

Initiation Report  
April 25, 2008

## Clayton Williams Energy, Inc.

### NASDAQ: CWEI

**Recent Price: \$64.59**  
**52 Week Range:**  
**\$21.63 – \$64.59**  
**Price Target: NA**  
**Rating: NA**

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### KEY STATISTICS

Shares outstanding, basic	11.3 million	Proved reserves(1P)	290.8 Bcfe
Market capitalization	\$ 733.4 million	Proved developed reserves	222.2 Bcfe
Enterprise value	\$ 1,232.6 million	PV-10	\$ 1.33 billion
Price /Earning	121 X	Production	35.9 Bcfe
Price/Book value	4.6 X	Market capitalization/1P	\$2.52 per Mcfe
Price/EBITDAX	3.0 X	Reserve replacement ratio	154%

### 52-week price and volume chart (source: msn.com)



**FINANCIAL HIGHLIGHTS**

Amounts in \$million, except per share amounts	2007	2006	2005	2004
Revenue	393.9	266.0	283.6	206.3
Operating income	74.0	5.2	80.3	10.4
Operating margin (%)	18.8%	2.0%	28.3%	5.0%
Net income	5.9	17.8	0.3	(14.0)
Net margin (%)	1.5%	6.7%	0.1%	-6.8%
Earning per share, basic	\$ 0.53	\$ 1.64	\$ 0.02	\$ (1.37)
EBITDAX	244.3	169.7	196.9	129.6
EBITDAX/Revenue	62.0%	63.8%	69.4%	62.8%
EBITDAX per basic share	\$ 21.55	\$ 15.59	\$ 18.22	\$ 12.69
Cash	12.3	13.8	5.9	16.4
Property and equipment, net	731.1	644.8	474.1	398.4
Long-term debt	430.2	431.3	235.7	177.5
Stockholders' equity	160.8	145.0	120.3	117.6
Total assets	861.1	795.4	587.3	462.2
Long-term debt/Total assets (%)	50.0%	54.2%	40.1%	38.4%
EBITDAX/Interest expense	7.6	8.1	13.6	16.4
Net working capital	(76.4)	(23.1)	(35.8)	(27.6)
Cash flow from operating activities	234.9	146.0	163.5	127.0

**SUMMARY**

Clayton Williams Energy, Inc. (hereinafter called "CWEI", or the "Company") is a growing independent exploration and development (E&P) oil and gas company. Its major oil and gas properties are located in the Permian Basin, Austin Chalk (trend), East Texas Bossier, North Louisiana, South Louisiana, and Utah.

As of December 31, 2007, CWEI had working interests in 6,694 gross (918.00 net) producing oil and gas wells and held working interest is about 1.3 million gross (784,00 net) undeveloped acres.

CWEI has a balanced portfolio of oil and natural gas reserves and balanced production of oil and gas. As of December 31, 2007, the Company had an estimated 290.8 Bcfe of proved oil and gas reserves, about 42% being natural gas reserves and about 58% being oil and natural gas liquids. As of December 31, 2007 about 67.8% of the Company's proved reserves were proved developed producing reserves.

During 2007 the Company produced 20.7 Bcf of gas, 2,318 MBbls of oil (13.9 Bcfe), and 222 MBbls of natural gas liquid (1.3 Bcfe). Total production on the gas equivalent

basis for the year 2007 was 35.9 Bcfe which was 22% more than total production of 2006.

The Company's oil and gas proved reserves as of December 31, 2007 was 19.3 Bcfe more than its oil and gas proved reserves of 171.8 Bcfe as of December 31, 2007. Thus, during 2007 the Company replaced 154% of its 2007 production of 35.9 Bcfe.

For the year ended December 31, 2007, CWEI reported \$0.53 earning per basic share (EPS) which was lower than its 2006 EPS of \$1.64. However, the EBITDAX<sup>(a)</sup> per basic share, which is a more appropriate measure of performance for oil and gas E&P companies, was \$21.55 as compared to EBITDAX per share of \$15.59 in 2006 and \$18.22 in 2005.

Over the past 12 month common shares of CWEI have outperformed the Jefferies North American Small/Midcap E & P Index by almost two times, on both an annual and on a daily basis. CWEI's common stock has been thinly traded, with an average volume of approximately 58,000 shares (0.51% of outstanding common shares) over the past three months and approximately 43,900 shares (0.39% of outstanding common shares) over the past twelve months.

CWEI's recent price earning (P/E) multiple is 121 based on 2007 EPS. But again looking at the stock valuation from the EBITDAX perspective, Price/EBITDAX multiple is just 3.0.

Currently the Company's major focus is on exploration and development activities in some of the larger producing regions of Louisiana and Texas. CWEI's exploration and development efforts are intended to find areas that might contain significant undiscovered oil and gas reserves, develop those reserves, and sell the production from the reserves at a profit. In addition to pursuing its exploration and development programs, Clayton Williams Energy, Inc. also engages in acquisition of proved oil and gas properties when there is the opportunity.

Prior to the year 2008 most of the Company's annual capital expenditures were related to exploratory prospects. However, for 2008 Clayton Williams Energy, Inc. plans to allocate a majority of its capital resources to developmental drilling activities. The Company's planned expenditure for exploration and development activities for 2008 is \$256.5 million, about 81% of which is planned to be spent on developmental prospects

CWEI's capital expenditures on exploration and development in 2007 was \$230.7 million, most of which was financed through cash flows from operating activities. The Company's planned 2008 capital expenditure is \$256.5 million. The Company has established revolving credit facility with a group of banks and uses the funds available under the credit facility for partial financing of its capital expenditures and short-term working capital needs.

The Company's common stock trades on the NASDAQ under the ticker symbol "CWEI".

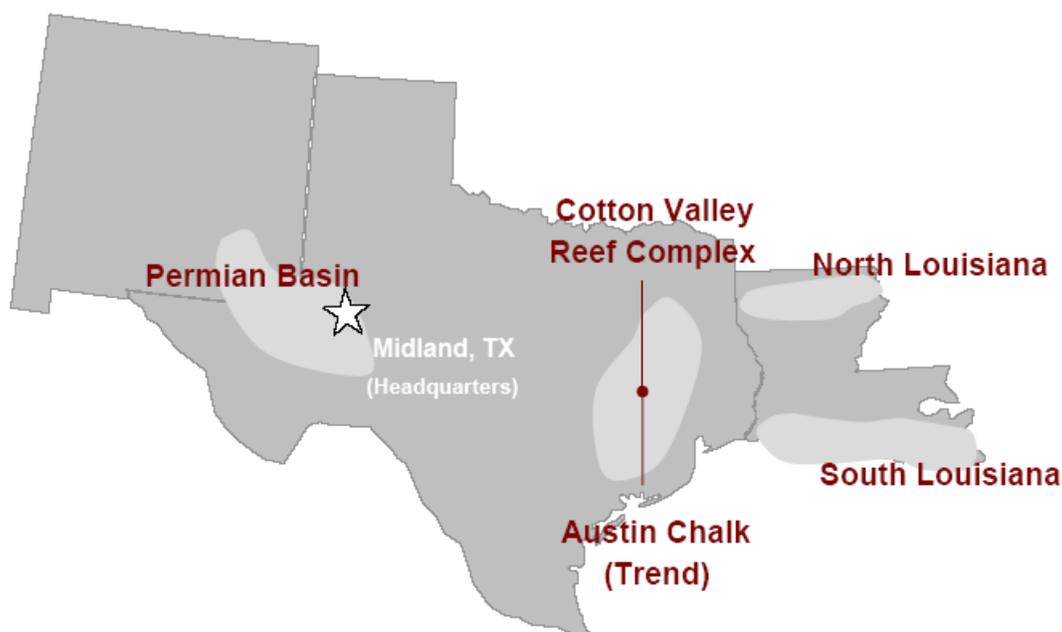
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(a) For our definition of EBDITAX see page 22.

## CWEI'S OIL AND GAS PROPERTIES

CWEI's has working interests in oil and gas properties in the Permian Basin, Austin Chalk (trend), East Texas Bossier, North Louisiana, South Louisiana, and Utah.

The following figure shows the key producing areas of CWEI operation:



Source: CWEI April 2008 Presentation

In the oil and gas business the term "working interest" means an interest in an oil and gas lease that gives the owner of interest the right to drill for and produce oil and gas on the leased acreage (or wells). Gross acres (or wells) is acres (or well) in which the Company has a working interest. Net acres (or wells) is the Company's aggregate working interests in the gross acres (or wells).

