

## Meter Reader

A Weekly Analysis of Energy Stocks Using the McDep Ratio

October 18, 2005

# Winter Rally

## Summary and Recommendation

After shaking off a critical test on the eve of the 18<sup>th</sup> anniversary of the Crash of 1987, buy-recommended stocks seemed poised for gains ahead of winter. A few stocks breached the 200-day average temporarily, but are again trading comfortably above it signaling the continuation of an uptrend in stock price. Commodity prices have barely wavered from well-defined upward trends buoyed recently by sluggish restarting of oil, natural gas and refinery production shut down by hurricanes. Low McDep Ratio buy recommendations include mega cap **Chevron (CVX)**; natural gas producers **Gazprom (OGZPF)** and **Anadarko (APC)**; and oil producer **Canadian Oil Sands Trust (COSWF)**. The quick failure of a prominent financial house last week reinforces our concern about the risks that appear to be ignored in sell-recommended **Kinder Morgan (KMI, KMP, KMR)**.

## Commodity Price and Present Value Support Investment

A new summary highlights critical valuation parameters (see table Oil and Gas Commodity and Stock Price). Crude oil quotes are well above the \$50 a barrel used in estimating present value, the denominator of the McDep Ratio. One-year natural gas is above our long-term estimate while six-year natural gas commodity price has extra appreciation potential. Refining margin is more than 50% above our long-term estimate.

### Oil and Gas Commodity and Stock Price Monday, October 17, 2005

	<i>Units</i>	<i>Futures Price</i>		<i>McDep Ratio</i>
		<i>Six-Year</i>	<i>One-Year</i>	<i>Denominator</i>
<b>Crude Oil</b>	\$/barrel	59.66	63.49	50
<b>Natural Gas</b>	\$/million btu	8.74	12.19	10
<b>Oil Refining</b>	\$/barrel		15.62	10

  

<i>Stocks</i>	<i>Median</i>
	<i>McDep Ratio</i>
<b>Mega Cap</b>	0.80
<b>Producer/Refiner</b>	0.82
<b>Independent - Large</b>	0.77
<b>Independent - Small</b>	0.74
<b>Income</b>	1.08

Source: McDep Associates, Bloomberg, New York Mercantile Exchange, Yahoo and company disclosures

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The McDep Ratio compares present value calculated from commodity price with enterprise value as determined in the stock market. A stock with a McDep Ratio of 1.0 presumably offers a 7% per year unlevered real return on constant real prices for oil of \$50 a barrel, natural gas of \$10 a million btu and refining crack of \$10 a barrel. Four of the five groups have median McDep Ratios below 1.0.

Thus while current commodity prices suggest our estimates of present value could be higher, current stock prices are less than the values we calculate. As a result, thriving commodity prices and low McDep Ratios make a positive case for investing in buy-recommended stocks.

#### **Select Stocks on Valuation and Strategic Considerations**

Stocks are ranked in descending order of McDep Ratio to suggest “buy low and sell high” (see table [Rank by McDep Ratio](#)). We recommend representation in each of the five groups from Mega Cap to Income with emphasis on low McDep Ratio stocks.

Next Twelve Months Cash Flow, Ebitda, changes weekly with futures prices for natural gas and oil (see table [Rank by EV/Ebitda](#)). We regularly check the correlation of present value with cash flow multiple by business and expected life of production.

Stocks of companies headquartered in other countries diversify political risk (see table [Home Country and Business Segments](#)). The Russian stocks offer more potential gain in resource value.

Finally, we recommend balance among business segments. Investors should be sure to be represented in the stocks of companies with strong natural gas concentration. Nor should that be at the expense of reasonable downstream exposure in other stocks.

Timely analyses are available on all recommended stocks (see table [Index of Recent Research](#)).

Kurt H. Wulff, CFA

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#### Oil and Gas Producers Rank by McDep Ratio: Market Cap and Debt to Present Value

