



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 11, 2010

President Jimmy Obama Bright Outlook for Pure Play Oil and Gas

Summary and Recommendation

Bottom Line Cash Payers including two buy-recommendations **Hugoton Royalty Trust (HGT)** and **San Juan Basin Royalty Trust (SJT)** along with peers **Mesa Royalty Trust (MTR)**, **Legacy Reserves, L.P. (LGCY)** and **Linn Energy (LINE)** are trending upward in stock price defined by current quote above the 200-day average. Only **Encore Energy Partners (ENP)** in the six stock group trades below its 200-day average as its general partner may be preparing to acquire the public units. McDep Ratios close to or above 1.0 suggest that the stocks are reasonably valued on expected oil and gas prices and investors would receive most of their return in cash distributions. Yet the strong performance of small cap and income stocks combined with the anti-oil rhetoric from our political leader takes us back mentally to 1977, the second year in the term of President Carter. The last two years of the Carter era, 1979 to 1980, were the best ever for oil and gas stocks. The more our leaders of that time punished oil companies, the higher oil price, gas price and gold price climbed. As political hot air drove investors to real assets, MTR was spawned in 1979 and SJT in 1980. Thus, while there may be a case for rebalancing holdings of stocks that have advanced to McDep Ratios above 1.0, we believe the underlying long-term trend is upward. Oil for the next six years is tracking at \$85 a barrel compared to the 40-week average of \$86 a barrel. Near-month natural gas tracks above the 200-day average perhaps pointing the way for six-year natural gas to resume an uptrend in the next few months above the 40-week average of about \$6.40 a million btu.

Investors would receive a projected distribution yield ranging from 6-12% for the next twelve months for the six stocks (see Table 1 on page 2). Ranking by McDep Ratio appears inverse to ranking by yield after considering concentration on oil and gas. Oil production leads to a higher yield than gas production perhaps in part because investors expect oil price to increase less than natural gas price in the future. Royalty Trusts have no debt as required by their structure while LINE, LGCY and ENP actively use borrowed funds (see Table 2 on page 3). LINE and ENP use the proceeds of hedging to pay more than can be sustained without hedging or allowing for debt repayment (see Table 3 on page 4). Cash flow multiples line up roughly with reserve life except for MTR where we believe the reported reserve life understates what would be a measure more comparable to peers.

The importance of whether the resource is natural gas or oil as it affects the cash flow multiple and reserve life relationship becomes more apparent in models for each stock (see tables [Functional Cash Flow and Present Value](#) on pages 5-6). We find that more detailed estimates of present value of future cash flow are handily characterized by the cash flow multiple and reserve life relationship. Cash flow and distribution estimates are updated weekly.

