

Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

August 20, 2001

Smart Money Buying Natural Gas

Summary and Recommendation

Devon Energy's offer to acquire Mitchell Energy is a favorable omen for natural gas investors. If a master of timing like Larry Nichols of Devon is making a new commitment now, might not others benefit from following the example? Each of our recommendations offers timely participation in natural gas, direct and indirect. Strong Buys **Burlington Resources Inc. (BR)** and **USX-Marathon Group (MRO)** are producers as are Buys **PanCanadian Petroleum Ltd. (PCP.TO)**, **Energy Partners, Ltd. (EPL)** and **PetroChina (PTR)** (see Tables L-1, L-2, S-1, S-2). Our power Buys, **American Electric Power (AEP)**, and **Exelon Corporation (EXC)** will make money with their old coal and nuclear facilities as power prices move up with natural gas. Conversely our Sell recommendation, **Calpine Corporation (CPN)**, expecting to be the largest buyer of natural gas in a few years, may see a cost squeeze.

Masters of Vision and Timing

John Nichols, Larry's father was a pioneer in developing San Juan Basin natural gas raising some of his capital in an early version of drilling funds fifty years ago. As chief executive officer of Devon Energy, Larry Nichols has made a string of well-timed acquisitions that make Devon part of a handful of largest North American independent producers. Years ago, Devon pounced on Alta Energy when the little producer was buckling under a heavy debt load as oil prices took a dive. Devon picked up Northstar Energy when the Canadian company's stock was suffering after a poorly timed acquisition of Morrison Petroleums. Perhaps the most advantageous buy was PennzEnergy when the stock collapsed as investors were still incredulous that management of the target company had turned down an offer four times what Devon's stock implied. The next deal, Santa Fe Snyder, was less a distress situation than the case of savvy sellers who were happy to join up with a winning buyer.

The market took no time to make up its mind that Devon's proposed acquisition of Mitchell Energy would prove to be well timed also. Mitchell's stock price jumped almost a third, or more than \$700 million on the Devon offer. Normally one would expect the market cap of the buyer to go down by the same amount, as a cynic would say that no new value is created in a paper shuffle. By not declining, Devon stock price implies that the buyer created \$700 million of value overnight.

Enough Price Decline Already

By acting now, or jumping the gun, some would say, Devon decided that the natural gas price decline has gone far enough. Sure there seems to be ample inventory to meet

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August 20, 2001

winter demands, normal demand is slow in the fall when there is neither heating load nor air conditioning load and economic activity is weak. At the same time long-term demand for natural gas is strong and supply is going to be hard pressed to keep up.

Traders also seem to sense that a turn in price could be near. Commodity prices advanced sharply in midweek before falling back partly.

Our weekly calculations of present value turned up last week after having leveled out previously (see Chart). The estimates take account of the latest futures prices, inflation rates, interest rates and operating results in projections detailed weekly in Meter Reader Tables, a stand-alone supplement or appendix to Meter Reader. The detailed weekly calculations are done for just five stocks. For all other stocks the process is briefer.

Use Ebitda to Estimate Present Value for Calculating a McDep Ratio

We believe one must consider many stocks in order to choose a few to invest in confidently. Specializing in energy we aim to give perspective on many stocks at the same time we narrow our choices to specific recommendations. Our recommendations need not be an investor's only choices, but we believe our recommendations are carefully analyzed choices. To use well the McDep Ratio, our tool for knowing how one stock compares with other stocks, one needs to know what is in the McDep Ratio and what is not.

For each stock we make estimates for the next twelve months (NTM) taking account of results for the most recent quarter. We recently did the analysis separately for Devon and for Mitchell and combined the two for the NTM (see table on page 8). We tend to hold volumes steady on a daily basis for entities reinvesting cash flow, but will also use management guidance. The impact of volume trends is greater beyond NTM. Our pricing is taken from the futures market. Continually changing price expectations is the main reason for making projections by quarter. Our primary goal is to estimate Ebitda. The "t" or tax in the result is usually limited to 35% of Ebt for valuation comparability.

