CHESAPEAKE ENERGY CORP
Form 424B2
November 13, 2003
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Filed Pursuant to Rule 424(b)(2)

Registration Number 333-109657

PROSPECTUS SUPPLEMENT

(To Prospectus dated October 23, 2003)

1,500,000 Shares

Chesapeake Energy Corporation

5% Cumulative Convertible Preferred Stock

(Liquidation Preference $100 per Share)

We are offering 1,500,000 shares of 5% cumulative convertible preferred stock. The annual dividend on each share of preferred stock is $5.00 and is payable quarterly in cash, in arrears, on each February 15, May 15, August 15 and November 15, commencing February 15, 2004. Each share of preferred stock will be convertible at the holder s option at any time into 6.0962 shares of common stock (which is calculated using an initial conversion price of $16.40 per share of common stock). The conversion price will be adjusted as described herein upon the occurrence of certain change of control transactions and other events. The preferred stock is not redeemable by us at any time. On or after November 18, 2006, if the closing price of our common stock exceeds 130% of the conversion price for 20 trading days during any consecutive 30 trading day period, we may at our option cause the preferred stock to be automatically converted into shares of common stock at the then prevailing conversion price.

Our common stock is listed on the New York Stock Exchange under the symbol CHK. On November 12, 2003, the last reported sale price of our common stock was $11.93 per share.

We expect to list the common stock issuable upon conversion of the preferred stock on the NYSE.

Investing in our preferred stock involves risks. See Supplemental Risk Factors beginning on page S-10 of this prospectus supplement and Risk Factors beginning on page 2 of the accompanying prospectus.

	Per Share	Total
Public Offering Price	$ 100.00	$ 150,000,000
Underwriting Discount	$ 2.75	$ 4,125,000
Proceeds to Us (before expenses)	$ 97.25	$ 145,875,000

The underwriters have an option to purchase up to an additional 225,000 shares of preferred stock on the same terms and conditions as set forth above solely to cover over-allotments, if any.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this prospectus supplement or the prospectus to which it relates is truthful or complete. Any representation to the contrary is a criminal offense.

Delivery of the shares of preferred stock in book-entry form will be made on or about November 18, 2003.

Joint Book-Running Managers

LEHMAN BROTHERS BANC OF AMERICA SECURITIES LLC MORGAN STANLEY

BEAR, STEARNS & CO. INC.

CREDIT SUISSE FIRST BOSTON

RAYMOND JAMES

HOWARD WEIL INCORPORATED

JOHNSON RICE & COMPANY, L.L.C.

RBC CAPITAL MARKETS

November 12, 2003

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You should rely only on the information contained in or incorporated by reference in this prospectus supplement and the accompanying prospectus. We have not authorized anyone to provide you with different information. We are not making an offer of these securities in any state where the offer is not permitted. You should not assume that the information contained in or incorporated by reference in this prospectus supplement or the accompanying prospectus is accurate as of any date other than the dates of this prospectus supplement or the accompanying prospectus or that any information we have incorporated by reference is accurate as of any date other than the date of the document incorporated by reference.

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PROSPECTUS SUPPLEMENT SUMMARY

This summary highlights selected information from this prospectus supplement and the accompanying prospectus, but may not contain all information that may be important to you. This prospectus supplement and the accompanying prospectus include specific terms of this offering, information about our business and financial data. We encourage you to read this prospectus supplement, the accompanying prospectus and the documents incorporated herein and therein in their entirety before making an investment decision. Unless otherwise indicated, this prospectus supplement assumes no exercise of the underwriters over-allotment option.

Chesapeake

We are among the ten largest independent natural gas producers in the United States, owning interests in over 14,500 producing oil and gas wells. We estimate that our proved reserves were approximately 3.1 tcfe as of September 30, 2003, pro forma for the recently completed Laredo Energy acquisition that closed on October 31, 2003. Approximately 91% of our pro forma proved reserves are natural gas, and approximately 87% of our pro forma proved reserves are located in the Mid-Continent region of the United States, which includes Oklahoma, western Arkansas, southwestern Kansas and the Texas Panhandle. We have smaller operations in the onshore Upper Gulf Coast region, the South Texas area, Deep Giddings field in Texas, the Tuscaloosa Trend in Louisiana, the Permian Basin region of southeastern New Mexico and the Williston Basin of North Dakota and Montana.

