PEYTO

Exploration & Development Corp.

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Interim Report
for the three months ended March 31, 2018

HIGHLIGHTS

	Three Months Ended March 31		%
	2018	2017	Change
Operations			
Production			
Natural gas (mcf/d)	**568,496**	549,037	*4%*
Oil & NGLs (bbl/d)	**10,043**	9,586	*5%*
Thousand cubic feet equivalent (mcfe/d @ 1:6)	**628,755**	606,556	*4%*
Barrels of oil equivalent (boe/d @ 6:1)	**104,793**	101,093	*4%*
Production per million common shares (boe/d)*	**636**	613	*4%*
Product prices			
Natural gas ($/mcf)	**2.86**	2.96	*-3%*
Oil & NGLs ($/bbl)	**59.67**	48.14	*24%*
Operating expenses ($/mcfe)	**0.29**	0.29	-
Transportation ($/mcfe)	**0.13**	0.17	*-24%*
Field netback ($/mcfe)	**2.95**	2.79	*6%*
General & administrative expenses ($/mcfe)	**0.08**	0.04	*100%*
Interest expense ($/mcfe)	**0.24**	0.20	*20%*
Financial ($000, except per share*)			
Revenue and realized hedging gains (losses)	**200,397**	187,849	*7%*
Royalties	**9,543**	10,635	*-10%*
Funds from operations	**148,986**	139,305	*7%*
Funds from operations per share	**0.90**	0.85	*6%*
Total dividends	**29,677**	54,387	*-45%*
Total dividends per share	**0.18**	0.33	*-45%*
Payout ratio	**20**	39	*-49%*
Earnings	**47,749**	40,255	*19%*
Earnings per diluted share	**0.29**	0.24	*21%*
Capital expenditures	**35,454**	153,874	*-77%*
Weighted average common shares outstanding	**164,874,175**	164,800,637	-
As at March 31			
End of period shares outstanding (includes shares to be issued)	**164,874,175**	164,874,175	-
Net debt	**1,243,291**	1,203,988	*3%*
Shareholders' equity	**1,725,131**	1,632,390	*6%*
Total assets	**3,762,835**	3,543,556	*6%*

**all per share amounts using weighted average common shares* outstanding

	Three Months Ended March 31	
($000 except per share)	**2018**	2017
Cash flows from operating activities	**143,995**	121,137
Change in non-cash working capital	**3,913**	16,160
Change in provision for performance based compensation	**1,078**	2,008
Funds from operations	**148,986**	139,305
Funds from operations per share	**0.90**	0.85

(1) Funds from operations - Management uses funds from operations to analyze the operating performance of its energy assets. In order to facilitate comparative analysis, funds from operations is defined throughout this report as earnings before performance based compensation, non-cash and non-recurring expenses. Management believes that funds from operations is an important parameter to measure the value of an asset when combined with reserve life. Funds from operations is not a measure recognized by Canadian generally accepted accounting principles ("GAAP") and does not have a standardized meaning prescribed by GAAP. Therefore, funds from operations, as defined by Peyto, may not be comparable to similar measures presented by other issuers, and investors are cautioned that funds from operations should not be construed as an alternative to net earnings, cash flow from operating activities or other measures of financial performance calculated in accordance with GAAP. Funds from operations cannot be assured and future dividends may vary.

Report from the president

Peyto Exploration & Development Corp. ("Peyto” or the “Company") is pleased to present its operating and financial results for the first quarter of the 2018 fiscal year. A 74% operating margin [(1)] and a 24% profit margin [(2)] in the quarter delivered an annualized 11% return on equity (“ROE”) and 8% return on capital employed (“ROCE”). Additional highlights included:

- **Earnings of $0.29/share, dividends of $0.18/share.** Earnings of $47 million were generated in the quarter while dividends of $30 million were paid to shareholders. Earnings per share of $0.29 were up 21% from the $0.24 in Q1 2017. The Company has never incurred a write down or recorded an impairment in its 19 year history and this quarter represents Peyto’s 53rd consecutive quarter of earnings which is the best evidence shareholder’s capital has been invested profitably.

- **Funds from operations (“FFO”) of $0.90/share.** Generated $149 million in FFO in Q1 2018 up 7% from $139 million in Q1 2017 (up 6%/share). For the quarter, funds from operations exceeded the combination of capital expenditures and dividends by $84 million.

