



Independent Stock Idea

January 28, 2011

rating: buy
s&p 500: 1300

Canadian Oil Sands Limited (COSWF) Ethical Oil for Generations

<i>Symbol</i>	COSWF	<i>Ebitda Next Twelve Months ending 12/31/11 (US\$m)</i>	1,940
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	-5
<i>Price (US\$/share)</i>	26.77	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	1/26/11	<i>Adjusted Reserves/Production NTM</i>	29.2
<i>Shares (mm)</i>	484	<i>EV/Ebitda</i>	7.5
<i>Market Capitalization (US\$m)</i>	13,000	<i>PV/Ebitda</i>	13.7
<i>Debt (US\$m)</i>	1,500	<i>Probable Reserves (%)</i>	48
<i>Enterprise Value (EV) (US\$m)</i>	14,500	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	45.11
<i>Present Value (PV) (US\$m)</i>	26,700	<i>Present Value Proven and Probable Reserves(US\$/boe)</i>	31.45
<i>Net Present Value (US\$/share)</i>	52	<i>Natural Gas and Oil Ebitda (\$/boe)</i>	51
<i>Debt/Present Value</i>	0.06	<i>Earnings Next Twelve Months (US\$/share)</i>	2.00
<i>McDep Ratio - EV/PV</i>	0.54	<i>Price/Earnings Next Twelve Months</i>	13
<i>Dividend Yield (%/year)</i>	3.0	<i>Dividend Next Twelve Months (US\$/share)</i>	0.80
Note: Estimated cash flow and earnings tied to one-year futures prices for oil.			
Estimated present value presumes a long-term price for oil of US\$100 a barrel and natural gas, \$8 a million btu.			
For historical analysis of COS since 2002 see www.mcdep.com/4cos.htm			

Summary and Recommendation

Buy-recommended **Canadian Oil Sands Limited (COSWF)** offers unlevered appreciation potential of 84% to a McDep Ratio of 1.0 where stock price would equal Net Present Value (NPV) of \$52 a share. On December 28, we raised NPV from \$38 a share on the basis of expecting a higher long-term oil price of \$100 a barrel, up from \$75. After the market close on January 27, management raised its guidance for 2011 cash flow as it reported results for 2010. Declaring a quarterly dividend of C\$0.20 a share as it had indicated earlier, management completed a transition from a high income paying trust to a lower, but surer payout policy pursued by strong financial corporations. Management estimates that cash flow of C\$2.72 a share, up from C\$2.59, would match the total of annual dividends and capital expenditures for 2011. At recent futures prices we estimate that the dividend could be increased to C\$0.50 a quarter in the second half of the year, also after covering capital expenditures (see table Next Twelve Months Dividend Estimates on page 3 derived from table Next Twelve Months Operating and Financial Estimates on page 4 and chart Syncrude Monthly Production on page 3). We expect management to apply the potential increase to a financial reserve and continue the dividend at C\$0.20 a quarter until 2012. The main appeal in COSWF is its concentration on long-life oil production that is becoming increasingly valuable as a consequence of political environmentalism among other driving forces.



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Current Markets Undervalue Long Life

A discounted cash flow calculation illustrates how value can be hidden in a long-life asset like COSWF (see table [Present Value of Future Cash Flow](#) on page 5). Projected cash flow at a constant price of oil before allowance for inflation is discounted at the rate of 7% a year, also before allowance for inflation. The return before inflation is higher than practically any corporation achieves on a long-term basis. The future is discounted even more heavily by investors as it would take a 14% a year discount rate to have NPV equal current stock price. The fortuitous outcome for long-term investors in quality assets is that the return is competitive in the early years and then after shorter life assets have expired, the future for the long life asset remains just as bright as ever. In other words, the widely applied discounted cash flow rationale undervalues long-term assets in a way that helps explain why long-term investors can profit by the pricing inefficiencies in a market dominated by traders with short-term time horizons.

Political Environmentalism Drives up Price

What started out as a movement that raised our sensitivity to the more subtle negative environmental consequences of economic activity seems, in many ways, to have degenerated into a political movement with an anti-business and especially anti-oil bias. Though the hypocrisy of the movement offends us, we are profiting from its consequences for oil price and the value of real assets. Oil sands have attracted disproportionate attention that we have commented on in the past. Fortunately, an independent author has analyzed the politics in great detail. The book is [Ethical Oil: The Case for Canada's Oil Sands](#) by Ezra Levant. It is available in traditional hard copy or as an online download from Amazon among others.

Political environmentalism is embodied at the highest level in the President of the United States. Last year's exaggerated hysteria over the BP oil spill has resulted in the near elimination of the Gulf of Mexico as a source of additional oil supply. The president would compound the pressure to increase global oil price by raising taxes on oil beyond already high levels. Mr. Obama increasingly looks like his predecessor Mr. Carter whose oil taxes and international stance contributed to a tripling of oil price in the last two years of his administration on top of the quadrupling that had already occurred in the decade. We don't need such increases as we think Canadian Oil Sands Limited is an attractive long-term investment at current or even lower oil price.

