

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the quarterly period ended April 3, 2005

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the transition period from _____ to _____.

Commission file number: 1-3203



CHESAPEAKE CORPORATION

(Exact name of registrant as specified in its charter)

Virginia

(State or other jurisdiction of incorporation or organization)

54-0166880

(I.R.S. Employer Identification No.)

1021 East Cary Street

Richmond, Virginia

(Address of principal executive offices)

23219

Zip Code

Registrant's telephone number, including area code: **804-697-1000**

Not Applicable

(Former name, former address, and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☒ No ☐

Number of shares of \$1.00 par value common stock outstanding as of April 28, 2005:
19,705,106 shares.

CHESAPEAKE CORPORATION
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED APRIL 3, 2005
INDEX

	PAGE NUMBER
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements (Unaudited)</u>	
<u>Consolidated Statements of Earnings - Quarters ended April 3, 2005,</u> <u>and April 4, 2004</u>	3
<u>Consolidated Balance Sheets at April 3, 2005, and January 2, 2005</u>	4
<u>Consolidated Statements of Cash Flows - Quarters ended April 3, 2005,</u> <u>and April 4, 2004</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and</u> <u>Results of Operations</u>	19
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	23
<u>Item 4. Controls and Procedures</u>	23
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	24
<u>Item 6. Exhibits</u>	24
<u>Signature</u>	25

PART I - FINANCIAL INFORMATION

Item 1: Financial Statements

CHESAPEAKE CORPORATION AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS *(in millions, except per share data; unaudited)*

	Quarters Ended	
	Apr. 3, 2005	Apr. 4, 2004
Net sales	\$ 272.4	\$ 263.6
Costs and expenses:		
Cost of products sold	224.8	219.8
Selling, general and administrative expenses	37.8	33.3
Other income, net	1.6	1.8
	11.4	12.3
Earnings from continuing operations before interest and taxes	11.4	12.3
Interest expense, net	8.9	11.3
	2.5	1.0
Income from continuing operations before taxes	2.5	1.0
Income tax expense	0.9	0.3
	1.6	0.7
Income from continuing operations	\$ 1.6	\$ 0.7
Discontinued operations:		
Loss from discontinued operations, net of income tax benefit of \$0.1	-	(0.2)
Gain on disposal of discontinued operations, net of income tax expense of \$0.0 and \$0.1	0.7	0.2
	2.3	0.7
Net income	\$ 2.3	\$ 0.7
Basic earnings per share:		
Earnings from continuing operations	\$ 0.08	\$ 0.04
Discontinued operations	0.04	-
	0.12	0.04
Basic earnings per share	\$ 0.12	\$ 0.04
Diluted earnings per share:		
Earnings from continuing operations	\$ 0.08	\$ 0.04
Discontinued operations	0.04	-
	0.12	0.04
Diluted earnings per share	\$ 0.12	\$ 0.04
Weighted average number of common shares outstanding:		
Basic	19.4	16.0
	19.4	16.1
Diluted	19.4	16.1
Cash dividends declared per share of common stock	\$ 0.22	\$ 0.22

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in millions, except shares and per share amounts; unaudited)

	Apr. 3, <u>2005</u>	Jan. 2, <u>2005</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 21.3	\$ 54.3
Accounts receivable (less allowance of \$5.2 and \$6.2)	153.9	148.8
Inventories:		
Finished goods	62.7	64.7
Work-in-process	21.8	21.3
Materials and supplies	28.5	28.4
Total inventories	<u>113.0</u>	<u>114.4</u>
Prepaid expenses and other current assets	22.6	19.0
Income taxes receivable	0.5	0.5
Total current assets	<u>311.3</u>	<u>337.0</u>
Property, plant and equipment, net	404.9	427.1
Goodwill	681.8	694.6
Other assets	90.5	96.2
Total assets	<u><u>\$ 1,488.5</u></u>	<u><u>\$ 1,554.9</u></u>

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS, continued
(in millions, except shares and per share amounts; unaudited)

	Apr. 3, 2005	Jan. 2, 2005
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 139.3	\$ 141.4
Accrued expenses	83.6	80.5
Income taxes payable	26.0	26.6
Current maturities of long-term debt	22.9	64.1
Dividends payable	4.3	4.3
Total current liabilities	276.1	316.9
Long-term debt	364.2	364.8
Environmental liabilities	36.5	41.8
Pensions and postretirement benefits	76.3	77.1
Deferred income taxes	24.5	25.0
Other long-term liabilities	17.2	17.5
Total liabilities	794.8	843.1
Stockholders' equity:		
Preferred stock, \$100 par value, issuable in series; authorized, 500,000 shares; issued, none	-	-
Common stock, \$1 par value; authorized, 60 million shares; outstanding 19.7 million shares and 19.6 million shares	19.7	19.6
Additional paid-in-capital	98.4	96.1
Unearned compensation	(5.3)	(3.3)
Accumulated other comprehensive income	58.4	74.9
Retained earnings	522.5	524.5
Total stockholders' equity	693.7	711.8
Total liabilities and stockholders' equity	\$ 1,488.5	\$ 1,554.9

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions; unaudited)

	Quarters Ended	
	<u>Apr. 3, 2005</u>	<u>Apr. 4, 2004</u>
Operating activities:		
Net income	\$ 2.3	\$ 0.7
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	14.8	16.2
Deferred income taxes	0.7	0.4
Gain on sales of property, plant and equipment	-	(0.5)
Changes in operating assets and liabilities, net of acquisitions and dispositions:		
Accounts receivable, net	(10.4)	(4.1)
Inventories	(2.4)	2.2
Other assets	0.6	4.3
Accounts payable	2.4	0.3
Accrued expenses	4.5	2.6
Income taxes payable and receivable, net	(0.2)	14.7
Termination of interest rate swaps	(0.6)	6.4
Other	(0.8)	(0.1)
Net cash provided by operating activities	<u>10.9</u>	<u>43.1</u>
Investing activities:		
Purchases of property, plant and equipment	(6.8)	(11.9)
Proceeds from sales of property, plant and equipment	-	1.1
Other	-	(0.3)
Net cash used in investing activities	<u>(6.8)</u>	<u>(11.1)</u>
Financing activities:		
Net borrowings (payments) on lines of credit	29.7	(21.5)
Payments on long-term debt	(62.9)	(5.4)
Proceeds from long-term debt	0.6	0.2
Proceeds from issuance of common stock, net of issuance costs	-	82.6
Debt issue costs	-	(2.6)
Dividends paid	(4.3)	(3.4)
Net cash (used in) provided by financing activities	<u>(36.9)</u>	<u>49.9</u>
Effect of exchange rate changes on cash and cash equivalents	<u>(0.2)</u>	<u>1.4</u>
(Decrease) increase in cash and cash equivalents	(33.0)	83.3
Cash and cash equivalents at beginning of period	54.3	11.9
Cash and cash equivalents at end of period	<u><u>\$ 21.3</u></u>	<u><u>\$ 95.2</u></u>

