PEYTO

Exploration & Development Corp.

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Interim Report
for the three months ended March 31, 2003

Highlights

Three Months Ended March 31	**2003**	2002	% Change
Operations			
Production			
Natural gas (mcf/d)	**57,452**	35,049	*64*
Oil & NGLs (bbl/d)	**2,689**	1,409	*91*
Barrels of oil equivalent (boe/d @ 6:1)	**12,265**	7,250	*69*
Average product prices			
Natural gas ($/mcf)	**8.50**	4.46	*91*
Oil & NGLs ($/bbl)	**44.23**	24.42	*81*
Average operating expenses ($/boe)	**1.01**	1.44	*(30)*
Field Netback ($/boe)	**35.09**	19.52	*80*
Financial ($000)			
Revenue	**54,670**	17,150	*219*
Royalties (net of ARTC)	**14,820**	3,472	*327*
Funds from operations	**37,309**	12,098	*208*
Net earnings	**18,495**	5,925	*212*
Capital expenditures	**40,486**	22,549	*80*
As at March 31			
Debt, including working capital deficit	**114,028**	71,976	*58*
Shareholders' equity	**89,696**	47,207	*90*
Total assets	**292,282**	155,390	*88*
Common shares outstanding (000)	**43,452**	42,976	*1*
Weighted average shares outstanding (000)	**43,446**	42,184	*3*

Per share data ($/share)			
Funds from operations			
Basic	**0.86**	0.29	*197*
Diluted	**0.81**	0.28	*189*
Earnings			
Basic	**0.43**	0.14	*207*
Diluted	**0.40**	0.14	*186*

Report from the President

Peyto Exploration & Development Corp. is pleased to present its quarterly financial and operating results for the period ended March 31, 2003.

Quarterly Review

Production for the quarter ended March 31, 2003 was up 69% from the same period in 2002, averaging 57.5 mmcf of natural gas and 2,689 barrels of light oil and natural gas liquids per day. Peyto has now grown its production for twelve consecutive quarters. This production gain combined with strong commodity prices increased cash flow 208% from $12.1 million in 2002 to $37.3 million in 2003. Earnings mirrored cash flow with a 212% year over year increase from $5.9 million in 2002 to $18.5 million in 2003. Product prices averaged $8.50 per mcf for gas and $44.23 per barrel for oil and natural gas liquids. Operating costs dropped 30% to $1.01 per barrel of oil equivalent ("boe", natural gas converted on a 6:1 basis throughout). The high commodity price environment caused field netbacks to increase 80% from $19.52 per boe to $35.09 per boe. Comparative operational and financial data is presented in the following table.

Given the record level of drilling activity in the first quarter of 2003, Peyto initiated an independent reserve review to evaluate the new additions. Proved developed reserves at the end of the quarter increased by 19% to 52.8 million boes from 44.4 million boes at year end 2002. As in the past, Peyto has not allocated a proved reserve designation to undeveloped property and accordingly had no proved undeveloped reserves booked at March 31, 2003. During the quarter, Peyto successfully drilled or re-entered 24 wells, all previously identified as probable reserves, and converted them to proved developed. Proved plus probable additional reserves remained constant at 86.1 million boes as the independent review did not address additional probable opportunities. Proved developed reserves maintained an 11.8 year reserve life based on first quarter average production. Discounted at 10%, the net present value of Peyto's proved petroleum and natural gas assets increased 27% from $517.4 million at December 31, 2002 to $655.2 million at March 31, 2003, an increase of 34% on a per share basis. The following table summarizes Peyto's reserves and the discounted net present value of future cash flow before income tax, using variable pricing, at March 31, 2003.

