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**Raymond James` Energy "Stat of the Week"**  
**The Downward Trend Continues: Q1 Gas Production Survey Shows Massive 4.2% Decline**

For the past several years, we have been publishing U.S. natural gas production surveys of publicly traded companies. The bottom-line story has remained essentially the same throughout this entire time: U.S. natural gas production is heading firmly downwards, despite a massive increase in drilling activity. Remember, our Q4 2003 survey, published in February, found a 1.5% year-over-year production drop. For the full-year 2003, the average YOY decline was approximately 2.3%.

How does the U.S. gas supply situation look now? We ask this same question every quarter, but the answer somehow just doesn't change very much. As our Q1 survey shows, U.S. publicly traded E&P companies are now showing a 4.2% YOY gas production decline. The key point to make remains quite simple: As before, we see no significant near-term catalysts to alter the declining supply picture, and therefore price rationing remains the only viable option to bring the market into equilibrium. With both front-month gas contracts and the 12-month strip staying well above \$5/Mcf since December, we believe pricing in the commodity markets reflects the tight supply environment – even if the equity markets (and most energy analysts) have yet to awaken to this reality. Even though the 2004 First Call consensus forecast for gas prices has increased from ~4.50/Mcf to ~\$5.00/Mcf over the past five months, the current \$6.30+ price level is still nearly 30% higher than street consensus and 5% higher than our \$6.00/Mcf forecast.

**Survey says: U.S. natural gas production fell 4.2% YOY, 0.5% sequentially.**

As mentioned above, our survey results suggest that after adjusting the data for property acquisitions and divestitures, U.S. gas production declined 4.2% on a year-over-year basis and 0.5% sequentially. To put this figure in context, our four surveys from 2003 on average posted YOY declines of 2.25%. Even though this most recent data does seem to imply that the year over year gas decline

<b>U.S. Natural Gas Production (MMcf/d)</b>			
<b>Category</b>	<b>Q1:04</b>	<b>Q4:03</b>	<b>Q1:03</b>
<b>Majors &amp; Gas Utilities</b>	12,414	12,545	13,666
Estimated Sequential Change	-1.0%		
Estimated Y-Y Change	-9.2%		
<b>Independents</b>	13,646	13,658	13,540
Estimated Sequential Change	-0.1%		
Estimated Y-Y Change	0.8%		
<b>Total</b>	26,060	26,203	27,206
Estimated Sequential Change	-0.5%		
Estimated Y-Y Change	-4.2%		

Source: Company reports, JS Herold (all numbers pro forma for acquisitions and divestitures)

rate is accelerating, we would caution that there appears to be substantial volatility in these YOY numbers.

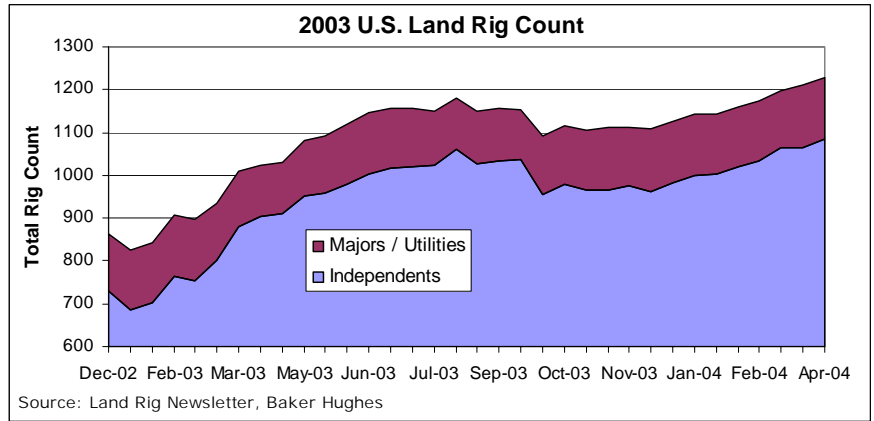
Our survey results also bring into question the data from the Energy Information Administration showing U.S. natural gas production on the rise. Though EIA data for 2003 (the latest available) has gone through several downward revisions, it still shows a YOY production **increase** of ~0.6% for the entire industry last year. This conclusion from the EIA seems to defy common sense when one considers that our surveys cover 48 of the largest natural gas producers in the United States, representing roughly 60% of total domestic gas production. Given that 60% of production was down 4.2% YOY in Q1, the other 40% would have to be up a whopping 6.3%, in order for total production just to break even! Expecting such a massive level of growth from the small, mostly privately held, producers outside our survey is wishful thinking, at best.