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June 11, 2010

						<i>Present Value by Segment (%)</i>					
<i>Symbol/Rating</i>	<i>(US\$/sh)</i>	<i>EV/</i>	<i>Enterprise</i>			<i>N.Amer.</i>			<i>Dist.</i>	<i>Dist.</i>	
B = Buy	10-Jun	Market	Value	Natural	Oil	NTM	Yield	McDep			
CB (see below)	2010	Cap	(\$mm)	Gas	Prod'n	(\$/un)	(%)	Ratio			
Canadian Income Trusts (US\$)											
Peyto Energy Trust	PEYUF	14.42	1.24	2,160	76	24	1.36	9.4	0.97		
Pengrowth Energy Trust	PGH	9.54	1.46	4,100	39	61	0.79	8.3	0.91		
Penn West Energy Trust	PWE	19.48	1.39	11,600	23	77	1.70	8.7	0.88		
Enerplus Resources Fund	ERF	22.54	1.22	4,900	42	58	2.04	9.1	0.79		
Canadian Oil Sands Trust	COSWF	CB	27.09	1.10	14,400		100	1.89	7.0	0.73	
<i>Total or Median</i>					37,200						0.88
Small Cap Independent Producers											
Range Resources	RRC	49.34	1.24	9,460	81	19	0.08	0.2	1.27		
Petro-Hawk	HK	20.77	1.45	8,830	97	3	-	-	1.16		
Cimarex Energy Company	XEC	B	77.79	1.09	7,260	66	34	0.32	0.4	1.03	
Ultra Petroleum	UPL	49.83	1.15	8,750	94	6	-	-	0.99		
Berry Petroleum Company	BRY	32.08	1.65	2,710	31	69	0.30	0.9	0.95		
Whiting Petroleum Corporation	WLL	87.41	1.23	6,050	13	87	-	-	0.90		
Birchcliff Energy Ltd. (US\$)	BIREF	B	9.89	1.19	1,500	65	35	-	-	0.74	
<i>Total or Median</i>					43,100						1.01
Top Line Cash Payers											
Sabine Royalty Trust	SBR	49.68	1.00	720	50	50	3.35	6.7	1.10		
Cross Timbers Royalty Trust	CRT	37.10	1.00	220	75	25	2.28	6.1	1.09		
Permian Basin RT	PBT	18.73	1.00	870	38	62	1.16	6.2	1.04		
Freehold Royalty Trust (US\$)	FRHLF	16.34	1.08	1,030	25	75	1.59	9.7	0.96		
Dorchester Minerals, L.P.	DMLP	B	25.50	1.02	780	71	29	1.77	6.9	0.95	
<i>Total or Median</i>					3,600						1.04
Bottom Line Cash Payers											
San Juan Basin Royalty Trust	SJT	B	26.70	1.00	1,240	100	-	1.45	5.4	1.16	
Linn Energy, LLC	LINE	25.59	1.46	5,390	42	58	2.52	9.8	1.14		
Legacy Reserves L.P.	LGCY	22.61	1.39	1,230	16	84	2.08	9.2	1.09		
Mesa Royalty Trust	MTR	48.23	1.00	90	75	25	3.79	7.9	1.01		
Hugoton Royalty Trust	HGT	B	20.99	1.00	840	90	10	1.60	7.6	1.00	
Encore Energy Partners, L.P. (52%)	ENP	16.68	1.35	530	23	77	2.00	12.0	0.99		
<i>Total or Median</i>					9,300						1.05
Composite (excl COSWF)											
<i>Enterprise Value Weighting</i>					80,300	57	43				1.00
<i>Equal Weighting</i>						56	44				1.01
<i>Equal Weighted Buys</i>						66	34				0.98

CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.

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

Present Value presumes long-term prices of \$75 a barrel for oil and \$8 a million btu for natural gas.

Dist. = Income distribution. NTM = Next Twelve Months Ended March 31, 2011. Enterprise Value = Market Cap and Debt.



