

Rating: Buy  
S&P 500: 1305

## EOG Resources Inc. New Natural Gas Buy Recommendation

<i>Symbol</i>	EOG	<i>Ebitda Next Twelve Months ending 3/31/07 (US\$mm)</i>	3,300
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	69
<i>Price (\$/sh)</i>	69.44	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	3/22/06	<i>Adjusted Reserves/Production NTM</i>	9.6
<i>Shares (mm)</i>	245	<i>EV/Ebitda</i>	5.5
<i>Market Capitalization (\$mm)</i>	17,000	<i>PV/Ebitda</i>	7.0
<i>Debt (\$mm)</i>	1,000	<i>Undeveloped Reserves (%)</i>	28
<i>Enterprise Value (EV) (\$mm)</i>	18,000	<i>Natural Gas and Oil Ebitda (\$/mcf)</i>	5.90
<i>Present Value (PV) (\$mm)</i>	23,100	<i>Present Value Proven Reserves(\$/boe)</i>	22.40
<i>Net Present Value (\$/share)</i>	90	<i>Present Value Proven Reserves(\$/mcf)</i>	3.70
<i>Debt/Present Value</i>	0.04	<i>Earnings Next Twelve Months (US\$/sh)</i>	5.56
<i>McDep Ratio - EV/PV</i>	0.78	<i>Price/Earnings Next Twelve Months</i>	12
<i>Dividend Yield (%/year)</i>	0.3	<i>Indicated Annual Dividend (US\$/sh)</i>	0.24

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.

### Summary and Recommendation

We recommend current purchase of **EOG Resources (EOG)** as a high-performance natural gas producer with conservative reserve reporting and low debt. The stock offers 30% appreciation potential to estimated net present value of \$90 a share that presumes a long-term oil price of \$50 a barrel and natural gas price of \$10 a million btu. Six-year oil currently trades at \$64 a barrel while six-year natural gas trading at about \$8.40 is below the competitive equivalent of oil at more than \$12 a million btu. Concentration of 79% of present value on North American natural gas is greater than buy recommendations **Anadarko (APC)** and **Devon (DVN)** and comparable to buy recommendations **Encana (ECA)** and **XTO Energy (XTO)**. Those four peers and EOG are closely related alternatives for the cash that investors in buy-recommended **Burlington Resources (BR)** expect to receive in the next few weeks as buy-recommended **ConocoPhillips (COP)** completes its acquisition. EOG appears to have attractive resource potential in unconventional natural gas plays in Texas, especially the Barnett Shale trend, and in the Rocky Mountains. Chairman Mark Papa has a distinguished record.

### Conservative Reserve Reporting

When Enron Oil and Gas, the predecessor of EOG Resources, was preparing for its initial public offering in 1989, we wrote in our independent analysis that the company “uses the most conservative engineering firm, DeGolyer & MacNaughton, to verify company estimates for fields accounting for about 75% of reported reserves.” Management continues the practice of seeking the opinion of DeGolyer and MacNaughton on some 80% of EOG’s reserves.

The company has performed well particularly in the six years since final and complete separation from its parent. Reserves may be understated, but management has continually built a backlog of prospects to be drilled, reserves to be booked and natural gas to be produced. An active driller in the Barnett Shale surrounding Fort Worth, the largest producing field in Texas, EOG sees more

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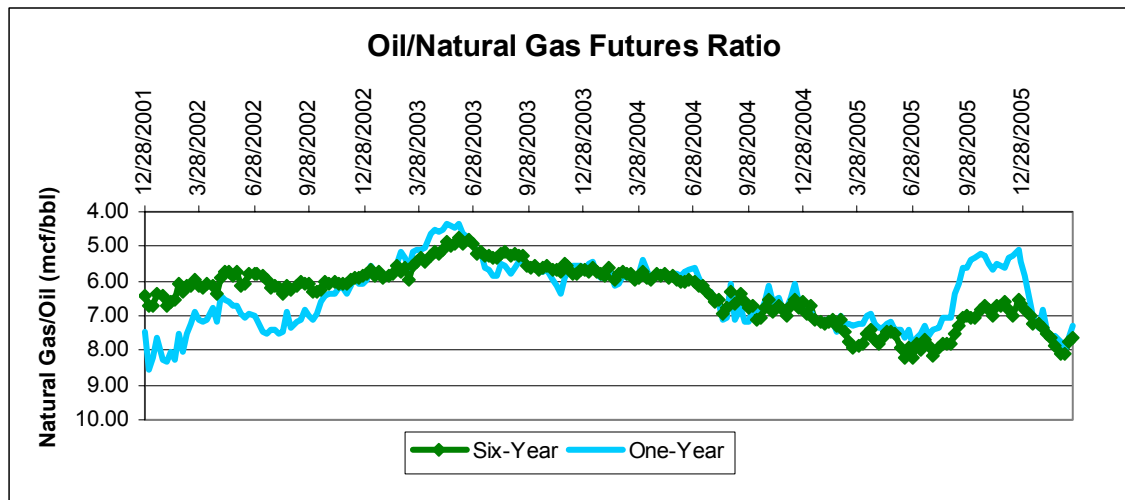
than three trillion cubic feet of potential on its properties compared to total company reserves just above 6 trillion cubic feet equivalent.

