



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 2, 2011

Cimarex Energy (XEC) Hedged against Frackophobia

<i>Symbol</i>	XEC	<i>Ebitda Next Twelve Months ending 12/31/12 (US\$mm)</i>	1,303
<i>Rating</i>	Contrarian Buy	<i>North American Natural Gas/Ebitda (%)</i>	27
<i>Price (\$/sh)</i>	66.71	<i>Natural Gas and Oil Production/Ebitda (%)</i>	100
<i>Pricing Date</i>	12/1/11	<i>Adjusted Reserves/Production NTM</i>	6.9
<i>Shares (mm)</i>	86	<i>EV/Ebitda</i>	5.0
<i>Market Capitalization (\$mm)</i>	5,750	<i>PV/Ebitda</i>	8.5
<i>Debt (\$mm)</i>	760	<i>Undeveloped Reserves (%)</i>	13
<i>Enterprise Value (EV) (\$mm)</i>	6,510	<i>Natural Gas and Oil Ebitda (\$/boe)</i>	34.60
<i>Present Value (PV) (\$mm)</i>	11,100	<i>Present Value Proven Reserves(\$/boe)</i>	40.00
<i>Net Present Value (\$/share)</i>	120	<i>Oil and Gas Ebitda Margin (%)</i>	72
<i>Debt/Present Value</i>	0.07	<i>Earnings Next Twelve Months (US\$/sh)</i>	6.76
<i>McDep Ratio - EV/PV</i>	0.59	<i>Price/Earnings Next Twelve Months</i>	10
<i>Dividend Yield (%/year)</i>	0.6	<i>Indicated Annual Dividend (US\$/sh)</i>	0.40
Note: Estimated cash flow and earnings tied to one-year futures prices for oil and natural gas.			
Reported results may vary widely from estimates. Estimated present value per share revised only infrequently.			
Estimated present value presumes a long-term price for oil of US\$100 a barrel and natural gas, \$8 a million btu.			
For historical analysis of XEC since 2003 see www.mcdep.com/4xec.htm			

Summary and Recommendation

Contrarian Buy **Cimarex Energy (XEC)** offers investors a leading driller and producer of shale oil and shale gas in West Texas and Oklahoma with a long, safe, and profitable record for a low McDep Ratio of 0.59. At the same time, the Federal Environmental Protection Agency (EPA) threatens a moratorium on fracking, which would likely cause U.S. oil and natural gas production to decline. Producers like Cimarex have a built-in hedge against the negative effect of government regulation because the restriction of supply tends to cause price to increase.

Fear of Fracking

EPA moves toward regulating the breakthrough technology that combined horizontal drilling with multi-stage hydraulic fracturing has the attention of North Dakota's top oil regulator, Mr. Lynn Helms, director of the state's department of mineral resources. Reported on November 27 in the *Bismarck Tribune*, Mr. Helms thinks the EPA may impose a moratorium on fracking as soon as January while it directs the states to prepare regulations the EPA thinks are required by the Safe Drinking Water Act. Two hundred rigs are drilling in ND to the Bakken Shale and related formations. Every well is fracked with high pressure injection of water and sand.

Critics contend that fracking contaminates fresh water supply. Industry representatives point out that fresh water formations are sealed off and fracking occurs thousands of feet lower. We think some criticism is helpful nonetheless, because it may reinforce the implementation of best practices for safe operation.



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It seems far-fetched that the EPA would shut down all new drilling in the U.S. Following the publicity attracted by Mr. Helms' candid assessment, Senator John Hoeven (R-ND) issued a press release declaring that the EPA was not planning a moratorium. Yet, the Obama administration did just that in the Gulf of Mexico using the hysteria of an oil spill, serious as it may have been, as justification. Similarly the Obama administration killed the Keystone XL pipeline after the State Department gave indications it would likely go ahead. There may be no widespread fracking moratorium, but there could be additional limited versions.