We are providing below a brief description of CWEI's properties:

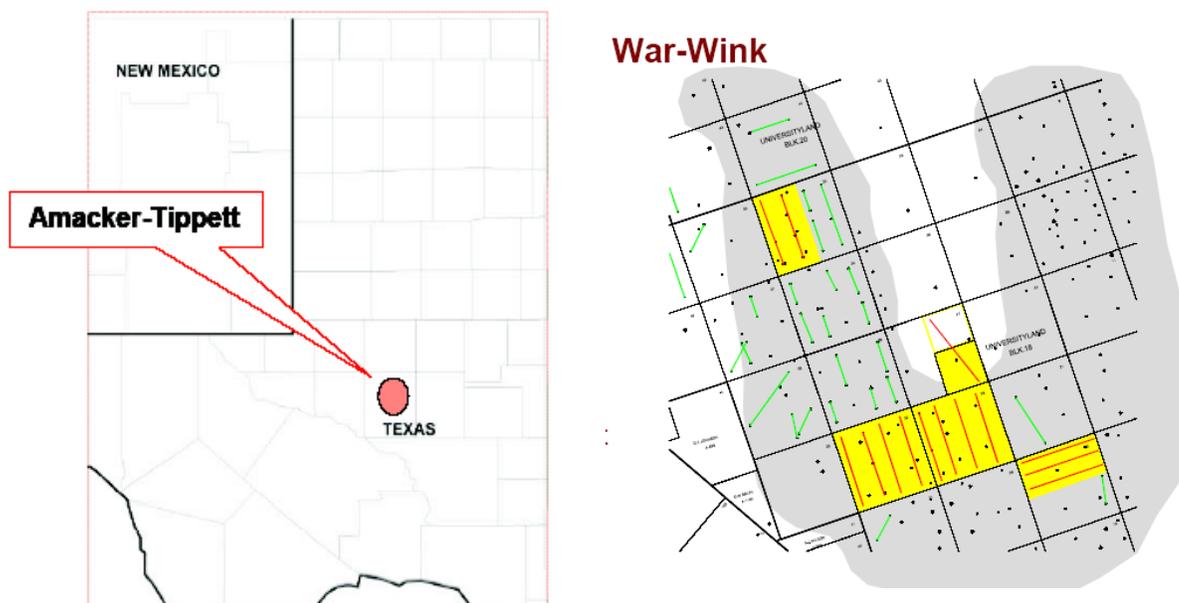
### The Permian Basin Properties

The Permian Basin is one of the largest structural basins in North America. It encompasses a surface area which consists of majority of counties in Railroad Commission of Texas Districts 7c, 8, and 8a in West Texas and Southeast New Mexico.

The Permian Basin is a mature area in which much of its future production will result

from improved recovery out of existing fields. The region is characterized by numerous known producing horizons, providing significant opportunities to increase reserves, production and ultimate recoveries through additional development, horizontal drilling, recompletions, enhanced recovery methods, and the use of 3-D seismic, reprocessed 2-D seismic data, and other advanced technologies.

The Permian Basin has been a significant source of production and cash flow for CWEI. As of December 31, 2007, CWEI had ownership interests in 5,509 gross (516.2 net) productive oil wells and in 733 gross (96.5 net) productive gas wells in the Permian Basin.



CWEI Key Development Fields in the Permian Basin. (Source: CWEI April 2008 Presentation)

**Most of CWEI's proved oil and gas reserves are in the Permian Basin.** As of December 31, 2007 out of 290.8 Bcfe proved oil and gas reserves of CWEI, 169.2 Bcfe or 58.2% of it were in the Permian Basin

During the year 2007, CWEI's average daily production from the Permian Basin was 14,649 Mcf of natural gas, 3,212 Bbls of oil, and 198 Bbls of natural gas liquids.

The Permian Basin is the Company's top priority for 2008 capital expenditures. Out of \$256.5 million capital expenditure budget for 2008, CWEI plans to spend 43% or \$110.3 million of it on development activities in the Permian Basin. Most of the planned drilling activities are related to the Company's prospects in the Amacker-Tippett Field and the War-Wink Field in the West Texas section of the Permian Basin.

In the Amacker-Tippett area CWEI plans 21 new drills, vertical and horizontal, and 11 re-completion in 2008 targeting oil-prone sands in the Devonian and Wolfcamp formations.

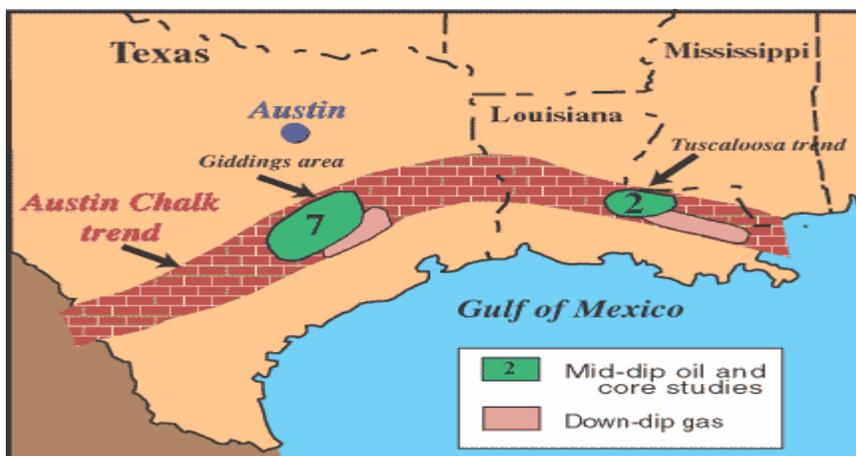
In the War-Wink area CWEI plans 11 new drills, horizontal, and 2 re-entries in 2008.

The following table summarizes key statistics about the Company's Permian Basin Properties, as of December 31, 2007.

<b>Permian Basin</b>	
<b>Number of productive wells (net)</b>	
Oil	516.2
Gas	96.5
Total	612.7
<b>Proved reserves</b>	
Oil (MMBbls)	17.3
Gas (Bcf)	65.2
Total (Bcfe)	169.2
PV 10 (\$million)	684.7
<b>Average daily production</b>	
Oil (Bbls)	3,212
Gas (Mcf)	14,649
Natural gas liquids (Bbls)	198

### Austin Chalk Trend Properties

The Austin Chalk Trend is comprised of a limestone formation which extends from South Texas into Louisiana and then into Mississippi. Three major fields along this trend are the Giddings (Austin Chalk) Field, the Luling/Salt Flat Field, and the Pearsall Field. There are also many small fields between these major fields in the trend which have produced substantial amounts of oil.

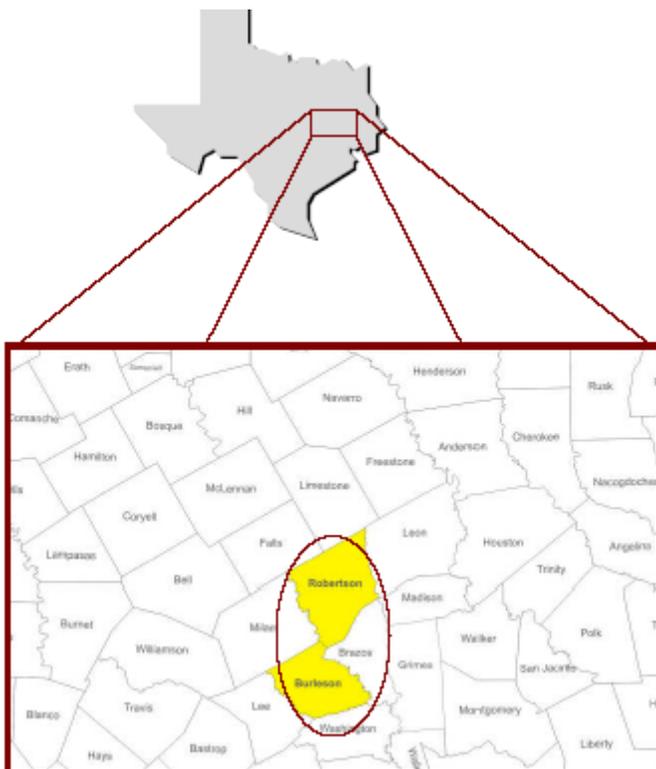


The Austin Chalk trend in Texas, Louisiana, and Mississippi. (Source: USGS)

In the Austin Chalk Trend horizontal drilling has been used extensively by E&P companies over the past several years. Horizontal drilling, also known as directional drilling, is an enhanced oil or gas recovery method that allows one well bore to

“communicate” many fractures which leads to reducing the cost of production, because one well would then yield the production of several (abandoned ) vertical wells.