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated interim financial statements of Chesapeake Corporation and subsidiaries included herein are unaudited. The January 2, 2005, consolidated balance sheet was derived from audited financial statements. As of April 4, 2004, the Land Development segment was liquidated, and this segment is accounted for as a discontinued operation (see Note 4). These statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and, in accordance with those rules and regulations, we have condensed or omitted certain information and footnotes normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP"). We believe that the disclosures made are adequate for a fair presentation of results of our operations and financial position. In the opinion of management, the consolidated financial statements reflect all adjustments, all of a normal recurring nature, necessary to present fairly our consolidated financial position and results of operations for the interim periods presented herein. All significant intercompany accounts and transactions are eliminated. The preparation of consolidated financial statements in conformity with GAAP requires management to make extensive use of estimates and assumptions that affect the reported amounts and disclosures. Actual results could differ from these estimates. Certain prior year amounts have been reclassified to conform to current presentations.

Our 52-53 week fiscal year ends on the Sunday nearest to December 31. Fiscal year 2005 contains 52 weeks, and fiscal year 2004 contained 53 weeks. The additional week in 2004 is included in the first quarter.

These consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in our latest Annual Report on Form 10-K; additional details on our significant accounting policies are provided therein. The results of operations for the 2005 interim period are not necessarily indicative of the results that may be expected for the full year.

In this report, unless the context requires otherwise, references to "we," "us," "our," "Chesapeake" or the "Company" are intended to mean Chesapeake Corporation and its consolidated subsidiaries.

Stock-Based Compensation

We use the intrinsic value method of accounting for our stock option plans. Under the intrinsic value method, compensation cost is not recognized for stock options unless the options are granted at an exercise price lower than the market price on the date of grant. See "New Accounting Pronouncements" for additional information regarding our method of accounting for stock options.

Had the compensation cost for our stock option plans been determined based on the fair value at the grant date, rather than the intrinsic value method, our pro forma amounts would be as follows:

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

(in millions, except per share data)

	<u>Quarters Ended</u>	
	<u>Apr. 3, 2005</u>	<u>Apr. 4, 2004</u>
Stock-based compensation expense, net of tax, included in net income as reported	\$ 0.2	\$ 0.2
Net income as reported	\$ 2.3	\$ 0.7
Additional stock-based compensation expense, net of tax	0.2	0.2
Pro forma net income	<u>\$ 2.1</u>	<u>\$ 0.5</u>
Earnings per share		
As reported:		
Basic	\$ 0.12	\$ 0.04
Diluted	0.12	0.04
Pro forma:		
Basic	\$ 0.11	\$ 0.03
Diluted	0.11	0.03

Pro forma disclosures for stock option accounting may not be representative of the effects on reported net income in future periods.

The stock-based compensation expense included in net income, as reported, principally represents the vesting of restricted stock under the Company's long-term incentive program. Approximately 0.1 million shares were granted under this program during the first quarter of 2005.

New Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 123 (revised 2004), *Share-Based Payment* ("SFAS 123R"). SFAS 123R is a revision of SFAS 123, *Accounting for Stock-Based Compensation* ("SFAS 123"), and it supersedes Accounting Principles Board ("APB") Opinion No. 25, *Accounting for Stock Issued to Employees*. SFAS 123R requires compensation cost related to share-based payment transactions to be recognized in the financial statements. That cost will be measured based on the fair value of the award on the grant date and recognized as expense over the requisite service or vesting period. As described previously in this note under the heading "Stock Options," we currently use the intrinsic value method of accounting for our stock option plans as defined in APB Opinion No. 25. Based on this method, no compensation cost has been recognized for our stock options, as the stock options granted had an exercise price equal to the fair market value of the underlying stock on the date of grant. We currently provide pro forma disclosures regarding the impact on net income and earnings per share as if we had applied the fair value method of accounting for stock-based compensation expense, which is based upon a Black-Scholes option pricing model. Depending on the model used to calculate stock-based compensation expense in the future and other requirements of SFAS 123R, the pro forma disclosure may not be indicative of the stock-based compensation expense that will be recognized in our financial statements in the future. SFAS 123R is effective for the first annual period beginning after June 15, 2005. We expect to adopt the new standard as of the beginning of fiscal year 2006 using the modified prospective method of transition, in which compensation cost for all share-based payments granted after the effective date is recognized in accordance with SFAS 123R, and compensation cost for unvested awards granted prior to the effective date is based on the requirements of SFAS 123 similar to the pro forma calculations provided herein. We are currently evaluating the impact this standard will have on our financial statements.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

On March 29, 2005 the SEC staff issued Staff Accounting Bulletin (“SAB”) No. 107, *Share-Based Payment*, which expresses the SEC staff's views on SFAS 123R. Among other things, SAB 107 describes the SEC staff's views on share-based payment transactions with nonemployees, valuation methods, the classification of compensation expense in the financial statements and first-time adoption of SFAS 123R in an interim period.

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs — an amendment of ARB No. 43, Chapter 4* (“SFAS 151”). SFAS 151 amends the guidance in Accounting Research Bulletin No. 43, Chapter 4, *Inventory Pricing*, to clarify that abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage) are to be recognized as current-period charges. SFAS 151 is effective for fiscal years beginning after June 15, 2005. SFAS 151 is not expected to have a material impact on our financial statements.

NOTE 2. EARNINGS PER SHARE ("EPS")

Calculation

Basic EPS is calculated using the weighted-average number of outstanding common shares during each period. Diluted EPS is calculated using the weighted-average number of diluted outstanding common shares during each period. Diluted EPS reflects the potential dilution that could occur if securities are exercised or converted into common stock, or result in the issuance of common stock that would then share in earnings. The difference between the weighted-average shares used for the basic and diluted calculation is due to the number of shares for which “in-the-money” stock options are outstanding.

