



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 21, 2012

Last Chance for Opportunistic Year-End Buys

Summary and Recommendation

Small cap and income stocks that have fallen sharply in price during 2012 may get a bounce in price in the new year including, in order of increasing year-to-date total return, **HGT, MTR, BIREF, CRT, ERF, SJT, PBT** and **SBR**. We believe the returns ranging from -58% to -27% are greatly overdone because we don't see underlying fundamental changes anywhere near that magnitude. Those stocks are essentially in the same businesses as the large cap stocks which as a group are up in 2012. The main underlying fundamental factor is volume, which is up or stable for each of the stocks. Price can be more volatile and is less predictable for next year. The global economy could go into recession next year, though the rest of the stock market does not seem to act as if that will be the case. Our personal bet is 70% probability of growth and 30% probability of recession and we have allocated our assets accordingly. With reasonable growth, oil price ought to be stable to up subject to local bottlenecks where producing capacity is expanding faster than transportation capacity. Natural gas price has been on an advancing trend from the weather-induced lows of 2012. That trend can continue subject to weather.

After analyzing monthly distributions declared on December 20 by five of the eight depressed stocks, we raise our estimate for **Cross Timbers Royalty Trust (CRT)** to \$2.94 a unit for 2012. That implies a cash yield of 10.8% (see Tables [ISC-1](#) through [ISC-3](#)).

We are pleasantly surprised to see that the trustee of **Permian Basin Royalty Trust (PBT)** disclosed monthly underlying volume for the first time. The message is that oil production in the trust's Texas oil fields is growing, not declining as the distribution trend might suggest. We had seen signs of that growth in disclosures by the state regulatory body and now it is confirmed. The operator of the trust's properties has completed another of several horizontal wells that are likely driving the volume increases. Since the cost of those expensive wells is deducted immediately from what otherwise would be distributed, monthly income is reduced. We forecast a distribution of \$1.04 a unit in 2012 for a cash yield of 8.5%. Spending could reduce distribution more than we project, but the resulting higher volume could raise distribution. Since the operator does not offer guidance, we rely on the reported trends for guidance.

Contrarian Buy **San Juan Basin Royalty Trust (SJT)** will distribute \$0.03 a unit for December, up from nil last month. Increased spending on growth capacity accounted for the difference compared to our estimate of \$0.06. SJT is a core recommendation in our RTF (Royalty Trust Fund) group. We believe investors have a particularly good chance to make money on any of the RTF stocks most depressed in price.

Kurt H. Wulff, CFA



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 21, 2012

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	20-Dec	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		33.89	1.77	1,810	52	48	14.0	-	-	1.07
Range Resources	RRC	B	63.38	1.34	13,570	75	25	16.9	0.16	0.3	0.93
Peyto Exploration and Developmen	PEYUF		22.61	1.23	3,980	76	24	10.5	0.73	3.2	0.86
Continental Resources (32%)	CLR	B	75.39	1.22	5,370	24	76	7.4	-	-	0.79
Halcón Resources	HK		6.93	1.62	3,820	15	85	5.8	-	-	0.79
Birchcliff Energy Ltd.	BIREF	B	7.45	1.47	1,630	63	37	9.7	-	-	0.71
Denbury Resources Inc.	DNR		16.38	1.50	9,620	6	94	6.3	-	-	0.68
Berry Petroleum Company	BRY		34.50	1.92	3,670	12	88	5.3	-	-	0.65
Cimarex Energy Company	XEC	CB	59.28	1.27	6,540	41	59	5.2	0.48	0.8	0.60
Whiting Petroleum Corporation	WLL	CB	43.13	1.41	7,260	9	91	4.7	-	-	0.58
<i>Total or Median</i>				<i>1.44</i>	<i>57,300</i>	<i>33</i>	<i>67</i>	<i>6.8</i>			<i>0.75</i>
Leveraged Cash Payers											
Linn Energy, LLC	LINE		37.07	1.67	14,430	43	57	12.9	2.90	7.8	1.13
Vanguard Natural Resources, LLC	VNR		26.70	1.65	2,330	33	67	11.8	2.40	9.0	1.04
Legacy Reserves L.P.	LGCY		23.75	1.52	1,710	25	75	9.1	2.26	9.5	0.85
Enerplus Corporation	ERF	CB	12.99	1.71	4,400	31	69	6.3	1.10	8.4	0.74
<i>Total or Median</i>				<i>1.66</i>	<i>22,900</i>	<i>32</i>	<i>68</i>	<i>10.4</i>		<i>8.7</i>	<i>0.95</i>
RTF Cash Payers											
Freehold Royalties Ltd.	FRHLF		22.47	TL	1,540	16	84	11.1	1.70	7.6	1.07
Enduro Royalty Trust (40%)	NDRO		16.42	BL	220	43	57	9.1	1.80	11.0	0.78
Dorchester Minerals, L.P.	DMLP	CB	20.48	TL	630	57	43	10.4	1.77	8.7	0.76
Sabine Royalty Trust	SBR		41.63	TL	610	51	49	10.7	3.90	9.4	0.64
Cross Timbers Royalty Trust	CRT		27.22	TL	160	70	30	8.9	2.94	10.8	0.62
Permian Basin RT	PBT		12.25	TL	570	33	67	8.2	1.04	8.5	0.61
San Juan Basin Royalty Trust	SJT	CB	12.58	BL	590	100	-	8.4	1.14	9.1	0.60
Hugoton RoyaltyTrust	HGT		7.29	BL	290	88	13	6.4	0.55	7.6	0.52
Mesa RoyaltyTrust	MTR		20.13	BL	38	75	25	8.2	1.98	9.8	0.51
<i>Total or Median</i>					<i>4,600</i>	<i>57</i>	<i>43</i>	<i>8.9</i>		<i>9.1</i>	<i>0.62</i>
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.											
TL = Top Line income sources, BL = Bottom Line income sources											