- **Total cash costs of $0.91/Mcfe (or $0.74/Mcfe, $4.43/boe, excluding royalties).** Total cash costs, including $0.17/Mcfe royalties, $0.29/Mcfe operating costs, $0.13/Mcfe transportation, $0.08/Mcfe G&A and $0.24/Mcfe interest, combined with a realized price of $3.54/Mcfe, resulting in a $2.63/Mcfe ($15.80/boe) cash netback, or a 74% operating margin.

- **Capital investment of $35 million**. A total of 8 gross wells (7.6 net) were drilled in the first quarter, 13 gross wells (12.6 net) were completed, and 14 gross wells (13.6 net) brought on production. Over the last 12 months, new wells brought on production accounted for 34,000 boe/d at the end of the quarter, which when combined with a trailing twelve month capital investment of $403 million, equates to an annualized capital efficiency of $11,900/boe/d.

- **Production per share up 4%.** First quarter 2018 production of 629 MMcfe/d (104,793 boe/d) was up 4%, on an absolute and per share basis, from 607 MMcfe/d in Q1 2017, comprised of 569 MMcf/d of natural gas and 10,043 bbls/d of oil and natural gas liquids.

First Quarter 2018 in Review

Peyto announced early in the quarter a strategic shift in its 2018 annual plans in response to the significant volatility in forecast natural gas prices. Those changes included a deferral of 2018 capital investment to later in the year when AECO natural gas prices were forecast to recover from summer lows, a reduction in the monthly dividend, a share buyback program, a term debt issuance and a market diversification strategy. These were prudent steps to postpone investment on a portion of Peyto’s lean gas inventory in order to maximize the returns from these opportunities over the longer term, while at the same time strengthening the Company’s financial position in the near term. As a result of these changes, the Company drilled only 8 wells in the quarter compared to 45 wells in Q1 2017. Capital investments combined with the reduced dividend payments represented just 44% of funds from operations for the quarter, allowing for net debt reduction of $84 million. Capital that was invested targeted liquids rich opportunities like the Cardium formation where result confirmed a significant improvement in type curve and investment return. Financial performance in the quarter remained strong with industry leading operating and profit margins delivering solid return on equity and capital employed. Peyto advanced its market diversification strategy during the quarter, with both synthetic and physical transportation agreements, as an initial step towards a corporate target of having 40% of natural gas production sold at US pricing hubs.

1. Operating Margin is defined as funds from operations divided by revenue before royalties but including realized hedging gains/losses.
2. Profit Margin is defined as net earnings for the quarter divided by revenue before royalties but including realized hedging gains/losses.

Natural gas volumes recorded in thousand cubic feet (mcf) are converted to barrels of oil equivalent (boe) using the ratio of six (6) thousand cubic feet to one (1) barrel of oil (bbl). Natural gas liquids and oil volumes in barrel of oil (bbl) are converted to thousand cubic feet equivalent (Mcfe) using a ratio of one (1) barrel of oil to six (6) thousand cubic feet. This could be misleading, particularly if used in isolation as it is based on an energy equivalency conversion method primarily applied at the burner tip and does not represent a value equivalency at the wellhead.

Exploration & Development

First quarter 2018 activity focused on the Greater Sundance areas, finishing up on the winter drilling program that began in the fall. In total, three horizontal Cardium wells were drilled and five Spirit River horizontal wells were drilled as shown in the table below. The Company continues to focus on the improved Cardium results coming from optimization of stimulation design.

Zone	Field							Total Wells Drilled
	Sundance	**Nosehill**	**Wildhay**	**Ansell**	**Berland**	**Kisku/ Kakwa**	**Brazeau**	
Belly River								
Cardium	2		1					3
Notikewin				1				1
Falher								
Wilrich		2		2				4
Bluesky								
Total	2	2	1	3				8

Horizontal well drilling costs (per meter drilled) in Q1 2018 were in line with both 2016 and 2017. Completion costs (per meter of horizontal lateral) were also similar to 2017; however, costs per stage have continued to decrease as reduced spacing, particularly in the Cardium, has yielded superior results. The following table illustrates the progression of cost optimization designed to contribute to lower overall development costs and greater returns:

	2010	2011	2012	2013	2014	2015	2016	2017	2018 Q1
Gross Hz Spuds	52	70	86	99	123	140	126	135	**8**
Measured Depth (m)	3,762	3,903	4,017	4,179	4,251	4,309	4,197	4,229	**4,091**
Drilling ($MM/well)	$2.76	$2.82	$2.79	$2.72	$2.66	$2.16	$1.82	$1.90	**$1.74**
$ per meter	$734	$723	$694	$651	$626	$501	$433	$450	**$425**
Completion ($MM/well)	$1.36	$1.68	$1.67	$1.63	$1.70	$1.21	$0.86	$1.00	**$1.15**
Hz Length (m)	1,335	1,303	1,358	1,409	1,460	1,531	1,460	1,241	**1,415**
$ per Hz Length (m)	$1,017	$1,286	$1,231	$1,153	$1,166	$792	$587	$803	**$810**
$ '000 per Stage	$231	$246	$257	$188	$168	$115	$79	$81	**$61**

Capital Expenditures

During the first quarter of 2018, Peyto invested $14 million on drilling, $17 million on completions, $4 million on wellsite equipment and tie-ins, $4 million on facilities and major pipeline projects, and $1 million on lands and seismic, for capital investments of $39.5 million. Peyto also disposed of some minor, non-producing property in the quarter for $4.0 million, reducing total capital to $35 million.

In addition to the 8 gross (7.6 net) horizontal wells, 13 gross (12.6 net) wells were completed and 14 gross (13.6 net) wells were equipped and tied in. Peyto also completed construction of a $3 million pipeline under the Sundance provincial park that connects the Swanson and Galloway gas plants.

Commodity Prices

Average daily AECO natural gas prices were $1.97/GJ in Q1 2018, up 23% from $1.60/GJ in Q4 2017 but down 23% from $2.55/GJ in Q1 2017. This volatility was in contrast to US Henry Hub spot prices which averaged $3.08/MMBTU for the quarter, similar to the $3.01/MMBTU in Q1 2017. A change in the prioritization of gas transmission service on the NGTL system in August 2017, which severely inhibited the ability for Alberta storage reservoirs to buffer the supply/demand imbalances, has led to daily market instability and extreme volatility in AECO daily prices, predominantly during summer months. This was further compounded by a surge of basin production in the fall of 2017 combined with a lack of access to external markets beyond Western Canada, all of which has contributed to the dramatic drop in average Alberta natural gas price relative to US pricing.

On average for Q1 2018, Peyto realized a natural gas price of $2.49/GJ or $2.86/Mcf. This was the result of a combination of approximately 12% of natural gas production being sold in the daily or monthly spot market at an average of $1.72/GJ ($1.98/Mcf) and 88% having been pre-sold at an average hedged price of $2.62/GJ (prices reported net of TCPL fuel).

Peyto's Q1 2018 liquid recoveries averaged 18 bbl/mmcf with a blended, realized, oil and natural gas liquids price of $59.67/bbl, which represented 83% of the $72.09/bbl average Canadian Light Sweet posted price. Details of realized commodity prices by component are shown in the following table:

Commodity Prices by Component

		Three Months ended March 31	
		2018	2017
AECO monthly	($/GJ)	**1.76**	2.79
AECO daily	($/GJ)	**1.97**	2.55
Henry Hub spot	($US/MMBTU)	**3.08**	3.01
Natural gas – prior to hedging	($/GJ)	**1.72**	2.73
	($/mcf)	**1.98**	3.14
Natural gas – after hedging	($/GJ)	**2.49**	2.58
	($/mcf)	**2.86**	2.96
Oil and natural gas liquids ($/bbl)			
Condensate ($/bbl)		**72.56**	60.91
Propane ($/bbl)		**26.04**	15.19
Butane ($/bbl)		**40.83**	29.12
Pentane ($/bbl)		**79.26**	64.60
Total Oil and natural gas liquids ($/bbl)		**59.67**	48.14
Canadian Light Sweet stream ($/bbl)		**72.09**	62.19
Peyto realized liquids price/Canadian Light Sweet		**83%**	77%

Liquids prices are Peyto realized prices (F.O.B. plant gate) in Canadian dollars adjusted for fractionation and transportation.