There was not a material amount of dilutive shares as of April 3, 2005, and 0.1 million dilutive shares were outstanding as of April 4, 2004, for purposes of calculating diluted EPS. As of April 3, 2005, and April 4, 2004, 1.3 million and 1.5 million, respectively, of potentially dilutive common shares were not included in the computation of diluted EPS, because the effect would be antidilutive.

Common Stock Public Offering

On March 15, 2004, Chesapeake completed the sale of 3.65 million shares of common stock at a public offering price of \$24 per share. Our net proceeds from the sale of these shares, after deducting discounts, commissions, and expenses, were approximately \$82.6 million. On April 8, 2004, the underwriters of the common stock offering partially exercised their over-allotment option and acquired an additional 0.4 million shares at a public offering price of \$24 per share. Our net proceeds from the sale of these additional shares, after deducting discounts, commissions and expenses, were approximately \$9.2 million.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

NOTE 3. COMPREHENSIVE INCOME

Comprehensive (loss) income is as follows:
(*in millions*)

	Quarters Ended	
	<u>Apr. 3, 2005</u>	<u>Apr. 4, 2004</u>
Net income	\$ 2.3	\$ 0.7
Foreign currency translation	(16.7)	3.8
Change in fair market value of derivatives, net of tax	(1.1)	1.8
Minimum pension liability, net of tax	1.3	(1.8)
	<hr/>	<hr/>
Comprehensive (loss) income	\$ (14.2)	\$ 4.5
	<hr/>	<hr/>

NOTE 4. DISCONTINUED OPERATIONS

Our former Land Development segment owned real estate that we retained when we sold the timberland associated with our former pulp and paper operations because we believed this land was more valuable when sold for development or other uses. The real estate was marketed to third parties for residential and commercial development, real estate investment and land conservation. As of the end of the first quarter of 2004, the Land Development segment was liquidated and, as a result, this segment is now accounted for as a discontinued operation.

Summarized results of discontinued operations are shown separately in the accompanying consolidated statements of earnings. Discontinued operations in 2005 primarily represent the reduction of the liability for contractual obligations related to our former Merchandising and Specialty Packaging segment that was divested in 2001.

NOTE 5. INCOME TAXES

The effective income tax rate from continuing operations for the first quarter of 2005 was approximately 35 percent compared to an effective income tax rate from continuing operations of 30 percent for the first quarter of 2004. The increase in our effective tax rate results from our inability to claim benefits for our U.S. tax losses in 2005. See Note 8 for information regarding an IRS proposed adjustment.

NOTE 6. DEBT

In the first quarter of 2005, we paid \$38.8 million principal amount of loan note maturities, and we redeemed, at par, the remaining \$18.2 million principal amount of the 7.2 percent notes which also matured during the first quarter.

In January 2004 we terminated interest rate swaps and received a cash settlement of \$6.4 million from the counterparty. This amount will be recognized as an interest rate yield adjustment over the remaining life of the underlying debt.

NOTE 7. EMPLOYEE RETIREMENT AND POSTRETIREMENT BENEFITS

The components of the net periodic benefit cost recognized during the first quarters of 2005 and 2004 were as follows:

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

(in millions)	Pension Benefits				Postretirement Benefits Other Than Pensions	
	U.S. Plans		Non-U.S. Plans			
	Apr. 3, 2005	Apr. 4, 2004	Apr. 3, 2005	Apr. 4, 2004	Apr. 3, 2005	Apr. 4, 2004
Service cost	\$ 0.1	\$ 0.1	\$ 1.5	\$ 1.2	\$ -	\$ -
Interest cost	1.0	1.0	5.1	4.2	0.2	0.2
Expected return on plan assets	(1.2)	(1.3)	(5.0)	(4.7)	-	-
Recognized actuarial loss	0.5	0.4	1.4	0.9	0.1	0.1
Net pension expense	\$ 0.4	\$ 0.2	\$ 3.0	\$ 1.6	\$ 0.3	\$ 0.3

NOTE 8. COMMITMENTS AND CONTINGENCIES

Environmental Matters

The costs of compliance with existing environmental regulations are not expected to have a material adverse effect on our financial position or results of operations.

The Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”) and similar state “Superfund” laws impose liability, without regard to fault or to the legality of the original action, on certain classes of persons (referred to as potentially responsible parties or “PRPs”) associated with a release or threat of a release of hazardous substances into the environment. Financial responsibility for the remediation and restoration of contaminated property and for natural resource damages can extend to previously owned or used properties, waterways and properties owned by third parties, as well as to properties currently owned and used by a company even if contamination is attributable entirely to prior owners. As discussed below, the U.S. Environmental Protection Agency (“EPA”) has given notice of its intent to list the Lower Fox River in Wisconsin on the National Priorities List under CERCLA and identified our subsidiary, Wisconsin Tissue Mills Inc., now WTM I Company (“WT”), as a PRP for the Lower Fox River site.

Except for the Fox River matter, we have not been identified as a PRP at any other CERCLA-related sites. However, there can be no assurance that we will not be named as a PRP at any other sites in the future or that the costs associated with additional sites would not be material to our financial position or results of operations.

In June 1994 the U.S. Department of Interior, Fish and Wildlife Service (“FWS”), a federal natural resources trustee, notified WT that it had identified WT as a PRP for natural resources damage liability under CERCLA arising from alleged releases of polychlorinatedbiphenyls (“PCBs”) in the Fox River and Green Bay System in Wisconsin from WT’s former recycled tissue mill in Menasha, Wisconsin. In addition to WT, six other companies (Appleton Papers, Inc., Fort Howard Corporation, P.H. Glatfelter Company (“Glatfelter”), NCR Corporation, Riverside Paper Corporation and U.S. Paper Mills Corporation) have been identified as PRPs for the Fox River site. The FWS and other governmental and tribal entities, including the State of Wisconsin (“Wisconsin”), allege that natural resources, including federal lands, state lands, endangered species, fish, birds, tribal lands or lands held by the U.S. in trust for various Indian tribes, have been exposed to PCBs that were released from facilities located along the Lower Fox River. On January 31, 1997, the FWS notified WT of its intent to file suit, subject to final

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

approval by the U.S. Department of Justice (“DOJ”), against WT to recover alleged natural resource damages, but the FWS has not yet instituted such litigation. On June 18, 1997, the EPA announced that it was initiating the process of listing the Lower Fox River on the CERCLA National Priorities List of hazardous waste sites. On September 30, 2003, EPA and the Wisconsin Department of Natural Resources (“DNR”), in connection with the issuance of General Notice Letters under CERCLA to the PRPs requesting a good faith offer to conduct the remedial design for downstream portions of the Lower Fox River site, also notified Menasha Corporation and Sonoco Products Company that those companies were also considered potentially liable for the cost of response activities at the Lower Fox River site.

