

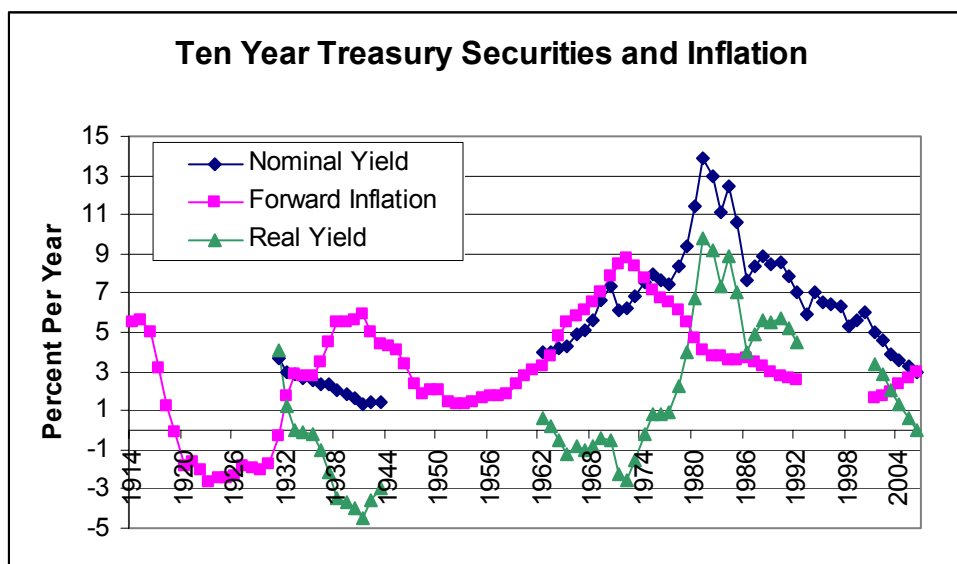
Good Inflation

Summary

Oil and gas price inflation that benefits investors is good for economic growth. In the current period of low real growth expectation, similar to the 1930s and 1970s, the global economy would benefit from energy investment. To stimulate that investment, rising inflation appears to be following a path between the low inflation of 70 years ago and the high inflation of 30 years ago. Natural gas price inflation is especially desirable to stimulate more supply of clean fuel to displace dirty fuel. While we wait for oil and gas trends to unfold, six trusts and a partnership are priced for median estimated distribution yield of 9.2% for the next twelve months and median unlevered cash flow multiple, EV/Ebitda, of 10.1 times.

The Challenge of Low Growth Expectation

The recent turn lower for yield on the U.S. Ten Year Note seems to fit an illustration we derived after reexamining the 20th century history of interest rates and inflation (see chart Ten Year Treasury Securities and Inflation). Because the chart was created more than two years ago, the points plotted for 2004 to 2006 are illustrations, not actual. The source is *Meter Reader*, Currency and TIPS Support Energy Investment, February 13, 2003. It is available online <http://www.mcdep.com/MR30213.PDF>. Current quotes near 3.9% for Nominal Yield and 1.5% for Real Yield imply 2.4% for Forward Inflation. The actual quotes seem to fit the illustration roughly.



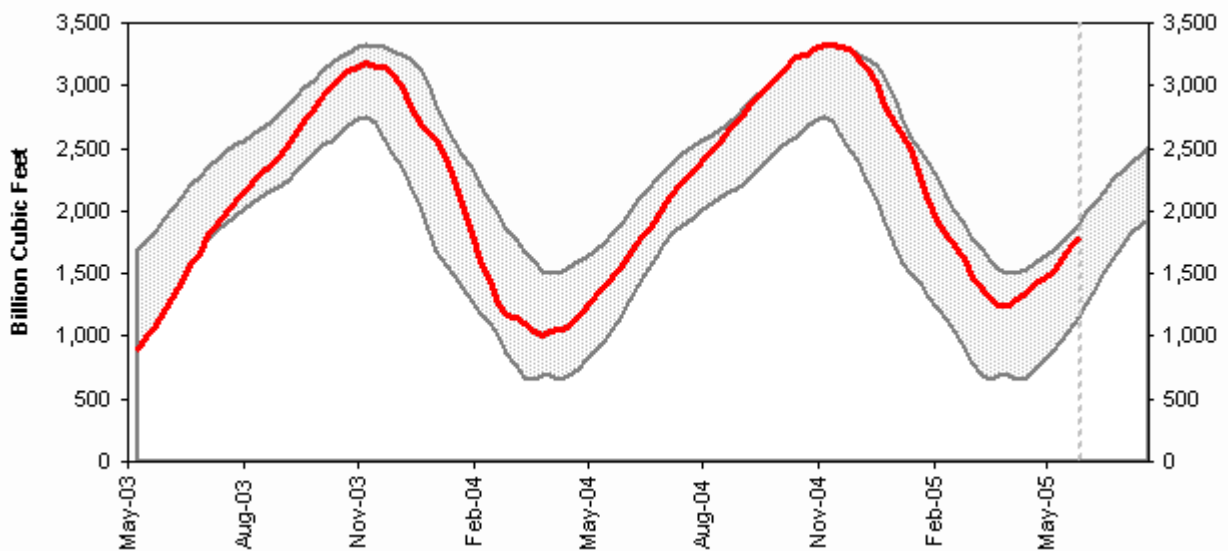
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Global Growth Requires More Natural Gas and Oil

