

**US Refining Sector Outlook Premcor, Valero, Suncor Rated Out Perform
March 25, 2004**

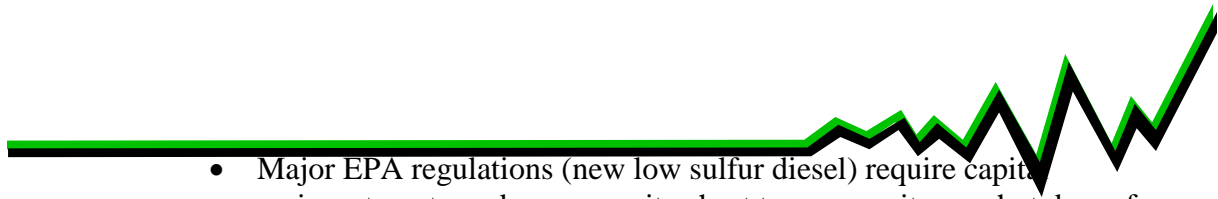
- crude oil pricing is likely to remain \$30- 35 the rest of the year based on strong demand (US transportation, China growth, no resolution to terrorism threat and geopolitical risk.
- Refining margins (crack spread) are in long term secular up trend irregardless of crude pricing
 - The number of gasoline grades has increased from historic 3 based on octane to 25 due to regulatory requirements: ozone compliance, oxygenates, MTBE ban, ethanol usage, seasonal and geographic factors. This increases storage requirements, complexity and costs. It complicates and reduces imports.
 - Ongoing industry consolidation. Capital and environmental costs force marginal refineries to shut down.

No new refineries in US since 1980, and number of operating refineries has fallen from 250 to 150 since 1980.

Independent Refiners Grow Via Acquisition, which should continue

Premcor	acq Motiva (Shell) Delaware City refinery & power plant, 180 KBPD, \$900M
Suncor	acquired Conoco Phillips Denver, CO refinery, Aug '03, 60 KBPD, \$150M
Hess	- primarily E&P
Frontier	-regional Rocky Mountain area only
Sunoco	acq El Paso Eagle Point, NJ refinery, Jan '04, 150 KBPD, \$235M
Tesoro	- balanced refining and marketing in Western US
Valero	acq El Paso's Aruba refinery Jan '04, 315KBPD, \$630M acq Orion Corp refinery, Jul '03, 215 KBPD, \$549M

- Major integrated oil companies focusing on most profitable sector (upstream E&P) which has driven consolidation and divestment of lower return downstream assets so that capital is available for E&P.
 - Exxon- Mobil merger. Exxon sold Benecia refinery to Valero, Bayway to TOSCO/Philips
 - Chevron -Texaco merger
 - Conoco- Phillips merger. Sold Denver to Suncor.
 - Shell – sold Motiva (JV with Saudi Govt), Delaware, to Premcor
 - BP- sold Ohio refinery to Premcor



- Major EPA regulations (new low sulfur diesel) require capital investments; reduces capacity short term, as units are shut down for construction, and long term if marginally profitability and new investment is not justified.

Refining margins have been in a long term uptrend (see Figure 1) for these reasons. The industry is near 90% capacity and margins have increased whether crude is up (cost pass through) or down (reductions are not given back, or done so over time). An examination of the long term and recent trends clearly shows this up/down pattern and series of higher lows.

Premcor (PCO, \$30.25)
Rating - Out Perform

Company went public in 2002 following acquisition by the Blackstone Group of the Clark Refining Company in St. Louis.

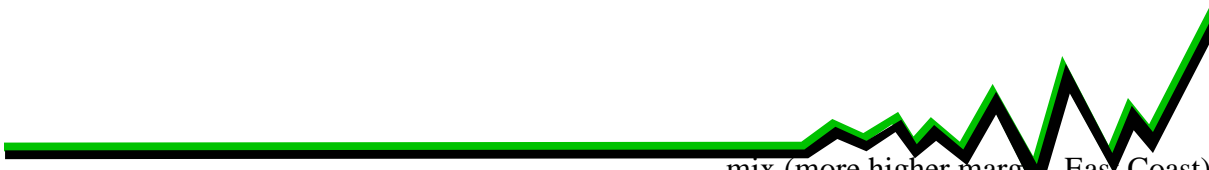
Strategy

- Grow by acquiring and operating complex refineries that can handle heavy crude which sells at a substantial discount to normal/'sweet' crude thereby achieving higher margins.
- Experienced management team which came from TOSCO- a \$30B independent refiner that was sold to Phillips in 2003. Another major acquisition within two years is probable although must be immediately accretive.
- Focus on refining, not retailing. Fedex is largest customer.
- Operating risk substantially reduced with purchase of Motiva Refinery in Delaware City so they now have 4 refineries and 790 KBPD capacity.

Substantial upside in 2004 based on:

- Higher volumes from existing capacity since turnarounds for new equipment were taken in 2003 which reduced throughput and capacity utilization to 82%. Should achieve 89% in 2004 which is about industry average.
 - Volume and margin contribution from Motiva refinery Higher product spreads given new exposure to East Coast markets which is more profitable
 - Relatively low SG & A expenses, now spread over larger base
 - Crack margins below trend in 2004 but volatile
- 2004 EPS estimate \$4.02 vs \$1.70 2003 (+140%). First Call consensus 2004 is \$2.85 net. See attached.

