



# Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 11, 2009

## **San Juan Basin Royalty Trust Natural Gas Income with Strong Upside and Limited Downside**

### **Summary and Recommendation**

Direct participation in the commodity value of natural gas and tax-efficient distribution of income make us want to own units of buy-recommended **San Juan Basin Royalty Trust (SJT)**.

Looking at the price chart of six-year natural gas we see a base that has formed after a steep decline (see chart on page 2, [Natural Gas Six-Year Futures Strip](#)). The forced selling of the 2008 financial panic appears to have run its course while a new uptrend has not yet been confirmed despite several attempts. Further sustained decline seems unlikely barring an unfavorable political/economic surprise. In other words, the downside looks limited. Instead the main risk may be further delay before a renewed uptrend begins.

Considering that SJT is concentrated 100% on natural gas with no debt and no hedging, it is logical that the stock price chart for SJT looks like that for the long-term resource (see chart on page 2, [SJT](#)). Like most energy stocks, SJT price has begun an uptrend with current quote above the 200-day average. That may be a leading indicator for natural gas price to move to an uptrend as it was for a downtrend last year.

Natural gas price translates directly to income for SJT. Monthly Declarations are likely to rise considering we already know the price trends through February because of the two month lag from real-time production to distribution declaration (see table on page 3, [Monthly Declarations](#)). If current natural gas futures prices materialize, distributions will likely be higher for the rest of 2010 (see table on page 4, [Next Twelve Months Operating and Financial Estimates](#)).

Estimated Distribution Yield of 8.0% for the Next Twelve Months looks competitive among attractively priced income stocks (see Table 1). Actually it is better after our latest estimates as we take account of a narrower price discount for San Juan Basin natural gas relative to Louisiana and slightly better than expected volume. Moreover as we roll forward our Next Twelve Months period by another calendar quarter, expectations automatically rise with the price trend. McDep Ratio at 0.82 also looks attractive for new investment (see Table 1 and Table 2). Finally, unlevered cash flow multiple (EV/Ebitda) is modest at 10.0 times considering the quality of the trust's properties and the equivalent of direct ownership combined with the liquidity of a publicly traded security (see Table 3).

