



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Volume Upside in Top Line Cash Payers FRHLF, PBT, SBR, DMLP and CRT

Summary and Recommendation

The outlook for sustaining 7% a year distributions by income stocks that collect a percentage off the top appears to be strengthening as the spreading boom in horizontal oil boosts underlying production volume. Signs are increasingly evident of a renaissance in U.S. oil production (see *Meter Reader*, [Horizontal Oil Leads Renewed U.S. Oil Growth](#), September 13, 2011). Producers are also stepping up activity in Western Canada where horizontal oil is at an earlier stage of development. As a result, we can begin to see improving volume trends and some pickup in distributions (see charts [Volume](#) and [Distribution](#) on page 2). We may see rebounding volumes in 2012 for **Freehold Royalties, Ltd. (FRHLF)**, the largest top line cash payer we have uncovered among publicly traded Canadian oil and gas companies (see table [Freehold](#) on page 3). FRHLF pays the highest dividend at 9.6% a year (see Table ISC-1 on page 3). Next most concentrated on oil at 58% of present value, **Permian Basin Royalty Trust (PBT)** has concentrated interests in Crane County and other areas in West Texas. Though little change in trend is evident yet in PBT oil volume, intense industry activity in the Permian Basin is a positive sign. Horizontal natural gas has boosted volume for **Sabine Royalty Trust (SBR)** while horizontal oil may boost future volume for the trust's royalties in West Texas. Contrarian Buy **Dorchester Minerals L.P. (DMLP)** has also scored horizontal natural gas gains and is beginning to see horizontal oil gains from North Dakota where the horizontal oil trend is most advanced.

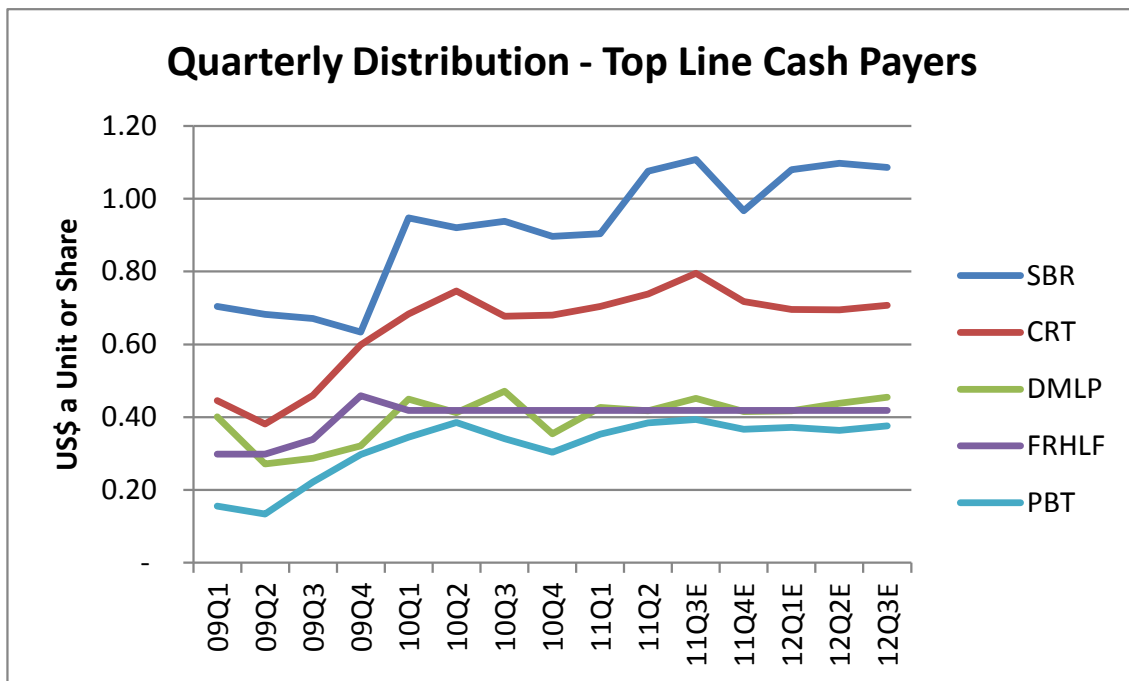
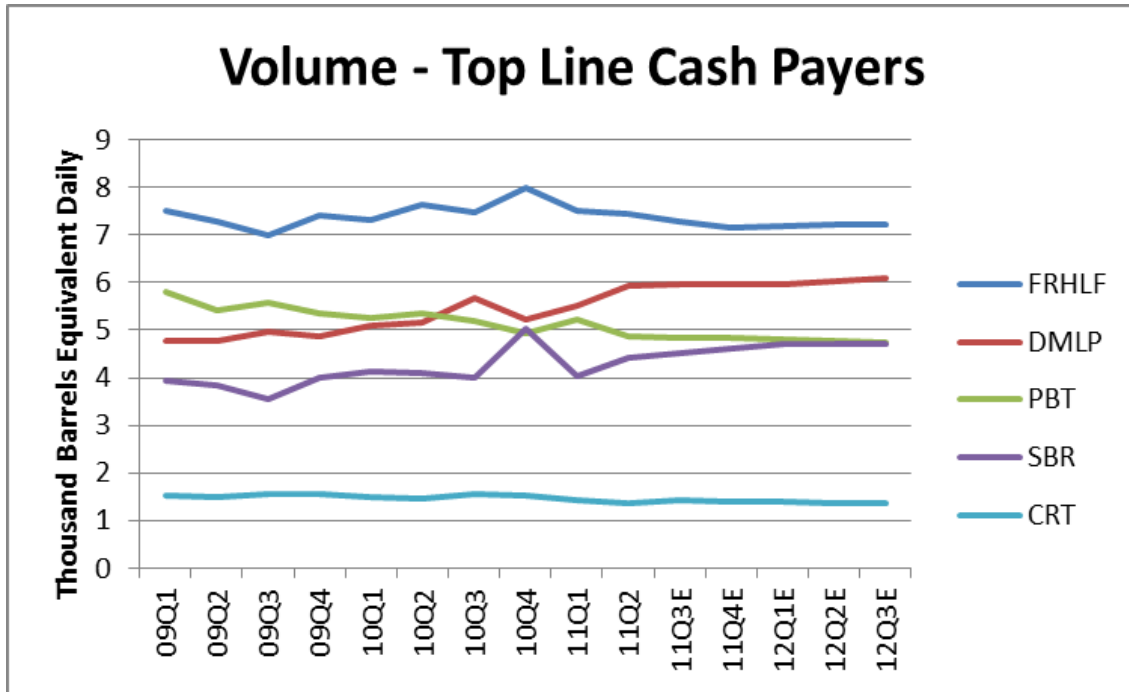
Expect 7% Real Return at McDep Ratio of 1.0