**Please read Investment Risks/Analyst Certification on page 4 and disclosure information on page 6.**

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**Production declines continue, despite continued growth in drilling activity.**

Despite the 20%+ increase in drilling activity over the course of the past 12 months, it seems clear to us that U.S. natural gas production continues to fall. This is contrary to what many of the natural gas bears have been suggesting over the past year. Perhaps more importantly, the majors (and gas utilities) continue to show the biggest decline in U.S. natural gas production, coming in this quarter at down 9.2% versus last



year and down 1.0% sequentially. This is important since: 1) the majors and utilities represent a large proportion of U.S. gas supply; and 2) drilling activity among the majors and utilities has been essentially flat since the start of 2003. This indicates that further production declines lie ahead for this group.

This also brings to light an even more astonishing reality: the independents are driving nearly all of the drilling activity increases, with little production response to show for it. Specifically, the independents have been responsible for putting an additional ~80 gas rigs to work (a 34% increase!) since April 2003, and yet their corresponding production grew only 0.8% year-over-year and was actually down 0.1% on a sequential basis (compared to the Q4 sequential decline of 0.2%). Even though these results seem mediocre compared to the independents' massive level of investment, it is important to note that at current gas prices, these companies are making excellent returns on almost every prospect they drill. As a group, however, they have not been able to "move the needle" on U.S. gas supply.

Furthermore, we emphasize that only four of the independents in our survey kept the overall group from posting substantial declines – as was the case in Q4, as well. Without the large organic increases in production from Chesapeake Energy (CHK/\$13.52/Strong Buy), EnCana (ECA/\$40.87), Pioneer Natural Resources (PXD/\$31.21/Strong Buy), and XTO Energy (XTO/\$26.61/Strong Buy), the E&P group's YOY growth rate would not have been 0.8%, but rather a negative 2.9%!

**What about the private E&P companies?**

As a caveat, we point out that while our survey covers about 60% of total U.S. gas production, its results are not necessarily reflective of the other 40% – which largely consist of smaller, mostly privately held, E&P companies. Given the vast number of these small players, it is impossible to get an accurate assessment of what their production is doing. However, as the table below shows, it is clear that the growth in gas rigs among companies outside our survey has lagged the independents included in the survey over the past 12 months. This realization, along with the fact that drilling prospect quality among smaller private companies is almost certainly worse than that of larger public companies, leads us to conclude that their Q1 production declined on a YOY basis, probably by as much as 3% to 4%.

	Gas Rigs		% Change in Rigs	Est. % of U.S. Gas Prod.	Est. Prod. Change
	3/26/03	3/26/04	(YOY)	(in Q1 2004)	(YOY Q1)
<b>Public Independents</b>	248	331	33.5%	31%	0.8% A
<b>Public Majors and Utilities</b>	112	106	-5.4%	29%	-9.2% A
<b>Subtotal - RJ Production Survey</b>	360	437	21.4%	60%	-4.2% A
<b>Non-Survey Cos (incl. Private Cos)</b>	377	472	25.2%	40%	-3.0% E
<b>Total - Entire Industry</b>	737	909	23.3%	100%	-3.7% E

Source: Smith International, RJ&A est.

**Conclusion**

Our bullish North American energy thesis has been, and continues to be, centered on the underlying problem of falling U.S. natural gas production. Much like in the 1970s, when oil production continued to fall, regardless of how many rigs were drilling, we think we are nearing (if not at) a similar crossroads in the U.S. gas supply picture. Given the inherent rate of decline in U.S. gas wells today, combined with what is still a muted response to drilling activity, we expect domestic gas production levels to continue trending south for the next several quarters. While this trend will almost certainly be led by the majors, the independents may not be able to reverse it as fast as many people might believe. As a result, expected year-over-year declines of 2.0% to 4.0% over the intermediate term should continue to hold average U.S. gas prices to a ratio versus corresponding oil product prices that is below the traditional 6:1 BTU parity. If oil prices remain near the \$40/Bbl level, that would imply fair value for gas above \$7/Mcf.

