



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

May 27, 2011

Cimarex Energy (XEC)

Timely Buy on Stock Price Underperformance

<i>Symbol</i>	XEC	<i>Ebitda Next Twelve Months ending 3/31/12 (US\$m)</i>	1,337
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	33
<i>Price (\$/sh)</i>	90.13	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	5/26/11	<i>Adjusted Reserves/Production NTM</i>	7.2
<i>Shares (mm)</i>	86	<i>EV/Ebitda</i>	6.3
<i>Market Capitalization (\$mm)</i>	7,760	<i>PV/Ebitda</i>	8.3
<i>Debt (\$mm)</i>	720	<i>Undeveloped Reserves (%)</i>	23
<i>Enterprise Value (EV) (\$mm)</i>	8,480	<i>Natural Gas and Oil Ebitda (\$/boe)</i>	34.60
<i>Present Value (PV) (\$mm)</i>	11,050	<i>Present Value Proven Reserves(\$/boe)</i>	35.20
<i>Net Present Value (\$/share)</i>	120	<i>Oil and Gas Ebitda Margin (%)</i>	70
<i>Debt/Present Value</i>	0.06	<i>Earnings Next Twelve Months (US\$/sh)</i>	6.94
<i>McDep Ratio - EV/PV</i>	0.77	<i>Price/Earnings Next Twelve Months</i>	13
<i>Dividend Yield (%/year)</i>	0.3	<i>Indicated Annual Dividend (US\$/sh)</i>	0.30
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.			
Estimated present value presumes a long-term price for oil of US\$100 a barrel and natural gas, \$8 a million bt			
For historical analysis of XEC since 2003 see www.mcdep.com/4xec.htm			

Summary and Recommendation

New commitments to buy-recommended **Cimarex Energy (XEC)** appear to be more timely on the basis of a low 0.77 McDep Ratio, conservative 0.06 ratio of debt to present value, low 6.3 multiple of unlevered cash flow (EV/Ebitda) and lowest 0.78 ratio of enterprise value to 52-week high. A favorable oil price trend has rewarded management's quick adjustment to emphasize oil drilling. Now a developing turn upward in natural gas price promises profits for many years in Cimarex's shale gas resources. A recent crossing above the 40-week average of six-year natural gas futures is being reinforced by the trend in the 40-week average also turning up. Price trends are an early indicator that consumers are turning increasingly to the bargain fuel and that the burst in supply, spurred by horizontal multi-stage fracturing, is transforming to steady growth. Investors can take advantage of the macro, or big picture, trends in oil and gas by owning shares of companies like Cimarex that are well positioned by the micro, or detailed, valuation measures.

Six-Year Natural Gas Confirming New Price Uptrend

Near the end of the first quarter of 2011, the futures price for the delivery over the next six years of Louisiana natural gas traded above its 40-week average for the first time on a sustained basis in three years. The confirming indicator for a sustained move is falling into place with the slope of the 40-week average also turning up. Today the upturn is measurable if barely perceptible (see chart [Six-Year Futures Strip](#) on page 3). That slope will automatically be steepening as lower prices from 40-weeks ago in the late summer and early fall of 2010 drop out of the 40-week average. If new prices continue near the current level, they will automatically be higher than 40-



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weeks ago and the slope of the 40-week average will continue up. The significance of such a detailed discussion is that natural gas may finally be starting the uptrend displayed by oil and the stock market for the past two years.

Natural Gas and Oil Balance at Low Relative Valuation

Among small cap independent producers, Cimarex is concentrated 45% by value on natural gas and 55% on oil (see [Table ISC-1](#) on page 4). Since most large cap stocks are most concentrated on oil, an important reason for our interest in small caps is to gain natural gas exposure. Though XEC has reduced its natural gas exposure in recent years, the remaining exposure is still higher than average and something we want to have. At a McDep Ratio near the low end of the range, XEC's combined oil and gas resources appear to be priced at a larger discount in the stock market to what we think they are worth on a fundamental basis.

Lowest Financial Risk

A low level of debt lends added comfort to investors in Cimarex (see Debt/Present Value in [Table ISC-2](#) on page 5). Investors who think management is too conservative can add their own risk by owning more stock.