In any case, the fourth year of President Obama may have more surprises that help oil price increase much like we saw during the fourth year of President Carter. Eventually, Federal Reserve Chairman Volker succeeded in using high interest rates to bring about a recession, which dampened oil price. Today, Federal Reserve Chairman Bernanke is leading the world to print money with the intended outcome of growth, which would be supportive of oil price. Among buy recommendations to capitalize on the economic and political trends, we highlight the current attraction in Cimarex, a long-time favorite driller.

Valuation Measures Support Purchase of Cimarex Stock

Along with a low McDep Ratio, Cimarex has low debt, the lowest among peers, measured by either EV/Market Cap at 1.13 (Table ISC -1) or Debt/Present Value at 0.07 (Table ISC-2). Unlevered cash flow multiple (EV/Ebitda) is near lowest at 5.0 times along with low life index of 6.9 years on conservatively reported reserves (see Tables ISC-3 on page 5). Cimarex stock is most out of favor measured by lowest enterprise value to 200-day average of 0.81 (see Table ISC-4 on page 6).

Attesting to management's quick response to changing industry trends the makeup of our estimated Net Present Value (NPV) of \$120 a share has morphed from nearly all natural gas to almost equal contributions from oil and natural gas (see tables Functional Cash Flow and Present Value and Next Twelve Months Operating and Financial Results on page 7).

Nor do we think McDep Ratio is low because our estimate of NPV is too high. We include less volume growth in Cimarex's NPV than for peers, though that may not necessarily be the case (see chart Volume on page 8). By design, Cimarex drills the most profitable wells it can find as a result of applying its own geoscience. The most profitable wells by Cimarex are often those that produce more of the reserves up front. A shorter reserve life measures some of that effect. Our Cimarex estimate is in line with that consideration (see chart Cash Flow Multiple and Reserve Life on page 8).

Kurt H. Wulff, CFA



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Table ISC-1											
McDep Income and Small Cap Energy Portfolio											
Debt, Segments, Cash Flow, Income and McDep Ratio											
			Price	EV/	Enterprise	PV(%)		EV/	Dist.	Dist.	
Symbol/Rating	(US\$/sh)	1-Dec	Market	Value	Nat	Oil	Ebitda	NTM	Yield	McDep	
CB (see below)	2011	Cap	(\$mm)	Gas			NTM	(\$/un)	(%)	Ratio	
Small Cap Independent Producers											
PDC Energy	PETD		33.68	1.68	1,340	62	38	8.0	-	-	1.03
Range Resources	RRC	B	71.43	1.19	13,560	66	34	16.3	0.16	0.2	1.02
Peyto Exploration and Developmen	PEYUF		24.30	1.16	3,760	75	25	11.0	0.70	2.9	1.01
Birchcliff Energy Ltd.	BIREF	B	13.54	1.23	2,170	56	44	12.3	-	-	0.87
Berry Petroleum Company	BRY		43.78	1.60	3,830	21	79	6.0	0.32	0.7	0.73
Denbury Resources Inc.	DNR		16.70	1.37	9,220	4	96	5.9	-	-	0.67
Whiting Petroleum Corporation	WLL	CB	48.14	1.28	7,340	11	89	4.3	-	-	0.60
Cimarex Energy Company	XEC	CB	66.71	1.13	6,510	46	54	5.0	0.40	0.6	0.59
<i>Total or Median</i>					47,700			7.0			0.80
Top Line Cash Payers											
Cross Timbers Royalty Trust	CRT		47.12	1.00	280	87	13		2.92	6.2	1.05
Sabine Royalty Trust	SBR		66.19	1.00	970	51	49		4.24	6.4	0.95
Permian Basin RT	PBT		20.05	1.00	940	42	58		1.42	7.1	0.91
Freehold Royalties Ltd.	FRHLF		18.87	1.06	1,180	18	82		1.62	8.6	0.86
Dorchester Minerals, L.P.	DMLP	CB	21.96	1.00	670	61	39		1.92	8.7	0.73
<i>Total or Median</i>					4,000					7.1	0.91
Bottom Line Cash Payers											
Linn Energy, LLC	LINE		36.65	1.46	9,410	31	69	13.2	2.76	7.5	1.05
Vanguard Natural Resources, LLC	VNR		27.76	1.54	2,080	27	73	10.1	2.31	8.3	1.02
Hugoton Royalty Trust	HGT		21.34	1.00	850	88	13	17.7	1.07	5.0	0.97
San Juan Basin Royalty Trust	SJT	CB	23.96	1.00	1,120	100	-	16.3	1.10	4.6	0.96
Legacy Reserves L.P.	LGCY		26.94	1.43	1,690	22	78	8.1	2.18	8.1	0.93
Enduro Royalty Trust (40%)	NDRO		18.19	1.00	240	47	53	7.7	1.64	9.0	0.83
Mesa Royalty Trust	MTR		43.25	1.00	81	75	25	11.2	3.44	7.9	0.82
Enerplus Corporation	ERF	CB	25.71	1.28	5,900	29	71	7.6	2.09	8.1	0.74
<i>Total or Median</i>					21,400			10.7		8.0	0.94
Composite											
<i>Enterprise Value Weighting</i>					73,100	38	62				0.80
<i>Equal Weighting</i>						48	52				0.87
<i>Equal Weighted Buys</i>						45	55				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 December 31, 2012. Enterprise Value = Market Cap and Debt.