Reserve Category	Gas (mmcf)	Oil & NGL (mstb)	BOE 6:1 (mstb)	Reserve Life Index (years)	Net Present Value ($000) Discounted at 8%	10%	12%
Proved Producing	220,562	9,769	46,529	10.4	652,469	591,470	542,649
Proved Non-producing	30,460	1,213	6,290		70,800	63,713	58,308
Proved Undeveloped	-	-	-		-	-	-
Total Proved	251,022	10,982	52,819	11.8	723,269	655,183	600,957
Probable Additional	159,758	6,632	33,258		271,696	230,658	199,225
Proved + Probable Additional	410,780	17,614	86,077	19.2	994,965	885,841	800,182

Note: Based on the Paddock Lindstrom & Associates report effective March 31, 2003

Activity Update

Prior to spring breakup, Peyto had five drilling rigs operating in the Deep Basin area which have drilled and cased 28 gas wells since year end, all with a total depth greater than 2,200 meters. Drilling, completion and pipeline operations are currently suspended and will resume following spring breakup.

Peyto Energy Trust

On April 14, 2003 Peyto announced that its Board of Directors had unanimously approved a proposal to reorganize Peyto into an energy trust (the "Trust"). The reorganization will be consummated by way of a plan of arrangement pursuant to the Business Corporations' Act (Alberta). The information circular containing details of the proposed reorganization and plan of arrangement is expected to be mailed out to shareholders on or about May 27, 2003. An annual and special meeting of shareholders will be held June 24, 2003 to approve among other things, the proposed reorganization.

The Trust will differentiate itself from other energy trusts by having a proven team that has successfully used the drill bit to build a high quality asset base with the unique combination of long life reserves and low operating costs. Peyto's proved producing reserve life at year end was 10.5 years. The reserve life of Peyto's tight gas production base is forecast to increase over time. Peyto plans to continue building value by developing high quality opportunities with the drill bit.

The Trust will make monthly cash distributions to holders of trust units while retaining a sufficient amount of cash to fund its ongoing exploration and development projects. For the second half of 2003, it is anticipated that Peyto will distribute at least 50% of the cash flow or a minimum of $0.15 per trust unit per month. Peyto's cash distributions appear low when expressed as a percentage of cash flow, however due to Peyto's low cost structure, on a per boe basis, the distributions will be on par with other energy trusts that distribute a significantly larger percentage of cash flow. Our competitive advantages that include a low rate of depletion and high netbacks, will allow us to expand our capital program in a non-dilutive manner in an effort to increase cash distributions over time.

Outlook

Capital expenditures for 2003 are expected to be between $110 million and $160 million, the bulk of which will be funded by cash flow. The majority of the 2003 capital program will involve the drilling, completion and tie-in of low risk development gas wells adjacent to existing infrastructure in the Sundance area. Peyto continues to have an abundance of investment ideas and opportunities to pursue. In order to learn more about Peyto we encourage you to visit Peyto's website at www.peyto.com where you will find a current presentation, financial and historical news releases and an updated insider trading summary.

Don T. Gray, P.Eng.
President and Chief Executive Officer
May 12, 2003

This report, or any part of it, may include comments that do not refer strictly to historical results or actions and may constitute forward-looking statements. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Corporation or of the industry to be materially different from any results, performance or achievements expressed or implied by such forward-looking statements. Such risks, uncertainties and other factors include general and industry economic and business conditions which, among other things, affect the demand for the commodities produced by the Corporation, competitive factors and industry capacity, the availability of personnel to manage the Corporation and manage and deliver the commodities produced, the ability of the Corporation to finance and implement its business strategy, changes in, or the failure to comply with, government law and regulations (especially relating to health, safety and environment), weather and other such risks as may be identified in this report or in other published documents. Accordingly, there is no certainty that the Corporation's plans will be achieved.

Management's discussion and analysis

Management's discussion and analysis of financial conditions and results of operations should be read in conjunction with the unaudited interim financial statements for the three month period ended March 31, 2003 and the audited financial statements for the year ended December 31, 2002.

Gross revenues totaled $54.7 million for the first quarter of 2003, an increase of 219 percent from $17.2 million in the first quarter of 2002. This increase is a result of higher production volumes combined with stronger commodity prices. The price of natural gas averaged $8.50 per mcf for 2003 up 91 percent from $4.46 per mcf in 2002. Oil and natural gas liquids prices averaged $44.23 per barrel in 2003 up 81 percent from $24.42 per barrel in 2002.

