

McDep Energy Income Producers

A Weekly Analysis of Royalty Trusts and Master Limited Partnerships

June 22, 2004

Chocolate Fudge

Summary and Recommendation

Eating a lot of chocolate fudge may not be good for your physical health, but we believe that owning a lot of units of **Canadian Oil Sands Trust (COSWF)**, the largest owner of the largest plant producing high quality oil from fudge-like oil sands, will be good for your financial health. In mid-June we were privileged to walk on sticky, gooey, oil-saturated sand in Northern Alberta that reminded us of licking the beaters during preparation of a favorite dessert. While the field trip was most interesting we also discuss reduced concerns about unlimited liability and Canadian ownership that seem to be contributing temporarily to a low stock price.

A Visit to Syncrude

The Aurora North lease contains some of the richest deposits that hold Canada's 175 billion barrels of recoverable oil from oil sands. We stood at the bottom of a formation hundreds of feet thick. An electric powered shovel scooped 100 tons at a time and dumped it into 400 ton trucks. Oil is separated from the sand by hot water. Some of the separation takes place at the lease and the remainder in a pipeline as the mixture is moved to the upgrader, essentially a complex oil refinery. The upgrader is where most of the money is being spent in the current expansion.

The key question we heard repeatedly was how could the owners of Syncrude, the oil sands joint venture, underestimate the costs of the expansion by more than a billion dollars? Our own two sentence interpretation is that because **ExxonMobil (XOM)** engineers were too busy with other projects they shifted responsibility to the engineering and construction firm, Halliburton. The project proved to be too complex for the contractor and now ExxonMobil engineers are personally on the scene and taking responsibility. Owning 70% of **Imperial Oil (IMO)** that owns 25% of Syncrude, ExxonMobil is the lead corporate owner.

Progress on the Limitation of Liability

Alberta has changed its law to limit the liability of trusts, further reducing any lingering concern. Limited liability to investors in a public corporation is one of the great innovations capitalists take for granted. Thus, when it appeared that income trusts in Canada may not have had that protection, it got the attention of thoughtful prospective investors in our favorite oil income stock.

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Apparently the concern has been sufficient to inhibit ownership of Canadian royalty trusts by some pension funds in Canada and it keeps some large trusts out of an index of Toronto Stock Exchange issues. Smart lawyers have devised structures to neutralize the issue for certain parties. Apparently at least one pension fund has created a corporate structure to own the trust units. That provides a shield to limit liability. At the other end, at least one royalty trust, PrimeWest, owns its oil and gas properties in a corporation, we are told. That provides a liability shield, too.

To save redundant legal work for others, an effort is underway to change the law. A measure that clarifies the issue has had its customary three readings in the Alberta legislative body and was made final by the Queen's representative last month as we understand it. Ontario is likely to finalize its effort, perhaps by fall.

Presumably the market for royalty trusts would then be expanded as a lingering concern is eliminated for some prospective investors. More pension funds may become active. The trust units would more readily qualify for indexing and the expanded demand that implies. More demand is positive for stock price.

