

PETROLEUM & RESOURCES CORP
Form N-30B-2
April 19, 2006

PETROLEUM & RESOURCES CORPORATION

Board of Directors

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Frederic A. Escherich ^{2,3}

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2. *Member of Audit Committee*

3. *Member of Compensation Committee*

4. *Member of Retirement Benefits Committee*

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Chairman, President and Chief Executive Officer

Executive Vice President

Vice President, General Counsel and Secretary

Vice President, Chief Financial Officer and Treasurer

Vice President

Vice President Research

Assistant Treasurer

Assistant Secretary

Stock Data

Market Price (3/31/06)	\$33.20
Net Asset Value (3/31/06)	\$37.09
Discount:	10.5%

New York Stock Exchange and Pacific Exchange ticker symbol: PEO

NASDAQ Mutual Fund Quotation Symbol: XPEOX

Newspaper stock listings are generally under the abbreviation: PetRs

Distributions in 2006

From Investment Income (paid or declared)	\$ 0.16
From Net Realized Gains	0.10
Total	\$ 0.26

2006 Dividend Payment Dates

March 1, 2006

June 1, 2006

September 1, 2006*

December 27, 2006*

*Anticipated

LETTER TO STOCKHOLDERS

We submit herewith the financial statements of the Corporation for the three months ended March 31, 2006. In addition, there is a schedule of investments, along with other financial information.

Net assets of the Corporation at March 31, 2006 were \$37.09 per share on 21,398,080 shares outstanding, compared with \$35.24 per share at December 31, 2005 on 21,621,072 shares outstanding. On March 1, 2006, a distribution of \$0.13 per share was paid, consisting of \$0.07 from 2005 long-term capital gain, \$0.03 from 2005 short-term capital gain and \$0.03 from 2005 investment income, all taxable in 2006. On April 13, 2006, an investment income dividend of \$0.13 per share was declared to shareholders of record May 18, 2006, payable June 1, 2006.

Net investment income for the three months ended March 31, 2006 amounted to \$2,015,304, compared with \$2,144,746 for the same period in 2005. These earnings are equal to \$0.09 and \$0.10 per share on the average number of shares outstanding during each period.

Net capital gain realized on investments for the three months ended March 31, 2006 amounted to \$19,616,857, the equivalent of \$0.92 per share.

The Annual Meeting, held on March 28, 2006, in Orlando, Florida, was well attended. The results of the voting at the Annual Meeting are shown on page 14.

Current and potential shareholders can find information about the Corporation, including the daily net asset value (NAV) per share, the market price, and the discount/premium to the NAV, at its website (www.peteres.com). Also available at the website are a brief history of the Corporation, historical financial information, and other useful content. Further information regarding shareholder services is located on page 15 of this report.

After serving 30 years on the Corporation's Board of Directors, Mr. Robert J.M. Wilson retired in March 2006. Mr. Wilson started his career with the Corporation as the President and a Director in 1975. He retired from the Corporation in 1986 and continued serving on the Board until this year. Over the years, his insight in the financial markets and strong analytical discipline were invaluable to the Corporation, and all of our shareholders gained from the wisdom and judgment that he provided. We wish him well in his retirement and thank him for all his years of commitment to the Corporation.

We are pleased to announce the appointment of Mr. Frederic A. Escherich to the Board of Directors of the Corporation, effective February 9, 2006. Mr. Escherich, a 25-year veteran of J.P. Morgan, is now a private investor. He retired from J.P. Morgan in 2002 as the head of Mergers and Acquisitions Research. Prior to that he was head of J.P. Morgan's Financial Advisory Department; he managed industry analyst teams in transportation and technology and in the consumer and health care sectors. With his broad knowledge and experience in the equities markets, he is a valuable addition to the Board of Directors.

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Effective March 28, 2006, the Board of Directors elected Mr. Robert E. Sullivan to Vice President Research. Mr. Sullivan, a CFA, joined the Corporation in 2004 as a senior analyst covering the energy sectors. Previously, he was a senior equity analyst with UBS focusing on the natural gas, electric and coal sectors.

The Corporation is an internally-managed equity fund emphasizing petroleum and other natural resource investments. The investment policy of the Corporation is based on the primary objectives of preservation of capital, the attainment of reasonable income from investments, and an opportunity for capital appreciation.

