

Rating: Buy
S&P 500: 1273

Occidental Petroleum Independent Oil Producer

<i>Symbol</i>	OXY	<i>Ebitda Next Twelve Months ending 12/31/06 (US\$m)</i>	9,900
<i>Rating</i>	Buy	<i>North American Natural Gas/Ebitda (%)</i>	13
<i>Price (US\$/sh)</i>	84.95	<i>Natural Gas and Oil Production/Ebitda (%)</i>	90
<i>Pricing Date</i>	1/4/06	<i>Adjusted Reserves/Production NTM</i>	11.3
<i>Shares (mm)</i>	432	<i>EV/Ebitda</i>	4.5
<i>Market Capitalization (US\$m)</i>	36,700	<i>PV/Ebitda</i>	6.0
<i>Debt (US\$m)</i>	7,200	<i>Undeveloped Reserves (%)</i>	24
<i>Enterprise Value (EV) (US\$m)</i>	43,900	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	38.60
<i>Present Value (PV) (US\$m)</i>	59,000	<i>Present Value Proven Reserves(US\$/boe)</i>	17.90
<i>Net Present Value (US\$/share)</i>	120	<i>Present Value Proven Reserves(US\$/mcf)</i>	2.98
<i>Debt/Present Value</i>	0.12	<i>Earnings Next Twelve Months (US\$/sh)</i>	11.17
<i>McDep Ratio - EV/PV</i>	0.74	<i>Price/Earnings Next Twelve Months</i>	8
<i>Dividend Yield (%/year)</i>	1.7	<i>Indicated Annual Dividend (US\$/sh)</i>	1.44

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.

Summary and Recommendation

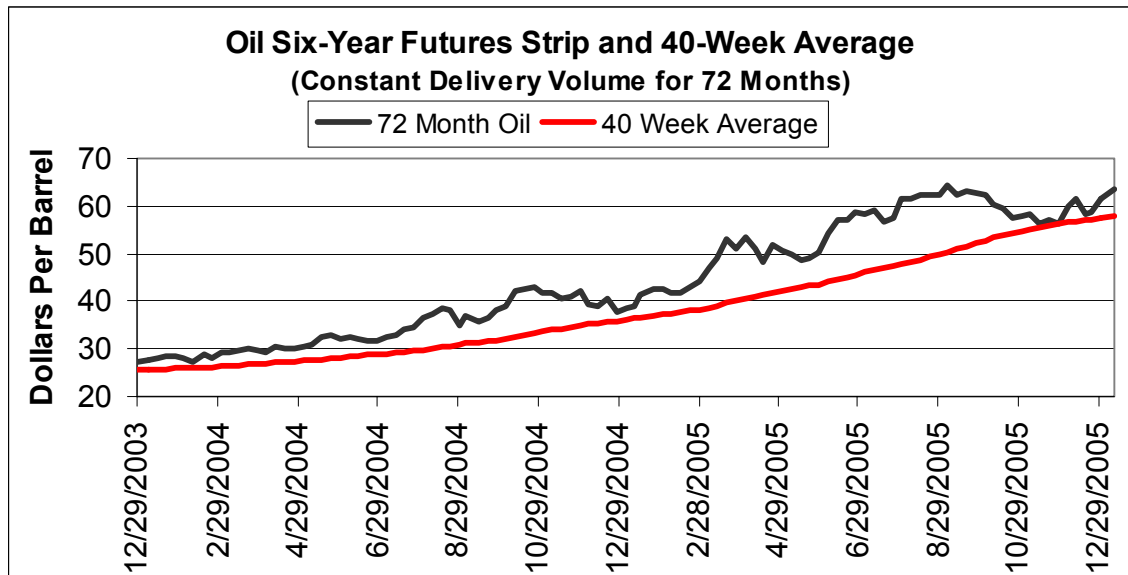
Buy-recommended **Occidental Petroleum (OXY)** offers 41% appreciation potential to estimated net present value of \$120 a share, unchanged since August 2005. New projections include the operations of Vintage Petroleum presuming the near \$4 billion deal is approved by selling shareholders at a meeting scheduled for January 26. Our correlation of cash flow multiple and reserve life for 30 companies indicates net present value about \$3 a share higher than our official estimate. Fourth quarter earnings are expected to be reported around January 30 and management will present to analysts at the end of February. Oxy may be an attractive takeover target. Patient investors may see appreciation for oil producers during the rest of the decade subject to political and economic risk.

