



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

April 20, 2012

Good Stuff

Summary and Recommendation

In an active week of making research contacts we received solid reinforcement of underlying strengths in oil and gas income and small cap stocks. Contrarian Buy **Cimarex (XEC)** may be developing its next step-change in resource value with a new shale/tight oil play in remote Culberson County, Texas (see slide Delaware Basin on page 2). Another active West Texas producer gives indirect support to the strong ranking of XEC as the fourth most active horizontal driller despite not being among the largest traditional producers in the Permian Basin (see slide Concho on page 2). Buy recommended **Whiting (WLL)** ranks itself as the operator with the most productive wells in North Dakota's Bakken shale. The list gives indirect support to Contrarian-Buy **Enerplus (ERF)** ranked #3 of more than 25 drillers (see slide Production by Operator on page 3). Contrarian Buy **Range Resources (RRC)** adds further oil and gas potential to its strong base as the originator of the Marcellus Shale play, each of which is worth a separate discussion (see slide Enhancements on page 3).

Some of our favorite stocks have lost market value rapidly while others have recovered from previously depressed levels. A wise, experienced client reminds us of the virtues of concentration. The more familiar he can be with his investments the more confidence he has to act when short-term trends may be adverse. We have seen that small cap stocks commonly rise 50% from the low to the high practically every year.

McDep Ratios are well within buy range below 1.0, while 1.0 still implies an attractive long-term return of 7% a year – unlevered and after adjustment for inflation. Ratios of Enterprise Value (EV) to Market Cap and ratios of Debt to Present Value (PV) measure financial strength (see Table ISC-1 and Table ISC-2 on pages 4-5). Unlevered cash flow multiples (EV/Ebitda) usually relate to reserve life except that reported reserves can be greatly understated (see Table ISC-3 on page 6). Finally, we see that the record gap between current natural gas inventories and the historical range is beginning to narrow (see chart Underground Storage on page 7).

Kurt H. Wulff, CFA

• **Delaware Basin – multiple plays:**

- New Mexico Bone Spring
65,000 net acres
- Texas Bone Spring
35,000 net acres
- Texas/New Mexico Unconventional (Wolfcamp, Avalon & Cisco/Canyon)
110,000-160,000 net acres
- Abo/Paddock
48,000 net acres



NYSE:XEC

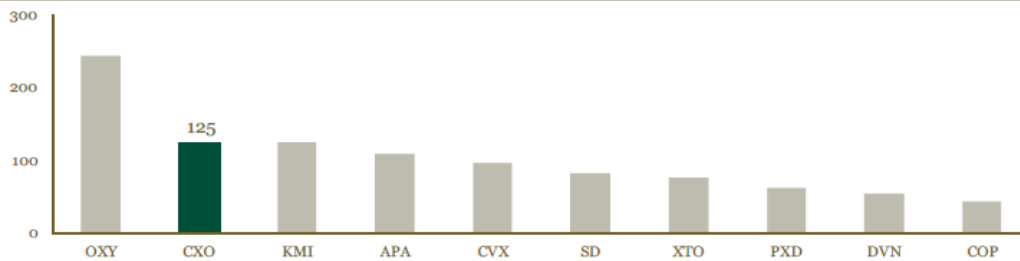
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CIMAREX

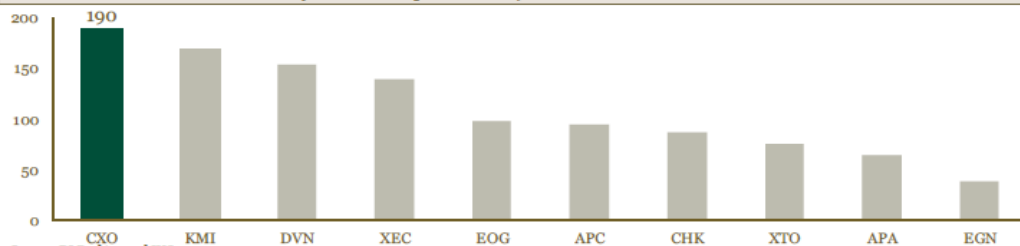


A Leader in the Permian Basin

Permian Gross Operated Production (MBoe/d)¹



Permian Horizontal Wells Drilled by Public Companies (2009 – 2011)