U.S. Natural Gas Production (MMcf/d)										
Majors & Gas Utilities	Ticker	Rating	Price	Q1:04	Q4:03	Q1:03	Percent		Absolute	
							Sequential	Y-O-Y	Sequential	Y-O-Y
Amerada Hess	AHC		\$73.41	183	213	260	-14.1%	-29.6%	(30)	(77)
BP plc	BP		\$52.93	2,869	2,919	3,187	-1.7%	-10.0%	(50)	(318)
ChevronTexaco	CVX		\$92.69	2,061	2,100	2,352	-1.9%	-12.4%	(39)	(291)
ConocoPhillips	COP		\$73.33	1,418	1,469	1,515	-3.5%	-6.4%	(51)	(97)
Dominion	D		\$62.46	935	942	961	-0.8%	-2.7%	(7)	(26)
Equitable Production	EQT		\$46.78	187	183	172	2.2%	8.6%	4	15
ExxonMobil	XOM		\$43.27	2,051	2,038	2,408	0.6%	-14.8%	13	(357)
Marathon Oil	MRO		\$33.59	679	712	748	-4.6%	-9.2%	(33)	(69)
Murphy Oil Corp.	MUR		\$66.04	99	82	78	19.5%	26.4%	16	21
Occidental	OXY		\$46.27	527	525	534	0.4%	-1.3%	2	(7)
Royal Dutch / Shell	RD		\$49.01	1,405	1,361	1,451	3.2%	-3.2%	44	(46)
Sub Total				12,414	12,545	13,666	-1.0%	-9.2%	(130)	(1,252)
Estimated Sequential Change				-1.04%						
Estimated Y-Y Change				-9.16%						
<b>E&amp;P Independents</b>										
Anadarko Petroleum	APC	OP2	\$55.19	1,328	1,365	1,373	-2.7%	-3.3%	(37)	(45)
Apache Corp.	APA	SB1	\$41.11	644	686	780	-6.0%	-17.4%	(41)	(136)
Burlington Resources	BR	OP2	\$67.30	880	880	877	0.0%	0.3%	(0)	3
Cabot Oil & Gas	COG		\$36.25	195	198	191	-1.7%	1.8%	(3)	3
Chesapeake Energy	CHK	SB1	\$13.52	770	766	732	0.6%	5.3%	5	39
Comstock Resources	CRK	SB1	\$19.13	91	91	93	0.1%	-1.4%	0	(1)
Denbury Resources	DNR	MP3	\$17.99	103	93	99	10.7%	4.3%	10	4
Devon Energy	DVN	MP3	\$60.83	1,669	1,730	1,720	-3.6%	-2.9%	(61)	(51)
EnCana Corp. *	ECA		\$40.87	684	654	534	4.6%	28.1%	30	150
Energren Resources	EGN		\$42.58	151	152	155	-0.5%	-2.6%	(1)	(4)
EOG Resources	EOG	OP2	\$54.17	618	632	642	-2.2%	-3.7%	(14)	(24)
Evergreen Resources	EVG	MP3	\$38.10	144	144	130	0.0%	10.8%	0	14
Forest Oil	FST	SB1	\$25.01	234	281	279	-16.8%	-16.2%	(47)	(45)
Houston Exploration	THX		\$44.96	309	291	297	6.1%	4.0%	18	12
Kerr-McGee	KMG		\$49.34	650	632	655	2.8%	-0.8%	18	(5)
Magnum Hunter	MHR	SB1	\$10.28	130	140	124	-6.9%	5.5%	(10)	7
Newfield Exploration	NFX		\$49.88	528	501	499	5.4%	5.8%	27	29
Noble Energy	NBL		\$46.05	250	252	262	-0.6%	-4.5%	(2)	(12)
Patina Oil & Gas	POG		\$26.79	205	209	189	-2.2%	8.5%	(5)	16
Pioneer Natural Res.	PXD	SB1	\$31.21	550	476	386	15.6%	42.6%	74	165
Pogo Producing	PPP		\$47.80	231	213	216	8.3%	6.8%	18	15
Questar Corp.	STR		\$36.03	241	231	223	4.3%	7.7%	10	17
Range Resources	RRC		\$11.32	126	130	121	-3.3%	4.1%	(4)	5
Remington Oil & Gas	REM	OP2	\$21.27	61	75	50	-17.7%	22.8%	(13)	11
Southwestern Energy	SWN	UP4	\$25.70	116	113	90	2.6%	28.4%	3	26
Spinnaker Exploration	SKE	OP2	\$32.80	91	101	129	-9.9%	-29.5%	(10)	(38)
St. Mary Land & Expl.	SM	OP2	\$33.12	128	130	133	-1.9%	-3.9%	(2)	(5)
Stone Energy	SGY		\$44.31	161	166	184	-3.1%	-12.3%	(5)	(23)
Swift Energy	SFY	OP2	\$20.36	34	37	40	-8.2%	-15.9%	(3)	(6)
Tom Brown, Inc.	TBI	MP3	\$47.91	263	265	222	-0.7%	18.5%	(2)	41
Ultra Petroleum	UPL	SB1	\$31.85	102	102	67	0.2%	53.1%	0	35
Unit Corp.	UNT	OP2	\$27.51	69	69	62	0.4%	11.1%	0	7
Unocal	UCL		\$35.27	515	500	703	3.0%	-26.8%	15	(188)
Vintage Petroleum	VPI	OP2	\$14.57	69	62	64	11.4%	7.9%	7	5
Western Gas Resources	WGR	SB1	\$54.40	145	151	149	-3.9%	-2.7%	(6)	(4)
Westport Resources	WRC		\$34.60	389	382	379	1.8%	2.5%	7	10
XTO Energy	XTO	SB1	\$26.61	771	758	692	1.7%	11.5%	13	80
Sub Total				13,646	13,658	13,540	-0.1%	0.8%	(12)	106
Estimated Sequential Change				-0.09%						
Estimated Y-Y Change				0.78%						
<b>Total</b>				<b>26,060</b>	<b>26,203</b>	<b>27,206</b>	<b>-0.5%</b>	<b>-4.2%</b>	<b>(143)</b>	<b>(1,146)</b>
<b>Estimated Sequential Change</b>				<b>-0.54%</b>						
<b>Estimated Y-Y Change</b>				<b>-4.21%</b>						
Source: Company reports, JS										
Note: Pro forma for acquisitions and divestitures										
* Covered by Raymond James										