For all but five small cap stocks, we assess present value, the denominator of the McDep Ratio, as a multiple of Ebitda. For Devon, including Mitchell, the new assessment is 6.0 times, the same as for Spinnaker Exploration and Swift Energy, for example, two small cap producers just added to coverage. Experienced investors will recognize that Devon has now become large enough that there probably is little relative hidden value not included in the 6.0 multiple. There might be considerable hidden value in Spinnaker and Swift that we are underestimating. Other producer stocks updated or added recently include BP, Chevron (with Texaco), Devon, Petro-Canada, Abraxas Petroleum, and Quicksilver Resources.

Kurt H. Wulff, CFA

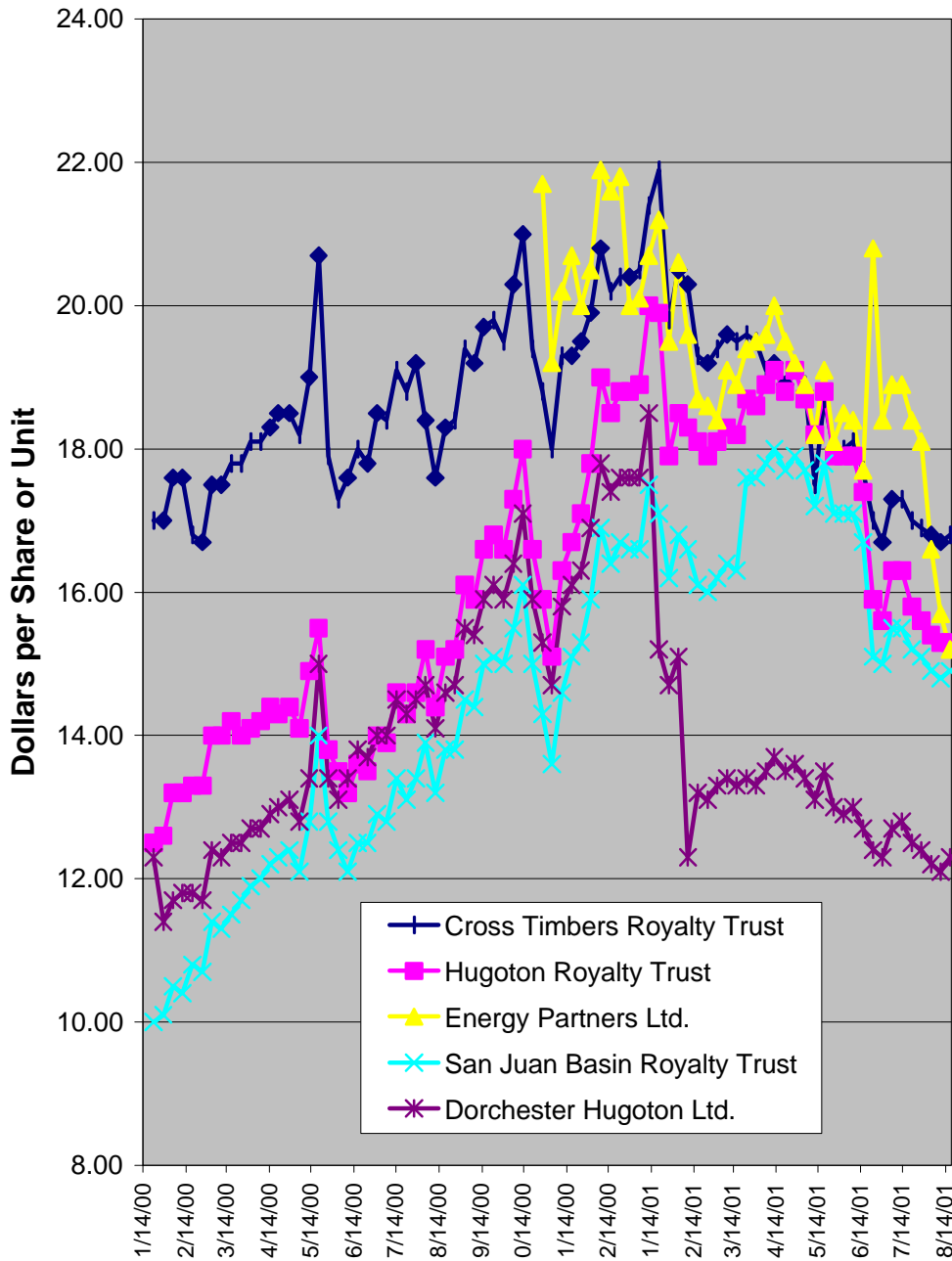
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August 20, 2001