Oil is worth more than the current six-year quote at \$52.58 a barrel for crude oil, just under the record \$53.42, but investors realize only a small share for profits worldwide. There seems to be a 1930s type tariff war raging. European governments tack on importing tariffs of perhaps 300% to drive up gasoline prices past \$5 a gallon (\$210 a barrel). It may be more than coincidence that with the highest oil taxes, Europe has among the slowest economic growth. In the tit for tat reminiscent of a trade war, governments of exporting countries impose export tariffs at an effective rate as high as 80%. Lower taxes or tariffs for government and more profits for investors would be better for trade and economic growth.

Natural Gas Price Too Low

Meanwhile oil has had a good run and has further to go as we are only half way through the decade. Natural gas has had a good run, too, but a wide gap in price has opened relative to oil. We attribute that partly to over reaction to short-term inventories. Natural gas in storage seems ample by the conditions of the past (see chart below from the EIA website). Two years ago, inventories at this time were at the bottom of the five-year range. Last year, inventories were in the middle of the range. Today, inventories are towards the top end of the range.



Paying too close attention to inventories misses the big picture. Shutting down just a few of the oldest and dirtiest coal-fired electric generating facilities would change the picture.

Prices could react quickly with a change in sentiment. We saw that in the past few months as natural gas futures in the U.K. almost doubled for some quotes. Futures for the first quarter of 2006 set a new high on June 1 of 70.4 pence per therm, as we see on

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Bloomberg. We translate that to \$12.80 a million btu. When natural gas is potentially in tight supply, it gets priced more realistically relative to oil. The heating equivalent of natural gas relative to crude oil is the crude oil price divided by 6. But hardly anyone burns crude oil. The equivalent fuel is heating oil or jet fuel for powering turbines in the most efficient electrical generation plants. The heating value equivalent of natural gas in those cases is about the price of crude oil divided by 5. Thus, oil at \$50 implies natural gas at \$10.

A Glut of LNG Would be Wonderful

We think it unlikely that the world could have too much Liquefied Natural Gas (LNG), the supplement to conventional production. Long-term investors might be concerned about too much supply eventually as the capital investment cycle moves past tight supply of the next several years. Actually low prices could strike at any time temporarily. Instead more supply of LNG could be an environmental blessing. A lot of electrical generating capacity has been built that could use natural gas, but is idle most of the time in favor of coal-fired plants.

We are not negative on the economic prospects for coal; we need a lot of it. We don't have enough natural gas to displace all coal, but when the natural gas price is less than the oil price divided by five we are using too much coal, in our opinion.