## **Specific Investment Risks Related to the Industry or Issuer**

### **Gas and Oil Price Volatility**

Prices for natural gas and oil fluctuate widely and Chesapeake's revenues, profitability and future growth depend substantially on prevailing prices for gas and oil. Also, lower oil and gas prices can influence the company's cash flow and capital available to reinvest in drilling projects, which could impact Chesapeake's ability to grow its operations. To manage commodity price volatility, in the normal course of its business, CHK will periodically enter into hedging transactions to secure pricing on its oil and gas production. Occasionally, as part of its proactive hedging philosophy, CHK will settle hedging transactions prior to maturity if the company believes that prices have moved to unsustainable levels. Since 2001, CHK has recorded sizable gains and losses from this strategy and future losses may be incurred.

### **Significant Financial Leverage**

Despite substantial improvement in recent years, Chesapeake still currently maintains a significant degree of financial leverage. Declines in future profitability and cash flow generation could impact its ability to service debt obligations as well as its ability to reinvest cash flow in operations.

### **Future Acquisition Risks**

Acquisitions are integral to Chesapeake's business model and future transactions are likely. Even though the company has previously been successful in executing and integrating several acquisitions, the success of future transactions or the availability of favorable future opportunities is difficult to predict. Ultimate transaction prices, economics and form of consideration, future production, etc. can all affect future profitability and CHK's stock price performance.

