McDep Energy Income Producers
A Weekly Analysis of Royalty Trusts and Master Limited Partnerships
March 9, 2004

Canadian Oil Sands Volatility Gift

Summary and Recommendation

There appears to be a special opportunity in buy-recommended **Canadian Oil Sands Trust (COSWF, COS.UN Toronto)** after the stock declined in price by 22% in two days while its future appears practically undimmed. True, a 40% expansion of capacity will cost about 15% of previous stock price more than previously publicized. Yet, prudent investors allow for cost overruns as we did in our present value calculations. We explained between the time of the announcement and the resumption of trading that our estimate of present value remained unchanged at US$50 per unit (see *Stock Idea*, March 5, 2004). At the current price of about US$31.50 the stock has the lowest McDep Ratio not only among our 16 buy recommendations, but also among 73 stocks in our research coverage.

Should Heads Roll?

Mr. Marcel Coutu, the chief executive of COS, and also chairman of the Syncrude joint venture, apparently was surprised at the magnitude of the now expected cost overrun. Nonetheless we noticed that Mr. Coutu's presentations in recent months have included progress reports that showed a slippage in schedule. Meanwhile, COS is essentially a financial partner in Syncrude rather than the source of engineering and operating expertise.

Ultimately the responsibility rests with the largest oil company in the world, **ExxonMobil (XOM)**. The global giant owns 70% of **Imperial Oil (IMO)** that in turn owns 25% of the oil sands joint venture, Syncrude. Mr. Charles Ruigrok, the chief executive of Syncrude is an employee of IMO. He was put in charge only last year. We believe that Mr. Ruigrok has the personal support of the chief executive of Imperial, Mr. Tim Hearn, who in turn has the personal support of the chief executive of Exxon, Mr. Lee Raymond. One might reckon that the revised cost estimate and schedule reflect the fresh approach of a new chief executive determined to make the project succeed. We believe that XOM is a competent company.

Not a Complete Surprise

Showing little tolerance for the slippage in schedule last year, the chief executive of Syncrude apparently called on partner engineers with world wide experience to take a closer look. Other Syncrude partners include **Petro-Canada (PCZ)** at 12%, **ConocoPhillips (COP)** at 9% and **Murphy (MUR)** at 5%. The inescapable conclusion was that the refinery portion of the expansion would require additional man-hours. The cost of the additional effort created an overrun. A decision not to expand the workforce stretched out the time.

We had a cushion in our capital expenditure estimates that covered more than half of the overrun. Nor is the valuation impact of a year delay as great as it might seem in different circumstances. In today's era of low capital cost, the diminished time value of money makes the future worth more relative to the near-term. Most of the appeal in COS is in the long life of its production. We also have a cushion in our 9.1% per year discount rate that is higher than necessary in a low capital cost environment.

Dividend 4.7% Annually While Awaiting Tripling

There are no plans to change the current annual distribution of C$2 per unit payable quarterly at this time. Ignoring hedges, after interest and assuming recent futures prices, current cash flow is running about C$7 per unit for the next twelve months ended March 31, 2005. Our initial target set two years ago that the dividend could double in 2006 and triple by the end of 2007 is still reasonable to us. Our recent statement that the dividend could triple after the expansion is complete in mid 2005 might have suggested that the timing could be moved up, but the latest announcement puts off the in-service date of the capacity expansion to mid 2006. Recall that the expansion under way would increase current capacity by 40% to 350 thousand barrels daily.

Ample Financial Capacity for New Capital Requirements

The trust's share of capital expenditures planned by the Syncrude joint venture is about C$1 billion in 2004 and C$600 in 2005, the last year of major outlays. At current cash flow those amounts are covered when supplemented by funds to be drawn on the current line of credit. Current debt is just 0.22 times present value as we quote it. In this era of low capital cost, more capital should be readily available on favorable terms, if necessary.

