

Rating: Buy  
S&P 500: 1178

## **XTO Energy** **Ready for Winter**

<i>Symbol</i>	XTO	<i>Ebitda Next Twelve Months ending 9/30/06 (US\$mm)</i>	3,790
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	80
<i>Price (US\$/sh)</i>	38.80	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	10/20/05	<i>Adjusted Reserves/Production NTM</i>	10.8
<i>Shares (mm)</i>	370	<i>EV/Ebitda</i>	4.9
<i>Market Capitalization (US\$mm)</i>	14,400	<i>PV/Ebitda</i>	5.8
<i>Debt (US\$mm)</i>	4,300	<i>Undeveloped Reserves (%)</i>	28
<i>Enterprise Value (EV) (US\$mm)</i>	18,700	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	44.10
<i>Present Value (PV) (US\$mm)</i>	22,100	<i>Present Value Proven Reserves(US\$/boe)</i>	20.48
<i>Net Present Value (US\$/share)</i>	48	<i>Present Value Proven Reserves(US\$/mcfe)</i>	3.41
<i>Debt/Present Value</i>	0.20	<i>Earnings Next Twelve Months (US\$/sh)</i>	4.61
<i>McDep Ratio - EV/PV</i>	0.85	<i>Price/Earnings Next Twelve Months</i>	8
<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**

Concentrated 83% by value on U.S. natural gas production, buy-recommended **XTO Energy (XTO)** ought to generate steep profit gains in the next two quarters. Natural gas futures for the winter ahead are some \$13 a million btu compared to actual reference price of less than \$9 for the quarter just reported. First quarter 2006 revenue may be about \$200 million higher because costly hedges expire at year end. The stock has 24% appreciation potential to net present value tied to a long-term natural gas price of \$10. Present value may understate the potential of a company that has practically the best growth record of energy stocks for the past ten years. The main risk in energy stocks currently seems to be the stock market rather than commodity price.

### **Quarterly Results Boost Projections**

Positive volume trends support higher future expectations. It looks like our latest projections of next twelve months cash flow combined with adjusted reserve life are within \$2 of estimated net present value of \$48 a share according to a correlation with about 30 companies (see table Functional Cash Flow and Present Value).

There are many moving parts to the projection including volume, price and costs (see table Next Twelve Months Operating and Financial Estimates). The quarterly projection of natural gas price is a striking feature with the higher prices immediately ahead. Similarly the line including hedging costs illustrates the opportunity when currently disadvantageous contracts run out at the end of 2005.

**Please see disclosures on the final page.**

**XTO Energy Inc.**  
**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	3,070	11.2	6.0	18,300	83%
Oil	760	9.4	5.0	3,800	17%
	3,830	10.8	5.8	22,100	100%
Debt (US\$mm)					4,300
Net Present Value (US\$mm)					17,800
Shares (mm)					370
Net Present Value (US\$/sh)					48
Over (-)/ Under (+) Correlation (US\$/sh)					(2)