Coincidentally distribution yield nearly matches our expected real return in estimating present value. If the distribution yield were 7% real for a long time it would be analogous to a long-term, inflation-linked bond priced at par with a 7% real annual coupon. The 30-year U.S. Treasury Inflation Protected Security has a real yield of about 1%. The main stock-specific variable affecting present value is the volume trend. The higher the rate of decline as normally exhibited by oil and gas properties, the higher the annual cash flow must be relative to value. If volume is near constant instead, the valuation of a top line cash payer is more like that of a bond and present value and stock price can be higher accordingly (see Tables ISC-2-4 on pages 5-7).

Freehold Royalty Fits Better in a Retirement, Pension or Endowment Account

U.S. investors in FRHLF should be aware that the dividend is taxable as ordinary income as it does not qualify for the maximum 15% tax rate in effect for 2011 and 2012. That penalty can be reduced or eliminated in a tax-exempt or tax-deferred account. Initially there may be a 15% Foreign Tax withheld that may be avoided on application to the Canadian payer. For FRHLF the letter requesting exemption should be sent to Computer Share Trust Company of Canada.

Kurt H. Wulff, CFA





Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Freehold Royalty Trust									
Next Twelve Months Operating and Financial Estimates									
(Canadian dollars)									
									<i>Next</i>
									<i>Twelve</i>
	<i>Q3</i>	<i>Q2</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Months</i>
	<i>9/30/10</i>	<i>6/30/11</i>	<i>9/30/11</i>	<i>12/31/11</i>	<i>2011E</i>	<i>3/31/12</i>	<i>6/30/12</i>	<i>9/30/12</i>	<i>9/30/12</i>
Volume									
Natural Gas (mmcf)	16.9	17.9	17.5	17.2	17.1	17.2	17.2	16.8	17.1
Days	92	91	92	92	365	91	91	92	366
Oil (mbd)	4.68	4.46	4.37	4.28	4.5	4.33	4.37	4.41	4.3
Total gas & oil (bcf)	4.1	4.1	4.0	3.9	16.1	3.9	3.9	4.0	15.8
Total gas & oil (mbd)	7.5	7.4	7.3	7.1	7.3	7.2	7.2	7.2	7.2
Price									
Natural gas (\$/mcf)									
Henry Hub (US\$/mmbtu)	4.38	4.32	4.19	4.01	4.16	4.30	4.29	4.40	4.25
Currency (US\$/C\$)	0.96	1.03	1.00	1.00	1.01	1.00	1.00	1.00	1.00
Henry Hub (C\$/mmbtu)	4.55	4.18	4.18	4.00	4.10	4.28	4.28	4.38	4.24
Company (C\$/mcf)	3.20	3.36	3.36	3.22	3.25	3.45	3.44	3.53	3.41
Oil (\$/bbl)									
WTI Cushing (US\$)	76.08	102.55	90.48	88.36	93.87	89.11	89.40	89.87	89.18
WTI Cushing (C\$/bbl)	79.05	99.21	90.17	88.06	92.59	88.81	89.09	89.57	88.88
Company (C\$/bbl)	62.87	82.69	75.15	73.39	75.54	74.02	74.26	74.65	74.08
Total gas & oil (\$/mcf)	7.74	9.60	8.85	8.62	8.99	8.79	8.84	8.97	8.81
Revenue (\$mm)									
Natural Gas	5.0	5.5	5.4	5.1	20	5.4	5.4	5.5	21
Oil	27.0	33.6	30.2	28.9	124	29.1	29.5	30.3	118
Other	(0.3)	0.6			0				-
Total	31.7	39.6	35.6	34.0	145	34.5	34.9	35.8	139
Expense	6.6	5.7	6.9	6.6	26	6.7	6.8	6.9	27
Ebitda (\$mm)	25.1	33.9	28.7	27.4	119	27.8	28.1	28.8	112
Deprec., Deplet., & Amort.	17.4	11.7	11.7	11.7	47	11.7	11.7	11.7	47
Other					-				-
Ebit	7.7	22.2	17.0	15.7	71	16.1	16.4	17.1	65
Interest	0.8	0.9	0.9	0.9	4	0.9	0.9	0.9	4
Ebt	6.9	21.3	16.1	14.8	68	15.2	15.5	16.2	62
Income Tax	(1.9)	4.6	4.0	3.7	12	3.8	3.9	4.1	15
Net Income (\$mm)	8.8	16.7	12.1	11.1	55	11.4	11.7	12.2	46
Units (millions)	58.5	59.8	59.8	59.8	59.7	59.8	58.4	58.4	59.1
Per unit (\$)	0.15	0.28	0.20	0.19	0.93	0.19	0.20	0.21	0.78
Ebitda Margin - O&G	79%	86%	81%	81%	82%	81%	81%	81%	81%
Tax Rate	-28%	22%	25%	25%	18%	25%	25%	25%	25%
Distribution (\$mm)	24.6	25.1	25.1	25.1	100	25.1	24.5	24.5	99
Per unit (\$)	0.42	0.42	0.42	0.42	1.68	0.42	0.42	0.42	1.68