Present Value of Small Cap Natural Gas Producers



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Table L-1
Mega Cap and Large Cap Energy Companies
Rank by McDep Ratio: Market Cap and Debt to Present Value

			<i>Price</i> (\$/sh)		<i>Market</i> <i>Cap</i> (\$mm)	<i>Net</i> <i>Present</i> <i>Value</i> (\$/sh)	<i>Debt/</i> <i>Present</i> <i>Value</i>	<i>McDep</i> <i>Ratio</i>
	<i>Symbol/</i> <i>Rating</i>	<i>17-Aug</i> <i>2001</i>	<i>Shares</i> <i>(mm)</i>					
Mega Cap								
Exxon Mobil Corporation	XOM		7,020		284,000	37.10	0.09	1.08
Chevron (incl. Texaco)	CHV		1,064		97,900	84.00	0.17	1.08
BP PLC	BP		3,744		194,000	48.40	0.15	1.06
TOTAL Fina Elf S.A.	TOT		1,400		102,000	72.00	0.16	1.01
Royal Dutch/Shell	RD		3,580		202,000	60.80	0.09	0.93
	<i>Total or Median</i>				<i>880,000</i>		<i>0.15</i>	<i>1.06</i>
Power								
Calpine Corporation	CPN 4	29.28	318		9,300	9.90	0.69	1.61
Enron Corp.	ENE	36.67	891		32,700	15.00	0.69	1.45
Dynegy Inc.	DYN	41.01	338		13,900	20.60	0.56	1.44
Duke Energy Corporation	DUK	38.15	779		29,700	19.90	0.62	1.35
Mirant Corporation	MIR	28.00	353		9,900	12.70	0.73	1.33
Williams Companies	WMB	31.91	485		15,500	16.60	0.69	1.28
AES Corporation	AES	34.07	538		18,300	17.40	0.71	1.28
American Electric Power Co. Inc.	AEP 2	45.01	322		14,500	20.10	0.78	1.27
El Paso Corporation	EPG	47.39	521		24,700	30.00	0.57	1.25
Southern Company	SO	22.87	683		15,600	16.90	0.54	1.16
Exelon Corporation	EXC 2	54.91	324		17,800	55.30	0.51	1.00
	<i>Total or Median</i>				<i>202,000</i>		<i>0.69</i>	<i>1.28</i>
Natural Gas and Oil								
Anadarko Petroleum Corp.	APC	58.25	263		15,300	66.30	0.24	0.91
Occidental Petroleum	OXY	28.05	370		10,400	35.60	0.46	0.89
Phillips (incl. Tosco)	P	58.02	383		22,200	75.90	0.31	0.84
Burlington Resources, Inc	BR 1	42.53	215		9,100	54.90	0.17	0.81
ENI S.p.A.	E	64.30	800		51,500	91.90	0.10	0.73
Conoco Inc.	COC.B	29.38	623		18,300	48.00	0.21	0.69
	<i>Total or Median</i>				<i>127,000</i>		<i>0.22</i>	<i>0.82</i>
Service								
Baker Hughes Inc.	BHI	34.75	338		11,700	24.50	0.13	1.36
Schlumberger Ltd.	SLB	52.13	581		30,300	37.70	0.14	1.33
Halliburton Company	HAL	31.92	430		13,700	27.20	0.13	1.15

Buy/Sell rating after symbol: 1 - Strong Buy, 2 - Buy, 4 - Sell

McDep Ratio = Market cap and Debt to present value of oil and gas and other businesses