As of December 31, 2007, CWEI had ownership interests in 293 gross (224.8 net) productive oil wells and in 17 gross (9.3 net) productive gas wells in the Austin Chalk Trend.



CWEI Properties in the Austin Chalk Trend, Texas. (Source: CWEI April 2008 Presentation)

As for the Company’s proved reserves of oil and gas, the Austin Chalk is second to the Permian Basin. As of December 31, 2006 out of 290.8 Bcfe proved oil and gas reserves of CWEI, 50.6 Bcfe or 17.4% of it were in the Austin Chalk Trend

The Company’s average daily production from the Austin Chalk Trend during 2007 was 1,737 Bbls of oil and 2, 220 Mcf of natural gas

The Austin Chalk Trend is also the Company’s second priority, after the Permian Basin, for 2008 capital expenditures. Out of \$256.5 million capital expenditure budget for 2008, CWEI plans to spend 23% or \$59.3 million of it in the Austin Chalk Trend projects.

The Company has identified 24 candidates for horizontal drilling to be conducted in 2008.

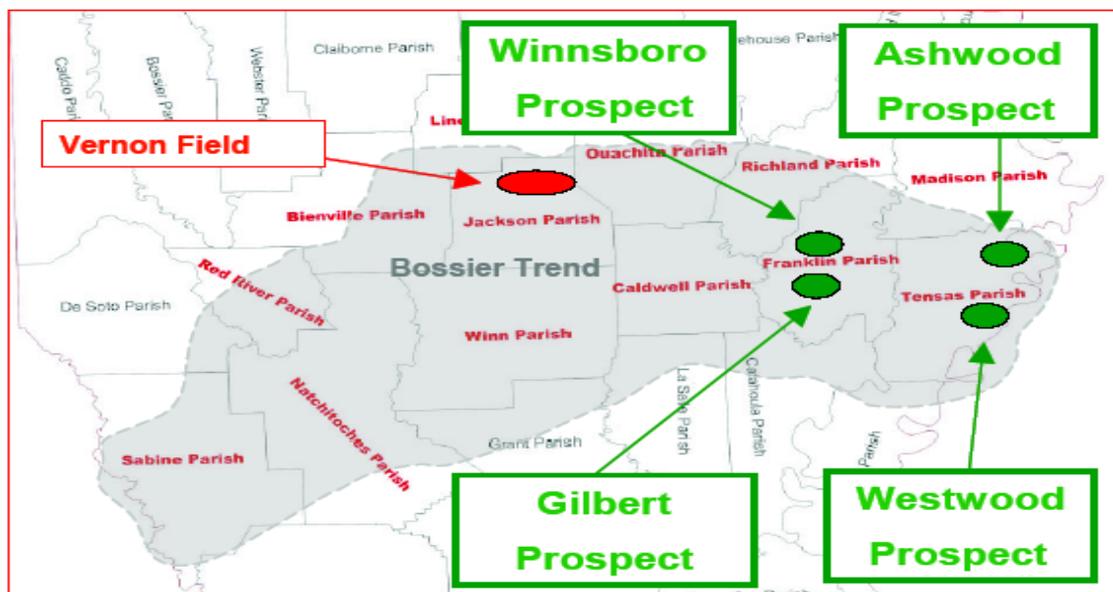
The following table summarizes key statistics about the Company’s Austin Chalk Trend Properties, as of December 31, 2007.

<b>Austin Chalk Trend</b>	
<b>Number of productive wells (net)</b>	
Oil	224.8
Gas	9.3
Total	234.1
<b>Proved reserves</b>	
Oil (MMBbls)	7.5
Gas (Bcf)	5.4
Total (Bcfe)	50.6
PV 10 (\$million)	305.2
<b>Average daily production</b>	
Oil (Bbls)	1,737
Gas (Mcf)	2,220
Natural gas liquids (Bbls)	259

### North Louisiana Properties

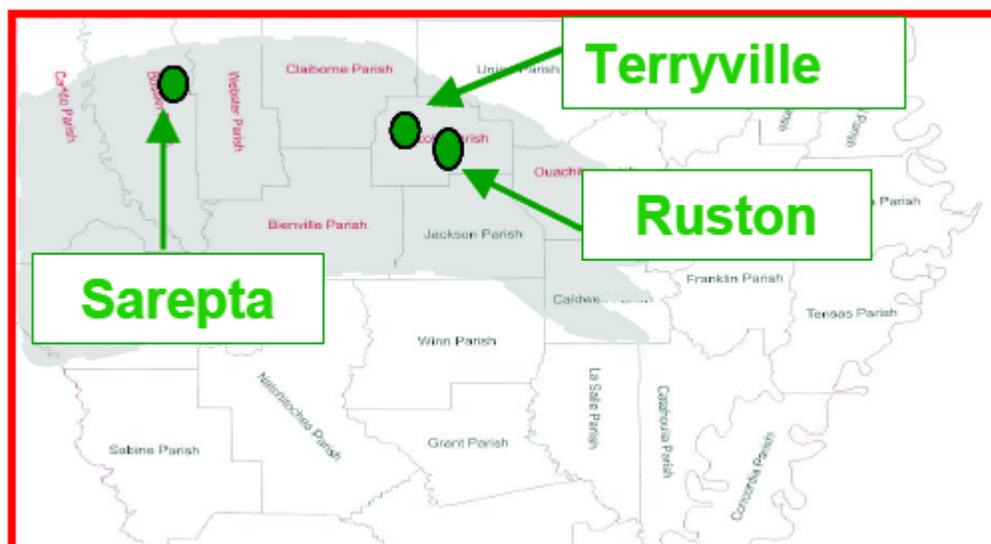
In north Louisiana CWEI is currently active in the Cotton Valley/Gray and Bossier formations.

In the Bossier trend North Louisiana CWEI has 169,848 net acreage working interest. As of January 2008 the Company had identified 4 prospects in this property, Winnsboro prospect, Ashwood prospect, Gilbert prospect, and Westwood prospects. One well has been drilled in the Winnsboro prospect and the Company has extensive 2-D Seismic plan for this property.



Bossier Trend Properties, North Louisiana (Source: CWEI April 2008 Presentation)

In the Cotton Valley/ Gray formations as of April 2008 the Company had drilled 18 wells in the Sarepta, Terryville, and Ruston fields, mostly in Terryville field, with 83% success rate; 14 wells producing, 1 well in completing stage, and 3 dry holes. In 2008 CWEI plans to drill 8 new wells in the Cotton Valley/Gray formations



Cotton Valley/Gray Properties, North Louisiana (Source: CWEI April 2008 Presentation)

As of December 31, 2007 the Company had 15.9 Bcfe proved oil and gas reserves in its North Louisiana properties which constituted 5.5% of its total proved oil and gas reserves, and the Cotton Valley properties had 9.2 Bcf of proved gas reserves making up 3.1% of the total proved oil and gas reserves of the Company for the year end 2007.

Average daily production from North Louisiana properties was 182 Bbls oil, 8,096 Mcf gas, and 1 Bbls natural gas liquids. At the Cotton Valley properties the Company's average daily production of gas was 7,133Mcf.

The Company's 2008 planned capital expenditures for North Louisiana properties is \$47.9 million which is 19% of its total 2008 planned capital expenditure of \$256.5 million.

The following tables summarize key statistics about the Company's North Louisiana and cotton Valley Properties, as of December 31, 2007.