By order of the Board of Directors,

Douglas G. Ober,

Chairman, President and

Chief Executive Officer

April 21, 2006

STATEMENT OF ASSETS AND LIABILITIES

March 31, 2006

(unaudited)

Assets		
Investments* at value:		
Common stocks and convertible securities (cost \$329,624,727)	\$ 778,986,352	
Short-term investments (cost \$13,658,706)	13,658,706	
Securities lending collateral (cost \$13,801,464)	13,801,464	\$ 806,446,522
Cash		274,928
Receivables:		
Investment securities sold		4,152,327
Dividends and interest		773,282
Prepaid pension cost		924,684
Prepaid expenses and other assets		494,837
<i>Total Assets</i>		813,066,580
Liabilities		
Investment securities purchased		2,687,292
Open written option contracts at value (proceeds \$698,918)		539,735
Obligations to return securities lending collateral		13,801,464
Accrued expenses		2,478,727
<i>Total Liabilities</i>		19,507,218
Net Assets		\$ 793,559,362
Net Assets		
Common Stock at par value \$1.00 per share, authorized 50,000,000 shares; issued and outstanding 21,398,080 shares (includes 15,052 restricted shares, restricted stock units for 7,200 shares and deferred stock units for 295 shares) (Note 6)		\$ 21,398,080
Additional capital surplus		302,199,467
Unearned compensation restricted stock awards (Note 6)		(569,910)
Undistributed net investment income		1,474,961
Undistributed net realized gain on investments		19,535,956
Unrealized appreciation on investments		449,520,808
Net Assets Applicable to Common Stock		\$ 793,559,362
Net Asset Value Per Share of Common Stock		\$37.09

* See Schedule of Investments on pages 9 and 10.

The accompanying notes are an integral part of the financial statements.

STATEMENT OF OPERATIONS

Three Months Ended March 31, 2006

(unaudited)

Investment Income	
Income:	
Dividends	\$ 2,946,331
Interest and other income	183,299
<i>Total income</i>	<i>3,129,630</i>
Expenses:	
Investment research	435,791
Administration and operations	286,205
Directors' fees	103,520
Reports and stockholder communications	71,276
Transfer agent, registrar and custodian expenses	39,071
Auditing and accounting services	24,776
Legal services	15,677
Occupancy and other office expenses	109,533
Travel, telephone and postage	16,119
Other	12,358
<i>Total expenses</i>	<i>1,114,326</i>
Net Investment Income	2,015,304
Realized Gain and Change in Unrealized Appreciation on Investments	
Net realized gain on security transactions	19,616,857
Change in unrealized appreciation on investments	20,709,463
Net Gain on Investments	40,326,320
Change in Net Assets Resulting from Operations	\$ 42,341,624

The accompanying notes are an integral part of the financial statements.

STATEMENTS OF CHANGES IN NET ASSETS

	Three Months Ended	Year Ended
	March 31, 2006	December 31, 2005
	(unaudited)	
From Operations:		
Net investment income	\$ 2,015,304	\$ 11,391,783
Net realized gain on investments	19,616,857	26,239,852
Change in unrealized appreciation on investments	20,709,463	153,388,454
<i>Change in net assets resulting from operations</i>	42,341,624	191,020,089
Distributions to Stockholders from:		
Net investment income	(646,975)	(12,030,248)
Net realized gain from investment transactions	(2,155,814)	(25,924,473)
<i>Decrease in net assets from distributions</i>	(2,802,789)	(37,954,721)
From Capital Share Transactions:		
Value of shares issued in payment of distributions	1,375	14,748,314
Cost of shares purchased (Note 4)	(7,981,320)	(24,891,727)
Deferred compensation (Notes 4,6)	86,820	104,296
<i>Change in net assets from capital share transactions</i>	(7,893,125)	(10,039,117)
Total Increase in Net Assets	31,645,710	143,026,251
Net Assets:		
Beginning of period	761,913,652	618,887,401
End of period (including undistributed net investment income of \$1,474,961 and \$106,632, respectively)	\$ 793,559,362	\$ 761,913,652

The accompanying notes are an integral part of the financial statements.

This report, including the financial statements herein, is transmitted to the stockholders of Petroleum & Resources Corporation for their information. It is not a prospectus, circular or representation intended for use in the purchase or sale of shares of the Corporation or of any securities mentioned in the report. The rates of return will vary and the principal value of an investment will fluctuate. Shares, if sold, may be worth more or less than their original cost. Past performance is not indicative of future investment results.