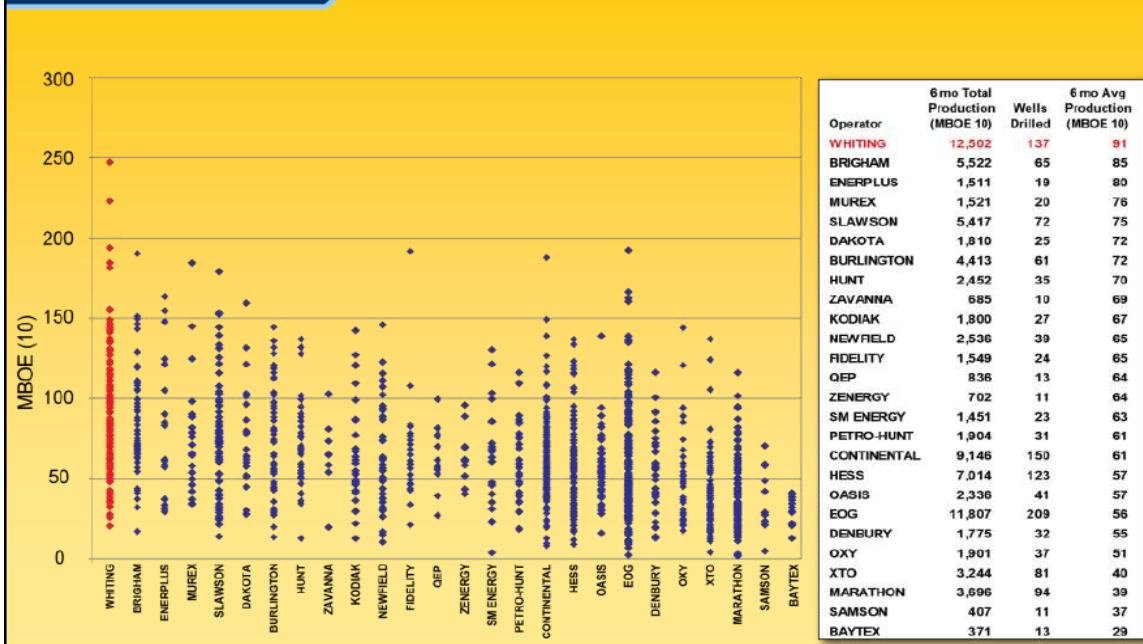
Source: DI Desktop and IHS.
1 Gross operated production for the month of November 2011.

Six Month Cumulative Production by Operator

For Bakken Wells Drilled Since January 2009

& Operators With Greater Than 10 Wells Producing

Source: IHS Energy, Inc. & North Dakota Industrial Commission (As of February 2012)



Enhancements to Portfolio

Range has five enhancements to the existing portfolio for 2012

1. Super-rich Marcellus – 1,350 Btu or higher wet gas
2. Super-rich Upper Devonian
3. Wet Utica Shale
4. Horizontal Mississippian oil play
5. Cline Shale oil play