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Table ISC-1											
McDep Income and Small Cap Energy Portfolio											
Debt, Segments, Cash Flow, Income and McDep Ratio											
			Price								
Symbol/Rating		(US\$/sh)	EV/	Enterprise	PV(%)		EV/	Dist.	Dist.		
B = Buy	15-Sep	Market	Value	Nat	Oil	Ebitda	NTM	Yield	McDep		
CB (see below)	2011	Cap	(\$mm)	Gas		NTM	(\$/un)	(%)	Ratio		
Small Cap Independent Producers											
Range Resources	RRC	B	63.27	1.20	12,040	69	31	15.1	0.16	0.3	0.92
Peyto Exploration and Developmen	PEYUF		21.56	1.17	3,370	76	24	9.9	0.74	3.4	0.91
Birchcliff Energy Ltd.	BIREF	B	13.51	1.21	2,150	56	44	13.1	-	-	0.87
Berry Petroleum Company	BRY		47.70	1.57	4,100	23	77	7.8	0.30	0.6	0.77
Denbury Resources Inc.	DNR		14.64	1.40	8,270	5	95	6.6	-	-	0.60
Cimarex Energy Company	XEC	CB	68.21	1.12	6,600	46	54	5.2	0.40	0.6	0.60
Whiting Petroleum Corporation	WLL	CB	45.63	1.30	7,030	11	89	4.5	-	-	0.57
<i>Total or Median</i>					43,600			7.8			0.77
Top Line Cash Payers											
Cross Timbers Royalty Trust	CRT		46.00	1.00	280	87	13		2.82	6.1	1.02
Permian Basin RT	PBT		22.14	1.00	1,030	42	58		1.48	6.7	1.01
Sabine Royalty Trust	SBR		63.51	1.00	930	51	49		4.23	6.7	0.91
Freehold Royalties Ltd.	FRHLF		17.64	1.06	1,110	18	82		1.69	9.6	0.81
Dorchester Minerals, L.P.	DMLP	CB	23.55	1.00	720	61	39		1.73	7.3	0.78
<i>Total or Median</i>					4,100					6.7	0.91
Bottom Line Cash Payers											
Linn Energy, LLC	LINE		37.83	1.47	9,760	31	69	15.5	2.76	7.3	1.07
Hugoton RoyaltyTrust	HGT	B	22.54	1.00	900	88	13	14.7	1.31	5.8	1.03
Vanguard Natural Resources, LLC	VNR		27.57	1.46	2,050	23	77	10.8	2.30	8.3	1.01
San Juan Basin Royalty Trust	SJT		23.77	1.00	1,110	100	-	13.9	1.41	5.9	0.95
Legacy Reserves L.P.	LGCY		27.20	1.48	1,750	21	79	9.3	2.16	7.9	0.93
Mesa RoyaltyTrust	MTR		45.46	1.00	85	75	25	13.4	2.84	6.2	0.86
Enerplus Corporation	ERF	CB	27.47	1.22	6,000	30	70	7.8	2.17	7.9	0.78
<i>Total or Median</i>					21,700			13.4		7.3	0.95
Composite											
<i>Enterprise Value Weighting</i>					69,300	38	62				0.78
<i>Equal Weighting</i>						48	52				0.86
<i>Equal Weighted Buys</i>						46	54				0.79

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 (PV) presumes long-term prices of \$100 a barrel for oil and \$8 a million btu for natural gas.

Dist. = Income distribution. NTM = Next Twelve Months Ended September 30, 2012. Enterprise Value = Market Cap and Debt.



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Table ISC-2								
McDep Income and Small Cap Energy Portfolio								
Net Present Value and McDep Ratio								
			Price (\$/sh)		Market	Net	Debt/	
	Symbol/ Rating		15-Sep 2011	Shares (mm)	Cap (\$mm)	Value (\$/un)	Present Value	McDep Ratio
Small Cap Independent Producers								
Range Resources	RRC	B	63.27	159.0	10,060	70.00	0.15	0.92
Peyto Exploration and Development Cor	PEYUF		21.56	133.1	2,870	24.00	0.14	0.91
Birchcliff Energy Ltd.	BIREF	B	13.51	131.0	1,770	16.00	0.15	0.87
Berry Petroleum Company	BRY		47.70	54.7	2,610	70.00	0.28	0.77
Denbury Resources Inc.	DNR		14.64	404.0	5,910	28.00	0.17	0.60
Cimarex Energy Company	XEC	CB	68.21	86.1	5,870	120.00	0.07	0.60
Whiting Petroleum Corporation	WLL	CB	45.63	119.0	5,430	90.00	0.13	0.57
<i>Total or Median</i>					34,520		0.15	0.77
Top Line Cash Payers								
Cross Timbers Royalty Trust	CRT		46.00	6.0	280	45.00	-	1.02
Permian Basin RT	PBT		22.14	46.6	1,030	22.00	-	1.01
Sabine Royalty Trust	SBR		63.51	14.6	930	70.00	-	0.91
Freehold Royalties Ltd.	FRHLF		17.64	59.1	1,040	22.00	0.05	0.81
Dorchester Minerals, L.P.	DMLP	CB	23.55	30.7	720	30.00	-	0.78
<i>Total or Median</i>					4,000			0.91
Bottom Line Cash Payers								
Linn Energy, LLC	LINE		37.83	176.0	6,660	34.00	0.34	1.07
Hugoton RoyaltyTrust	HGT	B	22.54	40.0	900	22.00	-	1.03
Vanguard Natural Resources, LLC	VNR		27.57	51.1	1,410	27.00	0.32	1.01
San Juan Basin Royalty Trust	SJT		23.77	46.6	1,110	25.00	-	0.95
Legacy Reserves L.P.	LGCY		27.20	43.6	1,190	30.00	0.30	0.93
Mesa RoyaltyTrust	MTR		45.46	1.9	85	53.00	-	0.86
Enerplus Corporation	ERF	CB	27.47	179.6	4,930	37.00	0.14	0.78
<i>Total or Median</i>					16,290			0.95
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 \$100 a barrel for oil and \$8 a million btu for natural gas.								



