



# Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

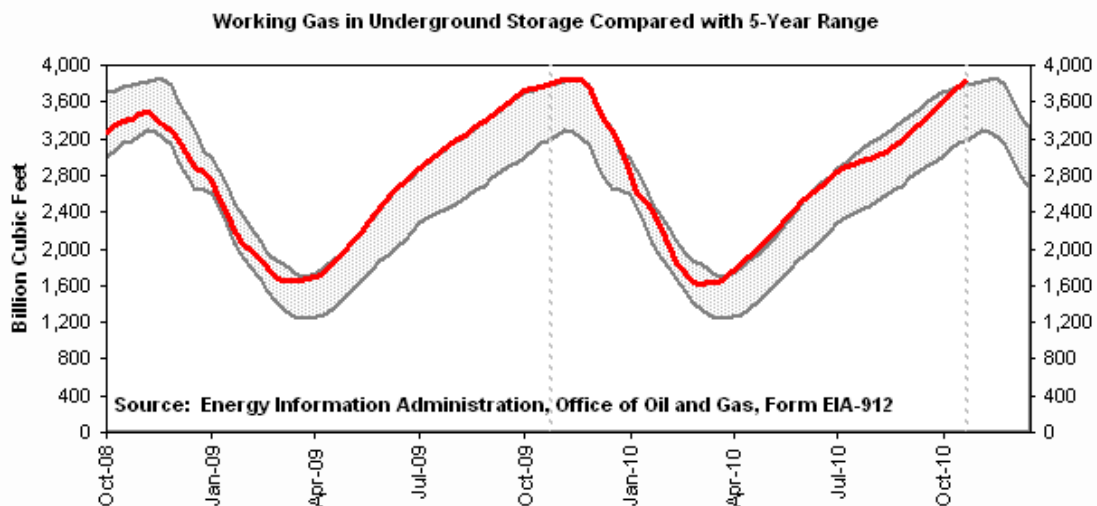
November 5, 2010

## Frac Shortage Limits Energy Supply

### Summary and Recommendation

A shortage of hydraulic fracturing services may be contributing to reduced natural gas drilling and thereby helping natural gas price to recover from a depressed level. Demand for high-pressure pumping equipment and skilled workers increases with the shift to horizontal from vertical drilling. It increases further as horizontal laterals lengthen up to two miles underground. Accordingly, frac prices may be two to three times normal according to **Petrohawk (HK)** president Richard Stoneburner speaking on the quarterly call on November 2. A frac job in the Eagle Ford shale that cost Petrohawk \$600,000 a year ago now costs \$3.5 million. The resulting speed bump in new supply development may slow the most rapidly expanding natural gas producers HK, **Range Resources (RRC)** and **Ultra Petroleum (UPL)**. Those three are the only stocks among 24 in our small cap and income coverage still trading below their 200-day average. Yet, all producers should benefit from the upward pressure on the price of flowing oil and gas. The six-year price of crude oil reached \$91 a barrel on November 4, well above the \$75 a barrel long-term price embedded in a McDep Ratio of 1.0. Six-year natural gas appears to have found its bottom just above \$5 a million btu. Natural gas storage is full and the peak winter demand season is about to begin (see chart below). Buy recommendations **Canadian Oil Sands Trust (COSWF)** and **Birchcliff Energy (BIREF)** shed their Contrarian qualifier and rejoin buy recommendations **Cimarex Energy (XEC)**, **Dorchester Minerals (DMLP)**, **San Juan Basin Royalty Trust (SJT)** and **Hugoton Royalty Trust (HGT)** in stock price up trends (see [Tables 1-4](#) on pages 2-5).

