



# Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

June 29, 2012

## Natural Gas Rising from the Price Gloom

### Summary and Recommendation

Natural gas stocks in our income and small cap coverage appear to have begun a new uptrend in stock price along with the price of the clean fuel. The six most concentrated stocks listed by percentage natural gas along with McDep Ratio are Contrarian Buy **Range Resources** (RRC – 71%, 0.90), **Peyto Exploration** (PEYUF – 77%, 0.80), **Cross Timbers Royalty Trust** (CRT – 70%, 0.80), Contrarian Buy **San Juan Basin Royalty Trust** (SJT – 100%, 0.70), Contrarian Buy **Birchcliff Energy** (BIREF – 62%, 0.53) and **Hugoton Royalty Trust** (HGT- 89%, 0.55) (see Table ISC-1 on page 2). Measured by EV/Market Cap (Table ISC-1) and Debt/Present Value (see Table ISC-2 on page 3) the operating companies RRC, PEYUF, and BIREF have modest financial risk while the royalty trusts CRT, SJT and HGT have no debt-related financial risk. The highest distributions estimated for the next twelve months are SJT 6.5%, CRT 6.0% and Peyto 3.8% (Table ISC-1). High volume growth at RRC, PEYUF and BIREF, long-life reserves at SJT and HGT, no operating or capital expense for top line royalty at CRT and low natural gas price for all support higher unlevered multiples of near-term cash flow (EV/Ebitda) (see Table ISC-3 on page 4). Meanwhile a sharp recovery in natural gas futures from the bottom in April suggests that more stock price gains may lie ahead. In the most extreme case we see ratios of enterprise value to the 52-week high at 0.32 for HGT and 0.45 for BIREF, which are lower than the ratio of natural gas price to the 52-week high whether compared to the most volatile near month or the less volatile 72-Month quote (see Table ISC-4 on page 5). For long-term value and near-term timing, we believe the odds are favorable for making money on each of the six natural gas stocks between now and the end of the year and thereafter.

### Birchcliff Competitor Acquisition by Asian Company

Among recent developments we call attention to two news items that reinforce the prospects for Birchcliff. First, the company announced on June 26 that it has renewed its financing agreements to cover its growth plan including a provision that bank loans are not callable for two years. Second, another Asian company, Petronas of Malaysia, is acquiring an independent Canadian producer, Progress Energy (PRQ CN), operating in the same Montney trend as Birchcliff. Announced on June 28, the buyer would pay C\$5.5 billion, a price that is about 70% higher than the target's 200-day average stock price. The buyer may have been encouraged to act now as natural gas price has started to turn up. In contrast, Birchcliff's Asian buyer backed away when natural gas began its warm winter dive in January. Both a better natural gas price trend and a renewed financing agreement strengthen Birchcliff's bargaining position should it restart the sale process it terminated in March.