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 11, 2010

Table 2

McDep Income and Small Cap Energy Portfolio Net Present Value and McDep Ratio

			<i>Price</i>			<i>Net</i>		
			<i>(\$/sh)</i>		<i>Market</i>	<i>Present</i>	<i>Debt/</i>	
	<i>Symbol/</i>		<i>10-Jun</i>	<i>Shares</i>	<i>Cap</i>	<i>Value</i>	<i>Present</i>	<i>McDep</i>
	<i>Rating</i>		<i>2010</i>	<i>(mm)</i>	<i>(\$mm)</i>	<i>(\$/un)</i>	<i>Value</i>	<i>Ratio</i>
Canadian Income Trusts (US\$)								
Peyto Energy Trust	PEYUF		14.42	120.5	1,740	15.00	0.19	0.97
Pengrowth Energy Trust	PGH		9.54	290.0	2,770	11.00	0.29	0.91
Penn West Energy Trust	PWE		19.48	428.3	8,340	23.00	0.25	0.88
Enerplus Resources Fund	ERF		22.54	178.0	4,010	30.00	0.14	0.79
Canadian Oil Sands Trust	COSWF	CB	27.09	484.0	13,110	38.00	0.07	0.73
<i>Total or Median</i>					<i>30,000</i>		<i>0.19</i>	<i>0.88</i>
Small Cap Independent Producers								
Range Resources	RRC		49.34	160.0	7,630	35.00	0.25	1.27
Petro-Hawk	HK		20.77	303.0	6,080	16.00	0.36	1.16
Cimarex Energy Company	XEC	B	77.79	85.4	6,640	75.00	0.09	1.03
Ultra Petroleum	UPL		49.83	154.0	7,590	50.00	0.13	0.99
Berry Petroleum Company	BRY		32.08	51.0	1,640	35.00	0.37	0.95
Whiting Petroleum Corporation	WLL		87.41	59.2	4,910	95.00	0.17	0.90
Birchcliff Energy Ltd. (US\$)	BIREF	B	9.89	127.0	1,260	14.00	0.12	0.74
<i>Total or Median</i>					<i>35,750</i>		<i>0.17</i>	<i>0.99</i>
Top Line Cash Payers								
Sabine Royalty Trust	SBR		49.68	14.6	720	45.00	-	1.10
Cross Timbers Royalty Trust	CRT		37.10	6.0	220	34.00	-	1.09
Permian Basin RT	PBT		18.73	46.6	870	18.00	-	1.04
Freehold Royalty Trust (US\$)	FRHLF		16.34	58.4	950	17.00	0.07	0.96
Dorchester Minerals, L.P.	DMLP	B	25.50	29.8	760	27.00	0.02	0.95
<i>Total or Median</i>					<i>3,520</i>			<i>1.04</i>
Bottom Line Cash Payers								
San Juan Basin Royalty Trust	SJT	B	26.70	46.6	1,240	23.00	-	1.16
Linn Energy, LLC	LINE		25.59	144.0	3,690	21.00	0.36	1.14
Legacy Reserves L.P.	LGCY		22.61	39.2	890	20.00	0.31	1.09
Mesa Royalty Trust	MTR		48.23	1.9	90	48.00	-	1.01
Hugoton Royalty Trust	HGT	B	20.99	40.0	840	21.00	-	1.00
Encore Energy Partners, L.P. (52%)	ENP		16.68	23.4	390	17.00	0.26	0.99
<i>Total or Median</i>					<i>7,140</i>			<i>1.05</i>

B=Buy; CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.

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

Present Value presumes long-term prices of \$75 a barrel for oil and \$8 a million btu for natural gas.