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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		1-Dec 2011	Royalty (%)	Ebitda	NTM	NTM	NTM
Small Cap Independent Producers								
Range Resources	RRC	B	71.43		-	14.0	16.0	16.3
Birchcliff Energy Ltd.	BIREF	B	13.54		-	19.3	14.1	12.3
Peyto Exploration and Development Corp	PEYUF		24.30		0.31	12.9	10.9	11.0
PDC Energy	PETD		33.68		-	8.1	7.7	8.0
Berry Petroleum Company	BRY		43.78		-	11.4	8.2	6.0
Denbury Resources Inc.	DNR		16.70		-	12.6	8.8	5.9
Cimarex Energy Company	XEC	CB	66.71		-	6.9	8.5	5.0
Whiting Petroleum Corporation	WLL	CB	48.14		-	8.5	7.2	4.3
	<i>Median</i>					12.0	8.6	7.0
Top Line Cash Payers								
Cross Timbers Royalty Trust	CRT		47.12	80	0.97	14.0	14.9	15.6
Sabine Royalty Trust	SBR		66.19	100	1.00	7.3	16.5	15.6
Permian Basin RT	PBT		20.05	32	0.98	17.2	15.2	13.8
Freehold Royalties Ltd.	FRHLF		18.87	71	0.82	6.7	11.1	9.6
Dorchester Minerals, L.P.	DMLP	CB	21.96	77	0.82	6.1	12.9	9.4
	<i>Median</i>					7.3	14.9	13.8
Bottom Line Cash Payers								
Hugoton Royalty Trust	HGT		21.34		0.88	14.3	18.2	17.7
San Juan Basin Royalty Trust	SJT	CB	23.96		0.75	8.7	17.0	16.3
Linn Energy, LLC	LINE		36.65		1.02	16.2	12.6	13.2
Mesa Royalty Trust	MTR		43.25		0.89	13.9	13.7	11.2
Vanguard Natural Resources, LLC	VNR		27.76		0.85	8.7	9.9	10.1
Legacy Reserves L.P.	LGCY		26.94		0.63	9.9	8.7	8.1
Enduro Royalty Trust (40%)	NDRO		18.19		0.70	7.4	9.4	7.7
Enerplus Corporation	ERF	CB	25.71		0.57	8.4	10.2	7.6
	<i>Median</i>					9.3	11.4	10.7
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 December 31, 2012; 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).								



