PEYTO

Exploration & Development Corp.

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Interim Report
for the six months ended June 30, 2002

Highlights

	Three Months Ended June 30			Six Months Ended June 30		
	2002	2001	% Change	**2002**	2001	% Change
Operations						
Production						
Natural gas (mcf/d)	**38,194**	15,502	*146*	**36,630**	**14,603**	*151*
Oil & NGL (bbl/d)	**1,512**	621	*143*	**1,461**	**547**	*167*
Barrels of oil equivalent (boe/d @ 6:1)	**7,878**	3,205	*146*	**7,566**	**2,981**	*154*
Average product prices						
Natural gas ($/mcf)	**4.43**	7.02	*(37)*	**4.44**	8.55	*(48)*
Oil & NGL ($/bbl)	**29.95**	36.82	*(19)*	**27.30**	38.14	*(28)*
Average operating expenses ($/boe)	**1.67**	1.55	*8*	**1.56**	1.47	*6*
Financial ($000)						
Revenue	**19,530**	11,987	*63*	**36,680**	26,373	*39*
Royalties (net of ARTC)	**4,197**	2,667	*57*	**7,669**	6,547	*17*
Funds from operations	**13,185**	8,160	*62*	**25,284**	17,841	*42*
Net earnings	**6,362**	4,450	*43*	**12,288**	9,068	*36*
Capital expenditures	**28,270**	18,641	*52*	**50,819**	39,454	*29*
As at June 30						
Debt, including working capital deficit				**86,953**	41,506	*109*
Shareholders’ equity				**53,685**	30,342	*77*
Total assets				**178,900**	96,493	*85*
Common shares outstanding (000)				**43,143**	41,813	*3*
Weighted average common shares outstanding (000)				**42,642**	41,338	*3*
Per share data ($/share)						
Funds from operations						
Basic	**0.31**	0.20	*55*	**0.59**	0.43	*37*
Diluted	**0.30**	0.19	*58*	**0.58**	0.42	*38*
Earnings						
Basic	**0.15**	0.11	*36*	**0.29**	0.22	*32*
Diluted	**0.14**	0.10	*40*	**0.28**	0.21	*33*

Report from the president

PEYTO Exploration & Development Corp. is pleased to present its second quarter financial and operating results for the period ended June 30, 2002.

Quarterly Review

In the second quarter of 2002, Peyto achieved corporate records for production, cash flow and earnings on both an absolute and a per share basis. Gas and liquids production per share for the quarter increased 139% and 136% respectively, over the same period in 2001. Daily production averaged 38.2 mmcf of natural gas and 1,512 barrels of oil and natural gas liquids. Despite a 37% drop in natural gas prices, our production gains and lower total costs per barrel of oil equivalent ("boe", natural gas converted on a 6:1 basis throughout) increased quarterly cash flow from $8.2 million in 2001 to $13.2 million in 2002. Quarterly earnings increased from $4.5 million in 2001 to $6.4 million in 2002. Product prices averaged $4.43 per mcf for gas and $29.95 per barrel for oil and natural gas liquids. Operating costs averaged $1.67 per boe. Our total cost structure (production, interest and general and administrative expense) decreased 25% from $3.81 per boe to $2.86 per boe. Capital expenditures for the quarter totaled $28.3 million. Drilling projects continued at record levels representing 67% of the total capital spent during the quarter. The expansion of our Sundance gas plant was completed on schedule at the end of the quarter. The capital spent on this expansion in the quarter was $7.1 million or 25% of the total.

Activity Update

Since the beginning of the year, Peyto has drilled or re-entered thirty five gross (30.7 net) wells targeting gas at depths greater than 2,200 meters. All of these wells have been successful. Our plan is to keep three drilling rigs active in the greater Sundance area for the remainder of the year. Two more compressors, each with capacity of 12 mmcf/d, have been ordered and are scheduled for installation in October and December of this year. Exploration and development activity is now underway in our new area.

Cardium Reserve Audit

In order to independently address questions from those unfamiliar with the greater Edson Cardium play, Peyto retained Gilbert Laustsen Jung Associates Ltd. ("GLJ") to conduct a reserve evaluation. The July 1, 2002 GLJ Evaluation ("GLJ Report") included all the wells that made up Peyto's proven producing Cardium reserves in the Sundance area and had an effective date of December 31, 2001. GLJ evaluated 75% of our total proven producing reserves, based on the year end 2001 Paddock Lindstrom & Associates Ltd. report dated January 21, 2002 ("Paddock Report"). The GLJ evaluation assigned proven producing company sales gas reserves of 71,470 mmcf. The proven producing reserves forecast in the GLJ Report were 2.7% lower than what had been assigned in the Paddock Report and had an average producing life of 36.5 years. The net present value (before income tax, discounted at 10%, GLJ July 1, 2002 price forecast) of the GLJ report was $162.3 million which was 1% higher than the value assigned in the Paddock Report. In our opinion, this reserve audit confirms our belief that our Cardium reserve assignments have been accurate.