Kurt H. Wulff, CFA





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| Table 1                                     |                 |            |                         |                              |            |     |                   |                 |             |
|---|-----------------|------------|-------------------------|------------------------------|------------|-----|-------------------|-----------------|-------------|
| McDep Income and Small Cap Energy Portfolio |                 |            |                         |                              |            |     |                   |                 |             |
| Debt, Business Segments and Income Yield    |                 |            |                         |                              |            |     |                   |                 |             |
| Symbol/Rating                               | Price (US\$/sh) | EV/Market  | Enterprise Value (\$mm) | Present Value by Segment (%) |            |     | Dist. NTM (\$/un) | Dist. Yield (%) | McDep Ratio |
|   |                 |            |                         | NAmer. Natural Gas           | Oil Prod'n |     |                   |                 |             |
| B = Buy<br>CB (see below)                   | 4-Nov 2010      | Market Cap |                         |                              |            |     |                   |                 |             |
| <b>Canadian Income Trusts (US\$)</b>        |                 |            |                         |                              |            |     |                   |                 |             |
| Pengrowth Energy Trust                      | PGH             | 12.76      | 1.35                    | 5,000                        | 35         | 65  | 0.83              | 6.5             | 1.11        |
| Penn West Energy Trust                      | PWE             | 23.85      | 1.31                    | 13,800                       | 22         | 78  | 1.06              | 4.5             | 1.03        |
| Enerplus Resources Fund                     | ERF             | 29.07      | 1.20                    | 6,200                        | 41         | 59  | 2.12              | 7.3             | 0.97        |
| Peyto Energy Trust                          | PEYUF           | 16.90      | 1.20                    | 2,420                        | 78         | 22  | 1.42              | 8.4             | 0.95        |
| Canadian Oil Sands Trust                    | COSWF B         | 27.10      | 1.12                    | 14,600                       |            | 100 | 1.67              | 6.2             | 0.74        |
| <i>Total or Median</i>                      |                 |            |                         | 42,000                       |            |     |                   | 6.5             | 0.97        |
| <b>Small Cap Independent Producers</b>      |                 |            |                         |                              |            |     |                   |                 |             |
| Denbury Resources Inc.                      | DNR             | 18.65      | 1.46                    | 10,890                       | 16         | 84  | -                 | -               | 1.16        |
| Petrohawk Energy Corporation                | HK              | 16.84      | 1.64                    | 8,690                        | 95         | 5   | -                 | -               | 1.06        |
| Berry Petroleum Company                     | BRY             | 37.83      | 1.51                    | 3,110                        | 32         | 68  | 0.30              | 0.8             | 1.05        |
| Whiting Petroleum Corporation               | WLL             | 106.86     | 1.20                    | 7,070                        | 15         | 85  | -                 | -               | 1.04        |
| Cimarex Energy Company                      | XEC B           | 80.48      | 1.09                    | 7,510                        | 59         | 41  | 0.32              | 0.4             | 1.01        |
| Range Resources                             | RRC             | 39.15      | 1.35                    | 8,060                        | 81         | 19  | 0.04              | 0.1             | 0.96        |
| Ultra Petroleum                             | UPL             | 43.45      | 1.21                    | 7,830                        | 94         | 6   | -                 | -               | 0.87        |