Management apparently would also consider an underwriting of new units. Though not needed at current oil price, the new equity could be helpful in event of a steep decline in oil price that seems unlikely, but cannot be ruled out. Meanwhile the longer that oil price remains in an uptrend, the less likely there would be any need for a new stock offering. We might add that last year's equity financing was amply justified to help finance the purchase of an additional interest in the Syncrude venture at a price below what it would be today.

The structure of the securities market may be contributing to the otherwise unexplained volatility in COS stock. Sellers may be expecting a new equity financing to cover some of the overrun of $US 500 million. In fact the financing may have already occurred as more than $US100 million of COS shares were transferred to buyers on March 5. Some sellers may expect to buy the stock back if a "bought deal financing" is announced. Yet, it is a free market and buyers today can take advantage of volatility. It can be especially attractive to accumulate COS before a financing in anticipation of gains thereafter as we have seen in the past year. Moreover, we do not believe a financing is necessary in which case the stock can also move back to its previous level and beyond.

Massive New Energy Projects Raise Value of Existing Supply

North American natural gas and international oil are both capacity-constrained. The expected solution is more and more large projects. For example, we don't believe for an instant that large quantities of liquefied natural gas will be available at the popularly quoted $3.50 an mcf. Also, new oil supplies from Iraq, Russia and even Saudi Arabia involve more capital-intensive, massive construction projects than historically.

The higher cost of new supply puts a floor under market prices and raises the value of existing supply. At Canadian Oil Sands Trust, the incremental 100 thousand barrels daily of capacity for Syncrude may be more expensive, but the base 250 thousand barrels daily is strongly profitable.

Kurt H. Wulff, CFA

McDep Energy Income Producers
Rank by McDep Ratio: Market Cap and Debt to Present Value

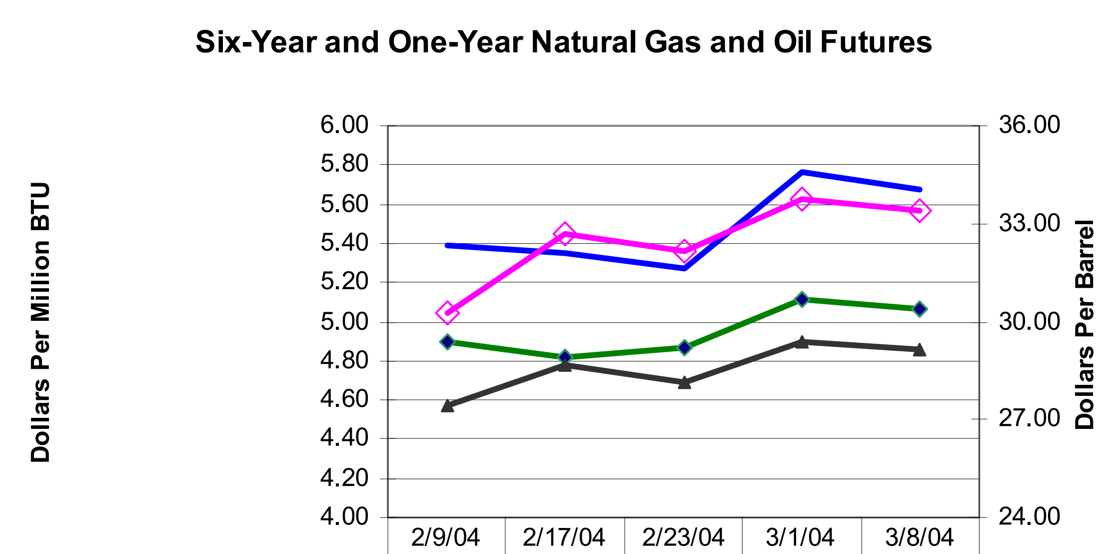
	Symbol/	Rating	Price ($/sh) 8-Mar 2004	Shares (mm)	Market Cap ($mm)	Net Present Value ($/sh)	Debt/ Present Value	McDep Ratio
Master Limited Partnerships and Canadian Royalty Trusts								
Kinder Morgan Energy Partners, L.P.	KMP	S	45.57	140.1	6,380	14.00	0.48	2.17
Kinder Morgan Management, LLC	KMR	S	42.95	48.6	2,090	14.00	0.48	2.07
Enerplus Resources Fund	ERF		30.90	88.5	2,740	25.00	0.14	1.20
Pengrowth Energy Trust	PGH		13.93	122.0	1,700	12.00	0.16	1.13
Provident Energy Trust	PVX		8.14	70.6	580	7.50	0.25	1.06
Dorchester Minerals, L.P.	DMLP		18.00	27.0	490	17.00	-	1.06
Canadian Oil Sands Trust (US$)	COSWF	B	31.54	86.9	2,740	50.00	0.22	0.71
Total or Median					*16,700*		*0.22*	*1.13*
U.S. Royalty Trusts								
Sabine Royalty Trust	SBR		31.37	14.6	460	26.00	-	1.21
Permian Basin RT (41%)	PBT		8.63	19.1	170	7.50	-	1.15
Cross Timbers Royalty Trust	CRT		26.89	6.0	161	25.00	-	1.07
Hugoton RoyaltyTrust (46%)	HGT		20.40	18.4	380	20.00	-	1.02
San Juan Basin Royalty Trust	SJT	B	19.93	46.6	930	22.00	-	0.91
Total or Median					*2,100*		-	*1.07*

