

The Power Within

Southwestern Energy Company 2003 Annual Report

$\frac{R^2}{A} \rightarrow V^+$


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The Right People doing the Right Things, wisely investing the cash flow from the underlying Assets will create Value +.

Southwestern Energy Company is an integrated energy company primarily focused on natural gas. Southwestern is engaged in natural gas and crude oil exploration and production activities in Arkansas, Oklahoma, Texas, New Mexico and Louisiana. The company's low risk development drilling activities in the Arkoma Basin and in East Texas are complemented by exploration efforts in the Permian Basin and onshore Gulf Coast. Southwestern is also involved in natural gas gathering, transmission, distribution, and marketing.

2003 Highlights

- A record year:
 - Net income
 - EBITDA
 - Production
 - Reserves
 - Reserve replacement
- Successful follow-on equity offering
- Significantly improved balance sheet
- \$4.1 million annual rate increase for utility
- Significant increase in market capitalization



Dear Shareholders, 2003 was an exceptional year for Southwestern Energy, its employees and its shareholders. We set records for production volumes delivered of 41.2 Bcfe, reserve replacement of 351%, total reserves of 503 Bcfe, and net income of \$48.9 million. In addition, we reduced our debt-to-capitalization ratio from 66% at year-end 2002 to 45% at year-end 2003. And, again in 2003, we did it “organically,” meaning that we internally generated the ideas into which we invested our cash flow — drilling wells to find new oil and gas reserves.

As always, we come back to the formula that we first stated in 1999 to define our purpose as a company: $\frac{FCF}{A} \rightarrow V^+$ — *The Right People doing the Right Things, wisely investing the cash flow from the underlying Assets will create Value +*. What are the elements of our equation? First, we have a team of intrinsically motivated people with expertise and experience in the areas in which we operate. Secondly, we have focused our investing into areas that have geological opportunities with the potential to yield significant returns. Thirdly, we have substantial discretionary cash flow as a result of our low cost structure to allow us the opportunity to grow. Fourthly, and I believe most importantly, we have the internal discipline that we have called “Wisely Investing” — to focus our decision making on Present Value Created Per Dollar Invested (PVI), thereby assuring we add value for our shareholders. The remaining ingredient is to assure that we maintain an environment in our company that fosters the generation of ideas — we know that oil and gas is first found in people’s minds.

2003 was a year of acceleration for Southwestern Energy as we moved forward with our drilling program. Foremost was our infill drilling activity at the Overton Field in East Texas. As a result of raising \$103 million of equity in February of 2003, we were able to accelerate the pace of drilling in Overton by drilling 57 wells there, up from 18 wells in 2002. Overton production continued to climb throughout the year and ended 2003 at 60 MMcfe per day. In addition, we continued to have an active year in the Arkoma Basin in Arkansas and Oklahoma with the drilling of 55 wells and an aggressive workover program. During the year, we also obtained approval from the state of Arkansas to increase the drilling density from one well per 640 acres to one well per 80 acres in our Ranger Anticline area in the southern part of the Arkoma Basin resulting in the drilling of 12 wells there.

The Overton and Ranger projects are excellent proxies for our formula at Southwestern Energy. A frequently asked question by investors is — “What will the next catalyst be for your stock?” We were asked that question throughout the period of 2000 to 2002, during a time when we were continuing to talk about our projects at Overton and Ranger. Were these projects recognized as catalysts during that time? Likely not, but they certainly were. I have found that this business requires constant and continuous effort on projects to make them work — it is not often that a large wildcat falls successfully into one’s hands.

This year’s theme to our Annual Report relates to the catalyst question. There are many ways to view the scene on the cover. One is, “What a beautiful picture.” Another would be, “What a peaceful scene.” But, visualize with me the activity that may be going on in the bowels of that beautiful mountain. Much as magma bubbles through cracks and fissures beneath the mountain scene seeking to take the mountain to new heights, the teams of Southwestern Energy are working tirelessly to bring forth the next catalysts to take the Company to new heights.

So, as we look forward to 2004 what will the year bring? We will again be very active in drilling in East Texas and the Arkoma Basin, moderately active in the Permian Basin and we will be less active in drilling in South Louisiana. Also during 2004, we will continue to pursue the New Ventures activity we began in 2003.

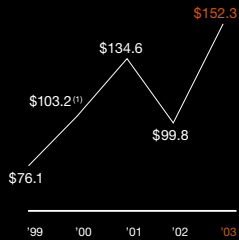
In July of 2004 we will celebrate our 75th year of providing energy solutions as a company. We look forward to 2004 with a great deal of excitement. As always, I wish to thank our people for their superb accomplishments in 2003 and our shareholders for believing in what we are doing.