	Symbol/ Rating		Price (\$/sh) 17-Oct 2005	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
<b>Mega Cap</b>								
BP plc	BP	B	66.63	3,545	236,000	82.00	0.10	0.83
Total S.A.	TOT	B	126.36	1,182	149,000	160.00	0.12	0.82
Exxon Mobil Corporation	XOM	B	58.86	6,370	375,000	74.00	0.04	0.80
Royal Dutch Shell plc	RDS-A	B	61.78	3,372	208,000	84.00	0.09	0.76
Chevron Corporation	CVX	B	59.95	2,256	135,000	90.00	0.12	0.71
<i>Total or Median</i>					<i>1,103,000</i>		<i>0.10</i>	<i>0.80</i>
<b>Producer/Refiners - Large Cap and Mid Cap</b>								
Kinder Morgan, Inc.	KMI	S2	89.69	123	11,040	20.00	0.76	1.85
Imperial Oil Limited (30%)	IMO	B	92.67	104	9,600	84.00	0.09	1.09
Marathon Oil Corporation	MRO	B	61.44	367	22,550	65.00	0.27	0.96
Petro-Canada	PCZ	B	36.66	526	19,280	42.00	0.19	0.90
Lukoil Oil Company	LUKOY	B	53.50	830	44,000	65.00	0.03	0.83
Suncor Energy	SU	B	53.45	461	24,650	68.00	0.10	0.81
Norsk Hydro ASA	NHY	B	99.25	251	24,910	130.00	0.12	0.79
ConocoPhillips	COP	B	63.02	1,419	89,400	100.00	0.15	0.69
Gazprom (50%)	OGZPF	B	58.60	1,022	59,900	90.00	0.03	0.66
PetroChina Company Ltd (10%)	PTR	B	77.92	176	13,700	120.00	0.01	0.65
<i>Total or Median</i>					<i>319,000</i>		<i>0.11</i>	<i>0.82</i>
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
Encana Corporation	ECA	B	50.51	892	45,100	51.00	0.16	0.99
XTO Energy Inc.	XTO	B	41.89	367	15,370	48.00	0.17	0.89
Burlington Resources	BR	B	71.00	385	27,300	86.00	0.09	0.84
Devon Energy Corporation	DVN	B	63.00	471	29,700	86.00	0.15	0.77
CNOOC Limited (29%)	CEO	B	64.10	119	7,640	84.00	0.01	0.76
Anadarko Petroleum Corp.	APC	B	91.45	238	21,800	140.00	0.11	0.69
Occidental Petroleum Corp.	OXY	B	75.23	406	30,500	120.00	0.11	0.67
<i>Total or Median</i>					<i>177,000</i>		<i>0.11</i>	<i>0.77</i>
<b>Independent Natural Gas and Oil - Small Cap</b>								
Berry Petroleum Company	BRY	B	59.13	23	1,330	65.00	0.10	0.92
Encore Acquisition Company	EAC	B	34.56	49	1,710	50.00	0.17	0.75
Energy Partners Ltd.	EPL	B	26.00	41	1,050	38.00	0.17	0.74
Cimarex Energy Company	XEC	B	40.51	85	3,440	64.00	0.12	0.68
<i>Total or Median</i>					<i>7,500</i>		<i>0.15</i>	<i>0.74</i>
<b>Income</b>								
Kinder Morgan Energy Partners, L.P.	KMP	S3	51.96	157	8,160	15.00	0.55	2.10
Kinder Morgan Management, LLC	KMR	S3	48.49	56	2,700	15.00	0.55	2.00
Pengrowth Energy Trust	PGH		22.78	157	3,570	20.00	0.17	1.12
San Juan Basin Royalty Trust	SJT		43.07	47	2,010	40.00	-	1.08
Enerplus Resources Fund	ERF		45.08	105	4,730	42.00	0.13	1.06
Penn West Energy Trust	PWTFF	B	28.28	174	4,910	28.00	0.16	1.01
Canadian Oil Sands Trust (US\$)	COSWF	B	95.57	93	8,880	136.00	0.12	0.74
<i>Total or Median</i>					<i>35,000</i>		<i>0.16</i>	<i>1.08</i>

B = Buy, S2 = Short half unlevered position, S3 = Short quarter unlevered position

