

Peyto Exploration & Development Corp.

President's Monthly Report

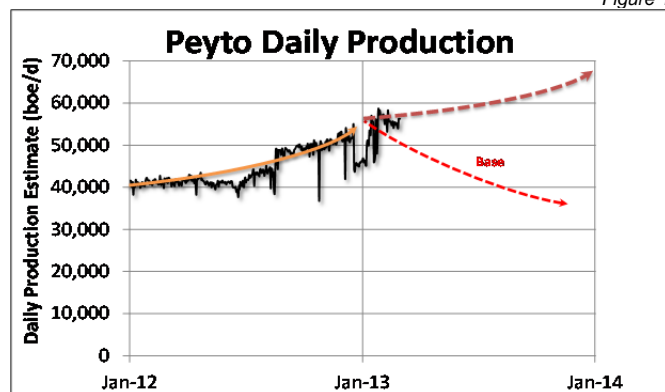
March 2013

From the desk of Darren Gee, President & CEO

It hasn't been the cold winter we were hoping for in North America. A cold winter would have burned off the excess natural gas in storage. Current weather forecasts to the end of March don't look particularly constructive either, but a recent surge in coal prices to within \$1.50 to \$1.75/mmbtu of natural gas prices has caused some fuel switching which is consuming more gas. It's good to know there is solid support for natural gas price at this level (\$3ish) - especially since it's a level where we still make a decent profit.

Our winter program is progressing with several new drill pads underway and we await another surge of new production in the coming weeks. Figure 1 shows the daily plot.

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*

2012/13 Capital Summary (millions\$ CND)*

	2011	Q1	Q2	Q3	Oct	Nov	Dec	Q4	2012	Jan	Feb	Mar	Q1
ONR Acq./other acq.				205			-21	-21	184				
Land & Seismic	28	3	1	2	4	0	2	6	12	0			
Drilling	178	52	23	59	26	30	23	78	211	24			
Completions	104	31	14	35	11	15	21	47	127	9			
Tie ins	32	8	5	11	8	5	9	22	46	6			
Facilities	40	4	3	6	2	3	20	25	37	9			
Total	379	99	46	317	50	53	54	157	618	49			

Production*

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

	2011	Q1 12	Q2 12	Q3 12	Oct	Nov	Dec	Q4 12	2012	Jan	Feb
Sundance	31.3	35.4	34.3	35.7	36.6	37.5	34.0	36.0	35.4	36.4	40.7
Kakwa	3.1	3.8	4.2	3.6	3.2	3.2	2.9	3.1	3.7	3.2	3.1
Ansell	-	-	-	2.9	5.9	6.5	8.1	6.8	2.4	9.2	9.0
Other	1.1	2.0	2.8	3.6	3.4	3.8	3.5	3.6	3.0	3.2	3.2
Total	35.5	41.2	41.3	45.9	49.1	51.0	48.5	49.5	44.5	52.0	56.0

*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.

Scalable Value Adds

This is the time of year, with our reserve report freshly in hand, when we can confirm whether the investments we've made this past year have paid off. And we made a lot of them - a record \$618 million worth! For the first time, a good chunk of the money was spent buying assets.

So, as a big shareholder myself, the burning question I always have is, what kind of return did **my** money generate?

It's not too difficult to break out all the "organic" capital and see what we got for that, because, as usual, it was spent drilling wells and building infrastructure. Of the \$452 million of "organic" capital, 85% was on well related investments - drilling and completing wells, installing wellsite equipment, and laying pipelines. Another 8% was invested into facilities, including modifying our Oldman plant to extract more natural gas liquids from the gas stream. The remaining 7% was spent on land sales, seismic acquisitions and tuck-in property acquisitions, just like any other year.

Unlike any previous year, however, \$452 million was the most we've ever invested. So inherent in the returns question is a question of efficiency and scalability. If we generated good returns at this and previous levels of capital investment, can we get the same results putting even more capital to work?

Figure 2

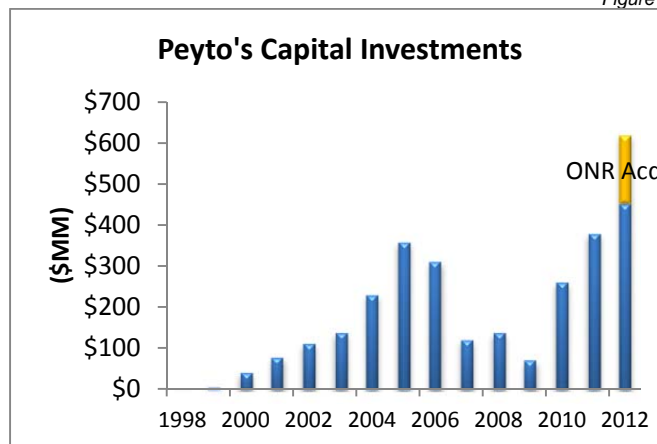


Figure 2 shows the annual capital investments Peyto has made. Note that in 2012, an extra \$166 million (net of dispositions) was spent acquiring Open Range.