Lowest Cash Flow Multiple

Lowest cash flow multiple (EV/Ebitda) of 6.3 is a telling indicator of relative value that is independent of our more subjective estimate of present value that helps determine the McDep Ratio (see [Table ISC-3](#) on page 6). The multiple also coincides with a short reserve life of 7.2. We put a heavy weight on reserve life in estimating present value. Yet, we might ask if management is just being more conservative as it is on debt? Most likely there are reserves likely to be classified as proven in the Cana shale of Oklahoma that might double XEC's corporate total.

Most Stock Price Underperformance Recently

Lagging stock price when combined with low valuation can be a good indicator of timing for future appreciation to begin again. Cimarex is down the most from its 52-week high of \$118 a share and its 50-week average of \$105 (see [Table ISC-4](#) on page 7).

Stock Price May Have Reacted to Lower Gulf Coast Volume

Prolific, but short-lived production that boosted Gulf Coast results in 2010 has tapered off for the remainder of 2011 according to company guidance (see chart [Volume by Region](#) on page 8). To us, timing is always a surprise, but the fact of the decline is not. The company has regularly made thorough disclosures of its Gulf Coast operations. Some of the decline has been taken deliberately and will be offset by lower daily volumes lasting longer.



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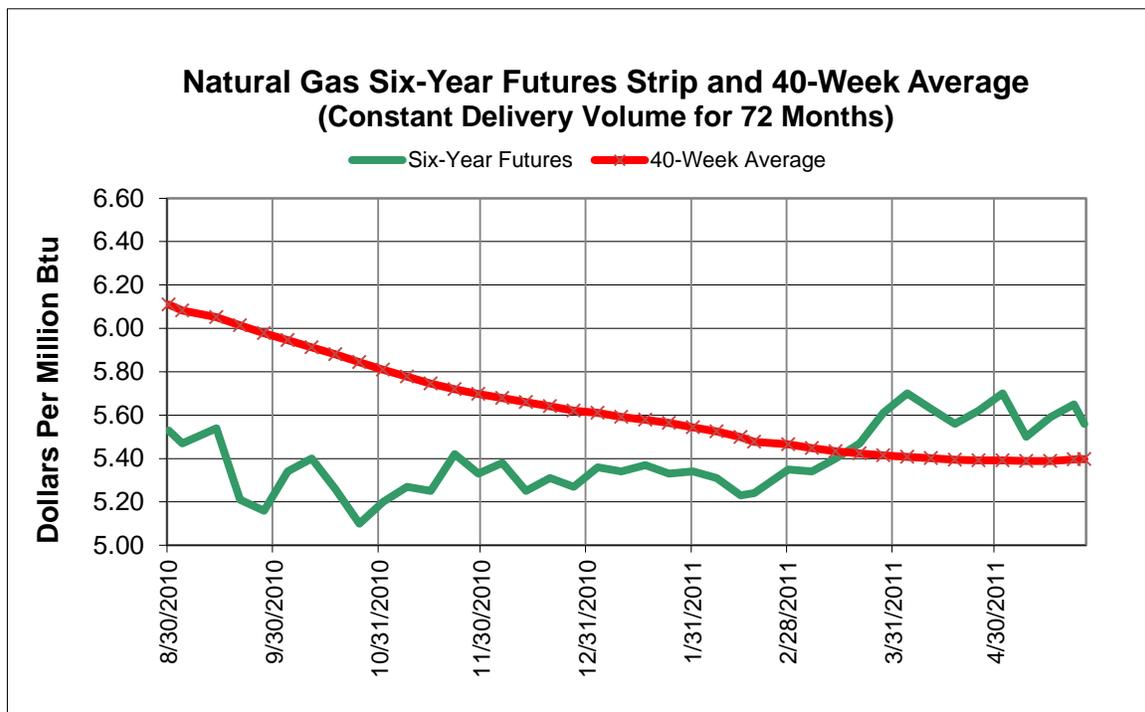
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Management expects an acceleration of production in the Permian and Midcontinent regions to keep overall corporate volumes growing. Here, too, there is always some uncertainty. We see that violent tornados in the past few days have damaged facilities near XEC's Oklahoma operations.

Net Present Value (NPV) Amply Supported by Cash Flow and Reserve Life

NPV of \$120 a share looks solid on a basis comparable to what we use for all stocks in our coverage (see table Functional Cash Flow and Present Value on page 8). The estimate incorporates latest quarterly results and projects volumes within management guidance (see Next Twelve Months Operating and Financial Performance on page 9).