On October 31, 2003, we acquired Laredo Energy, L.P. and its partners interests in certain assets in the Lobo Trend in Zapata County, Texas for approximately $200 million, which, by our internal estimates, will add approximately 108 bcfe to our estimated proved reserves and approximately 30 mmcfe to our daily production. We believe we have acquired a high-quality asset base from Laredo Energy, distinguished by proved reserves that are 100% gas and 32% proved developed and with a reserve-to-production index of approximately 10 years. We believe the acquisition of these relatively shorter-lived, less developed properties complements our base of longer-lived, more developed Mid-Continent assets and provides substantial opportunities for additional drilling and exploration activities. There is no assurance that our estimates of the acquired Laredo Energy reserves will prove correct.

We intend to use the net proceeds from this offering, together with a portion of the net proceeds from our pending private placement of senior notes described below, to repay amounts borrowed under our bank credit facility to finance the Laredo Energy acquisition. Please read Other Developments Pending Private Offering of Senior Notes and Use of Proceeds.

Our executive offices are located at 6100 North Western Avenue, Oklahoma City, Oklahoma 73118, and our telephone number is (405) 848-8000.

Business Strategy

From our inception in 1989, our business goal has been to create value for our investors by building one of the largest onshore natural gas resource bases in the United States. Since 1998, our business strategy to achieve this goal has been to integrate our aggressive and technologically advanced Mid-Continent drilling program with a Mid-Continent focused producing property consolidation program. We believe this balanced business strategy enables us to achieve greater economies of scale, increase our undrilled acreage inventory and attract and retain talented and motivated land, geoscientific and engineering personnel. We are executing our strategy by:

Consistently Making High-Quality Acquisitions. Our acquisition program is focused on small- to medium-sized acquisitions of Mid-Continent natural gas properties that provide high-quality, long-lived production and significant drilling opportunities. Since January 1, 2000, we have acquired $2.3 billion of such properties (primarily in 21 separate transactions of greater than $10 million each) at an estimated average cost of $1.24 per mcfe of proved reserves. The vast majority of these acquisitions either increased our ownership in existing wells or fields or added additional drilling locations in our core Mid-Continent operating area. We believe our recent acquisition of high-quality, shorter-lived

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assets from Laredo Energy complements our longer-lived Mid-Continent assets. In addition, we believe our expertise in drilling deep natural gas wells into challenging geological environments is well-suited to successfully developing the exploration potential of the Laredo Energy assets. Because the Mid-Continent and South Texas regions contain many small companies seeking market liquidity and larger companies seeking to divest non-core assets, we expect to find additional attractive acquisition opportunities in the future.

Consistently Growing Through the Drillbit. One of our most distinctive characteristics is our ability to increase reserves through the drillbit. We are currently conducting one of the three most active drilling programs in the United States with our program focused on finding gas in the Mid-Continent region. We currently have 43 rigs drilling on Chesapeake-operated prospects, and we are participating in approximately 40 wells being drilled by others. We believe our Mid-Continent drilling program is the most active in the region and is supported by our ownership of an extensive land and 3-D seismic base.

Consistently Focusing on the Mid-Continent. In this region, we believe we are the largest natural gas producer, the most active driller and the most active acquirer of undeveloped leases and producing properties. We believe the Mid-Continent region, which trails only the Gulf Coast and Rocky Mountain basins in U.S. gas production, has many attractive characteristics. These characteristics include long-lived natural gas properties with relatively predictable decline curves; multi-pay geological targets that decrease drilling risk, resulting in our historical Mid-Continent drilling success rate of approximately 93% over the past ten years; favorable basis differentials to benchmark commodity prices; generally lower service costs than in more competitive or more remote basins; and a favorable regulatory environment with virtually no federal land ownership. In addition, we believe the location of our headquarters in Oklahoma City provides us with many competitive advantages over other companies that direct their activities in this region from district offices in Oklahoma City or Tulsa or from out-of-state headquarters.