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								
Symbol/Rating		(US\$/sh)	EV/	Enterprise	PV(%)		EV/	Dist.	Dist.	
	B = Buy	28-Jun	Market	Value	Nat	Oil	Ebitda	NTM	Yield	McDep
CB (see below)		2012	Cap	(\$mm)	Gas		NTM	(\$/un)	(%)	Ratio
<b>Small Cap Independent Producers</b>										
Halcon Resources	HK	9.69	1.07	1,750	20	80	9.4	-	-	0.97
Continental Resources	CLR	62.97	1.21	13,660	27	73	8.4	-	-	0.91
Range Resources	RRC CB	61.37	1.27	12,510	71	29	14.9	0.16	0.3	0.90
Peyto Exploration and Developmen	PEYUF	18.36	1.19	3,030	77	23	10.2	0.70	3.8	0.80
PDC Energy	PETD	22.37	2.01	1,060	56	44	7.5	-	-	0.71
Berry Petroleum Company	BRY	37.28	1.77	3,600	13	87	6.2	0.32	0.9	0.67
Denbury Resources Inc.	DNR	14.15	1.49	8,250	6	94	5.9	-	-	0.60
Birchcliff Energy Ltd.	BIREF CB	5.02	1.59	1,210	62	38	8.8	-	-	0.53
Whiting Petroleum Corporation	WLL CB	38.35	1.41	6,430	8	92	4.7	-	-	0.52
Cimarex Energy Company	XEC CB	50.66	1.24	5,400	42	58	5.1	0.48	0.9	0.51
<i>Total or Median</i>				56,900			8.0			0.69
<b>Top Line Cash Payers</b>										
Permian Basin RT	PBT	17.57	1.00	820	37	63		1.22	7.0	0.88
Freehold Royalties Ltd.	FRHLF	17.61	1.04	1,190	16	84		1.63	9.2	0.84
Dorchester Minerals, L.P.	DMLP CB	21.80	1.00	670	57	43		1.72	7.9	0.81
Cross Timbers Royalty Trust	CRT	35.00	1.00	210	70	30		2.09	6.0	0.80
Sabine Royalty Trust	SBR	49.29	1.00	720	55	45		3.26	6.6	0.76
<i>Total or Median</i>				3,600					7.0	0.81
<b>Bottom Line Cash Payers</b>										
Linn Energy, LLC	LINE	37.70	1.65	11,990	40	60	13.1	2.90	7.7	1.14
Vanguard Natural Resources, LLC	VNR	25.50	1.51	2,030	27	74	11.1	2.37	9.3	1.01
Legacy Reserves L.P.	LGCY	24.80	1.41	1,670	23	77	8.8	2.22	9.0	0.87
Mesa RoyaltyTrust	MTR	33.18	1.00	62	75	25	11.5	2.43	7.3	0.83
Enduro Royalty Trust (40%)	NDRO	16.15	1.00	210	42	58	7.5	1.37	8.5	0.77
Enerplus Corporation	ERF CB	12.51	1.67	4,100	26	74	5.8	1.31	10.4	0.71
San Juan Basin Royalty Trust	SJT CB	14.74	1.00	690	100	-	11.6	0.95	6.5	0.70
Hugoton RoyaltyTrust	HGT	7.71	1.00	310	89	11	8.6	0.10	1.2	0.55
<i>Total or Median</i>				21,100			10.0		8.1	0.80
<b>Composite</b>										
<i>Enterprise Value Weighting</i>				81,600	36	64				0.77
<i>Equal Weighting</i>					45	55				0.77
<i>Equal Weighted Buys</i>					46	54				0.65

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 \$6 a million btu for natural gas.

Dist. = Income distribution. NTM = Next Twelve Months Ended June 30, 2013. Enterprise Value = Market Cap and Debt.



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Table ISC-2							
McDep Income and Small Cap Energy Portfolio							
Net Present Value and McDep Ratio							
		Price (\$/sh)		Market	Net	Debt/	
	Symbol/ Rating	28-Jun 2012	Shares (mm)	Cap (\$mm)	Value (\$/un)	Present Value	McDep Ratio
<b>Small Cap Independent Producers</b>							
	Halcon Resources	HK	9.69	169.1	1,640	10.00	0.06 0.97
	Continental Resources	CLR	62.97	180.0	11,330	70.00	0.16 0.91
	Range Resources	RRC CB	61.37	160.0	9,820	70.00	0.19 0.90
	Peyto Exploration and Development Cor	PEYUF	18.36	138.3	2,540	24.00	0.13 0.80
	PDC Energy	PETD	22.37	23.9	530	40.00	0.36 0.71
	Berry Petroleum Company	BRY	37.28	54.7	2,040	70.00	0.29 0.67
	Denbury Resources Inc.	DNR	14.15	391.0	5,530	28.00	0.20 0.60
	Birchcliff Energy Ltd.	BIREF CB	5.02	150.9	760	12.00	0.20 0.53
	Whiting Petroleum Corporation	WLL CB	38.35	119.0	4,560	88.00	0.15 0.52
	Cimarex Energy Company	XEC CB	50.66	86.1	4,360	110.00	0.10 0.51
	<i>Total or Median</i>				43,110		0.17 0.69
<b>Top Line Cash Payers</b>							
	Permian Basin RT	PBT	17.57	46.6	820	20.00	- 0.88
	Freehold Royalties Ltd.	FRHLF	17.61	64.7	1,140	21.00	0.03 0.84
	Dorchester Minerals, L.P.	DMLP CB	21.80	30.7	670	27.00	- 0.81
	Cross Timbers Royalty Trust	CRT	35.00	6.0	210	44.00	- 0.80
	Sabine Royalty Trust	SBR	49.29	14.6	720	65.00	- 0.76
	<i>Total or Median</i>				3,560		0.81
<b>Bottom Line Cash Payers</b>							
	Linn Energy, LLC	LINE	37.70	193.0	7,280	30.00	0.45 1.14
	Vanguard Natural Resources, LLC	VNR	25.50	52.5	1,340	25.00	0.34 1.01
	Legacy Reserves L.P.	LGCY	24.80	47.5	1,180	30.00	0.26 0.87
	Mesa RoyaltyTrust	MTR	33.18	1.9	62	40.00	- 0.83
	Enduro Royalty Trust (40%)	NDRO	16.15	13.2	210	21.00	- 0.77
	Enerplus Corporation	ERF CB	12.51	196.0	2,450	21.00	0.29 0.71
	San Juan Basin Royalty Trust	SJT CB	14.74	46.6	690	21.00	- 0.70
	Hugoton RoyaltyTrust	HGT	7.71	40.0	310	14.00	- 0.55
	<i>Total or Median</i>				13,520		0.80
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 \$6 a million btu for natural gas.							



