Management’s discussion and analysis

This Management's Discussion and Analysis (“MD&A”) should be read in conjunction with the audited financial statements of Peyto Exploration & Development Corp. (“Peyto” or the “Company”) for the years ended December 31, 2018 and 2017. The financial statements have been prepared in accordance with the International Accounting Standards Board’s (“IASB”) most current International Financial Reporting Standards (“IFRS” or “GAAP”) and International Accounting Standards (“IAS”).

This discussion provides management's analysis of Peyto's historical financial and operating results and provides estimates of Peyto's future financial and operating performance based on information currently available. Actual results will vary from estimates and the variances may be significant. Readers should be aware that historical results are not necessarily indicative of future performance. This MD&A was prepared using information that is current as of March 5, 2019. Additional information about Peyto, including the most recently filed annual information form is available at www.sedar.com and on Peyto’s website at www.peyto.com.

This MD&A contains certain forward-looking statements or information (“forward-looking statements”) as defined by applicable securities laws that involve substantial known and unknown risks and uncertainties, many of which are beyond Peyto's control. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. The use of any of the words "plan", "expect", "prospective", "project", "intend", "believe", "should", "anticipate", "estimate", or other similar words or statements that certain events "may" or "will" occur are intended to identify forward-looking statements. The projections, estimates and beliefs contained in such forward-looking statements are based on management's estimates, opinions, and assumptions at the time the statements were made, including assumptions relating to: the impact of economic conditions in North America and globally; industry conditions; changes in laws and regulations including, without limitation, the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced; increased competition; the adequacy of the Company's critical accounting estimates; the availability of qualified operating or management personnel; fluctuations in commodity prices, foreign exchange or interest rates; stock market volatility and fluctuations in market valuations of companies with respect to announced transactions and the final valuations thereof; results of exploration and testing activities; and the ability to obtain required approvals and extensions from regulatory authorities. Management of the Company believes the expectations reflected in those forward-looking statements are reasonable, but no assurances can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits that Peyto will derive from them. As such, undue reliance should not be placed on forward-looking statements. Forward-looking statements contained herein include, but are not limited to, statements regarding: expected royalty rate, earnings, cash flow and revenue fluctuations; the Company's expectation that funds generated from operations, together with credit facility borrowings, are sufficient; the expectation that the majority of the Company's capital program will involve drilling, completing and tying-in of lower risk development gas wells; the Company's risk management; the Company's critical accounting estimates; and the ongoing evaluation of the impact of IFRS 16 on the Company's financial statements.

The forward-looking statements contained herein are subject to numerous known and unknown risks and uncertainties that may cause Peyto's actual financial results, performance or achievement in future periods to differ materially from those expressed in, or implied by, these forward-looking statements, including but not limited to, risks associated with: imprecision of reserves estimates; competition from other industry participants; failure to secure required equipment; changes in general global economic conditions including, without limitations, the economic conditions in North America; increased competition; the lack of availability of qualified operating or management personnel; fluctuations in commodity prices, foreign exchange or interest rates; environmental risks; changes in laws and regulations including, without limitation, the adoption of new environmental and tax laws and regulations and changes in how they are interpreted and enforced; the results of exploration and development drilling and related activities; the ability to access sufficient capital from internal and external sources; and stock market volatility. Readers are encouraged to review the material risks discussed in Peyto's annual information form for the year ended December 31, 2017 under the heading "Risk Factors" and herein under the heading "Risk Management".

The Company cautions that the foregoing list of assumptions, risks and uncertainties is not exhaustive. Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Peyto's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits Peyto will derive there from. The forward-looking statements contained in this MD&A speak only as of the date hereof and Peyto does not assume any obligation to publicly update or revise them to reflect new information, future events or circumstances or otherwise, except as may be required pursuant to applicable securities laws.

All references are to Canadian dollars unless otherwise indicated. Natural gas liquids volumes are recorded in barrels of oil (bbl) and are converted to a thousand cubic feet equivalent (mcfe) using a ratio of six (6) thousand cubic feet to one (1) barrel of oil (bbl). Natural gas volumes recorded in thousand cubic feet (mcf) are converted to barrels of oil equivalent (boe) using the ratio of six (6) thousand cubic feet to one (1) barrel of oil (bbl). Boe may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf:1 bbl is based in an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, given that the value ratio based on the current price of oil as compared with natural gas is significantly different from the energy equivalent of six to one, utilizing a boe conversion ratio of 6 mcf:1 bbl may be misleading as an indication of value.

OVERVIEW

Peyto is a Canadian energy company involved in the development and production of natural gas and oil & natural gas liquids in Alberta's deep basin. As at December 31, 2018, the Company's total Proved plus Probable reserves were 4.8 trillion cubic feet equivalent (803 million barrels of oil equivalent) as evaluated by its independent petroleum engineers. Production is weighted approximately 88 per cent to natural gas and 12 per cent to oil & natural gas liquids.

The Peyto model is designed to deliver a superior total return with growth in value, assets, production and income, all on a debt adjusted per share basis. The model is built around three key strategies:

- Use technical expertise to achieve the best return on capital employed through the development of internally generated drilling projects.
- Build an asset base which is made up of high quality natural gas reserves.
- Over time, balance dividends paid to shareholders with earnings and cash flow, and balance funding for the capital program with cash flow, equity and available bank lines.

Operating results over the last twenty years indicate that these strategies have been successfully implemented. This business model makes Peyto a truly unique energy company.

ANNUAL FINANCIAL INFORMATION

The following is a summary of selected financial information of the Company for the periods indicated. Reference should be made to the audited consolidated financial statements of the Company, which are available at www.sedar.com.

Year Ended December 31 ($000 except per share amounts)	**2018**	2017	2016
Total revenue and realized hedging gains (before royalties)	**658,906**	760,956	678,388
Funds from operations	**473,740**	573,721	514,593
Per share – basic and diluted	**2.87**	3.48	3.17
Earnings	**129,110**	176,575	112,348
Per share – basic and diluted	**0.78**	1.07	0.69
Total assets	**3,688,852**	3,844,714	3,463,089
Total long-term debt (including current portion)	**1,150,000**	1,285,000	1,070,000
Dividends per share	**0.72**	1.32	1.32

Funds from Operations

"Funds from operations" is a non-GAAP measure which represents cash flows from operating activities before changes in non-cash operating working capital and provision for future performance-based compensation. Management considers funds from operations and per share calculations of funds from operations to be key measures as they demonstrate the Company's ability to generate the cash necessary to pay dividends, repay debt and make capital investments. Management believes that by excluding the temporary impact of changes in non-cash operating working capital, funds from operations provides a useful measure of Peyto's ability to generate cash that is not subject to short-term movements in operating working capital. The most directly comparable GAAP measure is cash flows from operating activities.

QUARTERLY FINANCIAL INFORMATION

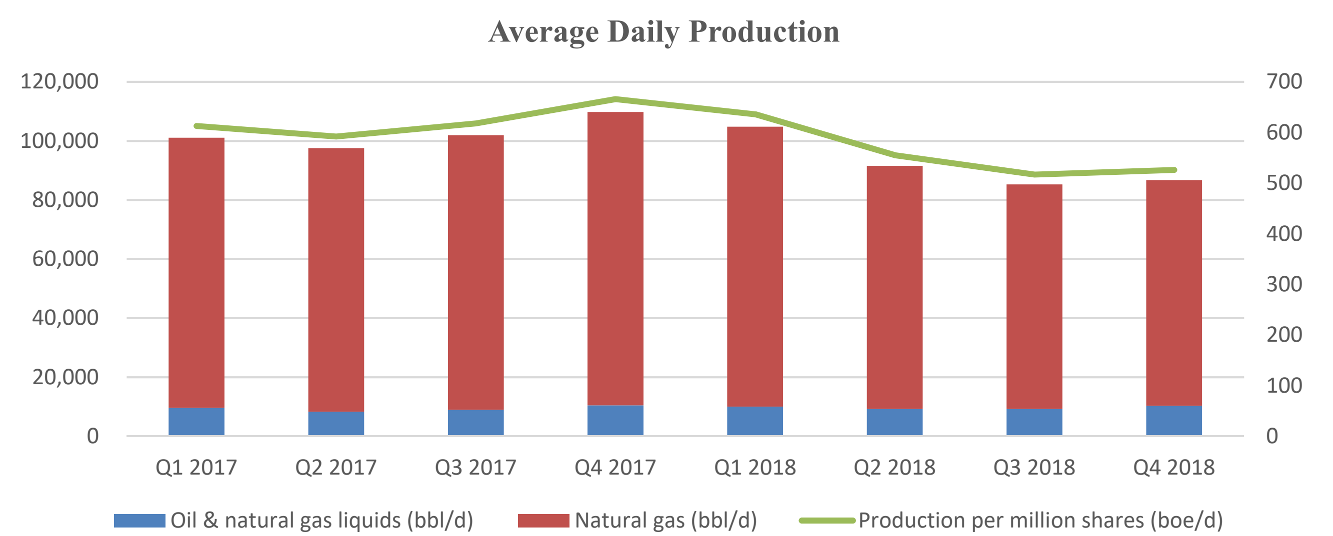
	2018				2017			
($000 except per share amounts)	**Q4**	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenue and realized hedging gains (losses) (net of royalties)	**139,308**	147,190	154,932	190,854	202,566	177,061	169,911	177,314
Funds from operations	**99,635**	109,549	115,571	148,986	161,672	139,257	133,487	139,305
Per share – basic and diluted	**0.60**	0.66	0.70	0.90	0.98	0.85	0.81	0.85
Earnings	**21,458**	29,506	30,397	47,749	51,547	44,818	39,957	40,255
Per share – basic and diluted	**0.13**	0.18	0.18	0.29	0.31	0.27	0.24	0.24
Dividends	**29,677**	29,677	29,677	29,677	54,408	54,408	54,408	54,387
Per share – basic and diluted	**0.18**	0.18	0.18	0.18	0.33	0.33	0.33	0.33

RESULTS OF OPERATIONS

Production

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Natural gas (mmcf/d)	**458.8**	595.9	**493.9**	559.7
Oil & natural gas liquids (bbl/d)	**10,273**	10,479	**9,692**	9,337
Barrels of oil equivalent (boe/d)	**86,738**	109,793	**92,012**	102,614
Thousand cubic feet equivalent (mmcfe/d)	**520.4**	658.8	**552.1**	615.7

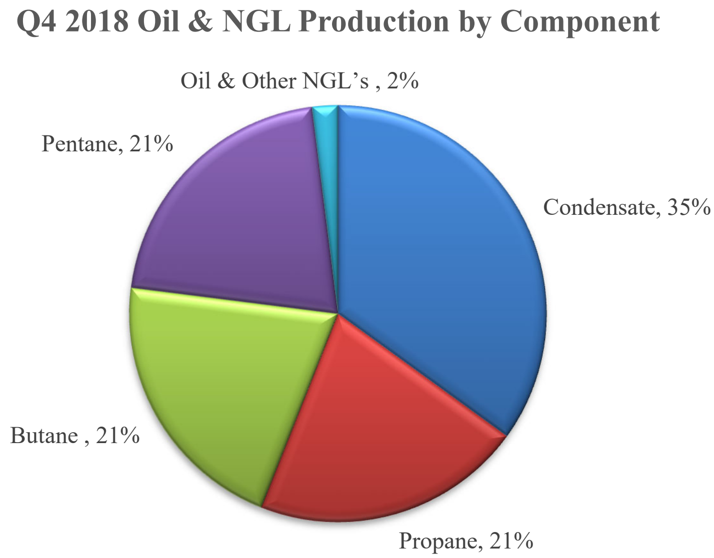
Natural gas production averaged 458.8 mmcf/d in the fourth quarter of 2018, 23 per cent lower than the 595.9 mmcf/d reported for the same period in 2017. Oil & natural gas liquids production averaged 10,273 bbl/d, a decrease of 2 per cent from 10,479 bbl/d reported in the prior year. Total fourth quarter production decreased 21 per cent from 658.8 mmcfe/d to 520.4 mmcfe/d. Production for the year decreased 10 per cent from 615.7 mmcfe/d to 552.1 mmcfe/d (102,614 boe/d to 92,012 boe/d). Production decreases are attributable to Peyto's planned reduced capital program which did not offset natural production declines.