### **Potential Increases in Service Costs**

Future increases in drilling and other service costs could affect Chesapeake's profitability. As industry participants accelerate drilling activity in response to the high commodity prices, costs will likely rise. However, attractive rates of return may continue to be achievable, depending on the level of future commodity prices and CHK's hedging program.

PXD's international operations expose shareholders to a multitude of risks associated with doing business in foreign markets. As the company expands its operations internationally, it will become increasingly more exposed to risks that include, among other things, loss of revenue, property and equipment as a result of hazards such as expropriation, war, insurrection and other political risks, increases in taxes and governmental royalties, renegotiation of contracts with governmental entities, changes in laws and policies governing operations of foreign-based companies, currency restrictions and exchange rate fluctuations and other uncertainties arising out of foreign government sovereignty over the company's international operations. The company's international operations may also be adversely affected by laws and policies of the United States affecting foreign trade and taxation. In particular, the company's Tunisian operations could be harmed by political instability and the threat of terrorism in northern Africa and the Middle East.

### **Future acquisition risks**

Acquisitions are integral to XTO's business model. Even though the company has successfully executed and integrated several acquisitions, future transactions are likely. Transaction prices, economics and form of consideration can all affect future profitability and stock price performance.

### **Future growth depends largely on extensions of current fields and infill drilling**

XTO's future success is largely dependent on its ability to replicate its previous results across its acreage positions. As the company extends its activity, results could diminish. The company has historically experienced development drilling success rates of about 96%, however future success rates could decline and impact overall project economics.

### **Significant financial leverage**

XTO maintains a significant degree of financial leverage. Declines in future profitability and cash flow generation could impact its ability to service debt obligations as well as its ability to reinvest cash flow in operations.

**For Company Specific Risks please see [www.rjcapitalmarkets.com/SearchForDisclosures\\_main.asp](http://www.rjcapitalmarkets.com/SearchForDisclosures_main.asp)**

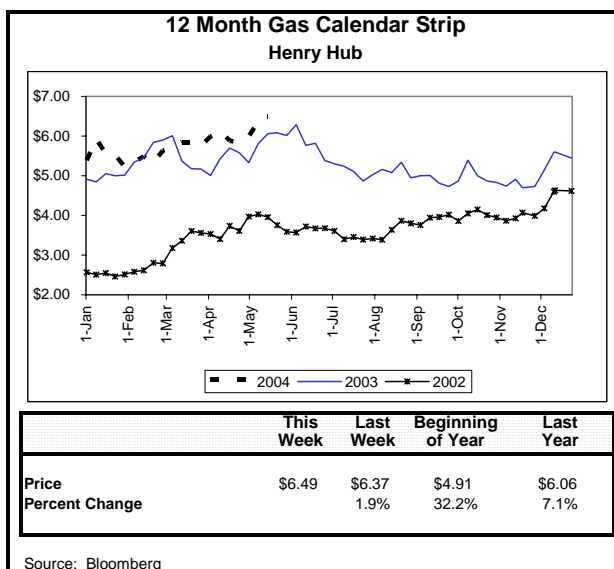
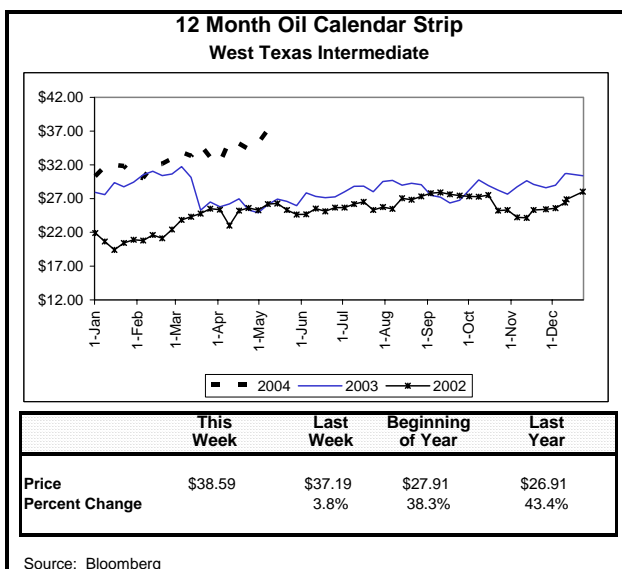
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**Investors should consider this report as only a single factor in making their investment decision.**