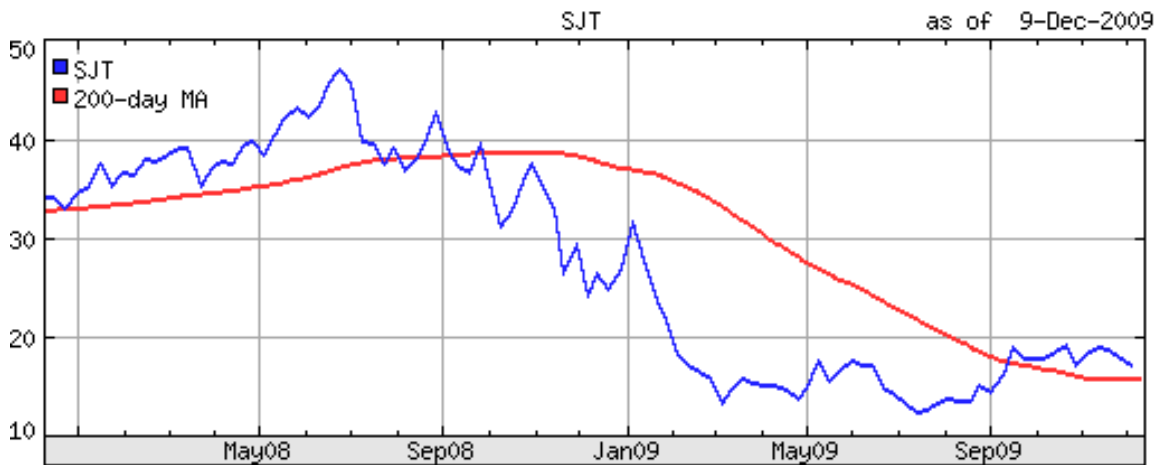
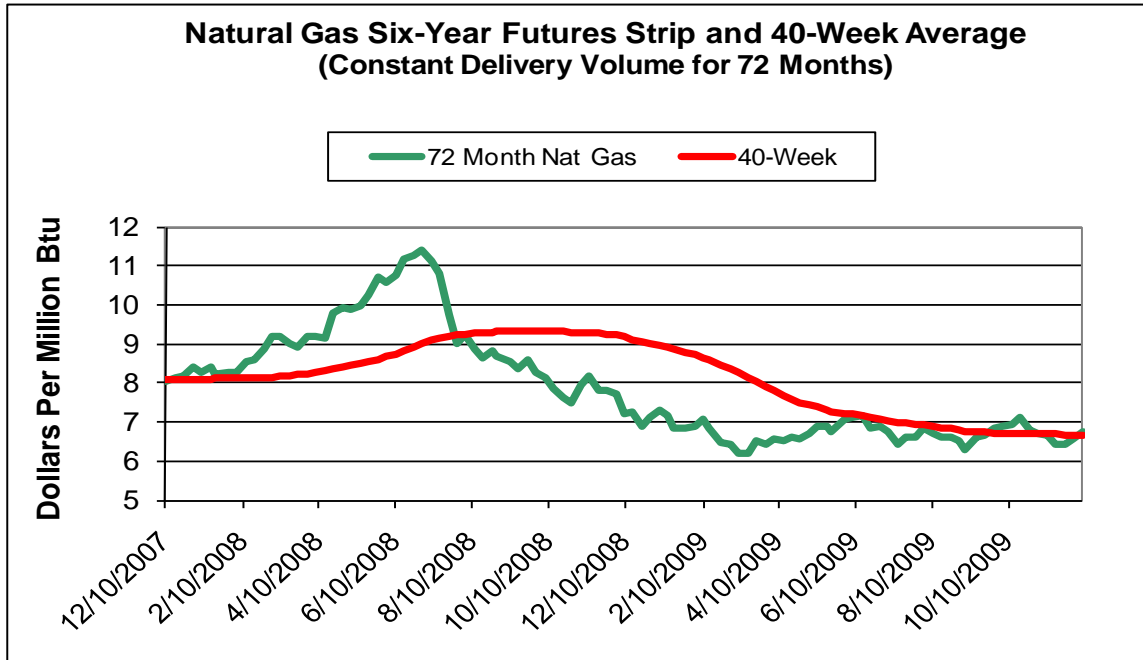
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San Juan Basin Royalty Trust									
Monthly Declarations									
	Dec-08	Jan-09	Sep-09	Oct-09	Nov-09	Dec-09	Jan-10	Feb-10	Mar-10
<b>Distribution (\$/unit)</b>									
Declared	0.16	0.04	0.05	0.10	0.05				
Projected						0.07	0.10	0.10	0.11
<b>Volume</b>									
Natural gas (mmbtu)	3.60	3.22	3.25	3.38	3.11	3.18	3.05	3.13	3.14
Heat Content(btu/cf)	1,062	1,081	1,089	1,088	1,089	1,083	1,085	1,085	1,086
Natural gas (bcf)	3.39	2.98	2.98	3.11	2.85	2.94	2.81	2.89	2.89
Natural Gas (mmcf)	109	99	96	100	95	95	94	93	93
Days	31	30	31	31	30	31	30	31	31
<b>Price</b>									
Natural gas industry quotes lagged two months (\$/mmbtu)									
Henry Hub Index/Futures	7.48	6.47	3.96	3.38	2.83	3.72	4.28	4.49	4.99
San Juan Monthly Index	4.27	2.84	2.98	3.18	2.48	3.42	4.26	4.28	4.50
San Juan Index/Henry Hub	0.57	0.44	0.75	0.94	0.88	0.92	1.00	0.95	0.90
SJT/San Juan Index	1.05	1.02	0.97	1.00	1.09	0.98	0.97	0.97	0.98
SJT (\$/mmbtu)	4.50	2.91	2.89	3.17	2.71	3.35	4.15	4.15	4.40
SJT (\$/mcf)	4.78	3.15	3.14	3.45	2.95	3.63	4.50	4.50	4.77
<b>Revenue (\$mm)</b>									
Natural Gas	16.2	9.4	9.4	10.7	8.4	10.7	12.6	13.0	13.8
Other	0.2	0.1	0.2	0.4	0.2	0.1	0.2	(0.1)	(0.2)
