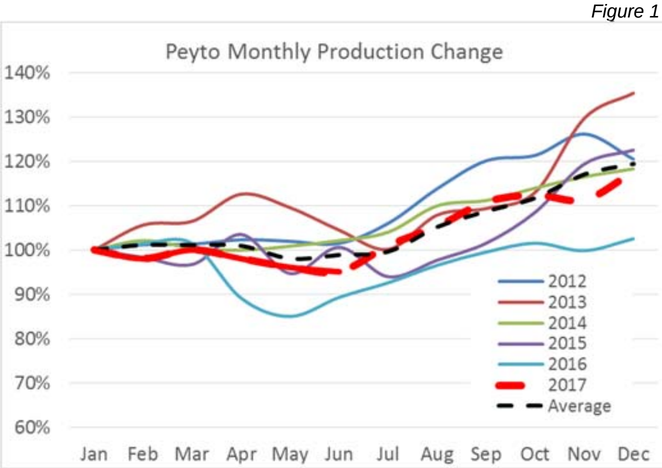
Peyto Exploration & Development Corp.
President's Monthly Report

July 2017 From the desk of Darren Gee, President & CEO

We seem to be through most of the heavy rains that followed spring breakup this year and caused excessively muddy conditions. We couldn't move a lot of equipment around in the field, especially frac pumpers, so we didn't put as much of a dent in our DUC (drilled uncompleted) well list as we had hoped. Now, as we move into the heart of summer, with long daylight hours and warmer weather, we should start to get caught up. That's normally when the bulk of our capital program and resulting volume additions really start to show up anyway. This year's not that dissimilar from past years when production has remained relatively flat for the first half, then ramped up in the second half (see Figure 1).

Figure 1



Source: 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*

2016/17 Capital Summary (millions$ CND)*

	Q1 16	Q2 16	Q3 16	Q4 16	2016	Jan	Feb	Mar	Q1 17	Apr	May
Acq.	28	0	5	1	34	0	0	3	4	0	0
Land & Seismic	4	1	1	4	9	8	0	1	9	1	1
Drilling	63	30	64	63	219	22	25	20	67	10	13
Completions	33	8	27	37	105	11	13	13	36	4	5
Tie ins	12	3	13	14	42	3	4	6	13	2	3
Facilities	37	9	4	11	60	9	5	11	25	9	5
Total	**176**	**50**	**114**	**130**	**469**	**53**	**47**	**54**	**154**	**25**	**28**

Production*

*2016/17 Production ('000 boe/d)**

	2015	Q1 16	Q2 16	Q3 16	Q4 16	2016	Jan	Feb	Mar	Q1 17	Apr	May	June	Q2 17
Sundance	59	61	54	58	59	58	59	59	59	59	58	55	55	56
Ansell	17	25	20	21	22	22	21	21	22	21	20	19	21	20
Brazeau	7	12	11	14	17	14	19	18	17	18	18	20	18	19
Kakwa	2	2	2	2	2	2	2	2	2	2	2	2	2	2
Other	2	2	1	1	1	1	2	2	1	1	2	1	1	1
Total	**86**	**101**	**88**	**96**	**102**	**97**	**102**	**100**	**102**	**101**	**100**	**98**	**97**	**98**

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

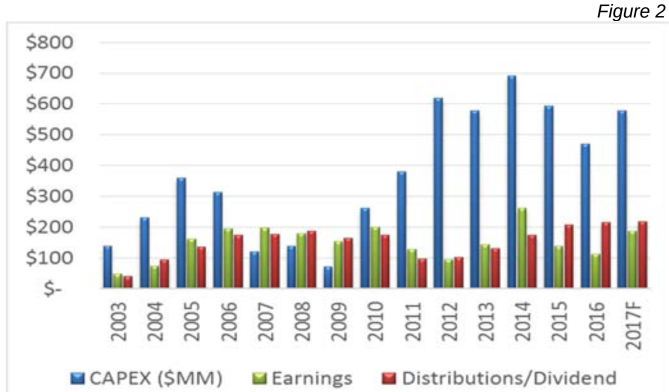
Why Pay A Dividend?

One of the most common questions I'm getting these days, from long time Peyto institutional investors who understand Peyto's returns driven strategy, is why we bother paying a dividend. If we believe we can continue to be as successful as we've been in the past, generating significantly above average returns for investors with our capital programs, why not re-invest the earnings into the business? Why take on debt or issue equity to outspend at certain times in the cycle? Why not cut off the dividend and re-invest those funds? Or, if we want to be counter-cyclical to the industry, which makes sense, why not offer special dividends at those times when you don't want to be investing as aggressively in the business (along with paying down debt and buying back stock)?

It's a great question and probably the one that we wrestle with the most as a board and management team when we're thinking about corporate strategy. Thankfully we can have this discussion, rather than what most companies discuss which is how to consistently generate any kind of profit? (*or maybe they don't, which is why they don't*). We also appreciate the confidence in our ongoing profitability shown to us by those investors asking this question in the first place.

Perhaps one of the single greatest reasons we pay a dividend is out of respect for the rightful owner of the money. As a management team, we invest our shareholder's capital. True, the vast majority of the Peyto team are also shareholders, but it doesn't change the fact that this is not Peyto's money - it's your money. We invest it on your behalf into the exploration and development of natural gas resources in Alberta. That investment is made in order to generate a profit or a return on that capital. And when we generate that profit, we deliver it to those who put up the capital in the first place. There is no assumption that we automatically get to re-invest the profit too.