Buy/Sell rating after symbol: B - Buy, S - Sell
McDep Ratio = **M**arket **c**ap and **De**bt to **p**resent value of oil and gas and other businesses

McDep Energy Income Producers
Rank by EV/Ebitda: Enterprise Value to Earnings Before Interest, Tax, Deprec.

	Symbol/	Rating	Price ($/sh) 8-Mar 2004	EV/ Sales NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)	PV/ Ebitda NTM
Master Limited Partnerships and Canadian Royalty Trusts								
Kinder Morgan Energy Partners, L.P.	KMP	S	45.57	3.3	19.3	23	6.0	8.9
Kinder Morgan Management, LLC	KMR	S	42.95	3.1	18.5	22	6.3	8.9
Dorchester Minerals, L.P.	DMLP		18.00	9.4	10.4	24	9.6	9.8
Canadian Oil Sands Trust (US$)	COSWF	B	31.54	4.1	7.7	12	4.7	10.8
Enerplus Resources Fund	ERF		30.90	5.4	7.2	11	10.2	6.0
Pengrowth Energy Trust	PGH		13.93	4.7	6.7	13	13.5	5.9
Provident Energy Trust	PVX		8.14	3.6	5.3	18	13.2	5.0
Median				*4.1*	*7.7*	*18*	*9.6*	*8.9*
U.S. Royalty Trusts								
Cross Timbers Royalty Trust	CRT		26.89	7.7	10.7	11	9.1	10.0
Sabine Royalty Trust	SBR		31.37	10.2	10.5	11	9.5	8.7
Permian Basin RT (41%)	PBT		8.63	6.9	9.5	11	8.7	8.3
Hugoton RoyaltyTrust (46%)	HGT		20.40	6.4	8.4	10	9.9	8.2
San Juan Basin Royalty Trust	SJT	B	19.93	6.6	8.1	10	9.9	8.9
Median				*6.9*	*9.5*	*11*	*9.5*	*8.7*

EV = Enterprise Value = Market Cap and Debt; Ebitda = Earnings before interest, tax, depreciation and amortization; NTM = Next Twelve Months Ended March 31, 2005; P/E = Stock Price to Earnings; PV = Present Value of oil and gas and other businesses



	2/9/04	2/17/04	2/23/04	3/1/04	3/8/04
12 Month Natural Gas	5.39	5.35	5.27	5.76	5.67
72 Month Natural Gas	4.90	4.82	4.87	5.11	5.06
12 Month Oil	30.27	32.70	32.16	33.76	33.39
72 Month Oil	27.41	28.67	28.16	29.37	29.16