

Rating: Buy  
S&P 500: 1466

## Encore Acquisition Company Nice to be Oily

<i>Symbol</i>	EAC	<i>Ebitda Next Twelve Months ending 6/30/08 (US\$m)</i>	509
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	15
<i>Price (\$/sh)</i>	27.78	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	8/1/07	<i>Adjusted Reserves/Production NTM</i>	15.5
<i>Shares (mm)</i>	54	<i>EV/Ebitda</i>	5.7
<i>Market Capitalization (\$mm)</i>	1,500	<i>PV/Ebitda</i>	8.5
<i>Debt (\$mm)</i>	1,400	<i>Undeveloped Reserves (%)</i>	30
<i>Enterprise Value (EV) (\$mm)</i>	2,900	<i>Natural Gas and Oil Ebitda (\$/boe)</i>	40.20
<i>Present Value (PV) (\$mm)</i>	4,320	<i>Present Value Proven Reserves(\$/boe)</i>	18.70
<i>Net Present Value (\$/share)</i>	54	<i>Present Value Proven Reserves(\$/mcf)</i>	3.10
<i>Debt/Present Value</i>	0.32	<i>Earnings Next Twelve Months (US\$/sh)</i>	1.99
<i>McDep Ratio - EV/PV</i>	0.67	<i>Price/Earnings Next Twelve Months</i>	14
<i>Dividend Yield (%/year)</i>	0.0	<i>Indicated Annual Dividend (US\$/sh)</i>	0.00

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.

Estimated present value presumes a long-term price for oil of US\$66 a barrel and natural gas, \$11 a million btu.

For historical research on Encore since 2003 see <http://www.mcdep.com/4eac.htm>

### Summary and Recommendation

Buy-recommended **Encore Acquisition (EAC)** offers unlevered appreciation potential of 49% to estimated net present value (NPV) of \$54 a share revised up from \$48 a share on May 29 when we raised long-term oil price to \$66 a barrel from \$60. Second quarter results reported on August 1 included higher than expected unlevered cash flow (Ebitda) driven by advancing production volume and a narrowing of the discount to benchmark oil price (see table Next Twelve Months Operating and Financial Estimates). The acquisition of oil properties and the divestiture of natural gas properties increases the concentration of NPV on oil production to 83% from 77% (see table Functional Cash Flow and Present Value). That will change again with the transfer of oil properties to a newly created Master Limited Partnership expected to be brought to market in the next few months. Nonetheless while presenting latest results, Chief Executive Jonny Brumley said, "It's Nice to be Oily". Pointing to more good quarters, we hope, long-term oil price appears to be in an uptrend despite volatility of short-term quotes (see chart Six-Year Commodity Price Meter). Up 7% on the day, EAC stock bounced to maintain positive momentum at 7% above its 200-day average.