In January 2003 DNR and EPA released a Record of Decision (the “OU1-2 ROD”) for Operable Units 1 and 2 (“OU1” and “OU2”) of the Fox River site. OU1 is the reach of the river that is the farthest upstream and is immediately adjacent to the former WT mill. The OU1-2 ROD selects a remedy, consisting primarily of dredging, to remove substantially all sediment in OU1 with concentrations of PCBs of more than 1 part per million in order to achieve a surface weighted-average PCB concentration level (“SWAC”) of not more than 0.25 parts per million. The OU1-2 ROD estimates the present-worth cost of the proposed remedy for OU1 is \$66.2 million. Present-worth cost as stated in the OU1-2 ROD means capital costs in undiscounted 2001 dollars and long-term operation, maintenance and monitoring costs discounted at 6 percent. This estimate is an engineering cost estimate and the OU1-2 ROD states that the actual project cost is expected to be within +50 percent to -30 percent of the estimate. The OU1-2 ROD estimates that the proposed dredging remedy for OU1 will be accomplished over a six-year period after commencement of dredging. For OU2, the reach of the river covering approximately 20 miles downstream from OU1, the OU1-2 ROD proposes a remedy of monitored natural recovery over a 40-year period. The OU1-2 ROD states that the present-worth cost of the proposed remedy for OU2 is an engineering cost estimate of \$9.9 million, based on estimated costs discounted at 6 percent.

On July 1, 2003, DNR and EPA announced that they had signed an agreement with WT under which WT will complete the design work for the sediment clean-up in OU1. The design work to be done by WT is estimated to cost approximately \$3.7 million. On October 1, 2003, EPA and DNR announced that WT and Glatfelter had entered into a proposed Consent Decree (the “Consent Decree”) regarding the remediation of OU1. The Consent Decree was entered by the court on April 12, 2004. Under the terms of the Consent Decree, WT and Glatfelter agreed to perform appropriate remedial action in accordance with the OU1-2 ROD. The remedial action will be performed under oversight by EPA and DNR. To fund the remedial action, WT and Glatfelter have each paid \$25 million to an escrow account, and EPA and Wisconsin will use their best efforts to obtain an additional \$10 million from another source to supplement the funding. Contributions and cooperation may also be obtained from local municipalities, and additional assistance may be sought from other potentially liable parties. As provided in the Consent Decree, WT has been reimbursed from the escrow account for \$2 million of OU1 design costs expended under the July 1, 2003, design agreement.

Upon completion of the remedial action for OU1 to the satisfaction of EPA and Wisconsin, WT and Glatfelter will receive covenants not to sue from EPA and Wisconsin for OU1, subject to conditions typical of settlements under CERCLA. We believe the required remedial action for OU1 can be completed with the expected funding provided under the Consent Decree. If the funding provided through the Consent Decree is not adequate to pay for the required remedial action, WT and Glatfelter have the option, but not the obligation, to contribute additional funds to complete the remedial action. WT remains potentially liable for the additional costs necessary to achieve the performance standards for OU1 specified in the OU1-2 ROD.

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

Under the terms of the Consent Decree, WT also paid EPA and the State of Wisconsin \$375,000 for past response costs, and paid \$1.5 million for natural resource damages (“NRD”) for the Fox River site and \$150,000 for past NRD assessment costs. These payments have been credited toward WT’s potential liability for response costs and NRD associated with the Fox River site as a whole. As discussed later in this section, we believe that WT is entitled to substantial indemnification from a prior owner of WT with respect to these costs, and the prior owner has reimbursed WT for the payments made as required in the Consent Decree.

In July 2003 EPA and DNR announced a Record of Decision (the “OU3-5 ROD”) for Operable Units 3, 4 and 5 (“OU3,” “OU4” and “OU5,” respectively), the remaining operable units for this site. The OU3-5 ROD requires primarily dredging and disposal of PCB contaminated sediments from OU3 and OU4 (the downstream portion of the river) and monitored natural recovery in OU5 (Green Bay). The OU3-5 ROD remedy for OU3 and OU4 provides for removal of substantially all sediment with concentrations of PCBs of more than 1 part per million in order to achieve a SWAC of not more than 0.25 parts per million. The OU3-5 ROD estimates the present-worth cost of the proposed remedy for OU3-5 is \$324 million. Present-worth cost as stated in the ROD means capital costs in undiscounted 2001 dollars and long-term operation, maintenance and monitoring costs discounted at 6 percent. This estimate is an engineering cost estimate, and the OU3-5 ROD states that the actual project cost is expected to be within +50 percent to -30 percent of the estimate.

Based on information available to us at this time, we believe that the range of reasonable estimates of the total cost of remediation and restoration for the Fox River site is \$280 million to \$1.59 billion. The low end of this range assumes costs estimated in the OU1-2 ROD and the OU3-5 ROD and takes into account the -30 percent engineering estimating factor. The upper end of the range assumes costs estimated by consultants for the PRPs and includes a +50 percent engineering estimating factor. The OU1-2 ROD and the OU3-5 ROD indicate that most of the active remediation and restoration at the site is expected to take place in the next 10 years.

Based on current information and advice from our environmental consultants, we believe that the 1 part per million remedial action level, and the resulting aggressive effort to remove substantial amounts of PCB-contaminated sediments (most of which are buried under cleaner material or are otherwise unlikely to move) and dispose of the sediment off-site, as contemplated by the OU1-2 ROD and the OU3-5 ROD are excessive and would be environmentally detrimental and therefore inappropriate. The OU1-2 ROD includes provisions that a contingent remedy for OU1 consisting of a combination of dredging and capping may be implemented if certain conditions in the OU1-2 ROD are met and such remedy would provide the same level of protection to human health and the environment as the selected remedy. We believe that alternative remedies that are less intrusive than those selected in the OU1-2 ROD and the OU3-5 ROD are more environmentally appropriate, cost effective and responsible methods of managing the risks attributable to the sediment contamination. Any enforcement of a definitive remedial action plan may be subject to judicial review.