Oil & Natural Gas Liquids Production by Component

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Condensate (bbl/d)	**3,548**	4,042	**3,370**	3,761
Propane (bbl/d)	**2,137**	1,917	**1,951**	1,477
Butane (bbl/d)	**2,161**	2,073	**2,045**	1,824
Pentane (bbl/d)	**2,112**	2,284	**2,122**	2,127
Other Oil & NGL'sbbl/d)	**315**	163	**204**	148
Oil & Natural gas liquids (bbl/d)	**10,273**	10,479	**9,692**	9,337
Barrels per million cubic feet	**22.4**	17.6	**19.6**	16.7

The liquid production to sales gas ratio increased 27 per cent from 17.6 bbl/mmcf in Q4 2017 to 22.4 bbl/mmcf in Q4 2018. On an annual basis, the liquid production to sales gas ratio increased 17 per cent. This increase was due to the addition of liquids rich production from new Cardium wells and to enhanced liquid recoveries from the deep cut processing facility.



Commodity Prices

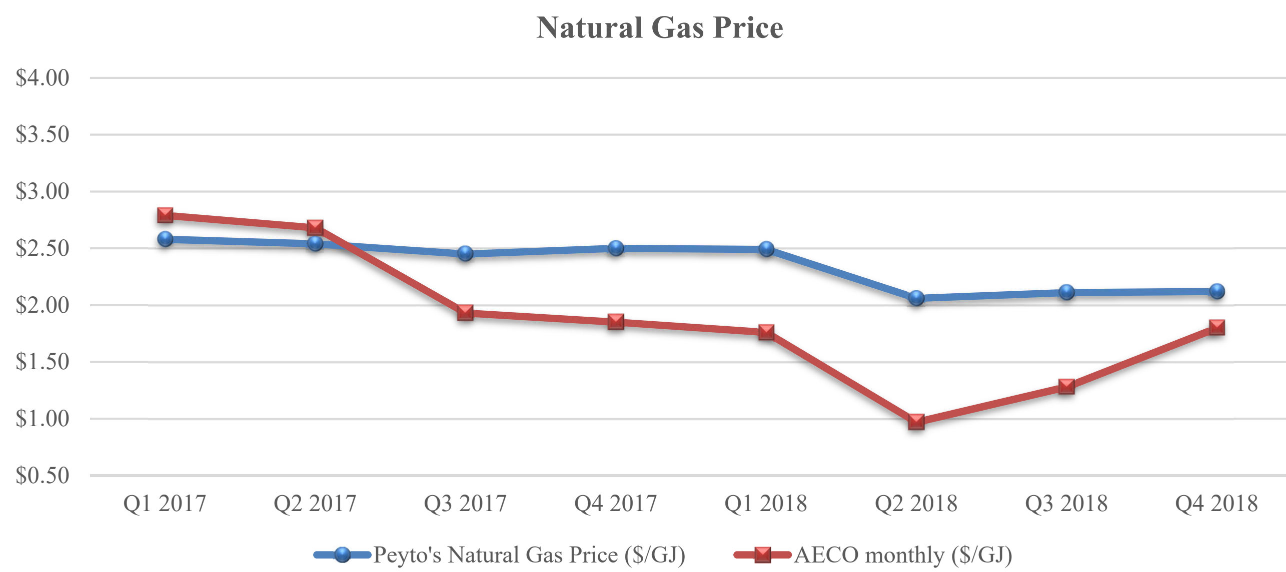
	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Oil & natural gas liquids ($/bbl)	**42.23**	56.52	**56.38**	50.02
Hedging – Oil & NGL ($/bbl)	**2.60**	-	**0.60**	-
Oil & NGL – after hedging ($/bbl)	**44.83**	56.52	**56.98**	50.02
Natural gas ($/mcf)	**2.09**	2.15	**1.68**	2.61
Hedging – gas ($/mcf)	**0.34**	0.72	**0.86**	0.28
Natural gas – after hedging ($/mcf)	**2.43**	2.87	**2.54**	2.89
Total Hedging ($/mcfe)	**3.03**	0.65	**3.27**	0.26
Total Hedging ($/boe)	**18.18**	3.89	**19.62**	1.55

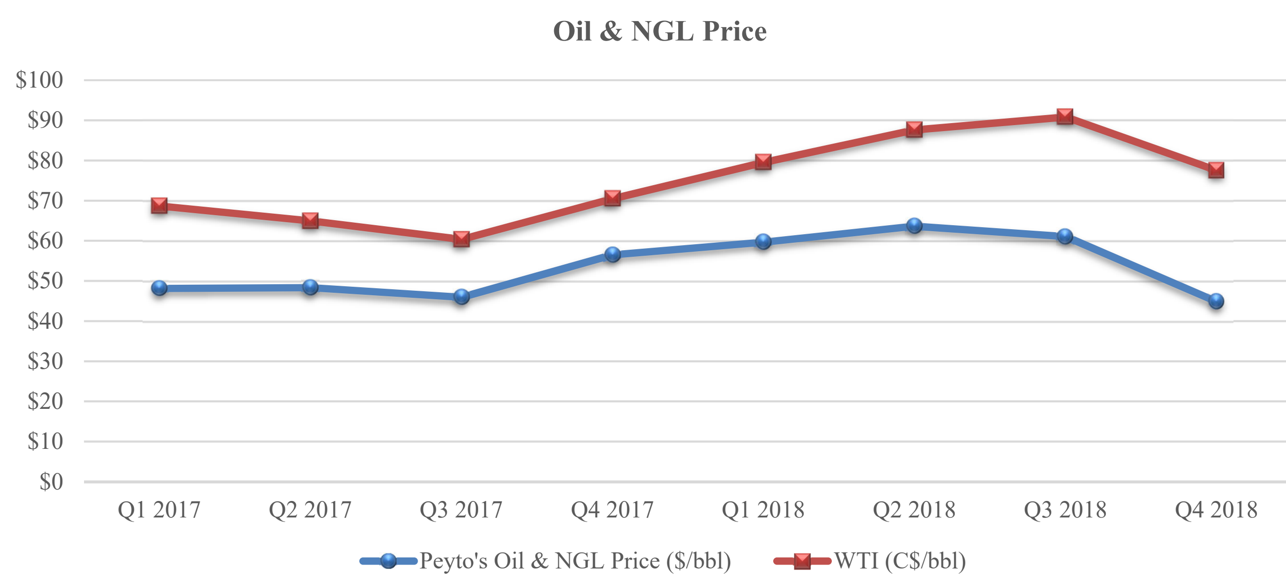
Peyto's natural gas price, before hedging, averaged $2.09/mcf during the fourth quarter of 2018, a decrease of 3 per cent from $2.15/mcf for the equivalent period in 2017. Oil & natural gas liquids prices, before hedging, averaged $42.23/bbl, a decrease of 25 per cent from $56.52/bbl a year earlier. On an annual basis, natural gas prices before hedging decreased 36 per cent from $2.61/mcf to $1.68/mcf while oil and natural gas liquids increased 14 per cent from $50.02/bbl to $56.98/bbl.

Commodity Prices by Component

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Natural gas – after hedging ($/mcf)	**2.43**	2.87	**2.54**	2.89
Natural gas – after hedging ($/GJ)	**2.12**	2.50	**2.21**	2.51
AECO monthly ($/GJ)	**1.80**	1.85	**1.45**	2.31
AECO daily ($/GJ)	**1.48**	1.60	**1.42**	2.03
Natural gas liquids ($/bbl)				
Condensate – after hedging ($/bbl)	**57.76**	67.54	**71.83**	60.20
Propane – after hedging ($/bbl)	**22.14**	34.95	**22.91**	23.16
Butane ($/bbl)	**27.71**	34.94	**38.77**	31.27
Pentane ($/bbl)	**61.34**	70.08	**78.00**	62.48
Total natural gas liquids ($/bbl)	**44.83**	56.52	**56.98**	50.02
Canadian WTI ($/bbl)	**77.54**	70.47	**83.89**	66.11

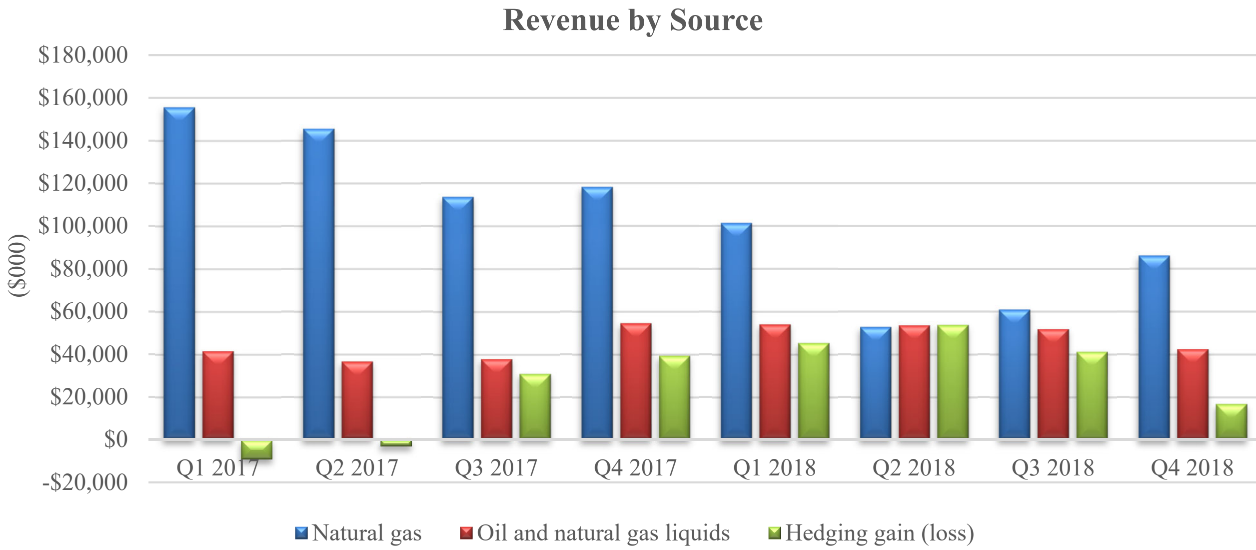
liquids prices are Peyto realized prices in Canadian dollars adjusted for fractionation and transportation.