A successful drilling program resulted in natural gas production for the quarter increasing by 64 percent to 57.5 mmcf per day in 2003 from 35.0 mmcf per day in 2002. Oil and natural gas liquids production increased by 91 percent to 2,689 barrels per day in 2003 from 1,409 barrels per day in 2002. Production for the quarter averaged 12,265 barrels of oil equivalent (boe", natural gas converted on a 6:1 basis) per day, an increase of 69 percent from 7,250 boe per day for 2002.

2003 royalties, net of Alberta Royalty Tax Credit (ARTC), increased by 327 percent to $14.8 million from $3.5 million in 2002 due to higher gross revenues associated with increased production volumes. The 2003 average royalty rate was 27 percent compared to 21 percent for 2002. The royalty rate, expressed as a percentage of sales, will fluctuate from period to period due to the fact that natural gas crown royalties are calculated based on the Alberta Natural Gas Reference Price rather than the price achieved by the corporation, which can differ significantly.

Increased production volumes caused operating costs to rise to $1.1 million in 2003 from $0.9 million in 2002. On a barrel of oil equivalent basis, operating costs were $1.01 per boe in 2003 compared to $1.44 per boe in 2002. Operating costs are comprised of field expenses and natural gas transportation costs net of income generated by the processing and gathering of joint venture gas. On a per boe basis, field expenses represent $1.18, transportation $0.56 and processing and gathering income a recovery of $0.73.

General and administrative expenses increased by 107 percent to $212,000 for 2003 from $102,000 in 2002. The Corporation does not capitalize general and administrative expenses. On a boe basis, general and administrative expenses decreased by 32 percent to $0.19 per boe in 2003 from $0.28 per boe in 2002. This reduction was the result of the increase in production volumes while maintaining a similar level of staff.

Financing charges for 2003 were $895,000 up from $467,000 in 2002. The increase was the result of higher debt levels associated with Peyto's 2003 first quarter capital expenditure program which totaled $40.5 million compared with $22.5 million in 2002.

Depreciation, depletion and site restoration expenses were $4.9 million for 2003 compared to $2.3 million for 2002 as a direct result of Peyto's increased asset base and production volumes. On a per boe basis, the average depreciation, depletion and site restoration rate decreased to $4.50 in 2003 from $5.14 in 2002.

The provision for future income tax increased to $13.8 million in 2003 from $3.9 million in 2002. The increase in the tax provision in 2003 is a direct result of Peyto's increased profitability due to higher production volumes and commodity prices.

The 69% increase in production volumes combined with strong commodity prices caused funds from operations for 2003 to increase to $37.3 million compared with $12.1 million in 2002. Higher average natural gas and liquids prices caused Peyto's field netback for the period to increase from $19.52 per boe in 2002 to $35.09 per boe in 2003. Earnings for 2003 were $18.5 million or $0.43 per share compared with $5.9 million in 2002 or $0.14 per share.

For the quarter ended March 31, 2003, the Corporation incurred net capital expenditures of $40.5 million. Capital expenditures for the quarter were comprised of $32.5 million for exploration and development, $6.6 million for facilities, gathering systems and equipment and $1.4 million for acquisitions and land. At March 31, 2003, the Corporation had a working capital deficiency, including the revolving demand loan, of $114.0 million, resulting in a net debt to running cash flow ratio of 0.8:1 based on annualized first quarter cash flow. Capital expenditures for 2003 were funded primarily by cash flow and bank debt, with equity issues limited to the exercise of stock options.