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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		1-Dec 2011	52Wk High	52Wk Low	50 Day Avg.	200 Day Avg.	McDep Ratio
Small Cap Independent Producers								
Range Resources	RRC	B	71.43	0.94	1.55	1.05	1.17	1.02
Peyto Exploration and Development C	PEYUF		24.30	0.96	1.37	1.12	1.12	1.01
Birchcliff Energy Ltd.	BIREF	B	13.54	0.89	1.34	1.02	1.03	0.87
PDC Energy	PETD		33.68	0.78	1.49	1.16	1.01	1.03
Berry Petroleum Company	BRY		43.78	0.80	1.23	1.06	0.95	0.73
Denbury Resources Inc.	DNR		16.70	0.71	1.40	1.10	0.92	0.67
Whiting Petroleum Corporation	WLL	CB	48.14	0.69	1.45	1.09	0.89	0.60
Cimarex Energy Company	XEC	CB	66.71	0.60	1.27	1.07	0.81	0.59
	<i>Median</i>			<i>0.79</i>	<i>1.38</i>	<i>1.08</i>	<i>0.98</i>	<i>0.80</i>
Top Line Cash Payers								
Cross Timbers Royalty Trust	CRT		47.12	0.97	1.25	1.02	1.05	1.05
Sabine Royalty Trust	SBR		66.19	0.94	1.40	1.02	1.04	0.95
Permian Basin RT	PBT		20.05	0.86	1.11	1.00	0.95	0.91
Freehold Royalties Ltd.	FRHLF		18.87	0.79	1.35	1.09	0.94	0.86
Dorchester Minerals, L.P.	DMLP	CB	21.96	0.73	1.06	0.91	0.84	0.73
	<i>Median</i>			<i>0.86</i>	<i>1.25</i>	<i>1.02</i>	<i>0.95</i>	<i>0.91</i>
Bottom Line Cash Payers								
San Juan Basin Royalty Trust	SJT	CB	23.96	0.86	1.17	1.00	0.98	0.96
Linn Energy, LLC	LINE		36.65	0.92	1.12	1.00	0.98	1.05
Vanguard Natural Resources, LLC	VNR		27.76	0.88	1.16	1.02	0.97	1.02
Mesa RoyaltyTrust	MTR		43.25	0.86	1.11	1.00	0.96	0.82
Hugoton RoyaltyTrust	HGT		21.34	0.87	1.11	0.99	0.96	0.97
Legacy Reserves L.P.	LGCY		26.94	0.85	1.15	0.99	0.95	0.93
Enerplus Corporation	ERF	CB	25.71	0.81	1.14	0.99	0.90	0.74
	<i>Median</i>			<i>0.86</i>	<i>1.14</i>	<i>1.00</i>	<i>0.96</i>	<i>0.96</i>