Consistently Focusing on Low Costs. By minimizing operating costs, we have been able to deliver consistently attractive financial returns through all phases of the commodity price cycle. We believe our general and administrative costs and our lease operating expenses are among the lowest in the industry. We believe these low costs are the result of our management s effective cost-control programs, our high-quality asset base and the extensive and competitive services, gas processing and transportation infrastructures in the Mid-Continent. We believe the recent Laredo Energy acquisition should reduce our overall operating cost structure per mcfe because our production costs per mcfe for these properties are expected to be lower than our current production costs per mcfe.

Consistently Improving our Capitalization. We have made significant progress in improving our balance sheet since the beginning of 1999. Upon completion of this offering of preferred stock, we will have increased our stockholders equity by $2.0 billion through a combination of earnings and common and preferred equity issuances. As of December 31, 1999, our debt to total capitalization ratio was 129%. As of September 30, 2003, after giving pro forma effect to this offering and our pending private placement of senior notes and the application of the net proceeds herefrom and therefrom, and assuming our pending tender offer for our 8.5% Senior Notes due 2012 described below is fully subscribed, this ratio would have been 55%. We plan to continue making the reduction of the debt to total capitalization ratio one of our primary financial goals.

Based on our view that natural gas has become the fuel of choice to meet growing power demand and increasing environmental concerns in the United States, we believe our Mid-Continent focused natural gas development strategy should provide substantial growth opportunities in the years ahead. Although U.S. gas production has been declining during the past nine quarters, we have increased our production in each of those quarters. Our goal is to increase our overall production by 10% to 15% per year, with approximately one-third of this growth projected to be generated organically through the drillbit and the remainder from acquisitions.

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Company Strengths

We believe the following six characteristics distinguish our past performance and future growth potential from other natural gas producers:

High-Quality Asset Base. Our producing properties are characterized by long-lived reserves, established production profiles and an emphasis on natural gas. Based upon current production and reserve levels (and pro forma for the Laredo Energy acquisition), our proved reserves-to-production ratio, or reserve life, is approximately 11.5 years. In each of our operating areas, our properties are concentrated in locations that enable us to establish substantial economies of scale in drilling and production operations and facilitate the application of more effective reservoir management practices. We intend to continue building our Mid-Continent asset base by concentrating both our drilling and acquisition efforts in this region.

Low-Cost Producer. Our high-quality asset base has enabled us to achieve a low operating cost structure. During the first three quarters of 2003, our cash operating costs per unit of production were $0.90 per mcfe, which consisted of general and administrative expenses of $0.09 per mcfe, production expenses of $0.52 per mcfe and production taxes of $0.29 per mcfe. We believe this is one of the lowest operating cost structures among publicly traded independent oil and natural gas producers. We believe the Laredo Energy acquisition should further lower our per unit cash operating costs because we project the Laredo Energy properties will have initial production expenses of approximately $0.10 per mcfe. We currently operate approximately 79% of our proved reserves. This large percentage of operational control provides us with a high degree of operating flexibility and cost control.

Successful Acquisition Program. Our experienced asset acquisition team focuses on adding to our attractive resource base in the Mid-Continent region and occasionally looks to supplement our Mid-Continent base by evaluating acquisition opportunities in the onshore Gulf Coast, South Texas and Permian Basin regions. These areas are characterized by medium- to long-lived natural gas reserves, low lifting costs, multiple geological targets that provide substantial drilling potential, favorable basis differentials to benchmark commodity prices, a well-developed oil and gas transportation infrastructure and considerable potential for further consolidation of assets. Since 1998 and including the Laredo Energy acquisition, we have completed $3.1 billion in acquisitions at an average cost of $1.14 per mcfe of proved reserves. We believe we are well-positioned to continue this consolidation as a result of our large existing asset base, our corporate presence in Oklahoma, our knowledge and expertise in the regions in which we operate and current trends in the industry.

Large Inventory of Drilling Projects. During the past 14 years, we believe we have been one of the ten most active drillers in the United States and the most active driller in the Mid-Continent. We believe we have developed a particular expertise in drilling deep vertical and horizontal wells in search of large natural gas accumulations in challenging reservoir conditions. We actively pursue deep drilling targets because of our view that most undiscovered gas reserves in the Mid-Continent will be found at depths below 12,500 feet. In addition, we believe that our large 3-D seismic inventory, much of which is proprietary to Chesapeake, provides us with an advantage over our competitors, which largely prefer to drill shallower development wells. As a result of our aggressive land acquisition strategies and Oklahoma s favorable forced-pooling regulations, we have been able to accumulate an onshore leasehold position of approximately 2.3 million net acres. In addition, our technical teams have identified over 2,500 exploratory and developmental drillsites, representing approximately five years of future drilling opportunities at our current rate of drilling. The Laredo Energy acquisition added to our existing land inventory and we have identified approximately 70 additional potential drillsites associated with the properties acquired in this transaction.