| Birchcliff Energy Ltd. (US\$)               | BIREF B         | 9.20       | 1.23                    | 1,440                        | 68         | 32  | -                 | -               | 0.70        |
| <i>Total or Median</i>                      |                 |            |                         | 54,600                       |            |     |                   |                 | 1.02        |
| <b>Top Line Cash Payers</b>                 |                 |            |                         |                              |            |     |                   |                 |             |
| Sabine Royalty Trust                        | SBR             | 57.50      | 1.00                    | 840                          | 50         | 50  | 3.60              | 6.3             | 1.28        |
| Permian Basin RT                            | PBT             | 22.36      | 1.00                    | 1,040                        | 38         | 62  | 1.33              | 6.0             | 1.24        |
| Cross Timbers Royalty Trust                 | CRT             | 39.25      | 1.00                    | 240                          | 75         | 25  | 2.54              | 6.5             | 1.16        |
| Freehold Royalty Trust (US\$)               | FRHLF           | 19.22      | 1.08                    | 1,210                        | 25         | 75  | 1.56              | 8.1             | 1.12        |
| Dorchester Minerals, L.P.                   | DMLP B          | 27.56      | 1.02                    | 860                          | 66         | 34  | 1.60              | 5.8             | 1.02        |
| <i>Total or Median</i>                      |                 |            |                         | 4,200                        |            |     |                   | 6.3             | 1.16        |
| <b>Bottom Line Cash Payers</b>              |                 |            |                         |                              |            |     |                   |                 |             |
| Linn Energy, LLC                            | LINE            | 35.56      | 1.43                    | 7,440                        | 45         | 55  | 2.64              | 7.4             | 1.40        |
| Legacy Reserves LP.                         | LGCY            | 25.96      | 1.37                    | 1,420                        | 17         | 83  | 2.08              | 8.0             | 1.20        |
| Encore Energy Partners, L.P. (52%)          | ENP             | 20.31      | 1.26                    | 600                          | 25         | 75  | 2.00              | 9.8             | 1.15        |
| Mesa Royalty Trust                          | MTR             | 49.00      | 1.00                    | 91                           | 75         | 25  | 3.06              | 6.2             | 1.02        |
| San Juan Basin Royalty Trust                | SJT B           | 24.53      | 1.00                    | 1,140                        | 100        | -   | 1.13              | 4.6             | 0.98        |
| Hugoton Royalty Trust                       | HGT B           | 19.98      | 1.00                    | 800                          | 90         | 10  | 1.14              | 5.7             | 0.95        |
| <i>Total or Median</i>                      |                 |            |                         | 11,500                       |            |     |                   | 6.8             | 1.08        |
| <b>Composite (excl COSWF)</b>               |                 |            |                         |                              |            |     |                   |                 |             |
| <i>Enterprise Value Weighting</i>           |                 |            |                         | 97,700                       | 49         | 51  |                   |                 | 1.04        |
| <i>Equal Weighting</i>                      |                 |            |                         |                              | 54         | 46  |                   |                 | 1.06        |
| <i>Equal Weighted Buys</i>                  |                 |            |                         |                              | 67         | 33  |                   |                 | 0.93        |

CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.

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

Present Value presumes long-term prices of \$75 a barrel for oil and \$8 a million btu for natural gas.

Dist. = Income distribution. NTM = Next Twelve Months Ended September 30, 2011. Enterprise Value = Market Cap and Debt.



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**Table 2**

## McDep Income and Small Cap Energy Portfolio

### Net Present Value and McDep Ratio

|  | <i>Symbol/<br/>Rating</i> | <i>Price<br/>(\$/sh)<br/>4-Nov<br/>2010</i> | <i>Shares<br/>(mm)</i> | <i>Market<br/>Cap<br/>(\$mm)</i> | <i>Net<br/>Present<br/>Value<br/>(\$/un)</i> | <i>Debt/<br/>Present<br/>Value</i> | <i>McDep<br/>Ratio</i> |      |
|--|---------------------------|---|------------------------|----------------------------------|--|------------------------------------|------------------------|------|
| <b>Canadian Income Trusts (US\$)</b>   |                           |   |                        |                                  |  |                                    |                        |      |
| Pengrowth Energy Trust                 | PGH                       | 12.76                                       | 290.0                  | 3,700                            | 11.00  | 0.29                               | 1.11                   |      |
| Penn West Energy Trust                 | PWE                       | 23.85                                       | 439.6                  | 10,480                           | 23.00  | 0.25                               | 1.03                   |      |
| Enerplus Resources Fund                | ERF                       | 29.07                                       | 177.5                  | 5,160                            | 30.00  | 0.16                               | 0.97                   |      |
| Peyto Energy Trust                     | PEYUF                     | 16.90                                       | 119.4                  | 2,020                            | 18.00  | 0.16                               | 0.95                   |      |
| Canadian Oil Sands Trust               | COSWF                     | B   | 27.10                  | 484.0                            | 13,120                                       | 38.00                              | 0.08                   | 0.74 |
| <i>Total or Median</i>                 |                           |   |                        | <i>34,500</i>                    |  | <i>0.16</i>                        | <i>0.97</i>            |      |
| <b>Small Cap Independent Producers</b> |                           |   |                        |                                  |  |                                    |                        |      |
| Denbury Resources Inc.                 | DNR                       | 18.65                                       | 401.0                  | 7,480                            | 15.00  | 0.36                               | 1.16                   |      |
| Petrohawk Energy Corporation           | HK                        | 16.84                                       | 302.0                  | 5,300                            | 16.00  | 0.41                               | 1.06                   |      |
| Berry Petroleum Company                | BRY                       | 37.83                                       | 54.4                   | 2,060                            | 35.00  | 0.35                               | 1.05                   |      |
| Whiting Petroleum Corporation          | WLL                       | 106.86                                      | 59.0                   | 5,890                            | 95.00  | 0.17                               | 1.04                   |      |
| Cimarex Energy Company                 | XEC                       | B   | 80.48                  | 85.8                             | 6,910  | 80.00                              | 0.08                   | 1.01 |
| Range Resources                        | RRC                       | 39.15                                       | 157.1                  | 5,970                            | 40.00  | 0.25                               | 0.96                   |      |
| Ultra Petroleum                        | UPL                       | 43.45                                       | 154.0                  | 6,480                            | 50.00  | 0.15                               | 0.87                   |      |
| Birchcliff Energy Ltd. (US\$)          | BIREF                     | B   | 9.20                   | 127.0                            | 1,170  | 14.00                              | 0.13                   | 0.70 |
| <i>Total or Median</i>                 |                           |   |                        | <i>41,260</i>                    |  | <i>0.21</i>                        | <i>1.02</i>            |      |
| <b>Top Line Cash Payers</b>            |                           |   |                        |                                  |  |                                    |                        |      |
| Sabine Royalty Trust                   | SBR                       | 57.50                                       | 14.6                   | 840                              | 45.00  | -                                  | 1.28                   |      |
| Permian Basin RT                       | PBT                       | 22.36                                       | 46.6                   | 1,040                            | 18.00  | -                                  | 1.24                   |      |
| Cross Timbers Royalty Trust            | CRT                       | 39.25                                       | 6.0                    | 240                              | 34.00  | -                                  | 1.16                   |      |
| Freehold Royalty Trust (US\$)          | FRHLF                     | 19.22                                       | 58.3                   | 1,120                            | 17.00  | 0.08                               | 1.12                   |      |
| Dorchester Minerals, L.P.              | DMLP                      | B   | 27.56                  | 30.7                             | 850  | 27.00                              | 0.02                   | 1.02 |
| <i>Total or Median</i>                 |                           |   |                        | <i>4,090</i>                     |  |                                    | <i>1.16</i>            |      |
| <b>Bottom Line Cash Payers</b>         |                           |   |                        |                                  |  |                                    |                        |      |
| Linn Energy, LLC                       | LINE                      | 35.56                                       | 146.5                  | 5,210                            | 21.00  | 0.42                               | 1.40                   |      |
| Legacy Reserves L.P.                   | LGCY                      | 25.96                                       | 40.1                   | 1,040                            | 20.00  | 0.32                               | 1.20                   |      |
| Encore Energy Partners, L.P. (52%)     | ENP                       | 20.31                                       | 23.6                   | 480                              | 17.00  | 0.24                               | 1.15                   |      |
| Mesa Royalty Trust                     | MTR                       | 49.00                                       | 1.9                    | 91                               | 48.00  | -                                  | 1.02                   |      |
| San Juan Basin Royalty Trust           | SJT                       | B   | 24.53                  | 46.6                             | 1,140  | 25.00                              | -                      | 0.98 |
| Hugoton Royalty Trust                  | HGT                       | B   | 19.98                  | 40.0                             | 800  | 21.00                              | -                      | 0.95 |
| <i>Total or Median</i>                 |                           |   |                        | <i>8,760</i>                     |  |                                    | <i>1.08</i>            |      |

