

Russian Resource Recommendations

Summary and Recommendation

Buy-recommended **Gazprom (OGZPY)** and **Lukoil (LUKOY)** represent 9% and 6% respectively of the illustrative McDep Energy Portfolio because we like their resource potential and we hope that global politics will be supportive. The two stocks give Russian companies 15% weighting in a global mix of U.S. 50%, Canada 19%, Europe 10% and China 6% (see table on page 3, Portfolio Composite of Buy Recommendations). The subject is timely as Russia attempts more independent management of its world leading energy resource potential. On October 9 Gazprom declared that it would develop the giant Arctic natural gas field, Shtokman, without the help of buy-recommended U.S. or European companies **Chevron (CVX)**, **ConocoPhillips (COP)**, **Total (TOT)**, or **Norsk Hydro (NHY)**. Perhaps a decade away, the project can have little quantitative valuation impact today, but the decision is probably directionally positive for Gazprom and a disappointment for the companies that had prepared proposals for joint investment. Meanwhile, on October 18, Lukoil, near 20% owned by COP, plans a half day investor presentation in New York. We think the appeal of potentially high global stock market recognition for Russian companies is a powerful motivator that can keep the politics supportive despite the risks.

Valuation of Russian Stocks Tied to Cash Flow

Unlevered market cash flow multiples for Gazprom and Lukoil are about 7.1 times and 5.6 times respectively within a range of about 4 to 14 for all the stocks in our coverage. Our adjusted reserve life is 24 and 19 years respectively, roughly connoting an exceptional amount of resources relative to current production (see table on page 5, Rank by EV/Ebitda). Thus, moderate, rather than high, cash flow multiple is a measure of allowance for political risk.

Indeed there is political risk in Russia as there is everywhere. Reformers and critics may be dealt with harshly whether they be murdered by unlawful elements or imprisoned by the government in Siberia. Yet, under President Putin, leading energy producers like Gazprom, 50% owned by the government, and Lukoil have made great progress toward becoming globally respected enterprises. We are betting that high, sustainable stock prices are a convincing measure worthy of achieving by Russia or any other country, but won't occur unless the important political actions make sense.