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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		28-Jun 2012	Royalty (%)	Ebitda	NTM	NTM	NTM
<b>Small Cap Independent Producers</b>								
Range Resources	RRC	CB	61.37		-	14.0	16.6	14.9
Peyto Exploration and Development Corp	PEYUF		18.36		0.37	10.0	12.8	10.2
Halcon Resources	HK		9.69		-	7.1	9.7	9.4
Birchcliff Energy Ltd.	BIREF	CB	5.02		-	21.6	16.5	8.8
Continental Resources	CLR		62.97		-	9.6	9.2	8.4
PDC Energy	PEID		22.37		-	8.1	10.5	7.5
Berry Petroleum Company	BRY		37.28		-	11.8	9.3	6.2
Denbury Resources Inc.	DNR		14.15		-	13.1	9.8	5.9
Cimarex Energy Company	XEC	CB	50.66		-	8.1	9.9	5.1
Whiting Petroleum Corporation	WLL	CB	38.35		-	9.5	9.0	4.7
	<i>Median</i>					9.8	9.8	8.0
<b>Top Line Cash Payers</b>								
Cross Timbers Royalty Trust	CRT		35.00	78	0.95	17.7	20.1	16.0
Sabine Royalty Trust	SBR		49.29	100	1.00	8.7	19.9	15.1
Dorchester Minerals, L.P.	DMLP	CB	21.80	77	1.00	6.6	15.7	12.7
Permian Basin RT	PBT		17.57	32	0.88	9.7	14.3	12.6
Freehold Royalties Ltd.	FRHLF		17.61	71	0.94	5.4	12.2	10.3
	<i>Median</i>					8.7	15.7	12.7
<b>Bottom Line Cash Payers</b>								
Linn Energy, LLC	LINE		37.70		1.11	14.3	11.5	13.1
San Juan Basin Royalty Trust	SJT	CB	14.74		0.75	8.6	16.6	11.6
Mesa Royalty Trust	MTR		33.18		0.84	8.0	13.8	11.5
Vanguard Natural Resources, LLC	VNR		25.50		1.04	13.6	11.0	11.1
Legacy Reserves L.P.	LGCY		24.80		0.75	11.3	10.1	8.8
Hugoton Royalty Trust	HGT		7.71		0.11	13.6	15.7	8.6
Enduro Royalty Trust (40%)	NDRO		16.15		0.63	5.5	9.7	7.5
Enerplus Corporation	ERF	CB	12.51		0.51	6.3	8.2	5.8
	<i>Median</i>					10.0	11.2	10.0
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, 2013; 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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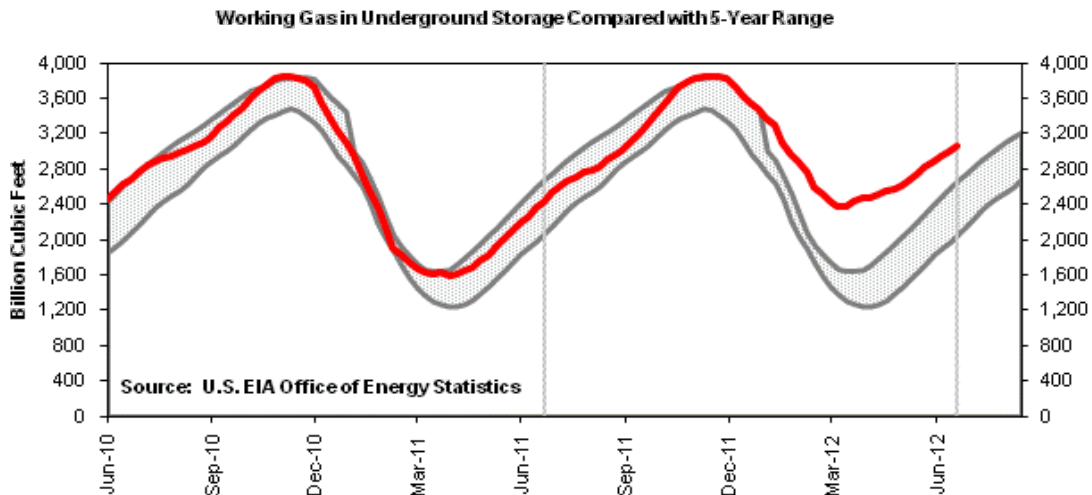
Table ISC-4								
Oil and Gas Income and Small Cap Stocks								
Rank by Enterprise Value to 200 Day Average								
			Price (\$/sh)	Enterprise Value/				