B=Buy; CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.  
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|  |                |   | <i>Price</i><br><i>(\$/sh)</i> | <i>Revenue</i> | <i>Dist/</i>  | <i>Adjstd</i>  |               |               |
|--|----------------|---|--------------------------------|----------------|---------------|----------------|---------------|---------------|
|  | <i>Symbol/</i> |   | <i>4-Nov</i>                   | <i>Royalty</i> | <i>Equity</i> | <i>Resrvs/</i> | <i>PV/</i>    | <i>EV/</i>    |
|  | <i>Rating</i>  |   | <i>2010</i>                    | <i>(%)</i>     | <i>Ebitda</i> | <i>Prod</i>    | <i>Ebitda</i> | <i>Ebitda</i> |
|  |                |   |                                |                |               | <i>NTM</i>     | <i>NTM</i>    | <i>NTM</i>    |
| <b>Canadian Income Trusts (US\$)</b>   |                |   |                                |                |               |                |               |               |
| Peyto Energy Trust   | PEYUF          |   | 16.90                          |                | 1.11          | 21.5           | 14.1          | 13.4          |
| Penn West Energy Trust   | PWE            |   | 23.85                          |                | 0.45          | 9.9            | 9.8           | 10.1          |
| Canadian Oil Sands Trust   | COSWF          | B | 27.10                          |                | 0.56          | 30.1           | 12.8          | 9.4           |
| Enerplus Resources Fund  | ERF            |   | 29.07                          |                | 0.62          | 9.7            | 8.7           | 8.5           |
| Pengrowth Energy Trust   | PGH            |   | 12.76                          |                | 0.53          | 9.3            | 7.0           | 7.8           |
|  | <i>Median</i>  |   |                                |                |               | 9.9            | 9.8           | 9.4           |
| <b>Small Cap Independent Producers</b>   |                |   |                                |                |               |                |               |               |
| Range Resources  | RRC            |   | 39.15                          |                | -             | 12.1           | 15.7          | 15.1          |
| Ultra Petroleum  | UPL            |   | 43.45                          |                | -             | 12.6           | 13.7          | 11.9          |
| Petrohawk Energy Corporation   | HK             |   | 16.84                          |                | -             | 7.0            | 10.6          | 11.2          |
| Birchcliff Energy Ltd. (US\$)  | BIREF          | B | 9.20                           |                | -             | 21.4           | 14.7          | 10.3          |
| Denbury Resources Inc.   | DNR            |   | 18.65                          |                | -             | 12.9           | 8.0           | 9.2           |
| Berry Petroleum Company  | BRY            |   | 37.83                          |                | -             | 11.3           | 8.3           | 8.7           |
| Cimarex Energy Company   | XEC            | B | 80.48                          |                | -             | 6.2            | 7.1           | 7.1           |
| Whiting Petroleum Corporation  | WLL            |   | 106.86                         |                | -             | 9.3            | 6.6           | 6.9           |
|  | <i>Median</i>  |   |                                |                |               | 11.7           | 9.4           | 9.8           |
| <b>Top Line Cash Payers</b>  |                |   |                                |                |               |                |               |               |
| Permian Basin RT   | PBT            |   | 22.36                          | 42             | 0.98          | 13.1           | 13.3          | 16.5          |
| Sabine Royalty Trust   | SBR            |   | 57.50                          | 100            | 1.00          | 8.9            | 12.5          | 15.9          |
| Dorchester Minerals, L.P.  | DMLP           | B | 27.56                          | 77             | 0.89          | 6.8            | 15.0          | 15.3          |
| Cross Timbers Royalty Trust  | CRT            |   | 39.25                          | 84             | 0.97          | 12.4           | 12.9          | 14.9          |
| Freehold Royalty Trust (US\$)  | FRHLF          |   | 19.22                          | 71             | 0.87          | 8.2            | 9.4           | 10.6          |
|  | <i>Median</i>  |   |                                |                |               | 8.9            | 12.9          | 15.3          |
| <b>Bottom Line Cash Payers</b>   |                |   |                                |                |               |                |               |               |
| Linn Energy, LLC   | LINE           |   | 35.56                          |                | 1.74          | 18.3           | 13.9          | 19.4          |
| San Juan Basin Royalty Trust   | SJT            | B | 24.53                          |                | 0.81          | 13.9           | 18.1          | 17.7          |
| Mesa RoyaltyTrust  | MTR            |   | 49.00                          |                | 0.93          | 9.0            | 14.6          | 14.8          |
| Hugoton RoyaltyTrust   | HGT            | B | 19.98                          |                | 0.84          | 12.9           | 15.4          | 14.7          |
| Legacy Reserves L.P.   | LGCY           |   | 25.96                          |                | 0.99          | 12.0           | 9.6           | 11.5          |
| Encore Energy Partners, L.P.   | ENP            |   | 20.31                          |                | 1.08          | 13.4           | 9.2           | 10.5          |
|  | <i>Median</i>  |   |                                |                |               | 13.2           | 14.2          | 14.8          |
| <p>B=Buy; CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.<br/> EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended September 30, 2011; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses<br/> Top Line Cash Payers defined as those having Revenue Royalty (see fifth column from right).</p> |                |   |                                |                |               |                |               |               |