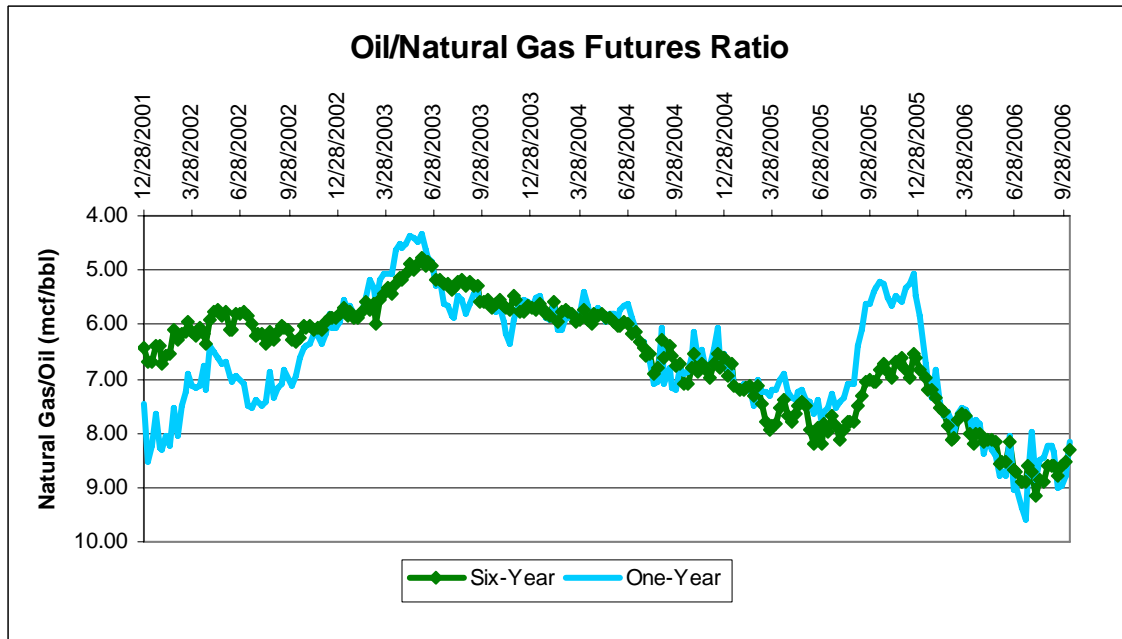
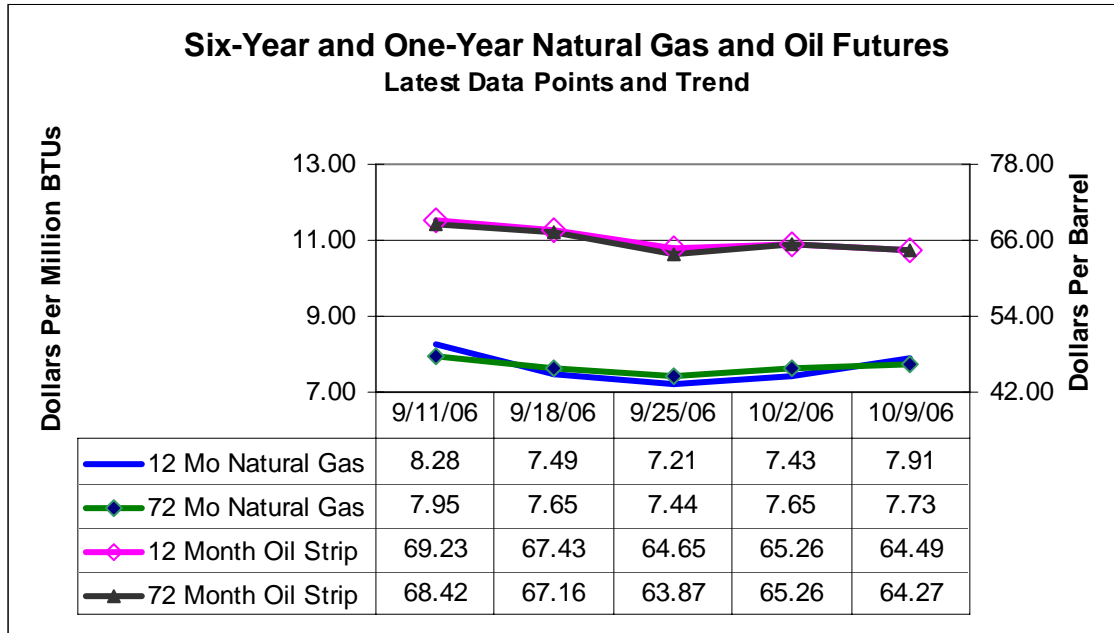
Natural Gas Strengthening Relative to Oil

Meanwhile in the daily global markets, natural gas may be staging a stealth recovery in relative terms. It might seem surprising that while natural gas for delivery in October

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was setting new lows in price and Amaranth and Mother Rock were failing, natural gas for longer one-year and six-year delivery has actually been gaining relative to oil since late July, early August (see chart below, Oil/Natural Gas Futures Ratio).

Kurt H. Wulff, CFA



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**Oil and Gas Producers
Portfolio Composite of Buy Recommendations**

