

Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

May 14, 2001

It's the Market, Stupid!

Summary and Recommendation

To paraphrase James Carville, electricity in California is going up because of market forces, not because of manipulation by energy companies or oil producing countries. Apparently the state paid a record \$1900 a megawatt hour at a peak during the past week (*The Bakersfield Californian*, May 11, 2001). That is equivalent to some 40 times the current national wellhead price for natural gas. California blackouts in 2001 are the gasoline lines of 1973 as an indicator of a readjustment underway of the whole energy pricing structure. Our Strong Buy recommendations **USX-Marathon Group** and **Energy Partners, Ltd. (EPL)**, and our Buy recommendation **American Electric Power**, are well positioned to make money for investors while delivering a valuable product for the economy.

Politics Poisons the Picture

Focus on understanding the market, we tell ourselves. Do not get emotionally distracted by false accusations from demagogues.

Nonetheless we cannot help but admit that widespread addiction to California Whine gets us riled up. Where were price controls and threats of a windfall profits tax when California technology companies sold their stock to the public at high prices? Why should the energy industry be singled out to subsidize a malingering state government?

Predictably, fewer electricity suppliers are willing to sell to a deadbeat buyer. Moreover what retiree will buy bonds to be issued by a state that cheated retirees out of their dividends from its largest electric utilities?

Through it all Californians keep a sense of humor and the opposition party appears muted in its criticism of the governor. As a possible explanation, *The Bakersfield Californian* quotes Woodrow Wilson, "Never attempt to murder a man who is committing suicide."

Williams Outbids Shell to Buy Barrett

Life moves on as one of the Large Cap Power companies in our coverage outbid one of the Mega Cap Energy companies this past week to buy a Mid Cap company concentrated on natural gas. Current McDep Ratios validate the logic of the transaction. **Williams Companies (WMB)**, the buyer, is at 1.44, **Royal Dutch/Shell (RD)**, the outbid initiator, is at 0.97 and **Barrett Resources**, the seller, is at 1.26. When high McDep Ratio companies buy lower McDep Ratio companies there is value enhancement to the buyer.

Analyses are prepared from original sources and data believed to be reliable, but no representation is made as to their accuracy or completeness. Independent energy investment research by Kurt Wulff is accessible at <http://www.mcdep.com>. Owning shares in about 16 energy stocks, neither Mr. Wulff nor his spouse act contrary to a buy or sell rating. Mr. Wulff is not paid by covered companies.

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Value-enhancing acquisitions tend to solidify some of the extra favorable recognition by investors enjoyed by higher McDep Ratio companies.

The acquisition would have been a stretch for Royal Dutch. The argument would have had to be that there was enough hidden value in Barrett to justify the McDep Ratio mismatch. Even more telling, Royal Dutch could not compete efficiently with Williams, because RD's McDep Ratio is lower than WMB's.

Logical targets remain for Mega Cap buyers. At the same time, Large Cap Power companies will have an easy time outbidding Mega Cap Energy companies. The fact that a power company outbid RD/Shell fits with the thesis that electricity is going to make natural gas more valuable. Power companies should know their market and the future need for energy to supply all those generators being built.

EPL Reports Better-Than-Expected Earnings

Selling natural gas on a monthly index basis netted more revenue than we had estimated using daily pricing. Volumes were close to expectations as the company produced 5% more volume in the first quarter of 2001 compared to the fourth quarter of 2000. Meanwhile insurance costs will be higher than expected in the future. Drilling and completion costs are also rising sharply implying that EPL must be sure to pick its targets carefully.

Management expects to announce soon an agreement with a major oil company to develop another choice old property in Louisiana. The company is in a good position to be awarded a favorable contract. In the wake of acquisitions and downsizing of past leaders in New Orleans, EPL apparently is the largest publicly traded exploration and production company in the Mardi Gras city today.

Weekly Changes Somewhat Negative

A 5% decline in next twelve months (NTM) natural gas price contributed to a median 5% decline in NTM cash flow for five small cap stocks where we update estimates weekly. After four years we tie gas price to oil that was unchanged weekly and to inflation that was up weekly. We discount future cash flow by a rate tied to bond yields that were higher at the end of the week. All that translates to present value that declined a median 3%. The stock market went in the opposite direction with price up a median 5% and McDep Ratios up a median 3% on the week. As a result there is less unrecognized attraction in small cap energy stocks this week than last week. Yet lower McDep Ratio stocks generally have relative appeal regardless of the industry outlook.