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Table ISC-3									
McDep Income and Small Cap Energy Portfolio									
Value Multiples - Rank by EV/Ebitda									
			Price (\$/sh)	Revenue	Dist/ Equity	Adjstd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda	
	Symbol/ Rating		15-Sep 2011	Royalty (%)	Ebitda	NTM	NTM	NTM	
Small Cap Independent Producers									
	Range Resources	RRC	B	63.27		-	14.4	16.4	15.1
	Birchcliff Energy Ltd.	BIREF	B	13.51		-	19.7	15.1	13.1
	Peyto Exploration and Development Corp	PEYUF		21.56		0.33	13.6	10.9	9.9
	Berry Petroleum Company	BRY		47.70		-	11.9	10.1	7.8
	Denbury Resources Inc.	DNR		14.64		-	13.4	10.9	6.6
	Cimarex Energy Company	XEC	CB	68.21		-	6.8	8.7	5.2
	Whiting Petroleum Corporation	WLL	CB	45.63		-	8.5	7.9	4.5
	<i>Median</i>						13.4	10.9	7.8
Top Line Cash Payers									
	Cross Timbers Royalty Trust	CRT		46.00	80	0.97	13.8	15.4	15.8
	Sabine Royalty Trust	SBR		63.51	100	1.00	7.2	16.5	15.0
	Permian Basin RT	PBT		22.14	32	0.98	16.5	14.6	14.7
	Dorchester Minerals, L.P.	DMLP	CB	23.55	77	0.84	6.6	14.7	11.5
	Freehold Royalties Ltd.	FRHLF		17.64	71	0.93	6.6	12.1	9.8
	<i>Median</i>						7.2	14.7	14.7
Bottom Line Cash Payers									
	Linn Energy, LLC	LINE		37.83		1.18	17.1	14.5	15.5
	Hugoton RoyaltyTrust	HGT	B	22.54		0.85	14.2	14.3	14.7
	San Juan Basin Royalty Trust	SJT		23.77		0.82	9.3	14.6	13.9
	Mesa RoyaltyTrust	MTR		45.46		0.83	14.5	15.6	13.4
	Vanguard Natural Resources, LLC	VNR		27.57		0.91	8.8	10.6	10.8
	Legacy Reserves L.P.	LGCY		27.20		0.71	10.2	9.9	9.3
	Enerplus Corporation	ERF	CB	27.47		0.59	8.3	10.0	7.8
	<i>Median</i>						10.2	14.3	13.4
<p>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 September 30, 2012; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses</p>									
<p>Top Line Cash Payers defined as those having Revenue Royalty (see fifth column from right).</p>									



