,707	1,266	1,266	1,266	1,266	5,063	1,266	5,063
Total	3,033	3,082	11,487	3,011	3,056	3,045	3,023	12,135	2,970	12,094
Expense (\$mm)										
Fixed	289	174	901	174	174	174	174	695	174	695
Variable	289	174	901	167	171	170	168	676	163	672
Other	1,004	1,069	4,044	1,069	1,069	1,069	1,069	4,277	1,069	4,277
Ebitda (\$mm)										
Exploration and Production	1,249	1,469	4,977	1,404	1,445	1,435	1,415	5,700	1,368	5,664
Other	201	197	663	197	197	197	197	786	197	786
Total Ebitda	1,450	1,665	5,640	1,601	1,642	1,632	1,612	6,487	1,565	6,450
Exploration	37	88	219	88	88	88	88	352	88	352
Deprec., Deplet., & Amort.	322	333	1,305	333	333	333	333	1,332	333	1,332
Other non cash										
Ebit	1,091	1,244	4,116	1,180	1,221	1,211	1,191	4,803	1,144	4,766
Interest	59	63	255	63	63	63	63	252	63	252
Ebt	1,032	1,181	3,861	1,117	1,158	1,148	1,128	4,551	1,081	4,514
Income Tax	274	413	1,264	391	405	402	395	1,593	378	1,580
Net Income (\$mm)										
Exploration and Production	1,003	977	3,544							
Other	137	130	402							
Unallocated	(382)	(339)	(1,349)							
Total	758	768	2,597	726	753	746	733	2,958	702	2,934
Shares (millions)	403	406	402	406	406	406	406	406	406	406
Per share (\$)	1.88	1.89	6.46	1.79	1.85	1.84	1.80	7.28	1.73	7.22
Ebitda Margin (E&P)	68%	81%	73%	80%	81%	81%	81%	81%	80%	81%
Tax Rate	27%	35%	33%	35%	35%	35%	35%	35%	35%	35%

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

	<i>Symbol/</i>	<i>Rating</i>	<i>Price</i> <i>(\$/sh)</i> <i>25-Jan</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>
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B1	34.90	279	9,730	45.00	0.16	0.81
Encana Corporation	ECA	B1	58.41	472	27,600	77.00	0.18	0.80
Unocal Corporation	UCL	B3	46.83	274	12,800	65.00	0.21	0.78
CNOOC Limited (19%)	CEO	B2	53.03	78	4,140	67.00	-	0.79
Occidental Petroleum Corp.	OXY	B3	56.95	406	23,100	87.00	0.15	0.71
Devon Energy Corporation	DVN	B3	39.89	500	19,900	63.00	0.20	0.71
Burlington Resources	BR	B1	43.77	395	17,300	67.00	0.12	0.70
Anadarko Petroleum Corp.	APC	B1	64.52	253	16,300	113.00	0.17	0.64
<i>Total or Median</i>					<i>131,000</i>		<i>0.17</i>	<i>0.74</i>

B1 = Buy full unlevered position, B2 = Buy half unlevered position, B3 = Alternative buy, H = Hold
 S2 = Short half unlevered position, S3 = Short quarter unlevered position
 McDep Ratio = **Market cap and Debt to present value of oil and gas and other businesses**

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