Hedging Program. We have historically used and intend to continue using hedging programs to reduce the risks inherent in producing oil and natural gas, commodities that are extremely volatile in price.

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We believe this volatility is likely to continue and may even increase in the years ahead. We believe that a producer can use this volatility to its benefit by taking advantage of prices when they exceed historical norms. Over the past three years, we have increased our oil and gas revenues by $127 million of realized gains through hedging. We currently have gas swaps hedging 55, 144, 46, 26 and 26 bcf for the fourth quarter of 2003 and for all of 2004, 2005, 2006 and 2007 at average NYMEX prices of $5.64, $5.25, $4.82, $4.74 and $4.76 per mcf, respectively. In addition, we have 100% of our projected oil production hedged for the fourth quarter of 2003 and 94% for all of 2004 at average NYMEX prices of $28.69 and $28.61 per barrel of oil, respectively.

Entrepreneurial Management. Our management team formed Chesapeake in 1989 with an initial capitalization of $50,000. Through the following years, this management team has guided our company through operational challenges and extremes of oil and gas prices to create one of the ten largest independent natural gas producers in the United States with an enterprise value of approximately $5.4 billion (pro forma for this offering and our pending private placement of senior notes). Our co-founders, Aubrey K. McClendon and Tom L. Ward, have been business partners in the oil and gas industry for 20 years and beneficially own, as of September 30, 2003, approximately 14.3 million and 15.8 million of our common shares, respectively. Each of Messrs. McClendon and Ward has indicated his desire to purchase $5 million of preferred stock in this offering at the price offered to the public.

Other Developments

We recently announced a series of transactions intended to improve our capitalization.

Pending Private Offering of Senior Notes. On November 12, 2003, we priced a private placement of $200 million of 6.875% Senior Notes due 2016. The senior notes are being offered only to qualified institutional buyers under Rule 144A under the Securities Act of 1933 and to non-U.S. persons in offshore transactions pursuant to Regulation S under the Securities Act. Net proceeds are expected to be used to fund the tender offer for our 8.5% Senior Notes due 2012 described below and to repay borrowings under our bank credit facility incurred primarily to finance the Laredo Energy acquisition. There is no assurance that the private offering will be completed or, if completed, completed for the amount contemplated. The closing of this offering is not conditioned on the closing of the senior notes offering.

Tender Offer for 8.5% Senior Notes due 2012. On November 12, 2003, we launched a cash tender offer for all of the approximately $111 million outstanding principal amount of our 8.5% Senior Notes due 2012. The tender offer is conditioned upon the closing of the private placement of senior notes described above and the receipt of consents to remove substantially all of the restrictive covenants on the 8.5% Senior Notes from holders of a majority of the outstanding principal amount of the notes. If fully subscribed, it is expected the tender offer will cost approximately $118 million, which would be funded with a portion of the net proceeds from the private placement of senior notes described above. There is no assurance that the tender offer, which is expected to be completed on December 10, 2003, will be subscribed for any amount.

Possible Exchange Offer for 8.125% Senior Notes due 2011. On November 11, 2003, we announced that we are considering making a private exchange offer to certain eligible holders for up to $500 million aggregate principal amount of our 8.125% Senior Notes due 2011. There is currently approximately $728 million in principal amount of our 8.125% Senior Notes due 2011 outstanding. The offer, if made, will be to exchange our 8.125% Senior Notes due 2011 for notes of one or more series of our senior notes with a final maturity date after 2011, including additional notes of an existing series of our senior notes or additional notes of the new series of senior notes to be offered in our pending private placement. There is no assurance that the exchange offer, if commenced, will be subscribed for any amount.

