

Rating: Buy  
S&P 500: 1166

## **XTO Energy Inc.**

### **Raise Net Present Value to \$36 a Share**

<i>Symbol</i>	XTO	<i>Ebitda Next Twelve Months ending 3/31/06 (US\$m)</i>	2,370
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	77
<i>Price (US\$/sh)</i>	30.65	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	5/10/05	<i>Adjusted Reserves/Production NTM</i>	11.8
<i>Shares (mm)</i>	364	<i>EV/Ebitda</i>	6.0
<i>Market Capitalization (US\$m)</i>	11,100	<i>PV/Ebitda</i>	6.9
<i>Debt (US\$m)</i>	3,200	<i>Undeveloped Reserves (%)</i>	28
<i>Enterprise Value (EV) (US\$m)</i>	14,300	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	30.20
<i>Present Value (PV) (US\$m)</i>	16,300	<i>Present Value Proven Reserves(US\$/boe)</i>	15.10
<i>Net Present Value (US\$/share)</i>	36	<i>Present Value Proven Reserves(US\$/mcfe)</i>	2.52
<i>Debt/Present Value</i>	0.20	<i>Earnings Next Twelve Months (US\$/sh)</i>	2.65
<i>McDep Ratio - EV/PV</i>	0.88	<i>Price/Earnings Next Twelve Months</i>	12
<i>Dividend Yield (%/year)</i>	0.7	<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 concentration on North American natural gas and a remarkable growth record developing that premium fuel resource. Continued favorable financial results justify an additional increase in net present value to \$36 a share following an increase earlier this year to \$33.75 from \$28.50. Previous estimates have been adjusted for a 4 for 3 stock split effective March 16, 2005. Present value analysis gives little credit for a practically unmatched record of growth in reserves per share of some 24% per year for the past ten years. XTO's stock price could double and the cash flow multiple, EV/Ebitda, at 11 times would still be low for the growth record.

### **Reserves per Share Grow 24% 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. Reserves per share are up almost nine times in ten years for a growth rate of about 24% per year. Production gains seem to validate the reserve gains. Debt, high at times historically, is modest today. Price increases turn a real growth rate into an even higher nominal growth rate.

### **Inspired by San Juan Basin Royalty Trust**

Members of XTO's current management contributed to the formation of the **San Juan Basin Royalty Trust (SJT)** in 1980. Now SJT and XTO are both ten baggers, stocks that returned more than ten times in ten years. The properties in the trust produce today more than almost anyone publicly contemplated twenty five years ago. XTO seems to have found similar types of properties in its acquisitions not only in the San Juan Basin, but also prominently in North Texas

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and East Texas. Thus, the company seems to have had remarkable success identifying properties that fit a model of profitable development and volume enhancement.

### **East Texas Acquisition Sets up More Growth**

Following a \$700 million acquisition of Barnett Shale properties in April, the company will pay \$350 million for Eastern Region properties in a deal expected to close in June. We include the volumes for the two acquisitions in reserves and next twelve months production. Concurrently we also include pro forma debt and shares that finance the deals.

The natural gas resources of the Eastern Region including East Texas and North Louisiana account for about a third of company reserves. Conceivably the Barnett Shale could become the second most important to XTO depending on continued successful drilling.

### **Higher Cash Flow Multiple for Natural Gas**

A disparity between natural gas price and oil price has widened enough to be reflected in different cash flow multiples for natural gas as opposed to oil production (see table Functional Cash Flow and Present Value). The separate cash flow multiples, PV/Ebitda, are consistent with the separate adjusted reserve life indices judging by the correlation for the companies in our coverage.

#### **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	1,830	12.0	7.3	13,300	82%
Oil	540	11.3	5.6	3,000	18%
	2,370	11.8	6.9	16,300	100%
Debt (US\$mm)					3,200
Net Present Value (US\$mm)					13,100
Shares (mm)					364
Net Present Value (US\$/sh)					36

### **Volume and Commodity Price Point to Further Gains**

Volume growth of 24% in 2005 over 2004 compares to current management guidance of 24-26%. 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. We reduce cash flow for a high level of overhead expense that includes an extra allowance for executive compensation.