On October 25, 2000, the federal and tribal natural resources trustees released a Restoration and Compensation Determination Plan (“RCDP”) presenting the federal and tribal trustees’ planned approach for restoring injured federal and tribal natural resources and compensating the public for losses caused by the release of PCBs at the Fox River site. The RCDP states that the final natural resource damage claim (which is separate from, and in addition to, the remediation and restoration costs that will be associated with remedial action plans) will depend on the extent of PCB clean-up undertaken by EPA and DNR, but estimates past interim damages to be \$65 million, and, for illustrative purposes only,

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

estimates additional costs of restoration to address present and future PCB damages in a range of \$111 million to \$268 million. To date Wisconsin has not issued any estimate of natural resource damages. We believe, based on the information currently available to us, that the estimate of natural resource damages in the RCDP represents the reasonably likely upper limit of the total natural resource damages. We believe that the alleged damages to natural resources are overstated in the RCDP and joined in the PRP group comments on the RCDP to that effect. No final assessment of natural resource damages has been issued.

Under CERCLA, each PRP generally will be jointly and severally liable for the full amount of the remediation and restoration costs and natural resource damages, subject to a right of contribution from other PRPs. In practice PRPs generally negotiate among themselves to determine their respective contributions to any multi-party activities based upon factors including their respective contributions to the alleged contamination, equitable considerations and their ability to pay. In draft analyses by DNR and federal government consultants, the volume of WT's PCB discharges into the Fox River has been estimated to range from 2.72 percent to 10 percent of the total discharges of PCBs. This range may not be indicative of the share of the cost of the remediation and restoration costs and natural resource damages that ultimately will be allocated to WT because of: inaccuracies or incompleteness of information about mill operations and discharges; inadequate consideration of the nature and location of various discharges of PCBs to the river, including discharges by persons other than the named PRPs and the relationship of those discharges to identified contamination; uncertainty of the geographic location of the remediation and restoration eventually performed; uncertainty about the ability of other PRPs to participate in paying the costs and damages; and uncertainty about the extent of responsibility of the manufacturers of the carbonless paper recycled by WT which contained the PCBs. We have evaluated the ability of other PRPs to participate in paying the remediation and restoration costs and natural resource damages based on our estimate of their reasonably possible shares of the liability and on public financial information indicating their ability to pay such shares. While we are unable to determine at this time what shares of the liability for the Fox River costs will be paid by the other identified PRPs (or other entities who are subsequently determined to have liability), based on information currently available to us and the analysis described above, we believe that most of the other PRPs have the ability to pay their reasonably possible shares of the liability.

The ultimate cost to WT of remediation and restoration costs and natural resource damages related to the Fox River site and the time periods over which the costs and damages may be incurred cannot be predicted with certainty at this time due to uncertainties with respect to: what remediation and restoration will be implemented; the actual cost of that remediation and restoration; WT's share of any multi-party remediation and restoration costs and natural resource damages; the outcome of the federal and state natural resource damage assessments; the timing of any remediation and restoration; the evolving nature of remediation and restoration technologies and governmental regulations; controlling legal precedent; the extent to which contributions will be available from other parties; and the scope of potential recoveries from insurance carriers and prior owners of WT. While such costs and damages cannot be predicted with certainty at this time, we believe that WT's reasonably likely share of the ultimate remediation and restoration costs and natural resource damages associated with the Fox River site, including disbursement on behalf of WT of the remaining amount deposited by WT under the terms of the Consent Decree, may fall within the range of \$32 million to \$130 million, payable over a period of up to 40 years. In our estimate of the lower end of the range, we have assumed remediation and restoration costs as estimated in the OU1-2 ROD and the OU3-5 ROD, and the low end of the governments' estimates of natural resource damages and WT's share of the aggregate liability. In our estimate of the upper end of the range, we have assumed large-scale dredging at a higher cost than

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

estimated in the OU1-2 ROD and the OU3-5 ROD, and that our share of the ultimate aggregate liability for all PRPs will be higher than we believe it will ultimately be determined to be. We have accrued an amount for the Fox River liability based on our estimate of the reasonably probable costs within the range as described above.

We believe that, pursuant to the terms of a stock purchase agreement between Chesapeake and Philip Morris Incorporated (now known as Philip Morris USA Inc., or "PM USA," a wholly owned subsidiary of Altria Group, Inc.), a former owner of WT, we are entitled to substantial indemnification from PM USA with respect to the liabilities related to this matter. Based on the terms of that indemnity, we believe that the costs and damages within our estimated range of liability should be indemnified by PM USA. We understand, however, that PM USA is subject to certain risks (including litigation risk in cases relating to health concerns regarding the use of tobacco products). Accordingly, there can be no assurance that PM USA will be able to satisfy its indemnification obligations in the future. However, PM USA is currently meeting its indemnification obligations under the stock purchase agreement and, based on our review of currently available financial information, we believe that PM USA has the financial ability to continue to meet its indemnification obligations.

Pursuant to the Joint Venture Agreement with Georgia-Pacific Corporation for Georgia-Pacific Tissue, LLC, WT has retained liability for, and the third party indemnity rights associated with, the discharge of PCBs and other hazardous materials in the Fox River and Green Bay System. Based on currently available information, we believe that if remediation and restoration are done in an environmentally appropriate, cost effective and responsible manner, and if natural resource damages are determined in a reasonable manner, the matter is unlikely to have a material adverse effect on our financial position or results of operations. However, because of the uncertainties described above, there can be no assurance that the ultimate liability with respect to the Lower Fox River site will not have a material adverse effect on our financial position or results of operations.

Our accrued environmental liabilities totaled approximately \$46.0 million as of April 5, 2005, of which \$9.5 million was considered short-term, and \$46.9 million as of January 2, 2005, of which \$5.1 million was considered short-term.