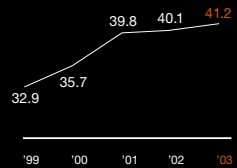
Harold M. Korell
President and Chief Executive Officer



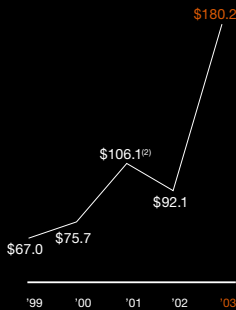
Net income (in millions)



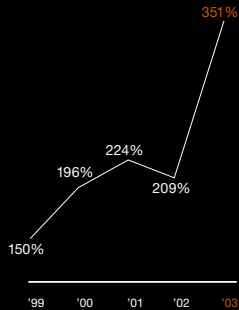
EBITDA (in millions)



Production (Bcfe)



Capital expenditures (in millions)



Reserve replacement⁽³⁾



Finding cost (\$/Mcfe)⁽³⁾

(1) Before unusual and extraordinary items.

(2) Includes \$13.5 million funded by the owner of the minority interest in Overton partnership.

(3) Excludes reserve revisions.

Financial and Operating Highlights

	2003	2002	2001
Revenues and Earnings			
Operating revenues (in millions)	\$ 327.4	\$ 261.5	\$ 344.9
Operating income (in millions)	\$ 97.3	\$ 46.5	\$ 82.7
Net income (in millions)	\$ 48.9	\$ 14.3	\$ 35.3
Diluted earnings per share	\$ 1.43	\$.55	\$ 1.38
EBITDA (in millions)	\$ 152.3	\$ 99.8	\$ 134.6
Capital expenditures (in millions)	\$ 180.2	\$ 92.1	\$ 106.1 ⁽¹⁾
Average diluted shares outstanding (in millions)	34.2	26.1	25.6
Exploration and Production			
Total proved reserves (Bcf equivalent)	503.1	415.3	402.0
Percent of reserves natural gas	91 %	90 %	89 %
Percent of reserves proved, developed	82 %	77 %	80 %
Total production (Bcf equivalent)	41.2	40.1	39.8
Average gas price (\$/Mcf)	\$ 4.20	\$ 3.00	\$ 3.85
Average oil price (\$/barrel)	\$ 26.72	\$ 21.02	\$ 23.55
Finding and development cost (\$/Mcf) ⁽²⁾	\$ 1.18	\$ 1.02	\$ 1.11
Reserve replacement ratio ⁽²⁾	351 %	209 %	224 %
Reserve life (years)	12.2	10.4	10.1
Natural Gas Distribution			
Sales and end-use transportation (Bcf)	24.7	25.1	24.0
Utility customers at year-end	141,573	139,543	136,242
Heating weather – percent of normal	99 %	98 %	91 %

(1) Includes \$13.5 million funded by the owner of the minority interest in Overton partnership.

(2) Excludes reserve revisions.



Arkoma Basin

Southwestern has been actively drilling in the Arkoma Basin for over 60 years and we believe that the basin still holds tremendous potential.

During 2003, we successfully completed 42 wells out of 55 drilled in the Arkoma Basin for a success ratio of 76%. We continue to keep our finding costs and production costs low, which make our activities in the Arkoma Basin highly economic. With average three-year finding costs of \$1.14 per Mcf and average three-year production costs of \$0.38 per Mcf, the cash netbacks on the wells we drill in the Arkoma add significant value in the current commodity price environment.

Our activity in the Ranger Anticline area, located in the southern edge of the basin in Arkansas, is a prime example of how some ideas, while they may take time to develop, can eventually evolve into projects that create substantial value. After drilling our first successful well at Ranger in 1997, we developed a better understanding of the complex faulting and highly-fractured nature of this play over the next several years. By the end of 2002, we had successfully drilled

13 out of 16 wells at Ranger. In early 2003 we received regulatory approval to downspace the field to 80-acre spacing, from what was originally 640-acre spacing. As a result, we stepped-up our drilling activity in the area and successfully drilled 10 out of 12 wells at Ranger, adding 13.1 Bcf of reserves at a finding cost of \$0.85 per Mcf.

Not only did the approved downspacing provide a new level of development activity at Ranger, but our growing understanding of the geology indicated that the productive area could be much larger than once thought. At December 31, 2003, we held a 65% average working interest in 37,100 gross undeveloped acres in the Ranger area. In February 2004, we production tested the Smith #1-10 well at 2.7 MMcf per day.

This exploratory test well is located six miles west of our existing Ranger production, and indicates that the gas-filled Borum sands could stretch over a significantly larger area. Also, in February 2004, we drilled the Doggle #2-15 and logged over 350 feet of pay in the well. This exploratory well is located one mile south of the Smith well in Logan County, Arkansas. We are currently drilling a third exploratory well in the area, the Albright #1-7, and are seeing encouraging results. The Albright #1-7 well is located east of the Smith and Doggle wells and approximately 3 miles west of our existing Ranger production. We believe that Ranger may hold significant development potential and we intend to drill up to 20 wells in 2004.