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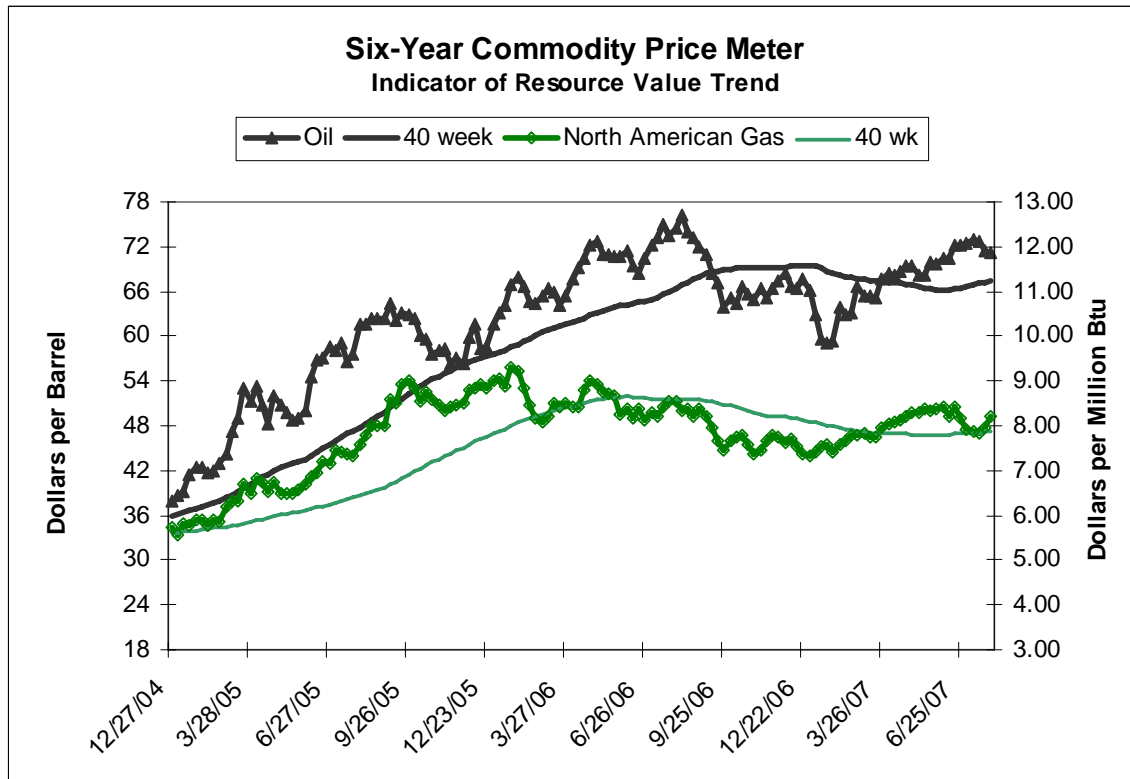
**Encore Acquisition Company**  
**Next Twelve Months Operating and Financial Estimates**