Symbol	Price (US\$/sh) 9-Oct 2006	Portfolio Weight		Non- U.S. Home (%)	North Amer. Natural Gas (%)	Rest of World Natural Gas (%)	Oil Prod'n (%)	Down- stream (%)	McDep Ratio	
		Equity (%)	EV (%)							
Mega Cap										
Exxon Mobil Corporation	XOM	66.55	3.2	2.9		0.2	0.6	1.1	0.8	0.86
Total S.A.	TOT	64.82	2.8	2.9	2.9		0.9	1.2	0.8	0.84
BP plc	BP	64.32	2.7	2.9	2.9	0.2	0.3	1.4	0.9	0.84
Gazprom	OGZPY	44.00	9.5	8.6	8.6		8.6	1.1		0.80
Royal Dutch Shell plc	RDS-A	64.31	2.9	2.9	2.9	0.1	0.5	1.1	1.1	0.79
Chevron Corporation	CVX	63.24	5.8	5.7		0.4	0.6	3.3	1.5	0.75
ConocoPhillips	COP	57.47	4.6	5.7		0.9	0.5	3.0	1.3	0.66
Producer/Refiners - Large Cap and Mid Cap										
Petro-Canada	PCZ	39.42	1.3	1.4	1.4	0.2	0.0	0.9	0.2	0.84
Marathon Oil Corporation	MRO	76.45	1.4	1.4		0.2	0.1	0.5	0.6	0.81
PetroChina Company Ltd.	PTR	105.69	3.2	2.9	2.9		0.2	2.4	0.2	0.76
Norsk Hydro ASA	NHY	21.70	1.4	1.4	1.4		0.4	0.5	0.5	0.74
Suncor Energy	SU	67.51	1.5	1.4	1.4	0.0		1.3	0.1	0.73
Lukoil Oil Company	LUKOY	76.75	6.6	5.7	5.7			4.3	1.4	0.70
Independent Natural Gas and Oil - Large Cap and Mid Cap										
XTO Energy Inc.	XTO	40.90	2.7	2.9		2.2		0.7		0.82
CNOOC Limited	CEO	80.58	3.4	2.9	2.9		0.3	2.6		0.82
Anadarko Petroleum Corp.	APC	41.63	1.4	2.9		1.6		1.2		0.75
Encana Corporation	ECA	45.36	5.6	5.7	5.7	4.0		1.3	0.4	0.73
EOG Resources	EOG	62.82	6.0	5.7		4.4	0.4	0.9		0.71
Occidental Petroleum Corp	OXY	45.09	3.0	2.9		0.3	0.0	2.2	0.3	0.68
Devon Energy Corporatior	DVN	61.55	5.2	5.7		3.1		2.6		0.60
Independent Natural Gas and Oil - Small Cap										
Energy Partners Ltd.	EPL	24.10	0.8	1.4		0.8		0.6		0.88
Berry Petroleum Company	BRY	27.32	1.3	1.4		0.2		1.2		0.76
Encore Acquisition Compe	EAC	24.36	2.2	2.9		0.7		2.1		0.55
Cimarex Energy Company	XEC	33.70	2.8	2.9		1.9		0.9		0.54
Income										
Penn West Energy Trust	PWE	34.89	5.8	5.7	5.7	1.7		4.0		0.91
San Juan Basin Royalty Tr	SJT	35.55	6.7	5.7		5.7				0.89
Canadian Oil Sands Trust	COSWF	25.87	6.0	5.7	5.7			5.7		0.76
Portfolio Composite			100	100	50	29	13	48	10	0.74

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

	Symbol/ Rating		Price (US\$/sh) 9-Oct 2006	Shares (mm)	Market Cap (US\$mm)	Net Present Value (US\$/sh)	Debt/ Present Value	McDep Ratio
Mega Cap								
Exxon Mobil Corporation	XOM	B	66.55	6,030	401,000	78.00	0.04	0.86
Total S.A.	TOT	B	64.82	2,323	151,000	80.00	0.13	0.84
BP plc	BP	B	64.32	3,362	216,000	80.00	0.16	0.84
Gazprom (50%)	OGZPY	B	44.00	2,847	125,300	56.00	0.05	0.80
Royal Dutch Shell plc	RDS-A	B	64.31	3,242	209,000	84.00	0.10	0.79
Chevron Corporation	CVX	B	63.24	2,206	140,000	88.00	0.10	0.75
ConocoPhillips	COP	B	57.47	1,678	96,000	100.00	0.21	0.66
<i>Total or Median</i>					<i>1,338,000</i>		<i>0.10</i>	<i>0.80</i>
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	105.07	135	14,180	33.00	0.75	1.54
Imperial Oil Limited (30%)	IMO	H	32.02	295	9,450	37.00	0.08	0.88
Petro-Canada	PCZ	B	39.42	512	20,180	49.00	0.18	0.84
Marathon Oil Corporation	MRO	B	76.45	367	28,060	98.00	0.14	0.81
PetroChina Company Ltd (10%)	PTR	B	105.69	179	18,920	140.00	0.04	0.76
Norsk Hydro ASA	NHY	B	21.70	1,247	27,060	31.00	0.14	0.74
Suncor Energy	SU	B	67.51	461	31,130	95.00	0.06	0.73
Lukoil Oil Company	LUKOY	B	76.75	830	64,000	110.00	0.01	0.70
<i>Total or Median</i>					<i>213,000</i>		<i>0.11</i>	<i>0.79</i>
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	40.90	369	15,090	52.00	0.18	0.82
CNOOC Limited (29%)	CEO	B	80.58	119	9,610	98.00	-	0.82
Anadarko Petroleum Corp.	APC	B	41.63	463	19,300	75.00	0.43	0.75
Encana Corporation	ECA	B	45.36	845	38,300	65.00	0.12	0.73
EOG Resources	EOG	B	62.82	246	15,500	92.00	0.07	0.71
Occidental Petroleum Corp.	OXY	B	45.09	868	39,100	69.00	0.08	0.68
Devon Energy Corporation	DVN	B	61.55	446	27,500	115.00	0.13	0.60
<i>Total or Median</i>					<i>164,000</i>		<i>0.12</i>	<i>0.73</i>
Independent Natural Gas and Oil - Small Cap								
Energy Partners Ltd.	EPL	B	24.10	75	1,810	31.00	0.44	0.88
Berry Petroleum Company	BRY	B	27.32	45	1,230	39.00	0.19	0.76
Encore Acquisition Company	EAC	B	24.36	54	1,300	54.00	0.19	0.55
Cimarex Energy Company	XEC	B	33.70	85	2,860	68.00	0.09	0.54
<i>Total or Median</i>					<i>7,200</i>		<i>0.19</i>	<i>0.65</i>
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	43.35	165	7,140	15.00	0.56	1.83
Kinder Morgan Management, LLC	KMR	S3	41.43	60	2,470	15.00	0.56	1.78
Enerplus Resources Fund	ERF		49.83	123	6,130	47.00	0.11	1.05
Pengrowth Energy Trust	PGH		18.45	161	2,980	20.00	0.17	0.94
Penn West Energy Trust	PWE	B	34.89	246	8,580	39.00	0.13	0.91
San Juan Basin Royalty Trust	SJT	B	35.55	47	1,660	40.00	-	0.89
Canadian Oil Sands Trust	COSWF	B	25.87	466	12,060	35.00	0.09	0.76
<i>Total or Median</i>					<i>41,000</i>		<i>0.13</i>	<i>0.94</i>