In 2004, we plan to invest approximately \$44 million in the Arkoma Basin and participate in over 80 wells and 95 workover projects. We have been actively drilling in the Arkoma Basin for over 60 years and believe that the basin still holds tremendous potential.

East Texas

We've greatly enhanced our economics at Overton with careful attention to our well completion techniques. The result has been an average increase of 200% in our initial production rates compared to the wells drilled by the previous operator.

Over the last few years, our drilling results at the Overton Field in Smith County, Texas have been nothing less than outstanding, and our excellent performance continued in 2003. The field's daily gross production increased to 60 MMcfe per day at the end of 2003, compared to approximately 27 MMcfe at year-end 2002. Likewise, our net production from the area increased to 13.6 Bcfe from 5.9 Bcfe in 2002, and we are projecting production from the field to grow to 19 – 21 Bcfe in 2004. Additionally, our reserves at Overton increased to 196.3 Bcfe at the end of 2003, up from 111.0 Bcfe at year-end 2002.

The significant growth in our Overton production and reserves was due to a decision we made in early 2003 to change our development strategy for the field. Instead of continuing to pursue our strategy of drilling 15 – 18 wells per year from internal cash flow, in February of 2003 we raised \$103 million of equity to accelerate the development of the field. In 2003, we drilled and completed 57 wells at Overton compared to 18 wells in 2002.

In 2004, we plan to invest approximately \$105.5 million at Overton and drill 70 wells in the field utilizing at least five drilling rigs, with some locations being 40-acre spaced wells. Although current field rules at Overton allow for development at optional 80-acre spacing (eight wells per 640-acre unit), regulatory approval allowed us to drill four wells during 2003 at locations that were effectively 40-acre spaced wells. Results from the four wells drilled at tighter spacing were encouraging. Of the four test

wells drilled at 40-acre spacing, three wells indicated pressures near original reservoir pressures and one showed partial depletion. The data from the four 40-acre spaced wells indicates that a significant portion of the field will likely require 40-acre spaced wells to adequately develop the field, while other areas of the field will not. Continued downspacing should allow us to drill an additional 80 wells in the area in 2005 and beyond. We also intend to invest approximately \$5.4 million in 2004 to drill 6 to 8 wells in other areas in East Texas.

Overton is another example of a project that, although completely unnoticed at first, has now become a significant part of our company and a tremendous catalyst in terms of our production and reserve growth in 2003 and 2004.





Exploration & New Ventures

In 2003, we began working on projects we are calling "New Ventures." We acquired 345,310 net undeveloped leasehold acres in these project areas during 2003, which more than doubled our total undeveloped acreage position at December 31, 2002. In 2004, we plan to invest approximately \$18.2 million in our "New Ventures" projects.

During the third quarter of 2003, we made a significant discovery on our River Ridge prospect located in Lea County, New Mexico. This discovery was made by deepening the Rio Blanco "4" Fed Com #1 well to the Devonian formation at 14,590 feet. This Devonian open-hole completion is currently producing at a rate of approximately 7.0 MMcf per day. We hold a 12.5% working interest in the discovery well. An offset well in the prospect, the Rio Blanco "33" #1 well, reached a total depth of 15,000 feet in February 2004 and encountered gas-bearing intervals, as measured by drill-stem testing and open-hole logs, in the Devonian formation. The initial drill-stem test tested the top 100 feet of the Devonian formation and flowed 3.2 MMcf of gas per day at a pressure of 800 pounds per square inch. A second drill-stem test selectively tested 30 feet of deeper pay and yielded an additional 10.6 MMcf per day at a pressure of 2,800 pounds per square inch. We believe

the overall prospect has approximately 30 to 50 Bcfe of gross potential. We hold a 50% working interest in this well which is expected to be placed on production in March 2004.

Since our first discovery in December 1999, the efforts of our Gulf Coast exploration program have resulted in 9 successful wells out of 21 wildcats drilled in South Louisiana. After three years of good drilling results from 1999 to 2001, we did not have a significant discovery in South Louisiana in 2002 or 2003. Our recent drilling activities in this area are not meeting our economic criteria, therefore we are reducing our investments in the Gulf Coast to \$12.8 million in 2004. While we still plan to drill 4 to 8 exploration and development wells in the Gulf

Coast area in 2004, we expect to decrease our activity in this area going forward.

In 2003, we began working on projects we are calling "New Ventures." During the year, we acquired 345,310 net undeveloped leasehold acres in these project areas for approximately \$11.0 million. This "New Venture" acreage more than doubled our total undeveloped acreage position at December 31, 2002. In addition, in early 2004, we acquired 95,000 net acres in a coal bed methane play located in the Crazy Mountain Basin in Montana. We plan to spud an initial test well on this acreage in the first quarter of 2004. If successful, we would likely drill a 4 to 8 well pilot program to further determine the economic viability of this project.

