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CHKR - Q4 2012 Chesapeake Granite Wash Trust Earnings Conference Call

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## CORPORATE PARTICIPANTS

**Nick Dell'Osso** *Chesapeake Granite Wash Trust - EVP and CFO*

**Steve Dixon** *Chesapeake Granite Wash Trust - EVP and COO*

## CONFERENCE CALL PARTICIPANTS

**Justin Albert** *Raymond James & Associates - Analyst*

**Minyoung Sohn** *Arrowpoint Partners - Analyst*

## PRESENTATION

### Operator

Good day, and welcome to the Chesapeake Granite Wash Trust 2012 fourth-quarter results conference call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Mr. Nick Dell'Osso. Please go ahead, sir.

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### **Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

Good morning, and welcome to the Chesapeake Granite Wash Trust distribution conference call. This is Nick Dell'Osso, Executive Vice President and Chief Financial Officer of Chesapeake Energy. Also joining me for the call this morning is Steve Dixon, Executive Vice President and Chief Operating Officer of Chesapeake. And via teleconference is Sarah Newell, Vice President of Bank of New York, Mellon Trust Company, the trustee for Chesapeake Granite Wash Trust.

I have a few prepared remarks, and then we will take any questions you may have. Please note that today's call will contain certain forward-looking statements and assumptions that are subject to inherent risks and uncertainties. The actual results may differ materially from those projected in the forward-looking statements. Additional information about risk factors and other factors that could potentially affect the Trust and its financial results are included in the Trust press release issued last Friday, and in the Trust filings with the SEC.

As a reminder, CHKR is a statutory trust, which is required to distribute all cash flow after expenses. The Trust has no employees or officers, and Chesapeake Energy, as the sponsor of the Trust, is responsible for operating the properties in which the Trust has an interest, and fulfilling certain drilling commitments, which is also detailed in the Trust filings with the SEC.

As stated in the press release on Friday, the distribution for the three-month period ended November 30, 2012 from CHKR will be \$0.67 per common unit and approximately \$0.38 per subordinated unit. Worth noting, Chesapeake Energy owns 100% of the subordinated units. The distribution will be paid on March 1, 2013 to unitholders of record at the close of business on February 19, 2013.

The calculated distribution for the period is approximately \$0.60 per unit. However, since this is below the predetermined subordination threshold for the quarter, of \$0.67 per unit, the distribution per subordinated unit will be reduced in order to make a distribution of \$0.67 per common unit.

Now I'll turn it over to Steve Dixon.

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### **Steve Dixon** - *Chesapeake Granite Wash Trust - EVP and COO*

Thanks, Nick. For the three-month period of September 1 through November 30 of 2012, total sales volumes attributed to the Trust royalty interest were 151,000 barrels of oil. That's up from 146,000 or 3% quarter-over-quarter increase.



329,000 barrels of natural gas liquids, that's up from 288,000, or that's a 14% quarter-over-quarter increase; and 3.06 billion cubic feet of natural gas, and that's down from 3.204 billion cubic feet, a 4% quarter-over-quarter decrease. This is for total sales of approximately 990,000 barrels equivalent, or BOE, and that's up from 968,000 or about 2% quarter-over-quarter.

The production mix in the fourth quarter was 15% oil, 33% NGLs, and 52% natural gas. Realized prices for the period were \$86.26 per barrel for oil, \$31.92 per barrel for natural gas liquids, and \$1.94 per MCF for natural gas. These prices include the effects of transportation and third-party deductions. When comparing quarter-over-quarter changes in realized price for 2012 fourth-quarter, unhedged realized oil prices were higher by \$2.04 per barrel. Natural gas liquids prices were higher by \$4.43 per barrel, and natural gas prices were higher by \$0.22 per Mcf.

Turning to hedges, the actual NYMEX oil prices were above swap contract prices held by the Trust. This resulted in a realized loss on oil contracts of approximately \$609,000 for the period. These fixed oil swap contracts were initially established to hedge approximately 50% of the projected oil and natural gas liquids volumes.

The use of crude oil derivatives to partially mitigate the price risk of NGL production is subject to basis risk to the extent oil and NGL prices are not highly correlated. The initial forecasted revenue of the Trust assumed an NGL price of 49% of WTI. Actual results were lower at 37%. The Trust has no natural gas hedges in place.

Turning to drilling results and the Trust AMI, during the quarter, Chesapeake brought online 9 gross operated wells. These 9 gross wells equated to approximately 9 development wells towards Chesapeake's overall commitment of 118 development wells under the development agreement with the Trust. Through January, Chesapeake has now drilled 58 equivalent wells, and is ahead of schedule in meeting this 118 development well commitment to the Trust. Chesapeake is currently operating 4 rigs in the Trust AMI, and this level of drilling is consistent with the original drilling plans outlined in the Trust SEC filings.

