



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

November 23, 2012

Invest through the RTF Cycle

Summary and Recommendation

We expect all nine stocks in the illustrative Royalty Trust Fund (RTF) created seven weeks ago to contribute to an estimated return of 10% a year (7% before inflation) in addition to a valuation uplift of 47% that takes average McDep Ratio to 1.0 from 0.68 (see table [RTF](#) below). Since RTF introduction, Distribution Yield has risen to 9.2% for the Next Twelve Months from 8.3% on lower stock price and higher distribution estimates. Rising distributions favor stock price gains over the next year (see charts [Quarterly Distribution](#) on page 2). Recent lower distributions, particularly for Bottom Line Payers, have been caused primarily by lower natural gas and natural gas liquids price as well as out-of-period cash accounting adjustments. Yet, operations run smoothly as evident in comparatively steady volume trends (see charts [Quarterly Volume](#) on page 3). Historical monthly disclosures through November 2012 further contribute to exaggerated stock price reaction that we believe the RTF approach can exploit (see tables [Monthly Distribution](#) and [Monthly Volume](#) on pages 4-5). One RTF stock with extra near-term appreciation prospects may be **Cross Timbers Royalty Trust (CRT)**. It is the lowest McDep Ratio Top Line Payer and is down the most in stock price in the past seven weeks, but it can be difficult to purchase without driving up stock price in a market with limited liquidity. **Permian Basin Royalty Trust (PBT)** may be timely as the cost of new horizontal multi-frac technology being applied on Bottom Line oil properties reduces monthly distribution temporarily. Meanwhile, Top Line Cash from properties where active drilling has no cost to the trust provides a floor level for the distribution. In any case, we believe the RTF approach offers a systematic framework for regularly investing in high-quality resource stocks when the stock price cycle appears to be in a low phase.

Kurt H. Wulff, CFA

The \$20 Million RTF (Royalty Trust Fund)										
Symbol/Rating	Price (US\$/sh)	Fund Shares or Units (thous.)	Market Value (\$mm)	Top Line (%)	PV(%)		Dist. NTM (\$/un)	Dist. Yield (%)	McDep Ratio	
B = Buy CB (see below)	21-Nov 2012				Nat Gas	Oil				
Freehold Royalties Ltd.	FRHLF	21.36	110	2.3	76	16	84	1.69	7.9	1.02
Enduro Royalty Trust (40%)	NDRO	17.78	130	2.3	0	43	57	1.76	9.9	0.85
Dorchester Minerals, L.P.	DMLP CB	21.45	100	2.1	77	57	43	1.89	8.8	0.79
Sabine Royalty Trust	SBR	45.72	50	2.3	100	51	49	4.10	9.0	0.70
Permian Basin RT	PBT	13.48	150	2.0	52	37	63	1.16	8.6	0.67
San Juan Basin Royalty Trust	SJT CB	12.88	160	2.1	0	100	-	1.31	10.2	0.61
Cross Timbers Royalty Trust	CRT	26.25	70	1.8	78	70	30	2.78	10.6	0.60
Mesa RoyaltyTrust	MTR	22.29	90	2.0	0	75	25	2.12	9.5	0.56
Hugoton RoyaltyTrust	HGT	7.80	350	2.7	0	88	13	0.68	8.7	0.56
Total				19.7		59	41		9.2	0.68

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.