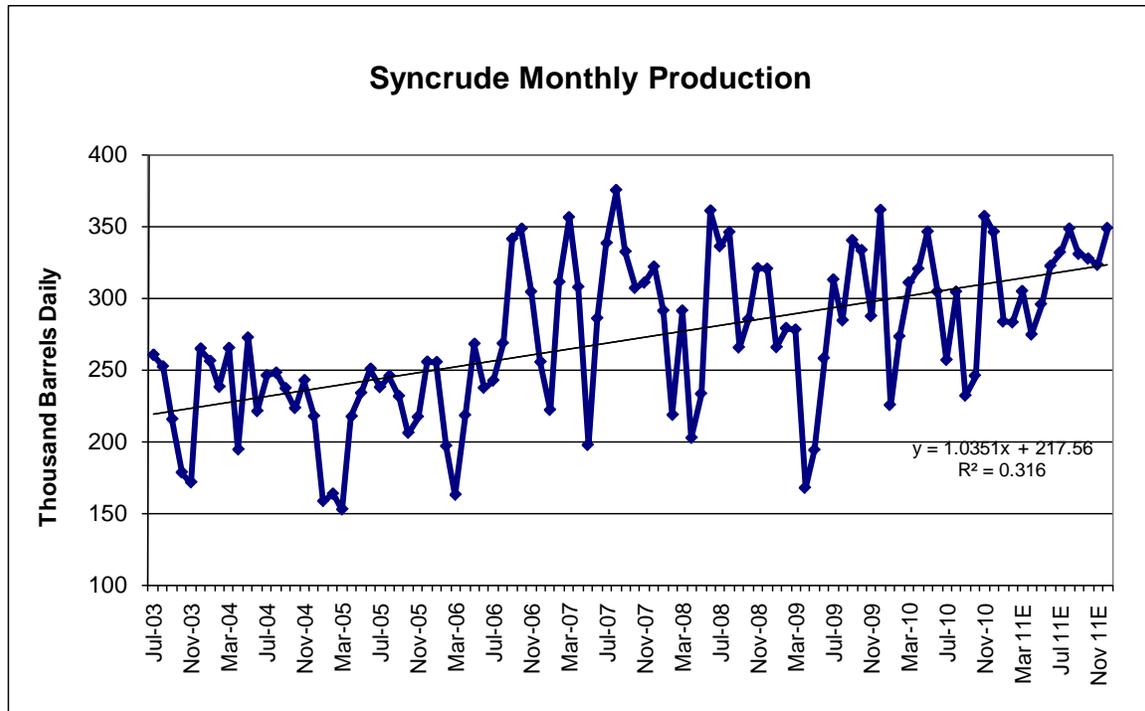
Kurt H. Wulff, CFA



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Canadian Oil Sands Trust									
Next Twelve Months Dividend Estimates									
(Canadian Dollars)									
									<i>Next</i>
	<i>Q4</i>	<i>Q3</i>	<i>Q4</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Twelve</i>
	<i>12/31/09</i>	<i>9/30/10</i>	<i>12/31/10</i>	<i>2010</i>	<i>3/31/11</i>	<i>6/30/11</i>	<i>9/30/11</i>	<i>12/31/11</i>	<i>Months</i>
									<i>12/31/11</i>
Ebitda	431	263	410	1,375	402	429	551	550	1,932
Interest	23	22	21	91	22	22	22	22	87
Current Income Tax					10	10	10	10	40
Cash Flow Before Reinvestment	408	241	389	1,284	370	397	519	518	1,805
Non-Production Expense	35	26	24	105	36	36	36	36	145
Capital Expenditures	101	137	163	506	232	232	232	232	927
Free Cash Flow	272	78	202	673	102	129	251	250	733
Per Share									
Cash Flow Before Reinvestment	0.84	0.50	0.80	2.65	0.77	0.82	1.07	1.07	3.73
Free Cash Flow	0.56	0.16	0.42	1.39	0.21	0.27	0.52	0.52	1.51
Dividend (C\$/share)	0.35	0.50	0.50	1.85	0.20	0.20	0.20	0.20	0.80





