

Value in Developing Country Growth

Summary and Recommendation

Contrarian Buy recommendations **Woodside Petroleum (WOPEY)**, **PetroChina (PTR)**, **Lukoil (LUKOY)** and **Gazprom (OGZPY)** have attractive investment value tied to the higher growth potential of developing countries. **Petrobras (PBR)** also has positive prospects while we wait for stock price to adjust for a giant public offering and to absorb lower expectations for deep water offshore oil. **CNOOC Ltd. (CEO)** has achieved what we would like to see in any investment. CEO stock has reached a McDep Ratio of 1.21, trades above the 200-day average currently and over the past nine years has multiplied 11 times while delivering a total return of 33% a year, according to Bloomberg. Offsetting the higher growth potential is the volatility of stock price and the recently declining patterns for five of the six stocks, hence our qualifier “contrarian”.

Investor confidence has been waning in the second year of a U.S. presidential term as it has at times in the past. Looking through the next few months we may see better stock prices before year end and we are optimistic about 2011 and 2012. In our Australia, Brazil, China and Russia group, McDep Ratios range as low as 0.38 and cash flow multiples (EV/Ebitda) as low as 3.5 (see [Tables 1-3](#) on pages 3-5). More of each stock’s story rises from company models (see tables [Functional Cash Flow and Present Value](#) on pages 6-8). The main industry trend is captured in oil price where the latest settlement of six-year futures at \$85 a barrel compares to the 40-week average of \$86 (see charts [Six-Year Commodity Price Meter](#) and [Six-Year and One-Year Natural Gas and Oil Futures](#) on page 9). We take a quick round-the-world tour in our comments below on the Contrarian Buys.

New Australian Prime Minister Less Tax Unfriendly

Investors in Australian stocks breathed a sigh of relief with the resignation of Mr. Kevin Rudd, the former Prime Minister who threatened mineral companies and natural gas producers with a 40% resource tax on top of income taxes and state taxes. Succeeding her Labor Party colleague, Ms. Julia Gillard, Australia’s first female Prime Minister, signals a retreat from attempted tax overreaching. As Alberta and Alaska may have realized, Australia may be seeing that too much tax is too much. Reinforced by popular resistance to Mr. Rudd’s unfriendliness, investors appear to rate political risk low in Australia.

WOPEY is an Australian company investing heavily in expensive new projects to develop liquefied natural gas exports. Estimated Net Present Value (NPV) includes 25% for natural gas resources not generating cash flow currently. We see strategic appeal in potential six-fold growth in natural gas volume fueled by demand from emerging economy China, and perhaps India.

Home Country Growth for PetroChina

PTR gets most of its current cash flow and profits in developing new domestic oil production to replace decline of existing production and in expanding overseas. Natural gas profits are growing



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more rapidly from a lower base. Eventually, low price under government control is likely to give way to world price as China increases imports to offset its primitive reliance on coal. Downstream, regulated price has been relaxed dramatically, at least in the past year, and there is long-term volume growth in the domestic transportation market.

China has proven to be a rewarding place to invest. Government control of prices and taxes may be tight, but relaxed on a sufficiently progressive scale to promote healthy resource companies. The Government appears motivated to promote growth in order to continue in power peacefully. Profitable companies provide efficient growth at a reasonable price for customers and for investors.

Political Discount May Narrow for Russian Stocks, LUKOY and OGZPY

The difference in McDep Ratios for Woodside (0.88), PetroChina (0.80) and Lukoil (0.43)/Gazprom (0.38) may be due mainly to the perception of political risk. Evidently, investors remain skeptical of investing in Russia. Perhaps the question should be whether that skepticism will grow or diminish from here. Much of any change in confidence is related generally to global appetite for investing in natural resources that are abundant in Russia. If resources are going to be worth more and Russia wants investment to produce and sell those resources, the climate for profit ought to improve.

Lukoil, the largest non-government owned oil company operates profitably today. There is a lot of room for excise taxes to be relaxed to encourage oil production in the Caspian Sea and through enhanced recovery in old fields, for example.