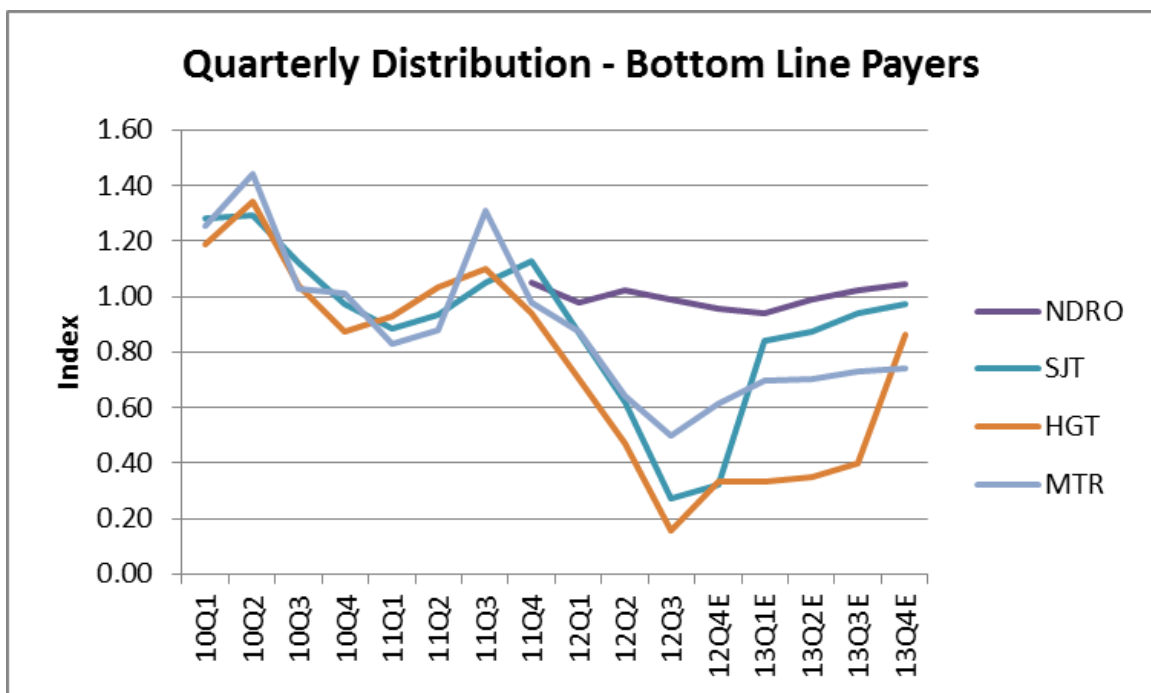
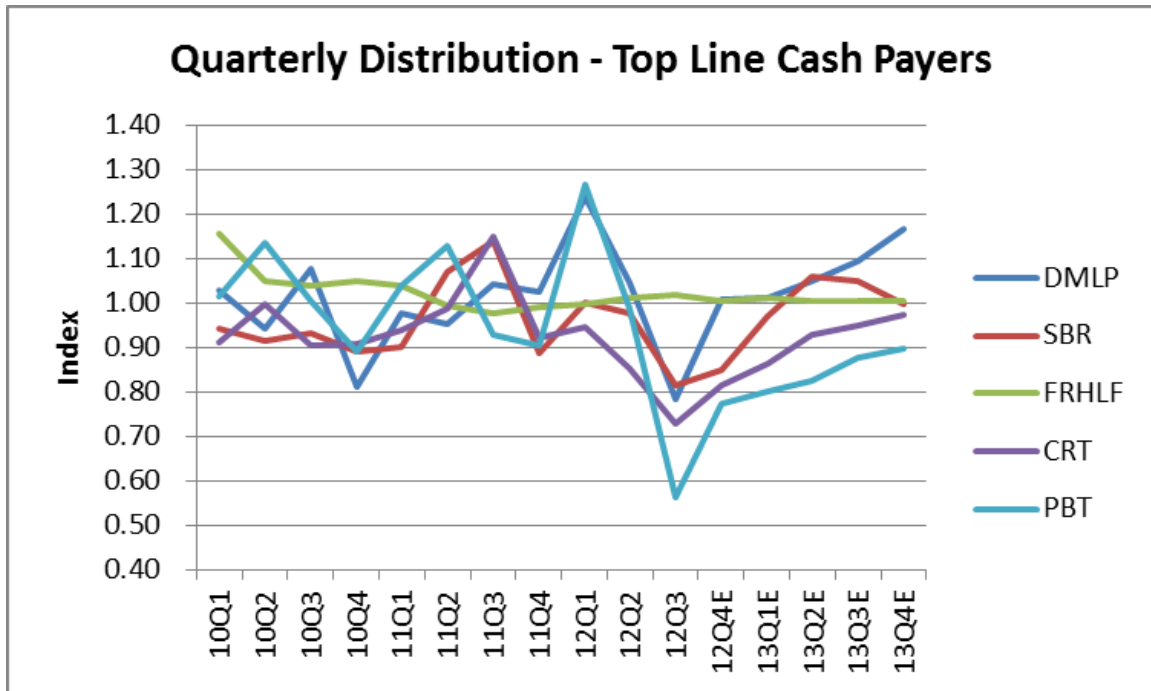
Dist. = Income distribution. NTM = Next Twelve Months Ended December 31, 2013. Enterprise Value = Market Cap and Debt.

