Peyto Exploration & Development Corp.
President's Monthly Report

March 2012 — From the desk of Darren Gee, President & CEO

Some North American natural gas producers have been playing a dangerous game of chicken with natural gas prices, waiting to see who flinches first and shuts in their production to alleviate the bulging supplies. Logically, it should be the high cost production that goes first, assuming producers are logical. So far, Chesapeake with up to 1.0 BCF/d and Encana with 0.25 BCF/d have flinched. So too, Progress with 25 mmcf/d and Conoco with 100 mmcf/d. But really, the effect of the current low gas price has not yet been felt by the industry. And it won't be, until lease operating statements show the real effects of sub $3 gas prices on cash flows. Typically, a production manager won't see the lease op statement until 2-3 months after the price has been realized. That means March or April before these latest low prices are felt. This also means several months of potential losses before some producers react by shutting in, making those reactions even more dramatic. Figure 1 shows that the gas prices above and below the 49th parallel really didn't fall to the current levels until after the Q4 reporting period.

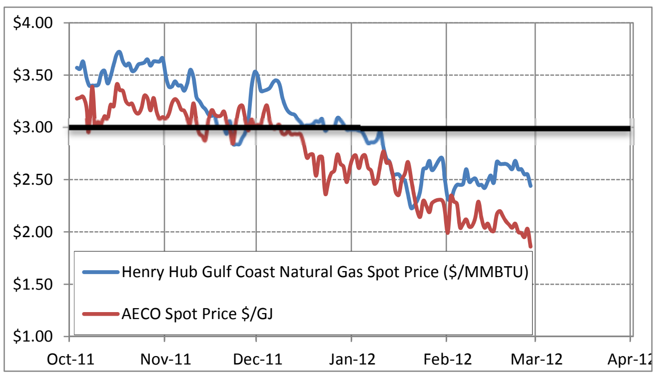

Figure 1

As in the past, this report includes an estimate of monthly capital spending, as well as our field estimate of production for the most recent month (see Capital Investment and Production tables below).

Capital Investment

*2011/12 Capital Summary (millions$ CND)**

	2010	Q1	Q2	Q3	Oct	Nov	Dec	Q4	2011	Jan	Feb	Mar	Q1 '12
Land & Seismic	18.5	6	1	14	6	0	1	7	28	2			
Drilling	140.5	51	32	46	15	19	15	49	178	20			
Completions	65.3	33	18	26	11	9	8	28	104	10			
Tie ins	30.3	7	5	10	4	2	5	10	32	2			
Facilities	19	8	16	16	0	0	0	0	40	1			
Drilling Credit Used	-7.6	0	-3	0	0	0	0	0	-3	0			
Total	**262**	**104**	**69**	**112**	**35**	**30**	**29**	**95**	**379**	**35**			

This is an estimate based on real field data, not a forecast, and the actual numbers will vary from the estimate due to accruals and adjustments. Such variance may be material. Tables may not add due to rounding.

Production

*2011/2012 Production ('000 boe/d)**

	Q1 11	Q2 11	Q3 11	Oct	Nov	Dec	Q4 11	Jan	Feb	Mar	Q1 12
Sundance	28.0	30.2	32.3	34.5	34.9	35.9	35.1	35.7	35.7		
Kakwa	2.6	3.2	3.0	3.1	3.2	3.9	3.4	3.6	3.7		
Other	1.1	1.1	1.0	1.0	1.4	1.5	1.3	1.7	1.8		
Total	**31.7**	**34.4**	**36.4**	**38.6**	**39.5**	**41.3**	**39.8**	**41.0**	**41.2**		

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The Value Proposition

Generally speaking, value is usually only created in our industry with the drill bit. Sure there is perceived value created if a company's stock price rises because they've bought a bunch of prospective land or paid full-up to acquire an asset that might have some inherent upside. But the real value creation usually only happens when the bit hits the ground and $1 of capital is turned into something more (in Peyto's case $2-$3).

That fact becomes evident when you really look hard at a company's performance year over year and what they've accomplished with their shareholder's capital. At Peyto, we're all shareholders. And so, every year we ask ourselves the hard questions like "what did my capital, in the hands of the Management, do for me this year?" "Did they create real value for me?" Pretty simple questions. Yet it's surprising how few companies endeavor to answer them.

Each year, as Management, we try to answer those very questions. By using independently determined reserves and net present value analysis of the company's assets, we attempt to dissect the changes that occurred from one year to the next and the results of the capital progams that were executed.

Unfortunately, in some years, there are many changes. Commodity prices change, royalties regimes can change, estimated costs change and well performance changes. All things that can change value and factor into the value creation answer.

Also, for any year's capital investment we can measure value creation a couple of different ways. Either we can measure it top down or bottom up. Top down is by comparing the total company value this year to last year and eliminating some of the changing variables; like commodity prices, for example. Or, bottom up, by just looking at the wells that were drilled with that capital and what value they hold.