We will now take any questions you may have. Operator, please open up the line for Q&A.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Justin Albert, Raymond James.

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**Justin Albert** - *Raymond James & Associates - Analyst*

Quick question -- I hopped on the call a little late. Did you guys -- was production affected by any ethane rejection this quarter?

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**Steve Dixon** - *Chesapeake Granite Wash Trust - EVP and COO*

Will you follow-up with our IR Department? We'll look and see, particularly, if the wells in this well set would have had any rejection. I'm not sure. I know we had some in the general area, but I can't tell you specifically on this well set.

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**Justin Albert** - *Raymond James & Associates - Analyst*

Okay. Okay. And then regarding the nine wells that you guys brought online, was that pace relatively even throughout the quarter? Or was it lumpy towards the latter half or the beginning?



**Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

Well, I think it was pretty lumpy towards the end, yes (multiple speakers) --.

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**Steve Dixon** - *Chesapeake Granite Wash Trust - EVP and COO*

(multiple speakers) Yes, it was --

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**Justin Albert** - *Raymond James & Associates - Analyst*

(multiple speakers) -- towards the end?

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**Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

Yes, it was towards the end.

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**Justin Albert** - *Raymond James & Associates - Analyst*

All right. That's all I have. Thanks, guys.

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**Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

Okay, great.

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**Operator**

Minyoung Sohn, Arrowpoint Partners.

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**Minyoung Sohn** - *Arrowpoint Partners - Analyst*

Just a follow-up on the 9 development wells drilled in the period. I know you said that it was lumpy. Could you give us some sense for how these wells came on, in terms of initial production for maybe a 30-day rate with regard to oil, NGL and natural gas?

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**Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

I don't even have IPs -- don't have VIPs with us here this morning. But we did look at a table with the IPs last week, so I'll answer it a bit generically, in that we did have a number -- we had some variability, for sure, in the IP rates. And we had some -- couple of pretty good wells and a few that were a little below pro forma.

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**Minyoung Sohn** - *Arrowpoint Partners - Analyst*

Of the 151,000 barrels of oil on average daily production, can you give me a sense for how many of these were from the initial producing wells conveyed into the Trust, as opposed to those coming from the development wells?

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**Steve Dixon** - Chesapeake Granite Wash Trust - EVP and COO

No, sir, I don't have that data here.

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**Nick Dell'Osso** - Chesapeake Granite Wash Trust - EVP and CFO

We don't break it out that way and haven't previously.

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**Minyoung Sohn** - Arrowpoint Partners - Analyst

Might there be a way for you to be able to provide investors with broader transparency regarding these wells? Again, I find it very difficult to try to analyze the cash flows of the Trust without having a greater sense for the well productivity that's being put into it.

And then, lastly, if I could, just on natural gas. Can you give me a sense for how your gases being priced? Ought we be using front-month prices, and then taking month averages and looking at deductions? The thing that I've noticed is that the differential, in terms of your realized price versus the, call it, the averages in the period, seem to have widened by about \$0.45 in this trust period.

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**Nick Dell'Osso** - Chesapeake Granite Wash Trust - EVP and CFO

The methodology for determining realized price for this -- or for the realized price of these wells received hasn't changed. It is, as you describe, where it's a forward price for that month and then deducts for transportation and for processing charges.

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**Minyoung Sohn** - Arrowpoint Partners - Analyst

Okay, thank you.

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**Nick Dell'Osso** - Chesapeake Granite Wash Trust - EVP and CFO

We will look into giving a better sense for the breakout of new well production versus legacy production on the next call.

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**Minyoung Sohn** - Arrowpoint Partners - Analyst

Yes, that'd be very helpful. I know that things, obviously, change, but I thought that there was a tremendous amount of detail provided in the registration statements and all the amendments that were filed later. And then, from there, I obviously have to make assumptions regarding production rates and decline, but what I've sensed is just kind of a growing disparity from trends that I would have otherwise thought would have been reasonable four to six quarters ago.

I just think it's critical information for an investor to be able to have to assess whether or not this is a worthwhile investment going forward. Thank you.

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**Nick Dell'Osso** - Chesapeake Granite Wash Trust - EVP and CFO

Very good.

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**Operator**

(Operator Instructions).

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**Nick Dell'Osso** - *Chesapeake Granite Wash Trust - EVP and CFO*

Okay. Thank you all very much for dialing in and your time.

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**Operator**

Thank you. That concludes today's conference call. Thank you for your participation.

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