Financial Results

Approximately 27%, or $0.95/Mcfe, of Peyto's revenue came from its liquids sales while 73%, or $2.59/Mcfe, came from natural gas and natural gas hedging. This liquids revenue covered all cash costs. Cash costs of $0.91/Mcfe, included royalties of $0.17/Mcfe, operating costs of $0.29/Mcfe, transportation costs of $0.13/Mcfe, G&A of $0.08/Mcfe and interest costs of $0.24/Mcfe. Cash costs were slightly higher than Q1 2017 due to increased interest rates and lower capital overhead recoveries from reduced capital expenditures. These total cash costs, when deducted from realized revenues of $3.54/Mcfe, resulted in a cash netback of $2.63/Mcfe or a 74% operating margin. Historical cash costs and operating margins are shown in the following table. Going forward, Peyto's goal is to achieve per unit cash costs in the $0.80-$0.90/Mcfe levels for the balance of 2018.

	2014	**2015**				**2016**				**2017**				**2018**
($/Mcfe)	FY	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	**Q1**
Revenue	5.04	4.17	3.81	3.80	3.58	3.24	2.92	3.16	3.38	3.44	3.36	3.24	3.50	**3.54**
Royalties	0.38	0.18	0.13	0.15	0.13	0.13	0.10	0.12	0.18	0.19	0.17	0.09	0.15	**0.17**
Operating Costs	0.34	0.32	0.31	0.28	0.25	0.23	0.26	0.25	0.26	0.29	0.24	0.26	0.28	**0.29**
Transportation	0.13	0.15	0.15	0.16	0.16	0.16	0.17	0.16	0.16	0.17	0.18	0.17	0.16	**0.13**
G&A	0.03	0.04	0.04	0.02	0.05	0.03	0.06	0.04	0.03	0.04	0.05	0.03	0.03	**0.08**
Interest	0.21	0.20	0.19	0.19	0.16	0.17	0.21	0.19	0.18	0.20	0.21	0.21	0.21	**0.24**
Total Cash Costs	1.09	0.89	0.82	0.80	0.75	0.72	0.80	0.76	0.81	0.89	0.85	0.76	0.83	**0.91**
Netback	3.95	3.28	2.99	3.00	2.83	2.52	2.12	2.40	2.57	2.55	2.51	2.48	2.67	**2.63**
Operating Margin	78%	79%	78%	79%	79%	78%	73%	76%	76%	74%	75%	76%	76%	**74%**

Depletion, depreciation and amortization charges of $1.44/Mcfe, along with a provision for deferred tax and market based bonus payments reduced the cash netback to earnings of $0.84/Mcfe, or a 24% profit margin. Dividends of $0.52/Mcfe were paid to shareholders.

Peyto continued to protect its balance sheet from rising interest rates with the closing of another private placement of senior unsecured notes in the first quarter. On January 2, 2018 Peyto issued CND$100 million of senior unsecured notes which bear a coupon rate of 3.95% and mature on January 2, 2028. The issuance of senior notes expanded Peyto's aggregate borrowing capacity to $1.92 billion, split into a $1.3 billion, 4 year revolver and $0.62 billion of senior unsecured notes.

Market Diversification and Hedging Strategy

Early in the first quarter Peyto announced that its Board of Directors had approved a new natural gas market diversification strategy. This was meant to complement the Company's historically successful hedging strategy which to date has yielded over $530 million in hedging gains. The diversification strategy is designed to link 40% of Peyto's natural gas sales to AECO based pricing, 40% to US based pricing and 20% to intra-Alberta markets. As has been Company practice, Peyto will continue to hedge future prices to smooth out the volatility in both AECO and US natural gas markets. To date, the Company has been successful initiating this marketing plan, putting in place both synthetic and physical transportation arrangements for future natural gas volumes. It is expected the above targets will be gradually achieved over several quarters through careful consideration of deal structure, long term transportation cost and market conditions.

Specifically in the short term, the Company has focused on the vulnerability of AECO summer prices when reduced intra-Alberta consumption requires movement of production to southern Alberta storage, a requirement that can no longer be satisfied due to insufficient Nova Gas Transmission Ltd. ("NGTL") pipeline capacity given the migration of Alberta production to the northwest corner of the province. The current pipeline deficiencies are targeted for expansion over the next couple of years and this work should eventually correct the AECO summer pricing handicap. In the interim, Peyto has focused on near term summer diversification as well as longer term, full year diversification. The following table outlines the approximate percentage of current natural gas sales that are split by market as of May 1, 2018.