<b>North Louisiana</b>	
<b>Number of productive wells (net)</b>	
Oil	-
Gas	17.9
Total	17.9
<b>Proved reserves</b>	
Oil (MMBbls)	0.3
Gas (Bcf)	14.1
Total (Bcfe)	15.9
PV 10 (\$million)	72.2
<b>Average daily production</b>	
Oil (Bbls)	182
Gas (Mcf)	8,096
Natural gas liquids (Bbls)	1

<b>Cotton Valley</b>	
<b>Number of productive wells (net)</b>	
Oil	-
Gas	11.6
Total	11.6
<b>Proved reserves</b>	
Oil (MMBbls)	-
Gas (Bcf)	9.2
Total (Bcfe)	9.2
PV 10 (\$million)	32.8
<b>Average daily production</b>	
Oil (Bbls)	-
Gas (Mcf)	7,133
Natural gas liquids (Bbls)	-

### South Louisiana Properties

Prior to 2007 CWEI had drilled 67 gross (53.6 net) exploratory wells in South Louisiana, of which 34 gross (25.9 net) were completed as producers. During 2007 the Company drilled 7 additional wells in South Louisiana 3 of which were dry hole and 4 are producing.

As of December 31, 2007 the Company had 33.9 Bcfe proved oil and gas reserves in its South Louisiana properties which constituted 11.7% of its total proved oil and gas reserves.

During 2007 average daily production from South Louisiana properties was 1,139 Bbls oil, 24,025 Mcf gas and 141 Bbls natural gas liquids.

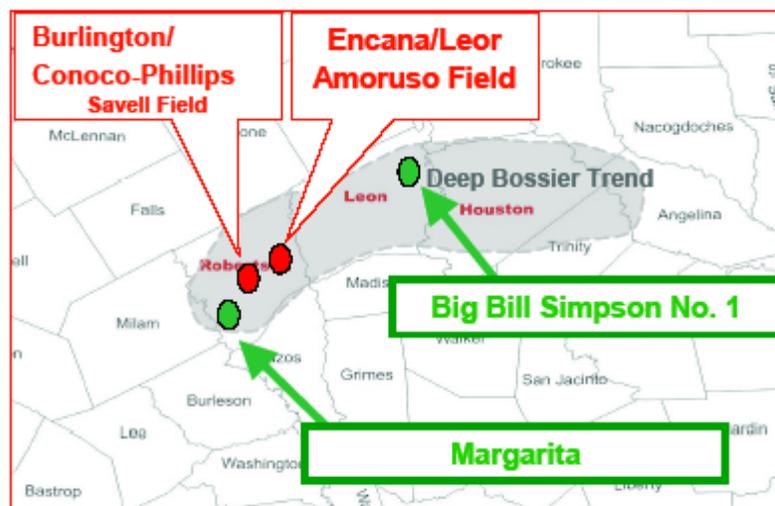
Capital expenditures planned for 2008 in South Louisiana properties is \$13.4 million (5% of total 2008 planned capital expenditures), \$2.9 the Company's share in a Partnership Agreement with an industry partner and \$10.5 million additional capital expenditure by CWEI on exploratory and developmental prospects. The Company plans to drill 6 wells in South Louisiana prospects through a Participation Agreement with an industry partner. According to CWEI's January 2008 press release, the partner will bear 85% of all drilling costs incurred to casing point and 50% of all subsequent costs to earn a 50% working interest.

The following table summarizes key statistics about the Company's South Louisiana Properties, as of December 31, 2007 .

<b>South Louisiana</b>	
<b>Number of productive wells (net)</b>	
Oil	4.2
Gas	25.4
Total	29.6
<b>Proved reserves</b>	
Oil (MMBbls)	1.1
Gas (Bcf)	27.2
Total (Bcfe)	33.9
PV 10 (\$million)	204.2
<b>Average daily production</b>	
Oil (Bbls)	1,139
Gas (Mcf)	24,025
Natural gas liquids (Bbls)	141

### East Texas Deep Bossier Trend Properties

As of December 31, 2007 CWEI had 142,000 net acreage working interest in East Texas, which includes the 70,000 net acres held by production from existing Austin Chalk Trend wells. . As of April 2008 the Company had 1 completed exploratory well and 1 well in the completing process in east Texas Bossier property and had commenced 3-D Seismic Shoot in Big Bill Simpson Area.



East Texas Deep Bossier Trend Properties (Source: CWEI April 2008 Presentation).

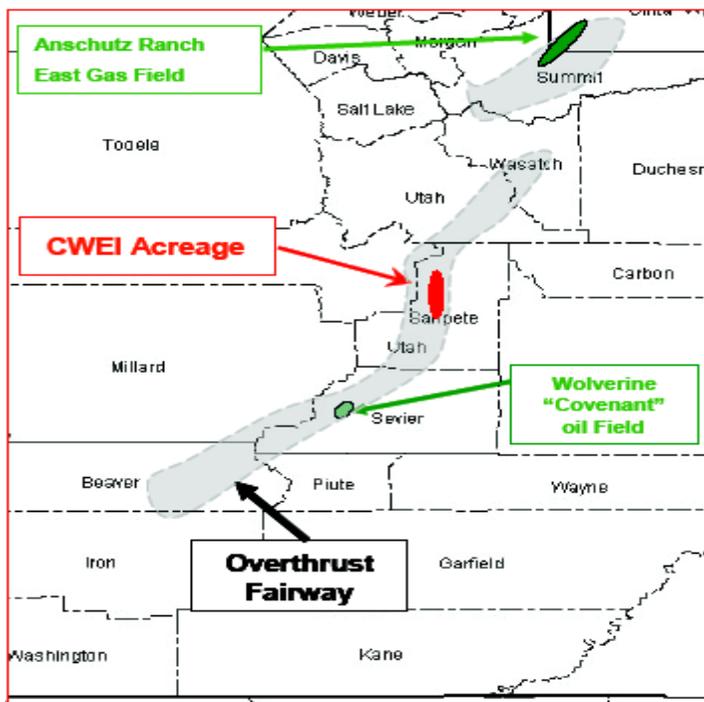
Planned 2008 capital expenditures for east Texas Bossier Trend properties is \$17.2 million or 7% of total 2008 planned capital expenditures.

## Overthrust Play Properties, Utah

The 2004 discovery of Covenant filed in central Utah Thrust Belt by the Wolverine Oil & Gas Corp. changed the declining trend of Utah oil production that had started since the mid-1980. According to Utah Geological Survey, “the Covenant oil field discovery changed the oil development potential in the play from hypothetical to proven. Cumulative production from Covenant field from late 2004 through September 30, 2006, was 2,611,688 barrels of oil, averaging over 6000 barrels of oil per day. The original oil in place is estimated at 100 million barrels ; the estimated recovery factor is 40 to 50 percent”.

The Covenant field provides an important “proof of concept” for future explorations in the Utah Overthrust Belt, as there might exist other oil and gas systems and plays with high reserve potentials in the Overthrust Belt. Since the discovery of the Covenant field many E&P companies have initiated exploration programs in the central Utah Overthrust Belt

In Overthrust Play Properties CWEI has 1/3 joint exploration interest with industry partners. The first well drilled was abandoned. The second well is scheduled to be drilled in 2008.



Overthrust Play Properties, Utah (Source: CWEI April 2008 Presentation).

## CWEI'S OIL AND GAS RESERVES

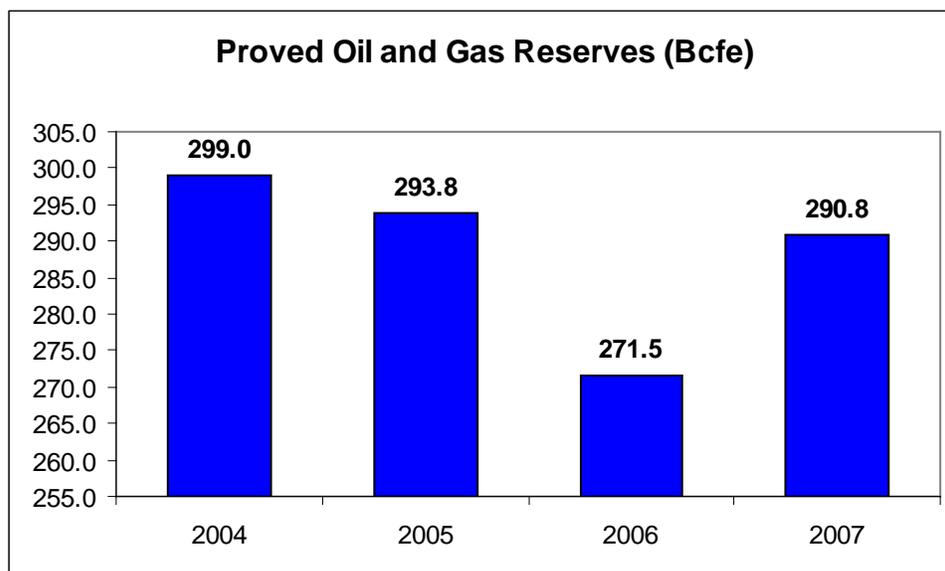
As of December 31, 2007 CWEI had 27.95 MMBbls (million barrels) proved oil reserves (167.7 Bcfe gas equivalent) and natural gas proved reserves of 123.16 Bcf, making it a total gas equivalent of 290.8 Bcfe.