Kurt H. Wulff, CFA





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Table ISC-1											
McDep Income and Small Cap Energy Portfolio											
Debt, Segments, Cash Flow, Income and McDep Ratio											
			Price		Enterprise	PV(%)		EV/	Dist.	Dist.	
Symbol/Rating		(US\$/sh)	EV/	Value	Nat	Oil	Ebitda	NTM	Yield	McDep	
CB (see below)		2011	Market	(\$mm)	Gas		NTM	(\$/un)	(%)	Ratio	
			Cap								
Small Cap Independent Producers											
Petrohawk Energy Corporation	HK	B	25.76	1.51	11,830	83	17	10.4	-	-	1.05
Range Resources	RRC	B	55.59	1.20	10,540	76	24	15.0	0.16	0.3	0.94
Payto Exploration and Developmen	PEYUF		21.15	1.15	3,220	76	24	11.7	0.74	3.5	0.90
Denbury Resources Inc.	DNR		21.57	1.27	10,890	6	94	8.3	-	-	0.89
Berry Petroleum Company	BRY		49.70	1.53	4,100	26	74	8.6	0.30	0.6	0.88
Birchcliff Energy Ltd.	BIREF	B	13.01	1.23	2,080	55	45	12.1	-	-	0.84
Ultra Petroleum	UPL		48.02	1.24	9,170	92	8	11.7	-	-	0.83
Whiting Petroleum Corporation	WLL	B	65.89	1.20	9,370	11	89	7.0	-	-	0.77
Cimarex Energy Company	XEC	B	90.13	1.09	8,480	44	56	6.3	0.30	0.3	0.77
<i>Total or Median</i>					69,700			10.4			0.88
Top Line Cash Payers											
Freehold Royalties Ltd.	FRHLF		22.16	1.07	1,380	18	82		1.72	7.8	1.01
Permian Basin RT	PBT		21.04	1.00	980	42	58		1.71	8.1	0.96
Sabine Royalty Trust	SBR		65.45	1.00	950	51	49		4.85	7.4	0.93
Dorchester Minerals, L.P.	DMLP	B	27.49	1.00	840	61	39		1.75	6.4	0.92
Cross Timbers Royalty Trust	CRT		40.99	1.00	250	87	13		2.98	7.3	0.91
<i>Total or Median</i>					4,400					7.4	0.93
Bottom Line Cash Payers											
Linn Energy, LLC	LINE		38.94	1.41	8,930	35	65	13.2	2.64	6.8	1.10
Legacy Reserves L.P.	LGCY		31.23	1.40	1,900	19	81	11.0	2.12	6.8	1.08
Vanguard Natural Resources, LLC	VNR		29.44	1.67	1,680	26	74	12.9	2.28	7.7	1.05
Hugoton RoyaltyTrust	HGT	B	23.02	1.00	920	88	13	14.2	1.39	6.1	1.05
Encore Energy Partners, L.P.	ENP		22.60	1.29	1,320	17	83	10.3	1.96	8.7	0.99
San Juan Basin Royalty Trust	SJT		23.94	1.00	1,120	100	-	14.1	1.43	6.0	0.96
Pengrowth Energy Corporation	PGH		13.08	1.40	6,000	30	70	8.8	0.86	6.6	0.95
Enerplus Corporation	ERF	B	31.96	1.27	7,300	33	67	8.8	2.22	6.9	0.89
Mesa RoyaltyTrust	MTR		41.11	1.00	77	75	25	11.4	2.91	7.1	0.78
<i>Total or Median</i>					29,200			11.4		6.8	0.99
Composite											
<i>Enterprise Value Weighting</i>					103,300	47	53				0.91
<i>Equal Weighting</i>						50	50				0.93
<i>Equal Weighted Buys</i>						53	47				0.90
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 (PV) presumes long-term prices of \$100 a barrel for oil and \$8 a million btu for natural gas.											
Dist. = Income distribution. NTM = Next Twelve Months Ended March 31, 2012. Enterprise Value = Market Cap and Debt.											