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 11, 2010

Table 3

McDep Income and Small Cap Energy Portfolio Value Multiples - Rank by EV/Ebitda

			<i>Price</i>	<i>Revenue</i>	<i>Dist/</i>	<i>Adjstd</i>	
	<i>Symbol/</i>		<i>(\$/sh)</i>	<i>Royalty</i>	<i>Equity</i>	<i>Resrvs/</i>	<i>PV/</i>
	<i>Rating</i>		<i>10-Jun</i>	<i>(%)</i>	<i>Ebitda</i>	<i>Prod</i>	<i>Ebitda</i>
			<i>2010</i>			<i>NTM</i>	<i>NTM</i>
						<i>NTM</i>	<i>NTM</i>
Canadian Income Trusts (US\$)							
Peyto Energy Trust	PEYUF		14.42		1.01	23.1	11.1
Canadian Oil Sands Trust	COSWF	CB	27.09		0.66	31.0	13.2
Penn West Energy Trust	PWE		19.48		0.66	9.9	9.0
Pengrowth Energy Trust	PGH		9.54		0.58	9.9	8.0
Enerplus Resources Fund	ERF		22.54		0.58	9.7	8.6
	<i>Median</i>					9.9	9.0
Small Cap Independent Producers							
Range Resources	RRC		49.34		-	13.2	10.7
Ultra Petroleum	UPL		49.83		-	14.1	11.3
Birchcliff Energy Ltd. (US\$)	BIREF	B	9.89		-	22.4	14.4
Petro-Hawk	HK		20.77		-	7.1	8.1
Berry Petroleum Company	BRY		32.08		-	13.1	8.0
Whiting Petroleum Corporation	WLL		87.41		-	10.3	7.7
Cimarex Energy Company	XEC	B	77.79		-	6.4	5.5
	<i>Median</i>					13.1	8.1
Top Line Cash Payers							
Cross Timbers Royalty Trust	CRT		37.10	84	0.96	13.5	14.3
Sabine Royalty Trust	SBR		49.68	100	1.00	9.1	13.4
Permian Basin RT	PBT		18.73	42	0.89	13.3	13.8
Dorchester Minerals, L.P.	DMLP	B	25.50	77	0.91	7.5	13.9
Freehold Royalty Trust (US\$)	FRHLF		16.34	71	0.86	8.6	9.3
	<i>Median</i>					9.1	13.8
Bottom Line Cash Payers							
Linn Energy, LLC	LINE		25.59		1.57	20.0	13.1
San Juan Basin Royalty Trust	SJT	B	26.70		0.80	14.8	12.6
Hugoton Royalty Trust	HGT	B	20.99		0.90	12.4	11.8
Mesa Royalty Trust	MTR		48.23		0.92	9.2	11.6
Legacy Reserves L.P.	LGCY		22.61		0.91	12.0	8.8
Encore Energy Partners, L.P.	ENP		16.68		1.14	12.9	9.7
	<i>Median</i>					12.7	11.7

B=Buy; CB=Contrarian Buy, Stock Price apparently 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
 Top Line Cash Payers defined as those having Revenue Royalty (see fifth column from right).



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 11, 2010

San Juan Basin Royalty Trust					
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>	
North American Natural Gas	85	14.8	12.6	1,070	100%
	85	14.8	12.6	1,070	100%
Debt (US\$mm)					-
Net Present Value (US\$mm)					1,070
Shares (mm)					47
Net Present Value - Standard Estimate (US\$/sh)					23

Hugoton Royalty Trust					
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>	
North American Natural Gas	62	12.5	12.3	760	90%
Oil	9	11.1	7.6	70	8%
	71	12.4	11.8	840	100%
Debt (US\$mm)					-
Net Present Value (US\$mm)					840
Shares (mm)					40
Net Present Value - Standard Estimate (US\$/sh)					21

Mesa Royalty Trust					
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>	
North American Natural Gas	4.8	9.2	13.2	63	
Oil	2.9	9.1	8.8	26	
	7.7	-	11.6	89	100%
Debt (US\$mm)					-
Net Present Value (US\$mm)					89
Units (mm)					1.86
Net Present Value - Standard Estimate (US\$/sh)					48



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 11, 2010

Linn Energy, LLC					
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>	
North American Natural Gas	134	18.6	14.9	2,000	42%
Oil	227	21.6	11.9	2,710	58%
	361	20.0	13.0	4,710	100%
Debt (US\$mm)					1,710
Net Present Value (US\$mm)					3,000
Shares (mm)					144
Net Present Value - Standard Estimate (US\$/sh)					21

Legacy Reserves L.P.					
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>	
North American Natural Gas	20	11.1	8.9	180	16%
Oil	108	12.3	8.8	950	84%
	129	12.0	8.8	1,130	100%
Debt (US\$mm)					350
Net Present Value (US\$mm)					780
Shares (mm)					39
Net Present Value - Standard Estimate (US\$/sh)					20

Encore Energy Partners					
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>	
North American Natural Gas	19	13.7	12.4	240	23%
Oil	87	12.5	9.1	790	77%
	106	12.9	9.7	1,030	100%
Debt (US\$mm)					260
Net Present Value (US\$mm)					770
Shares (mm)					45
Net Present Value - Standard Estimate (US\$/sh)					17



Income and Small Cap Weekly

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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 thirty 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.