Quarterly information

	2003	2002			
	Q1	Q4	Q3	Q2	Q1
Operations					
Production					
Natural gas (mcf/d)	**57,452**	50,556	45,018	38,194	35,049
Oil & NGLs (bbl/d)	**2,689**	2,349	2,009	1,512	1,409
Barrels of oil equivalent (boe/d @ 6:1)	**12,265**	10,775	9,512	7,878	7,250
Average product prices					
Natural gas ($/mcf)	**8.50**	5.90	3.49	4.43	4.46
Oil & natural gas liquids ($/bbl)	**44.23**	36.52	33.67	29.95	24.42
Average operating expenses ($/boe)	**1.01**	1.12	1.36	1.67	1.44
Field netback ($/boe)	**35.09**	25.15	16.42	19.72	19.52
Financial ($000)					
Revenue	**54,670**	35,354	20,676	19,530	17,150
Royalties (net of ARTC)	**14,820**	9,311	5,122	4,197	3,472
Funds from operations	**37,309**	23,746	13,474	13,185	12,098
Net earnings	**18,495**	10,310	5,957	6,362	5,925
Capital expenditures	**40,486**	37,627	24,105	28,270	22,549
Common shares outstanding (000)	**43,452**	43,418	43,321	43,143	42,976
Per share data ($/share)					
Funds from operations					
Basic	**0.86**	0.55	0.31	0.31	0.29
Diluted	**0.81**	0.52	0.30	0.30	0.28
Earnings					
Basic	**0.43**	0.24	0.14	0.15	0.14
Diluted	**0.40**	0.23	0.13	0.14	0.14

Financial statements

Balance Sheet

As at	**March 31 2003 (unaudited) $**	December 31 2002 (audited) $
Assets		
Current assets		
Cash	**10,794**	205,558
Accounts receivable	**33,658,621**	18,860,110
Prepaids and deposits	**800,130**	894,553
	34,469,545	19,960,221
Property, plant and equipment *(Notes 2 and 3)*	**257,812,804**	222,206,233
	292,282,349	242,166,454
Liabilities and Shareholders' Equity		
Current		
Accounts payable and accrued liabilities	**52,787,944**	50,778,415
Current taxes payable	**482,555**	166,922
Revolving demand loan *(Note 3)*	**95,226,908**	80,000,000
	148,497,407	130,945,337
Future site restoration and abandonment	**469,806**	380,914
Future income taxes	**53,619,126**	39,773,845
	54,088,932	40,154,759
Shareholders' equity		
Share capital *(Note 4)*	**19,365,013**	19,230,677
Retained earnings	**70,330,997**	51,835,681
	89,696,010	71,066,358
	292,282,349	242,166,454

See accompanying notes

Financial statements

Statements Of Earnings And Retained Earnings
(unaudited)

	Three Months Ended March 31	
	2003	2002
	$	$
Revenue		
Petroleum and natural gas sales, net	**39,849,623**	13,678,316
Expenses		
Operating *(Note 5)*	**1,117,044**	939,589
General and administrative	**211,506**	102,400
Interest	**895,322**	467,056
Depletion, depreciation and site restoration	**4,968,014**	2,274,930
	7,191,886	3,783,975
Earnings before taxes	**32,657,737**	9,894,341
Future income tax expense	**13,845,281**	3,897,871
Current tax expense	**190,256**	-
Capital tax expense	**126,884**	71,001
	14,162,421	3,968,872
Earnings for the period	**18,495,316**	5,925,469
Retained earnings, beginning of period	**51,835,681**	23,281,622
Retained earnings, end of period	**70,330,997**	29,207,091
Earnings per share		
Basic	**0.43**	0.14
Diluted	**0.40**	0.14

See accompanying notes

Financial statements

Statements Of Cash Flows
(unaudited)

Three Months Ended March 31	**2003**	2002
Cash provided by (used in)		
Operating Activities		
Earnings for the period	**$ 18,495,316**	$ 5,925,469
Items not requiring cash		
Future income tax expense	**13,845,281**	3,897,871
Depletion, depreciation and site restoration	**4,968,014**	2,274,930
Funds from operations	**37,308,611**	12,098,270
Change in non-cash working capital related to operating activities	**(6,870,092)**	(1,898,697)
	30,438,519	10,199,573
Financial Activities		
Issue of common shares, net of costs	**134,336**	2,005,829
Increase in revolving demand loan	**15,226,908**	274,803
	15,361,244	2,280,632
Investing Activities		
Additions to property, plant and equipment	**(40,485,693)**	(22,549,201)
Change in non-cash working capital related to investing activities	**(5,508,834)**	10,068,954
	(45,994,527)	(12,480,247)
Net decrease in cash	**(194,764)**	(42)
Cash, beginning of period	**205,558**	1,220
Cash, end of period	**$ 10,794**	$ 1,178