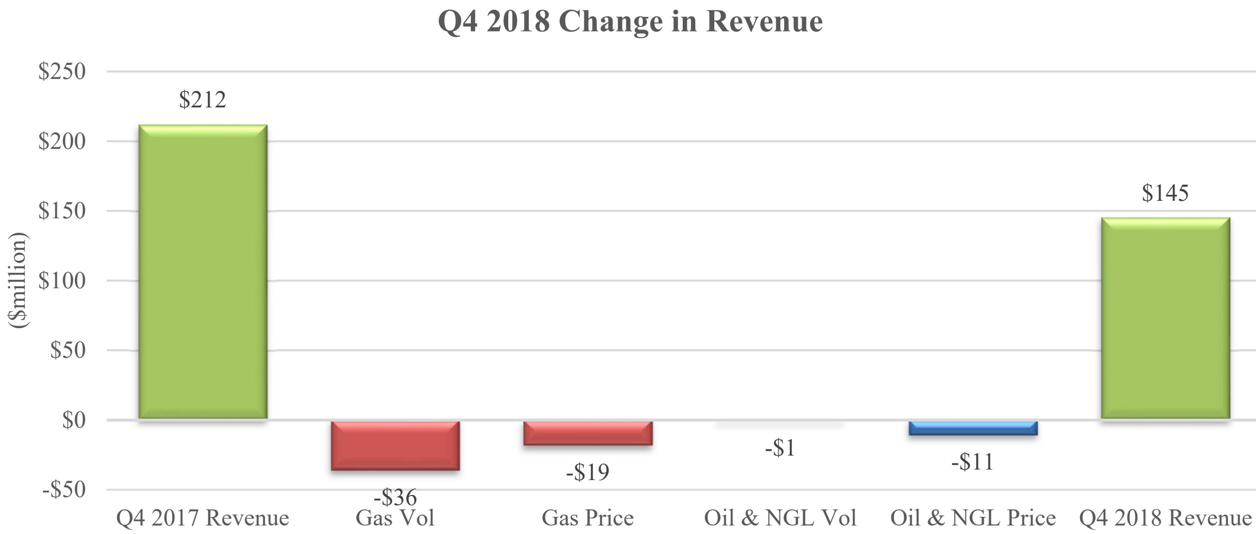
Revenue and Realized Hedging Gains

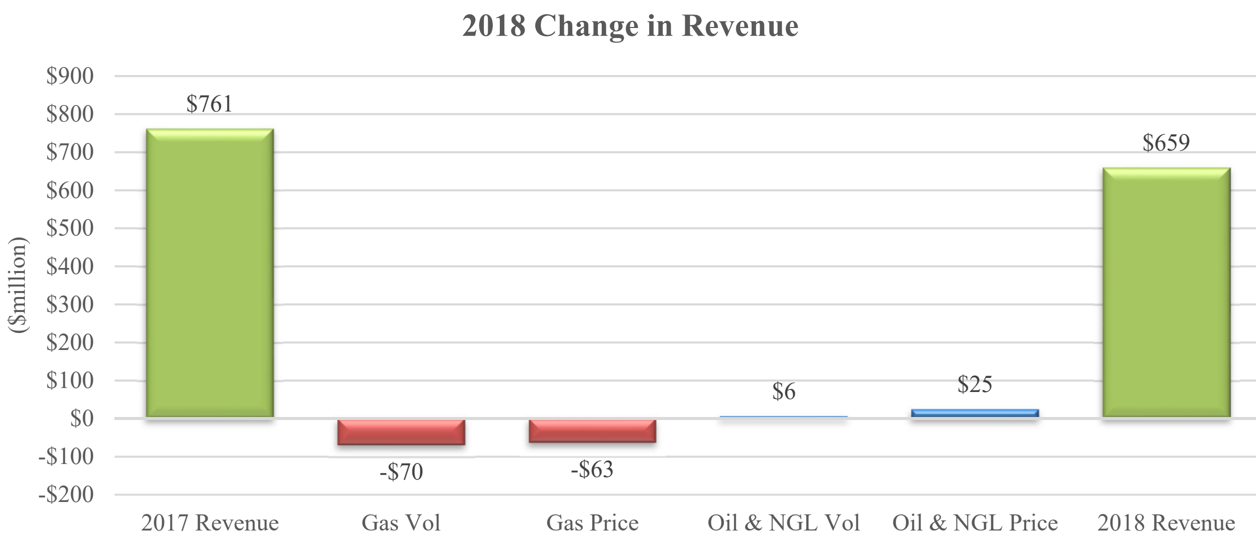
($000)	Three Months ended December 31 **2018**	2017	Twelve Months ended December 31 **2018**	2017
Natural gas	**85,955**	118,013	**300,590**	532,561
Oil & natural gas liquids	**42,370**	54,489	**201,556**	170,452
Hedging gain	**16,784**	39,297	**156,760**	57,943
	145,109	211,799	**658,906**	760,956



For the three months ended December 31, 2018, revenue and realized hedging gains (losses) decreased 31 per cent to $145.1 million from $211.8 million for the same period in 2017. On an annual basis, revenue decreased 13 per cent from $761.0 million in 2017 to $658.9 million in 2018. The decrease in revenue and realized hedging gains (losses) for the quarter was a result of decreased production volumes and prices, as detailed in the following table:

	Three Months ended December 31 2018	2017	**$million**	Twelve Months ended December 31 2018	2017	**$million**
Total Revenue, December 31, 2017			**211.8**			**761.0**
Revenue change due to:						
Natural gas						
Volume (mmcf)	42,209	54,821	**(36.2)**	180,281	204,277	**(69.6)**
Price ($/mcf)	$2.43	$2.87	**(18.5)**	$2.54	$2.89	**(63.2)**
Oil & NGL						
Volume (mbbl)	945	964	**(1.0)**	3,537	3,408	**6.2**
Price ($/bbl)	$44.83	$56.52	**(11.0)**	$56.98	$50.02	**24.5**
Total Revenue, December 31, 2018			**145.1**			**658.9**



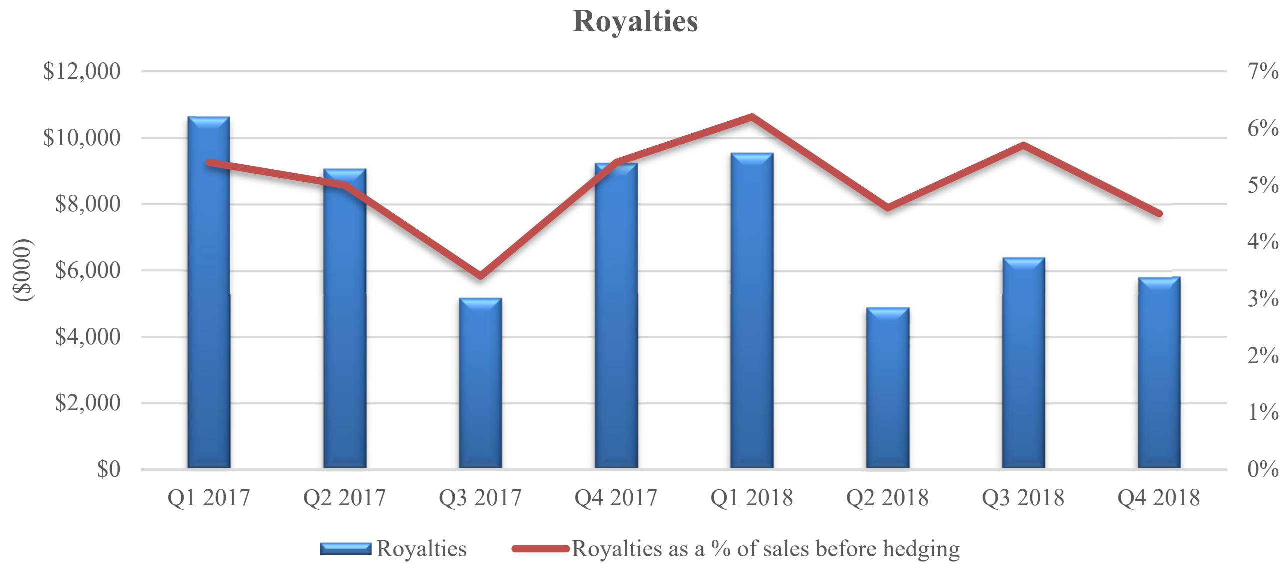


Royalties

Royalties are paid to the owners of the mineral rights with whom leases are held, including the provincial government of Alberta. Alberta Natural Gas Crown royalties are invoiced on the Crown's share of production based on a monthly established Alberta Reference Price. The Alberta Reference Price is a monthly weighted average price of gas consumed in Alberta and gas exported from Alberta reduced for transportation and marketing allowances. All of Peyto’s new natural gas wells qualify for the Crown incentive programs which have a 5 per cent initial royalty rate. The royalty rate expressed as a percentage of sales revenue will fluctuate from period to period due to the fact that the Alberta Reference Price can differ significantly from the commodity prices realized by Peyto and that hedging gains and losses are not subject to royalties.

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Royalties ($000)	**5,801**	9,232	**26,622**	34,104
per cent of sales before hedging	**4.5**	5.4	**5.3**	4.9
per cent of sales after hedging	**4.0**	4.4	**4.0**	4.5
$/mcfe	**0.12**	0.15	**0.13**	0.15
$/boe	**0.73**	0.91	**0.79**	0.91

For the fourth quarter of 2018, royalties averaged $0.12/mcfe or approximately 4.5 per cent of Peyto's total petroleum and natural gas sales excluding hedging gains. On an annual basis, royalties averaged $0.13/mcfe or 5.3 per cent of sales excluding hedging gains.



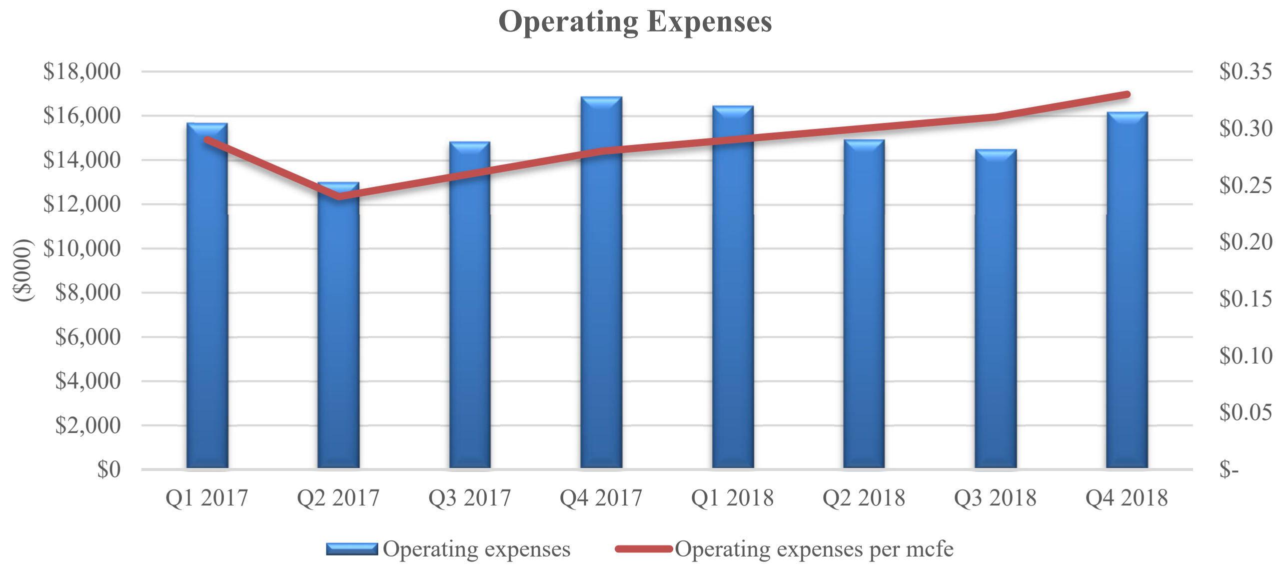
In its 20 year history, Peyto has invested over $5.9 billion in capital projects, found and developed 6.5 TCFe of natural gas reserves, and paid over $858 million in royalties.

