



Dear Shareholders:

Last year was a momentous one for our company in many respects. First and foremost, we generated remarkable financial results – net income of \$456 million, operating cash flow of \$305 million and a \$725 million increase in common equity. In addition, including our recently completed Gothic Energy acquisition, Chesapeake's proved reserves increased 37% to a record level of 1.7 trillion cubic feet of natural gas equivalent, a 436% reserve replacement rate.

Second, our performance in the stock market was among the country's finest - the 8th best performer on the NYSE, up 326% for the year. Since reaching a low of \$0.75 in early 1999, Chesapeake's stock price has increased over 1,500%, one of the strongest performances among all publicly traded companies during the past two years.

Third, we have successfully established Chesapeake as one of the top five pure plays in the U.S. natural gas exploration and production business. As we continue to grow our assets and improve our balance sheet, we believe Chesapeake's shareholders will enjoy another exceptional year in 2001.

Our Thoughts on the Natural Gas Business: Strategy Shift

Chesapeake's strategic shift toward natural gas as our fuel of choice in late 1997 did not occur by accident. To recall the context for this decision, we had just reported an expensive \$350 million failure in our efforts to extend Chesapeake's highly successful Deep Giddings Austin Chalk Trend from Texas into Louisiana, where we had hoped to find as much as \$5-10 billion of oil and natural gas. Realizing that we needed to adjust our business model to accept the limitations of slower future growth while lowering our risk profile, we embarked on the most ambitious corporate makeover the industry has seen during the past 10 years.

The fundamental goal in our transition was simple: we decided to acquire as many natural gas reserves as we could afford, ultimately acquiring 750 billion cubic feet of natural gas equivalent (bcfe) for \$750 million in six months. Although our acquisition pricing was considered aggressive at the time, in retrospect our purchases have proved to be great bargains.

Why Natural Gas vs. Oil?

Heavily influenced by our own experiences on the front lines searching for large new reserves of natural gas, we believed it would be almost impossible for our industry to meaningfully increase the supply of natural gas in the years ahead. We also recognized that a growing economy, stricter environmental regulations and the coming onslaught of gas-fired electrical generation

would serve as catalysts for strong natural gas demand growth and, almost certainly, higher natural gas prices.

In addition, we significantly lowered our risk profile by focusing Chesapeake's search for natural gas reserves in our own backyard of the Mid-Continent region (Oklahoma, the Texas Panhandle, and SW Kansas) and by growing through a balanced development program of both drilling and acquisitions.

The Downturn of '98

By mid-1998 we believed our strategic transformation was complete and would provide a strong base for the company to return to industry prominence. Unfortunately, we were a bit early. External factors such as the Asian financial crisis, three of the warmest winters of the 20th century and an oil production miscalculation by OPEC caused oil and natural gas prices to fall to 30-year inflation-adjusted lows by Early 1999.

It was time when the "experts" were all in agreement: oil and natural gas prices would remain low indefinitely, E&P companies were fundamentally flawed businesses (we spent too much, didn't find enough, were too small to matter, were too "old economy", etc), and worst of all - E&P management teams were alleged to have consistently destroyed value over the previous 15 years.

Unlike some of our peers who elected to sell assets (or their companies) at the bottom of this cycle, we were confident that Chesapeake's strategic repositioning had been well-executed and that a cyclical upturn in oil and natural gas prices was inevitable. The rest, as they say is history. In early 1999, investors could have acquired all of Chesapeake's common stock as the equivalent of a five-year call option on over a trillion cubic feet of natural gas for less than \$100 million. Today, the present value of our reserves is over \$3.2 billion.

California and the U.S. Energy Crunch

We believe this review of where we've been is not just important for your understanding of why Chesapeake's strategy is working, but it's also critical to understanding almost everything about the energy business today. California's electricity and natural gas shortages, high oil prices worldwide, high natural gas prices, potential electricity shortages this summer in NYC and in the Midwest, and finally, a possible replay of this in 2002 - all of these problems have their roots in the low energy prices and energy policy complacency of the past 15 years.

In a nutshell, when a country embarks on a binge of energy consumption (electricity usage is up 43% since 1985) and fails to invest enough in its energy supply and delivery infrastructures along the way, something has to give. That something is always price.

It's the Producers and their Shareholders' Turn Now

As it turns out, we and other E&P management teams have not done such a poor job of creating value during the past 15 years. It's simply that the value we created through the expensive, risky

and time-consuming search for new supplies of energy was transferred to American consumers rather than to our industry's shareholders as a result of excess supplies of oil, natural gas and electricity. The net result of this extended period of low energy prices was a 15-year boom in U.S. and worldwide growth from 1985-2000 (obviously accelerated by enormous technological advancements) that gradually eliminated the excess supply of electricity, natural gas and oil.

As we have all learned over the years, what goes around comes around and the imbalance is now in favor of energy producers. Today, we are in an environment where enormous value is being created by Chesapeake and our industry. This time, however, that value is being retained by our shareholders. Persistently high energy prices and huge value creation in the energy industry will be a fact of American life for at least the next five years.

High Energy Prices Will Be With Us for a While

Most Americans do not understand the time and money needed to make the required energy investments that can increase supply enough to lower energy prices. Simply stated, it has taken us 15 years to get into the current energy crunch and it's going to take a while to get out. This will require massive amounts of capital from investors - capital that in the past 15 years has generally been invested in everything that consumes energy and will now need to be invested in everything that produces and transports energy. Affecting such a change in investing preferences won't be easy, but we believe the market will force it to happen through the twin realizations that higher energy prices are with us for a while and that energy producers' stock prices don't reflect the intrinsic value of the assets they own.