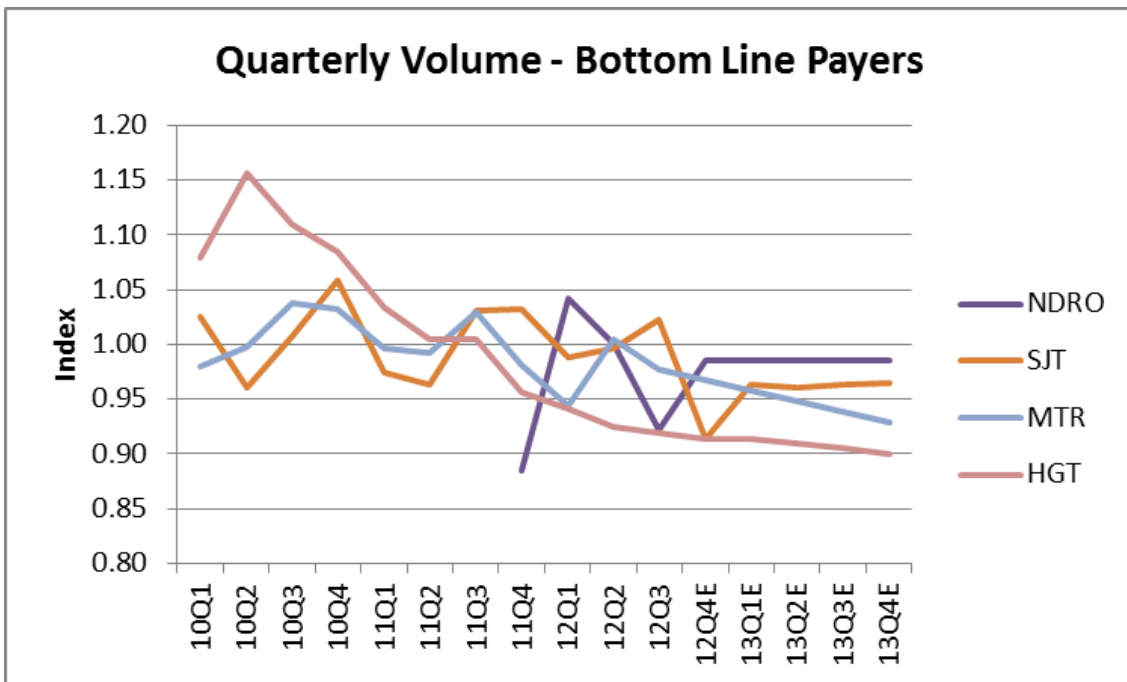
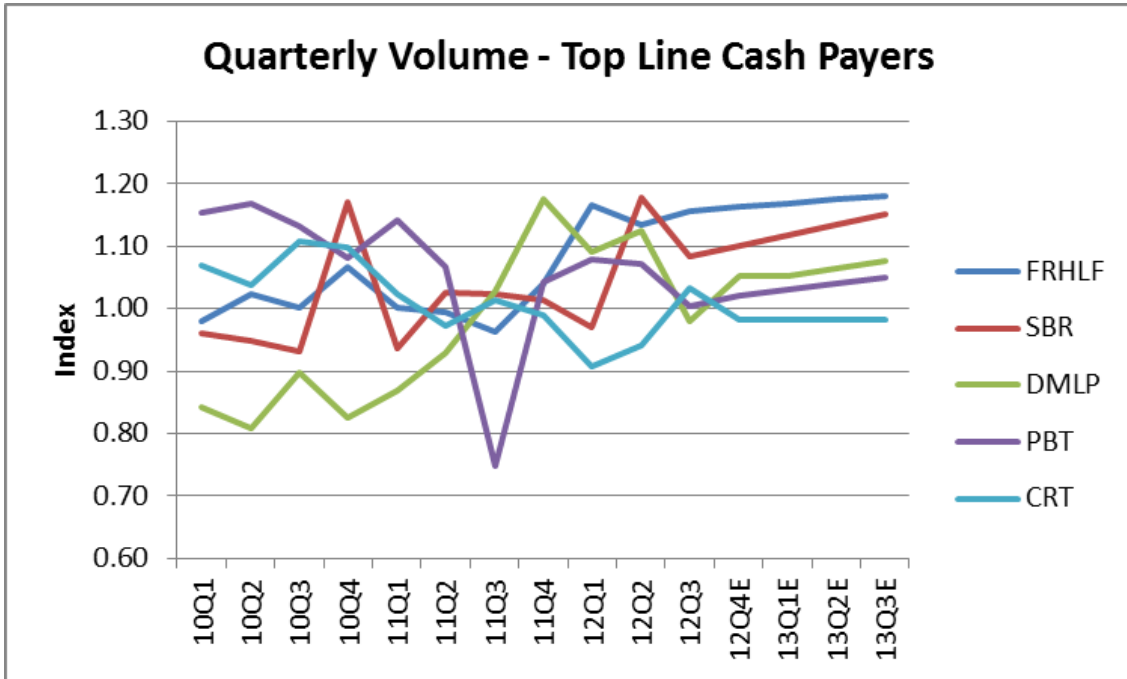