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Canadian Oil Sands Trust									
Next Twelve Months Operating and Financial Estimates									
(Canadian Dollars)									
									Next Twelve Months
	Q4 12/31/09	Q3 9/30/10	Q4 12/31/10	Year 2010	Q1E 3/31/11	Q2E 6/30/11	Q3E 9/30/11	Q4E 12/31/11	12/31/11
Volume									
Syncrude (mmb)	30.5	24.3	29.0	107.0	26.1	27.0	31.0	30.6	114.8
Syncrude (mbd)	331	264	316	293	290	297	337	333	314
Trust share (%)	36.0	36.5	36.4	36.6	36.7	36.7	36.7	36.7	36.7
Trust Oil (mmb)	10.97	8.88	10.56	39.2	9.60	9.93	11.38	11.25	42.2
Trust Oil (mbd)	119.3	96.5	114.7	107.3	106.7	109.2	123.7	122.3	115.5
Price									
WTI Cushing (US\$/bbl)	76.09	76.08	85.10	79.43	90.07	90.76	93.21	94.32	92.09
Currency (US\$/C\$)	0.95	0.96	0.99	0.97	1.00	1.00	1.00	1.00	1.00
WTI Cushing (C\$/bbl)	80.35	79.05	86.13	81.76	89.65	90.34	92.77	93.88	91.66
Differential	(1.68)	(1.11)	(2.16)	(1.22)	(1.50)	(1.50)	(1.50)	(1.50)	(1.38)
Trust Oil Price (C\$/bbl)	78.67	77.94	83.97	80.54	88.15	88.84	91.27	92.38	90.28
Henry Hub Nat Gas (US\$/mmbt)	4.16	4.38	3.80	4.40	4.40	4.62	4.73	4.96	4.68
Henry Hub Nat Gas (C\$/mmbt)	4.40	4.55	3.85	4.53	4.38	4.60	4.71	4.93	4.66
AECO Natural Gas (C\$/GJ)	4.33	3.44	3.45	3.88	3.93	4.13	4.23	4.43	4.18
Revenue (C\$m)	864	692	886	3,154	846	883	1,039	1,039	3,807
Expense (C\$m)									
Production	284	319	340	1,260	331	331	331	331	1,325
Purchased Energy	47	36	54	179	43	47	55	57	203
Crown Royalties	93	68	75	306	51	57	83	82	273
Insurance	3	5	1	11	3	3	3	3	10
Administration	6	1	6	23	7	7	7	7	26
Reclamation Spending	-	-	-	-	10	10	10	10	38
Total	433	429	476	1,779	444	454	488	490	1,875
Ebitda	431	263	410	1,375	402	429	551	550	1,932
Deprec., Deplet., & Amort.	312	95	88	380	100	100	100	100	400
Non-Production	35	26	24	105	36	36	36	36	145
Exchange on U.S. Debt	(23)	(30)	(35)						
Other	(13)	(20)	3						
Ebit	120	191	331	977	266	293	415	414	1,387
Interest	23	22	21	91	22	22	22	22	87
Ebt					244	271	393	392	1,300
Income Tax					63	70	102	102	338
Net Income (C\$m)	97	169	310	886	181	200	291	290	962
Shares (millions)	484	484	484	484	484	484	484	484	484
Earnings per share (C\$)	0.20	0.35	0.64	1.83	0.37	0.41	0.60	0.60	1.99
Ebitda Margin (E&P)	50%	38%	46%	44%	48%	49%	53%	53%	51%
Tax Rate					26%	26%	26%	26%	26%
Funds from Operations (\$mm)	373	215	365	1,266	344	371	493	492	1,700



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Present Value of Future Cash Flow												
Nymex Crude (US\$/b):		100		PV/unit (US\$):		52		Discount rate (%/yr):		7.0		
Canadian Dollar/\$US		1.00						Nymex Nat Gas (\$/mmbtu)		8.00		
Year	Volume		Price (US\$/bbl)	Revenue (C\$m)	Prod Cost (C\$/bbl)	Natural Gas (C\$/bbl)	NonOper (C\$/bbl)	Capital (C\$/bbl)	Royalty (C\$m)	Cash Flow (C\$m)	Disc Factor	Present Value (C\$m)
	Syncrude (mmb)	Trust (mmb)										
Total 2011 through 2060; years ending on 12/31												
		2339		233600					29500	93400	0.28	26000
2011	314	42.2	90.71	3825	31.42	4.82	1.75	25.42	273	878	0.97	849
2012	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.90	1706
2013	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.84	1595
2014	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.79	1490
2015	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.74	1393
2016	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.69	1302
2017	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.64	1217
2018	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.60	1137
2019	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.56	1063
2020	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.53	993
2021	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.49	928
2022	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.46	867
2023	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.43	811
2024	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.40	758
2025	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.37	708
2026	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.35	662
2027	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.33	618
2028	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.31	578
2029	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.29	540
2030	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.27	505
2031	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.25	472
2032	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.23	441
2033	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.22	412
2034	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.20	385
2035	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.19	360
2036	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.18	336
2037	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.17	314
2038	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.16	294
2039	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.15	275
2040	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.14	257
2041	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.13	240
2042	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.12	224
2043	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.11	209
2044	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.10	196
2045	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.10	183
2046	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.09	171
2047	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.08	160
2048	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.08	149
2049	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.07	140
2050	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.07	130
2051	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.06	122
2052	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.06	114
2053	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.06	106
2054	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.05	100
2055	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.05	93
2056	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.05	87
2057	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.04	81
2058	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.04	76
2059	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.04	71
2060	350	46.9	100.00	4688	26.00	8.00	2.00	11.00	596	1888	0.04	66

Please see disclosures on the final page.



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