Operating Costs & Transportation

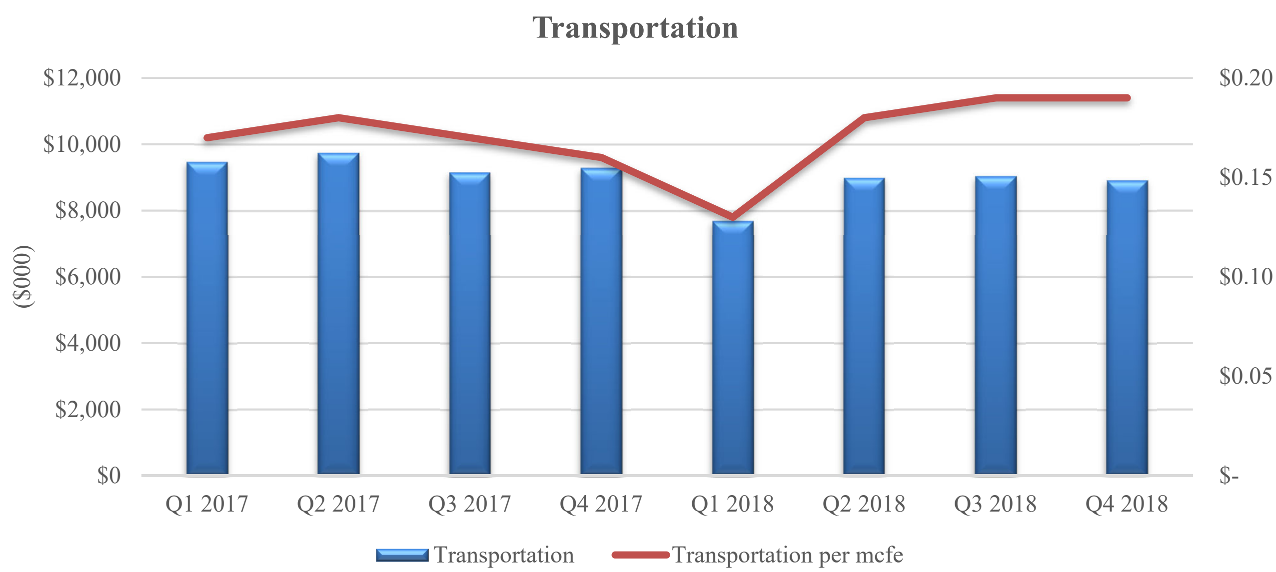
Peyto's operating expenses include all costs with respect to day-to-day well and facility operations.

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Operating costs ($000)	**16,189**	16,877	**62,085**	60,423
$/mcfe	**0.33**	0.28	**0.31**	0.27
$/boe	**2.03**	1.67	**1.85**	1.61
Transportation ($000)	**8,912**	9,282	**34,623**	37,640
$/mcfe	**0.19**	0.16	**0.17**	0.16
$/boe	**1.12**	0.92	**1.03**	1.00

For the fourth quarter, operating expenses decreased 4 per cent compared to the same quarter of 2017. On a unit-of-production basis, operating costs increased 18 per cent from $0.28/mcfe to $0.33/mcfe due to a combination of fixed and variable cost inflation including power, methanol, municipal taxes, AER Administration and other governmental fees and of lower production volumes. On an annual basis, operating costs per mcfe increased 15 per cent from $0.27/mcfe to $0.31/mcfe. These continued strong results were achieved despite increases in municipal taxes and the Alberta Energy Regulator fee levy. Peyto focuses on being the industry leader in operating costs and strives to achieve incremental cost reductions on a continuous basis.



Transportation expenses increased 19 per cent on a unit-of production basis from $0.16/mcfe in the fourth quarter 2017 to $0.19/mcfe in the fourth quarter 2018 due to the incremental cost of unutilized firm transportation.

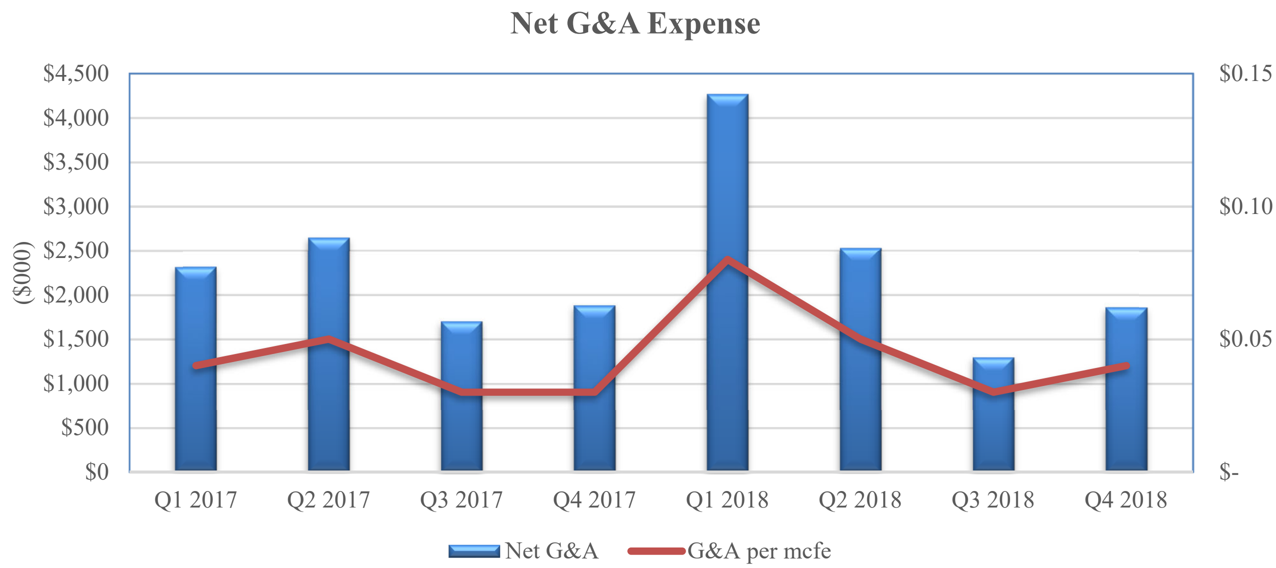


General and Administrative Expenses

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
G&A expenses ($000)	**4,591**	4,248	**17,436**	17,392
Overhead recoveries ($000)	**(2,734)**	(2,369)	**(7,486)**	(8,854)
Net G&A expenses ($000)	**1,857**	1,879	**9,950**	8,538
$/mcfe	**0.04**	0.03	**0.04**	0.04
$/boe	**0.23**	0.19	**0.29**	0.23

For the fourth quarter, general and administrative expenses before overhead recoveries was $4.6 million compared to $4.2 million for the same quarter of 2017. General and administrative expenses averaged $0.10/mcfe before overhead recoveries of $0.06/mcfe for net general and administrative expenses of $0.04/mcfe in the fourth quarter of 2018 ($0.07/mcfe before overhead recoveries of $0.04/mcfe for net general and administrative expenses of $0.03/mcfe in the fourth quarter of 2017).

Peyto capitalizes general and administrative costs and market and reserves based compensation related to the execution of its capital program. Most these costs are related to the execution of Peyto's capital program. In 2018, Peyto capitalized $7.0 million of expenses directly attributable to exploration and development activities compared to $8.3 million in 2017.



Performance Based Compensation

The Company awards performance based compensation to employees and key consultants annually. The performance based compensation is comprised of market and reserve value based components.

The reserve value based component is 4 per cent of the incremental increase in value, if any, as adjusted to reflect changes in debt, equity, dividends, general and administrative expenses and interest expense, of proved producing reserves calculated using a constant price at December 31 of the current year and a discount rate of 8 per cent. An estimate of reserve additions is made quarterly and is used to calculate an accrued reserve value based expense for the period. This methodology can generate interim results which vary significantly from the final compensation paid. Compensation expense of NIL million was recorded for the fourth quarter and the year 2018.

Under the market based component, rights with a three year vesting period are allocated to employees and key consultants. The number of rights outstanding at any time is not to exceed 6 per cent of the total number of common shares outstanding. At December 31 of each year, all vested rights are automatically cancelled and, if applicable, paid out in cash. Compensation is calculated as the number of vested rights multiplied by the total of the market appreciation (over the price at the date of grant) and associated dividends of a common share for that period. The 2018 market based component was based on 1.3 million vested rights at an average grant price of $24.09, average cumulative dividends of $1.32 and a ten day weighted average price of $33.80.

The total amount expensed under these plans was as follows:

($000)	**2018**	2017
Market based compensation	13,558	13,867
Reserve based compensation	-	1,817
Total market and reserves based compensation	**13,558**	15,684

Future Market Based Compensation

For the future market based component, compensation costs recovery of $9.2 million were recorded for the year ended December 31, 2018 related to 1.3 million vested rights with an average grant price of $24.09 and average cumulative dividends of $1.32 and 4.0 million rights with an average grant price of $14.68 and cumulative dividends of $0.72 valued at NIL December 31, 2018 (2017 – $2.2 related to 1.3 million vested rights with an average grant price of $24.09 and average cumulative dividends of $1.32). The cumulative provision for future performance based compensation as at December 31, 2018 was NIL (2017 - $9.2 million).

Subsequent to December 31, 2018, 2.5 million rights were granted at a price of $7.23 to be valued at the ten day weighted average market price and vesting 1/3 on each of December 31, 2019, December 31, 2020 and December 31, 2021.

The changes in total rights outstanding and related weighted average exercise prices for the years ended December 31, 2018 and 2017 were as follows:

	Rights (number of shares)	Weighted Average Grant Price ($)
Balance, December 31, 2016	**2,523,667**	**$24.09**
Granted	3,918,500	$33.64
Cancelled	(17,867)	$28.98
Paid out	(5,166,900)	$31.32
Balance, December 31, 2017	**1,257,400**	**$24.09**
Granted	3,942,400	$14.68
Cancelled	(46,000)	$20.41
Paid out	(5,153,800)	$16.96
Balance, December 31, 2018	**-**	**-**

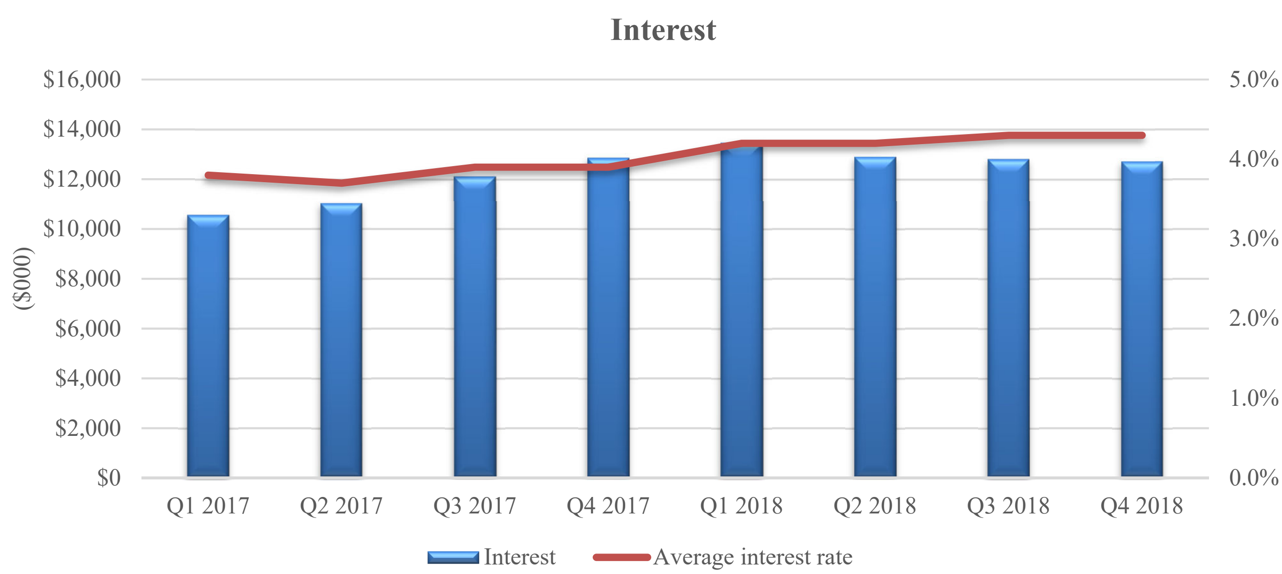
Rights Outstanding Under Market Based Compensation Plan