# Raymond James Weekly Oilfield Review

For Week Ending: **14-May-04**



	14-May-04	7-May-04	16-May-03	Change From:	
	This Week	Last Week	Last Year	Last Week	Last Year
<b>1. U.S. Rig Activity</b>					
U.S. Oil	157	158	168	-0.6%	-6.5%
U.S. Gas	1,004	994	868	1.0%	15.7%
U.S. Miscellaneous	1	1	4		
<b>U.S. Total</b>	<b>1,162</b>	<b>1,153</b>	<b>1,040</b>	<b>0.8%</b>	<b>11.7%</b>
U.S. Horizontal	115	111	75	3.6%	53.3%
U.S. Directional	282	284	269	-0.7%	4.8%
U.S. Offshore	95	98	113	-3.1%	-15.9%
U.S. Offshore Gulf of Mexico					
Fleet Size	164	164	182	0.0%	-9.9%
# Contracted	117	117	129	0.0%	-9.3%
Utilization	71.3%	71.3%	70.9%	0.0%	0.7%
U.S. Weekly Rig Permits *	1136	978	1003	16.2%	13.3%
<b>2. Canadian Activity</b>					
Rig Count	167	185	99	-9.7%	68.7%
Oil Well Completions (cum.)	973	938	1,186	3.7%	-18.0%
Gas Well Completions (cum.)	4,327	4,047	3,695	6.9%	17.1%
Dry Wells	396	392	519	1.0%	-23.7%
Total Well Completions (Incl. Dry)	5,696	5,377	5,400	5.9%	5.5%
<b>3. Stock Prices</b> (5/14/04)					
OSX	98.5	98.9	95.6	-0.4%	3.1%
TSE Oil/Gas Service Index	NA	NA	3,109.8	NA	NA
S&P 500	1,095.7	1,098.7	944.3	-0.3%	16.0%
DJIA	10,012.9	10,117.3	8,679.0	-1.0%	15.4%
S&P 1500 E&P Index	201.3	202.4	155.3	-0.5%	29.7%
<b>4. Inventories</b>					
U.S. Gas Storage (Bcf)	1,303	1,227	900	6.2%	44.8%
Canadian Gas Storage (Bcf)	188	174	117	8.1%	61.2%
Total Petroleum Inventories ('000 bbls)	610,000	610,100	594,287	0.0%	2.6%
<b>5. Spot Prices (US\$)</b>					
Oil (W.T.I. Cushing)	\$41.38	\$39.93	\$29.14	3.6%	42.0%
Oil (Hardisty Med.)	\$28.72	\$27.28	\$23.21	5.3%	23.8%
Gas (Henry Hub)	\$6.40	\$6.29	\$6.12	1.7%	4.6%
Residual Fuel Oil (New York)	\$4.87	\$4.71	\$4.07	3.4%	19.5%
Gas (AECO)	\$5.48	\$5.37	\$5.01	2.0%	9.4%

Sources: (Baker Hughes, ODS-Petrodata, API, EIA, Oil Week, Bloomberg)