Kurt H. Wulff, CFA

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Rank by McDep Ratio	Symbol/ Rating	Price (\$/sh)		Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio	
		11-May 2001	Shares (mm)					
Mega Cap								
	Exxon Mobil Corporation	XOM	87.64	3,520	309,000	72.10	0.16	1.18
	BP PLC	BP	51.94	3,720	193,000	48.90	0.17	1.05
	TOTAL Fina Elf S.A.	TOT	73.35	1,400	103,000	72.00	0.16	1.02
	Royal Dutch/Shell	RD	59.00	3,580	211,000	60.80	0.09	0.97
	<i>Total or Median</i>				816,000		0.16	1.03
Large Cap Natural Gas and Oil								
	Chevron (incl. Texaco)	CHV	94.02	1,060	99,700	103.40	0.15	0.92
	Burlington Resources, Inc	BR	45.96	216	9,900	60.50	0.17	0.80
	ENI S.p.A.	E	65.30	800	52,300	91.90	0.10	0.74
	Anadarko Petroleum Corp.	APC	62.49	249	15,500	90.90	0.17	0.74
	Conoco Inc.	COC.B	30.36	623	18,900	48.00	0.21	0.71
	Phillips (incl. Tosco)	P	59.51	379	22,600	102.10	0.27	0.70
	<i>Total or Median</i>				219,000		0.17	0.74
Large Cap Power								
	Enron Corp.	ENE	58.20	795	46,300	14.50	0.70	1.90
	Mirant Corporation	MIR	42.11	353	14,900	9.70	0.78	1.74
	Calpine Corporation	CPN	52.55	313	16,400	21.80	0.47	1.74
	Duke Energy Corporation	DUK	46.05	752	34,600	20.90	0.62	1.46
	Williams Companies	WMB	40.23	485	19,500	16.60	0.69	1.44
	El Paso Corporation	EPG	65.88	521	34,300	40.00	0.50	1.32
	American Electric Power Co. Inc.	AEP 2	48.18	324	15,600	25.90	0.73	1.23
	Southern Company	SO	22.60	683	15,400	16.90	0.54	1.15
	<i>Total or Median</i>				197,000		0.66	1.45
Mid Cap								
	Barrett Resources Corporation	BRR	71.08	34	2,400	53.80	0.21	1.26
	PanCanadian Pete Ltd. (15%)	PCP.TO	45.25	38	1,700	49.10	0.07	0.93
	Occidental Petroleum	OXY	29.50	370	10,900	35.60	0.46	0.91
	PetroChina Company Ltd (10%)	PTR	21.95	176	3,900	28.40	0.24	0.83
	Valero Energy Corp.	VLO	50.00	64	3,200	65.00	0.25	0.83
	Unocal Corporation	UCL	36.91	256	9,500	51.90	0.27	0.79
	USX-Marathon Group	MRO 1	31.81	360	11,500	47.00	0.30	0.77
	Petro-Canada	PCZ	26.39	272	7,200	38.70	0.08	0.71
	Devon Energy Corporation	DVN	56.69	135	7,700	89.70	0.15	0.69
	Norsk Hydro ASA	NHY	41.11	262	10,800	65.90	0.15	0.68
	<i>Total or Median</i>				64,700		0.22	0.81
Small Cap								
	Cross Timbers Royalty Tr*	CRT	22.97	6.0	138	17.50	-	1.31
	Dorchester Hugoton, Ltd.*	DHULZ	13.82	10.7	148	13.10	-	1.05
	San Juan Basin Royalty Tr*	SJT	17.94	46.6	840	17.20	-	1.04
	Encore Acquisition Corporation	EAC	15.05	30.0	450	16.70	0.12	0.91
	Hugoton RoyaltyTrust*	HGT	16.15	40.0	650	18.20	-	0.89
	Energy Partners Ltd.*	EPL 1	10.34	27.0	280	18.20	0.04	0.59
	<i>Total or Median</i>				2,510		-	0.98