Gazprom, half government owned, operates as a giant utility company that also produces natural gas and oil. Sales of natural gas to Europe are profitable at price that responds to the international market -- rising in 2008, declining in 2009 and recovering in 2010. Among the company's opportunities are market price for domestic sales, future sales to China and development of new production. On the negative side, interruption of supply through transit countries has incurred unfavorable publicity. The potential cost of new pipelines to carry natural gas around Belarus and Ukraine is also an incentive to settle differences amicably.

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Table 2								
McDep Large Cap Energy Portfolio								
Net Present Value and McDep Ratio								
			Price			Net		
			(US\$/sh)		Market	Present	Debt/	
	Symbol/Rating		28-Jun	Shares	Cap	Value	Present	McDep
	B = Buy, CB (see below)		2010	(mm)	(US\$mm)	(US\$/sh)	Value	Ratio
U.S. Integrated								
Exxon Mobil Corporation	XOM	CB	58.47	5,215	305,000	89.00	0.12	0.70
Marathon Oil Corporation	MRO	B	32.29	711	22,960	53.00	0.23	0.70
Chevron Corporation	CVX	B	69.96	2,004	140,000	110.00	0.11	0.68
ConocoPhillips	COP	B	51.19	1,504	77,000	95.00	0.27	0.66
	<i>Total or Median</i>				545,000		0.18	0.69
Europe								
BG Group plc	BRGXF		15.85	3,400	53,900	22.00	0.11	0.75
Royal Dutch Shell plc	RDS-A	CB	52.86	3,066	162,000	79.00	0.21	0.74
Statoil ASA (33%)	STO	CB	20.31	1,050	21,300	35.00	0.21	0.67
Total S.A.	TOT	CB	46.52	2,243	104,000	90.00	0.13	0.58
BP plc	BP		27.05	3,167	86,000	75.00	0.20	0.49
	<i>Total or Median</i>				427,000		0.20	0.67
Australia/Brazil/China/Russia								
CNOOC Limited (34%)	CEO		176.64	152	26,900	145.00	0.03	1.21
Woodside Petroleum Ltd.	WOPEY	CB	37.84	794	30,000	44.00	0.13	0.88
PetroChina Company Ltd (14%)	PTR	CB	114.46	256	29,300	150.00	0.15	0.80
Petrobras	PBR		35.34	4,387	155,000	58.00	0.20	0.69
Lukoil Oil Company	LUKOY	CB	54.20	847	45,900	135.00	0.05	0.43
Gazprom (50%)	OGZPY	CB	19.76	2,915	57,600	64.00	0.10	0.38
	<i>Total or Median</i>				345,000		0.12	0.74
U.S. Independent								
Southwestern Energy Company	SWN		41.05	349	14,300	35.00	0.09	1.16
EOG Resources	EOG	B	105.42	250	26,400	92.00	0.13	1.13
Anadarko Petroleum Corp.	APC		37.74	496	18,700	44.00	0.40	0.91
Occidental Petroleum Corp.	OXY	B	80.91	814	65,800	95.00	0.06	0.86
Chesapeake Energy Corp.	CHK		22.45	647	14,500	31.00	0.40	0.83
Devon Energy Corporation	DVN	B	62.91	448	28,200	98.00	0.03	0.65
	<i>Total or Median</i>				167,900		0.11	0.89
Canada								
Imperial Oil Limited (30%)	IMO	B	38.70	256	9,900	48.00	0.08	0.82
Canadian Natural Resources	CNQ	B	35.04	1,086	38,100	45.00	0.18	0.82
EnCana Corporation	ECA	B	32.02	749	24,000	42.00	0.22	0.81
Cenovus Energy Inc.	CVE	B	27.10	752	20,400	37.00	0.20	0.78
Canadian Oil Sands Trust	COSWF	B	27.09	484	13,100	38.00	0.07	0.73
Suncor Energy	SU	B	31.83	1,572	50,000	48.00	0.19	0.73
	<i>Total or Median</i>				156,000		0.19	0.80
CB=Contrarian Buy, Stock Price may in downtrend compared to 200-day average.								
McDep Ratio = Market cap and Debt to present value of oil and gas and other businesses								
Estimated present value presumes a long-term price for oil of US\$75 a barrel and natural gas, \$8 a million btu.								