The Company's oil and gas proved reserves as of December 31, 2007 was 19.3 Bcfe more than its oil and gas proved reserves of 171.8 Bcfe as of December 31, 2007. Thus, during 2007 the Company replaced 154% of its 2007 production of 35.9 Bcfe.

The gas equivalent of oil is calculated by converting one barrel of oil to six thousand cubic feet of gas, that is:

$$1 \text{ Bbl of oil} = 6 \text{ Mcf of natural gas}$$

The following chart shows historical trend of CWEI total proved reserves as of its fiscal years ending December 31, 2004 through 2007.



Most of the Company's proved reserves are in its Permian Basin properties. As of December 31, 2007 out of 290.8 Bcfe proved oil and gas reserves of CWEI, 169.16 Bcfe or 58.2% of it were in the Permian Basin.

Proved reserves are classified into proved developed and proved undeveloped reserves. Proved developed reserves (PD) are reserves that are expected to be recovered through existing wells with existing equipment and operating methods. Proved undeveloped reserves (PUD) are reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion.

Proved developed reserves could be producing or nonproducing. Proved developed producing (PDP) reserves are reserves that are expected to be recovered from the currently producing acreage under existing production methods. Proved developed nonproducing (PDNP) reserves consist of (i) proved reserves from wells which have been completed and tested but are not producing due to lack of market or minor completion problems which are expected to be corrected and (ii) proved reserves currently behind the pipe in existing wells and which are expected to be productive due to both the well log characteristics and analogous production in the immediate vicinity of the wells.

The following table shows the structure of CWEI proved reserves based on the above categories.

Reserve category	Bcfe	% of total	
Proved developed producing (PDP)	197.2	67.8%	
Proved developed nonproducing (PDNP)	25	8.6%	
Proved undeveloped (PUD)	68.6	23.6%	
<b>Total</b>	<b>290.8</b>	<b>100.0%</b>	

**It should be noted that reserve estimates, including proved reserve estimates, are not precise because of the factors considered in the estimation and may change as the underlying factors change.**

Oil and Gas companies are not permitted to discuss their non-proved (probable and possible) reserves in their SEC filings. But, they can provide that information to the public in the press releases or their corporate presentations. However, we did not see any information on CWEI's non-proved reserves being provided to the public at the time of preparing this report.

Below are definitions of proved, probable, and possible reserves as per The Society of Petroleum Engineers (SPE):

### Proved Reserves

“Proved reserves are those quantities which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations. Proved reserves can be categorized as developed or undeveloped. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate”.

Proved reserves is also referred to as **1P** reserves in the industry.

**Probable reserves :**

“Probable reserves are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable. In this context, when probabilistic methods are used, there should be at least a 50% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable reserves”.

Proved plus probable reserves is referred to as **2P** reserves in the industry.

#### **Possible reserves:**

“Possible reserves are those unproved reserves which analysis of geological and engineering data suggests are less likely to be recoverable than probable reserves. In this context, when probabilistic methods are used, there should be at least a 10% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable plus possible reserves”.

Proved plus probable plus possible reserves is referred to as **3P** reserves in the industry.

#### **Standardized Measure and PV-10 of Proved Reserves**

Companies in the oil and gas exploration and production are required by the SEC to estimate the present value of their future net cash flows related to **proved reserves**, called **the standardized measure**, in accordance with SFA No. 69 prepared by the Financial Accounting Standard Board (FASB). As per SFA No. 69 the standardized measure should be calculated by applying current year end prices (considering fixed and determinable price changes only to the extent provided by contractual arrangements or law) to estimated future production, less future expenditures (based on current costs) to be incurred in developing proved undeveloped and proved producing oil and gas reserves and less future income taxes and net abandonment costs. The resulting future net cash flows should then be discounted using a rate of 10% per annum to arrive at future net discounted cash flows, or the standardized measure. Because of keeping future prices and costs the same as current ones and the arbitrary discount rate of 10% it should be noted that **the standardized measure is merely a legal requirement and does not necessarily reflect a fair estimate of an oil and gas company's value.**

Some oil and gas E&P companies calculate a similar measure called **PV-10** in addition to the standardized measure. The PV-10 is calculated similarly to the standardized measure except that it does not include the estimated future income taxes and net abandonment costs that are unique for each company. The PV-10 is, therefore, a more realistic measure than the standardized measure for comparing the value of proved reserves of companies across the industry. Nevertheless, because of keeping future prices and costs the same as current ones and the arbitrary discount rate of 10%, PV-10 also does not necessarily represent a fair estimate of an E&P company's value.

As of December 31, 2007 the Company's standardized measure of proved reserves was \$925,97 million and its PV-10 of proved reserves was \$1,331.11 million

The following table shows the Company's standardized measure and PV-10 of proved reserves as of December 31, 2007 .

	Oil (MMBbls)	Gas (Bcf)	Total (Bcfe)	% of Total	PV-10 (\$million)	% PV-10
Permian Basin	17.32	65.25	169.16	58.2%	684.69	51.4%
North Louisiana	0.32	14.05	15.96	5.5%	72.24	5.5%
South Louisiana	1.12	27.19	33.89	11.7%	204.23	15.3%
Austin Chalk	7.53	5.39	50.57	17.4%	305.19	22.9%
Cotton Valley	-	9.16	9.16	3.1%	32.84	2.5%
Other	1.66	2.12	12.09	4.2%	31.93	2.4%
<b>Total</b>	<b>27.95</b>	<b>123.16</b>	<b>290.83</b>	<b>100.0%</b>	<b>\$ 1,331.11</b>	<b>100.0%</b>
<b>Standard measure of proved reserves (\$million)</b>					<b>\$ 925.97</b>	

The average prices utilized by CWEI to estimate its proved reserves, the standardized measure of proved reserves, and the present value of proved reserves as of December 31, 2007 were \$91.30 per Bbl of oil and natural gas liquids and \$7.37 per Mcf of gas, as compared to \$57.18 per Bbl of oil and \$5.24 per Mcf of gas as of December 31, 2006. **The Company estimates that a \$1 per Bbl change in oil price and a \$.50 per Mcf change in gas price from those utilized in calculating the present value of proved reserves would change the present value by approximately \$13.6 million and \$35.6 million, respectively.**

## PRODUCTION

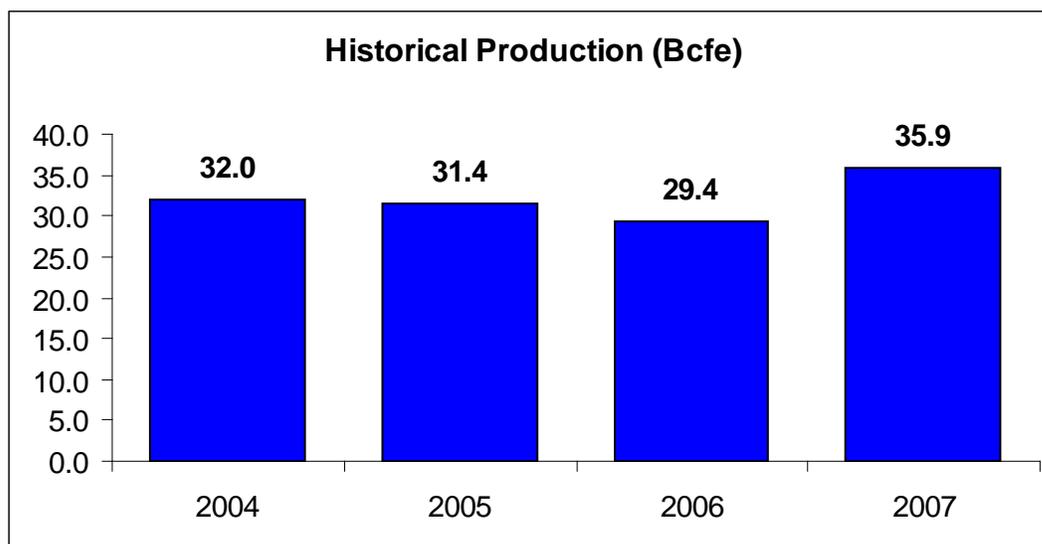
Historically CWEI has been having a balanced mix of oil and gas production. During the year 2007, CWEI produced 20,649 MMcf of gas (35.9% more than 2006), 2,318 MBbls of oil (6.8% more than 2006), and 222 MBbls of natural gas liquid (11.6% more than 2006). Total production on the gas equivalent basis for the year 2007 was 35,889 MMcfe which was 22% more than total production of 2006.