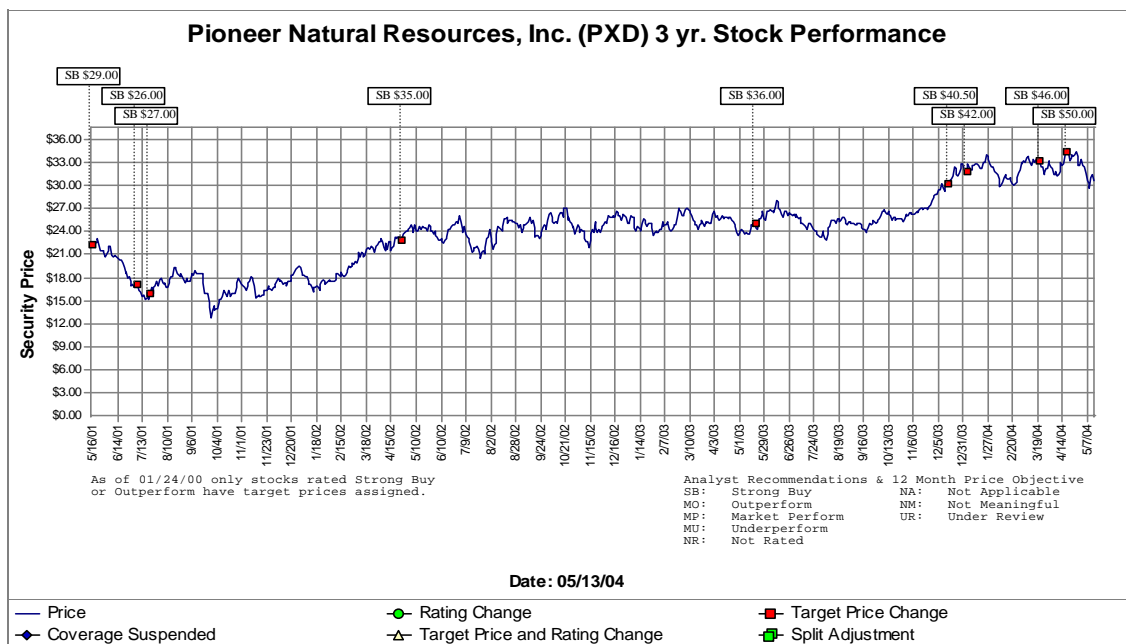
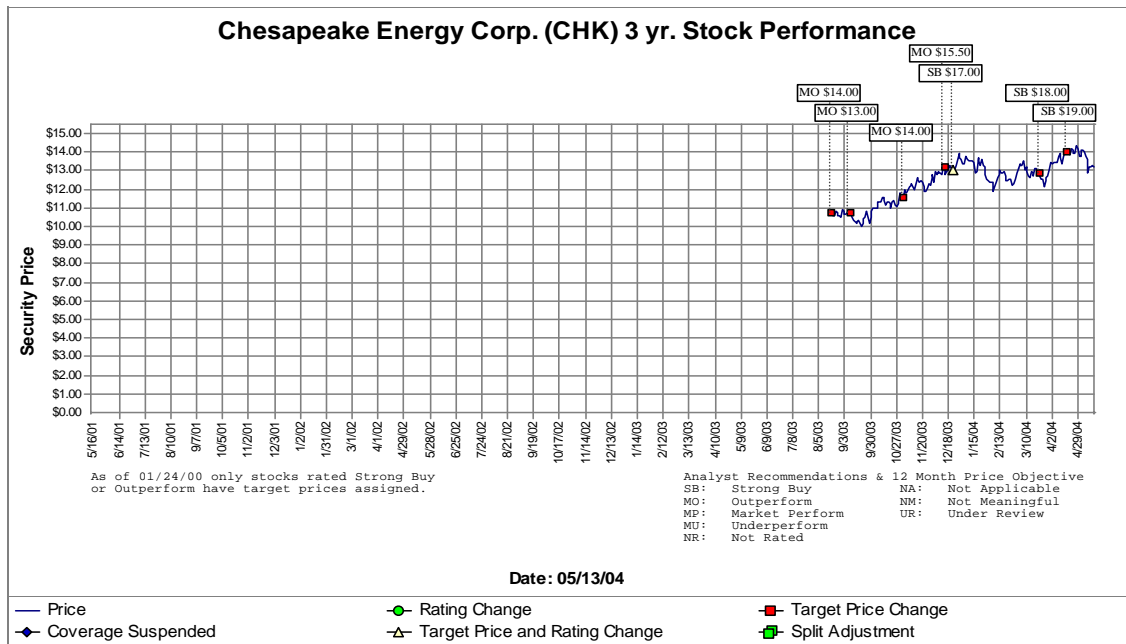
\* Note: Weekly rig permits reflect a 1 week lag