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Table 3								
McDep Large Cap Energy Portfolio								
Value Multiples and Distribution Yield								
			Price (US\$/sh)	Adjustd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda	P/E	Divd or Distrib NTM
	Symbol/Rating		28-Jun 2010	NTM	NTM	NTM	NTM	(%)
B = Buy, CB (see below)								
U.S. Integrated								
Exxon Mobil Corporation	XOM	CB	58.47	13.5	8.5	6.0	11	2.9
Marathon Oil Corporation	MRO	B	32.29	9.1	7.5	5.3	11	2.3
ConocoPhillips	COP	B	51.19	10.5	7.3	4.8	8	3.2
Chevron Corporation	CVX	B	69.96	9.1	6.6	4.5	9	3.9
<i>Total or Median</i>				9.8	7.4	5.1	10	3.0
Europe								
BG Group plc	BRGXF		15.85	13.4	8.8	6.6	12	0.8
Royal Dutch Shell plc	RDS-A	CB	52.86	8.7	6.4	4.7	8	6.4
Total S.A.	TOT	CB	46.52	9.6	7.2	4.2	7	6.0
Statoil ASA (33%)	STO	CB	20.31	6.4	5.8	3.9	8	4.6
BP plc	BP		27.05	9.7	6.1	3.0	4	12.4
<i>Total or Median</i>				9.6	6.4	4.2	8	6.0
Australia/Brazil/China/Russia								
Woodside Petroleum Ltd.	WOPEY	CB	37.84	17.8	13.2	11.6	20	2.5
PetroChina Company Ltd (14%)	PTR	CB	114.46	13.8	8.0	6.4	14	3.5
CNOOC Limited (34%)	CEO		176.64	6.8	5.0	6.1	11	2.9
Petrobras	PBR		35.34	9.1	8.9	6.1	9	3.8
Gazprom (50%)	OGZPY	CB	19.76	30.2	9.8	3.7	5	0.2
Lukoil Oil Company	LUKOY	CB	54.20	15.7	8.0	3.5	6	3.1
<i>Total or Median</i>				14.7	8.5	6.1	10	3.0
U.S. Independent								
Southwestern Energy Company	SWN		41.05	6.5	8.5	9.9	19	-
EOG Resources	EOG	B	105.42	9.7	8.0	9.0	34	0.6
Chesapeake Energy Corp.	CHK		22.45	12.0	10.6	8.9	13	1.3
Occidental Petroleum Corp.	OXY	B	80.91	10.5	7.5	6.4	14	1.3
Devon Energy Corporation	DVN	B	62.91	10.0	7.9	5.1	12	1.0
Anadarko Petroleum Corp.	APC		37.74	8.4	5.2	4.8		1.0
<i>Total or Median</i>				9.8	7.9	7.6	14	1.0
Canada								
Imperial Oil Limited (30%)	IMO	B	38.70	20.2	11.4	9.4	18	1.0
Canadian Natural Resources	CNQ	B	35.04	20.2	11.4	9.3	32	0.8
Canadian Oil Sands Trust	COSWF	B	27.09	31.0	12.1	8.8	14	7.1
EnCana Corporation	ECA	B	32.02	17.0	10.4	8.5	25	2.5
Suncor Energy	SU	B	31.83	25.3	11.2	8.2	19	1.2
Cenovus Energy Inc.	CVE	B	27.10	19.5	10.2	8.0	16	2.9
<i>Total or Median</i>				20.2	11.3	8.7	18	1.9
CB=Contrarian Buy, Stock Price may be in downtrend compared to 200-day average.								
EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended June 30, 2011; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses								



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Woodside Petroleum Ltd.					
Functional Cash Flow and Present Value					
				<i>Present</i>	
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Value</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>(US\$mm)</i>	
Natural Gas	1,500	24.9	13.3	20,000	50%
Oil	1,600	7.7	6.4	10,200	25%
Liquefied Natural Gas Projects				10,000	25%
	3,100	17.8	13.0	40,200	100%
Debt (US\$mm)					5,300
Net Present Value (US\$mm)					34,900
Shares (mm)					794
Net Present Value - Standard Estimate (US\$/sh)					44
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					39