	<u>2003</u>	<u>2004</u>	
Throughput volume, M B	183	225	+23% Motiva plus higher capacity utilization
Refining margin, \$/B	3.06	3.19	+4% industry margin up, product



SG&A	0.68	0.53	-22%	mix (more higher margin East Coast) efficiency from Motiva expansion
Interest, Depreciation	1.36	1.22	-11%	assumed Motiva debt at low interest
NIBT, \$/B	1.02	1.44	+41%	
NIAT,\$/B @34%	0.67	0.95	+42%	
EPS, cont operations, fully diluted	1.70	2.59	+52%	

Our 12 month price target is \$49 based on slightly higher Enterprise Value/EBITDA ratio and 2005 EPS estimates.

Valuation	2003	2004	2005
Stock Price	26	30	30
Market Capitalization,\$M	1,893	2,473	2,623
LT Debt, \$M	1426	1876	1876
Enterprise Value,\$M	3,319	4,349	4,499
Enterprise Value/EBITDA	7.6	7.3	5.8
Price Target @ EV/EBITDA		8.0	8.0
Price Target,\$/share		35.23	49.30

Estimates

EPS Continuing Operations, fully diluted	Q1	Q2	Q3	Q4	FY
2003 Actual	0.60	0.46	0.78	-0.16	1.68
2004 Estimate	0.33	0.73	0.84	0.65	2.59
2005 Estimate					3.56

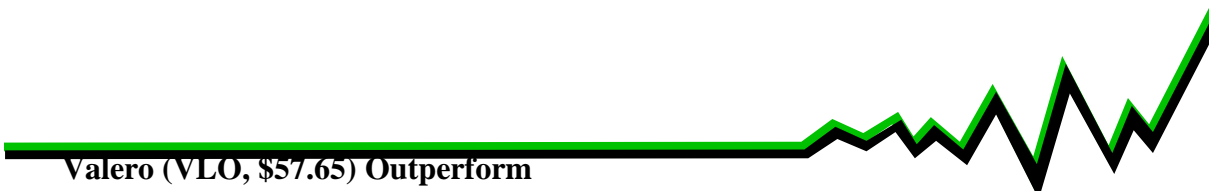
RISKS

Product Margins- This is a high volume/low margin business and earnings are very sensitive to the spread between sales price and cost of goods. A \$0.10 change in refining margin changes EPS \$0.08

Volume and Operations PCO has 3 refineries (expect to close on 4th May 1, 2004) and operating problems at one can have a major impact on earnings. A 1% change in volume changes EPS \$0.03

Narrow Product Line- PCO is solely involved in petroleum refining

Financial Risk- PCO has a debt to equity ratio of 1.3 EBITDA to interest expense in 2003 was 3.0 which should increase to 4.6 in 2004.



Valero (VLO, \$57.65) Outperform

- Largest independent refiner in US with 2,100 K BPD capacity, 10% market share, substantial marketing.
- Very high operating leverage (5 B throughput per share outstanding).

Suncor (SU US\$26.40 Out Perform) The stock is up 39% since our October 1,2003 report rating it Out Perform, and approaching our 12 month price target of \$31.50. While remaining a core holding the comparisons throughout the rest of the year may be more modest than what we see in the US refining sector. Most of SU's assets are in the oil sand recovery and conversion to synthetic crude which provides most of their profit, rather than conventional refining of crude to light products such as gasoline and fuel oil. It is less dependent on the refined product crack spread than the US refiners which we think is the place to be this year.

Supporting Tables, Financial Model, Comparative Valuation and historical analysis available from Pittsburg Research Sales Department 1-800-893-4422

Premcor

PCO Premcor Inc (NYSE)

3/26/2004 1:48 PM

Last: 30.25	Change: ▲ +0.50	Open: 29.75	High: 30.25	Low: 29.75	Volume: 106,000
	Percent Change: +1.68%	Yield: n/a	P/E Ratio: 18.01	52 Week Range: 20.05 to 31.94	



Chart Number	Date	Rating	Price
1	3/26/04	Out Perform	30.25

Valero VLO

Last: 57.65	Change: ▲ +1.10	Open: 57.00	High: 57.80	Low: 56.82	Volume: 739,800
	Percent Change: +1.95%	Yield: 0.83%	P/E Ratio: 11.33	52 Week Range: 35.16 to 61.50	



Chart Number	Date	Rating	Price
1	3/26/04	Out Perform	57.65

SU Suncor Energy Inc (NYSE)

3/26/2004 2:33 PM

Last: 26.40	Change: ▲ +0.15	Open: 26.30	High: 26.54	Low: 26.26	Volume: 582,800
	Percent Change: +0.57%	Yield: 0.57%	P/E Ratio: 14.08	52 Week Range: 16.10 to 28.75	



Chart Number	Date	Rating	Price
1	10/21/02	In Line	16.14
2	10/1/03	Out Perform	18.74

Rating Definitions and Allocation

Rating

Definition



1-Out Perform

Positive return potential as compared to applicable index over the next 18-24 months

2- In-Line

Return potential approximately equal to applicable index over the next 18-24 months

3- Under Perform

Negative return potential as compared to applicable index over the next 18-24 months

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Ratings for stocks:

1= Outperform- The stock is projected to outperform the stocks covered by the analyst within his industry over the next 12-18 months.

2= In-Line – The stock is projected to perform approximately in-line with the stocks covered by the analyst within his industry over the next 12-18 months.

3=Underperform The stock is projected to underperform the stocks covered by the analyst within his industry over the next 12-18 months

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