Valuation and Vesting Date	Number of Rights	Average Grant Price
December 31, 2019	825,000	$ 7.23
December 31, 2020	825,000	$ 7.23
December 31, 2021	825,000	$ 7.23

Interest Expense

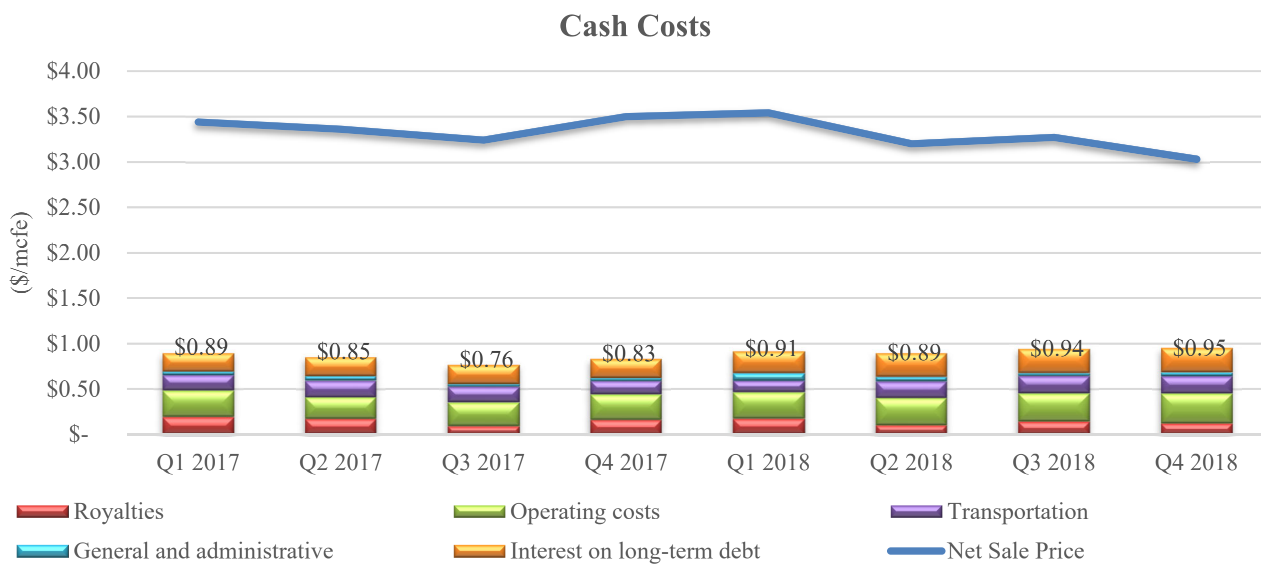
	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Interest expense ($000)	**12,717**	12,856	**51,886**	46,530
$/mcfe	**0.27**	0.21	**0.26**	0.21
$/boe	**1.59**	1.27	**1.55**	1.24
Average interest rate	**4.4%**	4.0%	**4.3%**	3.9%

Fourth quarter 2018 interest expense was $12.7 million or $0.27/mcfe compared to $12.9 million or $0.21/mcfe for the fourth quarter 2017. For the year ended December 31, 2018, interest expense was $51.9 million compared to $46.5 million for 2017. The average interest rate 2018 was 4.3 per cent compared to 3.9 per cent in 2017 due to Bank of Canada interest rate increases.



Netbacks

($/mcfe)	Three Months ended December 31 **2018**	2017	Twelve Months ended December 31 **2018**	2017
Gross Sale Price	**2.68**	2.85	**2.49**	3.13
Hedging gain (loss)	**0.35**	0.65	**0.78**	0.25
Net Sale Price	**3.03**	3.50	**3.27**	3.38
Less: Royalties	**0.12**	0.15	**0.13**	0.15
Operating costs	**0.33**	0.28	**0.31**	0.27
Transportation	**0.19**	0.16	**0.17**	0.16
Field netback	**2.39**	2.91	**2.66**	2.80
General and administrative	**0.04**	0.03	**0.05**	0.04
Interest on long-term debt	**0.27**	0.21	**0.26**	0.21
Cash netback ($/mcfe)	**2.08**	2.67	**2.35**	2.55
Cash netback ($/boe)	**12.49**	16.01	**14.11**	15.32



Netbacks are a non-GAAP measure that represent the profit margin associated with the production and sale of petroleum and natural gas. Netbacks are per unit of production measures used to assess Peyto's performance and efficiency. The primary factors that produce Peyto's strong netbacks and high margins are a low cost structure and the high heat content of its natural gas that results in higher commodity prices.

Depletion, Depreciation and Amortization

Under IFRS, Peyto uses proved plus probable reserves as its depletion base to calculate depletion expense. The 2018 fourth quarter provision for depletion, depreciation and amortization totaled $66.2 million ($1.38/mcfe) compared to $86.6 million ($1.43/mcfe) in the fourth quarter 2017. On a unit-of-production basis, depletion and depreciation costs averaged $1.42/mcfe in 2018 compared to $1.40/mcfe in 2017.

Income Taxes

The current provision for deferred income tax expense is $7.6 million compared to $19.1 million in the fourth quarter of 2017. The annual provision for 2018 is $47.4 million compared to $65.3 million for 2017. The corporate income tax rate in Alberta remained unchanged at 27 per cent. Resource pools are generated from the capital program, which are available to offset current and deferred income tax liabilities.

Income Tax Pool type ($ millions)	**December 31, 2018**	December 31, 2017	**Annual deductibility**
Canadian Oil and Gas Property Expense	191.7	211.2	10% declining balance
Canadian Development Expense	698.1	848.0	30% declining balance
Canadian Exploration Expense	89.2	76.0	100%
Undepreciated Capital Cost	322.5	406.3	Primarily 25% declining balance
Other	21.5	27.2	Various, 7% to 20% declining balance
Total Federal Tax Pools	**1,323.0**	1,568.7	
Additional Alberta Tax Pools	46.3	46.3	Primarily 100%

MARKETING

Commodity Price Risk Management

Financial Derivative Instruments
The Company is a party to certain derivative financial instruments, including fixed price contracts. The Company enters into these forward contracts with well-established counterparties for the purpose of protecting a portion of its future revenues from the volatility of oil and natural gas prices. In order to minimize counterparty risk, these marketing contracts are executed with financial institutions which are members of Peyto's banking syndicate. During the fourth quarter of 2018, a realized hedging gain of $16.8 million was recorded as compared to a $39.3 million gain for the equivalent period in 2017. A summary of contracts outstanding in respect of the hedging activities are as follows:

Natural Gas Period Hedged - Monthly Index	**Type**	**Daily Volume**	**Average Price (AECO CAD)**
January 1, 2018 to December 31, 2020	Fixed Price	20,000 GJ	$2.02/GJ
April 1, 2018 to March 31, 2019	Fixed Price	185,000 GJ	$2.34/GJ
April 1, 2018 to March 31, 2020	Fixed Price	10,000 GJ	$1.44/GJ
November 1, 2018 to March 31, 2019	Fixed Price	90,000 GJ	$1.64/GJ
November 1, 2018 to March 31, 2020	Fixed Price	5,000 GJ	$1.57/GJ
April 1, 2019 to October 31, 2019	Fixed Price	50,000 GJ	$1.37/GJ
April 1, 2019 to March 31, 2020	Fixed Price	80,000 GJ	$1.76/GJ
November 1, 2019 to March 31, 2020	Fixed Price	55,000 GJ	$2.00/GJ
April 1, 2020 to October 31, 2020	Fixed Price	15,000 GJ	$1.30/GJ
April 1, 2020 to March 31, 2021	Fixed Price	10,000 GJ	$1.65/GJ
April 1, 2021 to October 31, 2021	Fixed Price	10,000 GJ	$1.56/GJ

Natural Gas Period Hedged -Daily Index	**Type**	**Daily Volume**	**Average Price (AECO CAD)**
April 1, 2018 to March 31, 2019	Fixed Price	40,000 GJ	$1.54/GJ

Crude Oil Period Hedged	**Type**	**Daily Volume**	**Average Price (WTI CAD)**
July 1, 2018 to June 30, 2019	Fixed Price	400 bbl	$86.75/ bbl
August 1, 2018 to July 31, 2019	Fixed Price	600 bbl	$84.92/ bbl
September 1, 2018 to August 31, 2019	Fixed Price	400 bbl	$85.97/ bbl
October 1, 2018 to September 30, 2019	Fixed Price	500 bbl	$85.92/ bbl
November 1, 2018 to October 31, 2019	Fixed Price	500 bbl	$89.34/ bbl
December 1, 2018 to November 30, 2019	Fixed Price	300 bbl	$90.17/bbl

As at December 31, 2018, Peyto had committed to the future sale of 121,560,000 gigajoules (GJ) of natural gas at an average price of $1.80 per GJ or $2.07 per mcf and 688,500 barrels of crude at $87.23 per bbl. Had these contracts closed on December 31, 2018, Peyto would have realized a net gain in the amount of $78.8 million.

Subsequent to December 31, 2018 Peyto entered into the following contracts:

Natural Gas Period Hedged -Daily Index	Type	Daily Volume	Average Price (AECO CAD)
April 1, 2019 to October 31, 2019	Fixed Price	30,000 GJ	$1.27/GJ
November 1, 2019 to March 31, 2020	Fixed Price	10,000 GJ	$1.97/GJ

Natural Gas Period Hedged -Monthly Index	Type	Daily Volume	Average Price (AECO CAD)
November 1, 2019 to March 31, 2020	Fixed Price	5,000 GJ	$2.07/GJ

Physical Volume Contracts
The Company is a party to certain physical delivery contracts. The Company enters into these contracts with well-established counterparties for the purpose of protecting a portion of its future revenues from the volatility of oil and natural gas prices. A summary of contracts outstanding at December 31, 2018 are as follows:

Natural Gas Period Hedged – Fixed Price	Daily Volume	Average Price (USD/mmbtu)
January 1, 2019 – March 31, 2019	20,000 mmbtu	$4.00/mmbtu
April 1, 2019 to October 31, 2019	105,000 mmbtu	$1.34/mmbtu

Natural Gas Period Hedged – Floating Price	Daily Volume	Price (USD/mmbtu)
January 1, 2019 – March 31, 2019	5,000 mmbtu	Emerson
January 1, 2019 – March 31, 2019	15,000 mmbtu	Dawn
April 1, 2019 to October 31, 2019	55,000 mmbtu	Henry Hub/AECO - $1.43
April 1, 2019 to October 31, 2019	15,000 mmbtu	Emerson
April 1, 2019 to October 31, 2019	25,000 mmbtu	Dawn
November 1, 2019 to March 31, 2020	95,000 mmbtu	Henry Hub/AECO - $1.23
November 1, 2019 to March 31, 2020	40,000 mmbtu	Emerson
April 1, 2020 to October 31, 2020	160,000 mmbtu	Henry Hub/AECO - $1.43
April 1, 2020 to October 31, 2020	40,000 mmbtu	Emerson
November 1, 2020 to March 31, 2021	95,000 mmbtu	Henry Hub/AECO - $1.23
November 1, 2020 to March 31, 2021	40,000 mmbtu	Emerson
April 1, 2021 to October 31, 2021	160,000 mmbtu	Henry Hub/AECO - $1.43
April 1, 2021 to October 31, 2021	40,000 mmbtu	Emerson
November 1, 2021 to October 31, 2024	27,500 mmbtu	Henry Hub/Empress - $0.90
April 1, 2022 to October 31, 2022	50,000 mmbtu	Henry Hub/AECO - $1.41