Figure 2



Source: Peyto

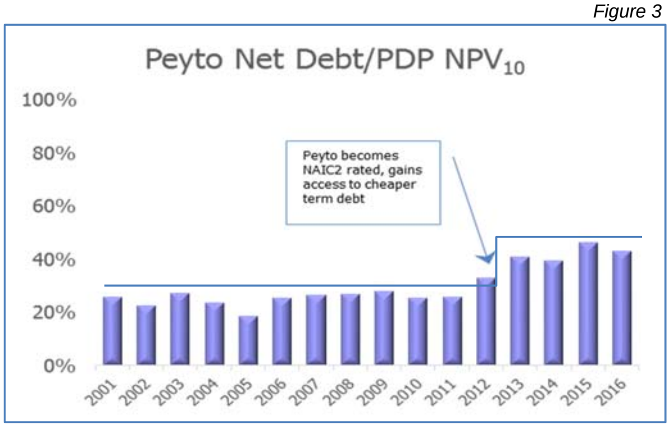
We've been doing it that way since 2003 when we first converted to a dividend paying energy trust (see Figure 2, where dividends/distributions are generally matched to earnings or profits from the capital investment). At that time, there was also a tax argument that could be made in favor of a payout model. Individual investors enjoyed a much lower aggregate tax rate than the corporation did (we estimated something around 20% for individual investors versus 45% for the corporation). So it made even more sense to put the profits in the hands of our investors. Today that tax advantage no longer exists as corporate tax rates have come down and personal tax rates gone up.

A steady dividend or distribution also broadened our investor base, as those investors that required a dividend could now invest in Peyto. The broader the investor base, the more liquidity we provide for all shareholders. A variable or sporadic dividend doesn't accomplish this.

We also knew from experience that a growth strategy alone has many pitfalls. They generally lack any kind of focus on profitability. Plus, it's a temporary strategy – you can't grow forever. Whereas a strategy that focuses on profits and returns can continue forever. So paying out the profits focuses the organization, and the entire Peyto team, on generating profit. And always paying out the profit creates competition for future capital. There is no entitlement to be able to re-invest the shareholders capital or his/her profits. You have to earn that right every year by delivering results.

Some investors will argue that the cost of any external capital is a burden on the business that doesn't need to be there. Perhaps. But is it really such a big burden? We have never used so much debt that it has created that much burden on the profitability of the business. Only in the last few years when our interest rates have become very attractive have we increased the leverage on the business. And even then, we're still conservatively levered.

Figure 3



Source: Peyto

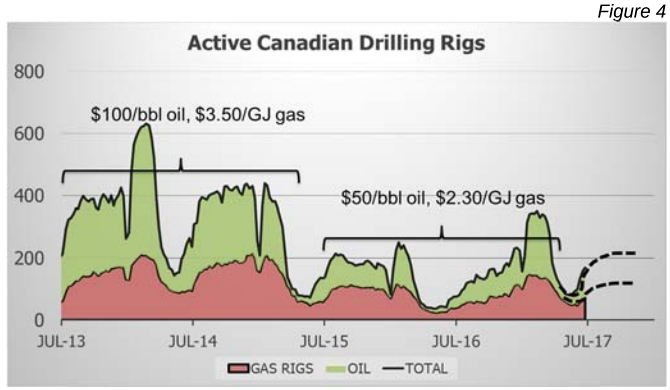
Plus, any equity we might issue (assuming its cost is competitive to debt), to accelerate the capital program, we can remove by buying back stock in the future when it's no longer the right time to aggressively invest capital. Just like paying down debt. That's all part of the counter cyclical strategy.

Lastly, when profits are paid to shareholders in cash, those dollars are now in your jeans and can't be deflated by market volatility, sentiment, machines trading on algorithms, or anything else that has nothing to do with Peyto's profitability. It provides shareholders with a much fairer form of liquidity. Just selling stock to achieve that liquidity sometimes results in selling a share of the reserves and the business at a steep discount to what it's really worth. We give you the real profits. If you want to reinvest your dividend because you feel the share price is undervalued, you have the ability to do just that.

Perhaps there will come a time when this payout model no longer makes sense or is no longer valued by investors. Nothing is ever set in stone. But that still won't change our focus on generating real returns and real profits on our shareholder's capital that we're deploying in the business. That has always been, and will always be, our primary goal.

Activity Levels and Commodity Prices

Figure 4



Source: Baker Hughes

The Canadian drilling rig count has increased slowly after spring breakup but has yet to climb back over 200. Considering the recent drop in oil prices and backwardation in the future gas curve (drops off as you go out) I don't think we can justify more than around 200 rigs with the industry's revised cashflows. That's good news for Peyto as it takes inflationary pressures off the service costs that were showing up in Q1. That should allow us access to additional pressure pumping equipment and people at reasonable pricing so we can catch up on completions. Perhaps, if costs even come down a bit, we might even justify a 10th drilling rig for a portion of Q3/Q4 to get ahead.

BTW, the oil price drop and pullback out of Canada by major US producers is also creating an opportunity for us to add new undeveloped lands in key areas at reasonable prices.