McDep Ratio Relates Oil Price to Opportunity

A low McDep Ratio tells us that Oxy's market cap and debt, or enterprise value, is less than the estimated present value of its energy resources assuming a long-term real price of \$50 a barrel for Light, Sweet Crude Oil. Alternatively we could say that Oxy's stock is priced for \$37 oil, an approximation derived by multiplying \$50 times the McDep Ratio.

Meanwhile six-year oil futures are about \$63 a barrel. Momentum has been positive for more than three years as the current quote stays above the 40-week average (see chart [Oil Six-Year Futures and 40-Week Average](#)). Six-year oil has tripled in the four years we have been calculating it on a weekly basis. We do not need further gains in oil price to make money in buy recommendations. Yet our vision of \$150 oil in 2010 implies additional scope to exceed common expectations.

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Oxy's McDep Ratio ranks low along with peer companies (see table [Rank by McDep Ratio](#)). Aside from the fundamental appreciation potential we outlined above, a McDep Ratio of 1.0 is an indication of takeover value. The McDep Ratio of peer company, buy-recommended **Burlington Resources (BR)**, increased to 1.0 immediately after buy-recommended **ConocoPhillips (COP)** announced its takeover offer. Since then we revised BR's present value upward to represent the present value in COP stock that would be exchanged for BR stock.

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

	Symbol/ Rating	Price (\$/sh) 4-Jan 2006	Shares (mm)	Market Cap (\$mm)	Net Present Value (\$/sh)	Debt/ Present Value	McDep Ratio
Independent Natural Gas and Oil - Large Cap and Mid Cap							
XTO Energy Inc.	XTO B	45.31	370	16,760	48.00	0.20	0.95
Encana Corporation	ECA B	46.30	876	40,600	51.00	0.20	0.93
CNOOC Limited (29%)	CEO B	70.15	119	8,370	84.00	0.00	0.84
Devon Energy Corporation	DVN B	65.99	454	30,000	86.00	0.15	0.80
Burlington Resources	BR B	87.40	381	33,300	115.00	-	0.76
Occidental Petroleum Corp.	OXY B	84.95	432	36,700	120.00	0.12	0.74
Anadarko Petroleum Corp.	APC B	98.27	238	23,400	140.00	0.12	0.74
<i>Total or Median</i>				<i>189,000</i>		<i>0.12</i>	<i>0.80</i>

Low Cash Flow Multiple

Unlevered cash flow multiples in mid to low single digits attest to low valuation (see table [Rank by EV/Ebitda](#)). Multiples may be low because investors do not think cash flow will last long at current levels. That depends on commodity price and reserve life. Cash flow estimated for the next twelve months, Ebitda NTM, reflects latest futures prices. Reserve life is measured as adjusted reserves divided by next twelve months

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production. Apparently longer life for Oxy's properties contributes to a more undervalued ranking by McDep Ratio than by unlevered cash flow multiple.