PetroChina					
Functional Cash Flow and Present Value					
				<i>Present</i>	
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Value</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>(US\$mm)</i>	
Natural Gas	4,100	19.0	11.0	45,000	14%
Oil	30,400	11.2	7.7	233,000	72%
Downstream	5,900		7.6	45,000	14%
	40,400	13.8	8.0	323,000	100%
Debt (US\$mm)					48,000
Net Present Value (US\$mm)					275,000
Shares (mm)					1,830
Net Present Value - Standard Estimate (US\$/sh)					150
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					144



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Lukoil					
Functional Cash Flow and Present Value					
				<i>Present</i>	
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Value</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>(US\$mm)</i>	
Natural Gas	109	22.6	9.2	1,000	1%
Oil	8,890	15.7	9.1	81,000	68%
Downstream	5,900		6.4	38,000	32%
	14,900	16.6	8.1	120,000	100%
Debt (US\$mm)					5,700
Net Present Value (US\$mm)					114,300
Shares (mm)					847
Net Present Value - Standard Estimate (US\$/sh)					135
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					146

Gazprom					
Functional Cash Flow and Present Value					
				<i>Present</i>	
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Value</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>(US\$mm)</i>	
Natural Gas	33,300	30.2	9.6	320,000	77%
Oil	9,000	25.8	10.6	95,000	23%
Downstream					
	42,300	29.8	9.8	415,000	100%
Debt (US\$mm)					42,000
Net Present Value (US\$mm)					373,000
Shares (mm)					5,830
Net Present Value - Standard Estimate (US\$/sh)					64
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					87



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Petrobras					
Functional Cash Flow and Present Value					
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Present</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>Value</i>	
				<i>(US\$mm)</i>	
Natural Gas	1,090	10.2	7.3	8,000	3%
Oil	28,430	8.9	6.1	174,000	55%
Downstream	6,000		7.5	45,000	14%
Pre Salt Deep Water Oil				89,000	28%
	35,520	9.1	8.9	316,000	100%
Debt (US\$mm)					62,000
Net Present Value (US\$mm)					254,000
Shares (mm)					4,387
Net Present Value - Standard Estimate (US\$/sh)					58
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					60