Outlook

Our low risk approach to generating high return projects which focus on finding and developing gas reserves has created significant shareholder value. Production per share has increased by over 50% and the value of that production (based on the gas futures market) has increased by 20% since we embarked on our exploration and development plan at the beginning of 2002. Significant production growth for the balance of the year is on track. We encourage you to visit Peyto's website at www.peyto.com where you will find a current presentation, financial and historical news releases and an updated insider trading summary.

Don T. Gray, P.Eng.
President and Chief Executive Officer
August 19, 2002

This report, or any part of it, may include comments that do not refer strictly to historical results or actions and may constitute forward-looking statements. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Corporation or of the industry to be materially different from any results, performance or achievements expressed or implied by such forward-looking statements. Such risks, uncertainties and other factors include general and industry economic and business conditions which, among other things, affect the demand for the commodities produced by the Corporation, competitive factors and industry capacity, the availability of personnel to manage the Corporation and manage and deliver the commodities produced, the ability of the Corporation to finance and implement its business strategy, changes in, or the failure to comply with, government law and regulations (especially relating to health, safety and environment), weather and other such risks as may be identified in this report or in other published documents. Accordingly, there is no certainty that the Corporation's plans will be achieved.

Management's discussion and analysis

Management's discussion and analysis of financial conditions and results of operations should be read in conjunction with the unaudited interim financial statements for the six months ended June 30, 2002 and the audited consolidated financial statements for the year ended December 31, 2001.

Gross revenues totaled $19.5 million during the second quarter of 2002 (Q2 2001 - $11.9 million) and $36.7 million for the first six months of 2002 (first half 2001 - $26.4 million). These increases of 63 percent and 39 percent, respectively, are a result of higher production volumes despite significantly lower commodity prices. The price of natural gas averaged $4.43 per mcf for the second quarter of 2002 (Q2 2001 - $7.02 per mcf) and $4.44 per mcf for the first six months of 2002 (first half 2001 - $8.55 per mcf). Oil and natural gas liquids prices averaged $29.95 for the second quarter of 2002 (Q2 2001 - $36.82 per barrel) and $27.30 per barrel for the first six months of 2002 (first half 2001 - $38.14 per barrel).

Natural gas production for the quarter increased 146 percent to 38.2 mmcf per day from 15.5 mmcf per day in the same quarter of 2001. Oil and natural gas liquids production increased 143 percent to 1,512 bbl/d in 2002 from 621 bbl/d in 2001. Production for the first half averaged 7,566 barrels of oil equivalent ("boe", natural gas converted on a 6:1 basis) per day up 154 percent from 2,981 boe per day for the first six months of 2001. All references to barrel of oil equivalent are now being reported on the accepted energy equivalent of six thousand cubic feet of natural gas being equivalent to one barrel of oil. All historical figures have been adjusted accordingly.

The 2002 royalties to date, net of Alberta Royalty Tax Credit (ARTC), increased 17 percent to $7.7 million from $6.5 million in 2001. The 2002 average royalty rate, before ARTC, was 22 percent unchanged from the same period in 2001.

Due to increased production volumes, operating costs for the six month period rose to $2.1 million in 2002 from $793,000 in 2001. On a barrel of oil equivalent basis, operating costs were $1.56 per boe in 2002 compared to $1.47 per boe in 2001. Operating costs are comprised of field expenses and natural gas transportation costs net of income generated by the processing and gathering of joint venture gas.

Net general and administrative expenses increased by 5 percent to $392,000 in the first half of 2002 from $372,000 in 2001 due primarily to the commitment fee of $190,000 on Peyto's $100 million line of credit which was partially offset by an increase in overhead recoveries associated with the capital program. On a boe basis, net general and administrative expenses decreased by 59 percent to $0.29 per boe in 2002 from $0.69 per boe in 2001.

Financing charges for the first half of 2002 were $1.0 million up 37 percent from $754,000 in 2001. The increase was due to higher debt levels associated with Peyto's aggressive 2002 capital program. On a per boe basis, interest charges were down 46 percent from $1.40 per boe in 2001 to $0.75 per boe in 2002.