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

Present Value = Shares times Net Present Value divided by (1-Debt/Present Value).

Debt = Present Value times Debt/Present Value

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 (US\$/sh) 9-Oct 2006	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
Mega Cap								
Gazprom (50%)	OGZPY	B	44.00	24.0	9.0	7.1	11	0.5
BP plc	BP	B	64.32	9.3	7.2	6.0	10	3.7
Exxon Mobil Corporation	XOM	B	66.55	11.4	6.7	5.8	10	1.9
Total S.A.	TOT	B	64.82	9.8	6.7	5.6	10	3.2
Chevron Corporation	CVX	B	63.24	10.9	6.2	4.6	8	3.3
Royal Dutch Shell plc	RDS-A	B	64.31	7.4	5.9	4.6	8	3.9
ConocoPhillips	COP	B	57.47	11.3	6.2	4.1	6	2.5
	<i>Median</i>			10.9	6.7	5.6	10	3.2
Producer/Refiners - Large Cap and Mid Cap								
Kinder Morgan, Inc.	KMI	S2	105.07		8.8	13.5	22	3.3
Suncor Energy	SU	B	67.51	18.8	10.9	7.9	15	0.3
Imperial Oil Limited (30%)	IMO	H	32.02	10.5	8.1	7.1	12	0.9
Petro-Canada	PCZ	B	39.42	6.8	7.1	6.0	11	0.9
Lukoil Oil Company	LUKOY	B	76.75	18.9	8.0	5.6	9	1.6
PetroChina Company Ltd (10%)	PTR	B	105.69	14.7	6.5	4.9	10	4.6
Norsk Hydro ASA	NHY	B	21.70	7.9	5.7	4.2	8	3.1
Marathon Oil Corporation	MRO	B	76.45	8.6	4.8	3.9	6	1.7
	<i>Median</i>			10.5	7.5	5.8	10	1.7
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	40.90	11.6	8.7	7.1	13	0.5
Anadarko Petroleum Corp.	APC	B	41.63	11.5	8.8	6.6	12	1.7
EOG Resources	EOG	B	62.82	9.7	9.2	6.5	15	0.4
Encana Corporation	ECA	B	45.36	8.7	7.5	5.5	13	0.9
Occidental Petroleum Corp.	OXY	B	45.09	10.6	7.5	5.1	10	2.0
Devon Energy Corporation	DVN	B	61.55	8.7	7.8	4.7	9	0.7
CNOOC Limited (29%)	CEO	B	80.58	10.6	5.6	4.6	8	3.5
	<i>Median</i>			10.6	7.8	5.5	12	0.9
Independent Natural Gas and Oil - Small Cap								
Berry Petroleum Company	BRY	B	27.32	9.9	7.6	5.8	13	1.1
Energy Partners Ltd.	EPL	B	24.10	6.2	5.8	5.1		-
Encore Acquisition Company	EAC	B	24.36	14.9	8.6	4.7	11	-
Cimarex Energy Company	XEC	B	33.70	7.8	7.3	3.9	9	0.5
	<i>Median</i>			8.9	7.4	4.9	11	0.2
Income								
Kinder Morgan Energy Partners, L.P.	KMP	S3	43.35		7.9	14.5	23	7.5
Kinder Morgan Management, LLC	KMR	S3	41.43		7.9	14.1	22	7.8
San Juan Basin Royalty Trust	SJT	B	35.55	9.3	12.0	10.7	13	7.4
Canadian Oil Sands Trust	COSWF	B	25.87	24.4	12.8	9.7	13	7.3
Enerplus Resources Fund	ERF		49.83	9.4	7.9	8.3	19	9.1
Penn West Energy Trust	PWE	B	34.89	8.0	8.4	7.6	13	10.5
Pengrowth Energy Trust	PGH		18.45	7.9	7.1	6.7	10	14.6
	<i>Median</i>			9.3	7.9	9.7	13	7.8