Average daily production in 2007 was 98.33 MMcfe as compared to average daily production of 80.64 MMcfe in 2006. In 2008 the company plans to increase daily production by 10% to reach 113.3 MMcfe production per day by the fourth quarter 2008 as compared to daily production of 102.9 MMcfe during the fourth quarter of 2007.

The following table shows CWEI's annual and average daily productions for the years ended December 31, 2005 through 2007

<b>Production</b>			
	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Gas (MMcf)</b>			
Average daily	56.57	41.64	44.95
Total for the year	20,649	15,198	16,408
<b>Oil (MBbls)</b>			
Average daily	6.35	5.95	6.19
Total for the year	2,318	2,171	2,258
<b>Natural gas liquids (MBbls)</b>			
Average daily	0.61	0.55	0.67
Total for the year	222	199	246
<b>Total production (MMcfe)</b>			
Average daily	98.33	80.64	86.11
Total for the year	35,889	29,418	31,432
<b>Average realized prices</b>			
Gas(\$/Mcf)	\$ 7.01	\$ 6.68	\$ 7.49
Oil (\$/Bbl)	\$ 70.36	\$ 62.92	\$ 53.37
Natural gas liquids (\$/Bbl)	\$ 43.74	\$ 38.18	\$ 33.57
Weighted average oil and gas (\$/Mcf)	\$ 8.83	\$ 8.36	\$ 8.04
<b>Oil and gas costs (\$/Mcf produced)</b>			
Production cost	\$ 2.10	\$ 2.15	\$ 1.83
DD&A	2.12	2.12	1.42

The following chart shows CWEI's total annual production on the gas equivalent basis for the years ended December 31, 2005 through 2007.



## 2008 CAPITAL EXPENDITURE PLANS

In 2008, CWEI plans to spend \$256.5 million on exploration and development activities, an increase of 11.2% over its 2007 capital expenditures on exploration and development activities

Most of the 2008 capital resources are planned to be spent on developmental drilling of oil wells in the Permian Basin and the Austin Chalk (Trend). The 2008 capital expenditure plan also includes continuation of drilling developmental gas wells in North Louisiana, primarily on their Terryville prospect. The Company estimates that approximately \$208.1 million (81%), of its expenditures for exploration and development activities for fiscal 2008 will relate to developmental prospects. In 2007 the Company spent 49% of its capital expenditure budget on developmental activities.

The following table shows breakdown of CWEI's 2008 planned capital expenditures in comparison with the actual 2007 numbers.

	Planned 2008 (in \$millions)	Percentage of total	Actual 2007 (in \$millions)	Percentage of total
Permian Basin	\$ 110.3	43%	\$ 34.2	15%
Austin Chalk (Trend)	59.3	23%	19.2	8%
North Louisiana	47.9	19%	74.3	32%
East Texas Bossier	17.2	7%	31.5	14%
South Louisiana	13.4	5%	65.7	28%
Utah/California	8.3	3%	5.3	2%
Other	0.1	0%	0.5	0%
<b>Total</b>	<b>\$ 256.5</b>	<b>100%</b>	<b>\$ 230.7</b>	<b>100%</b>

## COMPETITIVE LANDSCAPE

The U.S. upstream oil and gas industry is highly concentrated and has an oligopoly structure. The industry consists of a few large corporations, the Majors, that control reserves and productions, and numerous small independent companies entering into the industry as a result of the lucrative energy market in recent years.

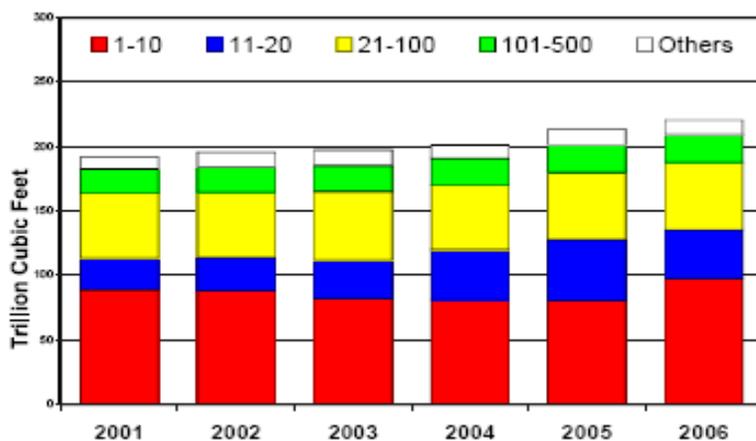
The U.S. Energy Information Administration (EIA) ranks the reporting companies according to total production size and then places the companies into 5 size classes; Class 1-10, containing the top 10 largest producing companies, Class 11-20, containing the second largest 10 producing companies, Class 21-100 containing next 80 largest companies, Class 101- 500 containing the next 400 largest companies, and Class Others which contains 14,658 small companies.

According to the EIA survey,

In 2006, the top 20 operators (Class 1-10 and Class 11-20) producing companies had 61 percent of the proved reserves of natural gas. The next two

size classes contain 80 and 400 companies and account for 24 and 10 percent of the U.S. natural gas proved reserves, respectively. The top 20 operators had an increase of 19 percent in their natural gas proved reserves from 2001 to 2006. The rest of the operators in (Class 21-100, Class 101-500, and Class Other) had an increase of 7 percent in their reserves in the same time period. In 2006, the top 20 operators' natural gas reserves had an increase of 6 percent from 2005. (EIA 2005 Annual Report)

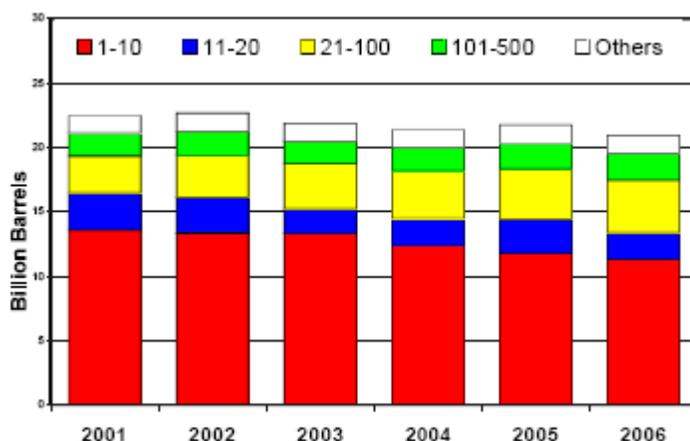
The following chart shows distribution of U.S. proved reserves of natural gas according to the company size for the period 2001-2006:



Source: EIA 2006 Annual Report

The EIA also reports that in the year 2006 the same top 10 producing companies had 54% of the US proved reserves of crude oil. The 20 largest oil and gas producing companies in 2006 had 64% of proved reserves of crude oil.

The following chart shows distribution of U.S. proved reserves of crude oil according to the company size for the period 2001-2006:

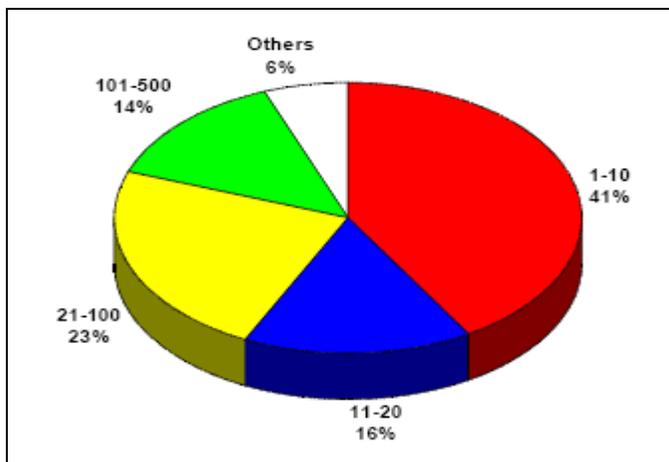


Source: EIA 2006 Annual Report

Similar size distributional numbers hold for production of crude oil and natural gas.