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



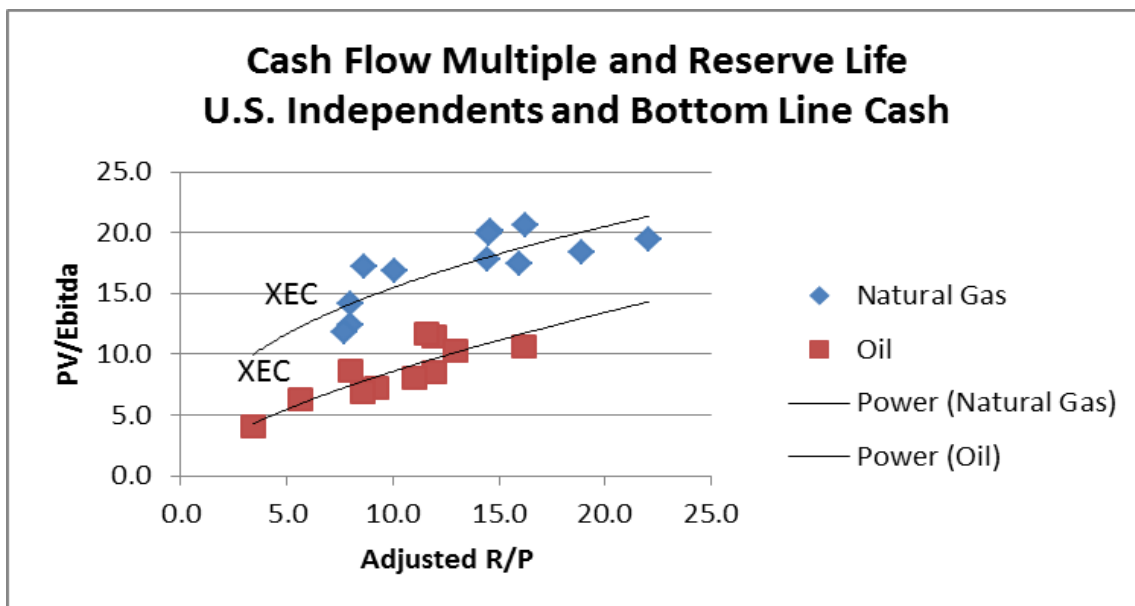
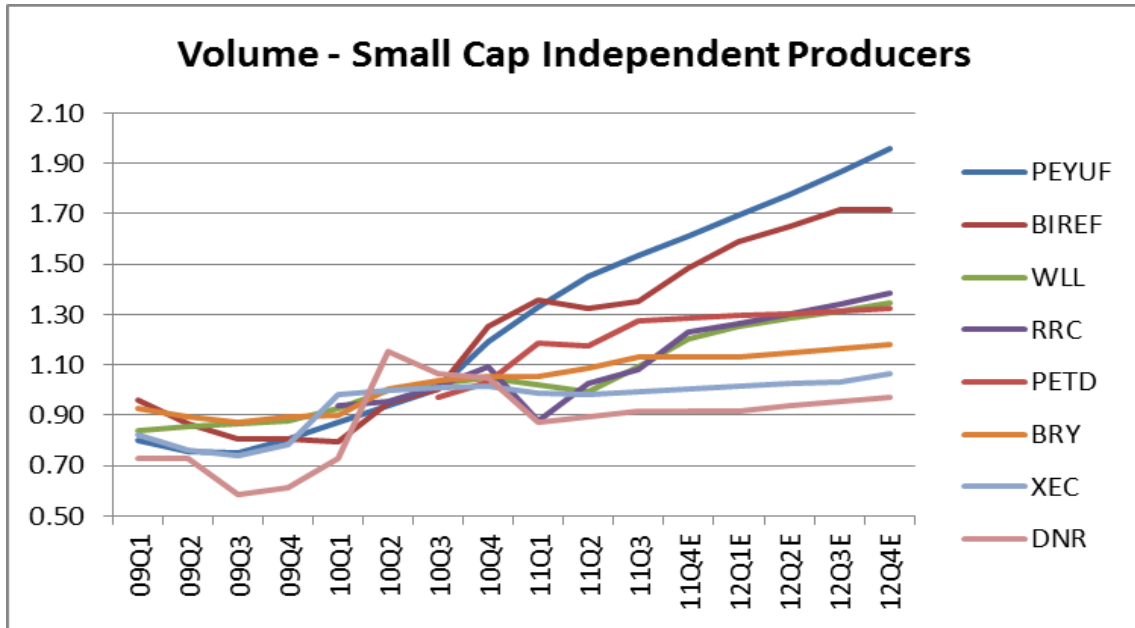
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Cimarex Energy Company					
Functional Cash Flow and Present Value					
	NTM Ebitda	Adjusted	PV/	Present	
	(US\$mm)	R/P	Ebitda	Value	
				(US\$mm)	
North American Natural Gas	360	8.0	14.2	5,100	46%
Oil	943	5.7	6.3	5,960	54%
	1,303	6.9	8.5	11,060	100%
Debt (US\$mm)					760
Net Present Value (US\$mm)					10,300
Shares (mm)					86
Net Present Value - Standard Estimate (US\$/sh)					120
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					120

