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CHKR - Q1 2013 Chesapeake Granite Wash Trust Earnings Conference Call

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CORPORATE PARTICIPANTS

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Steve Dixon *Chesapeake Granite Wash Trust - Acting CEO*

CONFERENCE CALL PARTICIPANTS

Justin Albert *Raymond James & Associates - Analyst*

Aaron Terry *Kayne Anderson Rudnick Investment Mgmt. - Analyst*

PRESENTATION

Operator

Good day everyone, and welcome to the Chesapeake Granite Wash Trust first quarter 2013 earnings results. 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.

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP, 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, acting Chief Executive Officer of Chesapeake, and via teleconference is Sarah Newell, Vice President of Bank of New York Mellon Trust Company, the Trustee for Granite Wash Trust. We 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 this morning, and in the trust filings with the SEC.

As a reminder CHKR is 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's filings with the SEC.

As stated in the press release this morning, the distribution for the three-month period ended February 28, 2013 from CHKR will be \$0.69 per common unit, and approximately \$0.30 per subordinated units. Worth noting Chesapeake Energy owns 100% of the subordinated units. The distribution will be paid on May 31st, 2013 to unitholders of record at the close of business on May 21st, 2013. The calculated distribution for this period is approximately \$0.59 per unit. However, since this is below the pre-determined subordination threshold for the quarter of \$0.69 per unit, the distribution per subordinated unit will be reduced in order to make a distribution of \$0.69 per common unit.

I will now turn the call over to Steve Dixon.

Steve Dixon - *Chesapeake Granite Wash Trust - Acting CEO*

Thanks Nick. For the three-month period of December 1st through February 28, 2013 total sales volume attributed to Trust royalty interests were 149,000 barrels of oil, a 2% sequential decrease. 312,000 barrels of natural gas liquids, a 5% sequential decrease. And 2.886 billion cubic feet of natural gas, a 6% sequential decrease. Total sales of approximately 942,000 barrels of oil equivalent, BOE were down 5% sequentially.



Production mix in first quarter of 2013 was 16% oil, 33% NGLs, and 51% natural gas. As development drilling continues, and as well performance is further analyzed, we are gaining additional knowledge about the Granite Wash Reservoir. For instance, we have learned that the reservoir permeability and sands body continuity within the Granite Wash AMI is higher than expected. This has resulted in lower than predicted reservoir pressure in some recent infill well locations. This has resulted in lower IP rates and lower recoverable reserves in some newer wells, as well as downward reserve revisions on some previously drilled wells. We are adjusting development plans in locations accordingly to maximize the value of this asset.

Realized prices for the period were \$88.08 per barrel of oil, \$32.67 per barrel of natural gas liquids, and \$2.28 per Mcf of natural gas. These prices include the effects of transportation and third-party deducts. For the quarter unhedged realized oil prices were higher by \$1.81 per barrel, natural gas liquid prices were higher by \$0.75 per barrel, and natural gas prices were higher by \$0.34 per Mcf when compared to the previous quarter.

On March 15th CHKR filed a 10-K with the SEC providing updated year-end 2012 reserve data. Total proved reserves as of December 31st, 2012 were 28.2 million BOE. During 2012 the Trust recorded downward reserve revisions of 11.5 million BOE, including 1.1 million BOE of downward revisions resulting from lower natural gas prices, and 10.4 million BOE of downward revisions resulting from changes to previous estimates. The changes to previous estimates were primarily as a result of higher than expected pressure depletion within certain areas of the Granite Wash AMI. To mitigate this issue we are evaluating the benefits of drilling only three wells per section rather than four wells. Preliminary results while early have been encouraging.

As noted in the 10-Q filed yesterday, the Trust evaluates the quarterly carrying value of the investment and Trust interest under the full cost accounting method prescribed by the SEC. This quarterly review is referred to as the ceiling test. Under the ceiling test the carrying value of the investment and royalty interest may not exceed an amount equal to the sum of the present value, using a 10% discount rate of the estimated future net revenues from the proved reserves. During the first quarter ceiling test evaluation, the carrying value of the investment in royalty interest exceeded its discounted present value of estimated future net revenues, resulting in a \$32.9 million impairment. This impairment is a noncash charge to Trust Corpus, and was no effect on distributed income or taxable income.