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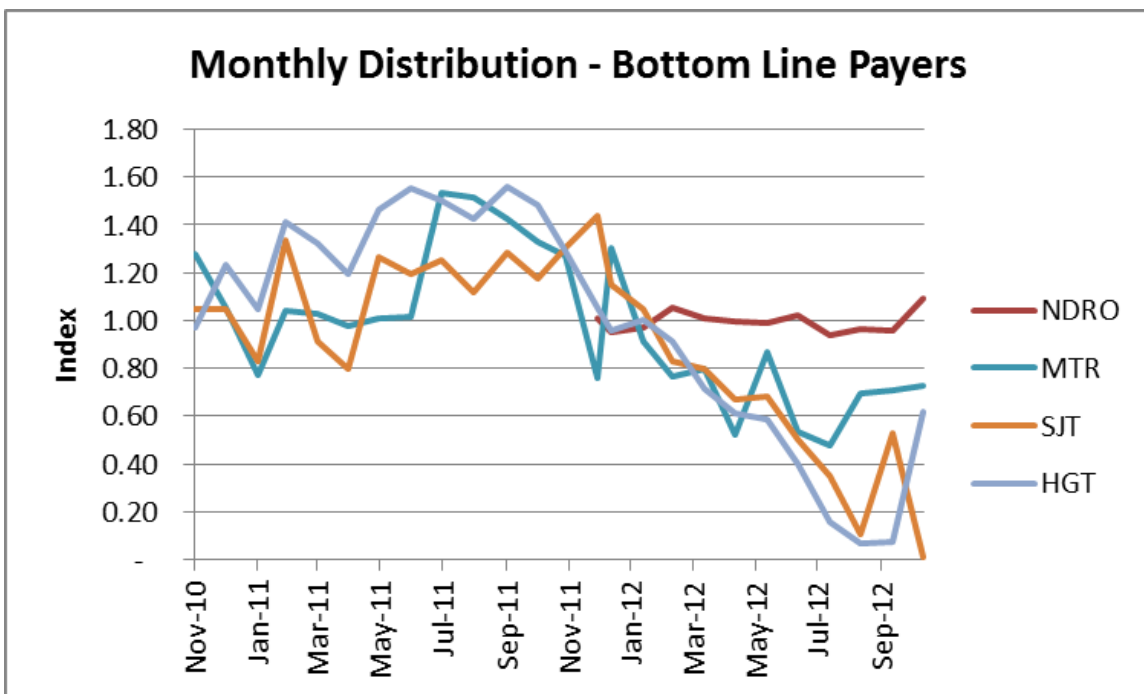
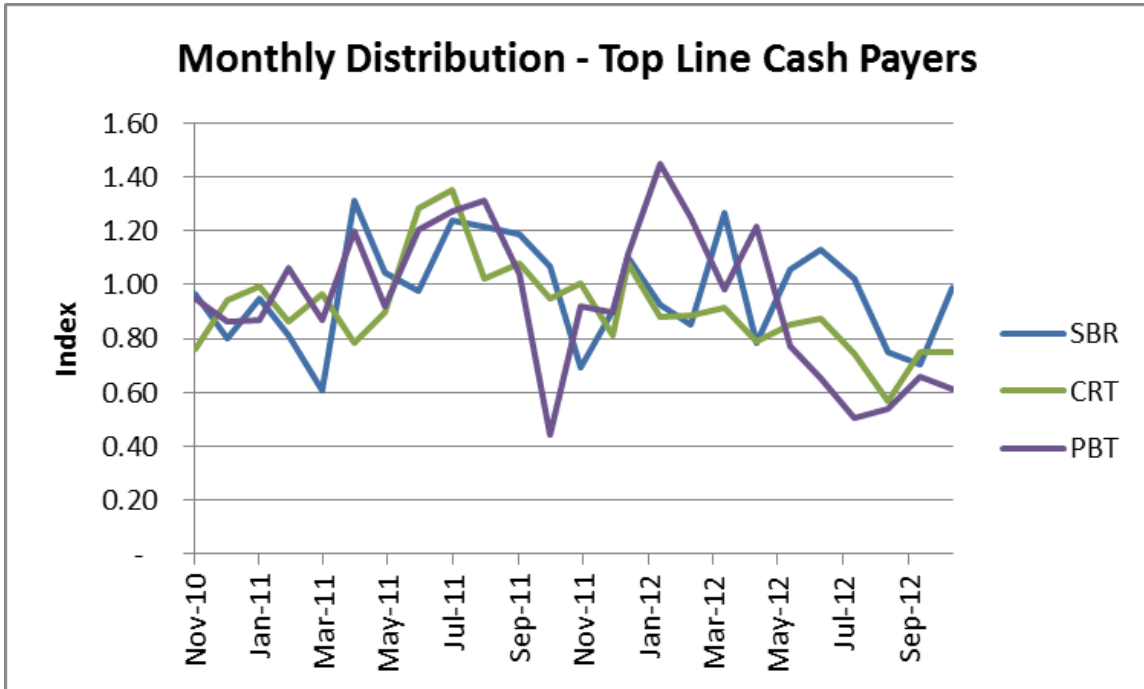