### Low Debt

Further distancing itself from its infamous former parent and a less credible sell-recommended sibling, EOG adds low debt to its conservative reserve reporting. The McDep Ratio tends to lead us to lower debt companies as the ratio exposes any tendency for investors to pay too much for high-debt companies. Debt by itself is not bad, it contributes to economic growth. Those investors who want more leverage than EOG offers can add their own debt or just simply own more of the stock in an optimized portfolio.

### Natural Gas Looks Timely

It is close, but six-year natural gas has been trading above its 40-week average for the past two weeks after trading below for three weeks in the wake of a warm January in North America. While stock price for several of our low McDep Ratio recommendations is below the 200-day average, EOG stock is above it again after a brief period below. When we plot natural gas price compared to oil price we can see a turn that has occurred after natural gas reached the low end of a trading range relative to oil (see chart [Oil/Natural Gas Futures Ratio](#)).



### EOG is North American Natural Gas

Our estimate of present value of EOG matches the current correlation for thirty stocks (see table [Functional Cash Flow and Present Value](#)). In addition to reported reserves, our estimate depends on projections for the next twelve months and beyond (see table [Operating and Financial Results](#)). Concentration on natural gas places EOG in an exclusive group of large cap independent producers (see table [Home Country and Business Segments](#)).

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**EOG Resources Inc.**  
**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	2,280	10.6	8.0	18,300	79%
Rest of World Natural Gas	350	8.1	5.1	1,800	8%
Oil	670	7.0	4.5	3,000	13%
	3,300	9.6	7.0	23,100	100%
Debt (US\$mm)					1,000
Net Present Value (US\$mm)					22,100
Shares (mm)					245
Net Present Value - Standard Estimate (US\$/sh)					90
Net Present Value - Approximation by Correlation (US\$/sh)					90

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

	<i>Symbol/</i> <i>Rating</i>	<i>Price</i> <i>(\$/sh)</i> <i>22-Mar</i> <i>2006</i>	<i>Shares</i> <i>(mm)</i>	<i>Market</i> <i>Cap</i> <i>(\$mm)</i>	<i>Net</i> <i>Present</i> <i>Value</i> <i>(\$/sh)</i>	<i>Debt/</i> <i>Present</i> <i>Value</i>	<i>McDep</i> <i>Ratio</i>
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>							
CNOOC Limited (29%)	CEO B	80.65	119	9,620	84.00	0.00	0.96
Encana Corporation	ECA B	46.30	873	40,400	51.00	0.18	0.92
XTO Energy Inc.	XTO B	41.83	372	15,560	52.00	0.16	0.84
Occidental Petroleum Corp.	OXY B	92.49	432	40,000	120.00	0.12	0.80
EOG Resources	EOG B	69.44	245	17,000	90.00	0.04	0.78
Burlington Resources	BR B	89.90	378	34,000	115.00	-	0.78
Devon Energy Corporation	DVN B	58.27	451	26,300	94.00	0.12	0.67
Anadarko Petroleum Corp.	APC B	97.87	234	22,900	160.00	0.10	0.65
	<i>Total or Median</i>			206,000		0.11	0.79

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

	<i>Symbol/</i> <i>Rating</i>	<i>Price</i> <i>(\$/sh)</i> <i>22-Mar</i> <i>2006</i>	<i>Adjstd</i> <i>Resrvs/</i> <i>Prod</i> <i>NTM</i>	<i>PV/</i> <i>Ebitda</i> <i>NTM</i>	<i>EV/</i> <i>Ebitda</i> <i>NTM</i>	<i>P/E</i> <i>NTM</i>	<i>Divd or</i> <i>Distrib</i> <i>NTM</i> <i>(%)</i>
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>							
XTO Energy Inc.	XTO B	41.83	12.4	7.9	6.6	12	0.5
EOG Resources	EOG B	69.44	9.6	7.0	5.5	12	0.3
Encana Corporation	ECA B	46.30	8.7	5.9	5.4	11	0.6
Occidental Petroleum Corp.	OXY B	92.49	10.2	6.3	5.1	9	1.6
CNOOC Limited (29%)	CEO B	80.65	9.0	5.2	5.0	9	2.9
Anadarko Petroleum Corp.	APC B	97.87	12.7	7.2	4.7	8	0.7
Devon Energy Corporation	DVN B	58.27	8.6	5.9	3.9	7	0.8
Burlington Resources	BR B	89.90	-	-	-	-	-
	<i>Median</i>		9.3	6.1	5.0	9	0.7

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**EOG Resources Inc.**  
**Operating and Financial Results**