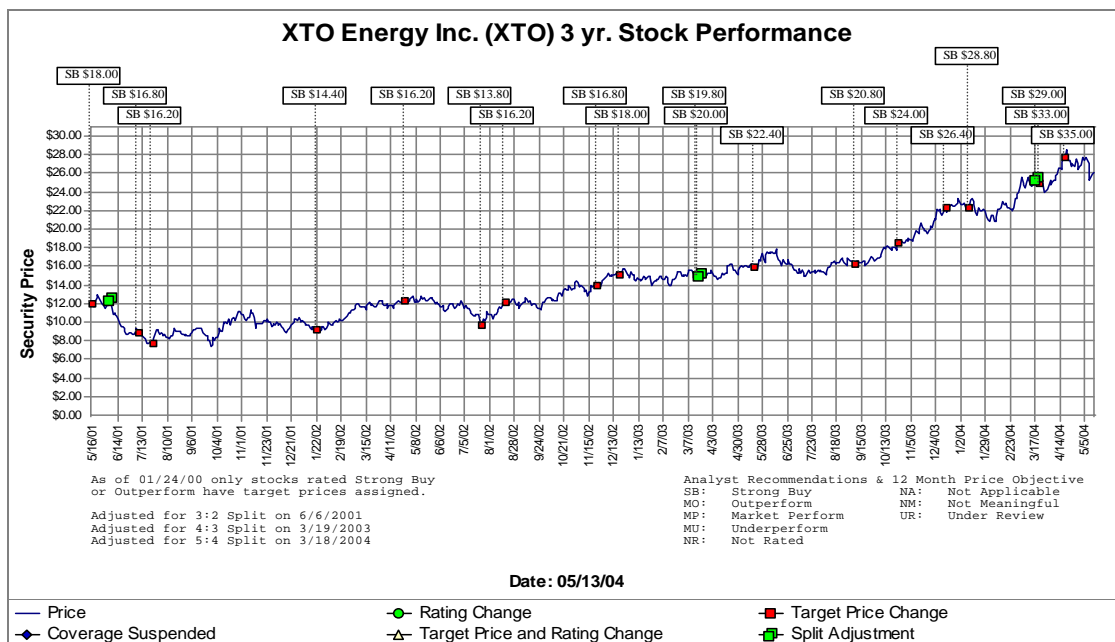
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**Stock Ratings:** Within our four-tiered rating system, Strong Buy means that the stock is expected to appreciate and produce a total return of at least 15% and outperform the S&P 500 over the next six months; for higher-yielding and more conservative equities, such as REITs and certain MLPs, a total return of at least 15% is expected to be realized over the next 12 months. Outperform means the stock is expected to appreciate and outperform the S&P 500 over the next 12 months; for higher-yielding and more conservative equities, such as REITs and certain MLPs, an Outperform rating is used for securities where we are comfortable with the relative safety of the dividend and expect a total return modestly exceeding the dividend yield over the next 12 months. Market Perform means the stock is expected to perform generally in line with the S&P 500 over the next 12 months and is potentially a source of funds for more highly rated securities; and Underperform means the stock is expected to underperform the S&P 500 or its sector over the next six to 12 months and should be sold.

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The information below indicates target price and rating changes for the subject companies included in this research.





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**Raymond James Relationships:** RJA expects to receive or intends to seek compensation for investment banking services from the subject companies in the next three months.

**Raymond James & Associates co-managed a follow-on offering of PXD shares and a public debt offering for the company in April 2002. Raymond James & Associates co-managed a follow-on offering of XTO shares in April 2003. Raymond James & Associates co-managed an offering of 1.5 million convertible preferred shares at \$100.00 per share for CHK in November 2003, a follow-on offering of 23.0 million CHK shares at \$13.51 per share in January 2004, and a private offering of 255,000 convertible preferred shares at \$1,000.00 per share for CHK in March 2004.**

Complete Risk and Disclosure information, as well as more information on the Raymond James rating system and suitability categories, is available at [www.rjcapitalmarkets.com/SearchForDisclosures\\_main.asp](http://www.rjcapitalmarkets.com/SearchForDisclosures_main.asp). Copies of research can be obtained by contacting any Raymond James & Associates or Raymond James Financial Services office (please see [www.rjf.com](http://www.rjf.com) for office locations) or by calling (727) 567-1000 or sending a written request to the Equity Research Library, Raymond James & Associates, Inc., Tower 3, 6th Floor, 880 Carillon Parkway, St. Petersburg, FL 33716.

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