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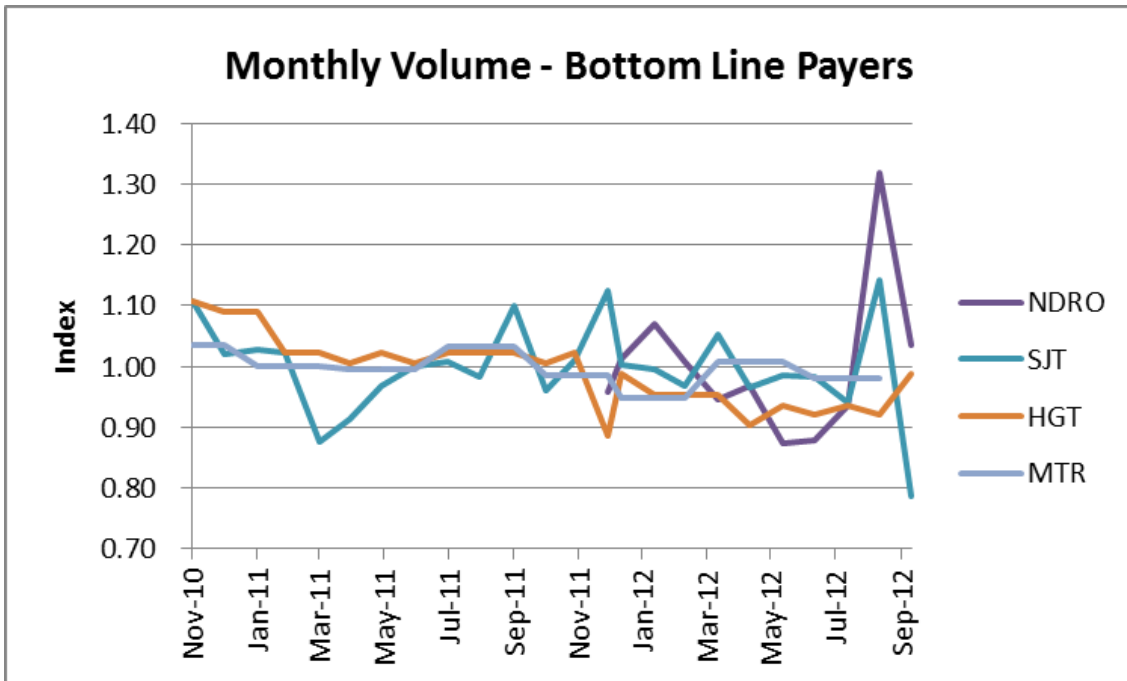
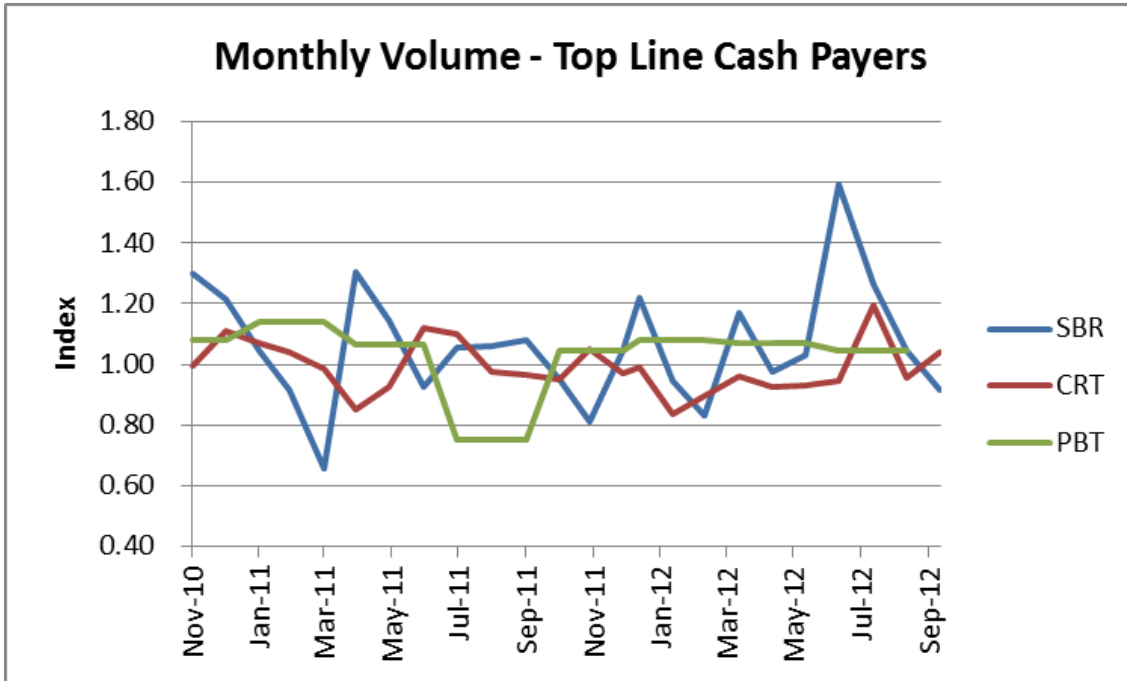