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The Offering

Securities Offered	1,500,000 shares of 5% cumulative convertible preferred stock; 1,725,000 shares if the underwriters exercise their option in full.
Dividends	Cumulative annual dividends of $5.00 per share payable quarterly in cash on each February 15, May 15, August 15 and November 15, commencing February 15, 2004, when, as and if declared by the board of directors. Dividends will be paid in arrears on the basis of a 360-day year consisting of twelve 30-day months. Dividends on the preferred stock will accumulate and be cumulative from the date of issuance thereof. Accumulated dividends on the preferred stock will not bear interest.
Liquidation Preference	$100 per share, plus accumulated and unpaid dividends.
Ranking	The preferred stock will rank with respect to dividend rights and rights upon our liquidation, winding-up or dissolution:

- senior to all of our common stock and to all of our other capital stock issued in the future unless the terms of that stock expressly provide that it ranks senior to, or on a parity with, the preferred stock;
- on a parity with our existing 6.75% Cumulative Convertible Preferred Stock, our existing 6.00% Cumulative Convertible Preferred Stock and with any of our capital stock issued in the future the terms of which expressly provide that it will rank on a parity with the preferred stock; and
- junior to all of our capital stock issued in the future the terms of which expressly provide that such stock will rank senior to the preferred stock.

We currently have 2,998,000 shares of 6.75% Cumulative Convertible Preferred Stock issued and outstanding, with an aggregate liquidation preference of $149.9 million, and 4,600,000 shares of 6.00% Cumulative Convertible Preferred Stock issued and outstanding, with an aggregate liquidation preference of $230.0 million.

Redemption	Shares of the preferred stock will not be redeemable by us.
Conversion Rights	Each share of the preferred stock may be converted at any time, at the option of the holder, into 6.0962 shares of common stock (which is calculated using an initial conversion price of $16.40 per share of common stock) plus cash in lieu of fractional shares. The conversion price is subject to adjustment upon the occurrence of certain events.
Mandatory Conversion	On or after November 18, 2006, we may, at our option, cause the preferred stock to be automatically converted into that number of shares of common stock that are issuable at the then prevailing conversion price. We may exercise our conversion right only if, for 20 trading days within any period of 30 consecutive trading days (including the last trading day of such

period), the closing price of our

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common stock exceeds 130% of the then prevailing conversion price of the preferred stock.

Change of Control	Except as provided below, upon a change of control, each holder of the preferred stock shall, in the event that the market value of our common stock at such time is less than the conversion price, have a one-time option to convert all of its shares of the preferred stock into shares of common stock at an adjusted conversion price equal to the greater of (x) the market value of the common stock (determined as described herein) and (y) $7.9533, which is approximately 66 $^{2}/3$% of the recent common stock price set forth on the cover of this prospectus supplement.

In lieu of issuing the shares of common stock issuable upon conversion in the event of a change of control, we may, at our option, make a cash payment equal to the market value of such common stock otherwise issuable as of the change of control date.

Notwithstanding the foregoing, upon a change of control in which (1) each holder of our common stock receives consideration consisting solely of common stock of the successor, acquiror or other third party that is listed on a national securities exchange or quoted on the NASDAQ National Market and (2) all our common stock has been exchanged for, converted into or acquired for common stock of the successor, acquiror or other third party and the preferred stock becomes convertible solely into such common stock, the conversion price will not be adjusted as described above.

Voting Rights	Except as required by Oklahoma law and our certificate of incorporation, which will include the certificate of designation for the preferred stock, the holders of preferred stock will have no voting rights unless dividends payable on the preferred stock are in arrears for six or more quarterly periods. In that event, the holders of the preferred stock, voting as a single class with the shares of any other preferred stock or preference securities having similar voting rights (including the existing preferred stock), will be entitled at the next regular or special meeting of our stockholders to elect two directors and the number of directors that comprise our board will be increased by the number of directors so elected. These voting rights and the terms of the directors so elected will continue until such time as the dividend arrearage on the preferred stock has been paid in full. The affirmative consent of holders of at least 66 $^{2}/3$% of the outstanding preferred stock will be required for the issuance of any class or series of stock (or security convertible into stock) ranking senior to the preferred stock as to dividend rights or rights upon our liquidation, winding-up or dissolution and for amendments to our certificate of incorporation that would affect adversely the rights of holders of the preferred stock.