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Table ISC-1											
McDep Income and Small Cap Energy Portfolio											
Debt, Segments, Cash Flow, Income and McDep Ratio											
			Price								
Symbol/Rating		(US\$/sh)	EV/	Enterprise	PV(%)		EV/	Dist.	Dist.		
B = Buy	19-Apr	Market	Value	Nat	Oil	Ebitda	NTM	Yield	McDep		
CB (see below)	2012	Cap	(\$mm)	Gas		NTM	(\$/un)	(%)	Ratio		
Small Cap Independent Producers											
PDC Energy	PETD		32.21	1.64	1,240	54	46	7.1	-	-	0.87
Range Resources	RRC	CB	58.58	1.27	11,870	71	29	13.5	0.16	0.3	0.87
Berry Petroleum Company	BRY		44.08	1.62	3,920	15	85	5.5	0.32	0.7	0.73
Denbury Resources Inc.	DNR		18.00	1.39	9,840	6	94	5.7	-	-	0.71
Peyto Exploration and Development	PEYUF		15.12	1.24	2,500	75	25	8.4	0.72	4.8	0.68
Whiting Petroleum Corporation	WLL	B	54.23	1.29	8,310	8	92	4.7	-	-	0.67
Cimarex Energy Company	XEC	CB	65.01	1.16	6,510	40	60	5.2	0.36	0.6	0.63
Birchcliff Energy Ltd.	BIREF	CB	5.80	1.44	1,220	60	40	7.9	-	-	0.45
<i>Total or Median</i>					45,400			6.4			0.70
Top Line Cash Payers											
Permian Basin RT	PBT		21.11	1.00	980	37	63		1.45	6.9	1.06
Cross Timbers Royalty Trust	CRT		39.84	1.00	240	70	30		2.55	6.4	0.91
Sabine Royalty Trust	SBR		57.04	1.00	830	55	45		3.81	6.7	0.88
Dorchester Minerals, L.P.	DMLP	CB	23.70	1.00	730	57	43		1.97	8.3	0.88
Freehold Royalties Ltd.	FRHLF		18.23	1.04	1,230	16	84		1.68	9.2	0.87
<i>Total or Median</i>					4,000					6.9	0.88
Bottom Line Cash Payers											
Linn Energy, LLC	LINE		38.51	1.75	11,820	37	63	11.3	2.76	7.2	1.14
Vanguard Natural Resources, LLC	VNR		27.70	1.46	2,100	20	80	9.7	2.35	8.5	1.07
Legacy Reserves L.P.	LGCY		28.77	1.35	1,850	24	76	8.6	2.20	7.6	0.97
Enduro Royalty Trust (40%)	NDRO		20.05	1.00	270	42	58	7.2	1.76	8.8	0.96
Mesa Royalty Trust	MTR		33.00	1.00	61	75	25	8.8	3.29	10.0	0.82
San Juan Basin Royalty Trust	SJT	CB	16.73	1.00	780	100	-	15.1	0.71	4.2	0.80
Enerplus Corporation	ERF	CB	18.09	1.40	5,000	28	72	5.7	2.16	12.0	0.76
Hugoton Royalty Trust	HGT		12.57	1.00	500	88	12	15.1	0.70	5.5	0.74
<i>Total or Median</i>					22,400			9.3		8.1	0.89
Composite											
<i>Enterprise Value Weighting</i>					71,800	36	64				0.79
<i>Equal Weighting</i>						46	54				0.83
<i>Equal Weighted Buys</i>						43	57				0.71

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 \$6 a million btu for natural gas.

Dist. = Income distribution. NTM = Next Twelve Months Ended March 31, 2013. 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)		Market	Net		
	Symbol/ Rating	19-Apr 2012	Shares (mm)	Cap (\$mm)	Present Value (\$/un)	Debt/ Present Value	McDep Ratio
Small Cap Independent Producers							
PDC Energy	PETD	32.21	23.6	760	40.00	0.34	0.87
Range Resources	RRC CB	58.58	160.0	9,370	70.00	0.18	0.87
Berry Petroleum Company	BRY	44.08	55.0	2,420	70.00	0.28	0.73
Denbury Resources Inc.	DNR	18.00	393.0	7,070	28.00	0.20	0.71
Peyto Exploration and Development Cor	PEYUF	15.12	133.9	2,020	24.00	0.13	0.68
Whiting Petroleum Corporation	WLL B	54.23	119.0	6,450	88.00	0.15	0.67
Cimarex Energy Company	XEC CB	65.01	86.2	5,600	110.00	0.09	0.63
Birchcliff Energy Ltd.	BIREF CB	5.80	147.0	850	16.00	0.14	0.45
<i>Total or Median</i>				34,540		0.17	0.70
Top Line Cash Payers							
Permian Basin RT	PBT	21.11	46.6	980	20.00	-	1.06
Cross Timbers Royalty Trust	CRT	39.84	6.0	240	44.00	-	0.91
Sabine Royalty Trust	SBR	57.04	14.6	830	65.00	-	0.88
Dorchester Minerals, L.P.	DMLP CB	23.70	30.7	730	27.00	-	0.88
Freehold Royalties Ltd.	FRHLF	18.23	64.8	1,180	21.00	0.03	0.87
<i>Total or Median</i>				3,960			0.88
Bottom Line Cash Payers							
Linn Energy, LLC	LINE	38.51	175.0	6,740	30.00	0.49	1.14
Vanguard Natural Resources, LLC	VNR	27.70	52.0	1,440	25.00	0.34	1.07
Legacy Reserves L.P.	LGCY	28.77	47.5	1,370	30.00	0.25	0.97
Enduro Royalty Trust (40%)	NDRO	20.05	13.2	270	21.00	-	0.96
Mesa Royalty Trust	MTR	33.00	1.9	61	40.00	-	0.82
San Juan Basin Royalty Trust	SJT CB	16.73	46.6	780	21.00	-	0.80
Enerplus Corporation	ERF CB	18.09	196.0	3,550	26.00	0.22	0.76
Hugoton Royalty Trust	HGT	12.57	40.0	500	17.00	-	0.74
<i>Total or Median</i>				14,710			0.89
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 \$6 a million btu for natural gas.							