In addition, for the energy industry to generate greater supplies, more attention will have to be paid to the cost-benefit relationship of environmental regulations. For years, our country's policies of favoring a pristine environment while demanding cheap energy have been on a collision course. A more rational approach is required. We believe that both environmentalists and policymakers will have to realize that natural gas is the only fuel that can quickly deliver much needed new supplies of energy in an environmentally friendly manner.

Natural gas has numerous natural advantages over coal, oil and renewables and we believe that it can continue to trade at a BTU premium to competing fuels. By extension, we believe that over time natural gas producers' stock prices will also be valued at much higher multiples in the market. As this summer rolls on and higher electricity and natural gas prices spread from California throughout the interconnected western U.S. and on to the Midwest and East Coast, we believe investors will increasingly appreciate how well Chesapeake is prepared for this opportunity and is positioned to profit from these trends.

Chesapeake's Primary Objective and Business Strategy

Chesapeake's primary objective is simple: we desire to be the most profitable producer of natural gas in the U.S. on a per-unit-of-production basis in order to generate the industry's highest returns to shareholders. Of the more than 200 publicly traded producers listed on U.S. stock exchanges, Chesapeake is already among the 10 most profitable by this important

measure. As we continue to grow our asset base and further improve our capital structure, we will continue advancing toward our goal of being the best in the industry at exploring for, developing, acquiring and producing onshore natural gas.

Chesapeake's strategy for achieving its goal is also straightforward: using our extensive geological and operational expertise created through having drilled or acquired over 6,700 wells during the past 12 years, our company will continue to conduct one of the most technologically sophisticated searches for onshore natural gas in the U.S. In addition, we will continue to increase our two million acre leasehold inventory, which contains more than 1,500 additional drilling opportunities. It is the backbone of our ability to create future shareholder value. Furthermore, we will continue to aggressively and economically consolidate smaller asset packages in each of our four major core operating areas, with particular emphasis on the key Mid-Continent area. The combination of these efforts should enable us to achieve Chesapeake's goal of generating industry-leading returns.

Chesapeake's Newest Exploration Project - The Georgetown in Deep Giddings

During the past three years, Chesapeake has transformed itself from a high-risk, exploration oriented operator in fractured carbonate formations into a low-risk driller and acquirer of Mid-Continent natural gas reserves. However, just because we have focused on lowering our risk profile, it would be a mistake to assume we no longer have an inventory of exciting drilling projects with the opportunity for significant production growth. In fact, Chesapeake is one of the top 10 drillers in the U.S. and has a number of high-potential drilling projects in both the Anadarko and Arkoma Basins of Oklahoma. Typically drilled to below 15,000', these deep projects in Oklahoma have the potential to find more than 10 bcfe per well.

Chesapeake's project area that is today generating more industry attention than any other is the Georgetown play in the Deep Giddings Field in Texas. Many of you may recall that the springboard for Chesapeake's phenomenal returns to shareholders during 1994-96 (when Chesapeake increased in value by 90-fold and was the best performing stock in America during that three-year period) was the company's extraordinary drilling success in its Navasota River and Independence project areas. Located in Brazos, Grimes and Washington Counties, Texas, Chesapeake's Deep Giddings wells developed over 600 bcfe of proved reserves, an amount that at today's prices would create over \$3 billion in value.

Virtually all of this gas was produced from the Austin Chalk, the uppermost of a series of four deep fractured carbonate reservoirs. The other three, the Georgetown, Edwards, and Glen Rose, were largely ignored as potential drilling targets because of the enormous productivity of the Austin Chalk. As production from the company's Chalk wells began to deplete, Chesapeake's geoscientists initiated a project to test the exciting potential of these deeper zones.

The company's first two deeper wells have demonstrated the tremendous potential of at least one of the deeper zones, the Georgetown. Both of these wells generated sufficient revenues in

just their first 30 days of production to completely pay for their drilling costs. Although they have only been producing on average for less than four months, the wells have generated 5.1 bcfe of production and total revenues of \$30 million compared to total costs of \$7 million. These are ideal wells to be drilling in today's natural gas price environment.

While the company does not expect all of its Georgetown wells to be of this same quality, we believe the combination of our 100,000 leasehold acres in the Deep Giddings area and today's \$5+ natural gas prices mandate an acceleration of our Georgetown drilling. As of this date, Chesapeake has decided to increase its Deep Giddings commitment from one to 4-5 rigs to broadly test our prospective Georgetown acreage. Based on initial results and our expertise in drilling deep horizontal wells, we are optimistic that the Georgetown, and possibly the other two deeper zones in Giddings, have the potential to make a significant contribution to the company's production and reserves in 2001 and beyond.

Looking Ahead

As we look ahead to what should be a terrific environment for Chesapeake and our shareholders, we believe it's worth repeating our conclusion from last year's letter to you: "As this decade unfolds, we believe investors will increasingly envision this 21st century as the age of natural gas. Just as great wealth was created during the 20th century in the age of oil and in the 19th century as the age of coal, we believe investors will greatly profit from embracing the tremendous potential of the natural gas industry." A year later, we still feel the same way and believe many more investors share our view.

The year 2000 was a pivotal and rewarding year for our company. In just 12 years, Chesapeake has progressed from a \$50,000 start up to one of the largest and most profitable natural gas producers in the industry. And in just the eight years since our IPO, \$100 invested in Chesapeake would today have grown to \$657, compared to \$287 if invested in the DJIA, \$263 in the NASDAQ and \$258 in the S&P 500. Although we are proud of Chesapeake's past track record of value creation, we believe the years ahead can be even more rewarding.

Best regards,

Aubrey K. McClendon

Tom L. Ward

April 12, 2001