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Table ISC-1											
McDep Income and Small Cap Energy Portfolio											
Debt, Segments, Cash Flow, Income and McDep Ratio											
			Price								
Symbol/Rating	(US\$/sh)	EV/	Enterprise	PV(%)	EV/	Dist.	Dist.				
B = Buy	21-Nov	Market	Value	Nat	Ebitda	NTM	Yield	McDep			
CB (see below)	2012	Cap	(\$mm)	Gas	Oil	NTM	(\$/un)	(%)	Ratio		
Small Cap Independent Producers											
PDC Energy	PDCE		31.47	1.83	1,740	52	48	12.8	-	-	1.03
Range Resources	RRC	B	68.79	1.31	14,440	75	25	16.8	0.16	0.2	0.99
Peyto Exploration and Development	PEYUF		25.27	1.20	4,350	76	24	10.7	0.72	2.9	0.95
Continental Resources (32%)	CLR	CB	70.53	1.23	5,090	24	76	6.7	-	-	0.75
Birchcliff Energy Ltd.	BIREF	B	7.95	1.44	1,700	63	37	9.5	-	-	0.74
Halcón Resources	HK		6.21	1.50	4,080	13	87	6.0	-	-	0.71
Denbury Resources Inc.	DNR		15.50	1.53	9,280	6	94	5.9	-	-	0.65
Berry Petroleum Company	BRY		32.16	1.99	3,540	12	88	5.0	-	-	0.63
Cimarex Energy Company	XEC	CB	62.02	1.26	6,780	41	59	5.2	0.48	0.8	0.62
Whiting Petroleum Corporation	WLL	CB	44.36	1.40	7,410	9	91	4.7	-	-	0.59
<i>Total or Median</i>					58,400			6.4			0.72
Top Line Cash Payers											
Freehold Royalties Ltd.	FRHLF		21.36	1.05	1,470	16	84	10.4	1.69	7.9	1.02
Dorchester Minerals, L.P.	DMLP	CB	21.45	1.00	660	57	43	10.2	1.89	8.8	0.79
Sabine Royalty Trust	SBR		45.72	1.00	670	51	49	11.2	4.10	9.0	0.70
Permian Basin RT	PBT		13.48	1.00	630	37	63	8.4	1.16	8.6	0.67
Cross Timbers Royalty Trust	CRT		26.25	1.00	160	70	30	9.1	2.78	10.6	0.60
<i>Total or Median</i>					3,600			10.2		8.8	0.70
Bottom Line Cash Payers											
Linn Energy, LLC	LINE		38.88	1.64	14,850	43	57	12.7	2.90	7.5	1.16
Vanguard Natural Resources, LLC	VNR		27.72	1.62	2,390	33	67	11.6	2.40	8.7	1.06
Legacy Reserves L.P.	LGCY		24.41	1.50	1,740	25	75	8.9	2.26	9.3	0.87
Enduro Royalty Trust (40%)	NDRO		17.78	1.00	240	43	57	9.5	1.76	9.9	0.85
Enerplus Corporation	ERF	CB	12.58	1.72	4,200	31	69	5.9	1.08	8.6	0.72
San Juan Basin Royalty Trust	SJT	CB	12.88	1.00	600	100	-	7.7	1.31	10.2	0.61
Mesa Royalty Trust	MTR		22.29	1.00	42	75	25	8.5	2.12	9.5	0.56
Hugoton Royalty Trust	HGT		7.80	1.00	310	88	13	6.2	0.68	8.7	0.56
<i>Total or Median</i>					24,400			8.7		9.0	0.78
Composite											
<i>Enterprise Value Weighting</i>					86,400	39	61				0.80
<i>Equal Weighting</i>						45	55				0.78
<i>Equal Weighted Buys</i>						49	51				0.73