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Table ISC-2

McDep Income and Small Cap Energy Portfolio Net Present Value and McDep Ratio

			Price (\$/sh)	Shares	Market Cap (\$mm)	Net Present Value (\$/un)	Debt/ Present Value	McDep Ratio
	Symbol/ Rating	26-May 2011		(mm)				
Small Cap Independent Producers								
Petrohawk Energy Corporation	HK	B	25.76	305.0	7,860	24.00	0.35	1.05
Range Resources	RRC	B	55.59	158.0	8,780	60.00	0.16	0.94
Peyto Exploration and Development Cor	PEYUF		21.15	132.7	2,810	24.00	0.11	0.90
Denbury Resources Inc.	DNR		21.57	397.0	8,560	25.00	0.19	0.89
Berry Petroleum Company	BRY		49.70	54.0	2,680	60.00	0.30	0.88
Birchcliff Energy Ltd.	BIREF	B	13.01	130.0	1,690	16.00	0.16	0.84
Ultra Petroleum	UPL		48.02	154.0	7,400	60.00	0.16	0.83
Whiting Petroleum Corporation	WLL	B	65.89	118.0	7,780	90.00	0.13	0.77
Cimarex Energy Company	XEC	B	90.13	86.1	7,760	120.00	0.06	0.77
<i>Total or Median</i>					55,320		0.16	0.88
Top Line Cash Payers								
Freehold Royalties Ltd.	FRHLF		22.16	58.4	1,290	22.00	0.06	1.01
Permian Basin RT	PBT		21.04	46.6	980	22.00	-	0.96
Sabine Royalty Trust	SBR		65.45	14.6	950	70.00	-	0.93
Dorchester Minerals, L.P.	DMLP	B	27.49	30.7	840	30.00	-	0.92
Cross Timbers Royalty Trust	CRT		40.99	6.0	250	45.00	-	0.91
<i>Total or Median</i>					4,310			0.93
Bottom Line Cash Payers								
Linn Energy, LLC	LINE		38.94	163.0	6,350	34.00	0.32	1.10
Legacy Reserves L.P.	LGCY		31.23	43.5	1,360	28.00	0.31	1.08
Vanguard Natural Resources, LLC	VNR		29.44	34.2	1,010	27.00	0.42	1.05
Hugoton Royalty Trust	HGT	B	23.02	40.0	920	22.00	-	1.05
Encore Energy Partners, L.P.	ENP		22.60	45.0	1,020	23.00	0.22	0.99
San Juan Basin Royalty Trust	SJT		23.94	46.6	1,120	25.00	-	0.96
Pengrowth Energy Corporation	PGH		13.08	326.0	4,260	14.00	0.27	0.95
Enerplus Corporation	ERF	B	31.96	179.5	5,740	37.00	0.19	0.89
Mesa Royalty Trust	MTR		41.11	1.9	77	53.00	-	0.78
<i>Total or Median</i>					21,860			0.99

B=Buy; 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 \$100 a barrel for oil and \$8 a million btu for natural gas.



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Table ISC-3								
McDep Income and Small Cap Energy Portfolio								
Value Multiples - Rank by EV/Ebitda								
			Price (\$/sh)	Revenue	Dist/ Equity	Adjstd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda
	Symbol/ Rating		26-May 2011	Royalty (%)	Ebitda	NTM	NTM	NTM
Small Cap Independent Producers								
Range Resources	RRC	B	55.59		-	17.4	16.0	15.0
Birchcliff Energy Ltd.	BIREF	B	13.01		-	20.1	14.4	12.1
Peyto Exploration and Development Corp	PEYUF		21.15		0.40	17.2	13.1	11.7
Ultra Petroleum	UPL		48.02		-	27.2	14.1	11.7
Petrohawk Energy Corporation	HK	B	25.76		-	7.6	10.0	10.4
Berry Petroleum Company	BRY		49.70		-	12.0	9.8	8.6
Denbury Resources Inc.	DNR		21.57		-	13.6	9.4	8.3
Whiting Petroleum Corporation	WLL	B	65.89		-	9.6	9.2	7.0
Cimarex Energy Company	XEC	B	90.13		-	7.2	8.3	6.3
	<i>Median</i>					<i>13.6</i>	<i>10.0</i>	<i>10.4</i>
Top Line Cash Payers								
Sabine Royalty Trust	SBR		65.45	100	1.00	7.0	14.4	13.5
Dorchester Minerals, L.P.	DMLP	B	27.49	77	0.85	7.1	14.6	13.3
Cross Timbers Royalty Trust	CRT		40.99	80	0.97	14.5	14.6	13.3
Permian Basin RT	PBT		21.04	32	0.94	15.6	12.1	11.6
Freehold Royalties Ltd.	FRHLF		22.16	71	0.82	6.4	10.4	10.5
	<i>Median</i>					<i>7.1</i>	<i>14.4</i>	<i>13.3</i>
Bottom Line Cash Payers								
Hugoton Royalty Trust	HGT	B	23.02		0.86	13.6	13.6	14.2
San Juan Basin Royalty Trust	SJT		23.94		0.84	9.1	14.7	14.1
Linn Energy, LLC	LINE		38.94		0.93	17.5	12.0	13.2
Vanguard Natural Resources, LLC	VNR		29.44		1.03	13.2	12.2	12.9
Mesa Royalty Trust	MTR		41.11		0.80	14.3	14.6	11.4
Legacy Reserves L.P.	LGCY		31.23		0.77	12.0	10.2	11.0
Encore Energy Partners, L.P.	ENP		22.60		0.89	13.0	10.5	10.3
Pengrowth Energy Corporation	PGH		13.08		0.57	9.2	9.2	8.8
Enerplus Corporation	ERF	B	31.96		0.59	8.4	9.9	8.8
	<i>Median</i>					<i>13.0</i>	<i>12.0</i>	<i>11.4</i>
B=Buy; CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.								
EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation								
and amortization; NTM = Next Twelve Months Ended March 31, 2012; P/E = Stock Price to								
Earnings; PV = Present Value of oil and gas and other businesses								
Top Line Cash Payers defined as those having Revenue Royalty (see fifth column from right).								