Legal and Other Commitments

Chesapeake is a party to various other legal actions and tax audits, which are ordinary and incidental to our business. While the outcome of environmental, tax and legal actions cannot be predicted with certainty, we believe the outcome of any of these proceedings, or all of them combined, will not have a material adverse effect on our consolidated financial position or results of operations.

On March 26, 2001, the SEC issued a formal order that a private investigation be conducted concerning matters related to our financial reporting. The investigation was based on SEC inquiries arising out of our restatements of earnings in 2000 related to the U.S. Display business which was included in our former Merchandising and Specialty Packaging segment. The U.S. Display business was sold in 2001. On October 21, 2004, the staff of the SEC notified the Company and four of our former employees that the staff of the SEC had preliminarily decided to recommend that the Commission file civil enforcement actions against the Company and those former employees based on alleged violations of U.S. securities laws related to issues surrounding the earnings restatements in 2000. After extensive discussions with the SEC staff regarding, among other things, the nature of the alleged violations, our actions in response

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

thereto and our cooperation throughout the investigation, we believe that this matter will not have a material adverse effect on our consolidated financial position or results of operations.

The IRS has proposed certain adjustments relating to our tax treatment of our disposition of assets of WT in 1999. We have estimated our maximum potential exposure with respect to the matter to be approximately \$26 million; however, we are disputing the proposed adjustment as we continue to believe that our tax treatment of the transaction was correct and our tax advisor has confirmed its view that we should prevail in any dispute with the IRS related to this matter. Accordingly, no amount has been accrued for this proposed IRS adjustment. We expect to defend the matter vigorously through the IRS appeal process and, if necessary, through litigation. We do not expect that the ultimate resolution of this matter will have a material adverse effect on our financial condition or results of operations.

Guarantees and Indemnifications

We have entered into agreements for the sale of assets or businesses that contain provisions in which we agree to indemnify the buyers or third parties involved in the sale for certain liabilities or risks related to the sale. In these sale agreements, we typically agree to indemnify the buyers or other involved third parties against a broadly-defined range of potential “losses” (typically including, but not limited to, claims, costs, damages, judgments, liabilities, fines or penalties, and attorneys’ fees) arising from: (i) a breach of our representations or warranties in the sale agreement or ancillary documents; (ii) our failure to perform any of the covenants or obligations of the sale agreement or ancillary documents; and (iii) other liabilities expressly retained or assumed by us related to the sale. Most of our indemnity obligations under these sale agreements are: (i) limited to a maximum dollar value significantly less than the final purchase price; (ii) limited by time within which indemnification claims must be asserted (often between one and three years); and (iii) subject to a deductible or “basket.” Many of the potential indemnification liabilities under these sale agreements are unknown, remote or highly contingent, and most are unlikely to ever require an indemnity payment. Furthermore, even in the event that an indemnification claim is asserted, liability for indemnification is subject to determination under the terms of the applicable sale agreement, and any payments may be limited or barred by a monetary cap, a time limitation or a deductible or basket. For these reasons, we are unable to estimate the maximum potential amount of the potential future liability under the indemnity provisions of the sale agreements. However, we accrue for any potentially indemnifiable liability or risk under these sale agreements for which we believe a future payment is probable and a range of loss can be reasonably estimated. Other than the Fox River matter discussed in Environmental Matters above, as of April 3, 2005, we believe our liability under such indemnification obligations was immaterial.

In the ordinary course of our business, we may enter into agreements for the supply of goods or services to customers that provide warranties to their customers on one or more of the following: (i) the quality of the goods and services supplied by us; (ii) the performance of the goods supplied by us; and (iii) our compliance with certain specifications and applicable laws and regulations in supplying the goods and services. Liability under such warranties often is limited to a maximum amount, by the nature of the claim or by the time period within which a claim must be asserted. As of April 3, 2005, we believe our warranty obligations under such supply agreements were immaterial.

In the ordinary course of our business, we may enter into service agreements with service providers in which we agree to indemnify the service provider against certain losses and liabilities arising from the service provider’s performance of the agreement. Generally, such indemnification obligations do not

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

apply in situations in which the service provider is grossly negligent, engages in willful misconduct or acts in bad faith. As of April 3, 2005, we believe our liability under such service agreements was immaterial.

NOTE 9. SEGMENT DISCLOSURE

We currently conduct our business in two segments: the Paperboard Packaging segment and the Plastic Packaging segment. Our Paperboard Packaging segment designs and manufactures folding cartons, leaflets, labels and other value-added paperboard packaging products. The primary end-use markets for this segment are pharmaceutical and healthcare; international and branded products (such as alcoholic drinks, confectioneries, cosmetics and fragrances); tobacco; and food and household. Our Plastic Packaging segment designs and manufactures plastic containers, bottles, preforms and closures. The primary end-use markets for this segment are agrochemicals and other specialty chemicals, and food and beverages. General corporate expenses are shown as Corporate. Earnings from continuing operations before interest and taxes is abbreviated hereafter as EBIT. EBIT by segment excludes any gains or losses related to business divestitures and plant closures. There were no business divestitures or plant closures in the first quarter of 2005 or 2004. The following tables summarize the net sales from continuing operations; EBIT; depreciation; and identifiable assets for each of our segments:

(*in millions*)

	First Quarter	
	<u>2005</u>	<u>2004</u>
Net sales from continuing operations:		
Paperboard Packaging	\$ 221.7	\$ 219.1
Plastic Packaging	50.7	44.5
	<hr/>	<hr/>
	\$ 272.4	\$ 263.6
	<hr/>	<hr/>
EBIT:		
Paperboard Packaging	\$ 10.6	\$ 11.1
Plastic Packaging	5.4	5.1
Corporate	(4.6)	(3.9)
	<hr/>	<hr/>
	\$ 11.4	\$ 12.3
	<hr/>	<hr/>
Depreciation:		
Paperboard Packaging	\$ 12.3	\$ 13.4
Plastic Packaging	2.4	2.7
Corporate	0.1	0.1
	<hr/>	<hr/>
	\$ 14.8	\$ 16.2
	<hr/>	<hr/>

(*in millions*)

	<u>Apr. 3,</u>	<u>Jan. 2,</u>
	<u>2005</u>	<u>2005</u>
Identifiable assets:		
Paperboard Packaging	\$ 1,208.7	\$ 1,273.2
Plastic Packaging	184.1	183.2
Corporate	95.7	98.5
	<hr/>	<hr/>
	\$ 1,488.5	\$ 1,554.9
	<hr/>	<hr/>