Depreciation, depletion and site restoration expenses were $4.8 million in the first half of 2002 compared to $2.3 million for the same period in 2001 as a direct result of Peyto's increased asset base and production volumes. On a per boe basis, the average depreciation, depletion and site restoration rate decreased to $3.53 in 2002 from $4.32 in 2001 as a result of successful reserve additions.

The 2002 provision for future income taxes increased to $8.2 million compared to $6.4 million in 2001 as a result of increased profitability in Peyto due to higher production volumes.

Funds from operations for the first half of 2002 were $25.3 million compared with $17.8 million in 2001. This 42% increase was the result of increased production volumes despite significantly lower commodity prices. On a per share basis, the first half of 2002 resulted in funds from operations of $0.59 per share versus $0.43 per share in 2001. The decreased natural gas and liquids prices resulted in a field netback for the period of $19.62 per boe in 2002 compared to $35.28 per boe in 2001. Net earnings in 2002 were $12.3 million or $0.29 per share compared with $9.1 million in 2001 or $0.22 per share.

At June 30, 2002, the Company had a working capital deficiency (including the revolving demand loan (see Note 2 to financial statements)) of $86.9 million resulting in a debt to running cash flow ratio of approximately 1.6:1. Peyto's first half $50.8 million capital program was funded through cash flow and working capital. Peyto currently has a $100 million line of credit.

Quarterly information

	2002		2001		
	Q2	Q1	Q4	Q3	Q2
Operations					
Production					
Natural gas (mcf/d)	**38,194**	35,049	30,175	22,431	15,502
Oil & NGLs (bbl/d)	**1,512**	1,409	1,222	815	621
Barrels of oil equivalent (boe/d @ 6:1)	**7,878**	7,250	6,251	4,553	3,205
Average product prices					
Natural gas ($/mcf)	**4.43**	4.46	4.32	4.32	7.02
Oil & NGLs ($/bbl)	**29.95**	24.42	23.84	30.48	36.82
Average operating expenses ($/boe)	**1.67**	1.44	1.57	0.93	1.55
Field netback ($/boe)	**19.72**	19.52	19.72	20.83	30.41
Financial ($000)					
Revenue	**19,530**	17,150	14,679	11,195	11,987
Royalties (net of ARTC)	**4,197**	3,472	2,437	2,082	2,667
Funds from operations	**13,185**	12,098	9,546	8,115	8,160
Net earnings	**6,362**	5,925	4,969	3,486	4,450
Capital expenditures	**28,270**	22,549	22,029	18,472	18,641
Common shares outstanding (000)	**43,143**	42,976	41,999	41,816	41,813
Per share data ($/share)					
Funds from operations					
Basic	**0.31**	0.29	0.23	0.19	0.20
Diluted	**0.30**	0.28	0.22	0.19	0.19
Earnings					
Basic	**0.15**	0.14	0.12	0.08	0.11
Diluted	**0.14**	0.14	0.12	0.08	0.10

Financial statements

Balance Sheet

As at		June 30 2002 (unaudited)		December 31 2001 (audited)
Assets				
Current assets				
Cash	**$**	**31,177**	$	1,220
Accounts receivable		**10,622,674**		8,245,973
Prepaids		**492,360**		526,291
		11,146,211		8,773,484
Property, plant and equipment *(Note 2)*		**167,754,148**		121,700,469
	$	**178,900,359**	$	130,473,953
Liabilities and Shareholders' Equity				
Current				
Accounts payable and accrued liabilities	**$**	**18,680,746**	$	13,113,286
Capital taxes payable		**166,534**		245,360
Revolving demand loan *(Note 3)*		**79,252,104**		58,945,472
		98,099,384		72,304,118
Site restoration provision		**264,013**		202,322
Future income taxes		**26,852,117**		18,349,387
		27,116,130		18,551,709
Shareholders' equity				
Share capital *(Note 4)*		**18,115,532**		16,336,504
Retained earnings		**35,569,313**		23,281,622
		53,684,845		39,618,126
	$	**178,900,359**	$	130,473,953