See accompanying notes

Notes to financial statements

1. Accounting Principles

The interim financial statements of the Peyto Exploration & Development Corp. (the "Company") have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"), and on the same basis as the audited financial statements as at and for the year ended December 31, 2002. The interim financial statement disclosures are incremental to those included with the annual financial statements and certain disclosures, which are normally required to be included in the notes to the annual financial statements, have been condensed or omitted. These interim financial statements should be read in conjunction with the financial statements and notes in the Company's annual report for the year ended December 31, 2002.

2. Property, Plant and Equipment

	March 31, 2003 $	December 31, 2002 $
Property, plant and equipment	**283,635,325**	243,180,014
Office furniture and equipment	**314,617**	284,236
	283,949,942	243,464,250
Accumulated depletion and depreciation	**(26,137,138)**	(21,258,017)
	257,812,804	222,206,233

At March 31, 2003, costs of $20,027,423 (December 31, 2002 - $20,122,240) related to undeveloped land have been excluded from the depletion and depreciation calculation. No general and administrative expenses relating to the Company's exploration, development and acquisition programs were capitalized.

3. Revolving Demand Loan

The Company has a revolving credit facility to a maximum of $105,000,000. Outstanding amounts on this facility bear interest at bank prime and are due on demand. A General Security Agreement with a floating charge on land registered in Alberta is held as collateral by the bank.

While the bank has confirmed that it is not its intention to call for repayment of this loan before March 31, 2004, provided there is no adverse change in the financial position of the Company, this loan is demand in nature and pursuant to the CICA pronouncement is presented as a current liability.

4. Share Capital

Authorized

Unlimited number of common voting shares
Unlimited number of preferred shares, issuable in series

Issued and Outstanding - Common shares

	Number of Shares	**Amount** $
Balance, December 31, 2002	43,418,188	19,230,677
Exercise of stock options	33,334	134,336
Balance, March 31, 2003	43,451,522	19,365,013

Notes to financial statements (continued)

Stock Options

The Company has a director and employee stock option plan. The number of common shares reserved for issuance at any one time shall not exceed 4,314,262 shares subject to shareholder and regulatory approval. The exercise price of an option is set at the market price of the common shares at the date of grant. Each option vests over a three year period and has a term of 5 years.

	As at March 31, 2003		As at December 31, 2002	
	Options	**Weighted - Average Exercise Price**	Options	Weighted- Average Exercise Price
Opening	**3,615,333**	**$3.95**	3,310,333	$2.39
Granted	**-**	**-**	1,679,557	$5.52
Exercised	**(33,334)**	**$4.03**	(1,324,557)	$1.99
Cancelled	**-**	**-**	(50,000)	$5.51
Closing	**3,581,999**	**$3.95**	3,615,333	$3.95

Per Share Amounts

Earnings per share have been calculated based upon the weighted average number of common shares outstanding during the period of 43,446,337 (for the period ended March 31, 2002 – 42,184,129). Diluted per share amounts are calculated using the treasury stock method. The weighted average number of common shares used to determine the diluted per share amount for the period ended March 31, 2003 was 45,889,454 (for the period ended March 31, 2002 – 43,187,159).