	Symbol/ Rating		28-Jun 2012	52Wk High	52Wk Low	50 Day Avg.	200 Day Avg.	McDep Ratio
<b>Small Cap Independent Producers</b>								
	Range Resources	RRC CB	61.37	0.83	1.14	1.01	0.98	0.90
	Peyto Exploration and Development C	PEYUF	18.36	0.75	1.21	1.06	0.95	0.80
	Berry Petroleum Company	BRY	37.28	0.73	1.11	0.97	0.92	0.67
	Denbury Resources Inc.	DNR	14.15	0.74	1.23	0.92	0.90	0.60
	Continental Resources	CLR	62.97	0.69	1.37	0.86	0.89	0.91
	PDC Energy	PETD	22.37	0.71	1.19	0.91	0.85	0.71
	Whiting Petroleum Corporation	WLL CB	38.35	0.68	1.21	0.87	0.85	0.52
	Cimarex Energy Company	XEC CB	50.66	0.60	1.08	0.91	0.82	0.51
	Birchcliff Energy Ltd.	BIREF CB	5.02	0.43	1.01	0.88	0.59	0.53
	Halcon Resources	HK	9.69	0.74		0.99		0.97
	<i>Median</i>			<i>0.72</i>	<i>1.19</i>	<i>0.91</i>	<i>0.89</i>	<i>0.69</i>
<b>Top Line Cash Payers</b>								
	Freehold Royalties Ltd.	FRHLF	17.61	0.78	1.27	0.98	0.95	0.84
	Dorchester Minerals, L.P.	DMLP CB	21.80	0.77	1.10	0.97	0.93	0.81
	Permian Basin RT	PBT	17.57	0.75	1.07	0.93	0.86	0.88
	Sabine Royalty Trust	SBR	49.29	0.73	1.08	0.95	0.81	0.76
	Cross Timbers Royalty Trust	CRT	35.00	0.69	1.10	0.93	0.80	0.80
	<i>Median</i>			<i>0.75</i>	<i>1.10</i>	<i>0.95</i>	<i>0.86</i>	<i>0.81</i>
<b>Bottom Line Cash Payers</b>								
	Linn Energy, LLC	LINE	37.70	0.95	1.12	1.01	1.01	1.14
	Vanguard Natural Resources, LLC	VNR	25.50	0.86	1.10	0.99	0.96	1.01
	Legacy Reserves L.P.	LGCY	24.80	0.85	1.09	0.95	0.92	0.87
	Mesa RoyaltyTrust	MTR	33.18	0.67	1.33	1.09	0.85	0.83
	San Juan Basin Royalty Trust	SJT CB	14.74	0.58	1.22	0.95	0.74	0.70
	Enerplus Corporation	ERF CB	12.51	0.51	1.06	0.90	0.68	0.71
	Hugoton RoyaltyTrust	HGT	7.71	0.32	1.20	0.78	0.48	0.55
	<i>Median</i>			<i>0.67</i>	<i>1.12</i>	<i>0.95</i>	<i>0.85</i>	<i>0.83</i>
<b>Natural Gas Futures</b>								
	Near Month		2.77	0.58	1.42	1.11	0.95	
	12-Month Average		3.18	0.67	1.24	1.05	0.96	
	72-Month Average		4.00	0.73	1.06	1.01	0.92	



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