All of the 86 gross (76 net) wells drilled and brought on production in 2012, with the \$452 million, were drilled horizontal and completed with multi-stage fracture stimulations. This organic capital investment resulted in a total wedge of new production that peaked during the week of

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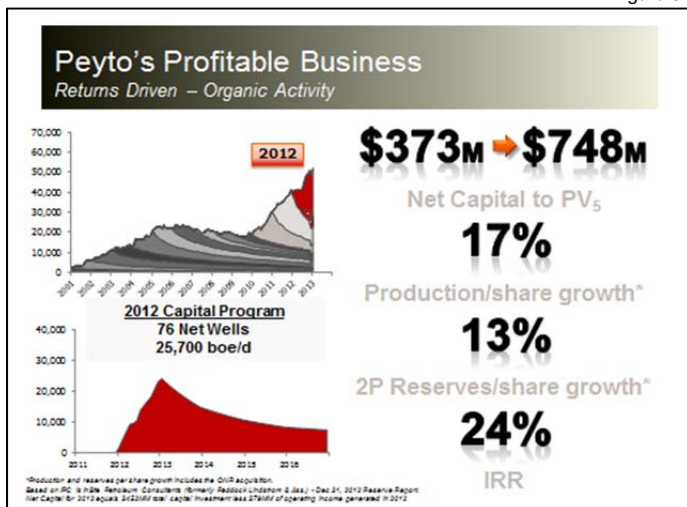
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January 14th at 25,700 boe/d (after we solved our plant outage). The ratio of \$452 million over 25.7 kboe/d is \$17,600/boe/d, or what we often call capital efficiency. Although this metric doesn't tell us returns or profitability, it is the same ratio as we've had in the past three years, so does give us a hint about the answer to the question of efficiency and scalability.

We can extract from our independent engineering report this group of wells and look at the value assigned to their reserves to get an idea about the internal rate of return of the capital used to develop them. However, because this value analysis is as of December 31, 2012, we have to adjust for the net operating income these same wells generated up to that date. If we subtract from the \$452 million of total capital, the \$79 million that these wells generated during 2012, we arrive at the \$373 million of net investment as of December 31, 2012.

The independent engineers say these wells are worth \$748 million of before tax net present value (5% discount rate). So just like much of Peyto's history, we took \$1 and turned it into \$2. I like that math. Conversely, if we discount all future cashflows at 24%, then the before tax net present value is \$373 million, equal to the net capital investment, thus giving us the internal rate of return (see Figure 3).

Figure 3



When we compare this same analysis to last year (see my March 2012 monthly report) we see that last year we generated a 31% IRR vs this year at 24%. At first blush, not quite as good. But we also need to remember that the commodity price forecast the independent engineers are using is some 20% lower this year than last year. So adjusting for that, 2012 looks to be a very similar economic result to 2011.

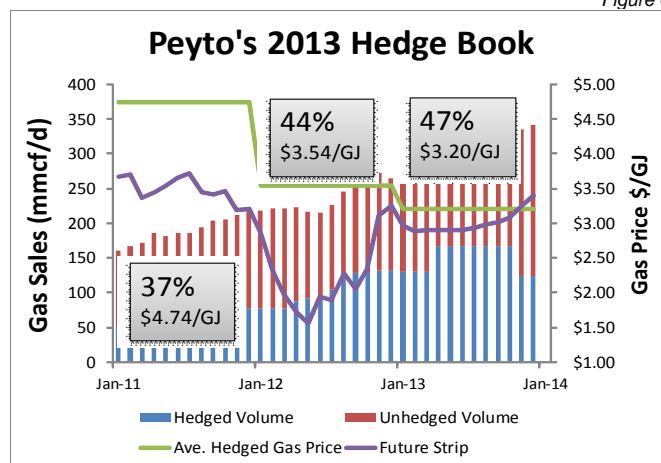
So now we've answered both questions. *What kind of return did Peyto generate with my money?* A very good one in aggregate. *Was the level of capital investment scalable?* It sure looks like it, considering that a 20% larger capital program delivered similar results.

But what about the corporate acquisition? Peyto spent some \$166 million (net of a minor asset disposition) for Open Range. What's the return on that?

Unfortunately, we can't really answer that question yet because we haven't finished with that investment. We've only invested the first half of an estimated \$400 million of total investment. As we start to develop the undeveloped lands and fill the excess processing capacity with new producing reserves, we'll begin to realize the true returns for shareholders. I suspect they will ultimately be very competitive with our organic program.

Activity Update and Commodity Prices

Figure 4



The current 2013 strip for Alberta natural gas price is still hanging around \$3/GJ despite the lackluster winter we've had. At Peyto, we have been consistently forward selling to secure that's at least what we'll get. Almost half of our projected volumes for 2013 are now forward sold at an average of \$3.20/GJ (Figure 4). With Peyto's heat content, this \$3.20/GJ price would translate into approximately \$3.70/mcf, to which we would add natural gas liquids revenues, further lifting it to approximately \$4.75/mcfe.

When you consider that Peyto's operating margin is the highest in the industry at 75%, that leaves us with a pretty healthy netback and ample justification for the current aggressive pace of investment.