Percentage of current gas volume*	**2018 Summer/ Winter**	**2019 Summer**	**2019/20 Winter**	**2020 Summer**	**2020/21 Winter**	**2021 Summer**	**2021/22 Winter**	**2022 Summer**	**2022/23 Winter**
AECO Based Pricing	100%	89%	98%	89%	98%	86%	73%	63%	73%
Non-AECO Based Pricing	-	11%	2%	11%	2%	14%	27%	37%	27%

**Winter period is from November to March, summer period is April to October*

Peyto has additional initiatives in progress directed towards contracting future production volumes to strong intra-Alberta markets. There has been much discussion about Alberta's economic diversification and the recent government announcement of two royalty incentive programs designed to stimulate investment into the development of additional petrochemical plants requiring natural gas and NGL feedstock. Peyto's Greater Sundance asset base is geographically well situated and the concentrated collection of resource, along with pipeline, road and rail infrastructure, is a ideal source of supply for many of these projects which include petrochemical manufacturing, power generation, and NGL product upgrade. Consequently, Peyto is involved in active discussions for supply of future natural gas and NGL volumes to many of these exciting ventures.

The current volatility in natural gas markets in Alberta remains extremely high, reinforcing the value of Peyto's hedging practice of layering in future sales in the form of fixed price swaps. For the balance of 2018, approximately 77% of Company forecast gas volumes have been hedged to protect against this increased AECO volatility. Peyto's hedging program aims to achieve a fixed price on a descending, graduated schedule of up to 85% of gross production for the immediate summer or winter season and 75%, 65%, 55%, 45% and 30% targets thereafter for the successive following seasons. These fixed prices, which are settled against the AECO Monthly price, are achieved through a series of frequent transactions which are similar to "dollar cost averaging" the future gas prices in order to smooth out volatility. The following table summarizes the remaining hedged natural gas volumes and prices for the upcoming years as of May 1, 2018:

	Future Sales		Average Price (CAD)	
	GJ	Mcf	$/GJ	$/Mcf
2018	112,735,000	98,030,435	$2.16	$2.48
2019	71,980,000	62,591,304	$1.86	$2.13
2020	11,830,000	10,286,957	$1.80	$2.07
2021	1,970,000	1,713,043	$1.64	$1.89
Total	196,545,000	170,908,696	$2.02	$2.33

**prices and volumes in mcf use Peyto's historic heat content premium of 1.15.*

Both the market diversification and hedging strategies are designed to remove the uncertainty of system access and AECO price volatility while at the same time leaving Peyto with the maximum operating margin and future market optionality.

Activity Update

Since the end of the first quarter, drilling and completion activity has been suspended due to spring break up. In April, Peyto finished the installation of a strategic pipeline under the Sundance provincial park which directly connects the Peyto owned and operated Swanson and Galloway gas plants. This pipeline will allow for greater operational flexibility resulting in reduced operating costs as well as increased liquids recovery.

Peyto has also used this period of reduced activity to sharpen its drilling and well completion designs, focus on cost reduction initiatives, and acquire licenses for the post break up drilling program. The Company expects to be back drilling in early June once road bans are removed, initially starting with 3 drilling rigs focused on the Cardium resource play in the Greater Sundance area. Peyto plans to drill and bring on production another 40 to 50 Cardium locations during the remainder of 2018.

Outlook

Despite the outlook for weak AECO spot natural gas prices for the summer of 2018, Peyto remains bullish on the prospect for stronger pricing in the following winter season and has planned the timing of its capital program and subsequent production additions accordingly. The Company is confident that the much improved returns in its Cardium play, as a result of innovation in completion design, will support expanding capital investment going forward, even at current strip pricing. Longer term, both market diversification strategies and NGTL system expansions should help reduce the discount to AECO price further enhancing returns for shareholders. The quality of Peyto's resource base, supported by its strategic midstream assets provides the springboard for these future opportunities.

(signed) *"Darren Gee"*

Darren Gee
President and CEO
May 8, 2018

Management's discussion and analysis

This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the audited financial statements of Peyto Exploration & Development Corp. ("Peyto" or the "Company") for the years ended December 31, 2017 and 2016. The financial statements have been prepared in accordance with the International Accounting Standards Board's ("IASB") most current International Financial Reporting Standards ("IFRS" or "GAAP") and International Accounting Standards ("IAS").