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Use of Proceeds	The net proceeds to us from the sale of the preferred stock offered hereby are estimated to be $145.6 million, after deducting discounts to the underwriters and the estimated expenses of the offering. We intend to use the net proceeds from this offering, together with a portion of the net proceeds from the pending private placement of senior notes, to repay borrowings under our bank credit facility incurred primarily to finance the recent Laredo Energy acquisition. Please read Use of Proceeds.
Tax Consequences	The U.S. Federal income tax consequences of purchasing, owning and disposing of the preferred stock and any common stock received upon its conversion are described in Federal Income Tax Considerations. Prospective investors are urged to consult their own tax advisors regarding the tax consequences of purchasing, owning and disposing of the preferred stock and any common stock received upon its conversion in light of their personal investment circumstances, including consequences resulting from the possibility that actual or constructive distributions on the preferred stock may exceed our current and accumulated earnings and profits, as calculated for U.S. Federal income tax purposes, in which case they would not be treated as dividends for U.S. Federal income tax purposes.
Book-Entry, Delivery and Form	Initially, the preferred stock will be represented by one or more permanent global certificates in definitive, fully registered form deposited with a custodian for, and registered in the name of, a nominee of DTC.
Common Stock	Our common stock is listed for trading on the NYSE under the symbol CHK.

Risk Factors

You should carefully consider all information in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein. In particular, you should evaluate the specific risk factors set forth in the section entitled Supplemental Risk Factors in this prospectus supplement and the section entitled Risk Factors in the accompanying prospectus for a discussion of risks relating to an investment in our preferred stock.

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Summary Consolidated Financial Data

The following tables set forth summary consolidated financial data as of and for each of the three years ended December 31, 2000, 2001 and 2002 and the nine months ended September 30, 2002 and 2003. These data were derived from our audited consolidated financial statements included in our annual report on Form 10-K/A for the year ended December 31, 2002, which is incorporated by reference herein, and from our unaudited consolidated financial statements included in our quarterly report on Form 10-Q for the nine months ended September 30, 2003, which is incorporated by reference herein. The financial data below should be read together with, and are qualified in their entirety by reference to, our historical consolidated financial statements and the accompanying notes and the Management s Discussion and Analysis of Financial Condition and Results of Operations which are set forth in our annual report on Form 10-K/A and in our quarterly report on Form 10-Q, which are incorporated by reference herein.

	Years Ended December 31,			Nine Months Ended September 30,	
	2000	**2001**	**2002**	**2002**	**2003**
				(unaudited)	
	(in thousands, except ratios and per share data)				
Statement of Operations Data:					
Revenues:					
Oil and gas sales	$ 470,170	$ 820,318	$ 568,187	$ 367,810	$ 951,125
Oil and gas marketing sales	157,782	148,733	170,315	112,334	309,566
Total revenues	627,952	969,051	738,502	480,144	1,260,691
Operating costs:					
Production expenses	50,085	75,374	98,191	71,252	101,664
Production taxes	24,840	33,010	30,101	19,934	57,336
General and administrative	13,177	14,449	17,618	11,930	17,254
Oil and gas marketing expenses	152,309	144,373	165,736	108,836	302,064
Oil and gas depreciation, depletion and amortization	101,291	172,902	221,189	157,731	266,131
Depreciation and amortization of other assets	7,481	8,663	14,009	10,489	12,647
Total operating costs	349,183	448,771	546,844	380,172	757,096
Income from operations	278,769	520,280	191,658	99,972	503,595
Other income (expense):					
Interest and other income	3,649	2,877	7,340	7,343	1,356
Interest expense	(86,256)	(98,321)	(112,031)	(77,779)	(115,891)
Loss on investment in Seven Seas			(17,201)	(4,770)	
Impairment of investment in securities		(10,079)			
Loss on repurchases of Chesapeake debt		(76,667)	(2,626)	(1,353)	
Gain on sale of Canadian subsidiary		27,000			
Gothic standby credit facility costs		(3,392)			
Total other income (expense)	(82,607)	(158,582)	(124,518)	(76,559)	(114,535)
Income before income taxes and cumulative effect of accounting change	196,162	361,698	67,140	23,413	389,060
Provision (benefit) for income taxes	(259,408)	144,292			