

Peyto Exploration & Development Corp.

President's Monthly Report

November 2011

From the desk of Darren Gee, President & CEO

My sprinklers are blown out, my winter tires are on and my eaves are clear of all the fallen leaves. I'm officially ready for winter. At Peyto, we're also readying ourselves for a busy winter drilling season ahead. Six rigs are currently active and we expect they will remain so right through to spring. The Farmers' Almanac is calling for "Clime and Punishment" this winter. They predict the Canadian Prairies will be very cold, while the rest of Canada will be normal. As for our neighbors to the south, it's no surprise that North Dakota can't attract enough oilfield workers with a bitter winter forecast for this year, while all the money managers out east will have to deal with big-time snow, similar to last year. In general, it looks to be a cold one, which should bolster natural gas prices.

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 Capital Summary (millions\$ CND)*

	2010	Q1 '11	Apr	May	Jun	Q2 '11	July	Aug	Sept	Q3 '11
Land & Seismic	18.5	6	0	1	1	1	1	7	6	14
Drilling	140.5	51	13	10	9	32	17	14	15	46
Completions	65.3	33	8	4	5	18	8	10	8	26
Tie ins	30.3	7	2	1	1	5	4	3	4	10
Facilities	19	8	4	4	8	16	4	6	6	16
Drilling Credit Used	-7.6	0	-1	0	-2	-3	0	0	0	0
Total	262	104	26	20	22	69	33	40	39	112

*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

2010/11 Production ('000 boe/d)*

	Q4 09	Q1 10	Q2 10	Q3 10	Q4 10	Q1 11	Q2 11	Jul	Aug	Sept	Q3 11	Oct
Sundance	15.9	16.5	18.5	20.1	24.6	28.0	30.2	31.2	32.1	33.8	32.3	34.5
Kakwa	2.4	2.8	2.7	2.6	2.6	2.6	3.2	2.9	3.1	3.1	3.0	3.1
Other	1.1	1.3	1.1	1.0	1.1	1.1	1.1	1.1	1.0	1.0	1.0	1.0
Total	19.4	20.6	22.3	23.8	28.2	31.7	34.4	35.1	36.2	37.9	36.4	38.6

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Cash Back

An investment, by definition, is about putting money to work to ultimately yield more money. But couldn't you also describe a business the same way? Regardless what industry you are in, or whether you produce barrels of oil or widgets, the goal of any business is to make more money back than what you put in. It's at the root of any business. My daughter on the sidewalk understands this simple math all too well, especially when my wife starts charging her for the lemonade mix and the cookies she's so eager to sell. All of a sudden the price has to reflect more than the input cost. But the difference between an investment and a business is that the business has to be profitable to be successful. Profitability, on the other hand, doesn't always have to be

present for an investment to yield more money back than you put in.

This concept has always been a tough one for me because I think about investing the same way I think about business. In reality, there are many investors who obviously do not. That is where capital markets play a dual role. You can use the capital markets to invest in a stock, with the goal of making more money if it goes up, or you can use it to purchase a share of a company that is in the business of generating a profit. Warren Buffet is more critical in differentiating the two. He would say one is a bet, banking on the greater fool theory, and the other is a value investment that can be held forever.

In the publicly traded oil and gas industry, sometimes the biggest challenge is differentiating the two. Is a company about selling hydrocarbons for profit or is it about selling shares in a story? Both can be (and are) valid options for investors in today's markets. But if its about the former, how can one get a sense of that profitability?

If, as in Peyto's case, the company is about the business of making money from the development and sale of oil and natural gas, then it is all about the input costs versus the price we're selling it for. Unfortunately, unlike my daughters sidewalk stand, we can't dictate the selling price. Truth be told neither can she. I'm not paying \$5 for a cookie and \$10 for a glass of lemonade! (Well, maybe I am, but most people won't). Peyto, on the other hand, has to take the price that the market is offering since we're not the only producer on the block. That said, the only thing we can then control is the input cost.

Our input costs are the cost to build it and the costs to produce it. In quick and dirty terms, we measure the costs to build it is as either the Finding, Development & Acquisition cost (FD&A) or the Capital Efficiency. FD&A is measured in total cost per ultimate recoverable barrel that will come out of the ground and Capital Efficiency is the total cost to build the next producing barrel. In Peyto's case, for 2010, FD&A was \$12/boe for the Proved Producing barrel of reserves or \$17,300 per flowing boe in capital efficiency.

In addition to the costs to build it, we have the cost to produce it. Operating costs, royalties, transportation, G&A and interest all make up the cash costs which is often just netted off the selling price to give us how much cash we retain from the sale of every barrel (ie. the netback). Combining both the cost to build it and the cost to produce it, we get a sense of how quickly we can get our cash back from every dollar invested in oil and gas and how much profit we might make.