According to the EIA in the year 2006 the top 20 largest U.S. companies accounted for 57% of wet U.S. natural gas production. The next two size classes have 23% and 14% of the wet natural gas production, respectively. Smaller companies (the others) accounted for only 6% of U.S. wet natural gas production in 2006

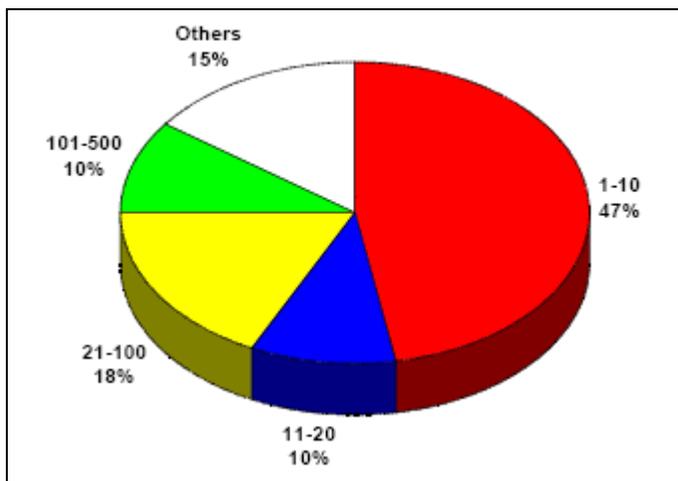
The chart below shows distribution of US natural gas production according to the company size for the year 2006:



Source: EIA 2006 Annual Report

Similarly, the 20 largest oil and gas producing companies had 60% of U.S. production of crude oil in 2006.

The chart below shows distribution of U.S. crude oil production according to the company size for the year 2006:



Source: EIA 2006 Annual Report

Given the commodity nature of oil and natural gas and the fact that prices are uniquely determined by the market, internationally for crude oil, and regionally and nationally for natural gas, it is not possible for independent oil and gas companies to establish competitive advantage through product differentiation and price advantage. Competitive advantage through cost reduction is also not viable for these companies because they are small and it is the major oil companies that enjoy the economies of scale.

**The key to competitive advantage in the independent upstream oil and gas industry segment is, therefore, to discover or acquire new opportunities with high potentials, secure them, and act upon them in a timely manner.**

## OPERATING HIGHLIGHTS

### CWEI's Statement of Operation Highlights

(In thousand except per share amounts)

	For the Year Ended December 31		
	2007	2006	2005
<b>Revenues</b>			
Oil and Gas Sales	\$ 316,992	\$ 245,967	\$ 252,599
Other revenues <sup>1</sup>	76,903	20,031	31,000
<b>Total Revenues</b>	<b>393,895</b>	<b>265,998</b>	<b>283,599</b>
<b>Operating expenses</b>			
Production	(75,319)	(63,298)	(57,404)
Depreciation, depletion, and amortization (DD&A)	(84,476)	(66,163)	(47,509)
Exploration	(73,635)	(76,472)	(50,737)
General and administration	(19,266)	(16,676)	(15,410)
Other operating expenses	(67,169)	(38,143)	(32,198)
<b>Total operating expenses</b>	<b>(319,865)</b>	<b>(260,752)</b>	<b>(203,258)</b>
<b>Operating income</b>	<b>74,030</b>	<b>5,246</b>	<b>80,341</b>
Interest expense	(32,118)	(20,895)	(14,498)
Other non-operating income (expenses) <sup>2</sup>	(30,425)	35,427	(66,037)
Income tax expense (benefit)	(5,497)	(1,979)	451
<b>Net income</b>	<b>\$ 5,990</b>	<b>\$ 17,799</b>	<b>\$ 257</b>
Net income per share: Basic	\$ 0.53	\$ 1.64	\$ 0.02
Net income per share: Diluted	\$ 0.52	\$ 1.58	\$ 0.02
Weighted average shares outstanding, Basic	11,337	10,885	10,804
Weighted average shares outstanding, Diluted	11,494	11,244	11,241

1-Consists of natural gas services, drilling rig services, and gain on sale of property and equipment.

2-Mostly consists of gain (loss) on derivatives.

CWEI is a profitable E&P company.

In 2007 oil and gas revenues increased by 29% as compared to 2006 and reached to about \$317 million. The increase was due to both higher production and higher average

oil and gas prices. Total oil and gas production in 2007 was 35.9 Bcfe which was 22% higher than 2006 total production of 29.4 Bcfe. Oil production increased 7% and gas production increased 38% in 2007. Average realized oil prices in 2007 was \$70.36/Bbls, 12% higher than 2006 average price, and average realized gas price was \$7.01/Mcfe, 5% higher than 2006 average price, making the weighted average realized oil and gas price to be \$8.83/Mcfe, an increase of 5.6% as compared to weighted average realized oil and gas price of \$8.36/Mcfe in 2006. With \$76.9 revenues from natural gas services, drilling rig services, and gain on sales of property and equipment total 2007 revenues amounted to \$393.9 million, an increase of over 48% as compared to total revenues of \$256.9 million in 2006.

Total operating expenses in 2007 were \$319.9 million, an increase of about 23% over 2006 operating expense of \$260.7 million. Major items in CWEI's operating expenses are oil and gas production, DD&A, and exploration expenses. Production and DD&A expenses increased in 2007 as compared to 2006, primarily due to increase in production volume. However, on an Mcfe basis production expenses decreased from \$2.15/Mcfe of production in 2006 to \$2.10/Mcfe of production in 2007 and DD&A in 2007 remained at the 2006 level of \$2.12/Mcfe of production. Exploration costs in 2007 was \$73.6 million which consisted of \$68.9 million abandonment and impairments and \$4.7 million seismic and other costs. The exploration costs is the result of CWEI adopting the successful effort method of accounting and is charged to expenses in any accounting period in which significant seismic costs, exploratory dry hole costs, and unproved acreage impairments occur.

With regard to capital expenditure on oil and gas properties, CWEI has adopted the Successful Efforts (SE) method of accounting, in contrast to Full Cost (FC) method for its oil and gas properties. In the FC method all costs associated with acquisition, exploration, and development of oil and gas reserves, including directly related overhead costs, are capitalized and subsequently amortized on the unit-of-production method using estimates of proved reserves. The SE method, on the other hand, allows only costs incurred in successful exploration activities to be capitalized and subsequently amortized according to the unit of production method.

Operating income for 2007 was \$74.0 million, substantially greater than 2006 operating income of \$5.2 million. However, net income for 2007 was \$5.9 million as compared to net income of \$17.8 million in 2006. The reason for such differences between net and operating income is that in 2006 the Company recorded \$37.3 million gain on derivatives while in 2007 the Company recorded \$31.9 million loss on derivatives.

Overall, earning per basic share in 2007 was \$0.53 and in 2006 was \$1.64

**We think traditional performance metrics like net operating margin and net margin ratios are not useful indicators to assess an oil and gas E&P company or compare different E&P companies.** This is because different oil and gas companies use different accounting methods to capitalize or expense their exploration and development costs. Instead we think a better metric to assess the performance of E&P companies is the EBITDAX, EBITDAX margin, and EBITDAX per share.

EBITDAX is computed in slightly different ways by different companies or different analyst. We compute the EBITDAX by adding back to **operating income**, which is the traditional definition of EBIT, the exploration expense, the DD&A expense, and the

impairment of property and equipment. **Thus by computing EBITDAX metrics, we assess the companies' performance independent of financing policies, accounting policies, and non-operating results.**

The following table contains some supplementary information about CWEI's operating performance including EBITDAX metrics.