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

1. SIGNIFICANT ACCOUNTING POLICIES

Petroleum & Resources Corporation (the Corporation) is registered under the Investment Company Act of 1940 as a non-diversified investment company. The Corporation's investment objectives as well as the nature and risk of its investment transactions are set forth in the Corporation's registration statement.

Security Valuation Investments in securities traded on national security exchanges are valued at the last reported sale price on the day of valuation. Over-the-counter and listed securities for which a sale price is not available are valued at the last quoted bid price. Short-term investments (excluding purchased options) are valued at amortized cost. Purchased and written options are valued at the last quoted asked price.

Security Transactions and Investment Income Investment transactions are accounted for on the trade date. Gain or loss on sales of securities and options is determined on the basis of identified cost. Dividend income and distributions to shareholders are recognized on the ex-dividend date, and interest income is recognized on the accrual basis.

2. FEDERAL INCOME TAXES

The Corporation's policy is to distribute all of its taxable income to its shareholders in compliance with the requirements of the Internal Revenue Code applicable to regulated investment companies. Therefore, no federal income tax provision is required. For federal income tax purposes, the identified cost of securities at March 31, 2006 was \$357,055,074, and net unrealized appreciation aggregated \$449,391,448, of which the related gross unrealized appreciation and depreciation were \$452,682,645 and \$3,291,197, respectively.

Distributions are determined in accordance with income tax regulations which may differ from generally accepted accounting principles. Accordingly, annual reclassifications are made within the Corporation's capital accounts to reflect income and gains available for distribution under income tax regulations.

3. INVESTMENT TRANSACTIONS

The Corporation's investment decisions are made by a committee of management, and recommendations to that committee are made by the research staff.

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Purchases and sales of portfolio securities, other than options and short-term investments, during the three months ended March 31, 2006 were \$25,700,736 and \$31,938,300 respectively. Options may be written (sold) or purchased by the Corporation. The Corporation, as writer of an option, bears the risks of possible illiquidity of the option markets and from movements in security values. The risk associated with purchasing an option is limited to the premium originally paid. A schedule of outstanding option contracts as of March 31, 2006 can be found on page 12.

Transactions in written covered call and collateralized put options during the three months ended March 31, 2006 were as follows:

	Covered Calls		Collateralized Puts	
	Contracts	Premiums	Contracts	Premiums
Options outstanding, December 31, 2005	1,940	\$ 292,777	1,050	\$ 129,891
Options written	2,909	375,404	2,185	280,071
Options terminated in closing purchase transactions	(150)	(20,549)	(100)	(13,199)
Options expired	(1,450)	(175,394)	(750)	(85,797)
Options exercised	(570)	(84,286)		
Options outstanding, March 31, 2006	2,679	\$ 387,952	2,385	\$ 310,966

4. CAPITAL STOCK

The Corporation has 5,000,000 authorized and unissued preferred shares without par value.

On December 27, 2005, the Corporation issued 438,416 shares of its Common Stock at a price of \$33.64 per share (the average market price on December 12, 2005) to stockholders of record on November 22, 2005 who elected to take stock in payment of the year-end distribution from 2005 capital gain and investment income.

During 2006, the Corporation issued 42 shares of its Common Stock at a weighted average price of \$32.60 per share as dividend equivalents to holders of deferred stock units and restricted stock units under the 2005 Equity Incentive Compensation Plan.

The Corporation may purchase shares of its Common Stock from time to time at such prices and amounts as the Board of Directors may deem advisable.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Transactions in Common Stock for 2006 and 2005 were as follows:

	Shares		Amount	
	Three months ended March 31, 2006	Year ended December 31, 2005	Three months ended March 31, 2006	Year ended December 31, 2005
Shares issued in payment of dividends	42	438,416	\$ 1,375	\$ 14,748,314
Shares purchased (at a weighted average discount from net asset value of 8.2% and 8.1%, respectively)	(237,750)	(806,050)	(7,981,320)	(24,891,727)
Restricted shares/units granted under the equity incentive compensation plan	14,716	9,030	86,820	104,296
Net change	(222,992)	(358,604)	\$ (7,893,125)	\$ (10,039,117)

5. RETIREMENT PLANS

The Corporation's qualified defined benefit pension plan covers all employees with at least one year of service. In addition, the Corporation has a nonqualified defined benefit plan which provides eligible employees with retirement benefits to supplement the qualified plan. Benefits are based on length of service and compensation during the last five years of employment. The Corporation's policy is to contribute annually to the plans those amounts that can be deducted for federal income tax purposes, plus additional amounts as the Corporation deems appropriate in order to provide assets sufficient to meet benefits to be paid to plan participants. During the three months ended March 31, 2006, the Corporation contributed \$7,802 to the plans. The Corporation anticipates contributing an additional \$23,406 to the plans during the remainder of 2006.