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Table ISC-4									
Oil and Gas Income and Small Cap Stocks									
Rank by Enterprise Value to 200 Day Average									
			Price (\$/sh)	Enterprise Value/					
	Symbol/ Rating		26-May 2011	52Wk High	52Wk Low	50 Day Avg.	200 Day Avg.	McDep Ratio	
Small Cap Independent Producers									
	BIRCLIFF ENERGY LTD.	BIREF	B	13.01	0.92	1.50	1.01	1.19	0.84
	RANGE RESOURCES	RRC	B	55.59	0.94	1.54	1.02	1.18	0.94
	PETROHAWK ENERGY CORPORATION	HK	B	25.76	0.96	1.42	1.03	1.18	1.05
	PEYTO EXPLORATION AND DEVELOPMENT C	PEYUF		21.15	0.98	1.57	1.03	1.16	0.90
	BERRY PETROLEUM COMPANY	BRY		49.70	0.95	1.50	1.00	1.12	0.88
	WHITING PETROLEUM CORPORATION	WLL	B	65.89	0.89	1.58	0.97	1.11	0.77
	DENBURY RESOURCES INC.	DNR		21.57	0.86	1.38	0.97	1.08	0.89
	ULTRA PETROLEUM	UPL		48.02	0.91	1.23	1.00	1.05	0.83
	CIMAREX ENERGY COMPANY	XEC	B	90.13	0.78	1.38	0.87	1.00	0.77
	<i>Median</i>				0.92	1.50	1.00	1.12	0.88
Top Line Cash Payers									
	SABINE ROYALTY TRUST	SBR		65.45	0.93	1.43	1.01	1.11	0.93
	FREEHOLD ROYALTIES LTD.	FRHLF		22.16	0.92	1.48	0.97	1.10	1.01
	DORCHESTER MINERALS, L.P.	DMLP	B	27.49	0.91	1.16	0.97	1.01	0.92
	PERMIAN BASIN RT	PBT		21.04	0.89	1.24	0.99	1.00	0.96
	CROSS TIMBERS ROYALTY TRUST	CRT		40.99	0.85	1.27	0.93	0.99	0.91
	<i>Median</i>				0.91	1.27	0.97	1.01	0.93
Bottom Line Cash Payers									
	HUGOTON ROYALTY TRUST	HGT	B	23.02	0.93	1.28	1.00	1.09	1.05
	LEGACY RESERVES L.P.	LGCY		31.23	0.95	1.33	1.00	1.08	1.08
	ENERPLUS CORPORATION	ERF	B	31.96	0.97	1.38	1.02	1.08	0.89
	LINN ENERGY, LLC	LINE		38.94	0.97	1.41	1.00	1.06	1.10
	ENCORE ENERGY PARTNERS, L.P.	ENP		22.60	0.91	1.35	0.98	1.05	0.99
	PENGROWTH ENERGY CORPORATION	PGH		13.08	0.92	1.30	0.97	1.04	0.95
	VANGUARD NATURAL RESOURCES, LLC	VNR		29.44	0.92	1.27	0.96	1.02	1.05
	SAN JUAN BASIN ROYALTY TRUST	SJT		23.94	0.84	1.15	0.94	0.98	0.96
	MESA ROYALTY TRUST	MTR		41.11	0.81	1.04	0.87	0.87	0.78
	<i>Median</i>				0.92	1.30	0.98	1.05	0.99