Contrasting Approaches to Canadian Ownership

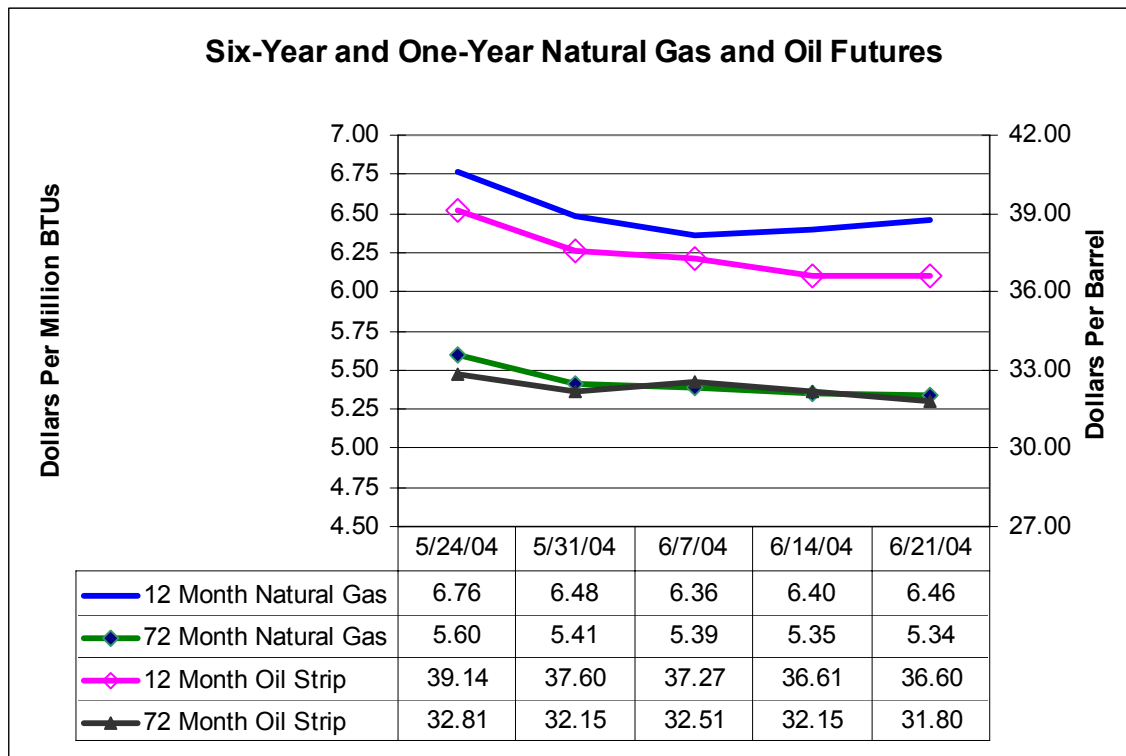
PrimeWest Energy Trust (PWI), newly added to our research coverage at a McDep Ratio slightly above 1.0, lobbies to clarify Federal law to allow more non-Canadian ownership already at some 54% for PWI. At the other extreme, **Pengrowth Energy Trust (PGH)** will soon implement a dual class stock structure to assure majority Canadian ownership. Because non-Canadian ownership of Canadian Oil Sands Trust remains at about 43% there is time to see how resolution of the issue proceeds for those trusts with greater non-Canadian ownership. Our preference is that ownership restrictions be dropped entirely in recognition of the increasing efficiency of the global marketplace.

Kurt H. Wulff, CFA

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Rank by McDep Ratio: Market Cap and Debt to Present Value

	Symbol/ Rating	Price (\$/sh) 21-Jun 2004	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio	
Master Limited Partnerships and Canadian Royalty Trusts								
Kinder Morgan Energy Partners, L.P.	KMP	S2	40.43	145.0	5,860	15.00	0.49	1.87
Kinder Morgan Management, LLC	KMR	S2	37.00	52.7	1,950	15.00	0.49	1.75
Provident Energy Trust	PVX		7.98	88.0	700	6.20	0.33	1.19
Dorchester Minerals, L.P.	DMLP		19.21	27.0	520	17.00	-	1.13
NAV Energy Trust (US\$)	NVG.UN		7.77	19.0	150	7.00	0.18	1.09
Enerplus Resources Fund	ERF		27.83	90.4	2,520	28.00	0.13	0.99
Pengrowth Energy Trust	PGH		13.71	125.0	1,710	14.00	0.13	0.98
PrimeWest Energy Trust	PWI		17.71	50.5	890	19.00	0.21	0.95
Canadian Oil Sands Trust (US\$)	COSWF	B1	32.84	86.9	2,850	62.00	0.20	0.62
		<i>Total or Median</i>			<i>17,200</i>		<i>0.20</i>	<i>1.09</i>
U.S. Royalty Trusts								
Sabine Royalty Trust	SBR		34.92	14.6	510	27.00	-	1.29
Permian Basin RT (41%)	PBT		9.11	19.1	170	7.70	-	1.18
San Juan Basin Royalty Trust	SJT	B1	24.90	46.6	1,160	22.00	-	1.13
Hugoton Royalty Trust (46%)	HGT		23.87	18.4	440	22.00	-	1.08
Cross Timbers Royalty Trust	CRT		29.10	6.0	180	30.00	-	0.97
		<i>Total or Median</i>			<i>2,500</i>		<i>-</i>	<i>1.13</i>