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 December 31, 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							
			<i>Price (\$/sh)</i>		<i>Net Present Value</i>	<i>Debt/ Present Value</i>	
	<i>Symbol/ Rating</i>	<i>21-Nov 2012</i>	<i>Shares (mm)</i>	<i>Market Cap (\$mm)</i>	<i>Value (\$/un)</i>		<i>McDep Ratio</i>
Small Cap Independent Producers							
PDC Energy	PDCE		31.47	30.2	950	30.00	0.46 1.03
Range Resources	RRC	B	68.79	160.0	11,010	70.00	0.23 0.99
Peyto Exploration and Development Cor	PEYUF		25.27	143.2	3,620	27.00	0.16 0.95
Continental Resources (32%)	CLR	CB	70.53	58.6	4,130	100.00	0.14 0.75
Birchcliff Energy Ltd.	BIREF	B	7.95	149.0	1,180	12.00	0.22 0.74
Halcón Resources	HK		6.21	436.0	2,710	10.00	0.24 0.71
Denbury Resources Inc.	DNR		15.50	391.0	6,060	28.00	0.23 0.65
Berry Petroleum Company	BRY		32.16	55.3	1,780	70.00	0.31 0.63
Cimarex Energy Company	XEC	CB	62.02	86.9	5,390	110.00	0.13 0.62
Whiting Petroleum Corporation	WLL	CB	44.36	119.0	5,280	88.00	0.17 0.59
<i>Total or Median</i>					<i>42,110</i>		<i>0.23 0.72</i>
Top Line Cash Payers							
Freehold Royalties Ltd.	FRHLF		21.36	65.7	1,400	21.00	0.05 1.02
Dorchester Minerals, L.P.	DMLP	CB	21.45	30.7	660	27.00	- 0.79
Sabine Royalty Trust	SBR		45.72	14.6	670	65.00	- 0.70
Permian Basin RT	PBT		13.48	46.6	630	20.00	- 0.67
Cross Timbers Royalty Trust	CRT		26.25	6.0	160	44.00	- 0.60
<i>Total or Median</i>					<i>3,520</i>		<i>0.70</i>
Bottom Line Cash Payers							
Linn Energy, LLC	LINE		38.88	233.0	9,060	30.00	0.45 1.16
Vanguard Natural Resources, LLC	VNR		27.72	53.1	1,470	25.00	0.41 1.06
Legacy Reserves L.P.	LGCY		24.41	47.5	1,160	30.00	0.29 0.87
Enduro Royalty Trust (40%)	NDRO		17.78	13.2	240	21.00	- 0.85
Enerplus Corporation	ERF	CB	12.58	196.0	2,470	21.00	0.30 0.72
San Juan Basin Royalty Trust	SJT	CB	12.88	46.6	600	21.00	- 0.61
Mesa RoyaltyTrust	MTR		22.29	1.9	42	40.00	- 0.56
Hugoton RoyaltyTrust	HGT		7.80	40.0	310	14.00	- 0.56
<i>Total or Median</i>					<i>15,350</i>		<i>0.78</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 \$100 a barrel for oil and \$6 a million btu for natural gas.							
* PEYUF NPV rased to \$27 from \$24 on November 15 to take account of strong performance in third quarter 2012 disclosed on November 8.							