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 21, 2012

Table ISC-2							
McDep Income and Small Cap Energy Portfolio							
Net Present Value and McDep Ratio							
		Price			Net		
		(\$/sh)			Present	Debt/	
	Symbol/	20-Dec	Shares	Market	Value	Present	McDep
	Rating	2012	(mm)	Cap	(\$/un)	Value	Ratio
				(\$mm)			
Small Cap Independent Producers							
PDC Energy	PDCE	33.89	30.2	1,020	30.00	0.46	1.07
Range Resources	RRC	B	63.38	160.0	10,140	70.00	0.23
Peyto Exploration and Development Cor	PEYUF		22.61	143.2	3,240	27.00	0.16
Continental Resources (32%)	CLR	B	75.39	58.6	4,410	100.00	0.14
Halcón Resources	HK		6.93	339.0	2,350	10.00	0.30
Birchcliff Energy Ltd.	BIREF	B	7.45	149.0	1,110	12.00	0.23
Denbury Resources Inc.	DNR		16.38	391.0	6,400	28.00	0.23
Berry Petroleum Company	BRY		34.50	55.3	1,910	70.00	0.31
Cimarex Energy Company	XEC	CB	59.28	86.9	5,150	110.00	0.13
Whiting Petroleum Corporation	WLL	CB	43.13	119.0	5,130	88.00	0.17
<i>Total or Median</i>					40,860		0.23
Leveraged Cash Payers							
Linn Energy, LLC	LINE		37.07	233.0	8,640	30.00	0.45
Vanguard Natural Resources, LLC	VNR		26.70	53.1	1,420	25.00	0.41
Legacy Reserves L.P.	LGCY		23.75	47.5	1,130	30.00	0.29
Enerplus Corporation	ERF	CB	12.99	196.0	2,550	21.00	0.30
<i>Total or Median</i>					13,740		0.36
RTF Cash Payers							
Freehold Royalties Ltd.	FRHLF		22.47	65.7	1,480	21.00	0.05
Enduro Royalty Trust (40%)	NDRO		16.42	13.2	220	21.00	-
Dorchester Minerals, L.P.	DMLP	CB	20.48	30.7	630	27.00	-
Sabine Royalty Trust	SBR		41.63	14.6	610	65.00	-
Cross Timbers Royalty Trust	CRT		27.22	6.0	160	44.00	-
Permian Basin RT	PBT		12.25	46.6	570	20.00	-
San Juan Basin Royalty Trust	SJT	CB	12.58	46.6	590	21.00	-
Hugoton RoyaltyTrust	HGT		7.29	40.0	290	14.00	-
Mesa RoyaltyTrust	MTR		20.13	1.9	38	40.00	-
<i>Total or Median</i>					4,590		0.62
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.							