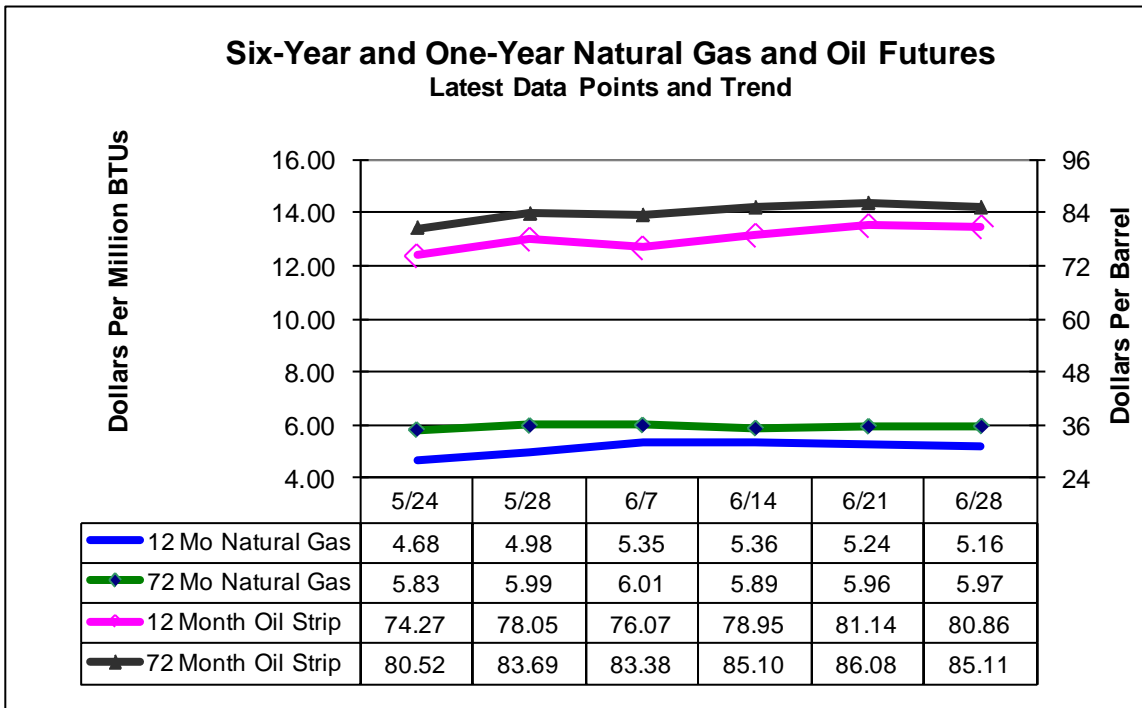
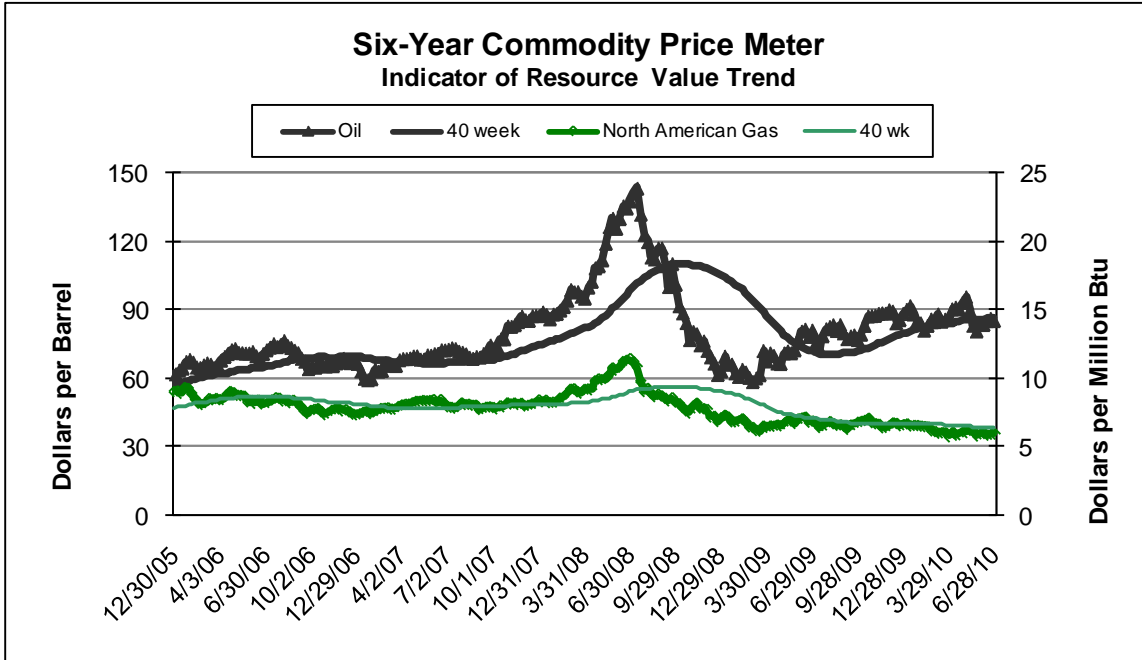
CNOOC Limited					
Functional Cash Flow and Present Value					
	<i>NTM Ebitda</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Present</i>	
	<i>(US\$mm)</i>	<i>R/P</i>	<i>Ebitda</i>	<i>Value</i>	
				<i>(US\$mm)</i>	
Natural Gas	970	13.3	8.2	8,000	12%
Oil	12,230	5.4	4.8	58,600	88%
	13,200	6.8	5.0	66,600	100%
Debt (US\$mm)					1,700
Net Present Value (US\$mm)					64,900
Shares (mm)					448
Net Present Value - Standard Estimate (US\$/sh)					145
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					148