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

	<i>Q4</i>	<i>Year</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Next</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>6/30/06</i>	<i>9/30/06</i>	<i>Twelve</i>
											<i>Months</i>
											<i>9/30/06</i>
<b>Volume</b>											
Natural Gas (mmcf)	916	<b>835</b>	922	1,019	1,087	1,100	<b>1,032</b>	1,100	1,100	1,100	<b>1,100</b>
Oil (mbd)	42	<b>30</b>	46	47	52	52	<b>49</b>	52	52	52	<b>52</b>
Total gas & oil (bcf)	108	<b>372</b>	109	119	129	130	<b>486</b>	128	128	130	<b>516</b>
<b>Price</b>											
Natural gas (\$/mcf)											
Henry Hub (\$/mmbtu)	7.10	<b>6.15</b>	6.27	6.76	8.56	13.39	<b>8.75</b>	13.49	10.36	10.30	<b>11.89</b>
Company (\$/mcf)	5.91	<b>5.52</b>	5.65	6.10	7.04	11.38	<b>7.66</b>	11.47	8.80	8.76	<b>10.10</b>
Oil (\$/bbl)											
WTI Cushing	48.31	<b>41.44</b>	49.65	53.05	62.52	61.10	<b>56.58</b>	60.11	60.16	60.05	<b>60.35</b>
Company (\$/bbl)	42.96	<b>37.41</b>	41.65	40.51	49.10	53.77	<b>46.54</b>	52.89	52.94	52.84	<b>53.11</b>
Total gas & oil (\$/mcf)	6.18	<b>5.64</b>	5.95	6.24	7.29	10.85	<b>7.68</b>	10.89	8.81	8.77	<b>9.83</b>
<b>Revenue (\$mm)</b>											
Natural Gas	498	<b>1,685</b>	474	566	704	1,152	<b>2,896</b>	1,148	881	886	<b>4,068</b>
Oil	166	<b>413</b>	175	174	234	256	<b>839</b>	249	249	251	<b>1,005</b>
Other											
Total	665	<b>2,098</b>	649	740	938	1,408	<b>3,735</b>	1,397	1,130	1,138	<b>5,073</b>
<b>Expense</b>											
Production	134	<b>424</b>	144	164	192	314	<b>813</b>	311	242	243	<b>1,110</b>
Overhead	15	<b>79</b>	50	35	34	34	<b>152</b>	34	34	34	<b>134</b>
<b>Ebitda (\$mm)</b>	516	<b>1,595</b>	456	541	713	1,061	<b>2,770</b>	1,053	855	861	<b>3,829</b>
Exploration	5	<b>11</b>	1	6	13	13	<b>32</b>	13	13	13	<b>50</b>
Deprec., Deplet., & Amort.	128	<b>410</b>	129	155	182	182	<b>648</b>	182	182	182	<b>727</b>
Hedging and other	80	<b>282</b>	42	3	(10)	205	<b>241</b>	5	2	2	<b>215</b>
<b>Ebit</b>	302	<b>893</b>	284	377	528	662	<b>1,850</b>	853	659	664	<b>2,838</b>
Interest	28	<b>93</b>	29	38	44	44	<b>155</b>	44	44	44	<b>176</b>
<b>Ebt</b>	274	<b>800</b>	255	339	484	618	<b>1,695</b>	809	615	620	<b>2,662</b>
Income Tax	96	<b>288</b>	89	119	169	216	<b>593</b>	283	215	217	<b>932</b>
<b>Net Income (\$mm)</b>	178	<b>512</b>	165	220	315	401	<b>1,102</b>	526	400	403	<b>1,730</b>
Shares (millions)	349	<b>338</b>	352	367	370	370	<b>367</b>	370	370	370	<b>370</b>
Per share (\$)	0.51	<b>1.52</b>	0.47	0.60	0.85	1.08	<b>3.00</b>	1.42	1.08	1.09	<b>4.68</b>
Ebitda Margin - O&G	78%	<b>76%</b>	70%	73%	76%	75%	<b>74%</b>	75%	76%	76%	<b>75%</b>
Tax Rate	35%	<b>36%</b>	35%	35%	35%	35%	<b>35%</b>	35%	35%	35%	<b>35%</b>

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**Model Better Than Ever**

On the quarterly call, Chairman Bob Simpson recalled that for years the company operated on the philosophy that reserves and production could be held flat by reinvesting half of cash flow. Now at a long-term natural gas price of \$10 a million btu, Mr. Simpson believes that XTO can grow reserves and production at 10-12% per year while reinvesting half of cash flow. The other half of cash flow can be used for acquisitions when great assets are available at attractive price or for stock repurchase to increase concentration on the great assets XTO already owns.

The new value creation model implies a rate of return of more than 20% per year compared to 7% per year plus inflation in our present value calculation. If Mr. Simpson is right, and he has a remarkable record, XTO should remain an outstanding investment.

**Valuation Trends Continue**

Six-year natural gas continues to trade above its 40-week average as it has since 2002. Similarly XTO stock continues to trade above its 200-day average as it has also since 2002. Thus, there is no indication of a change in momentum despite recent declines and we are not expecting a change to occur soon. Yet we can't control events and if momentum did change we would acknowledge that and be more conservative in our immediate expectations. Meanwhile stocks appear valued at less than the levels that correspond to our long-term commodity price expectations (see table [Rank by McDep Ratio](#)).

**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>20-Oct</i>	<i>(mm)</i>	<i>Cap</i>	<i>Value</i>	<i>Present</i>	<i>Ratio</i>
			<i>2005</i>		<i>(\$mm)</i>	<i>(\$/sh)</i>	<i>Value</i>	
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
Encana Corporation	ECA	B	48.55	892	43,300	51.00	0.16	0.96
XTO Energy Inc.	XTO	B	38.80	370	14,360	48.00	0.20	0.85
Burlington Resources	BR	B	65.03	385	25,000	86.00	0.09	0.78
CNOOC Limited (29%)	CEO	B	61.70	119	7,360	84.00	0.01	0.74
Devon Energy Corporation	DVN	B	57.52	471	27,100	86.00	0.15	0.72
Anadarko Petroleum Corp.	APC	B	85.51	238	20,400	140.00	0.11	0.66
Occidental Petroleum Corp.	OXY	B	69.94	406	28,400	120.00	0.11	0.63
			<i>Total or Median</i>		<i>166,000</i>		<i>0.11</i>	<i>0.74</i>

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