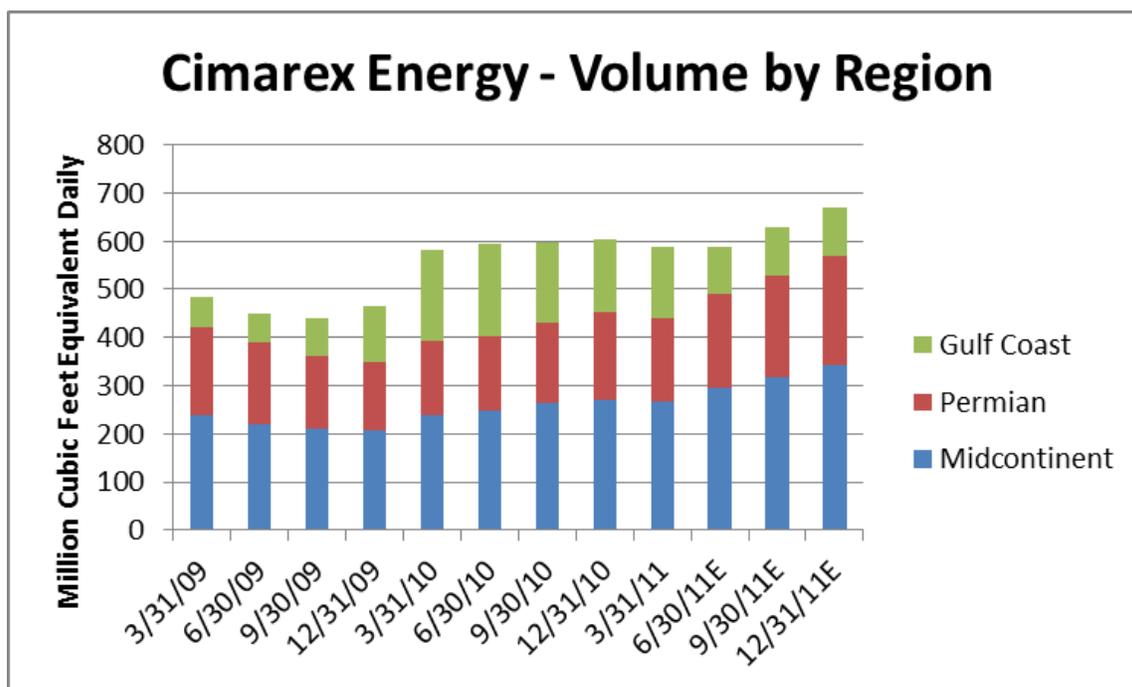
CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.



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Cimarex Energy Company					
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	440	8.3	11.1	4,900	44%
Oil	897	5.8	6.8	6,120	56%
	1,337	7.2	8.2	11,020	100%
Debt (US\$mm)					720
Net Present Value (US\$mm)					10,300
Shares (mm)					86
Net Present Value - Standard Estimate (US\$/sh)					120
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					129