Please see disclosures on the final page.



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| Table 4                                     |                                    |       |                  |                   |             |                |                 |                |
|---|------------------------------------|-------|------------------|-------------------|-------------|----------------|-----------------|----------------|
| Oil and Gas Income and Small Cap Stocks     |                                    |       |                  |                   |             |                |                 |                |
| Rank by Enterprise Value to 200 Day Average |                                    |       |                  |                   |             |                |                 |                |
|   |                                    |       | Price<br>(\$/sh) | Enterprise Value/ |             |                |                 |                |
|   | Symbol/<br>Rating                  |       | 4-Nov<br>2010    | 52Wk<br>High      | 52Wk<br>Low | 50 Day<br>Avg. | 200 Day<br>Avg. | McDep<br>Ratio |
| <b>Canadian Income Trusts (US\$)</b>        |                                    |       |                  |                   |             |                |                 |                |
|   | Enerplus Resources Fund            | ERF   | 29.07            | 0.99              | 1.78        | 1.12           | 1.20            | 0.97           |
|   | Peyto Energy Trust                 | PEYUF | 16.90            | 1.00              | 1.43        | 1.13           | 1.17            | 0.95           |
|   | Pengrowth Energy Trust             | PGH   | 12.76            | 0.99              | 1.98        | 1.12           | 1.15            | 1.11           |
|   | Penn West Energy Trust             | PWE   | 23.85            | 1.00              | 1.33        | 1.12           | 1.14            | 1.03           |
|   | Canadian Oil Sands Trust           | COSWF | B 27.10          | 0.84              | 1.15        | 1.06           | 1.01            | 0.74           |
|   | <i>Median</i>                      |       |                  | <i>0.99</i>       | <i>1.43</i> | <i>1.12</i>    | <i>1.15</i>     | <i>0.97</i>    |
| <b>Small Cap Independent Producers</b>      |                                    |       |                  |                   |             |                |                 |                |
|   | Cimarex Energy Company             | XEC   | B 80.48          | 0.99              | 1.76        | 1.13           | 1.18            | 1.01           |
|   | Berry Petroleum Company            | BRY   | 37.83            | 1.00              | 1.31        | 1.12           | 1.16            | 1.05           |
|   | Whiting Petroleum Corporation      | WLL   | 106.86           | 0.94              | 1.52        | 1.03           | 1.14            | 1.04           |
|   | Denbury Resources Inc.             | DNR   | 18.65            | 0.97              | 1.29        | 1.09           | 1.11            | 1.16           |
|   | Birchcliff Energy Ltd. (US\$)      | BIREF | B 9.20           | 0.89              | 1.27        | 1.06           | 1.02            | 0.70           |
|   | Ultra Petroleum                    | UPL   | 43.45            | 0.81              | 1.11        | 1.03           | 0.95            | 0.87           |
|   | Petrohawk Energy Corporation       | HK    | 16.84            | 0.75              | 1.15        | 1.05           | 0.95            | 1.06           |
|   | Range Resources                    | RRC   | 39.15            | 0.76              | 1.13        | 1.03           | 0.91            | 0.96           |
|   | <i>Median</i>                      |       |                  | <i>0.94</i>       | <i>1.28</i> | <i>1.05</i>    | <i>1.06</i>     | <i>1.02</i>    |
| <b>Top Line Cash Payers</b>                 |                                    |       |                  |                   |             |                |                 |                |
|   | Permian Basin RT                   | PBT   | 22.36            | 1.00              | 1.73        | 1.13           | 1.21            | 1.24           |
|   | Freehold Royalty Trust (US\$)      | FRHLF | 19.22            | 0.98              | 1.38        | 1.11           | 1.17            | 1.12           |
|   | Sabine Royalty Trust               | SBR   | 57.50            | 0.99              | 1.45        | 1.09           | 1.15            | 1.28           |
|   | Cross Timbers Royalty Trust        | CRT   | 39.25            | 1.00              | 1.39        | 1.08           | 1.12            | 1.16           |
|   | Dorchester Minerals, L.P.          | DMLP  | B 27.56          | 0.94              | 1.37        | 1.06           | 1.11            | 1.02           |
|   | <i>Median</i>                      |       |                  | <i>0.99</i>       | <i>1.39</i> | <i>1.09</i>    | <i>1.15</i>     | <i>1.16</i>    |
| <b>Bottom Line Cash Payers</b>              |                                    |       |                  |                   |             |                |                 |                |
|   | Linn Energy, LLC                   | LINE  | 35.56            | 1.00              | 1.83        | 1.09           | 1.18            | 1.40           |
|   | Mesa Royalty Trust                 | MTR   | 49.00            | 0.90              | 1.40        | 1.07           | 1.10            | 1.02           |
|   | Legacy Reserves L.P.               | LGCY  | 25.96            | 0.97              | 1.37        | 1.03           | 1.09            | 1.20           |
|   | Hugoton Royalty Trust              | HGT   | B 19.98          | 0.90              | 1.33        | 1.02           | 1.05            | 0.95           |
|   | Encore Energy Partners, L.P. (52%) | ENP   | 20.31            | 0.94              | 1.73        | 1.05           | 1.05            | 1.15           |
|   | San Juan Basin Royalty Trust       | SJT   | B 24.53          | 0.86              | 1.46        | 1.03           | 1.05            | 0.98           |
|   | <i>Median</i>                      |       |                  | <i>0.92</i>       | <i>1.43</i> | <i>1.04</i>    | <i>1.07</i>     | <i>1.08</i>    |

CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.



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