Kurt H. Wulff, CFA

U.S. Natural Gas and Oil Royalty Trusts

The Account

		<i>Price</i>			<i>Next</i>	<i>NTM</i>
	<i>Symbol</i>	<i>(\$/un)</i>		<i>Market</i>	<i>Twelve</i>	<i>Distrib.</i>
		<i>2-Jun</i>	<i>Units</i>	<i>Value</i>	<i>Months</i>	<i>Yield</i>
		<i>2005</i>		<i>(\$)</i>	<i>Distrib.</i>	<i>(%/yr)</i>
					<i>(\$/un)</i>	
Mesa RoyaltyTrust	MTR	65.98	200	13,196	5.66	8.6
Cross Timbers Royalty Trust	CRT	39.07	400	15,628	3.38	8.7
Sabine Royalty Trust	SBR	39.73	400	15,892	3.47	8.7
San Juan Basin Royalty Trust	SJT	36.76	500	18,380	3.31	9.0
Dorchester Minerals, L.P.	DMLP	21.22	700	14,854	2.04	9.6
Hugoton Royalty Trust	HGT	27.70	500	13,850	2.74	9.9
Permian Basin Royalty Trust	PBT	12.85	1,200	15,420	1.28	10.0
	<i>Total</i>			<i>107,220</i>		<i>9.2</i>
Futures Strip						
12 Month - Oil (\$/bbl)		55.09				
12 Month - Natural Gas (\$/mmbtu)		7.42				
72 Month - Oil (\$/bbl)		52.58				
72 Month - Natural Gas (\$/mmbtu)		6.79				

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

	<i>Symbol</i>	<i>Price (\$/sh) 2-Jun 2005</i>	<i>Shares (mm)</i>	<i>Market Cap (\$mm)</i>	<i>Net Present Value (\$/sh)</i>	<i>EV/ Ebitda NTM</i>	<i>McDep Ratio</i>
Sabine Royalty Trust	SBR	39.73	14.6	580	33.00	11.5	1.20
San Juan Basin Royalty Trust	SJT	36.76	46.6	1,710	32.00	10.1	1.15
Mesa RoyaltyTrust	MTR	65.98	1.9	120	60.00	10.3	1.10
Cross Timbers Royalty Trust	CRT	39.07	6.0	230	36.00	11.4	1.08
Permian Basin RT (41%)	PBT	12.85	19.1	250	12.00	9.2	1.07
Dorchester Minerals, L.P.	DMLP	21.22	28.2	600	21.00	9.5	1.01
Hugoton RoyaltyTrust (46%)	HGT	27.70	18.4	510	27.00	8.3	1.03
<i>Total or Median</i>				<i>4,000</i>		<i>10.1</i>	<i>1.08</i>

Rank by PV/Ebitda: Present Value to Earnings Before Interest, Tax, Deprec.

	<i>Symbol</i>	<i>Total Present Value (\$mm)</i>	<i>Unit Present Value (\$/mcf)</i>	<i>Reserves (bcf)</i>	<i>Natural Gas/ Ebitda (%)</i>	<i>Adjusted Reserves/ Production NTM</i>	<i>Revenue Royalty (%)</i>	<i>PV/ Ebitda</i>
Cross Timbers Royalty Trust	CRT	216	3.10	70	73	20.0	85	10.5
Sabine Royalty Trust	SBR	481	3.70	130	58	11.9	100	9.5
Dorchester Minerals, L.P.	DMLP	593	3.79	157	79	13.4	54	9.4
Mesa RoyaltyTrust	MTR	112	2.58	43	74	20.0	-	9.4
San Juan Basin Royalty Trust	SJT	1,491	2.85	523	99	12.0	-	8.8
Permian Basin RT (41%)	PBT	229	2.30	100	39	16.4	30	8.6
Hugoton RoyaltyTrust (46%)	HGT	497	2.90	171	92	13.7	-	8.1
<i>Total or Median</i>		<i>3,620</i>		<i>1,194</i>	<i>74</i>	<i>13.7</i>		<i>9.4</i>

Index of Recent U.S. Royalty Trust Research

Single Trust Analyses

<i>Date</i>	<i>Symbol</i>	<i>Stock</i>	<i>Theme</i>
13-May	DMLP	Dorchester Minerals, L.P.	Royalty Volume Increasing
28-Apr	* SJT	San Juan Basin Royalty Trust	Ten Bagger
24-Mar	* MTR	Mesa Royalty Trust	Long Reserve Life Reported
11-Feb	* HGT	Hugoton Royalty Trust	Improving Volume Trend

U.S. Natural Gas Royalty Trusts - A Weekly Analysis

3-Jun		Good Inflation
27-May		Understated Reserves
20-May		Institutional Longs
13-May	*	The Bottomless Well
6-May	*	Contango and Backwardation Mythology
29-Apr	*	No Debt, No Hedges

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