Subsequent to December 31, 2018 Peyto fixed the price on the following contracts which were floating at December 31, 2018:

Natural Gas Period Hedged – Fixed Price	Daily Volume	Average Price (USD/mmbtu)
April 1, 2019 to October 31, 2019	65,000 mmbtu	$1.37/mmbtu
November 1, 2019 to March 31, 2020	45,000 mmbtu	$1.80/mmbtu

Subsequent to December 31, 2018 Peyto entered into the following contracts:

Natural Gas Period Hedged – Floating Price	Daily Volume	Price (USD/mmbtu)
April 1, 2019 to October 31, 2019	10,000 mmbtu	Ventura
November 1, 2019 to March 31, 2020	72,500 mmbtu	Henry Hub/AECO - $1.43
November 1, 2019 to October 31, 2027	20,000 mmbtu	Ventura
April 1, 2020 to October 31, 2020	87,500 mmbtu	Henry Hub/AECO - $1.43
November 1, 2020 to March 31, 2021	87,500 mmbtu	Henry Hub/AECO - $1.43
April 1, 2021 to October 31, 2021	87,500 mmbtu	Henry Hub/AECO - $1.43
November 1, 2021 to March 31, 2022	87,500 mmbtu	Henry Hub/AECO - $1.43
April 1, 2022 to October 31, 2022	72,500 mmbtu	Henry Hub/AECO - $1.42

Commodity Price Sensitivity
Peyto's earnings are largely determined by commodity prices for crude oil and natural gas including the US/Canadian dollar exchange rate. Volatility in these oil and gas prices can cause fluctuations in Peyto's earnings. Low operating costs and a long reserve life reduce Peyto's sensitivity to changes in commodity prices.

Currency Risk Management
The Company is exposed to fluctuations in the Canadian/US dollar exchange ratio since commodities are effectively priced in US dollars and converted to Canadian dollars. In the short term, this risk is mitigated indirectly as a result of a commodity hedging strategy that is conducted in a Canadian dollar currency. Over the long term, the Canadian dollar tends to rise as commodity prices rise. There is a similar correlation between oil and gas prices. Currently Peyto has not entered into any agreements to further manage its currency risks.

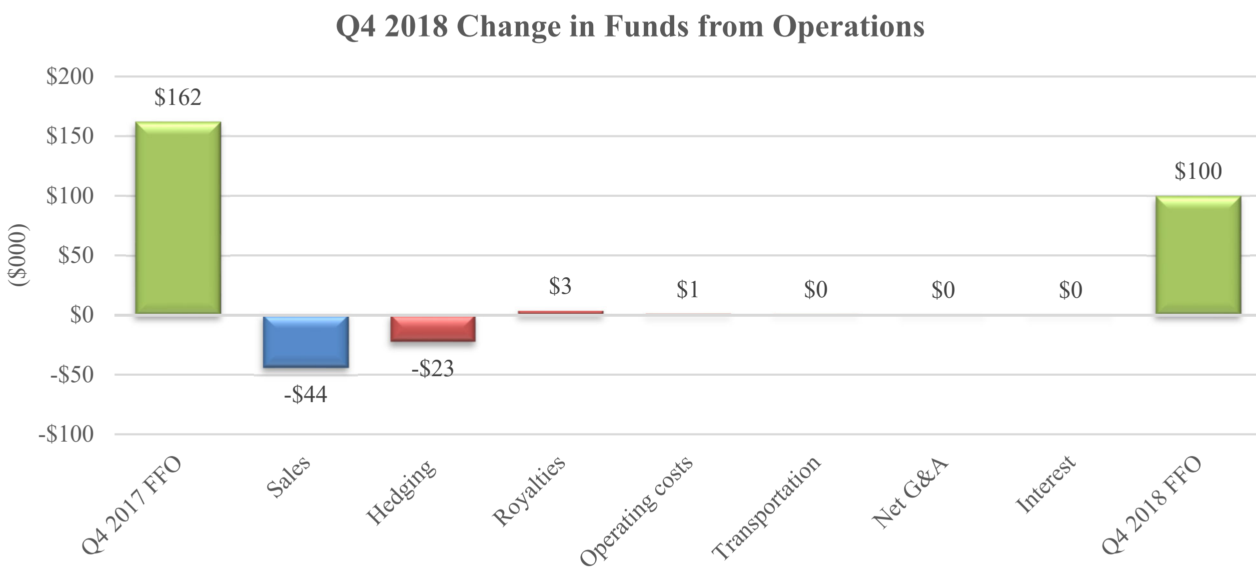
Interest Rate Risk Management
The Company is exposed to interest rate risk in relation to interest expense on its revolving credit facility while interest rates on the senior notes are fixed. Currently there are no agreements to manage the risk on the credit facility. At December 31 2018, the increase or decrease in earnings for each 100 bps (1 per cent) change in interest rate paid on the outstanding revolving demand loan amounts to approximately $1.4 million per quarter. Average debt outstanding for the quarter was $1.2 billion (including $620 million fixed rate debt).

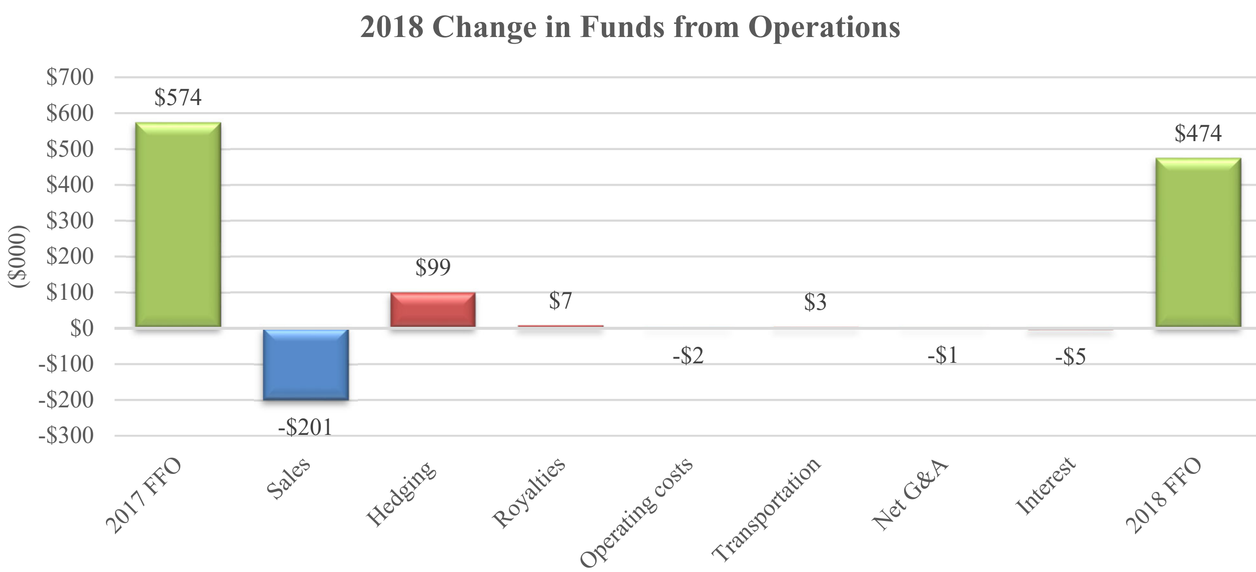
LIQUIDITY AND CAPITAL RESOURCES

Funds from operations is reconciled to cash flows from operating activities below:

	Three Months ended December 31		Twelve months ended December 31	
($000)	**2018**	2017	**2018**	2017
Cash flows from operating activities	**102,559**	143,568	**486,478**	535,344
Change in non-cash working capital	**(3,955)**	6,444	**(17,131)**	20,381
Change in provision for performance based compensation	**(12,527)**	(4,024)	**(9,165)**	2,312
Performance based compensation	**13,558**	15,684	**13,558**	15,684
Funds from operations	**99,635**	161,672	**473,740**	573,721
Funds from operations per share	**0.60**	0.98	**2.87**	3.48

For the fourth quarter ended December 31, 2018, funds from operations totaled $99.6 million or $0.60 per share, compared to $161.7 million or $0.98 per share during the same quarter in 2017. For the year ended December 31, 2018 funds from operations was $473.7 million or $2.87 per share, compared to $573.7 million or $3.48 per share for 2017. The decrease in funds from operation on a quarterly and annual basis was due to a decrease in production volumes and in oil and NGL prices.





Peyto's policy is to balance dividends to shareholders with earnings and cash flow, and to balance funding for the capital program with cash flow, equity and available bank lines. Earnings and cash flow are sensitive to changes in commodity prices, exchange rates and other factors that are beyond Peyto's control. Current volatility in commodity prices creates uncertainty as to the funds from operations and capital expenditure budget. Accordingly, results are assessed throughout the year and operational plans revised as necessary to reflect the most current information.

Revenues will be impacted by drilling success and production volumes as well as external factors such as the market prices for commodities and the exchange rate of the Canadian dollar relative to the US dollar.

Current and Long-Term Debt

($000)	**December 31, 2018**	December 31, 2017
Current senior unsecured notes	100,000	-
Long-term senior unsecured notes	520,000	520,000
Bank credit facility	530,000	765,000
Balance, end of the period	**1,150,000**	1,285,000

The Company has a syndicated $1.3 billion extendible unsecured revolving credit facility with a stated term date of October 13, 2021. The bank facility is made up of a $40 million working capital sub-tranche and a $1.26 billion production line. The facilities are available on a revolving basis. Borrowings under the facility bear interest at Canadian bank prime or US base rate, or, at Peyto's option, Canadian dollar bankers' acceptances or US dollar LIBOR loan rates, plus applicable margin and stamping fees. The total stamping fees range between 50 basis points and 215 basis points on Canadian bank prime and US base rate borrowings and between 150 basis points and 315 basis points on Canadian dollar bankers' acceptance and US dollar LIBOR borrowings. The undrawn portion of the facility is subject to a standby fee in the range of 30 to 63 basis points.

Peyto is subject to the following financial covenants as defined in the credit facility and note purchase agreements:

- Long-term debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 3.0 times trailing twelve month net income before non-cash items, interest and income taxes (covenant amended to 3.25 times effective March 1, 2019);

  as at December 31, 2018 – 2.34:1.0

- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 4.0 times trailing twelve month net income before non-cash items, interest and income taxes;

  as at December 31, 2018 – 2.34:1.0

- Trailing twelve months net income before non-cash items, interest and income taxes to exceed 3.0 times trailing twelve months interest expense;

  as at December 31, 2018 – 9.8 times

- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 55% of shareholders' equity and long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items.

  as at December 31, 2018 – 41%

Peyto is in compliance with all financial covenants and has no subordinated debt as at December 31, 2018.

On March 1, 2019, the Company extended the revolving credit facility by one year with a new stated term date of October 13, 2022. The definition of debt and the Senior Debt to EBITDA (twelve-month net income before non-cash items, interest and income taxes) covenant ratio were changed to be in accordance with industry standards. The changes are outlined below:

- Definition of debt has changed to long-term debt including current portion of senior unsecured notes and letters of credit,
- Long-term debt at the end of each fiscal quarter not to exceed 3.25 times trailing twelve-month net income before non-cash items, interest and income taxes.

On January 2, 2018, the Company closed an issuance of CDN $100 million of senior unsecured notes. The notes were issued by way of a private placement, pursuant to a note purchase agreement and a note purchase and private shelf agreement, and rank equally with Peyto's obligations under its bank facility and existing note purchase agreements. The notes have a coupon rate of 3.95% and mature on January 2, 2028. Interest will be paid semi-annually in arrears. Proceeds from the notes were used to repay a portion of Peyto's outstanding bank debt.