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Table L-2

Mega Cap and Large Cap Energy Companies

Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

	Symbol	Price (\$/sh) 17-Aug 2001	EV/ Sales 2001E	EV/ Ebitda NTM	P/E NTM	Dividend or Distribution NTM (%)	PV/ Ebitda NTM
Mega Cap							
	XOM	40.47	1.4	7.6	15	2.2	7.0
	CHV	92.01	1.2	7.6	16	2.8	7.0
	BP	51.70	1.3	7.4	15	2.6	7.0
	TOT	72.93	1.1	7.1	17	1.5	7.0
	RD	56.31	1.4	6.5	14	2.5	7.0
	<i>Median</i>		<i>1.3</i>	<i>7.4</i>	<i>15</i>	<i>2.5</i>	<i>7.0</i>
Power							
	ENE	36.67	0.3	14.5	19	1.4	10.0
	DYN	41.01	0.3	13.0	20	0.7	9.0
	CPN 4	29.28	2.3	11.3	16	-	7.0
	DUK	38.15	0.9	10.8	15	2.9	8.0
	MIR	28.00	0.6	10.6	13	-	8.0
	WMB	31.91	3.3	10.3	14	1.9	8.0
	AES	34.07	3.6	10.2	16	-	8.0
	AEP 2	45.01	0.7	8.9	12	5.3	7.0
	EPG	47.39	0.6	8.7	14	1.8	7.0
	SO	22.87	2.7	8.1	14	5.9	7.0
	EXC 2	54.91	2.4	7.0	12	3.1	7.0
	<i>Median</i>		<i>0.9</i>	<i>10.3</i>	<i>14</i>	<i>1.8</i>	<i>8.0</i>
Natural Gas and Oil							
	BR 1	42.53	4.5	7.3	32	1.3	9.0
	P	58.02	0.8	5.9	10	2.5	7.0
	APC	58.25	2.4	5.4	10	0.3	6.0
	OXY	28.05	1.3	5.3	8	3.6	6.0
	COC.B	29.38	0.6	4.2	8	2.6	6.0
	E	64.30	1.1	3.6	6	2.5	5.0
	<i>Median</i>		<i>1.2</i>	<i>5.4</i>	<i>9</i>	<i>2.5</i>	<i>6.0</i>
Service							
	BHI	34.75	2.2	10.9	24	1.3	8.0
	SLB	52.13	2.7	9.3	26	1.4	7.0
	HAL	31.92	1.1	9.2	22	1.6	8.0

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended March 31, 2002; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Table S-1
Mid Cap and Small Cap Energy Companies
Rank by McDep Ratio: Market Cap and Debt to Present Value

	<i>Symbol/ Rating</i>	<i>Price (\$/sh) 17-Aug 2001</i>	<i>Shares (mm)</i>	<i>Market Cap (\$mm)</i>	<i>Net Present Value (\$/sh)</i>	<i>Debt/ Present Value</i>	<i>McDep Ratio</i>	
Power								
Consol Energy Inc.	CNX	26.30	79	2,100	19.70	0.65	1.12	
Sempra Energy	SRE	26.37	203	5,400	23.10	0.65	1.05	
CMS Energy Corporation	CMS	24.19	128	3,100	19.80	0.80	1.04	
Constellation Energy Group	CEG	30.04	152	4,600	37.10	0.45	0.90	
	<i>Total or Median</i>			<i>15,200</i>		<i>0.65</i>	<i>1.05</i>	
Natural Gas and Oil								
Triton Energy Limited	OIL	44.98	59	2,700	24.50	0.24	1.64	
TEPPCO Partners, L.P.	TPP	32.00	38	1,220	13.20	0.65	1.50	
Valero Energy Corp.(with UDS)	VLO	35.84	110	3,900	30.80	0.63	1.06	
Ocean Energy, Inc.	OEI	19.72	177	3,500	21.90	0.27	0.93	
Devon Energy Corp (incl MND)	DVN	52.00	165	8,600	59.30	0.29	0.91	
Marathon Oil Corporation	MRO	1	30.57	310	9,500	42.60	0.26	0.79
Unocal Corporation	UCL	36.45	256	9,300	51.90	0.27	0.78	
Petro-Canada	PCZ	24.93	267	6,700	33.00	0.08	0.78	
Norsk Hydro ASA (49%)	NHY	42.85	128	5,500	61.60	0.16	0.74	
PanCanadian Petroleum (US\$)	PCP.TO	2	26.95	262	7,060	37.50	0.06	0.74
PetroChina Company Ltd (10%)	PTR	2	19.95	176	3,500	32.50	0.15	0.67
	<i>Total or Median</i>			<i>61,500</i>		<i>0.26</i>	<i>0.79</i>	
Small Cap								
Quicksilver Resources Inc.	KWK	18.00	19.3	350	10.80	0.59	1.27	
Dorchester Hugoton, Ltd.*	DHULZ	14.40	10.7	155	12.30	-	1.17	
Spinnaker Exploration Company	SKE	43.01	28.4	1,220	37.00	-	1.16	
Cross Timbers Royalty Tr*	CRT	19.27	6.0	116	16.80	-	1.15	
Swift Energy Company	SFY	29.99	25.7	770	27.70	0.24	1.06	
Encore Acquisition Corporation	EAC	14.90	30.0	450	16.40	0.15	0.92	
San Juan Basin Royalty Tr*	SJT	13.25	46.6	620	14.90	-	0.89	
Penn Virginia Corporation	PVA	37.91	8.8	330	44.20	0.00	0.86	
Hugoton RoyaltyTrust*	HGT	13.11	40.0	520	15.30	-	0.86	
Energy Partners Ltd.*	EPL	2	9.95	27.0	270	15.20	0.08	0.68
	<i>Total or Median</i>			<i>4,800</i>		<i>0.00</i>	<i>0.99</i>	
Micro Cap								
Abraxas Petroleum Corporation	ABP	3.25	23.6	77	1.70	0.89	1.11	
Purcell Energy, Ltd. (US\$)	PEL.TO	2.46	26.0	64	3.70	0.07	0.70	