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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		21-Nov 2012	Royalty (%)	Ebitda	NTM	NTM	NTM
Small Cap Independent Producers								
Range Resources	RRC	B	68.79		-	13.5	17.0	16.8
PDC Energy	PDCE		31.47		-	9.9	12.5	12.8
Peyto Exploration and Development Corp	PEYUF		25.27		0.30	9.2	11.3	10.7
Birchcliff Energy Ltd.	BIREF	B	7.95		-	19.4	13.0	9.5
Continental Resources (32%)	CLR	CB	70.53		-	9.0	9.0	6.7
Halcón Resources	HK		6.21		-	5.5	8.5	6.0
Denbury Resources Inc.	DNR		15.50		-	13.0	9.0	5.9
Cimarex Energy Company	XEC	CB	62.02		-	7.3	8.4	5.2
Berry Petroleum Company	BRY		32.16		-	11.3	8.0	5.0
Whiting Petroleum Corporation	WLL	CB	44.36		-	9.1	7.9	4.7
	<i>Median</i>					9.5	9.0	6.4
Top Line Cash Payers								
Sabine Royalty Trust	SBR		45.72	100	1.00	7.6	15.9	11.2
Freehold Royalties Ltd.	FRHLF		21.36	76	0.82	5.1	10.2	10.4
Dorchester Minerals, L.P.	DMLP	CB	21.45	77	0.90	6.8	12.9	10.2
Cross Timbers Royalty Trust	CRT		26.25	78	0.97	16.5	15.3	9.1
Permian Basin RT	PBT		13.48	52	0.72	9.4	12.4	8.4
	<i>Median</i>					7.6	12.9	10.2
Bottom Line Cash Payers								
Linn Energy, LLC	LINE		38.88		1.06	14.0	10.9	12.7
Vanguard Natural Resources, LLC	VNR		27.72		1.04	13.2	10.9	11.6
Enduro Royalty Trust (40%)	NDRO		17.78		0.94	7.2	11.2	9.5
Legacy Reserves L.P.	LGCY		24.41		0.78	11.0	10.3	8.9
Mesa RoyaltyTrust	MTR		22.29		0.80	7.7	15.2	8.5
San Juan Basin Royalty Trust	SJT	CB	12.88		0.78	9.1	12.6	7.7
Hugoton RoyaltyTrust	HGT		7.80		0.54	13.6	11.2	6.2
Enerplus Corporation	ERF	CB	12.58		0.43	6.3	8.2	5.9
	<i>Median</i>					10.0	11.1	8.7
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, 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	21-Nov 2012	52Wk High	52Wk Low	50 Day Avg.	200 Day Avg.	McDep Ratio	
Small Cap Independent Producers								
Peyto Exploration and Development C	PEYUF		25.27	0.96	1.54	1.03	1.22	0.95
Range Resources	RRC	B	68.79	0.95	1.22	1.00	1.06	0.99
PDC Energy	PDCE		31.47	0.87	1.27	1.01	1.03	1.03
Birchcliff Energy Ltd.	BIREF	B	7.95	0.65	1.35	1.03	1.01	0.74
Cimarex Energy Company	XEC	CB	62.02	0.75	1.25	1.02	0.99	0.62
Denbury Resources Inc.	DNR		15.50	0.80	1.11	0.98	0.96	0.65
Whiting Petroleum Corporation	WLL	CB	44.36	0.76	1.16	0.97	0.95	0.59
Continental Resources (32%)	CLR	CB	70.53	0.77	1.12	0.95	0.93	0.75
Berry Petroleum Company	BRY		32.16	0.72	1.03	0.92	0.87	0.63
Halcón Resources	HK		6.21	0.57		0.94	0.78	0.71
	<i>Median</i>			<i>0.76</i>	<i>1.22</i>	<i>0.99</i>	<i>0.97</i>	<i>0.72</i>
Top Line Cash Payers								
Freehold Royalties Ltd.	FRHLF		21.36	0.99	1.26	1.04	1.09	1.02
Dorchester Minerals, L.P.	DMLP	CB	21.45	0.81	1.08	0.96	0.94	0.79
Sabine Royalty Trust	SBR		45.72	0.68	1.06	0.91	0.84	0.70
Permian Basin RT	PBT		13.48	0.58	1.12	0.93	0.73	0.67
Cross Timbers Royalty Trust	CRT		26.25	0.52	1.08	0.89	0.71	0.60
	<i>Median</i>			<i>0.68</i>	<i>1.08</i>	<i>0.93</i>	<i>0.84</i>	<i>0.70</i>
Bottom Line Cash Payers								
Linn Energy, LLC	LINE		38.88	0.95	1.08	0.97	1.00	1.16
Vanguard Natural Resources, LLC	VNR		27.72	0.95	1.12	0.98	1.00	1.06
Legacy Reserves L.P.	LGCY		24.41	0.87	1.04	0.91	0.92	0.87
Enerplus Corporation	ERF	CB	12.58	0.61	1.06	0.87	0.83	0.72
San Juan Basin Royalty Trust	SJT	CB	12.88	0.52	1.07	0.92	0.81	0.61
Hugoton RoyaltyTrust	HGT		7.80	0.36	1.37	1.14	0.81	0.56
Mesa RoyaltyTrust	MTR		22.29	0.50	1.10	0.90	0.72	0.56
	<i>Median</i>			<i>0.61</i>	<i>1.08</i>	<i>0.92</i>	<i>0.83</i>	<i>0.72</i>

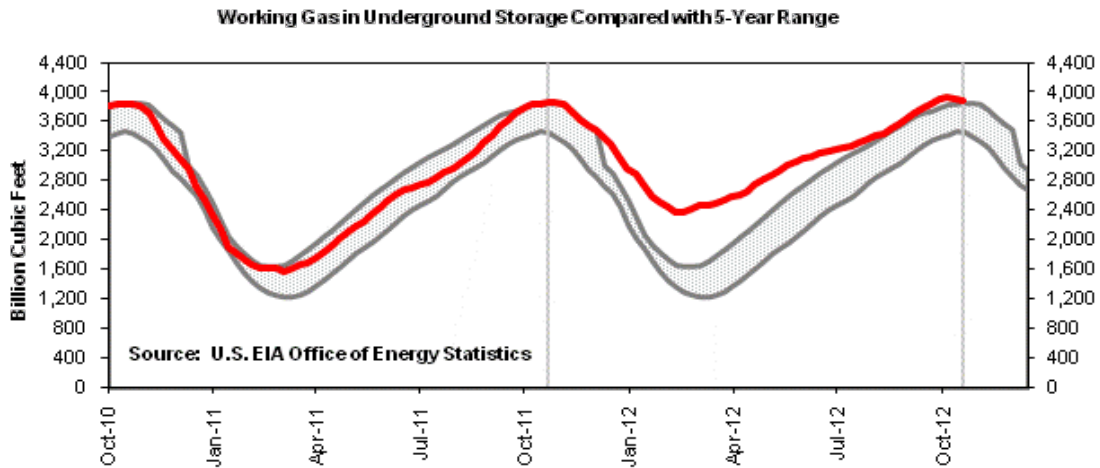
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