Cimarex Energy Company									
Next Twelve Months Operating and Financial Performance									
	Q4	Q3	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Next
	12/31/10	9/30/11	12/31/11	2011E	3/31/12	6/30/12	9/30/12	12/31/12	Twelve
									Months
									12/31/12
Volume									
Natural Gas (mmcf)	342	330	330	328	330	330	330	340	332
Oil (mbd)	43.8	43.7	45.0	44.0	45.9	46.8	47.8	49.0	47.4
Total (mmcf)	604	592	600	592	605	611	616	634	617
Price									
Henry Hub (\$/mmbtu)	3.80	4.19	3.55	4.04	3.56	3.64	3.76	3.99	3.74
Company (\$/mcf)	4.18	4.57	3.87	4.41	3.87	3.97	4.10	4.35	4.08
WTI Cushing (\$/bbl)	85.10	89.76	93.81	95.06	98.16	98.29	97.60	96.74	97.70
Company (\$/bbl)	65.27	69.91	73.06	73.39	76.45	76.55	76.02	75.34	76.08
Total (\$/bbl)	42.56	46.24	45.65	47.37	47.46	48.08	48.51	48.94	48.26
Revenue (\$mm)									
Natural Gas	131	139	117	527	116	119	124	136	496
Oil	263	281	302	1,178	319	326	334	340	1,319
Total	394	420	420	1,705	436	445	458	476	1,815
Expense									
Operating	70	78							
Production taxes	33	31							
General and administrative	12	9							
Expense	115	118	118	477	123	126	129	134	512
Ebitda	279	302	301	1,228	313	320	329	341	1,303
Deprec., Deplet., & Amor	84	108	99	387	99	100	102	105	406
Other Non Cash	(13)	2		10					-
Ebit	209	192	202	831	213	220	227	236	896
Interest	-	-	-	-	-	-	-	-	-
Ebt	209	192	202	831	213	220	227	236	896
Income Tax	73	67	71	291	75	77	79	83	314
Net Income (\$mm)	136	125	131	540	139	143	147	154	583
Per Share (\$)	1.58	1.45	1.52	6.27	1.61	1.66	1.71	1.78	6.76
Shares (millions)	86	86	86	86	86	86	86	86	86
Ebitda Margin	71%	72%	72%	72%	72%	72%	72%	72%	72%
Tax rate	35%	35%	35%	35%	35%	35%	35%	35%	35%

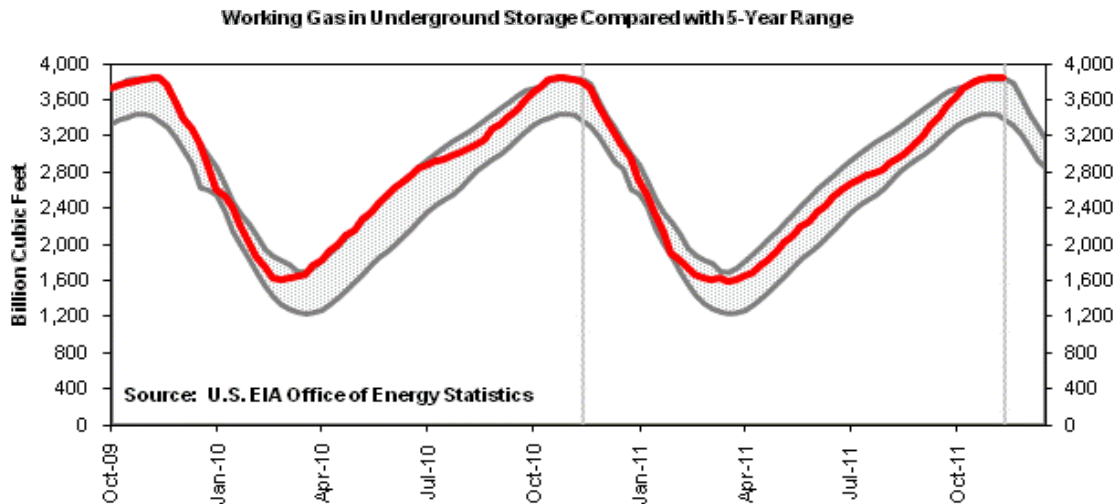




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Research Methodology/Ratings Description: McDep LLC is an independent research originator focused on oil and gas stocks exclusively. The firm applies the forty years of experience of its analyst to estimate a present value of the oil and gas resources 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.