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011

Table ISC-4									
Oil and Gas Income and Small Cap Stocks									
Rank by Enterprise Value to 200 Day Average									
			Price (\$/sh)	Enterprise Value/					
	Symbol/ Rating		15-Sep 2011	52Wk High	52Wk Low	50 Day Avg.	200 Day Avg.	McDep Ratio	
Small Cap Independent Producers									
	Range Resources	RRC	B	63.27	0.95	1.61	1.03	1.15	0.92
	Birchcliff Energy Ltd.	BIREF	B	13.51	0.91	1.55	1.00	1.08	0.87
	Peyto Exploration and Development C	PEYUF		21.56	0.87	1.45	0.96	1.04	0.91
	Berry Petroleum Company	BRY		47.70	0.85	1.33	0.96	0.99	0.77
	Whiting Petroleum Corporation	WLL	CB	45.63	0.66	1.09	0.91	0.81	0.57
	Denbury Resources Inc.	DNR		14.64	0.64	1.05	0.90	0.79	0.60
	Cimarex Energy Company	XEC	CB	68.21	0.61	1.14	0.91	0.76	0.60
	<i>Median</i>				<i>0.85</i>	<i>1.33</i>	<i>0.96</i>	<i>0.99</i>	<i>0.77</i>
Top Line Cash Payers									
	Cross Timbers Royalty Trust	CRT		46.00	0.95	1.32	1.03	1.05	1.02
	Permian Basin RT	PBT		22.14	0.93	1.18	1.00	1.02	1.01
	Sabine Royalty Trust	SBR		63.51	0.90	1.34	1.01	1.01	0.91
	Dorchester Minerals, L.P.	DMLP	CB	23.55	0.78	1.13	0.92	0.87	0.78
	Freehold Royalties Ltd.	FRHLF		17.64	0.74	1.11	0.90	0.84	0.81
	<i>Median</i>				<i>0.90</i>	<i>1.18</i>	<i>1.00</i>	<i>1.01</i>	<i>0.91</i>
Bottom Line Cash Payers									
	Hugoton RoyaltyTrust	HGT	B	22.54	0.91	1.20	1.01	1.02	1.03
	Linn Energy, LLC	LINE		37.83	0.94	1.16	1.00	0.99	1.07
	Mesa RoyaltyTrust	MTR		45.46	0.89	1.15	1.00	0.98	0.86
	San Juan Basin Royalty Trust	SJT		23.77	0.85	1.16	0.99	0.97	0.95
	Vanguard Natural Resources, LLC	VNR		27.57	0.87	1.14	0.98	0.95	1.01
	Legacy Reserves L.P.	LGCY		27.20	0.86	1.15	0.98	0.95	0.93
	Enerplus Corporation	ERF	CB	27.47	0.85	1.13	0.95	0.91	0.78
	<i>Median</i>				<i>0.87</i>	<i>1.15</i>	<i>0.99</i>	<i>0.97</i>	<i>0.95</i>

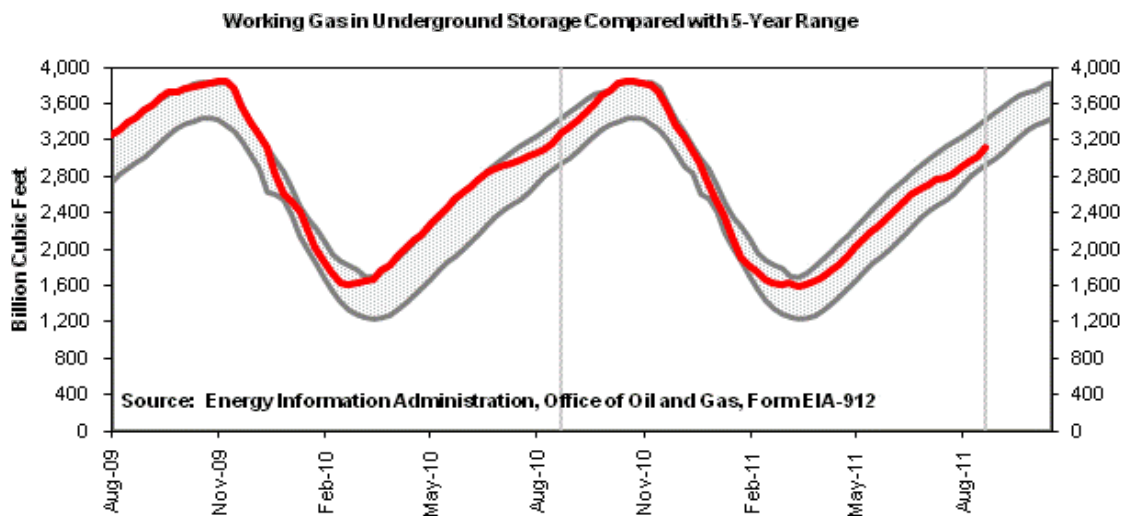
CB=Contrarian Buy, Stock Price apparently in downtrend compared to 200-day average.



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

September 16, 2011



Disclaimer: This analysis was prepared by Kurt Wulff, Manager of McDep LLC. The firm used sources and data believed to be reliable, but makes no representation as to their accuracy or completeness. This analysis is intended for informational purposes and is not a solicitation to buy or sell a security. Past performance is no guarantee of future results.

McDep or its employees may take positions in stocks the firm covers for research purposes. No trades in a subject stock shall be made within a week before or after a change in recommendation.

Certification: I, Kurt H. Wulff, certify that the views expressed in this research analysis accurately reflect my personal views about the subject securities and issuers. No part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research analysis.

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.