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Index of Recent Research			
Stock Ideas			
<u>Date</u>	<u>Symbol</u>	<u>Subject</u>	<u>Theme</u>
25-Jun	DNR	Denbury Resources	Small Cap Oil Growth (Income and Small Cap Weekly)
22-Jun	CVE	Cenovus Energy	Quintuple in Deep Oil Sands (Meter Reader)
18-Jun	BIREF, FRHLF, PWE, COSWF		Montney Buzz from Calgary (Income and Small Cap Weekly)
15-Jun	XOM, COP, OXY, CVE, BP, APC		Onshore On, Offshore Off (Meter Reader)
11-Jun	HGT, SJT, MTR, LGCY, LINE, ENP		Bright Outlook for Pure Play Oil and Gas (ISCW)
8-Jun	* OXY, DVN, EOG, SWN, CHK, APC		U.S. Independent Producers Unlocking Resources (MReader)
4-Jun	* DMLP, FRHLF, CRT, PBT, SBR		Top Line Cash - Pure Plays in Reawakening Oil and Gas (ISC)
3-Jun	LUKOY	Lukoil Oil Company	Underrated Oil Performer
1-Jun	* ECA, COSWF, CNQ, CVE, IMO, SU		Long-Life Resources in Canada (Meter Reader)
28-May	* XEC, BIREF, WLL, BRY, RRC, HK, UPL		Shell Shale Gas Deal Boosts Independent Producers (ISCW)
25-May	* XOM, BP, TOT		Large Caps Go Contrarian (Meter Reader)
21-May	* COSWF, PWE, ERF, PGH, PEYUF		Canadian Income Trusts for Value and Distributions (ISCW)
20-May	* CEO	CNOOC Ltd	Remove Buy on Valuation and Trend
18-May	* RDSA, STO, TOT		European Oil for Contrarians (Meter Reader)
13-May	* BIREF	Birchcliff Energy Ltd.	New Buy for Small Cap Natural Gas Growth
11-May	* XOM, CVX, COP, MRO		U.S. Integrated Oil in New Trend (Meter Reader)
10-May	* XEC	Cimarex Energy Company	Raise NPV Again on More Production
5-May	* DVN	Devon Energy Corporation	Stock Repurchase Compelling
4-May	* BP	BP p.Lc.	Oil Spill and BP Stock Spill (Meter Reader)
30-Apr	* WLL	Whiting Petroleum Corporation	Raise NPV to \$95 a Share on Onshore Oil Drilling (ISCW)
30-Apr	* PBR, BG, APC and BP		Remove Buys - Accident May Delay Deep Water Oil
26-Mar	* PTR	PetroChina Company Limited	Gas Growth - Natural Gas and Gasoline
25-Feb	* WOPEY	Woodside Petroleum	Financing in Place for 2010
Meter Reader			
29-Jun			
22-Jun	CVE	Cenovus Energy	Quintuple in Deep Oil Sands
15-Jun	XOM, COP, OXY, CVE, BP, APC		Onshore On, Offshore Off
8-Jun	* OXY, DVN, EOG, SWN, CHK, APC		U.S. Independent Producers Unlocking Resources
1-Jun	* ECA, COSWF, CNQ, CVE, IMO, SU		Long-Life Resources in Canada
25-May	* XOM, BP, TOT		Large Caps Go Contrarian
Income and Small Cap Weekly			
25-Jun	DNR	Denbury Resources	Small Cap Oil Growth
18-Jun	BIREF, FRHLF, PWE, COSWF		Montney Buzz from Calgary
11-Jun	HGT, SJT, MTR, LGCY, LINE, ENP		Bright Outlook for Pure Play Oil and Gas
4-Jun	DMLP, FRHLF, CRT, PBT, SBR		Top Line Cash Payers - Pure Plays in Reawakening Oil and Gas
28-May	* XEC, BIREF, WLL, BRY, RRC, HK and UPL		Shell Shale Gas Deal Boosts Independent Producers
21-May	* COSWF, PWE, ERF, PGH and PEYUF		Canadian Income Trusts for Value and Distributions
Industry Ideas			
30-Apr	* PBR, BG, APC and BP		Remove Buys - Accident May Delay Deep Water Oil
			* Archived on www.mcdep.com



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Research Methodology/Ratings Description: McDep LLC is an independent research originator focused on oil and gas stocks exclusively. The firm applies the forty years of experience of its analyst to estimate a present value of the oil and gas resources and other businesses of covered companies. That value is compared with a company's stock market capitalization and debt. Stocks with low market cap and debt relative to present value tend to outperform stocks with high market cap and debt relative to present value. Buy recommendations are expected to deliver a total return better than 7% per year above inflation. Hold recommendations assume the attributes of the underlying business are reflected in the current price of the stock. Sell recommendations are expected to deliver a total return less than inflation.