

Rating: Buy
S&P 500: 1210

XTO Energy Inc.

Raise Net Present Value to \$45 a Share

<i>Symbol</i>	XTO	<i>Ebitda Next Twelve Months ending 3/31/06 (US\$mm)</i>	2,020
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	76
<i>Price (US\$/sh)</i>	40.83	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	2/16/05	<i>Adjusted Reserves/Production NTM</i>	11.6
<i>Shares (mm)</i>	280	<i>EV/Ebitda</i>	6.8
<i>Market Capitalization (US\$mm)</i>	11,400	<i>PV/Ebitda</i>	7.4
<i>Debt (US\$mm)</i>	2,300	<i>Undeveloped Reserves (%)</i>	22
<i>Enterprise Value (EV) (US\$mm)</i>	13,800	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	28.35
<i>Present Value (PV) (US\$mm)</i>	14,900	<i>Present Value Proven Reserves(US\$/boe)</i>	16.10
<i>Net Present Value (US\$/share)</i>	45	<i>Present Value Proven Reserves(US\$/mcf)</i>	2.68
<i>Debt/Present Value</i>	0.16	<i>Earnings Next Twelve Months (US\$/sh)</i>	2.93
<i>McDep Ratio - EV/PV</i>	0.92	<i>Price/Earnings Next Twelve Months</i>	14
<i>Dividend Yield (%/year)</i>	0.5	<i>Indicated Annual Dividend (US\$/sh)</i>	0.20

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 to recommend current purchase of the common shares of **XTO Energy (XTO)** for its concentration on North American natural gas and a remarkable growth record developing the premium fuel resource. We raised our estimate of net present value for the independent producer to \$45 a share from \$38 on January 26, 2005 when we revised our estimate of long-term oil price to \$40 a barrel constant real from \$35. The new NPV matches the level previously calculated in a sensitivity illustration (see *Stock Idea, XTO Energy*, September 8, 2004). Present value analysis gives little credit for a practically unmatched record of growth in reserves per share of more than 20% per year for the past ten years. XTO's stock price could double and the cash flow multiple, EV/Ebitda, at 12 times would still be low for the growth record.

Reserves per Share Grow 21% per Year

Our estimate of present value appears to validate the growth that XTO has achieved to date, but it gives no credit for future performance beyond earning a normal return. We further validate the growth by stating it in real terms --- physical units of natural gas reserves per share. Reserves per share are up about seven times in ten years for a growth rate of about 21% per year. The results are similar in terms of annual production per share thereby ruling out changes in reserve life or reserve statement as an artificial explanation for growth. A modest ratio of debt today rules out debt as the major explanation for growth. Price increases turn a real growth rate into an even higher nominal growth rate.

Acquisition Puts Company in Barnett Shale

The Fort Worth-based company has just become a leader in the rapidly growing field in the counties around Fort Worth. In a deal that is expected to close in April, XTO will buy the Barnett

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Shale properties of a private company, Antero Resources, for almost \$700 million, half stock and warrants. Nursed for decades by pioneer George Mitchell, the Barnett Shale field has apparently become the largest natural gas field in Texas by current production. Devon Energy, the successor to Mitchell Energy, has by far the dominant position and XTO may now be second, close in rank with a few other producers.

XTO's leading area continues to be East Texas and North Louisiana that accounted for 41% of fourth quarter 2004 production. Conceivably the Barnett Shale could become the second most important to XTO depending on continued successful drilling.

The company's natural gas representation dominates resource value (see table Functional Cash Flow and Present Value). The overall adjusted reserve life of 11.7 years might support a higher cash flow multiple, PV/Ebitda, judging by the correlation for the companies in our coverage. The numerator and the denominator are rapidly moving targets considering the company's high growth rate.

XTO Energy Inc.
Functional Cash Flow and Present Value

	<i>NTM Ebitda</i> <i>(US\$mm)</i>	<i>Adjusted</i> <i>R/P</i>	<i>PV/</i> <i>Ebitda</i>	<i>Present</i> <i>Value</i> <i>(US\$mm)</i>	
North American Natural Gas	1,530	11.7	7.8	12,000	81%
Oil	490	11.2	5.9	2,900	19%
	2,020	11.6	7.4	14,900	100%
Debt (US\$mm)				2,300	
Net Present Value (US\$mm)				12,600	
Shares (mm)				280	
Net Present Value (US\$/sh)				45	

Volume and Commodity Price Point to Further Gains

Holding volume constant at the latest quarterly rate implies annual growth of 15% in 2005. Management expects growth of 18-20% without the Antero acquisition and 21-23% with it. Natural gas and oil futures prices drive further gains in cash flow in our model (see table Next Twelve Months Operating and Financial Estimates).