Stock Based Compensation

The Company has chosen to recognize no compensation when stock options are granted to employees and directors under stock option plans with no cash settlement features. However, direct awards of stock to employees and stock and stock option awards granted to non-employees have been accounted for in accordance with the fair value method of accounting for stock-based compensation. The fair value of direct awards of stock is determined by the quoted market price of the Company's stock and the fair value of stock options are determined using the Black Scholes option pricing model. In periods prior to January 1, 2002, the Company recognized no compensation when stock or stock options were issued to employees. Pro forma information regarding net income is required and has been determined as if the Company had accounted for its employee stock options granted after December 31, 2001 under the fair value method. The fair value for these options was estimated at the date of granting using a Black-Scholes Option Pricing Model with the following assumptions: weighted-average risk-free interest rate of 3%; dividend yield of 0%; weighted-average volatility factors of the expected market price of the Company's Common Shares of 43%; and a weighted-average expected life of the options of 3 years. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the option vesting periods. The Company's pro forma net income under Canadian GAAP would be reduced by $260,493 for the three months ended March 31, 2003 (2002 - $56,733). Basic and diluted earnings-per-share figures would have been reduced by $0.01 and $0.00 respectively (2002 – no change).

5. Operating Expenses

The Corporation's operating expenses include all costs with respect to day-to-day well and facility operations and the cost of transportation of natural gas. Processing and gathering income related to joint venture and third party gas is included in operating expenses.

	Three Months Ended March 31	
	2003	2002
	$	$
Field expenses	**1,312,904**	792,682
Transmission	**619,914**	401,620
Processing & gathering income	**(815,774)**	(254,713)
Total operating costs	**1,117,044**	939,589

6. Financial Instruments

The Company is a party to certain off balance sheet derivative financial instruments, including fixed price contracts. The Company enters into these contracts for the purpose of protecting a portion of its future earnings and cash flows from operations from the volatility of natural gas commodity prices by locking in a minimum and maximum forward price.

A summary of contracts outstanding in respect to the hedging activities at March 31, 2003 were as follows:

Period Hedged	Type	Daily Volume	Floor	Ceiling
Nov. 1, 2002 to March 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$7.00/GJ
Nov. 1, 2002 to March 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$6.60/GJ
Nov. 1, 2002 to March 31, 2003	Costless collar	6,000 GJ	$3.50/GJ	$6.70/GJ
April 1 to October 31, 2003	Costless collar	6,000 GJ	$3.50/GJ	$7.25/GJ
April 1 to October 31, 2003	Costless collar	8,000 GJ	$3.50/GJ	$6.85/GJ
April 1 to October 31, 2003	Costless collar	6,000 GJ	$3.50/GJ	$7.00/GJ
April 1 to October 31, 2003	Costless collar	5,000 GJ	$5.50/GJ	$7.61/GJ
Nov. 1, 2003 to March 31, 2004	Costless collar	5,000 GJ	$5.90/GJ	$8.45/GJ
April 1 to October 31, 2003	Fixed Price	5,000 GJ	$7.40/GJ	
April 1 to October 31, 2003	Fixed Price	5,000 GJ	$8.20/GJ	
Nov. 1, 2003 to March 31, 2004	Fixed price	5,000 GJ	$7.49/GJ	
Nov. 1, 2003 to March 31, 2004	Fixed price	5,000 GJ	$7.90/GJ	

Based on dealer quotes, had these contracts been closed on March 31, 2003, a gain in the amount of $4,451,850 would have been realized.

7. Subsequent Events

On April 14, 2003, Peyto announced a reorganization initiative that will result in its conversion to an income trust through the exchange of trust units for all outstanding common shares. Peyto Energy Trust will make monthly cash distributions to investors while retaining sufficient cash flow for capital expenditures. The reorganization is subject to certain conditions including the approval of Peyto's shareholders, court approval, and applicable regulatory approvals. A special meeting of shareholders will be held on June 24, 2003, to approve the proposed reorganization. An information circular containing details of the proposed reorganization and plan of arrangement is expected to be mailed out to shareholders on or about May 27, 2003.

Corporate information

Officers

Don Gray
President and Chief Executive Officer

Roberto Bosdachin
Vice-President, Exploration

Darren Gee
Vice President, Engineering

Lyle Skaien
Vice President, Operations

Sandra Brick
Vice President, Finance

Stephen Chetner
Corporate Secretary

Directors

Rick Braund

Don Gray

Mike Broadfoot

Brian Craig

Stephen Chetner

John Boyd

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