Buy/Sell rating after symbol: B1 - Buy full unlevered position, S2 - short quarter unlevered position

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

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

	Symbol/ Rating	Price (\$/sh) 21-Jun 2004	EV/ Sales NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)	PV/ Ebitda NTM
Master Limited Partnerships and Canadian Royalty Trusts							
Kinder Morgan Energy Partners, L.P.	KMP S2	40.43	2.7	15.0	21	6.8	8.0
Kinder Morgan Management, LLC	KMR S2	37.00	2.6	14.0	19	7.5	8.0
Dorchester Minerals, L.P.	DMLP	19.21	9.2	10.1	19	9.9	8.9
Enerplus Resources Fund	ERF	27.83	4.6	6.6	12	11.2	6.7
Canadian Oil Sands Trust (US\$)	COSWF B1	32.84	3.8	6.5	10	4.5	10.5
Provident Energy Trust	PVX	7.98	4.6	5.8	17	13.1	4.9
Pengrowth Energy Trust	PGH	13.71	4.0	5.3	10	13.4	5.4
PrimeWest Energy Trust	PWI	17.71	3.7	5.0	10	13.5	5.3
NAV Energy Trust (US\$)	NVG.UN	7.77	2.6	4.2	11	17.2	3.9
	<i>Median</i>		<i>3.8</i>	<i>6.5</i>	<i>12</i>	<i>11.2</i>	<i>6.7</i>
U.S. Royalty Trusts							
Sabine Royalty Trust	SBR	34.92	11.5	12.0	12	8.3	9.3
Cross Timbers Royalty Trust	CRT	29.10	8.1	11.1	11	8.9	11.4
Permian Basin RT (41%)	PBT	9.11	6.5	8.9	10	8.2	7.5
San Juan Basin Royalty Trust	SJT B1	24.90	7.1	8.7	10	9.7	7.7
Hugoton RoyaltyTrust (46%)	HGT	23.87	6.5	8.4	10	10.1	7.8
	<i>Median</i>		<i>7.1</i>	<i>8.9</i>	<i>10</i>	<i>8.9</i>	<i>7.8</i>

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended March 31, 2005; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

Determinants of Present Value

	Symbol/ Rating	NG & O Prod/ Ebitda (%)	N. Am. Gas/ Ebitda (%)	Adjusted Reserves/ Production NTM	PV/ Ebitda NTM	NG&O Ebitda/ mcf	Natural Royalty (%)
Master Limited Partnerships and Canadian Royalty Trusts							
NAV Energy Trust (US\$)	NVG.UN	100	40	3.7	3.9	3.43	-
Provident Energy Trust	PVX	79	49	4.5	4.9	3.89	-
PrimeWest Energy Trust	PWI	100	68	7.2	5.3	4.18	-
Pengrowth Energy Trust	PGH	100	45	8.0	5.4	3.14	-
Dorchester Minerals, L.P.	DMLP	100	84	8.4	8.9	4.68	54
Enerplus Resources Fund	ERF	100	57	9.3	6.7	3.55	-
Kinder Morgan Energy Partners, L.P.	KMP S2	22	-	12.0	8.0		
Kinder Morgan Management, LLC	KMR S2	22	-	12.0	8.0		
Canadian Oil Sands Trust (US\$)	COSWF B1	100	(9)	20.0	10.5	3.48	-
	<i>Median</i>		<i>45</i>	<i>8.4</i>	<i>6.7</i>	<i>3.55</i>	
U.S. Royalty Trusts							
Sabine Royalty Trust	SBR	100	64	8.5	9.3	5.19	100
Permian Basin RT (41%)	PBT	100	44	9.1	7.5	3.55	24
Cross Timbers Royalty Trust	CRT	100	74	12.7	11.4	4.29	85
Hugoton RoyaltyTrust (46%)	HGT	100	94	13.9	7.8	4.31	-
San Juan Basin Royalty Trust	SJT B1	100	99	13.9	7.7	3.94	-
	<i>Median</i>		<i>74</i>	<i>12.7</i>	<i>7.8</i>	<i>4.29</i>	

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