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

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#### Oil and Gas Producers

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

	Symbol/ Rating		Price (\$/sh) 17-Oct 2005	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
<b>Mega Cap</b>								
Exxon Mobil Corporation	XOM	B	58.86	11.5	6.8	5.4	9	2.0
BP plc	BP	B	66.63	9.4	6.5	5.4	9	3.2
Total S.A.	TOT	B	126.36	9.2	6.1	4.9	8	2.6
Royal Dutch Shell plc	RDS-A	B	61.78	7.2	5.5	4.2	8	3.6
Chevron Corporation	CVX	B	59.95	9.3	5.9	4.1	7	3.0
	<i>Median</i>			9.3	6.1	4.9	8	3.0
<b>Producer/Refiners - Large Cap and Mid Cap</b>								
Kinder Morgan, Inc.	KMI	S2	89.69		8.2	15.1	21	3.3
Gazprom (50%)	OGZPF	B	58.60	22.0	12.9	8.6	17	0.6
Suncor Energy	SU	B	53.45	18.1	8.9	7.2	14	0.4
Imperial Oil Limited (30%)	IMO	B	92.67	10.5	6.0	6.6	11	0.9
Petro-Canada	PCZ	B	36.66	5.9	4.9	4.4	7	1.9
Marathon Oil Corporation	MRO	B	61.44	7.1	4.5	4.3	7	1.8
Norsk Hydro ASA	NHY	B	99.25	8.2	5.4	4.3	9	3.1
ConocoPhillips	COP	B	63.02	11.2	5.7	3.9	6	2.0
PetroChina Company Ltd (10%)	PTR	B	77.92	13.9	5.9	3.9	8	4.8
Lukoil Oil Company	LUKOY	B	53.50	19.8	4.6	3.8	6	1.8
	<i>Median</i>			11.2	5.8	4.3	8	1.8
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
XTO Energy Inc.	XTO	B	41.89	11.3	5.5	4.9	9	0.5
Encana Corporation	ECA	B	50.51	7.1	4.2	4.1	7	1.2
CNOOC Limited (29%)	CEO	B	64.10	9.4	5.1	3.9	7	3.6
Burlington Resources	BR	B	71.00	9.9	4.6	3.9	8	0.6
Anadarko Petroleum Corp.	APC	B	91.45	12.5	5.6	3.9	7	0.8
Occidental Petroleum Corp.	OXY	B	75.23	11.3	5.8	3.8	6	1.9
Devon Energy Corporation	DVN	B	63.00	7.3	3.9	3.0	5	0.5
	<i>Median</i>			9.9	5.1	3.9	7	0.8
<b>Independent Natural Gas and Oil - Small Cap</b>								
Berry Petroleum Company	BRY	B	59.13	11.0	5.3	4.9	13	1.0
Encore Acquisition Company	EAC	B	34.56	14.7	6.5	4.8	11	-
Cimarex Energy Company	XEC	B	40.51	7.7	4.0	2.7	5	-
Energy Partners Ltd.	EPL	B	26.00	5.1	3.1	2.2	5	-
	<i>Median</i>			9.3	4.6	3.7	8	-
<b>Income</b>								
Kinder Morgan Energy Partners, L.P.	KMP	S3	51.96		8.3	17.4	29	6.0
Kinder Morgan Management, LLC	KMR	S3	48.49		8.3	16.6	27	6.4
San Juan Basin Royalty Trust	SJT		43.07	12.0	7.7	8.3	9	11.3
Canadian Oil Sands Trust (USS)	COSWF	B	95.57	20.0	10.4	7.7	8	1.8
Pengrowth Energy Trust	PGH		22.78	7.6	5.1	5.7	8	10.3
Enerplus Resources Fund	ERF		45.08	9.8	5.1	5.5	8	9.5
Penn West Energy Trust	PWTFF	B	28.28	8.0	4.1	4.2	6	9.4
	<i>Median</i>			9.8	7.7	7.7	8	9.4

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended September 30, 2006; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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#### Oil and Gas Producers Home Country and Business Segments

	Symbol/ Rating		Non- U.S. Domicile	North Amer. Natural Gas (%)	Rest of World Natural Gas (%)	Oil Prod'n (%)	Down- stream (%)	Total Present Value (US\$mm)
<b>Mega Cap</b>								
Exxon Mobil Corporation	XOM	B		10	19	39	33	492,000
BP plc	BP	B	UK	10	12	44	34	324,000
Royal Dutch Shell plc	RDS-A	B	UK	4	19	33	45	313,000
Chevron Corporation	CVX	B		9	9	54	28	230,000
Total S.A.	TOT	B	France	-	27	38	35	215,000
			<i>Total or Median</i>	9	19	39	34	1,574,000
<b>Producer/Refiners - Large Cap and Mid Cap</b>								
PetroChina Company Ltd.	PTR	B	China	-	9	71	20	213,000
Gazprom	OGZPF	B	Russia		100			190,000
ConocoPhillips	COP	B		13	7	45	35	166,900
Lukoil Oil Company	LUKOY	B	Russia	-	-	62	38	55,700
Norsk Hydro ASA	NHY	B	Norway	-	27	38	35	37,200
Suncor Energy	SU	B	Canada	5	-	89	7	34,900
Marathon Oil Corporation	MRO	B		14	8	33	46	32,900
Imperial Oil Limited	IMO	B	Canada	13	-	62	25	31,900
Petro-Canada	PCZ	B	Canada	23	4	53	20	27,200
			<i>Median</i>	9	7	58	30	790,000
<b>Independent Natural Gas and Oil - Large Cap and Mid Cap</b>								
Occidental Petroleum Corp.	OXY	B		15	1	73	11	54,900
Encana Corporation	ECA	B	Canada	84	-	16	-	54,500
Devon Energy Corporation	DVN	B		62	-	38	-	47,500
Anadarko Petroleum Corp.	APC	B		60	-	40	-	37,500
Burlington Resources	BR	B		69	5	26	-	36,300
CNOOC Limited	CEO	B	China	-	12	88	-	34,800
XTO Energy Inc.	XTO	B		82	-	18	-	21,300
			<i>Median</i>	62	-	38	-	287,000
<b>Independent Natural Gas and Oil - Small Cap</b>								
Cimarex Energy Company	XEC	B		70	-	30	-	6,140
Encore Acquisition Company	EAC	B		27	-	73	-	2,990
Berry Petroleum Company	BRY	B		16	-	84	-	1,920
Energy Partners Ltd.	EPL	B		56	-	44	-	1,860
			<i>Median</i>	42	-	58	-	12,910
<b>Income</b>								
Canadian Oil Sands Trust (US\$)	COSWF	B	Canada	-	-	100	-	14,400
Penn West Energy Trust	PWTFF	B	Canada	43	-	57	-	5,800
Enerplus Resources Fund	ERF		Canada	61	-	39	-	5,070
Pengrowth Energy Trust	PGH		Canada	43	-	57	-	3,720
San Juan Basin Royalty Trust	SJT			100	-	-	-	1,860
			<i>Median</i>	43	-	57	-	30,900