<b>Cost (\$mm)</b>									
Severance tax	1.6	1.0	1.0	1.1	0.9	1.1	1.3	1.3	1.4
Operating	3.2	3.2	2.6	2.2	2.1	2.6	2.6	2.5	2.5
Total	4.7	4.1	3.6	3.3	3.0	3.7	3.8	3.8	3.9
<b>Cash flow (\$mm)</b>									
Development	2.0	2.8	2.7	1.3	2.2	2.8	2.8	2.8	2.8
<b>Net proceeds (\$mm)</b>									
	9.7	2.6	3.3	6.5	3.4	4.4	6.2	6.2	6.8
<b>Royalty income (\$mm)</b>									
Royalty/Net proceeds	75%	75%	75%	75%	75%	75%	75%	75%	75%
One time				0.2					
<b>Distributable income (\$mm)</b>									
	7.3	1.9	2.5	4.7	2.5	3.3	4.7	4.7	5.1
<b>Units (millions)</b>									
	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6
<b>Distribution (\$/unit)</b>									
	0.16	0.04	0.05	0.10	0.05	0.07	0.10	0.10	0.11
<i>Latest Twelve Month Average</i>									
Heat Content(btu/cf)	1,081	1,080	1,082	1,082	1,083	1,085	1,085	1,086	1,086
Natural Gas (mmcf)	95	95	97	97	97	96	95	95	96
San Juan Index/Henry Hub	0.83	0.80	0.70	0.71	0.72	0.75	0.79	0.82	0.83
SJT/San Juan Index	1.00	1.00	0.97	0.97	0.98	0.97	0.97	0.98	0.98
Other revenue	0.2	0.2	0.0	0.0	(0.0)	(0.0)	0.0	0.0	0.0
Operating	2.7	2.8	2.8	2.8	2.7	2.6	2.6	2.6	2.5
Development	2.2	2.3	3.0	2.9	2.8	2.9	2.9	2.9	2.8
Severance tax/revenue	9.6%	9.6%	9.9%	10.0%	10.1%	10.1%	10.1%	10.1%	10.1%
Ebitda Margin	79%	78%	67%	65%	63%	62%	64%	64%	65%