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 21, 2012

Table ISC-3

McDep Income and Small Cap Energy Portfolio Value Multiples - Rank by EV/Ebitda

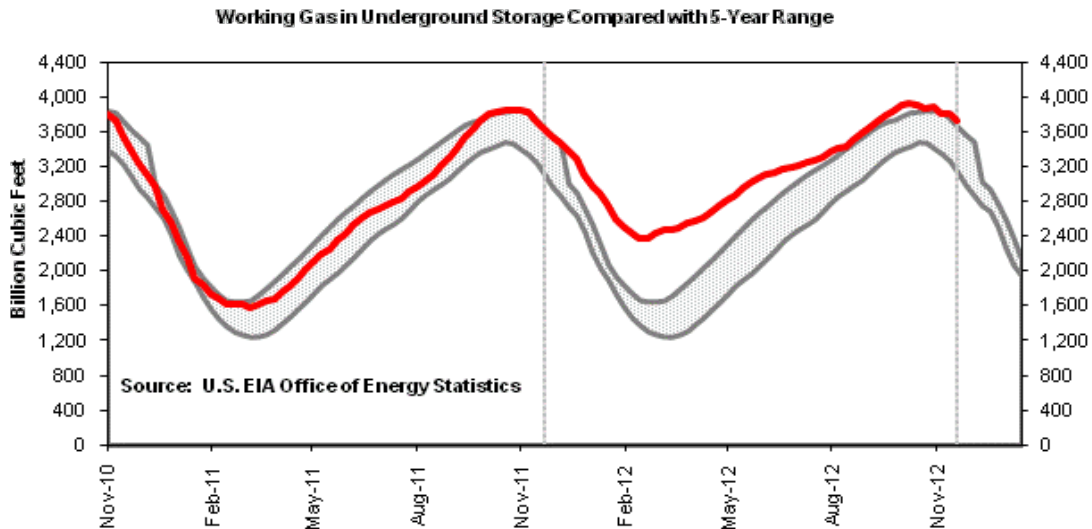
			Price (\$/sh)	Revenue	Dist/ Equity	Adjstd Resrvs/ Prod	PV/ Ebitda	EV/ Ebitda
	Symbol/ Rating	20-Dec 2012	Royalty (%)	Equity Ebitda	NTM	NTM	NTM	NTM
Small Cap Independent Producers								
Range Resources	RRC	B	63.38		-	13.5	18.3	16.9
PDC Energy	PDCE		33.89		-	9.9	13.1	14.0
Peyto Exploration and Development Corp	PEYUF		22.61		0.33	9.2	12.2	10.5
Birchcliff Energy Ltd.	BIREF	B	7.45		-	19.4	13.8	9.7
Continental Resources (32%)	CLR	B	75.39		-	9.0	9.3	7.4
Denbury Resources Inc.	DNR		16.38		-	13.0	9.2	6.3
Halcón Resources	HK		6.93		-	5.5	7.4	5.8
Berry Petroleum Company	BRY		34.50		-	11.3	8.2	5.3
Cimarex Energy Company	XEC	CB	59.28		-	7.3	8.8	5.2
Whiting Petroleum Corporation	WLL	CB	43.13		-	9.1	8.2	4.7
	<i>Median</i>					9.5	9.3	6.8
Leveraged Cash Payers								
Linn Energy, LLC	LINE		37.07		1.11	14.0	11.4	12.9
Vanguard Natural Resources, LLC	VNR		26.70		1.09	13.2	11.3	11.8
Legacy Reserves L.P.	LGCY		23.75		0.80	11.0	10.7	9.1
Enerplus Corporation	ERF	CB	12.99		0.45	6.3	8.6	6.3
	<i>Median</i>					12.1	11.0	10.4
RTF Cash Payers								
Freehold Royalties Ltd.	FRHLF		22.47	76	0.84	5.1	10.4	11.1
Sabine Royalty Trust	SBR		41.63	100	1.00	7.6	16.7	10.7
Dorchester Minerals, L.P.	DMLP	CB	20.48	77	0.90	6.8	13.7	10.4
Enduro Royalty Trust (40%)	NDRO		16.42		1.00	6.4	11.6	9.1
Cross Timbers Royalty Trust	CRT		27.22	78	0.97	14.2	14.5	8.9
San Juan Basin Royalty Trust	SJT	CB	12.58		0.76	9.1	14.0	8.4
Permian Basin RT	PBT		12.25	52	0.70	9.9	13.4	8.2
Mesa Royalty Trust	MTR		20.13		0.79	7.7	16.0	8.2
Hugoton Royalty Trust	HGT		7.29		0.48	12.9	12.2	6.4
	<i>Median</i>					7.7	13.7	8.9
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).								



Income and Small Cap Weekly

Analysis of Oil & Gas Stocks

December 21, 2012



Disclaimer: This analysis was prepared by Kurt Wulff, Manager of McDep LLC. The firm used sources and data believed to be reliable, but makes no representation as to their accuracy or completeness. This analysis is intended for informational purposes and is not a solicitation to buy or sell a security. Past performance is no guarantee of future results.

McDep or its employees may take positions in stocks the firm covers for research purposes. No trades in a subject stock shall be made within a week before or after a change in recommendation.

Certification: I, Kurt H. Wulff, certify that the views expressed in this research analysis accurately reflect my personal views about the subject securities and issuers. No part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research analysis.

Research Methodology/Ratings Description: McDep LLC is an independent research originator focused on oil and gas stocks exclusively. The firm applies the forty years of experience of its analyst to estimate a present value of the oil and gas resources and other businesses of covered companies. That value is compared with a company's stock market capitalization and debt. Stocks with low market cap and debt relative to present value tend to outperform stocks with high market cap and debt relative to present value. Buy recommendations are expected to deliver a total return better than 7% per year above inflation. Hold recommendations assume the attributes of the underlying business are reflected in the current price of the stock. Sell recommendations are expected to deliver a total return less than inflation.