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#### Index of Recent Research

##### Stock Ideas

<u>Date</u>	<u>Symbol</u>	<u>Stock</u>	<u>Theme</u>
14-Oct	OXY	Occidental Petroleum Corporation	Buy Despite Momentum Signal
13-Oct	APC BR DVN OXY XTO		Edge of Panic
7-Oct	ECA IMO PCZ SU		Exaggerated Stock Price Change
5-Oct	RDSA	Royal Dutch Shell plc	Downstream Beneficiary
4-Oct	BR	Burlington Resources, Inc.	Natural Gas Beneficiary
27-Sep	ECA	EnCana Corporation	Canada's Largest Company
26-Sep	LUKOY	Lukoil Oil Company	Adapting to New Russia
22-Sep	MRO	Marathon Oil Corporation	Hurricane Watch
19-Sep	* NHY	Norsk Hydro ASA	Acquiring U.S. Producer for \$2.45 Billion
16-Sep	* XOM	Exxon Mobil Corporation	New Highs Ahead
15-Sep	* OGZPF	Gazprom	The Ultimate Natural Gas Stock
9-Sep	* APC	Anadarko Petroleum Corporation	Natural Gas Jumps
7-Sep	* EPL	Energy Partners, Ltd.	Katrina Survivor
6-Sep	* COP	ConocoPhillips	Refining and Natural Gas Event
30-Aug	* CEO	CNOOC Ltd	Independent Producer with Income
28-Aug	* PTR	PetroChina Company Limited	Income Stock
21-Aug	* PTR	PetroChina Company Limited	Understated Natural Gas Resources
18-Aug	* SJT	San Juan Basin Royalty Trust	Sharp Stock Price Drop
17-Aug	* CVX	Chevron Corporation	Astute Acquisition
16-Aug	* EPL	Energy Partners, Ltd.	Denali 2006
15-Aug	* XEC	Cimarex Energy Company	\$Billion Cash Flow for Small Cap NG Producer
11-Aug	* PWTF	Penn West Energy Trust	Undiscovered by U.S. Investors
11-Aug	* SU	Suncor Energy Inc.	Oil Price and Operating Reliability
11-Aug	* KMx	Kinder Morgan	Canada May Block KM-Terasen Deal
8-Aug	* TOT	Total S.A.	Oil Sands Oui!
3-Aug	* DVN	Devon Energy Corporation	Raise Net Present Value to \$86 a Share
2-Aug	*	26 Stocks - Single Issue Statistics	Raise Net Present Value to \$xx a Share
28-Jul	* EAC	Encore Acquisition Company	HPAI Incline
27-Jul	* BP	BP p.l.c.	Steady-State Growth
22-Jul	* PCZ	Petro-Canada	Approaching Par
22-Jul	* IMO	Imperial Oil Limited	Syncrude Boost
22-Jul	* COSWF	Canadian Oil Sands Trust	Distribution Capability Blossoming
20-Jul	* XTO	XTO Energy Inc.	Simpson Sense
6-Jul	* COSWF	Canadian Oil Sands Trust	Free (Cash Flow) at Last
5-May	* BRY	Berry Petroleum Company	Oil in the Kitty Litter

##### Meter Reader - A Weekly Analysis

17-Oct		Winter Rally
11-Oct	*	Oil, Natural Gas and the U.S. Economy
6-Oct	*	Flash: Industry Outlook Stable
4-Oct	*	Accentuate the Positive

##### Natural Gas and Oil Royalty Trusts - A Weekly Analysis

14-Oct		Fraud on the Street
7-Oct	*	October Jitters
30-Sep	*	Seven Eleven
23-Sep	*	Canada Looks at Income Trusts

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