This discussion provides management's analysis of Peyto's historical financial and operating results and provides estimates of Peyto's future financial and operating performance based on information currently available. Actual results will vary from estimates and the variances may be significant. Readers should be aware that historical results are not necessarily indicative of future performance. This MD&A was prepared using information that is current as of May 7, 2018. Additional information about Peyto, including the most recently filed annual information form is available at www.sedar.com and on Peyto's website at www.peyto.com.

This MD&A contains certain forward-looking statements or information ("forward-looking statements") as defined by applicable securities laws that involve substantial known and unknown risks and uncertainties, many of which are beyond Peyto's control. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. The use of any of the words "plan", "expect", "prospective", "project", "intend", "believe", "should", "anticipate", "estimate", or other similar words or statements that certain events "may" or "will" occur are intended to identify forward-looking statements. The projections, estimates and beliefs contained in such forward-looking statements are based on management's estimates, opinions, and assumptions at the time the statements were made, including assumptions relating to: the impact of economic conditions in North America and globally; industry conditions; changes in laws and regulations including, without limitation, the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced; increased competition; the availability of qualified operating or management personnel; fluctuations in commodity prices, foreign exchange or interest rates; stock market volatility and fluctuations in market valuations of companies with respect to announced transactions and the final valuations thereof; results of exploration and testing activities; and the ability to obtain required approvals and extensions from regulatory authorities. Management of the Company believes the expectations reflected in those forward-looking statements are reasonable, but no assurances can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits that Peyto will derive from them. As such, undue reliance should not be placed on forward-looking statements. Forward-looking statements contained herein include, but are not limited to, statements regarding: assumptions regarding the dismissal of the Poseidon Shareholder Application, the Ontario Poseidon Shareholder Action and the Poseidon Action; and the Company's risk management.

The forward-looking statements contained herein are subject to numerous known and unknown risks and uncertainties that may cause Peyto's actual financial results, performance or achievement in future periods to differ materially from those expressed in, or implied by, these forward-looking statements, including but not limited to, risks associated with: imprecision of reserves estimates; competition from other industry participants; failure to secure required equipment; changes in general global economic conditions including, without limitations, the economic conditions in North America; increased competition; the lack of availability of qualified operating or management personnel; fluctuations in commodity prices, foreign exchange or interest rates; environmental risks; changes in laws and regulations including, without limitation, the adoption of new environmental and tax laws and regulations and changes in how they are interpreted and enforced; the results of exploration and development drilling and related activities; the ability to access sufficient capital from internal and external sources; and stock market volatility. Readers are encouraged to review the material risks discussed in Peyto's annual information form for the year ended December 31, 2017 under the heading "Risk Factors" and in Peyto's annual management's discussion and analysis under the heading "Risk Management".

The Company cautions that the foregoing list of assumptions, risks and uncertainties is not exhaustive. Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Peyto's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits Peyto will derive there from. The forward-looking statements contained in this MD&A speak only as of the date hereof and Peyto does not assume any obligation to publicly update or revise them to reflect new information, future events or circumstances or otherwise, except as may be required pursuant to applicable securities laws.

All references are to Canadian dollars unless otherwise indicated. Natural gas liquids volumes are recorded in barrels of oil (bbl) and are converted to a thousand cubic feet equivalent (mcfe) using a ratio of six (6) thousand cubic feet to one (1) barrel of oil (bbl). Natural gas volumes recorded in thousand cubic feet (mcf) are converted to barrels of oil equivalent (boe) using the ratio of six (6) thousand cubic feet to one (1) barrel of oil (bbl). Boe may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf:1 bbl is based in an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, given that the value ratio based on the current price of oil as compared with natural gas is significantly different from the energy equivalent of six to one, utilizing a boe conversion ratio of 6 mcf:1 bbl may be misleading as an indication of value.

OVERVIEW

Peyto is a Canadian energy company involved in the development and production of natural gas and oil & natural gas liquids in Alberta's deep basin. As at December 31, 2017, the Company's total Proved plus Probable reserves were 4.3 trillion cubic feet equivalent (722 million barrels of oil equivalent) as evaluated by its independent petroleum engineers. Production is weighted approximately 90% to natural gas and 10% to oil & natural gas liquids.