Outstanding unsecured senior notes are as follows (includes notes due within one year):

Senior Unsecured Notes	**Date Issued**	**Rate**	**Maturity Date**
$100 million	January 3, 2012	4.39%	January 3, 2019
$120 million	December 4, 2013	4.50%	December 4, 2020
$50 million	July 3, 2014	3.79%	July 3, 2022
$50 million	September 6, 2012	4.88%	September 6, 2022
$100 million	October 24, 2016	3.70%	October 24, 2023
$100 million	May 1, 2015	4.26%	May 1, 2025
$100 million	January 2, 2018	3.95%	January 2, 2028

Peyto's total borrowing capacity after the issuance of the senior, unsecured notes on January 2, 2018 is $1.92 billion of which the credit facility is $1.3 billion.

Senior unsecured notes in the amount of CAD $100 million with a coupon rate of 4.39% mature on January 3, 2019 and have therefore been classified as a current liability.

On January 3, 2019, the Company closed an issuance of CDN $100 million of senior unsecured notes. The notes were issued by way of a private placement, pursuant to a note purchase agreement and rank equally with Peyto's obligations under its bank facility and existing note purchase agreements. The notes have a coupon rate of 4.39% and mature on January 3, 2026. Interest will be paid semi-annually in arrears. Proceeds from the notes were used to repay the senior notes of Peyto which matured on January 3, 2019.

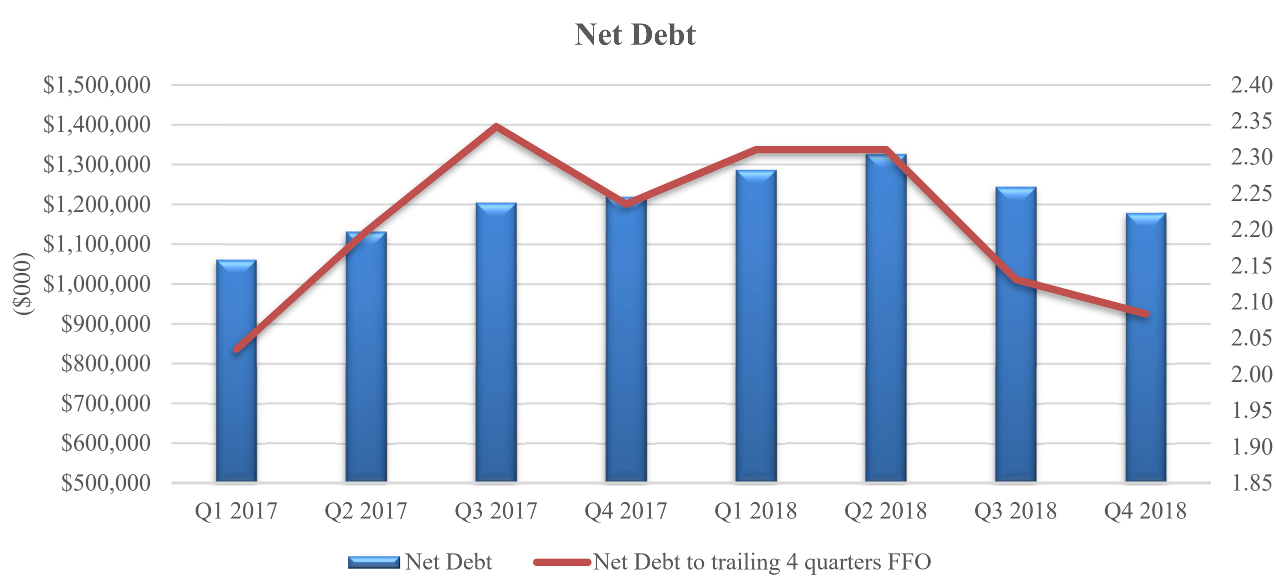
Peyto believes funds generated from operations, together with borrowings under the credit facility will be sufficient to maintain dividends, finance current operations, and fund the planned capital expenditure program of approximately $150 to $200 million for 2019. The total amount of capital invested in 2019 will be driven by the number and quality of projects generated. Capital will only be invested if it meets the long-term objectives of the Company. The majority of the capital program will involve drilling, completion and tie-in of lower risk development gas wells. Peyto's rapidly scalable business model has the flexibility to match planned capital expenditures to actual cash flow.

Net Debt

"Net debt" is a non-GAAP measure that is the sum of long-term debt and working capital excluding the current financial derivative instruments and current provision for future performance-based compensation. It is used by management to analyze the financial position and leverage of the Company. Net debt is reconciled below to long-term debt which is the most directly comparable GAAP measure:

($000)	**As at December 31, 2018**	As at December 31, 2017
Bank credit facility - drawn	**530,000**	765,000
Senior unsecured notes	**620,000**	520,000
Current assets	**(135,231)**	(243,489)
Current liabilities (excludes current portion of senior unsecured notes)	**143,884**	160,078
Financial derivative instruments	**65,769**	135,017
Provision for future performance-based compensation	**-**	(9,166)
Net debt	**1,224,422**	1,327,440

Net debt has decreased 8 per cent from $1.33 billion at December 31, 2017 to $1.22 billion at December 31, 2018.



Capital
Authorized: Unlimited number of voting common shares

Issued and Outstanding

Common Shares (no par value)	Number of Common Shares	Amount ($000)
Balance, December 31, 2017	**164,874,175**	**1,649,537**
Common shares issued	-	-
Common share issuance costs, (net of tax)	-	-
Balance, December 31, 2018	**164,874,175**	**1,649,537**

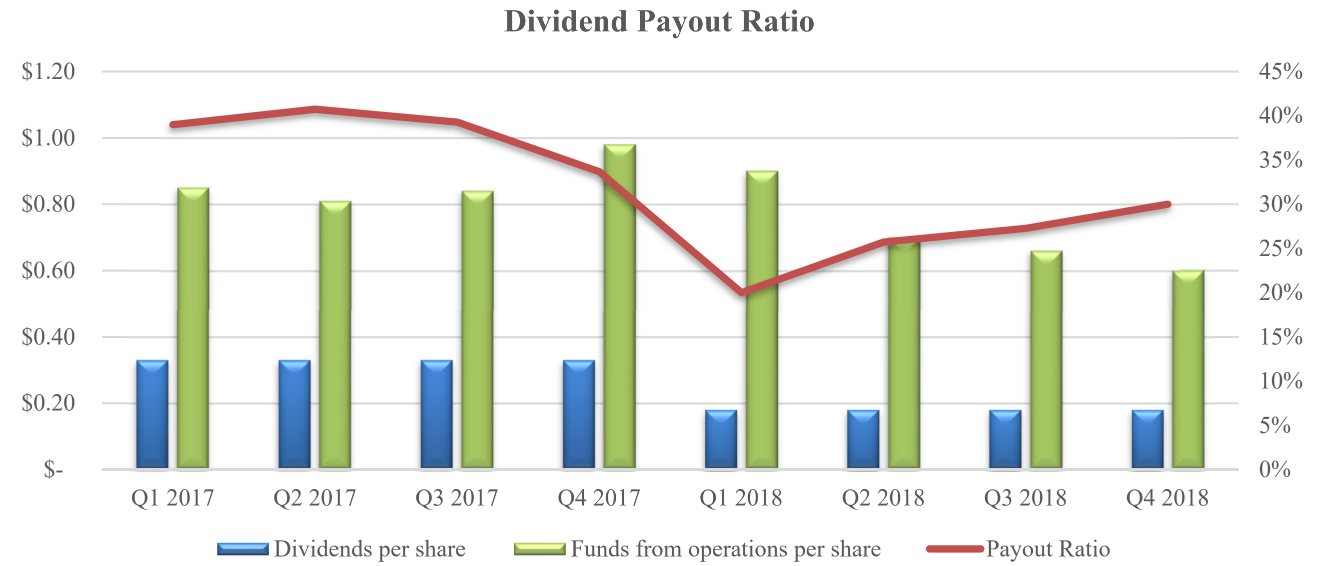
Capital Expenditures
Net capital expenditures for the fourth quarter of 2018 totaled $112.2 million. Exploration and development related activity represented $93.8 million (84 per cent), while expenditures on facilities, gathering systems and equipment totaled $14.4 million (13 per cent) and land, seismic, and acquisitions totaled $4.0 million (3 per cent). The following table summarizes capital expenditures for the period:

	Three Months ended December 31		Twelve Months ended December 31	
($000)	**2018**	2017	**2018**	2017
Land	**106**	3,609	**3,291**	10,328
Seismic	**2,000**	270	**5,216**	6,007
Drilling	**57,383**	68,909	**115,610**	256,932
Completions	**36,369**	42,124	**72,274**	133,732
Equipping & Tie-ins	**10,716**	15,695	**20,766**	53,146
Facilities & Pipelines	**3,691**	3,610	**17,293**	57,284
Acquisitions	**1,950**	194	**1,950**	3,823
Dispositions	**-**	-	**(4,037)**	(42)
Total Capital Expenditures	**112,215**	134,411	**232,363**	521,210

Dividends

	Three Months ended December 31		Twelve Months ended December 31	
	2018	2017	**2018**	2017
Funds from operations ($000)	**99,635**	161,672	**473,740**	573,721
Total dividends ($000)	**29,677**	54,408	**118,709**	217,612
Total dividends per common share ($)	**0.18**	0.33	**0.72**	1.32
Payout ratio (%)	**30**	34	**25**	38

Peyto's policy is to balance dividends to shareholders with earnings and cash flow; and funding for the capital program with cash flow, equity and available bank lines. The Board of Directors is prepared to adjust the payout ratio levels (dividends declared divided by funds from operations) to achieve the desired dividends while maintaining an appropriate capital structure.



Contractual Obligations

In addition to those recorded on the Company's balance sheet, the following is a summary of Peyto's contractual obligations and commitments as at December 31, 2018:

($000)	2019	2020	2021	2022	2023	Thereafter
Interest payments [1]	23,840	21,645	16,245	16,245	11,910	24,165
Transportation commitments	52,132	42,670	31,779	28,909	27,950	249,471
Operating lease	2,240	2,240	2,240	2,315	2,315	6,946
Methanol	3,727	-	-	-	-	-
Total	81,939	66,555	50,264	47,469	42,175	280,582

(1) Fixed interest payments on senior unsecured notes

RELATED PARTY TRANSACTIONS

Certain directors of Peyto are considered to have significant influence over other reporting entities that Peyto engages in transactions with. Such services are provided in the normal course of business and at market rates. These directors are not involved in the day to day operational decision making of the Company. The dollar value of the transactions between Peyto and the related reporting entities is summarized below:

($000) Expense				Accounts Payable	
Three Months ended December 31		Twelve Months ended December 31		As at December 31	
2018	2017	**2018**	2017	**2018**	2017
283.6	211.3	**716.4**	671.7	**650.5**	549.2

RISK MANAGEMENT

Investors who purchase shares are participating in the total returns from a portfolio of western Canadian natural gas producing properties. As such, the total returns earned by investors and the value of the shares are subject to numerous risks inherent in the oil and natural gas industry.

Expected returns depend largely on the volume of petroleum and natural gas production and the price received for such production, along with the associated costs. The price received for oil depends on a number of factors, including West Texas Intermediate oil prices, Canadian/US currency exchange rates, quality differentials and Edmonton par oil prices. The price received for natural gas production is dependent on current Alberta, Henry Hub and Dawn market prices and Canadian/US currency exchange rates. Peyto's marketing strategy is designed to smooth out short term fluctuations in the price of natural gas through future sales. It is meant to be methodical and consistent and to avoid speculation.