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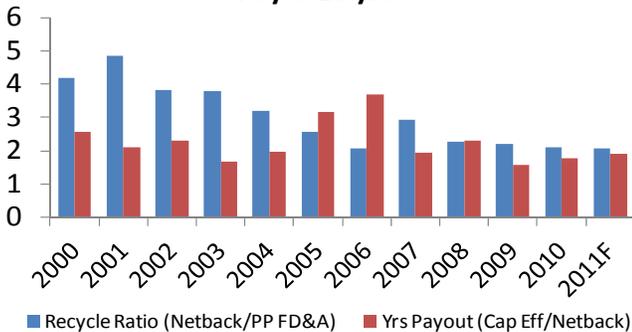
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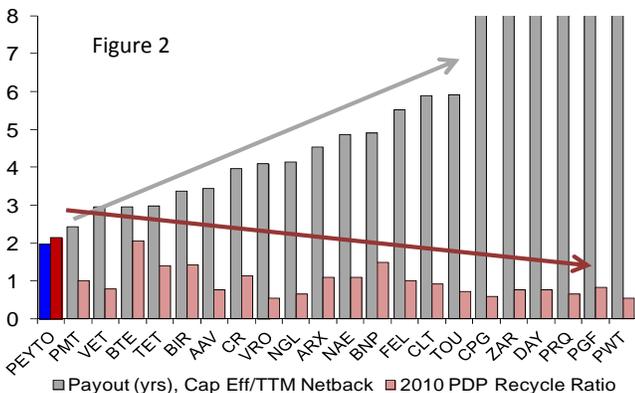
For instance, if we divide our Q2 2011 cash netback of \$24/boe by the FD&A cost of \$12/boe, then we determine that we should make \$2 for every \$1 we invest or \$12 on every barrel we develop and sell. Pretty simple, except that it doesn't tell us how long it will take to get our cash back. If we divide the capital efficiency of \$17,300/boe/d by the \$24/boe netback we get 720 days or about 2 years to get our money back. Between the two simple calculations, we get a sense of how much and how quickly we get cash back (and how much is left to get after we do). Looking at those two numbers over time we can see how Peyto was doing historically, even with changing commodity prices.

Quickie Profitability Analysis Figure 1
Peyto 10 yrs



Generally speaking, the most profitable years were the ones with the highest recycle ratio and shortest payout. But does that quick math always work? Obviously there is a much more rigorous calculation of return and payout when we use detailed forecasts of cash-flow brought back into today's dollars. But the quick math shown above is reasonably close to the detailed cases we've run.

How does the rest of the industry stack up for perspective? I've borrowed the base declines for each producer from Peter's and Co. research in order to calculate capital



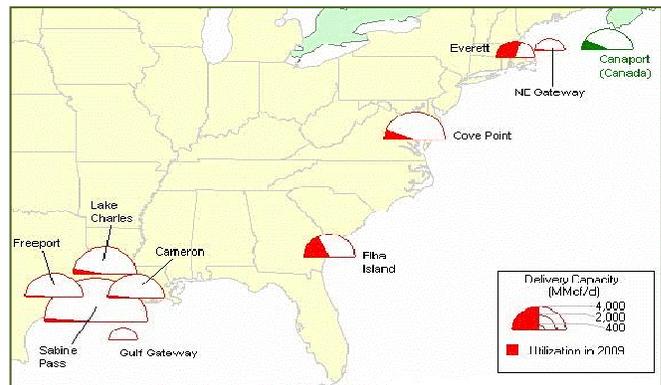
efficiency for the trailing four quarters and compared that to the PDP recycle ratio from year end 2010.

Perhaps it doesn't come as a surprise that as payout times increase and profitability drops, recycle ratios also drop off. Admittedly it's not a perfect correlation. Sometimes capital projects can payout quickly but have little left over, meaning recycle ratios would be low. Conversely, sometimes projects take a while to payout but yield higher returns and high recycle ratios.

In general, however, if cash back is quick and there is a decent amount left, then profitability is usually high, and those are the types of businesses that make money. If there is also growth, then you know that the growth is profitable. In those cases, you're less reliant on the greater fool paying more for the potential than you paid, because you own a share of a real, profitable business.

Activity Update and Commodity Prices

Kitamat was officially granted its LNG export license by the National Energy Board (NEB) on October 13, 2011. A 20 year license that brings real Canadian exports of natural gas, to markets other than the U.S., just one step closer. And starts to put pressure on similar projects on the U.S. west coast from a market competition standpoint. In addition to east coast proposals for bi-directional LNG terminals at Cove Point, Sabine Pass and Freeport (see map below), there is talk of a terminal in Coos Bay, Oregon that would tap the same markets as Kitamat.



All of these are solutions to the natural gas oversupply situation we are currently experiencing in North America but are also 4-5 years away at best. Until then we are going to have to continue to endure selling our natural gas for just a fraction of what the world is prepared to pay. Thankfully, with our long reserve life assets, much of the production and reserves we are developing today will still be on when the time comes to see those better prices.