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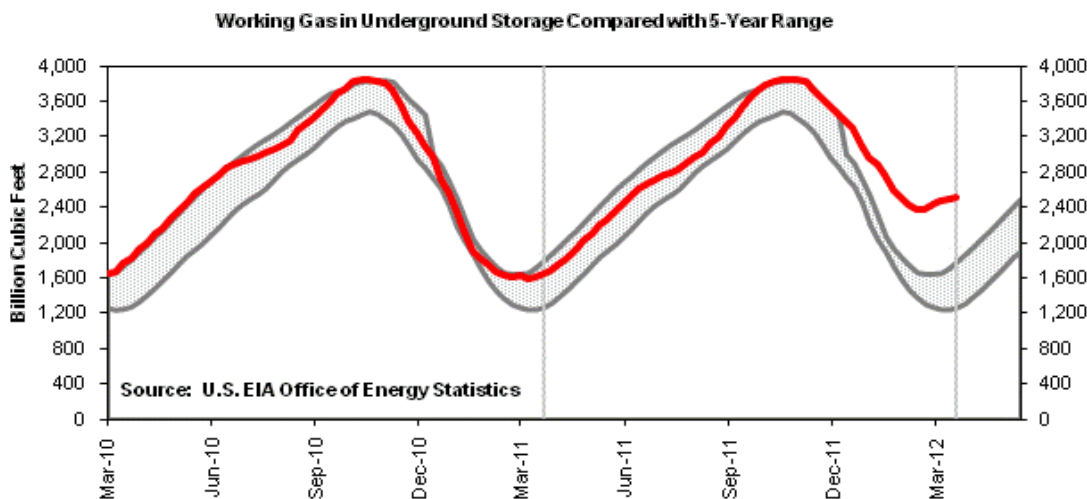
Table ISC-3								
McDep Income and Small Cap Energy Portfolio								
Value Multiples - Rank by EV/Ebitda								
			Price (\$/sh)	Revenue	Dist/ Equity	Adjstd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda
	Symbol/ Rating		19-Apr 2012	Royalty (%)	Ebitda	NTM	NTM	NTM
Small Cap Independent Producers								
Range Resources	RRC	CB	58.58		-	14.5	15.5	13.5
Peyto Exploration and Development Corp	PEYUF		15.12		0.37	109.9	12.5	8.4
Birchcliff Energy Ltd.	BIREF	CB	5.80		-	23.7	17.6	7.9
PDC Energy	PETD		32.21		-	8.1	8.1	7.1
Denbury Resources Inc.	DNR		18.00		-	14.1	8.0	5.7
Berry Petroleum Company	BRY		44.08		-	11.8	7.5	5.5
Cimarex Energy Company	XEC	CB	65.01		-	8.2	8.3	5.2
Whiting Petroleum Corporation	WLL	B	54.23		-	9.8	7.0	4.7
	<i>Median</i>					13.0	8.2	6.4
Top Line Cash Payers								
Cross Timbers Royalty Trust	CRT		39.84	78	0.96	16.3	16.6	15.0
Sabine Royalty Trust	SBR		57.04	100	1.00	8.2	17.0	15.0
Permian Basin RT	PBT		21.11	32	0.92	9.7	12.7	13.4
Dorchester Minerals, L.P.	DMLP	CB	23.70	77	1.00	6.1	13.7	12.0
Freehold Royalties Ltd.	FRHLF		18.23	71	0.74	5.9	9.2	8.0
	<i>Median</i>					8.2	13.7	13.4
Bottom Line Cash Payers								
San Juan Basin Royalty Trust	SJT	CB	16.73		0.64	8.8	19.0	15.1
Hugoton RoyaltyTrust	HGT		12.57		0.83	12.8	20.4	15.1
Linn Energy, LLC	LINE		38.51		0.91	15.7	9.9	11.3
Vanguard Natural Resources, LLC	VNR		27.70		0.85	14.0	9.1	9.7
Mesa RoyaltyTrust	MTR		33.00		0.88	7.5	10.8	8.8
Legacy Reserves L.P.	LGCY		28.77		0.65	11.9	8.9	8.6
Enduro Royalty Trust (40%)	NDRO		20.05		0.63	5.2	7.5	7.2
Enerplus Corporation	ERF	CB	18.09		0.62	6.5	7.5	5.7
	<i>Median</i>					10.3	9.5	9.3
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, 2013; 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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