

Peyto Exploration & Development Corp.

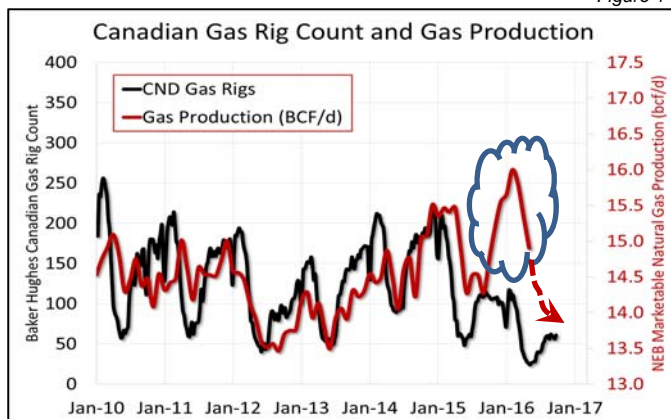
President's Monthly Report

October 2016

From the desk of Darren Gee, President & CEO

The NEB has updated their data on Canadian Marketable gas production and something has gone awry. Last winter's gas rig count should have resulted in less gas production than we saw according to previous correlations (Figure 1). There are 3 possible answers for this divergence: 1) a dramatic improvement in rig productivity, 2) an inventory of previously drilled but unconnected wells (DUCs) that are now used up, or 3) like in the US, we had a lot of oil rigs adding associated gas production. I personally believe its #2 and expect the correlation to re-emerge.

Figure 1



Source: Baker Hughes, NEB, Peyto

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) as well as any production deferrals.

Capital Investment*

2015/16 Capital Summary (millions\$ CND)*

	Q1 15	15	Q3 15	Q4 15	2015	Q1 16	Apr	May	Jun	Q2 16	Jul	Aug
Acq.	3	0	-6	0	-3	28	0	0	0	0	0	4
Land & Seismic	4	1	4	2	12	4	1	0	1	1	0	0
Drilling	70	59	88	71	287	63	8	7	15	30	20	21
Completions	43	33	44	54	173	33	2	0	5	8	5	11
Tie ins	7	11	15	16	49	12	0	1	1	3	4	6
Facilities	12	12	32	20	76	37	3	2	4	9	1	1
Total	138	117	177	163	594	176	14	10	26	50	30	43

Production*

2015/16 Production ('000 boe/d)*

	Q1 15	Q2 15	Q3 15	Q4 15	2015	Q1 16	Apr	May	June	Q2 16	Jul	Aug	Sept	Q3 16
Sundance	56.5	57.1	58.2	62.9	58.7	60.9	54.9	54.0	54.1	54.3	54.3	59.6	59.3	57.7
Ansell	16.8	15.4	12.6	21.2	16.5	24.6	20.5	19.1	20.1	19.9	20.5	20.5	22.0	21.0
Brazau	4.3	6.4	6.8	8.9	6.6	12.2	11.2	9.5	11.4	10.7	14.2	12.8	15.7	14.2
Kakwa	2.2	2.1	1.9	2.1	2.1	2.2	2.2	2.2	2.2	2.2	2.1	2.0	2.0	2.0
Other	1.7	1.6	1.5	1.7	1.6	1.7	0.6	1.2	1.7	1.2	1.4	1.5	1.4	1.4
Total	81.6	82.6	81.1	96.8	85.5	101.4	89.4	86.0	89.5	88.3	92.5	96.4	100.4	96.4
Deferral							17.1	19.9	15.1	17.4	9.3	4.3	3.4	5.7

*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.

A Barrel of Water

Last month I discussed Peyto's emissions intensity from various subsectors of our operations and compared it to other parts of Canada's oil and gas industry to illustrate how our focus on efficiency and profitability has translated into superior environmental performance. You can find more information on this topic in our recently posted 2016 Sustainability Report on our website at www.Peyto.com.

The other area we are also focused on with respect to environmental impact is water. Significant volumes of water are used in both drilling and completion operations to remove drill cuttings from wellbores and to fracture stimulate the tight sandstone reservoirs thus liberating the natural gas reserves. With the implementation of horizontal multi-stage fractured well designs in 2010, Peyto's use of water for fracturing has increased significantly. Which also means our management of water has become a larger part of our operations.

As you might expect, sourcing, pumping, hauling, heating and disposing of water throughout our operating areas comes with a significant cost. We drill source water wells into shallow aquifers for use in drilling fluids and frac water make up. We then store water at central sites to pump through pipelines or truck to pad locations for fracture stimulations. In winter, we have to heat all that water so it doesn't freeze. And then when we flow the fracs back and recover the majority of the frac water, we filter and store the reusable water in order to recycle it into the next stimulation. What we can't recycle, we truck away for disposal.

In total last year, we spent approximately \$46 million of the \$173 million of completion capital (27%) on activities associated with water (trucking, heating, pumping, disposing, etc.). In addition, we spent approximately \$10 million of the total operating costs of \$54 million (19%) dealing with flow back water. Combined, that's a lot of money spent handling water, which is surprising especially considering that our reservoirs in the Deep Basin are under saturated and don't contain any mobile water to begin with.