<b>Supplementary Operating Information</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Total production (MMcfe)</b>			
Average daily	98.33	80.64	86.11
Total for the year	35,889	29,418	31,432
<b>Average realized prices</b>			
Gas(\$/Mcf)	\$ 7.01	\$ 6.68	\$ 7.49
Oil (\$/Bbl)	\$ 70.36	\$ 62.92	\$ 53.37
Natural gas liquids (\$/Bbl)	\$ 43.74	\$ 38.18	\$ 33.57
Weighted average oil and gas (\$/Mcf)	\$ 8.83	\$ 8.36	\$ 8.04
<b>Oil and gas costs (\$/Mcf produced)</b>			
Production cost	\$ 2.10	\$ 2.15	\$ 1.83
DD&A	2.12	2.12	1.42
<b>Operating metrics</b>			
EBITDAX (\$million)	244.3	169.7	196.9
EBITDAX/Mcfe production	\$ 6.8	\$ 5.8	\$ 6.3
EBITDAX per basic share	\$ 21.55	\$ 15.59	\$ 18.22
EBITDAX margin	62.0%	63.8%	69.4%
Operating margin	18.8%	2.0%	28.3%
Net margin	1.5%	6.7%	0.1%

## STOCK PRICE BEHAVIOR

The 52-Week price and volume behavior of CWEI from April 25, 2007 to April 25, 2008 is exhibited below:

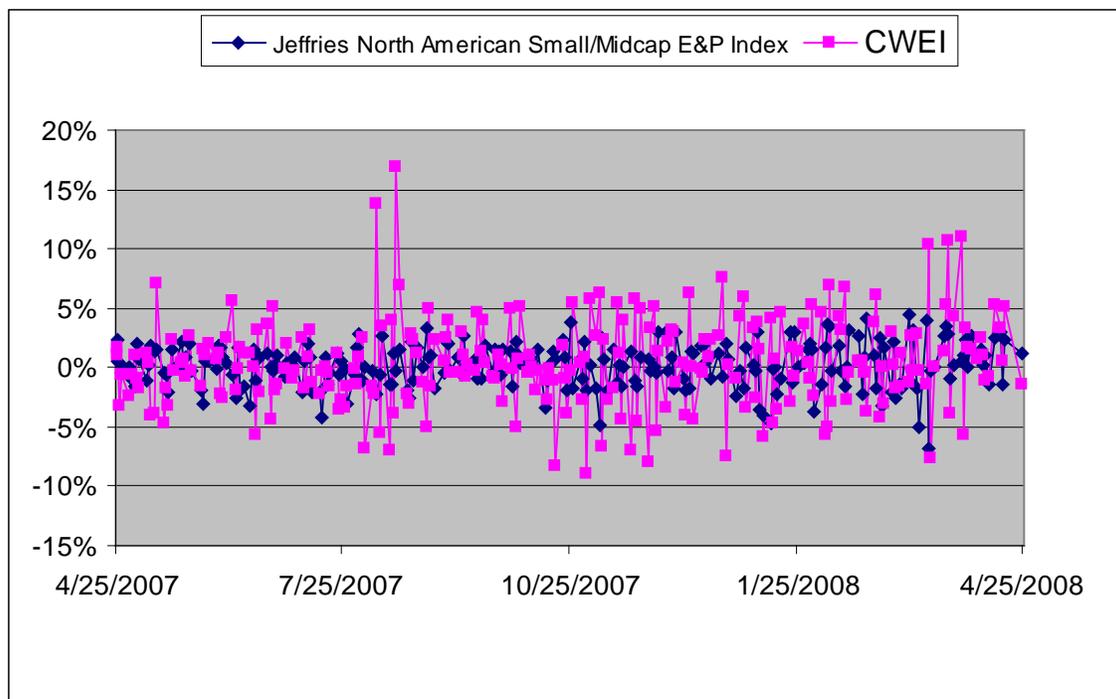


Source: MSN.com

During the one-year period, CWEI was trading (closing prices) in the \$21.33 to \$64.59 range. The average daily volume for the one year period was about 43,900 shares. For the most recent 90 days the stock was trading in the \$28.71 to \$64.59 range with an average daily volume of around 58,000 shares. With 11.3 million common shares of CWEI outstanding as of December 31, 2007 the one-year average daily volume represents about 0.39% of the company's outstanding shares and the 90-day average daily volume represents 0.51% of the Company's outstanding shares.

We think a suitable benchmark to assess return behavior of CWEI is the Jefferies North American Small/Midcap E&P Index<sup>SM</sup>. Unlike the S&P E&P index that incorporates all capitalizations including integrated oil and gas companies, the Jefferies North American Small and Midcap E&P Index contains only small and midcap exploration and production oil and gas companies and, therefore, it is a more suitable benchmark to evaluate return behavior of CWEI.

The figure below shows daily price return volatility of CWEI versus Jefferies North American Small and Midcap E&P Index during the one year period:



Analysis of daily prices of CWEI from April 21, 2007 to April 21, 2008 indicates a daily price return volatility of 3.72% with average daily price rate of return of 0.38%. For the same period of time, the risk-return profile for the Jefferies North American Small and Midcap E&P Index shows a daily return volatility of 1.84% with average daily rate of return of 0.19%.

The following table summarizes price return of CWEI versus the Jefferies North American Small and Midcap E&P Index for the period April 25, 2007 to April 25, 2008

	Jefferies North American Small/Midcap E&P Index	CWEI
<b>Total one year price return</b>	<b>51.34%</b>	<b>125.92%</b>
<b>Average daily price return</b>	<b>0.19%</b>	<b>0.38%</b>
<b>Daily price return volatility</b>	<b>1.84%</b>	<b>3.72%</b>
<b>Daily price return /volatility</b>	<b>0.103</b>	<b>0.102</b>

As the above risk-return profile indicates, in the past twelve months, common shares of CWEI have outperformed the Jefferies North American Small/Midcap E & P Index by over two times, on both an annual and on a daily basis. However, the daily price volatility of CWEI has also been almost two times higher than the daily price volatility of the Jefferies North American Small/Midcap E & P Index.

## **ANALYST CERTIFICATION**

We, **Mohammad Sharifzadeh, PhD, CFA and Simin Hojat, M.Phil** are, the Research Analyst responsible for the preparation of this Research Report hereby certify that:

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(2) the compensation payable to the Research Analysts, is not, has not, and will not, directly or indirectly, be related to the specific views and opinions expressed by the Research Analysts in this Research Report.

(3) We have no ownership in, nor any affiliations with the company in this research report.

**Mohammad Sharifzadeh, PhD, CFA**, is a member of CFA Institute, Los Angeles CFA, and GARP.

The analysts' biographical details are at <http://www.alphabetaresearch.com>

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### **Rating and Price Target Methodology**

In arriving at an investment rating and price target, we use the following analytical measures:

- 1) Potentials and opportunities: Competitive advantage, market potentials, patents, properties, reserves.
- 2) Risk factors: Regulatory approvals, R&D results, ability to raise capital, going concern issues, competition, industry prospects.
- 3) Evaluation of the stocks fair value given the company's potentials and risks through various valuation metrics.

## RESEARCH RATING SYSTEM

<b>STRONG BUY</b>	<b>(5)</b>
<b>BUY</b>	<b>(4)</b>
<b>SPECULATIVE BUY</b>	<b>(3)</b>
<b>HOLD</b>	<b>(2)</b>
<b>SELL</b>	<b>(1)</b>
<b>AVOID</b>	<b>(1)</b>

## DEFINITION OF OUR RATINGS

**STRONG BUY (5):** Company's stock price appears to be substantially undervalued relative to its future growth potential.

**BUY (4):** Shares appear to be undervalued in light of several factors.

**\*SPECULATIVE BUY (3):** Shares appear to offer potential gains though risk is considerably higher. Such a company may have "going concern" problems, or company's future prospects may hinge on critical assumptions, such as (but not limited to) the company's ability to compete effectively in the marketplace, achieve most or all of its stated business goals, maintain sufficient financial liquidity and resources for daily operations, for expansion, and for the avoidance of legal or other pitfalls.

**HOLD (2):** Shares appear to be fairly valued and while there is no incentive to add such shares, there are similarly no current known compelling factors that would warrant selling absent a subsequent trading drop in value.

**SELL (1):** At present, shares appear to be overvalued.

**AVOID (1):** At present, shares appear to be significantly overvalued

### **\*What does "speculative" mean in a rating?**

Companies with meager or no historical data or that are at the development stage, are generally considered highly SPECULATIVE. Such companies may even have "going concern" problems and an analyst recommendation should be considered only as a part of a total investigative process by anyone considering purchase. A speculative buy opinion generally refers to future valuations only if the company is able to achieve most or all of its business goals and avoid most or all of the possible risks, including raising sufficient capital and effectively competing in its marketplace.