Buy/Sell rating after symbol: 1 - Strong Buy, 2 - Buy

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* For small cap stocks marked with asterisk, estimated present value recalculated weekly.

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Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

	Symbol/ Rating	Price (\$/sh) 17-Aug 2001	EV/ Sales 2001E	EV/ Ebitda NTM	P/E NTM	Dividend or Distribution NTM (%)	PV/ Ebitda NTM	
Power								
Consol Energy Inc.	CNX	26.30	2.1	7.8	9	4.3	7.0	
Sempra Energy	SRE	26.37	1.2	7.4	10	3.8	7.0	
CMS Energy Corporation	CMS	24.19	0.9	7.3	9	6.0	7.0	
Constellation Energy Group	CEG	30.04	1.8	6.3	9	1.6	7.0	
	<i>Median</i>		<i>1.5</i>	<i>7.3</i>	<i>9</i>	<i>4.0</i>	<i>7.0</i>	
Natural Gas and Oil								
TEPPCO Partners, L.P.	TPP	32.00	0.7	12.0	16	6.6	8.0	
Triton Energy Limited	OIL	44.98	6.3	9.8	24	-	6.0	
Valero Energy Corp.(with UDS)	VLO	35.84	0.3	6.4	5	0.9	6.0	
Ocean Energy, Inc.	OEI	19.72	3.5	5.6	12	0.8	6.0	
Devon Energy Corp (incl MND)	DVN	52.00	3.0	5.5	13	0.4	6.0	
Unocal Corporation	UCL	36.45	1.7	4.7	13	2.2	6.0	
Petro-Canada	PCZ	24.93	1.3	4.7	10	1.1	6.0	
PanCanadian Petroleum (US\$)	PCP.TO	2	26.95	1.1	4.1	7	1.0	5.5
Marathon Oil Corporation	MRO	1	30.57	0.4	4.0	7	3.0	5.0
Norsk Hydro ASA (49%)	NHY		42.85	0.8	3.7	9	2.4	5.0
PetroChina Company Ltd (10%)	PTR	2	19.95	1.4	2.7	5	8.6	4.0
	<i>Median</i>		<i>1.3</i>	<i>4.7</i>	<i>10</i>	<i>1.1</i>	<i>6.0</i>	
Small Cap								
Quicksilver Resources Inc.	KWK		18.00	5.1	11.5	-	9.0	
Cross Timbers Royalty Tr*	CRT		19.27	6.9	11.0	12	8.6	9.5
Dorchester Hugoton, Ltd.*	DHULZ		14.40	7.3	10.2	12	7.5	8.7
San Juan Basin Royalty Tr*	SJT		13.25	6.1	7.7	10	9.6	8.7
Hugoton RoyaltyTrust*	HGT		13.11	5.1	7.4	10	9.9	8.7
Spinnaker Exploration Company	SKE		43.01	6.1	7.0	20	-	6.0
Swift Energy Company	SFY		29.99	4.8	6.4	15	-	6.0
Encore Acquisition Corporation	EAC		14.90	3.7	5.5	13	-	6.0
Penn Virginia Corporation	PVA		37.91	3.7	5.2	11	2.4	6.0
Energy Partners Ltd.*	EPL	2	9.95	2.0	3.7	29	-	5.4
	<i>Median</i>			<i>5.1</i>	<i>7.2</i>	<i>12</i>	<i>1.2</i>	<i>7.3</i>
Micro Cap								
Abraxas Petroleum Corporation	ABP		3.25	5.2	7.8	-	7.0	
Purcell Energy, Ltd. (US\$)	PEL.TO		2.46	3.2	4.2	14	-	6.0