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended September 30, 2007; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses

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Index of Recent Research**Stock Ideas**

<u>Date</u>	<u>Symbol</u>	<u>Stock</u>	<u>Theme</u>
6-Oct	ECA	EnCana Corporation	Raise NPV to \$65 a Share
6-Oct	COP	ConocoPhillips	Oil Sands Link with Encana
5-Oct	OGZPY	Gazprom	Russian Natural Gas Price Too Low
5-Oct	APC	Anadarko Petroleum Corporation	Financial Risk Declines
19-Sep	IMO	Imperial Oil Limited	Change to Hold on Oil Price Momentum
15-Sep	PTR	PetroChina Company Limited	Future Natural Gas and Downstream Profits
15-Sep	SJT	San Juan Basin Royalty Trust	Sub \$5 Natural Gas and SJT
7-Sep	* EPL	Energy Partners, Ltd.	Woodside Offers \$23 a Share
6-Sep	* DVN	Devon Energy Corporation	Raise NPV to \$115 a Share
29-Aug	* CEO	CNOOC Ltd	Volume Growth and Commodity Price
23-Aug	* PTR	PetroChina Company Limited	Profits despite Government Limits
15-Aug	* PWTF	Penn West Energy Trust	Marketable High Current Income
10-Aug	* BRY	Berry Petroleum	Oil Rich
10-Aug	* EPL	Energy Partners, Ltd.	Gulf of Mexico and Natural Gas
7-Aug	* OXY	Occidental Petroleum Corporation	Positive Profit and Volume Trends
4-Aug	* EAC	Encore Acquisition Company	Abundant Appreciation Potential
4-Aug	* SU	Suncor Energy Inc.	Trading Oil Sands Leadership
4-Aug	* TOT	Total S.A.	Positioned to Profit
3-Aug	* XEC	Cimarex Energy Company	Volume Slippage
3-Aug	* DVN	Devon Energy Corporation	Best Value Large Cap Producer
2-Aug	* MRO	Marathon Oil Corporation	Raise NPV to \$98 a Share
2-Aug	* EOG	EOG Resources Inc.	Add Natural Gas to Your Portfolio
28-Jul	* CVX	Chevron Corporation	Lagging a Little Lately
28-Jul	* XOM	Exxon Mobil Corporation	Volume and Cash Advancing
28-Jul	* PCZ	Petro-Canada	Temporary Difficulties
28-Jul	* RDSA	Royal Dutch Shell plc	Share Buyback Enhances Return
26-Jul	* BP	BP p.l.c.	Cash Flow per Barrel Lags
26-Jul	* COSWF	Canadian Oil Sands Trust	0.7% Opportunity Loss
26-Jul	* XTO	XTO Energy Inc.	Growth Standout
25-Jul	* NHY	Norsk Hydro ASA	Commodity Price Beneficiary
20-Jul	* KMx	Kinder Morgan	Focus Sharpens on Limited Partners
30-Jun	* LUKOY	Lukoil Oil Company	Russia Stronger than Ever

Meter Reader - A Weekly Analysis

10-Oct		Russian Resource Recommendations
3-Oct	*	Value Buoyed by Calendar and Chart
26-Sep	*	Seasonal Scare
19-Sep	*	Oil Price Breaks Trend

Natural Gas and Oil Royalty Trusts - A Weekly Analysis

6-Oct		Basic Reasons
29-Sep		Mesa Royalty Trust Liquidity Opportunity
22-Sep	*	Sub \$5 Natural Gas and CRT
15-Sep	*	Sub \$5 Natural Gas and SJT

Industry Ideas

27-Jun	*	Presentation Slides	Oil and Gas Investment to 2010
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* Archived on www.mcdep.com

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