The following table aggregates the components of the plans' net periodic pension cost for the three months ended March 31, 2006.

Service Cost	\$ 83,719
Interest Cost	81,998
Expected return on plan assets	(78,048)
Amortization of prior service cost	9,429
Amortization of net loss	56,341
Net periodic pension cost	\$ 153,439

The Corporation also sponsors a defined contribution plan that covers substantially all employees. For the three months ended March 31, 2006, the Corporation expensed contributions of \$25,497. The Corporation does not provide postretirement medical benefits.

6. STOCK-BASED COMPENSATION

The Stock Option Plan adopted in 1985 (1985 Plan) permits the issuance of stock options and stock appreciation rights for the purchase of up to 895,522 shares of the Corporation's Common Stock at the fair market value on the date of grant. The exercise price of the options and related stock appreciation rights is reduced by the per share amount of capital gains paid by the Corporation during subsequent years. Options are exercisable beginning not less than one year after the date of grant and stock appreciation rights are exercisable beginning not less than two years after the date of grant. The stock appreciation rights allow the holders to surrender their rights to exercise their options and receive cash or shares in an amount equal to the difference between the option exercise price and the fair market value of the Common Stock at the date of surrender. All options terminate 10 years from the date of grant if not exercised. With the adoption of the 2005 Equity Incentive Compensation Plan (2005 Plan) at the 2005 Annual Meeting, no further grants will be made under the 1985 Plan, although unexercised awards granted in 2004 and prior years remain outstanding.

A summary of option activity under the 1985 Plan as of March 31, 2006, and changes during the period then ended is presented below:

	Options	Weighted-Average Exercise Price	Weighted-Average Remaining Life (Years)
Outstanding at December 31, 2005	103,997	\$ 18.24	5.07
Exercised	(2,500)	13.49	
Cancelled	(4,474)	20.34	
Outstanding at March 31, 2006	97,023	\$ 18.17	4.79
Exercisable at March 31, 2006	46,986	\$ 17.61	4.14

The options outstanding as of March 31, 2006 are set forth below:

Exercise Price	Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Life (Years)
\$12.50-\$14.99	14,398	\$ 13.11	1.99
\$15.00-\$17.49	32,301	16.29	4.17
\$17.50-\$19.99	18,583	19.45	5.75
\$20.00-\$22.49	31,741	21.63	6.15
Outstanding at March 31, 2006	97,023	\$ 18.17	4.79

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Compensation cost resulting from stock options and stock appreciation rights granted under the 1985 Plan is based on the intrinsic value of the award, recognized over the award's vesting period, and remeasured at each reporting date through the date of settlement. The total compensation cost recognized for the three months ended March 31, 2006 was \$59,330.

The 2005 Equity Incentive Compensation Plan (2005 Plan) permits the grant of stock options, restricted stock awards and other stock incentives to key employees and all non-employee directors. The 2005 Plan provides for the issuance of up to 872,639 shares of the Corporation's Common Stock, including both performance and nonperformance-based restricted stock. Performance-based restricted stock awards vest at the end of a specified three year period, with the ultimate number of awards earned contingent on achievement of certain performance targets. If performance targets are not achieved, all or a portion of the performance-based awards are forfeited and become available for future grants.

Nonperformance-based restricted stock awards vest ratably over a three year period and nonperformance-based restricted stock units (granted to non-employee directors) vest over a one year period. The Plan provides for accelerated vesting in the event of death or retirement.

Non-employee directors also may elect to defer a portion of their cash compensation, with such deferred amount to be paid by delivery of deferred stock units. Outstanding awards were granted at fair market value on grant date. The number of shares of Common Stock which remain available for future grants under the Plan at March 31, 2006 is 848,893 shares.

The Company pays dividends and dividend equivalents on outstanding awards, which are charged to net assets when paid. Dividends and dividend equivalents paid on restricted awards that are later forfeited are reclassified to compensation expense.

A summary of the status of the Corporation's awards granted as of March 31, 2006, and changes during the period then ended is presented below:

Awards	Shares/ Units	Weighted Average Grant-Date Fair Value
Balance at December 31, 2005	8,630	\$ 28.35
Granted:		