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

	Symbol/ Rating		Price (\$/sh) 4-Jan 2006	Adjstd Resrvs/ Prod NTM	PV/ Ebitda NTM	EV/ Ebitda NTM	P/E NTM	Divd or Distrib NTM (%)
Independent Natural Gas and Oil - Large Cap and Mid Cap								
XTO Energy Inc.	XTO	B	45.31	10.8	6.4	6.1	10	0.4
Encana Corporation	ECA	B	46.30	7.1	5.5	5.1	10	0.6
Anadarko Petroleum Corp.	APC	B	98.27	12.5	6.4	4.7	9	0.7
Occidental Petroleum Corp.	OXY	B	84.95	11.3	6.0	4.5	8	1.7
CNOOC Limited (29%)	CEO	B	70.15	9.2	5.2	4.3	8	3.3
Devon Energy Corporation	DVN	B	65.99	7.8	4.9	3.9	7	0.5
Burlington Resources	BR	B	87.40	-	-	-	-	-
	<i>Median</i>			9.2	5.5	4.5	8	0.6

Concentration on Oil

Each oil and gas stock has its own unique mix of energy resources (see table Business Segments). Oxy is one of two close peers concentrated on oil while the other four are concentrated on natural gas. While we hold our present value estimates steady for months, prices of peer stocks may react in the short-term depending on relative changes in expectations for natural gas and oil. We recommend that investors have both natural gas and oil representation.

Home Country and Business Segments

	Symbol/ Rating		Non- U.S. Domicile	North Amer. Natural Gas (%)	Rest of World Natural Gas (%)	Oil Prod'n (%)	Down- stream (%)	Total Present Value (US\$mm)
Independent Natural Gas and Oil - Large Cap and Mid Cap								
Encana Corporation	ECA	B	Canada	83	-	17	-	55,600
Occidental Petroleum Corp.	OXY	B		14	1	75	11	59,000
Devon Energy Corporation	DVN	B		64	-	36	-	46,000
Anadarko Petroleum Corp.	APC	B		60	-	40	-	37,700
Burlington Resources	BR	B						
CNOOC Limited	CEO	B	China	-	12	88	-	34,600
XTO Energy Inc.	XTO	B		83	-	17	-	22,100
	<i>Median</i>			62	-	38	-	255,000

Static Present Value Justified by Dynamic Cash Flow

Present value analysis presumes that fundamental value is measured by the projection of cash flows years into the future and bringing them to the present applying a real discount rate, currently 7% a year. We generally hold present value estimates static until there is justification to make new commodity price assumptions.

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Next Twelve Months (NTM) cash flow represents the volumes and costs that form the base for future projections. Reserve life index tells how long cash flow will last. NTM cash flow and reserve life are the two main variables in our correlation by function for about 30 companies. Net present value indicated by the current combined correlation is about \$8 a share higher than our ongoing standard estimate for the company (see table Functional Cash Flow and Present Value).

Occidental Petroleum Corporation
Functional Cash Flow and Present Value

	<i>NTM Ebitda</i> <i>(US\$mm)</i>	<i>Adjusted</i> <i>R/P</i>	<i>PV/</i> <i>Ebitda</i>	<i>Present</i> <i>Value</i> <i>(US\$mm)</i>	
North American Natural Gas	1,268	9.1	6.4	8,100	14%
Rest of World Natural Gas	87	17.8	5.8	500	1%
Oil	7,534	11.5	5.9	44,200	75%
Downstream	969		6.4	6,200	11%
	9,857	11.3	6.0	59,000	100%
Debt (US\$mm)				7,200	
Net Present Value (US\$mm)				51,800	
Shares (mm)				432	
Net Present Value (US\$/sh)				120	
Over (-)/ Under (+) Correlation (US\$/sh)				8	

Futures Prices Propel Estimated Cash Flow by Quarter

Properties to be acquired with Vintage are included in the estimated results for 2006 to facilitate consistent relative valuation. In reality, production from the Vintage resources may be included for just part of the first quarter because the deal has not yet closed. Cash flow for the next year is projected from a base through the latest reported quarter (see table Next Twelve Months Operating and Financial Estimates). Company disclosures provide the clues for future volumes and costs as well as geographic and quality differences in price. Futures prices from the New York Mercantile Exchange determine industry benchmarks for the next year in our model.

