

# Chesapeake



## Letter to Shareholders - Third Quarter 2003

### Dear Fellow Shareholders:

Our recently released 2003 third quarter results continue a steady succession of exceptional quarterly performances from Chesapeake. We are proud to report that the company once again delivered record quarterly results to its shareholders, with oil and natural gas production, proved oil and natural gas reserves, revenues, cash flow from operations and net income to common shareholders each reaching an all-time high.

Of equal importance, the building blocks for future success (undeveloped leasehold and 3-D seismic) are in place and were enhanced by additional investments made during the quarter. After spending \$42 million during the quarter to further expand our inventory of undeveloped leasehold and 3-D seismic, the company's commitment to these critical investment categories during the past two years has now reached \$200 million. As a result, Chesapeake continues to enjoy significant competitive advantages from having built an inventory of organic growth opportunities that features an undrilled prospect inventory of 2,500 locations on an undeveloped leasehold inventory of 2.5 million acres.

Many of these undrilled locations have been identified using our 12,000 square mile inventory of 3-D seismic. Our commitment to leading-edge science and to developing topnotch geological, land and engineering professionals is the key reason for Chesapeake's 95% drilling success rate. This success rate is well above the industry average, is critical to keeping our finding and development costs at attractive levels and forms the foundation for our attractive returns on invested capital.

### Operating and Financial Highlights

The following highlights demonstrate the strength of our operational and financial performance during the 2003 third quarter as compared to the 2002 third quarter:

- \* Oil and gas production reached the record level of 71.0 billion cubic feet of natural gas equivalent (bcfe), up 52%;
- \* Oil and gas proved reserves increased to a record level of 3.0 trillion cubic feet of natural gas equivalent (tcfe), up 39%;
- \* Total revenues climbed to a record \$455 million, up 131%;
- \* Operating cash flow (defined as cash flow from operating activities before changes in assets and liabilities) reached a record level of \$248 million, up 143%, and, most importantly;
- \* Net income available to common shareholders soared to a record \$82 million, up 482%.

### Continuing Production Gains Driven by Drilling Success

As mentioned above, gas equivalent production in the 2003 third quarter increased 52% year-over-year from the 2002 third quarter and grew 5.4% sequentially over the 2003 second quarter. Over the past nine quarters, Chesapeake's production has increased 81%, for an average sequential quarterly growth rate of 7% and an annualized growth rate of 30%. Chesapeake's production growth continues to compare very favorably to our industry's ongoing multi-year 2-3% annual decline rate.

The major reason for the continuing strength in the company's organic growth rate is the exceptional performance of our high potential exploratory drilling programs. We believe this success is a testament to the high caliber of Chesapeake's exploration teams and our commitment to aggressive investments in exploration science and undeveloped leasehold.

#### ***Profit Margins Expand as Unit Revenues Increase***

While Chesapeake is pleased with its record of building and maintaining one of the industry's best operating cost structures, the company believes its success in enhancing revenue per unit of production through successful commodity price risk management is one of its most important core competencies. While cost reductions are typically measured in only pennies per unit of production, revenue enhancements through value-creating commodity price risk management can add dimes, quarters, and even dollars to the company's revenues per unit of production. In fact, in the third quarter alone, realized gains from our commodity price risk hedging activities increased Chesapeake's revenue by \$0.25 per mcf, which increased our net profit margin by 16%.

These oil and natural gas risk management skills are an increasingly important point of differentiation among independent energy producers in an environment of volatile oil and natural gas prices. We believe the best performers in the oil and natural gas industry during the next few years are likely to be those companies that can prove their expertise as active "price makers" rather than as passive "price takers". Chesapeake's track record of value creation through such risk management is impressive. Since 2001, the company's revenues have been enhanced by more than \$125 million in realized gains through astute hedging decisions.

In addition, Chesapeake's unrealized gains on its future hedging positions exceed \$130 million as of October 30, 2003. Through these open positions, the company has hedged 85% and 54% respectively of its projected production for the fourth quarter of 2003 and for all of 2004 at the very attractive average NYMEX prices of \$5.56 and \$5.23 per mcf. With many natural gas analysts predicting gas prices to average \$4.00 per mcf in 2004, Chesapeake's open hedges have the potential to create \$175 million of hedging gains in 2004.

#### ***Production Forecasts Increased Again, Proved Reserves Reach Record Level***

Because of this quarter's especially strong operational performance and management's confidence in its 2004 business plan, we have once again increased the company's production forecasts, this time to 269-270 bcfe for 2003 and to 297-303 bcfe for 2004. This represents projected production growth of 11% from 2003 to 2004.

In addition, Chesapeake's estimated proved reserves as of September 30, 2003 (proforma for the recently announced south Texas acquisition of assets from Laredo Energy L.P.) reached the record level of 3.1 tcf, up 905 bcfe in 2003 to date. Reserve replacement this year has exceeded 500%.

#### ***Dividend Reinvestment Plan Instituted***

As a benefit to our shareholders, Chesapeake has recently implemented a common stock dividend

reinvestment plan. Eligibility to participate in this plan is available to any registered shareholder. Beneficial owners of Chesapeake common stock should contact their bank, broker or nominee regarding options for participating in the plan. For further details or the documents necessary to participate in the plan, please call Chesapeake's Transfer Agent, UMB Bank, N.A. at (800) 884-4225.

### Management's Outlook

We are pleased to have delivered another solid quarter of operational and financial performance and value creation for our shareholders. During the past 12 months, Chesapeake's stock price has increased more than 74%, making the company one of the top three performers among large and madcap E&P companies. We remain confident in our execution of Chesapeake's business strategy and appreciate the confidence you have placed in us as stewards of your capital.

Through our ownership of 21 million common shares, our capital is invested alongside yours. During the past 12 months we have increased our commitment to the company through open market purchases of 2.5 million common shares at a total cost of \$22 million. We remain excited about Chesapeake's potential in the years ahead to continue generating one of the best records of shareholder value creation in our industry.

Best regards,

Aubrey K. McClendon  
Chairman and Chief Executive Officer

Tom L. Ward  
President and Chief Operating Officer

October 30, 2003