CHESAPEAKE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (*unaudited*)

NOTE 10. SUBSEQUENT EVENT

On April 18, 2005, the Company completed the sale of the assets of its French wine and spirits label operation, Bourgeot Etiquo Lesbats (“Bourgeot”), to Autajon Group. The sale price was approximately €1.16 million (\$1.5 million). The Company estimates that it will incur a pre-tax and after-tax, non-cash loss on the sale of approximately \$3.5 million in the second quarter of 2005. The transaction is a sale of substantially all of the assets of the business, including machinery, equipment and inventory and an assignment by the Company of the rights, and an assumption by the buyer of the obligations, under certain contracts related to the business, including a lease for the plant building and the employer’s post-closing obligations for substantially all of the employee obligations and contracts. The Company will retain the accounts receivable of Bourgeot. Because the Company had not committed to the sale of the Bourgeot operation before quarter end, the Company has reported the assets of the Bourgeot operation as held for use as of April 3, 2005.

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Earnings from continuing operations before interest and taxes is abbreviated hereafter as EBIT. Consistent with our segment reporting in Note 9 to the Consolidated Financial Statements, EBIT by segment excludes any gains or losses related to business divestitures and plant closures. Excluding these amounts from our calculation of segment EBIT is consistent with how our management reviews segment performance and, we believe, affords the reader consistent measures of our operating performance. There were no business divestitures or plant closures in the first quarter of 2005 or 2004.

The following table sets forth first quarter net sales from continuing operations and EBIT by business segment:

Sales and EBIT by Segment

(in millions)

	Quarter Ended Apr. 3, 2005		Quarter Ended Apr. 4, 2004	
	Net Sales	EBIT	Net Sales	EBIT
Paperboard Packaging	\$ 221.7	\$ 10.6	\$ 219.1	\$ 11.1
Plastic Packaging	50.7	5.4	44.5	5.1
Corporate	-	(4.6)	-	(3.9)
Total	\$ 272.4	\$ 11.4	\$ 263.6	\$ 12.3

Net sales from continuing operations for the first quarter of 2005 were \$272.4 million, an increase of \$8.8 million over the comparable period in 2004. Changes in foreign currency exchange rates increased net sales from continuing operations for the first quarter of 2005 by \$10.5 million. The offsetting decrease in net sales for the quarter was primarily due to decreased sales volume in the pharmaceutical market of the Paperboard Packaging segment as well as pricing pressure and volume declines in the household packaging market of the Paperboard Packaging segment, offset in part by increased volume in the Plastic Packaging segment.

Gross margin, which is defined as net sales less cost of products sold, for the first quarter of 2005 was \$47.6 million compared to \$43.8 million for the first quarter of 2004. This increase was due to changes in foreign currency exchange rates and approximately \$1.4 million in start-up costs for our two new German facilities in the first quarter of 2004. Gross margin as a percentage of net sales was flat at 17 percent for each quarter.

Selling, general and administrative ("SG&A") expenses as a percentage of net sales for the first quarter increased from 13 percent in 2004 to 14 percent in 2005, primarily as a result of increased pension expense and costs associated with strategic initiatives.

EBIT for the first quarter of 2005 was \$11.4 million compared to EBIT of \$12.3 million for the first quarter of 2004. In addition to the items noted above, foreign currency exchange rates increased EBIT for the first quarter of 2005 by approximately \$0.7 million.

Net interest expense was \$8.9 million for the first quarter of 2005, down \$2.4 million compared to the first quarter of 2004. The decrease was primarily due to the redemption of higher rate debt in the second quarter of 2004 with a portion of the proceeds from the March 2004 common stock offering.

The effective income tax rate from continuing operations for the first quarter of 2005 was approximately 35 percent compared to an effective income tax rate from continuing operations of 30 percent for the first quarter of 2004. The increase in our effective tax rate results from our inability to claim benefits for our U.S. tax losses in 2005.

Net income for the first quarter of 2005 was \$2.3 million, or \$0.12 per diluted share, compared to net income of 0.7 million, or \$0.04 per diluted share, for the first quarter of 2004.

Discontinued Operations

Our former Land Development segment owned real estate that we retained when we sold the timberland associated with our former pulp and paper operations because we believed this land was more valuable when sold for development or other uses. The real estate was marketed to third parties for residential and commercial development, real estate investment and land conservation. As of the end of the first quarter of 2004, the Land Development segment was liquidated and, as a result, this segment is now accounted for as a discontinued operation.

Discontinued operations in 2005 primarily represent the reduction of the liability for contractual obligations related to our former Merchandising and Specialty Packaging segment that was divested in 2001.

Subsequent Event

On April 21, 2005, the company announced the sale of the assets of its French wine and spirits label operation, Bourgeot Etiqso Lesbats, to the Autajon Group for approximately €1.16 million (\$1.5 million). In the second quarter of 2005 the company expects to recognize a pre-tax and after-tax non-cash loss on the sale, which is currently estimated at approximately \$3.5 million. The company also expects the transaction to be accretive to earnings starting in the third quarter of 2005.

Segment Information

Paperboard Packaging

<i>(in millions)</i>	<u>2005</u>	<u>2004</u>	<u>Increase/(Decrease)</u>	
			<u>\$</u>	<u>%</u>
First Quarter:				
Net sales	\$221.7	\$219.1	2.6	1.2
EBIT	10.6	11.1	(0.5)	(4.5)
EBIT margin %	4.8%	5.1%		

Net sales for the Paperboard Packaging segment were \$221.7 million for the first quarter of 2005, an increase of \$2.6 million, or 1 percent, over the comparable period in 2004. Excluding changes in foreign currency exchange rates, which increased net sales by \$8.1 million, net sales were down 3 percent for the quarter. Net sales for the first quarter of 2005 were negatively impacted by decreased volume in pharmaceutical and healthcare packaging, pricing pressure and volume declines in food and household packaging, which were partially offset by higher sales volumes in alcoholic drinks packaging.