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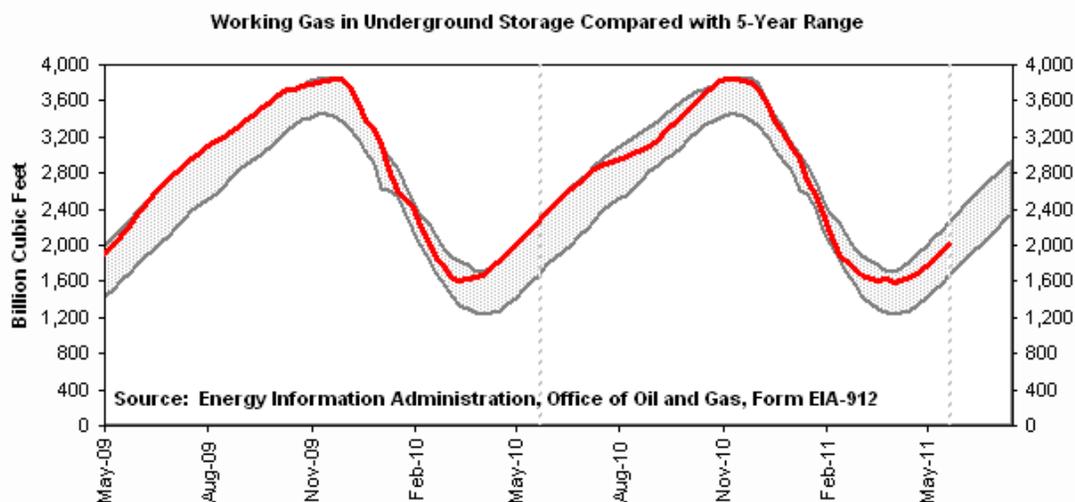
Cimarex Energy Company									
Next Twelve Months Operating and Financial Performance									
	Q2	Year	Q1	Q2E	Q3E	Q4E	Year	Q1E	Next Twelve Months
	6/30/10	2010	3/31/11	6/30/11	9/30/11	12/31/11	2011E	3/31/12	3/31/12
Volume									
Natural Gas (bcf)	33.8	133	29.5	31.0	32.6	33.9	127	33.5	131
Natural Gas (mmcf)	371	364	328	341	354	369	348	369	358
Days	91	365	90	91	92	92	365	91	366
Oil (mmb)	3.4	14.1	3.9	4.0	4.2	4.3	16.4	4.3	16.8
Oil (mbd)	37.2	38.7	43.7	43.7	45.4	47.3	45.0	47.3	45.9
Total (bcfe)	54.1	217	53.1	54.9	57.7	60.0	226	59.3	232
Total (mmcf)	594	596	590	603	627	652	618	652	634
Price									
Henry Hub (\$/mmbtu)	4.09	4.40	4.11	4.32	4.42	4.68	4.38	4.38	4.45
Differential (\$/mmbtu)	(0.39)	(0.52)	(0.34)	(0.36)	(0.37)	(0.39)	(0.37)	(0.36)	(0.37)
Company (\$/mcf)	4.48	4.92	4.45	4.67	4.79	5.07	4.76	4.74	4.82
WTI Cushing (\$/bbl)	77.85	79.43	94.10	103.34	97.98	98.94	98.59	98.36	99.66
Differential	14.73	14.32	22.24	24.43	23.16	23.39	23.30	23.25	23.60
Company (\$/bbl)	63.12	65.11	71.86	78.91	74.82	75.55	75.29	75.11	76.05
Total (\$/bbl)	40.48	43.00	46.77	50.17	48.77	50.05	48.98	48.75	49.43
Revenue (\$mm)									
Natural Gas	151	653	131	145	156	172	604	159	632
Oil	214	919	283	314	313	329	1,238	323	1,278
Other		(14)					-		
Total	365	1,559	414	459	469	500	1,842	482	1,910
Expense									
Operating	56	239	71						
Production taxes	28	121	34						
General and administrative	12	51	14						
Total	96	411	119	138	141	150	547	145	573
Ebitda	269	1,148	295	321	328	350	1,294	337	1,337
Deprec., Deplet., & Amor	75	311	87	99	104	108	398	107	417
Other Non Cash	2	(25)	6				6		-
Ebit	192	862	201	222	224	242	890	231	920
Interest	-	-	-	-	-	-	-	-	-
Ebt	192	862	201	222	224	242	890	231	920
Income Tax	67	302	70	78	79	85	312	81	322
Net Income (\$mm)	125	560	131	145	146	158	579	150	598
Per Share (\$)	1.46	6.54	1.52	1.68	1.69	1.83	6.72	1.74	6.94
Shares (millions)									
Operating (\$/mcfe)	1.04	1.10	1.34						
Production taxes (%rev)	7.7	7.8	8.2						
General and admin (\$/mcf)	0.22	0.23	0.26						
Deprec., D, & A (\$/mcf)	1.39	1.43	1.64	1.80	1.80	1.80	1.76	1.80	1.80
Ebitda Margin	74%	74%	71%	70%	70%	70%	70%	70%	70%
Tax rate	35%	35%	35%	35%	35%	35%	35%	35%	35%



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

May 27, 2011



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