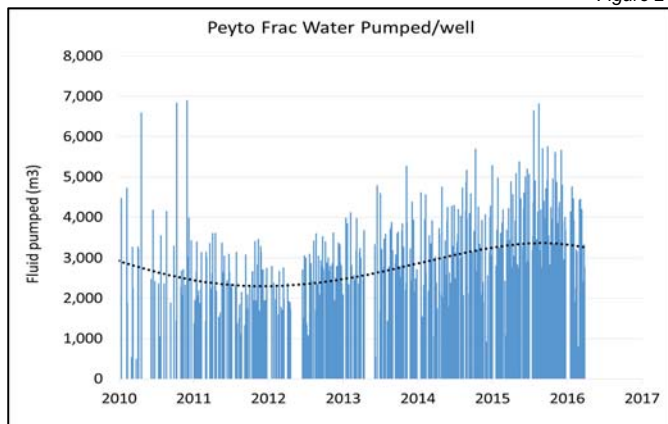
On average in 2015, we used approximately 3,800 m³ (24,000 bbls) of water per well, see Figure 2, or a total of 537,957 m³ (3,383,648 bbls). Of that water, about 22% was recycled from previous completions while 78% was obtained from fresh water sources. We expect in 2016, the percentage of recycled water will increase to 30% with a goal to be over 50% by 2018 (see Pg 8 of our Sustainability Report). Based on all the dollars spent to manage all that water it equates to almost \$17/bbl. Obviously optimization of all this water can have an enormous impact on both our capital costs and operating costs which directly impacts our profitability.

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Figure 2

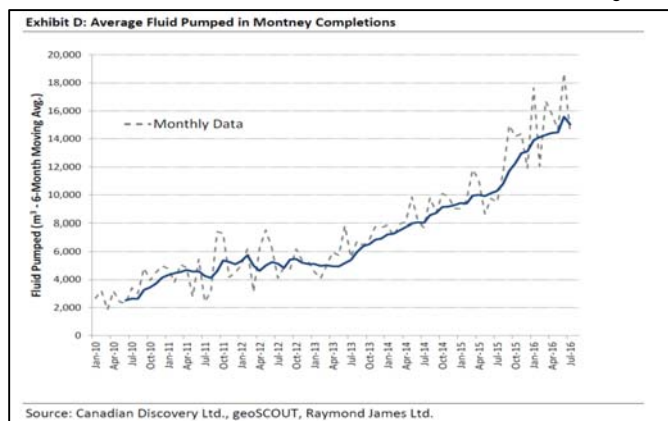


Source: Peyto

This cost is why we tend to have a “less is more” attitude towards increasing frac sizes. And is in big contrast to the rest of our industry which takes the opposite approach. It's also why we're trying to reuse as much water as we can throughout our operations.

Compare our volume for example, to the water used in the average Montney completion of late. Those wells are now receiving over 15,000 m³ of water in an effort to get higher rates and reserves from more intense frac'ing. Some operators are pushing this to 35,000 m³ (220,000 bbls)! Even at our incredibly low cost of \$17/bbl, that's over \$3.7MM per well in water costs alone (capital and operating). Not to mention the environmental impact of all that water. So when the goal is to try and make more money, as opposed to just more production, it's important to consider where your costs are actually coming from and the impact you're having.

Figure 3



Source: Raymond James

At the end of the day though, there should be something to gain from all this water that we use and all these cost we incur. So I

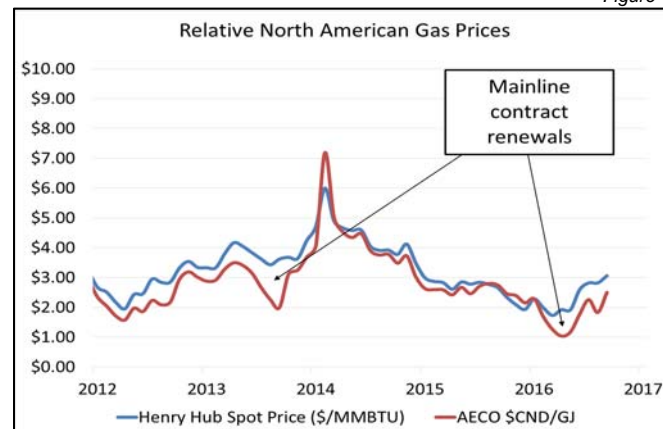
wondered, how much water does it take to develop the natural gas we need to heat our homes for a year?

Alberta Energy's website states that the average Alberta household uses about 120 GJs of natural gas per year. <http://www.energy.alberta.ca/NaturalGas/726.asp>. In 2015, Peyto developed an average 3.2 BCFe per well (about 3,600,000 GJ) using approximately 3,800 m³ of water (24,000 bbls). Therefore, our average well, which requires 24,000 bbls of water, can heat 30,000 homes for a year, or put another way, we used 0.8 bbls of water to heat your home for a year. Doesn't seem like very much, especially when you consider that's the same amount of water your teenager uses for one 15 minute shower.

Still, when it comes to fresh water, less is always more. The more energy we can extract with the least amount of water and cost, the more efficient we become, and the more profitable. And since that's the name of the game for Peyto, far be it from us to use a barrel more water than we need to.

Activity Levels and Commodity Prices

Figure 4



Source: Peyto, EIA

Both AECO and Henry Hub natural gas prices have recovered from their summer lows with HH pushing \$3/MMBTU and AECO now over \$2.50/GJ. With more TCPL mainline contract renewals this fall, I'd expect to see AECO tighten up to HH like we had for most of 2014 & 2015. The ol' Farmer's Almanac is predicting a very cold winter across much of North America so we should put a sizeable dent in the natural gas storage levels of both Eastern and Western Canada, as well as the US. That should take AECO back over \$3/GJ in 2017. Of course, that's all speculation on my part. At those levels, though, Peyto's business hums along very nicely. Other gas producers will be making more too, so we might have to be on the lookout for some cost inflation creeping back into the industry due to increased activity.