Kurt H. Wulff, CFA

Occidental Petroleum
Next Twelve Months Operating and Financial Estimates

	<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 Twelve Months</i>
	<i>12/31/04</i>	<i>9/30/05</i>	<i>12/31/05</i>	<i>2005E</i>	<i>3/31/06</i>	<i>6/30/06</i>	<i>9/30/06</i>	<i>12/31/06</i>	<i>12/31/06</i>
Volume									
Natural Gas (mmcf)									
U.S. (or North America)	499	564	564	551	640	640	640	640	640
Overseas (or Int'l)	145	116	116	125	150	150	150	150	150
Total	644	680	680	676	790	790	790	790	790
Oil (mbd)	427	449	449	435	500	500	500	500	500
Total gas & oil (mmb)	49	52	52	200	57	57	58	58	231
Total gas & oil (mbd)	534	562	562	548	632	632	632	632	632
Price									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	7.10	8.56	13.00	8.65	10.15	9.80	9.91	10.55	10.10
U.S. (or North America)	5.65	6.33	9.61	7.05	7.50	7.25	7.33	7.80	7.47
Overseas (or Int'l)	1.53	2.19	2.19	1.92	2.19	2.19	2.19	2.19	2.19
Total	4.72	5.62	8.35	6.10	6.49	6.29	6.35	6.73	6.47
Oil (\$/bbl)									
WTI Cushing	48.31	62.52	59.99	56.30	62.65	64.98	65.67	66.04	64.83
Worldwide	39.11	55.04	52.81	49.16	55.15	57.21	57.81	58.14	57.09
Total gas & oil (\$/bbl)	36.95	50.75	52.26	46.58	51.78	53.14	53.71	54.44	53.28
Revenue (\$mm)									
Natural Gas									
U.S. (or North America)	259	328	499	1,418	432	422	431	459	1,745
Overseas (or Int'l)	20	23	23	87	30	30	30	30	120
Total	280	352	522	1,505	462	452	462	489	1,865
Oil	1,536	2,274	2,182	7,812	2,482	2,603	2,659	2,674	10,418
Other	1,266	1,432	1,432	5,734	1,432	1,432	1,432	1,432	5,726
Total	3,082	4,057	4,135	15,050	4,375	4,486	4,553	4,595	18,009
Expense (\$mm)									
Fixed	174	362	362	1,206	391	391	391	391	1,564
Variable	174	362	373	1,217	439	455	465	472	1,831
Other	1,069	1,189	1,189	4,670	1,189	1,189	1,189	1,189	4,757
Ebitda (\$mm)									
Exploration and Production	1,469	1,901	1,968	6,894	2,114	2,209	2,265	2,301	8,888
Other	197	242	242	1,063	242	242	242	242	969
Total Ebitda	1,665	2,143	2,210	7,958	2,356	2,451	2,507	2,543	9,857
Exploration	88	55	90	303	90	90	90	90	360
Deprec., Deplet., & Amort.	333	376	376	1,452	464	464	464	464	1,856
Other non cash									
Ebit	1,244	1,712	1,744	6,203	1,802	1,897	1,953	1,989	7,641
Interest	63	40	40	202	55	55	55	55	220
Ebt	1,181	1,672	1,704	6,001	1,747	1,842	1,898	1,934	7,421
Income Tax	413	585	597	2,100	611	645	664	677	2,597
Net Income (\$mm)									
Exploration and Production	977	1,769							
Other	130	167							
Unallocated	(339)	(849)							
Total	768	1,087	1,108	3,900	1,135	1,197	1,234	1,257	4,824
Shares (millions)	406	404	404	405	432	432	432	432	432
Per share (\$)	1.89	2.69	2.74	9.63	2.63	2.77	2.86	2.91	11.17
Ebitda Margin (E&P)	81%	72%	73%	74%	72%	72%	73%	73%	72%
Tax Rate	35%	35%	35%	35%	35%	35%	35%	35%	35%

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