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**XTO Energy Inc.**  
**Next Twelve Months Operating and Financial Estimates**

	<i>Q3</i>	<i>Q4</i>	<i>Year</i>	<i>Q1</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>
<b>Volume</b>										
Natural Gas (mmcf)	847	916	<b>835</b>	922	1,000	1,040	1,040	<b>1,001</b>	1,040	<b>1,030</b>
Oil (mbd)	33	42	<b>30</b>	46	43	43	43	<b>44</b>	43	<b>43</b>
Total gas & oil (bcf)	96	108	<b>372</b>	109	114	119	119	<b>462</b>	118	<b>471</b>
<b>Price</b>										
Natural gas (\$/mcf)										
Henry Hub (\$/mmbtu)	5.75	7.10	<b>6.15</b>	6.27	6.94	6.83	7.37	<b>6.85</b>	8.00	<b>7.28</b>
Company (\$/mcf)	5.44	5.91	<b>5.52</b>	5.65	6.25	6.15	6.64	<b>6.19</b>	7.21	<b>6.57</b>
Oil (\$/bbl)										
WTI Cushing	43.89	48.31	<b>41.44</b>	49.65	52.14	53.75	53.68	<b>52.31</b>	53.33	<b>53.22</b>
Company (\$/bbl)	38.58	42.96	<b>37.41</b>	41.65	45.88	47.30	47.24	<b>45.46</b>	46.93	<b>46.84</b>
Total gas & oil (\$/mcf)	5.63	6.18	<b>5.64</b>	5.95	6.54	6.50	6.89	<b>6.48</b>	7.33	<b>6.82</b>
<b>Revenue (\$mm)</b>										
Natural Gas										
	424	498	<b>1,685</b>	-	-	-	-	-	-	-
Overseas (or Int'l)	-	-	-	-	-	-	-	-	-	-
Natural Gas	424	498	<b>1,685</b>	474	569	589	636	<b>2,267</b>	683	<b>2,476</b>
Oil	117	166	<b>413</b>	175	180	187	187	<b>729</b>	184	<b>737</b>
Other										
Total	541	665	<b>2,098</b>	649	748	776	823	<b>2,996</b>	866	<b>3,213</b>
<b>Expense</b>										
Production	111	134	<b>424</b>	144	154	157	162	<b>617</b>	166	<b>640</b>
Overhead	33	15	<b>79</b>	50	50	50	50	<b>200</b>	50	<b>200</b>
<b>Ebitda (\$mm)</b>	398	516	<b>1,595</b>	456	544	569	611	<b>2,179</b>	650	<b>2,373</b>
Exploration	3	5	<b>11</b>	1	1	1	1	<b>4</b>	1	<b>4</b>
Deprec., Deplet., & Amort.	107	128	<b>410</b>	129	137	143	143	<b>553</b>	142	<b>566</b>
Hedging and other	36	80	<b>282</b>	42	42	42	54	<b>181</b>	68	<b>207</b>
<b>Ebit</b>	252	302	<b>893</b>	284	363	382	412	<b>1,441</b>	439	<b>1,597</b>
Interest	23	28	<b>93</b>	29	29	29	29	<b>116</b>	29	<b>116</b>
<b>Ebt</b>	229	274	<b>800</b>	255	334	353	383	<b>1,325</b>	410	<b>1,481</b>
Income Tax	88	96	<b>288</b>	89	117	124	134	<b>464</b>	144	<b>518</b>
<b>Net Income (\$mm)</b>	141	178	<b>512</b>	165	217	230	249	<b>861</b>	267	<b>962</b>
<b>Shares (millions)</b>	348	349	<b>338</b>	352	364	364	364	<b>361</b>	364	<b>364</b>
Per share (\$)	0.41	0.51	<b>1.52</b>	0.47	0.60	0.63	0.68	<b>2.38</b>	0.73	<b>2.65</b>
Ebitda Margin - O&G	73%	78%	<b>76%</b>	70%	73%	73%	74%	<b>73%</b>	75%	<b>74%</b>
Tax Rate	38%	35%	<b>36%</b>	35%	35%	35%	35%	<b>35%</b>	35%	<b>35%</b>

**Buy Oil and Gas Producers at Mid Decade**

Multi-fold gain potential for oil and gas price over the years ahead justifies investment in recommended oil and gas producers, in our opinion. A McDep Ratio of 1.0 implies that a stock is valued at present value assuming a constant real oil price of US\$40 (see table Rank by McDep Ratio). That is lower than the current benchmark oil average futures price for the next six years of about US\$50 a barrel. Moreover the average 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 of about \$42 a barrel.

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**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>10-May</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>
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
Encana Corporation	ECA	B	69.17	471	32,600	77.00	0.19	0.92
Unocal Corporation	UCL	B	55.90	271	15,100	65.00	0.21	0.89
XTO Energy Inc.	XTO	B	30.65	364	11,150	36.00	0.20	0.88
CNOOC Limited (19%)	CEO	B	56.21	78	4,390	67.00	-	0.84
Occidental Petroleum Corp.	OXY	B	68.97	406	28,000	87.00	0.14	0.82
Burlington Resources	BR	B	49.17	389	19,100	67.00	0.12	0.76
Devon Energy Corporation	DVN	B	44.30	500	22,200	63.00	0.16	0.75
Anadarko Petroleum Corp.	APC	B	73.03	246	18,000	113.00	0.14	0.70
	<i>Total or Median</i>				<i>151,000</i>		<i>0.15</i>	<i>0.83</i>

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