# Income and Small Cap Weekly

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December 11, 2009

San Juan Basin Royalty Trust									
Next Twelve Months Operating and Financial Estimates									
									<i>Next</i>
	<i>Q4</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Next</i>
	<i>12/31/08</i>	<i>9/30/09</i>	<i>12/31/09</i>	<i>2008E</i>	<i>3/31/10</i>	<i>6/30/10</i>	<i>9/30/10</i>	<i>12/31/10</i>	<i>Twelve</i>
									<i>Months</i>
									<i>12/31/10</i>
<b>Highlights</b>									
Revenue (\$mm) (75%)	47.5	20.6	23.2	<b>88.5</b>	30.4	31.6	31.6	30.8	<b>124.4</b>
Cash flow (\$mm) (75%)	36.2	12.8	15.7	<b>56.2</b>	21.7	22.8	22.7	22.0	<b>89.3</b>
Per unit	0.78	0.27	0.34	<b>1.21</b>	0.47	0.49	0.49	0.47	<b>1.92</b>
Distributable Income (\$mm)	30.7	7.0	10.5	<b>28.3</b>	14.4	18.3	18.2	17.4	<b>68.4</b>
Per unit	0.66	0.15	0.23	<b>0.61</b>	0.31	0.39	0.39	0.37	<b>1.47</b>
Units (millions)	46.6	46.6	46.6	<b>46.6</b>	46.6	46.6	46.6	46.6	<b>46.6</b>
<b>Volume</b>									
Natural gas (mmbtu)	10.1	9.7	9.7	<b>37.8</b>	9.3	8.9	9.1	9.0	<b>36.4</b>
Heat Content(btu/cf)	1,075	1,090	1,087	<b>1,085</b>	1,085	1,085	1,086	1,085	<b>1,086</b>
Natural gas (bcf)	9.4	8.9	8.9	<b>34.9</b>	8.6	8.2	8.4	8.3	<b>33.6</b>
Natural Gas (mmcf)	102.1	96.9	96.7	<b>95.6</b>	93.4	92.4	91.5	90.6	<b>92.0</b>
Days	92	92	92	<b>365</b>	92	89	92	92	<b>365</b>
Oil (mb)	0.0	0.0	0.0	<b>0.1</b>	0.0	0.0	0.0	0.0	<b>0.1</b>
Oil (mbd)	0.2	0.2	0.2	<b>0.2</b>	0.2	0.2	0.2	0.2	<b>0.2</b>
Days	92	92	92	<b>365</b>	92	89	92	92	<b>365</b>
Total gas & oil (bcf)	9.5	9.0	9.0	<b>35.3</b>	8.7	8.3	8.5	8.4	<b>34.0</b>
<b>Price</b>									
Natural gas (\$/mmbtu) (Henry Hub lagged two months)									
Henry Hub (\$/mmbtu)	8.37	3.61	3.31	<b>4.37</b>	4.59	5.11	5.26	5.50	<b>5.11</b>
Differential (%)	16	24	7	<b>30</b>	8	10	15	20	<b>13</b>
Net to SJT (\$/mmbtu)	7.06	2.73	3.08	<b>3.04</b>	4.23	4.60	4.47	4.40	<b>4.42</b>
Natural gas (\$/mcf)	7.59	2.98	3.35	<b>3.30</b>	4.59	4.99	4.86	4.78	<b>4.80</b>
Oil (\$/bbl) (WTI Cushing lagged two months)									
WTI Cushing	99.06	64.29	72.10	<b>57.22</b>	75.63	77.41	80.27	82.02	<b>78.83</b>
SJT	88.98	56.08	62.90	<b>50.30</b>	66.49	68.05	70.57	72.11	<b>69.29</b>
Total gas & oil (\$/mcf)	6.69	3.05	3.43	<b>3.35</b>	4.67	5.06	4.94	4.86	<b>4.88</b>
<b>Revenue (\$mm)</b>									
Natural Gas	62.1	26.5	29.8	<b>115.0</b>	39.5	41.0	40.9	39.8	<b>161.2</b>
Oil	1.2	1.0	1.1	<b>3.1</b>	1.1	1.1	1.2	1.2	<b>4.6</b>
Total	63.4	27.5	30.9	<b>118.0</b>	40.6	42.1	42.1	41.0	<b>165.8</b>
<b>Cost (\$mm)</b>									
Severance tax	6.0	2.7	3.0	<b>11.6</b>	4.0	4.1	4.1	4.0	<b>16.3</b>
Operating	9.1	7.8	6.9	<b>31.5</b>	7.6	7.6	7.6	7.6	<b>30.5</b>
Total	15.1	10.4	9.9	<b>43.1</b>	11.6	11.8	11.7	11.7	<b>46.8</b>
<b>Cash flow (\$mm)</b>									
Development	7.1	7.4	6.3	<b>34.6</b>	8.5	5.5	5.5	5.6	<b>25.0</b>
<b>Net proceeds (\$mm)</b>									
Royalty income (\$mm)	30.8	7.2	11.0	<b>30.2</b>	15.4	18.7	18.6	17.8	<b>70.5</b>
Royalty/Net proceeds	75%	75%	75%	<b>75%</b>	75%	75%	75%	75%	<b>75%</b>
Administration	0.1	0.2	0.5	<b>1.9</b>	0.9	0.4	0.4	0.4	<b>2.1</b>
One-time				<b>-</b>					<b>-</b>
<b>Distributable income (\$mm)</b>									
Severance tax/revenue	9.5%	9.8%	9.8%	<b>9.8%</b>	9.8%	9.8%	9.8%	9.8%	<b>9.8%</b>
Operating cost (\$/mcf)	0.96	0.86	0.77	<b>0.89</b>	0.88	0.92	0.90	0.90	<b>0.90</b>
Development/Cash flow	15%	44%	30%	<b>46%</b>	29%	18%	18%	19%	<b>21%</b>



# Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 11, 2009

<b>Table 1</b>										
<b>McDep Income and Small Cap Energy Portfolio</b>										
<b>Debt, Business Segments and Income Yield</b>										
						<i>Present Value</i>				
						<i>by Segment (%)</i>				
	<i>Symbol/Rating</i>	<i>Price</i>	<i>EV/</i>	<i>Enterprise</i>	<i>NAmer.</i>		<i>Dist.</i>	<i>Dist.</i>		
	B = Buy	<i>10-Dec</i>	<i>Market</i>	<i>Value</i>	<i>Natural</i>	<i>Oil</i>	<i>NTM</i>	<i>Yield</i>	<i>McDep</i>	
	H = Hold	<i>2009</i>	<i>Cap</i>	<i>(\$mm)</i>	<i>Gas</i>	<i>Prod'n</i>	<i>(\$/un)</i>	<i>(%)</i>	<i>Ratio</i>	
<b>Canadian Income Trusts (US\$)</b>										
Penn West Energy Trust	PWE		16.78	1.58	11,200	22	78	1.70	10.1	0.92
Peyto Energy Trust	PEYUF		11.33	1.30	1,690	72	28	1.36	12.0	0.90
Pengrowth Energy Trust	PGH		9.22	1.56	4,200	35	65	0.79	8.6	0.84
Enerplus Resources Fund	ERF		22.68	1.22	4,700	42	58	2.04	9.0	0.79
Canadian Oil Sands Trust	COSWF	B	27.37	1.11	14,700		100	1.75	6.4	0.67
<i>Total or Median</i>					36,500					0.84
<b>Small Cap Independent Producers</b>										
Cimarex Energy Company	XEC	B	47.58	1.20	4,700	67	33	0.24	0.5	0.96
Encore Acquisition Company	EAC		45.75	1.68	4,020	22	78	-	-	0.95
Berry Petroleum Company	BRY		27.10	1.91	2,330	31	69	0.30	1.1	0.87
Birchcliff Energy Ltd. (US\$)	BIREF		7.38	1.21	1,180	64	36	-	-	0.85
<i>Total or Median</i>					12,200					0.91
<b>Top Line Cash Payers</b>										
Cross Timbers Royalty Trust	CRT		34.47	1.00	210	64	36	2.46	7.1	1.23
Freehold Royalty Trust (US\$)	FRHLF		14.28	1.21	860	25	75	1.62	11.4	0.86
Dorchester Minerals, L.P.	DMLP	B	20.51	1.00	610	68	32	1.64	8.0	0.76
Sabine Royalty Trust	SBR		40.95	1.00	600	38	63	2.88	7.0	0.74
Permian Basin RT	PBT		13.04	1.00	610	27	73	1.03	7.9	0.72
<i>Total or Median</i>					2,900					0.76
<b>Bottom Line Cash Payers</b>										
Linn Energy, LLC	LINE		25.22	1.56	4,480	36	64	2.52	10.0	1.35
Encore Energy Partners, L.P. (52%)	ENP		18.48	1.31	560	24	76	2.15	11.6	1.07
San Juan Basin Royalty Trust	SJT	B	17.12	1.00	800	100	-	1.37	8.0	0.82
Mesa Royalty Trust	MTR		36.60	1.00	68	75	25	2.40	6.6	0.76
Hugoton Royalty Trust	HGT	B	15.82	1.00	630	89	11	1.16	7.3	0.69
<i>Total or Median</i>					6,500					0.82
<b>Composite (excl COSWF)</b>										
<i>Enterprise Value Weighting</i>					43,400	39	61			0.91
<i>Equal Weighting</i>						50	50			0.89
<i>Equal Weighted Buys</i>						54	46			0.83

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 December 31, 2010. Enterprise Value = Market Cap and Debt.



# Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 11, 2009

Table 2								
Oil and Gas Income and Small Cap Stocks								
Net Present Value and McDep Ratio								
			Price (\$/sh)		Market Cap	Net Present Value	Debt/ Present Value	McDep Ratio
	Symbol/ Rating	10-Dec 2009	Shares (mm)		(\$mm)	(\$/un)		
<b>Canadian Income Trusts (US\$)</b>								
	PWE		16.78	420.0	7,050	19.00	0.34	0.92
	PEYUF		11.33	114.9	1,300	13.00	0.21	0.90
	PGH		9.22	290.0	2,670	12.00	0.30	0.84
	ERF		22.68	169.0	3,830	30.00	0.14	0.79
	COSWF	B	27.37	484.0	13,250	42.00	0.06	0.67
	<i>Total or Median</i>				28,100		0.21	0.84
<b>Small Cap Independent Producers</b>								
	XEC	B	47.58	82.2	3,910	50.00	0.16	0.96
	EAC		45.75	52.3	2,390	50.00	0.38	0.95
	BRY		27.10	44.9	1,220	35.00	0.41	0.87
	BIREF		7.38	132.5	980	9.00	0.15	0.85
	<i>Total or Median</i>				8,500		0.27	0.91
<b>Top Line Cash Payers</b>								
	CRT		34.47	6.0	210	28.00	-	1.23
	FRHLF		14.28	49.6	710	17.00	0.15	0.86
	DMLP	B	20.51	29.8	610	27.00	-	0.76
	SBR		40.95	14.6	600	55.00	-	0.74
	PBT		13.04	46.6	610	18.00	-	0.72
	<i>Total or Median</i>				2,740			0.76
<b>Bottom Line Cash Payers</b>								
	LINE		25.22	114.0	2,880	15.00	0.48	1.35
	ENP		18.48	23.2	430	17.00	0.25	1.07
	SJT	B	17.12	46.6	800	21.00	-	0.82
	MTR		36.60	1.9	68	48.00	-	0.76
	HGT	B	15.82	40.0	630	23.00	-	0.69
	<i>Total or Median</i>				4,810			0.82
B = Buy, Hold ratings discontinued October 23, 2009								
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

December 11, 2009

Table 3								
Oil and Gas Income and Small Cap Stocks								
Value Multiples - Rank by EV/Ebitda								
			Price (\$/sh)	Revenue	Dist/ Equity	Adjstd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda
	Symbol/ Rating		10-Dec 2009	Royalty (%)	Ebitda	NTM	NTM	NTM
<b>Canadian Income Trusts (US\$)</b>								
	PEYUF		11.33		1.37	18.2	13.1	11.7
	COSWF	B	27.37		0.56	23.1	13.5	9.1
	PWE		16.78		0.78	8.3	8.7	8.0
	ERF		22.68		0.63	9.8	9.3	7.4
	PGH		9.22		0.53	8.3	8.1	6.8
	<i>Median</i>					9.8	9.3	8.0
<b>Small Cap Independent Producers</b>								
	BIREF		7.38		-	10.6	15.8	13.4
	EAC		45.75		-	11.7	8.0	7.6
	BRY		27.10		-	12.4	7.8	6.8
	XEC	B	47.58		-	7.6	5.4	5.1
	<i>Median</i>					11.2	7.9	7.2
<b>Top Line Cash Payers</b>								
	SBR		40.95	100	1.00	11.7	19.1	14.2
	CRT		34.47	84	0.95	12.7	10.8	13.2
	DMLP	B	20.51	64	0.89	7.8	14.7	11.2
	PBT		13.04	32	0.87	11.6	15.3	11.1
	FRHLF		14.28	71	0.92	6.8	9.6	8.3
	<i>Median</i>					11.6	14.7	11.2
<b>Bottom Line Cash Payers</b>								
	LINE		25.22		2.27	18.3	13.5	18.3
	MTR		36.60		0.88	9.2	17.6	13.3
	SJT	B	17.12		0.80	9.3	12.3	10.0
	HGT	B	15.82		0.70	13.4	13.8	9.5
	ENP		18.48		1.12	13.2	8.8	9.4
	<i>Median</i>					13.2	13.5	10.0
EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended December 31, 2010; 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

December 11, 2009

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