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

McDep Ratio = Market cap and Debt to 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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Rank by EV/Ebitda		Symbol	Price	EV/	EV/	Dividend or		PV/ Ebitda	
			(\$/sh)	Sales	Ebitda	P/E	NTM		NTM
			11-May 2001	2001E	NTM	NTM	NTM (%)	NTM	
Mega Cap									
		Exxon Mobil Corporation	XOM	87.64	1.5	8.3	18	2.0	7.0
		BP PLC	BP	51.94	1.3	7.4	12	2.7	7.0
		TOTAL Fina Elf S.A.	TOT	73.35	1.1	7.1	17	1.5	7.0
		Royal Dutch/Shell	RD	59.00	1.4	6.8	15	2.4	7.0
		<i>Median</i>			1.4	7.2	16	2.2	7.0
Large Cap Natural Gas and Oil									
		Chevron (incl. Texaco)	CHV	94.02	1.1	5.5	11	2.8	6.0
		Burlington Resources, Inc	BR	45.96	3.3	4.8	9	1.2	6.0
		Anadarko Petroleum Corp.	APC	62.49	2.1	4.4	9	0.3	6.0
		Conoco Inc.	COC.B	30.36	0.6	4.2	8	2.5	6.0
		Phillips (incl. Tosco)	P	59.51	0.7	4.2	7	2.3	6.0
		ENI S.p.A.	E	65.30	1.2	3.7	7	2.5	5.0
		<i>Median</i>			1.1	4.3	9	2.4	6.0
Large Cap Power									
		Enron Corp.	ENE	58.20	0.4	19.0	33	0.9	10.0
		Calpine Corporation	CPN	52.55	4.6	17.4	29	-	10.0
		Mirant Corporation	MIR	42.11	0.8	13.9	22	-	8.0
		Duke Energy Corporation	DUK	46.05	1.0	11.7	18	2.4	8.0
		Williams Companies	WMB	40.23	3.7	11.5	18	1.5	8.0
		El Paso Corporation	EPG	65.88	0.8	10.6	20	1.3	8.0
		American Electric Power Co. Inc.	AEP 2	48.18	0.7	8.6	13	5.0	7.0
		Southern Company	SO	22.60	2.7	8.1	14	5.9	7.0
		<i>Median</i>			0.9	11.6	19	1.4	8.0
Mid Cap									
		Barrett Resources Corporation	BRR	71.08	5.4	7.5	16	-	6.0
		PanCanadian Pete Ltd. (15%)	PCP.TO	45.25	1.9	5.6	13	0.6	6.0
		Occidental Petroleum	OXY	29.50	1.3	5.4	8	3.4	6.0
		PetroChina Company Ltd (10%)	PTR	21.95	2.0	5.0	7	6.5	6.0
		Valero Energy Corp.	VLO	50.00	0.3	5.0	7	0.6	6.0
		Unocal Corporation	UCL	36.91	1.7	4.7	13	2.2	6.0
		USX-Marathon Group	MRO 1	31.81	0.4	4.6	6	2.9	6.0
		Petro-Canada	PCZ	26.39	1.1	4.2	10	1.0	6.0
		Devon Energy Corporation	DVN	56.69	2.9	3.8	8	0.4	5.5
		Norsk Hydro ASA	NHY	41.11	0.8	2.7	7	2.5	4.0
		<i>Median</i>			1.5	4.9	8	1.6	6.0
Small Cap									
		Cross Timbers Royalty Tr*	CRT	22.97	6.8	10.5	11	9.2	8.0
		San Juan Basin Royalty Tr*	SJT	17.94	6.5	8.0	11	9.2	7.7
		Dorchester Hugoton, Ltd.*	DHULZ	13.82	5.6	7.0	8	8.9	6.7
		Hugoton RoyaltyTrust*	HGT	16.15	5.0	6.8	9	10.9	7.7
		Encore Acquisition Corporation	EAC	15.05	4.0	5.5		-	6.0
		Energy Partners Ltd.*	EPL 1	10.34	1.6	2.5	9	-	4.3
		<i>Median</i>			5.3	6.9	9	9.0	7.2

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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