	<i>Q2</i>	<i>Q3</i>	<i>Year</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Year</i>	<i>Next</i>
	<i>6/30/06</i>	<i>9/30/06</i>	<i>2006</i>	<i>3/31/07</i>	<i>6/30/07</i>	<i>9/30/07</i>	<i>12/31/07</i>	<i>2007E</i>	<i>Twelve</i>
									<i>Months</i>
									<i>6/30/08</i>
<b>Volume</b>									
Natural Gas (mmcf)	65.7	59.5	<b>64.3</b>	67.9	76.1	46.0	46.0	<b>58.9</b>	<b>46.0</b>
Oil (mbd)	19.9	19.7	<b>20.10</b>	21.2	28.7	27.0	27.0	<b>25.99</b>	<b>27.00</b>
Total (mb)	2,809	2,728	<b>11,244</b>	2,924	3,766	3,189	3,189	<b>13,069</b>	<b>12,653</b>
Total (mbd)	30.9	29.7	<b>30.8</b>	32.5	41.4	34.7	34.7	<b>35.8</b>	<b>34.7</b>
<b>Price</b>									
Henry Hub (\$/mmbtu)	6.81	6.58	<b>7.23</b>	6.81	7.56	6.64	7.64	<b>7.16</b>	<b>7.83</b>
Differential (\$/mmbtu)	(0.01)	0.52	<b>0.70</b>	0.99	1.04	0.91	1.05	<b>0.98</b>	<b>1.08</b>
EAC (\$/mcf)	6.82	6.06	<b>6.54</b>	5.82	6.52	5.73	6.59	<b>6.18</b>	<b>6.75</b>
WTI Cushing (\$/bbl)	70.47	70.42	<b>66.05</b>	58.08	64.91	75.91	75.47	<b>68.59</b>	<b>74.50</b>
Differential	11.19	8.22	<b>11.11</b>	9.05	7.90	9.24	9.18	<b>8.22</b>	<b>9.06</b>
EAC (\$/bbl)	59.28	62.20	<b>54.95</b>	49.03	57.01	66.68	66.29	<b>60.37</b>	<b>65.45</b>
Total (\$/bbl)	52.77	53.56	<b>49.48</b>	44.12	51.53	59.54	60.37	<b>53.98</b>	<b>59.93</b>
<b>Revenue (\$mm)</b>									
Natural Gas	41	33	<b>153</b>	36	45	24	28	<b>133</b>	<b>113</b>
Oil	107	113	<b>403</b>	93	149	166	165	<b>573</b>	<b>645</b>
Total	148	146	<b>556</b>	129	194	190	193	<b>706</b>	<b>758</b>
<b>Expense</b>									
Lease operating	23	25	<b>98</b>	31	38	35	35	<b>138</b>	<b>139</b>
Production taxes	13	14	<b>50</b>	13	19	18	18	<b>68</b>	<b>72</b>
General and administrative	7	6	<b>32</b>	10	9	10	10	<b>38</b>	<b>38</b>
Total	43	44	<b>180</b>	53	65	63	63	<b>244</b>	<b>249</b>
<b>Ebitda</b>	106	102	<b>376</b>	76	129	127	130	<b>462</b>	<b>509</b>
Exploration	4	12	<b>32</b>	12	3	3	3	<b>22</b>	<b>14</b>
Deprec., Deplet., & Amort.	28	28	<b>114</b>	35	52	45	45	<b>177</b>	<b>177</b>
Hedging and other	19	5	<b>54</b>	5	9	15	16	<b>45</b>	<b>64</b>
<b>Ebit</b>	55	57	<b>177</b>	25	64	67	69	<b>225</b>	<b>268</b>
Interest	10	11	<b>44</b>	16	27	27	27	<b>97</b>	<b>103</b>
<b>Ebt</b>	44	46	<b>133</b>	9	37	40	42	<b>127</b>	<b>165</b>
Income Tax	15	25	<b>55</b>	3	13	14	15	<b>45</b>	<b>58</b>
<b>Net Income (\$mm)</b>	29	21	<b>79</b>	6	24	26	27	<b>83</b>	<b>107</b>
Per Share (\$)	0.55	0.39	<b>1.49</b>	0.11	0.44	0.48	0.50	<b>1.53</b>	<b>1.99</b>
<b>Shares (millions)</b>	54	54	<b>53</b>	53	54	54	54	<b>54</b>	<b>54</b>
Lease operating (\$/bbl)	8.23	8.98	<b>8.73</b>	10.44	9.98	11.00	11.00	<b>10.58</b>	<b>11.00</b>
Production taxes (%rev)	8.5	9.3	<b>9.0</b>	9.7	9.9	9.5	9.5	<b>9.6</b>	<b>9.5</b>
General and admin (\$/bbl)	2.49	2.31	<b>2.83</b>	3.39	2.28	3.00	3.00	<b>2.88</b>	<b>3.00</b>
Deprec., D, & A (\$/bbl)	9.97	10.08	<b>10.09</b>	11.98	13.89	14.00	14.00	<b>13.51</b>	<b>14.00</b>
Ebitda Margin	71%	70%	<b>68%</b>	59%	66%	67%	67%	<b>65%</b>	<b>67%</b>
Tax rate	34%	54%	<b>41%</b>	35%	35%	35%	35%	<b>35%</b>	<b>35%</b>

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**Encore Acquisition Company**  
**Functional Cash Flow and Present Value**

	<i>NTM Ebitda</i> <i>(US\$mm)</i>	<i>Adjusted</i> <i>R/P</i>	<i>PV/</i> <i>Ebitda</i>	<i>Present</i> <i>Value</i> <i>(US\$mm)</i>	
North American Natural Gas	76	12.1	9.9	750	17%
Oil	433	16.5	8.2	3,570	83%
	509	15.5	8.5	4,320	100%
Debt (US\$mm)					1,400
Net Present Value (US\$mm)					2,920
Shares (mm)					54
Net Present Value - Standard Estimate (US\$/sh)					54
Net Present Value - Approximation by Correlation (US\$/sh)					60



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