EBIT for the Paperboard Packaging segment for first quarter of 2005 was \$10.6 million, a decrease of \$0.5 million, or 5 percent, versus the comparable period in 2004. Excluding changes in foreign currency exchange rates, which increased EBIT by \$0.4 million, EBIT was down 8 percent for the quarter. EBIT for the first quarter of 2005 was negatively impacted by decreased sales volume in pharmaceutical and healthcare packaging, pricing pressure and decreased volume in food and household packaging and increased pension costs. These decreases were partially offset by increased volume in alcoholic drinks packaging and improved performance at our two new German factories, which produce tobacco and international and branded packaging.

Plastic Packaging

(in millions)

	2005	2004	Increase	
			\$	%
First Quarter:				
Net sales	\$50.7	\$44.5	6.2	13.9
EBIT	5.4	5.1	0.3	5.9
EBIT margin %	10.7%	11.5%		

Net sales for the Plastic Packaging segment for the first quarter of 2005 were \$50.7 million, an increase of \$6.2 million, or 14 percent, over the comparable period in 2004. Excluding changes in foreign currency rates, which increased net sales by \$2.4 million, net sales were up 8 percent for the quarter. The increase in net sales for the first quarter of 2005 was primarily due to higher volume in specialty chemical packaging as a result of increased shipments to new customers and increased volume in food and beverage packaging.

EBIT for the Plastic Packaging segment for the first quarter of 2005 was \$5.4 million, an increase of \$0.3 million, or 6 percent, over the comparable period in 2004. Excluding changes in foreign currency exchange rates, which increased EBIT by \$0.3 million for the quarter, EBIT was flat. During the first quarter of 2005, increased sales in specialty chemical packaging were offset by a less favorable mix of products in food and beverage packaging and a lag in recovery of resin price increases.

Liquidity and Financial Position

Net cash provided by operating activities was \$10.9 million for the first quarter of 2005, a decrease of \$32.2 million from the first quarter of 2004. The decrease primarily reflects receipt of a \$17.4 million income tax refund and \$6.4 million from the termination of interest rate swaps in the first quarter of 2004, and an increase in working capital outflows in 2005.

Net cash used in investing activities in the first quarter of 2005 was \$6.8 million compared to net cash used in investing activities of \$11.1 million in the first quarter of 2004. The cash used in investing activities in the first quarter of 2005 and 2004 was primarily used for capital expenditures.

Net cash used in financing activities in the first quarter of 2005 was \$36.9 million, compared to net cash provided by financing activities of \$49.9 million in the first quarter of 2004. During the first quarter of 2005, we made debt repayments of \$62.9 million, offset in part by an increase in borrowings on our credit line of \$29.7 million. During the first quarter of 2004, we completed the sale of 3.65 million shares of our common stock at a public offering price of \$24 per share. Our net proceeds from the sale of these shares, after deducting discounts, commissions and estimated expenses, were approximately \$82.6 million. Cash provided by the common stock offering was partially offset by debt repayments. We

paid cash dividends of \$4.3 million, or \$0.22 per share, in the first quarter of 2005, and \$3.4 million, or \$0.22 per share, in the first quarter of 2004.

Our debt at April 3, 2005, was \$387.1 million, down \$41.8 million compared to January 2, 2005. Our debt-to-capital ratio was 36 percent as of April 3, 2005, compared to 38 percent at January 2, 2005. (Capital consists of debt and stockholders' equity.) The change in the ratio from year-end 2004 to first quarter-end 2005 is primarily due to the redemption of debt which matured during the first quarter of 2005.

We were in compliance with all of our debt covenants as of the end of the first quarter of 2005. We believe we will have adequate financial resources to support anticipated short-term and long-term capital needs and commitments.

Critical Accounting Policies

Our consolidated financial statements have been prepared by management in accordance with GAAP. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenue and expenses. We believe that the estimates, assumptions and judgments described in the section "Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies" of our most recent Annual Report on Form 10-K have the greatest potential impact on our financial statements, so we consider these to be our critical accounting policies. These policies include our accounting for: (a) goodwill and other long-lived asset valuations; (b) environmental and other contingencies; (c) pension and other postretirement employee benefits; and (d) deferred tax assets. Because of the uncertainty inherent in these matters, reported results could have been materially different using a different set of assumptions and estimates for these critical accounting policies. We believe that the consistent application of these policies enables us to provide readers of our financial statements with useful and reliable information about our operating results and financial condition. There has been no significant change in these policies, or the estimates used in the application of the policies, since our 2004 fiscal year end.

Environmental

See Note 8 to the Consolidated Financial Statements for additional information on environmental matters.

New Accounting Pronouncements

See Note 1 to the Consolidated Financial Statements.

Seasonality

Our Paperboard Packaging segment competes in several end-use markets, such as alcoholic drinks, confectioneries, cosmetics and fragrances, that are seasonal in nature. As a result, our Paperboard Packaging segment earnings stream is seasonal, with peak operational activity during the third and fourth quarters of the year. Our Plastic Packaging segment's markets include beverage and agrochemical markets in the southern hemisphere that are seasonal in nature. As a result, our Plastic

Packaging segment earnings stream is also seasonal, with peak operational activity during the first and fourth quarters of the year.

Forward-Looking Statements

Forward-looking statements in the foregoing Management's Discussion and Analysis of Financial Condition and Results of Operations include statements that are identified by the use of words or phrases including, but not limited to, the following: "will likely result," "expected to," "will continue," "is anticipated," "estimated," "project," "believe," "expect," and words or phrases of similar import. Changes in the following important factors, among others, could cause our actual results to differ materially from those expressed in any such forward-looking statements: competitive products and pricing; production costs, particularly for raw materials such as folding carton and plastics materials; fluctuations in demand; possible recessionary trends in United States and global economies; governmental policies and regulations; interest rates; fluctuations in currency translation rates; our ability to remain in compliance with our debt covenants; and other risks that are detailed from time to time in reports we file with the SEC.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

There are no material changes to the disclosure on this matter made in our Annual Report on Form 10-K for the year ended January 2, 2005.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management timely. An evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of April 3, 2005. Based upon that evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of April 3, 2005.

There has been no change in our internal control over financial reporting during the first quarter of fiscal year 2005 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Reference is made to Note 8 of the Notes to Consolidated Financial Statements included herein.

Item 6. Exhibits

(a) Exhibits:

- 31.1 Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certifications of CEO and CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CHESAPEAKE CORPORATION
(Registrant)

Date: May 2, 2005

BY: /s/ Thomas G. Hayes
Thomas G. Hayes
Controller
(Principal Accounting Officer)