Although Peyto's focus is on internally generated drilling programs, any acquisition of oil and natural gas assets depends on an assessment of value at the time of acquisition. Incorrect assessments of value can adversely affect dividends to shareholders and the value of the shares. Peyto employs experienced staff and performs appropriate levels of due diligence on the analysis of acquisition targets, including a detailed examination of reserve reports; if appropriate, re-engineering of reserves for a large portion of the properties to ensure the results are consistent; site examinations of facilities for environmental liabilities; detailed examination of balance sheet accounts; review of contracts; review of prior year tax returns and modeling of the acquisition to attempt to ensure accretive results to the shareholders.

Inherent in development of the existing oil and gas reserves are the risks, among others, of drilling dry holes, encountering production or drilling difficulties or experiencing high decline rates in producing wells. To minimize these risks, Peyto employs experienced staff to evaluate and operate wells and utilize appropriate technology in operations. In addition, prudent work practices and procedures, safety programs and risk management principles, including insurance coverage protect Peyto against certain potential losses.

The value of Peyto's shares is based on among other things, the underlying value of the oil and natural gas reserves. Geological and operational risks can affect the quantity and quality of reserves and the cost of ultimately recovering those reserves. Lower oil and gas prices increase the risk of write-downs on oil and gas property investments. In order to mitigate this risk, proven and probable oil and gas reserves are evaluated each year by a firm of independent reservoir engineers. The reserves committee of the Board of Directors reviews and approves the reserve report.

Access to markets may be restricted at times by pipeline or processing capacity. These risks are minimized by controlling as much of the processing and transportation activities as possible and ensuring transportation and processing contracts are in place with reliable cost efficient counterparties.

The petroleum and natural gas industry is subject to extensive controls, regulatory policies and income and resource taxes imposed by various levels of government. These regulations, controls and taxation policies are amended from time to time. Peyto has no control over the level of government intervention or taxation in the petroleum and natural gas industry. Peyto operates in such a manner to ensure, to the best of its knowledge that it is in compliance with all applicable regulations and are able to respond to changes as they occur.

The petroleum and natural gas industry is subject to both environmental regulations and an increased environmental awareness. Peyto has reviewed its environmental risks and is, to the best of its knowledge, in compliance with the appropriate environmental legislation and have determined that there is no current material impact on operations. Peyto employs environmentally responsible business operations, and looks to both Alberta provincial authorities and Canada's federal authorities for direction and regulation regarding environmental and climate change legislation.

Peyto is subject to financial market risk. In order to maintain substantial rates of growth, Peyto must continue reinvesting in, drilling for or acquiring petroleum and natural gas. The capital expenditure program is funded primarily through funds from operations, debt and, if appropriate, equity.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: (i) material information relating to the Company is made known to the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation. Such officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Company's disclosure controls and procedures at the year end of the Company and have concluded that the Company's disclosure controls and procedures are effective at the financial period end of the Company for the foregoing purposes.

Internal Control over Financial Reporting

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, internal control over financial reporting to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Such officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Company's internal control over financial reporting at the financial period end of the Company and concluded that the Company's internal control over financial reporting is effective, at the financial period end of the Company, for the foregoing purpose.

Peyto is required to disclose herein any change in Peyto's internal control over financial reporting that occurred during the period ended December 31, 2018 that has materially affected, or is reasonably likely to materially affect, Peyto's internal control over financial reporting. No material changes in Peyto's internal control over financial reporting were identified during such period that has materially affected, or are reasonably likely to materially affect, Peyto's internal control over financial reporting.

It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

CRITICAL ACCOUNTING ESTIMATES

Reserve Estimates

Estimates of oil and natural gas reserves, by necessity, are projections based on geologic and engineering data, and there are uncertainties inherent to the interpretation of such data as well as the projection of future rates of production and the timing of development expenditures. Reserve engineering is an analytical process of estimating underground accumulations of oil and natural gas that can be difficult to measure. The accuracy of any reserve estimate is a function of the quality of available data, engineering and geological interpretation and judgment. Estimates of economically recoverable oil and natural gas reserves and future net cash flows necessarily depend upon a number of variable factors and assumptions, such as historical production from the area compared with production from other producing areas, the assumed effects of regulations by governmental agencies and assumptions governing future oil and natural gas prices, future royalties and operating costs, development costs and workover and remedial costs, all of which may in fact vary considerably from actual results. For these reasons, estimates of the economically recoverable quantities of oil and natural gas attributable to any particular group of properties, classifications of such reserves based on risk recovery, and estimates of the future net cash flows expected there from may vary substantially. Any significant variance in the assumptions could materially affect the estimated quantity and value of the reserves, which could affect the carrying value of Peyto's oil and natural gas properties and the rate of depletion of the oil and natural gas properties as well as the calculation of the reserve value based compensation. Actual production, revenues and expenditures with respect to Peyto's reserves will likely vary from estimates, and such variances may be material.

Peyto's estimated quantities of proved and probable reserves at December 31, 2018 were evaluated by independent petroleum engineers InSite Petroleum Consultants Ltd. InSite has been evaluating reserves in this area and for Peyto since inception.

Depletion and Depreciation Estimate

All costs of exploring for and developing petroleum and natural gas reserves, together with the costs of production equipment, are capitalized and then depleted and depreciated on the unit-of-production method based on proved plus probable reserves. Petroleum and natural gas reserves and production are converted into equivalent units based upon estimated relative energy content (6 mcf to 1 barrel of oil). Costs for gas plants and other facilities are capitalized and depreciated on a declining balance basis.

Impairment of Long-Lived Assets

Impairment is indicated if the carrying value of the long-lived asset or oil and gas cash generating unit exceeds its recoverable amount under IFRS. If impairment is indicated, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. The determination of the recoverable amount for impairment purposes under IFRS involves the use of numerous assumptions and judgments including future net cash flows from oil and gas reserves, future third-party pricing, inflation factors, discount rates and other uncertainties. Future revisions to these assumptions impact the recoverable amount.

Decommissioning Provision

The decommissioning provision is estimated based on existing laws, contracts or other policies. The fair value of the obligation is based on estimated future costs for abandonment and reclamation discounted at a credit adjusted risk free rate. The liability is adjusted each reporting period to reflect the passage of time and for revisions to the estimated future cash flows, with the accretion charged to earnings. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material.

Future Market Performance Based Compensation

The provision for future market based compensation is estimated based on current market conditions, distribution history and on the assumption that all outstanding rights will be paid out according to the vesting schedule. The conditions at the time of vesting could vary significantly from the current conditions and may have a material effect on the calculation.

Reserve Value Performance Based Compensation
The reserve value-based compensation is calculated using the year end independent reserves evaluation which was completed in February 2019. A quarterly provision for the reserve value based compensation is calculated using estimated proved producing reserve additions adjusted for changes in debt, equity and dividends. Actual proved producing reserves additions and forecasted commodity prices could vary significantly from those estimated and may have a material effect on the calculation.

Income Taxes
The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded.

Accounting Changes
Voluntary changes in accounting policy are made only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impractical to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and changes in accounting estimates are applied prospectively by including these changes in earnings. When the Company has not applied a new primary source of GAAP that has been issued, but is not effective, the Company will disclose the fact along with information relevant to assessing the possible impact that application of the new primary source of GAAP will have on the financial statements in the period of initial application.

STANDARDS ISSUED BUT NOT YET EFFECTIVE

The IASB issued the following standards and amendments which are not yet effective for Peyto and discussed in further detail in Note 2 to the Financial Statements for the fiscal period ended December 31, 2018.

In January 2016, the IASB issued IFRS 16, which replaces IAS 17 Leases ("IAS 17") and related interpretations. IFRS 16 requires the recognition of a right-of-use ("ROU") asset and lease liability on the balance sheet for most leases, where the entity is acting as a lessee. For lessees applying IFRS 16, the dual classification model of leases as either operating leases or finance leases no longer exists, effectively treating all leases as finance leases. IFRS 16 allows lessors to continue with the dual classification model for recognized leases with the resultant accounting remaining unchanged from IAS 17.

The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted if the entity is also adopting IFRS 15. IFRS 16 is required to be adopted either retrospectively or using a modified retrospective approach. The modified retrospective approach does not require restatement of prior period financial information as it recognizes the cumulative effect of IFRS 16 as an adjustment to opening retained earnings and applies the standard prospectively. IFRS 16 will be applied by Peyto on January 1, 2019, using the modified retrospective transition approach.

IFRS 16 is expected to increase the Company's total assets and liabilities and affect Peyto's opening retained earnings at January 1, 2019 as Peyto recognizes leases on its balance sheet that were not recognized prior to adoption. Future net income will be impacted as the finance charges and depreciation charges associated with lease contracts are not expected to correspond in any one period to the amount of related cash flows. Cash flows associated with lease repayments will be allocated between operating and financing activities based on their interest repayment and principal repayment portions.

The Company is expecting an estimated recognition of additional ROU assets and lease liabilities in the range of $8-$10 million, as of January 1, 2019. The difference between the asset and liability amounts will be related to any prepaids which will be recorded as an adjustment to the ROU assets and any lease incentives will be recorded as an adjustment to retained earnings.

The financial statement impact of IFRS 16 is subject to certain management judgments and estimates. Most notably, extension and termination provisions are included in certain lease contracts. In determining the lease term to be recognized, Management considers all facts and circumstances that create an economic incentive to exercise an extension option, or not to exercise a termination option.

ADDITIONAL INFORMATION

Additional information relating to Peyto Exploration & Development Corp. can be found on SEDAR at www.sedar.com and www.peyto.com.

Quarterly information

	2018				2017
	Q4	Q3	Q2	Q1	Q4
Operations					
Production					
Natural gas (mcf/d)	458,792	456,197	493,821	568,496	595,885
Oil & NGLs (bbl/d)	10,273	9,209	9,243	10,043	10,479
Barrels of oil equivalent (boe/d @ 6:1)	86,738	85,242	91,547	104,793	109,793
Thousand cubic feet equivalent (mcfe/d @ 6:1)	520,430	511,453	549,281	628,755	658,759
Average product prices					
Natural gas ($/mcf)	2.43	2.43	2.37	2.86	2.87
Oil & natural gas liquids ($/bbl)	44.83	61.04	63.64	59.67	56.52
$/MCFE					
Average sale price ($/mcfe)	3.03	3.27	3.20	3.54	3.50
Average royalties paid ($/mcfe)	0.12	0.14	0.10	0.17	0.15
Average operating expenses ($/mcfe)	0.33	0.31	0.30	0.29	0.28
Average transportation costs ($/mcfe)	0.19	0.19	0.18	0.13	0.16
Field netback ($/mcfe)	2.39	2.63	2.62	2.95	2.91
General & administrative expense ($/mcfe)	0.04	0.03	0.05	0.08	0.03
Interest expense ($/mcfe)	0.27	0.27	0.26	0.24	0.21
Cash netback ($/mcfe)	2.08	2.33	2.31	2.63	2.67
Financial ($000 except per share)					
Revenue and realized hedging gains (losses)	145,109	153,589	159,811	200,397	211,799
Royalties	5,801	6,399	4,879	9,543	9,232
Funds from operations	99,635	109,549	115,571	148,986	161,672
Funds from operations per share	0.60	0.66	0.70	0.90	0.98
Total dividends	29,677	29,677	29,677	29,677	54,408
Total dividends per share	0.18	0.18	0.18	0.18	0.33
Payout ratio	30%	27%	26%	20%	34%
Earnings	21,458	29,506	30,397	47,749	51,547
Earnings per share	0.13	0.18	0.18	0.29	0.31
Capital expenditures	112,215	69,716	14,978	35,454	134,411
Weighted average shares outstanding	164,874,175	164,874,175	164,874,175	164,874,175	164,874,175