In 2004, we plan to invest approximately \$18.2 million in our "New Ventures" projects.

Natural Gas Distribution

In June 2003, the Milken Institute named Northwest Arkansas as the "Best Performing City" in the United States based on job creation and local economic growth. The area's vibrant economy has spurred significant growth in the area's residential housing market, creating future opportunities for our utility operations.

Since 1929, Arkansas Western Gas Company has provided a safe, dependable and economical energy source to the citizens and businesses in northern Arkansas. Today, 75 years later, the future looks brighter than ever for our utility business and the communities we serve.

Our utility operations continue to benefit from the strong population growth and economic vitality taking place in our service territory. Our Northwest Arkansas service territory has become one of the most dynamic economies in the country. Not only was Northwest Arkansas recognized by the U.S. Census

Bureau as the 6th fastest growing community in the United States in 2001, but in June of 2003, the Milken Institute ranked the area as the "Best Performing City" in the United States based on job creation and local economic growth. As home to the largest public corporation in the world, Wal-Mart Stores, Inc., the region has experienced significant growth due to its presence in the area. Other major corporations such as Tyson Foods and J.B. Hunt Transportation, along with the University of Arkansas, have also significantly contributed to the area's growth. What was formerly a collection of country towns is now a growing cosmopolitan area with affordable housing, live theater, award-winning public schools, a low crime rate and a vibrant economy.

In September 2003, we received regulatory approval for a rate increase totaling \$4.1 million annually, and were allowed to recover certain additional costs totaling \$2.3 million over a two-year period. The rate increase was effective on October 1, 2003, and improves the profitability of our utility.

We are proud of our 75-year history of providing the growing natural gas needs of the communities in northern Arkansas. We look forward to the continued growth in our service area, and are committed to providing a clean and affordable energy supply for our customers while maximizing our earnings and cash flow for our shareholders.



Directors



Photo of Directors as shown from left to right: Lewis E. Epley, Jr., John Paul Hammerschmidt, Charles E. Scharlau, Harold M. Korell, Robert L. Howard, Kenneth R. Mourton, and Vello A. Kuuskraa

Executive Officers



Directors

Lewis E. Epley, Jr. (6)
Attorney at Law

John Paul Hammerschmidt (12)
Retired, U.S. Congressman

Robert L. Howard (9)
Retired, Shell Oil Company

Vello A. Kuuskraa (1)
President and Chairman of the Board, Advanced Resources International, Inc.

Harold M. Korell (7)
President, Chief Executive Officer and Chairman of the Board, Southwestern Energy Company

Kenneth R. Mourton (9)
Managing Partner, Ball and Mourton, Ltd., PLLC

Charles E. Scharlau (52)
Retired CEO, Southwestern Energy Company



Corporate Officers

Harold M. Korell (7)
President, Chief Executive Officer and Chairman of the Board

Greg D. Kerley (14)
Executive Vice President and Chief Financial Officer

Mark K. Boling (2)
Executive Vice President, General Counsel and Secretary

Dee W. Hency (26)
Vice President - Administration and Chief Information Officer

Timothy J. O'Donnell (13)
Vice President - Human Resources and Treasurer

Stanley T. Wilson (18)
Controller and Chief Accounting Officer



Subsidiary Operating Officers

Southwestern Energy Production Company and SEECO, Inc.

Richard F. Lane (6)
Executive Vice President

Jim R. Dewbre (6)
Vice President - Land

J. Alan Stubblefield (6)
Vice President - Production

John D. Thaeler (5)
Vice President - SEECO, Inc.



Arkansas Western Gas Company

Alan N. Stewart
Executive Vice President

Charles V. Stevens (32)
Senior Vice President

Ricky A. Gunter (31)
Vice President - Rates and Regulation

Bob Lamb (13)
Vice President - Community Development

Jeffrey L. Dangeau (18)
General Counsel and Secretary

Glenn M. Morgan (27)
Controller and Treasurer



Photo of Executive Officers as shown from left to right:

Harold M. Korell
Greg D. Kerley
Richard F. Lane
Mark K. Boling
Alan N. Stewart

Years of service with the Company are shown in parentheses.

Annual Meeting

May 12, 2004 at
11:00 a.m. CDT
Wyndham Hotel –
Greenspoint
Houston, Texas

**Independent Public
Accountants**

Pricewaterhouse-
Coopers LLP
Tulsa, Oklahoma



Investor Relations

Greg D. Karley
Executive Vice President
and Chief Financial Officer

Brad D. Sylvester
Manager,
Investor Relations
281-618-4807

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and Registrar**

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