Turning to hedges actual NYMEX oil prices were above swap contract prices held by the Trust, resulting in a realized loss on all contracts of approximately \$1 million for the period. These fixed oil swap contracts were initially established to hedge approximately 50% of projected oil and natural gas liquids volumes. The use 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 revenues of the Trust assumed an NGL price of 49% of WTI. Actual NGL prices during the quarter were lower at 37% of WTI. The Trust has no natural gas hedges in place.

Turning to the drilling results and the Trust AMI during the quarter Chesapeake brought online seven gross operated wells, by running four rigs in the Trust AMI. Through April Chesapeake has completed approximately 65 development wells, as calculated under the development agreement, and is ahead of schedule to meet its 118 development well commitment to the Trust by June 30th, 2016.

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

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). And we will go first to Justin Albert with Raymond James.

Justin Albert - Raymond James & Associates - Analyst

In light of the three wells per section versus the typical four wells per section, in your estimation guys, how many locations do you believe you have remaining in the AMI?



Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

We have plenty of locations to meet our commitment. I believe we have 53 wells yet to drill. We have plenty of remaining locations.

Justin Albert - Raymond James & Associates - Analyst

Alright. Perfect. And then just a follow-on to the negative PUD revision in your reserve report. Do you guys have an updated type curve, you mentioned the IPs are lower. Do you have any numbers for that?

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

Well, we are hoping by increasing our spacing that we don't have near the influence, and so that our PUDs going forward will not be as influenced, so we are studying that hard, and again, trying to maximize what we get out of the Trust AML.

Justin Albert - Raymond James & Associates - Analyst

Alright. Great Thanks.

Operator

And we will take our next question from Aaron Terry with Kayne Anderson.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

Good morning, guys. I just wanted to follow up on Justin's questions. Can you at least give what the PUD bookings were, the AURs on the PUD bookings on the 2012 reserve port?

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

I don't know the average PUD bookings, No, sir.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

And then as far as talking through the three wells per section, if you are stating you have around 50 to 56 wells remaining, do you plan on three wells per section, or can you kind of give the development concept for what you guys have planned for those?

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

We are studying that hard and it kind of depends on how good the first wells were, and how inter-connected we think it is across that section. So I don't know that all wells will be three. Some could probably still handle four.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

Okay. And I am sorry, I actually didn't get the number that you stated, as far as wells that you brought online during the quarter, and I don't think it was in the press release. What was that number again?



Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

Seven.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

Seven wells during the quarter. Is that a pretty fair assessment for what you would expect to be the run-rate for the number of wells to come online in the future?

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

Yes, sir. I think seven to eight. Good run-rate.

Nick Dell'Osso - Chesapeake Granite Wash Trust - EVP, CFO

It has been lumpy at times due to completion activity, but that has been not abnormal to be right in that range.

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

That is the pace I believe that was in the original prospectus also.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

Okay. And so you haven't seen any wells flow yet on the three wells per section, or have you seen any expectations, is there any color you can guide, as far as how you would expect that to change the original IP rates? Are you just expecting that should be closer to what the original type curve was?

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

We have seen some with some positive results. Again, when you have three versus four, you have just got a lot less straws in that same reservoir, so you will have less pressure draw-down and interference effect.

Aaron Terry - Kayne Anderson Rudnick Investment Mgmt. - Analyst

Alright thanks, guys. That is all I have.

Operator

(Operator Instructions).

Steve Dixon - Chesapeake Granite Wash Trust - Acting CEO

No further questions? Okay. Thank you everyone.



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

Appreciate your time this morning. Thank you.

Operator

Again that does conclude today's presentation. We thank you for your participation.

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