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended June 30, 2002; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

* For small cap stocks marked with asterisk, estimated present value recalculated weekly.

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Devon Energy Next Twelve Months Operating and Financial Estimates (including Mitchell NTM)

	Q1	Q2	Q3E	Q4E	Year	Q1E	Q2E	Next Twelve Months
	3/31/01	6/30/01	9/30/01	12/31/01	2001E	3/31/02	6/30/02	6/30/02
Volume								
Natural Gas (mmcf)								-
U.S.	1,052	997	1,400	1,400	1,214	1,400	1,400	1,400
Canada	169	170	170	170	170	170	170	170
Overseas	21	25	25	25	24	25	25	25
Total	1,243	1,192	1,595	1,595	1,408	1,595	1,595	1,595
Days	90	91	92	92	365	90	91	365
Oil (mbd)	131	128	133	133	131	133	133	133
Total gas & oil (bcf)	182	178	220	220	801	216	218	874
Price								
Natural gas (\$/mcf)								-
Henry Hub (\$/mmbtu)	6.31	4.36	3.17	3.59	4.36	3.88	3.63	3.57
U.S.	6.79	4.27	3.17	3.59	4.29	3.88	3.63	3.57
Canada	5.21	3.36	2.67	3.09	3.57	3.38	3.13	3.07
Overseas	1.32	1.45	1.45	1.45	1.42	1.45	1.45	1.45
Total	6.48	4.08	3.09	3.50	4.16	3.79	3.54	3.48
Oil (\$/bbl)								-
WTI Cushing	28.81	27.90	26.77	25.59	27.27	25.17	24.58	25.53
Worldwide	24.18	23.11	22.38	21.20	22.69	20.78	20.19	21.14
Total gas & oil (\$/mcf)	5.53	3.99	4.67	4.87	4.81	5.07	4.86	4.87
Revenue (\$mm)								
Natural Gas								
U.S.	643	387	409	462	1,901	489	463	1,823
Canada	79	52	42	48	221	52	48	190
Overseas	3	3	3	3	13	3	3	13
Total	725	443	454	514	2,135	544	514	2,027
Oil	284	268	274	260	1,087	249	245	1,028
Other	14	15	300	300	629	300	300	1,200
Total	1,023	726	1,028	1,074	3,851	1,094	1,059	4,255
Expense								
Natural Gas and Oil	207	188	204	211	810	213	209	837
Other	38	14	272	272	596	272	272	1,088
Total	245	202	476	483	1,406	485	481	1,925
Ebitda (\$mm)								
Natural Gas and Oil	802	523	524	564	2,413	580	551	2,218
Other	(24)	1	28	28	33	28	28	112
Total Ebitda	778	524	552	592	2,446	608	579	2,330
Exploration			2	2	4	2	2	8
Deprec., Deplet., & Amort.	193	193	241	241	868	241	241	964
Interest	35	34	71	71	211	71	71	284
Ebt	550	297	238	278	1,363	294	265	1,074
Income tax	193	104	83	97	477	103	93	376
Net Income (\$mm)	358	193	155	180	886	191	172	698
Per share (\$)	2.65	1.43	0.94	1.09	6.11	1.16	1.04	4.23
Shares (millions)	135	135	165	165	145	165	165	165
Ebitda margin	76%	72%	54%	55%	64%	56%	55%	55%
Tax rate	35%	35%	35%	35%	35%	35%	35%	35%

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