The complications of the cash flow model include incentive compensation and hedging. The cash flow we calculate for valuation purposes excludes hedging and unusual compensation. The hedging exposure appears well-defined.

Perhaps our estimated present value should be reduced by a few dollars a share to reflect future incentive compensation at some 7% of incremental value created. While the amount is quite rewarding to the recipients and is generous by exploration company standards it is not large enough to cause valuation concern. To the contrary, we might instead contemplate how continued performance along the lines of past results might magnify the values we identify.

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XTO Energy Inc.
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)	847	916	835	916	916	916	916	916	916	916
Oil (mbd)	33	42	30	42	42	42	42	42	42	42
Total gas & oil (bcf)	96	108	372	106	106	108	108	428	106	428
Price										
Natural gas (\$/mcf)										
Henry Hub (\$/mmbtu)	5.75	7.10	6.15	6.20	6.23	6.38	6.76	6.39	7.21	6.65
Company (\$/mcf)	5.44	5.91	5.52	5.56	5.59	5.72	6.07	5.74	6.47	5.96
Oil (\$/bbl)										
WTI Cushing	43.89	48.30	41.44	46.93	48.10	47.42	46.57	47.25	45.47	46.89
Company (\$/bbl)	38.58	42.96	37.41	41.75	42.33	41.73	40.98	41.69	40.01	41.26
Total gas & oil (\$/mcf)	5.63	6.18	5.64	5.86	5.91	5.99	6.23	6.00	6.51	6.16
Revenue (\$mm)										
Natural Gas	424	498	1,685	463	466	482	511	1,923	539	1,999
Oil	117	166	413	160	162	162	159	643	153	636
Other										
Total	541	665	2,098	623	628	644	670	2,566	693	2,635
Expense										
Production	111	134	424	130	130	132	135	527	137	534
Overhead	33	15	79	20	20	20	20	80	20	80
Ebitda (\$mm)	398	516	1,595	474	478	492	515	1,959	536	2,021
Exploration	3	5	11	5	5	5	5	20	5	20
Deprec., Deplet., & Amort.	107	128	410	128	128	129	129	513	128	513
Hedging and other	36	80	282	19	21	23	31	94	40	115
Ebit	252	302	893	322	324	334	350	1,331	364	1,373
Interest	23	28	93	28	28	28	28	112	28	112
Ebt	229	274	800	294	296	306	322	1,219	336	1,261
Income Tax	88	96	288	103	104	107	113	427	117	441
Net Income (\$mm)	141	178	512	191	193	199	210	793	218	819
Shares (millions)	261	262	254	262	262	286	286	274	286	280
Per share (\$)	0.54	0.68	2.02	0.73	0.73	0.70	0.73	2.89	0.76	2.93
Ebitda Margin - O&G	73%	78%	76%	76%	76%	76%	77%	76%	77%	77%
Tax Rate	38%	35%	36%	35%	35%	35%	35%	35%	35%	35%

Buy Oil and Gas Producers at Mid Decade

XTO stock appears undervalued along with peers (see table Rank by McDep Ratio). Though its degree of undervaluation may appear to be less, XTO has a superior growth record.

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.

Kurt H. Wulff, CFA

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

	<i>Symbol/</i>	<i>Rating</i>	<i>Price</i> <i>(\$/sh)</i>	<i>Shares</i>	<i>Market</i>	<i>Net</i>	<i>Debt/</i>	<i>McDep</i>
			<i>16-Feb</i>	<i>(mm)</i>	<i>Cap</i>	<i>Present</i>	<i>Present</i>	<i>Ratio</i>
			<i>2005</i>		<i>(\$mm)</i>	<i>Value</i>	<i>Value</i>	
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	40.83	280	11,430	45.00	0.16	0.92
Encana Corporation	ECA	B	63.95	472	30,200	77.00	0.18	0.86
Unocal Corporation	UCL	B	51.42	271	13,900	65.00	0.21	0.83
CNOOC Limited (19%)	CEO	B	53.77	78	4,200	67.00	-	0.80
Occidental Petroleum Corp.	OXY	B	66.60	406	27,100	87.00	0.15	0.80
Burlington Resources	BR	B	48.04	391	18,800	67.00	0.12	0.75
Devon Energy Corporation	DVN	B	43.61	500	21,800	63.00	0.16	0.74
Anadarko Petroleum Corp.	APC	B	70.00	246	17,200	113.00	0.14	0.67
	<i>Total or Median</i>				<i>145,000</i>		<i>0.15</i>	<i>0.80</i>

B = Buy, 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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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 negative total return less than 7% per year including the effects of inflation.

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