Financial statements

Statements of Earnings and Retained Earnings
(unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
	2002	2001	**2002**	2001
Revenue				
Oil and gas sales, net	**$ 15,332,881**	$ 9,320,298	**$ 29,011,197**	$ 19,825,846
Interest and other income	**-**	6,504	**-**	10,284
	15,332,881	9,326,802	**29,011,197**	19,836,130
Expenses				
Operating	**1,198,725**	452,336	**2,138,314**	793,457
General and administrative	**289,878**	206,858	**392,278**	372,377
Interest	**563,262**	459,050	**1,030,318**	754,290
Depletion, depreciation and site restoration	**2,552,474**	1,128,867	**4,827,404**	2,330,866
	4,604,339	2,247,111	**8,388,314**	4,250,990
Earnings before taxes	**10,728,542**	7,079,691	**20,622,883**	15,585,140
Future income tax expense	**(4,270,598)**	(2,581,761)	**(8,168,469)**	(6,442,214)
Capital tax expense	**(95,722)**	(48,281)	**(166,723)**	(75,208)
Earnings for the period	**6,362,222**	4,449,649	**12,287,691**	9,067,718
Retained earnings, beginning of period	**29,207,091**	10,376,120	**23,281,622**	5,758,051
Retained earnings, end of period	**$ 35,569,313**	$ 14,825,769	**$ 35,569,313**	$ 14,825,769
Earnings per share				
Basic	**$0.15**	$0.11	**$0.29**	$0.22
Diluted	**$0.14**	$0.10	**$0.28**	$0.21

Financial statements

Statements of Cash Flows
(unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
	2002	2001	**2002**	2001
Cash provided by (used in)				
Operating Activities				
Earnings for the period	**$ 6,362,222**	$ 4,449,649	**$ 12,287,691**	$ 9,067,718
Items not requiring cash:				
Future income taxes	**4,270,598**	2,581,761	**8,168,469**	6,442,214
Depletion, depreciation and site restoration	**2,552,474**	1,128,867	**4,827,404**	2,330,866
Funds from operations	**13,185,294**	8,160,277	**25,283,564**	17,840,798
Change in non-cash working capital related to operating activities	**2,141,272**	4,185,652	**242,575**	7,184,497
	15,326,566	12,345,929	**25,526,139**	25,025,295
Financing Activities				
Issue of common shares, net of costs	**107,460**	62,387	**2,113,289**	932,030
Increase in revolving demand loan	**20,031,829**	10,807,688	**20,306,632**	19,986,022
	20,139,289	10,870,075	**22,419,921**	20,918,052
Investing Activities				
Additions to property, plant and equipment	**(28,270,191)**	(18,641,261)	**(50,819,392)**	(39,453,933)
Change in non-cash working capital related to investing activities	**(7,165,665)**	(4,608,819)	**2,903,289**	(6,456,085)
	(35,435,856)	(23,250,080)	**(47,916,103)**	(45,910,018)
Net increase (decrease) in cash	**29,999**	(34,076)	**29,957**	33,329
Cash, beginning of period	**1,178**	120,432	**1,220**	53,027
Cash, end of period	**$ 31,177**	$ 86,356	**$ 31,177**	$ 86,356
Funds from operations per share				
Basic	**$0.31**	$0.20	**$0.59**	$0.43
Diluted	**$0.30**	$0.19	**$0.58**	$0.42

Notes to financial statements

1. Accounting Principles

The financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles. These interim financial statements have been prepared on the same basis as the audited financial statements as at and for the year ended December 31, 2001. Management's discussion and analysis of financial conditions and results of operations should be read in conjunction with the unaudited interim financial statements for the six months ended June 30, 2002 and the audited financial statements for the year ended December 31, 2001.

Effective January 1, 2002, the Company adopted the CICA recommendations for measurement standards for stock-based compensation plans. The standard allows a choice of either valuing stock options at fair value at inception and recording this cost as compensation or charging equity when the options are exercised. Peyto has determined it will not apply the fair value based approach and will continue to follow the equity approach.

2. Property, Plant and Equipment

	2002	2001
	$	$
Property, plant and equipment	**181,469,335**	130,693,300
Office furniture and equipment	**263,704**	220,347
	181,733,039	130,913,647
Accumulated depletion and depreciation	**(13,978,891)**	(9,213,178)
	167,754,148	121,700,469

At June 30, 2002, costs of $15,188,000 (June 30, 2001 - $8,250,000) related to undeveloped land have been excluded from the depreciation calculation. No general and administration expenses relating to the Company's exploration, development and acquisition programs were capitalized.

3. Revolving Demand Loan

The Company has a revolving credit facility to a maximum of $100,000,000. Outstanding amounts on this facility bear interest at bank prime and are due on demand. A General Security Agreement with a floating charge on land registered in Alberta is held as collateral by the bank.

Effective January 1, 2002 the Company adopted the recommendations of the Emerging Issues Committee of the Canadian Institute of Chartered Accountants concerning the presentation of revolving demand loans. These new recommendations require that the classification of debt on the balance sheet be based upon the facts existing at the balance sheet date rather than expectations. Prior to the adoption of the new recommendations, the Company presented the demand loan as long term on the basis that the bank had indicated it was not its intention to call for repayment within one year provided there was no adverse change in the financial position of the Company.