	<i>Q1</i>	<i>Q4</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Next</i>
	<i>3/31/05</i>	<i>12/31/05</i>	<i>3/31/06</i>	<i>6/30/06</i>	<i>9/30/06</i>	<i>12/31/06</i>	<i>2006E</i>	<i>3/31/07</i>	<i>Twelve</i>
									<i>Months</i>
									<i>3/31/07</i>
<b>Volume</b>									
Natural Gas (mmcf)									
U.S.	689	749	749	749	749	749	<b>749</b>	749	<b>749</b>
Canada	234	225	225	225	225	225	<b>225</b>	225	<b>225</b>
Overseas	240	338	338	338	338	338	<b>338</b>	338	<b>338</b>
Total	1,163	1,312	1,312	1,312	1,312	1,312	<b>1,312</b>	1,312	<b>1,312</b>
Oil (mbd)	36	36	36	36	36	36	<b>36</b>	36	<b>36</b>
Total gas & oil (bcf)	124	141	138	139	141	141	<b>558</b>	138	<b>558</b>
<b>Price</b>									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	6.27	13.00	8.97	6.98	7.43	8.93	<b>8.08</b>	10.72	<b>8.52</b>
U.S.	5.97	10.38	8.08	6.29	6.69	8.04	<b>7.27</b>	9.65	<b>7.66</b>
Canada	5.69	9.73	7.18	5.59	5.95	8.04	<b>6.69</b>	8.58	<b>7.03</b>
Overseas	-	3.28	3.28	3.28	3.28	3.28	<b>3.28</b>	3.28	<b>3.28</b>
Total	5.19	8.44	6.69	5.39	5.69	6.81	<b>6.14</b>	7.82	<b>6.42</b>
Oil (\$/bbl)									
WTI Cushing	49.65	60.02	62.86	61.81	64.17	65.11	<b>63.49</b>	65.59	<b>64.17</b>
Worldwide	44.24	55.29	57.90	56.94	59.11	59.98	<b>58.49</b>	60.42	<b>59.11</b>
Total gas & oil (\$/mcf)	5.54	8.63	7.11	5.98	6.28	7.27	<b>6.66</b>	8.14	<b>6.91</b>
<b>Revenue (\$mm)</b>									
Natural Gas									
U.S.	423	715	544	428	461	554	<b>1,988</b>	650	<b>2,094</b>
Canada	120	201	145	114	123	166	<b>549</b>	174	<b>578</b>
Overseas	-	102	100	101	102	102	<b>405</b>	100	<b>405</b>
Total	543	1,019	790	644	686	822	<b>2,942</b>	924	<b>3,076</b>
Oil	145	185	189	188	197	200	<b>775</b>	197	<b>783</b>
Other	0	11					-		-
Total	688	1,214	979	832	884	1,023	<b>3,717</b>	1,121	<b>3,860</b>
<b>Expense</b>									
Cash costs	150	149	149	113	126	160	<b>548</b>	160	<b>559</b>
<b>Ebitda</b> (\$mm)	538	1,065	829	719	758	862	<b>3,169</b>	961	<b>3,301</b>
Exploration	62	100	100	100	100	100	<b>400</b>	100	<b>400</b>
Deprec., Deplet., & Amort.	153	177	179	181	183	183	<b>726</b>	179	<b>726</b>
Hedging and other									-
<b>Ebit</b>	323	788	550	438	475	579	<b>2,043</b>	682	<b>2,175</b>
Interest	14	20	20	20	20	20	<b>80</b>	20	<b>80</b>
<b>Ebt</b>	309	768	530	418	455	559	<b>1,963</b>	662	<b>2,095</b>
Income Tax	108	285	186	146	159	196	<b>687</b>	232	<b>733</b>
<b>Net Income (\$mm)</b>	201	483	345	272	296	364	<b>1,276</b>	430	<b>1,362</b>
<b>Shares</b> (millions)	242	245	245	245	245	245	<b>245</b>	245	<b>245</b>
Per Share (\$)	0.83	1.97	1.41	1.11	1.21	1.48	<b>5.21</b>	1.76	<b>5.56</b>
Ebitda Margin	78%	88%	85%	86%	86%	84%	<b>85%</b>	86%	<b>86%</b>
Tax Rate	35%	37%	35%	35%	35%	35%	<b>35%</b>	35%	<b>35%</b>

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### Home Country and Business Segments

				<i>North Amer. Non- U.S. Home</i>	<i>Rest of World Natural Gas (%)</i>	<i>Oil Prod'n (%)</i>	<i>Down- stream (%)</i>	<i>McDep Ratio</i>
	<i>Symbol/ Rating</i>							
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
CNOOC Limited	CEO	B	China	-	12	88	-	0.96
Encana Corporation	ECA	B	Canada	81	-	19	-	0.92
XTO Energy Inc.	XTO	B		83	-	17	-	0.84
Occidental Petroleum Corp.	OXY	B		14	2	74	11	0.80
EOG Resources	EOG	B		79	8	13	-	0.78
Devon Energy Corporation	DVN	B		64	-	36	-	0.67
Anadarko Petroleum Corp.	APC	B		60	-	40	-	0.65
	<i>Median</i>			<i>64</i>	<i>-</i>	<i>36</i>	<i>-</i>	<i>0.79</i>

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