Let's try bottom up to start. If we islotate the $379 million of total capital that Peyto invested in 2011, we see that money bought lands, shot seismic, built facilities, laid pipelines and

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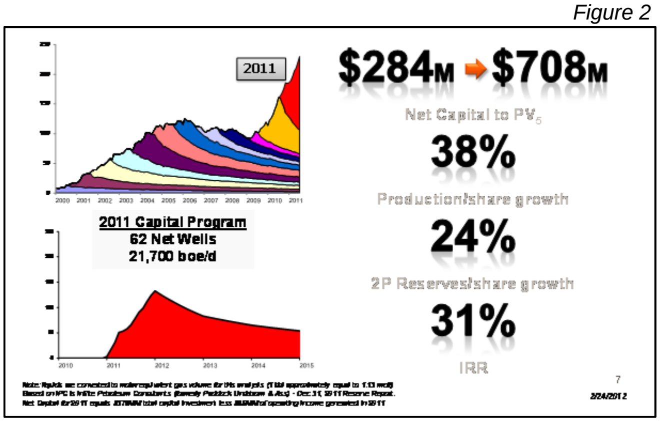
drilled 70 gross (62 net) wells that were ultimately brought on stream. The independent reserves evaluation valued those 62 net wells as at December 31, 2011 but the wells came on at various stages throughout the year, so we need to account for the $95 million of operating income they generated during the year. Net of the operating income, shareholders were out of pocket $284MM *($379MM-$95MM)* on December 31st. So what are those wells now worth?

The independent engineering evaluation of those wells suggests their net present value is $1.13B (undiscounted), $708MM (at a 5% discount rate) or $524MM (at a 10% discount rate). Conservatively, these assets are worth twice what it cost to build them. Or put another way, the $284MM will generate an internal rate of return of 31%. In isolation, very good return on capital and value creation for shareholders.

Figure 2



However, this isn't really a complete answer. "What if these wells were tapping into reserves that were already developed with previous vertical wells? That's not incremental value creation." Correct. Or, "don't these wells keep facilities full and per unit costs lower for existing reserves, thereby enhancing their value? Shouldn't they get some credit for that?" Also correct. So there can be a few pitfalls to looking just at the value of the wells drilled this year.

This is where a top down approach to measuring value creation can give a more complete picture. Subtracting one year from the last, accounts for all the changes in value, from incremental reserves development, changes in operating costs, backout of old production with new, new hedging activity, enhanced liquid recovery, etc. Everything that the Peyto team has done to increase (or decrease) value in the year.

Changing commodity prices can cloud that answer significantly, though, so we need to compare one year to the next using the same commodity price assumptions to isolate the value change.

In that total, top down analysis, which we detailed in our recent reserves release (http://www.peyto.com/news/2011Reserves.pdf), we showed that the $379MM of capital investment created net present value of $928MM (undiscounted), $745MM (at a 5% discount rate), or $639MM (at a 10% discount rate), and that was just in the Proved Developed Producing category. The discount rate where the value created equalled the capital investment was 60%, or a 60% IRR. If we include the new undeveloped value (P+P) that things like land purchases, new seismic and deep cut facilities create, the value creation can be as high as $1.6B (at a 5% discount rate).

Even though the bulk of the value creation starts with the drill bit, we can compliment it with many other value-adds from facility optimizations, to operating cost reductions. All value that the Peyto team creates with shareholder's capital.

If you are looking for a value proposition that involves sustainable value creation, then a company better be able to show you the math. Otherwise, where is the evidence? Peyto, on the other hand, has consistently demonstrated it can take a $1 of shareholders capital and turn it into more than $2 of value (Figure 3). I'll take that proposal all day long.

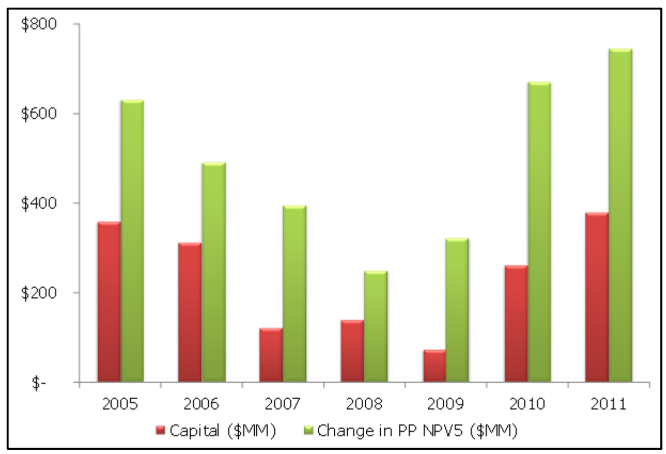


Figure 3

Activity Update and Commodity Prices

This past week finally showed some signs that dry gas production in the US is declining. Whether this is because of reductions in new drilling or shut ins of exisitng wells, it's hard to tell yet but it is at least encouraging. It is unlikely to have much effect on this year's storage situation, but at least market forces appear to be working.