While the bank has confirmed that it is not its intention to call for repayment of this loan before June 30, 2003, provided there is no adverse change in the financial position of the Company, this loan is demand in nature and pursuant to the CICA pronouncement is presented as a current liability.

4. Share Capital

Authorized

Unlimited number of common voting shares
Unlimited number of preferred shares, issuable in series

Issued - Common shares

	Number of Shares	Amount $
Balance, December 31, 2001	41,999,731	16,336,504
Exercise of stock options	1,142,890	2,152,973
Tax benefits transferred to shareholders	—	(350,976)
Share issue costs, net of associated tax benefits	—	(22,969)
Balance, June 30, 2002	43,142,621	18,115,532

Stock Options

The Company has a director and employee stock option plan. The number of common shares reserved for issuance at any one time shall not exceed 4,314,262 shares subject to shareholder and regulatory approval. The exercise price of an option is set at the market price of the common shares at the date of grant. Each option vests over a three year period and has a term of 5 years.

	As at June 30, 2002		As at June 30, 2001	
	Options	**Weighted - Average Exercise Price**	**Options**	**Weighted-Average Exercise Price**
Opening	**3,310,333**	**$2.39**	2,987,000	$0.63
Granted	**1,306,224**	**$5.17**	2,655,334	$2.65
Exercised	**(1,142,890)**	**$1.88**	(2,014,333)	$0.48
Cancelled	**(50,000)**	**$5.51**	(754,334)	$1.82
Closing	**3,423,667**	**$3.57**	2,873,667	$2.29

Per Share Amounts

Earnings per share and funds from operations per share have been calculated based upon the weighted average number of common shares outstanding during the year of 42,642,082 (2001 – 41,338,377). Diluted per share amounts are calculated using the treasury stock method. The weighted average number of common shares used to determine diluted per share amounts in 2002 was 43,985,521 (2001 – 42,574,836).

5. Financial Instruments

Financial instruments of the Company consist of cash, accounts receivable, accounts payable and accrued liabilities and a revolving demand loan. As at June 30, 2002 there are no significant differences between their carrying values and their estimated market values.

The Company is a party to certain off balance sheet derivative financial instruments, including fixed price contracts. The Company enters into these contracts for the purpose of protecting a portion of its future earnings and cash flows from operations from the volatility of natural gas commodity prices by locking in a minimum and maximum forward price.

A summary of contracts outstanding in respect to the hedging activities at June 30, 2002 were as follows:

Period Hedged	**Type**	**Daily Volume**	**Floor**	**Ceiling**
April, 2002	Fixed	14,000 GJ	$4.41/GJ	
April, 2002	Fixed	2,000 GJ	$4.45/GJ	
May, 2002	Fixed	10,000 GJ	$4.43/GJ	
May, 2002	Fixed	2,000 GJ	$4.46/GJ	
June, 2002	Fixed	4,000 GJ	$4.68/GJ	
August, 2002	Fixed	4,000 GJ	$2.61/GJ	
September, 2002	Fixed	4,000 GJ	$3.00/GJ	
September, 2002	Fixed	6,000 GJ	$3.31/GJ	
September, 2002	Fixed	8,000 GJ	$3.26/GJ	
October, 2002	Fixed	4,000 GJ	$3.48/GJ	
October, 2002	Fixed	6,000 GJ	$3.31/GJ	
October, 2002	Fixed	8,000 GJ	$3.26/GJ	
April 1, 2002 to Nov. 1, 2002	Costless collar	3,500 GJ	$3.50/GJ	$5.75/GJ
June 1, 2002 to Nov. 1, 2002	Costless collar	3,500 GJ	$3.75/GJ	$6.20/GJ
Nov. 1, 2002 to March 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$7.00/GJ
Nov. 1, 2002 to March 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$6.60/GJ
Nov. 1, 2002 to March 31, 2003	Costless collar	6,000 GJ	$3.50/GJ	$6.70/GJ
April 1 to October 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$6.85/GJ
April 1 to October 31, 2003	Costless collar	6,000 GJ	$3.50/GJ	$7.00/GJ

Corporate information

Officers

Don Gray
President and Chief Executive Officer

Roberto Bosdachin
Vice-President, Exploration

Lyle Skaien
Vice President, Operations

Darren Gee
Vice President, Engineering

Sandra Brick
Vice President, Finance

Stephen Chetner
Corporate Secretary

Directors

Rick Braund

Don Gray

Mike Broadfoot

Brian Craig

Stephen Chetner

John Boyd

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