The Peyto model is designed to deliver a superior total return with growth in value, assets, production and income, all on a debt adjusted per share basis. The model is built around three key strategies:

- Use technical expertise to achieve the best return on capital employed through the development of internally generated drilling projects.
- Build an asset base which is made up of high quality natural gas reserves.
- Over time, balance dividends paid to shareholders with earnings and cash flow, and balance funding for the capital program with cash flow, equity and available bank lines.

Operating results over the last nineteen years indicate that these strategies have been successfully implemented. This business model makes Peyto a truly unique energy company.

QUARTERLY FINANCIAL INFORMATION

	2018		2017				2016	
($000 except per share amounts)	**Q1**	Q4	Q3	Q2	Q1	Q4	Q3	Q2
Revenue and realized hedging gains (losses) (net of royalties)	**190,854**	202,566	177,061	169,911	177,314	179,862	161,813	136,017
Funds from operations	**148,986**	161,672	139,257	133,487	139,305	144,593	127,915	102,178
Per share – basic and diluted	**0.90**	0.98	0.85	0.81	0.85	0.88	0.78	0.63
Earnings	**47,749**	51,547	44,818	39,957	40,255	38,489	22,814	9,102
Per share – basic and diluted	**0.29**	0.31	0.27	0.24	0.24	0.23	0.14	0.06
Dividends	**29,677**	54,408	54,408	54,408	54,387	54,328	54,328	53,735
Per share – basic and diluted	**0.18**	0.33	0.33	0.33	0.33	0.33	0.33	0.33

Funds from Operations

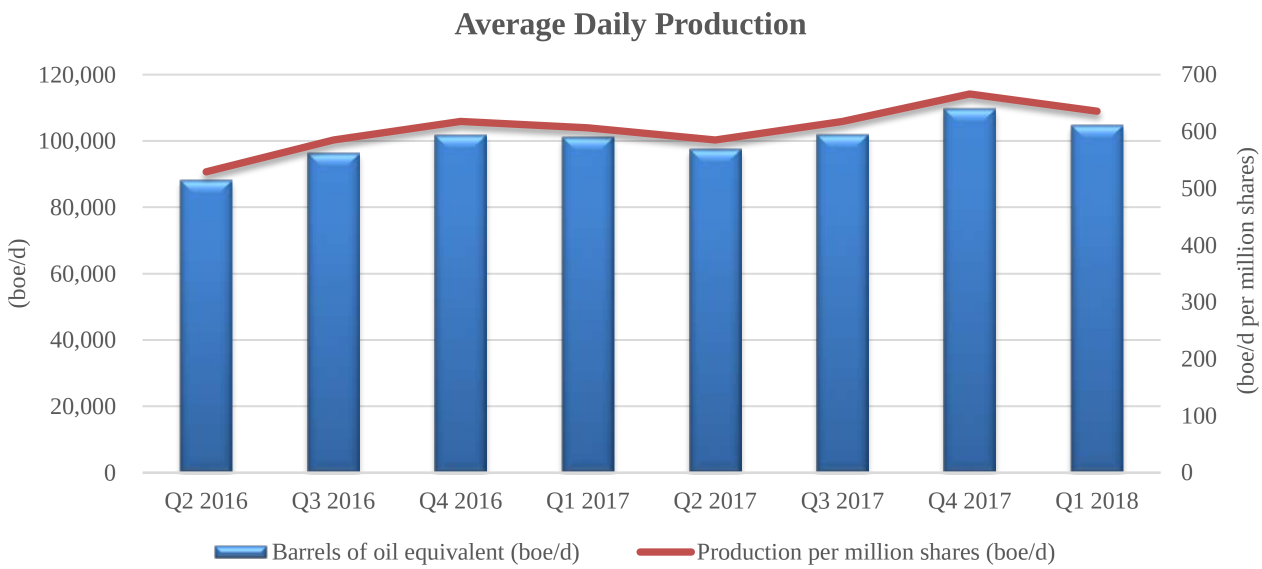
"Funds from operations" is a non-GAAP measure which represents cash flows from operating activities before changes in non-cash operating working capital and provision for future performance-based compensation. Management considers funds from operations and per share calculations of funds from operations to be key measures as they demonstrate the Company's ability to generate the cash necessary to pay dividends, repay debt and make capital investments. Management believes that by excluding the temporary impact of changes in non-cash operating working capital, funds from operations provides a useful measure of Peyto's ability to generate cash that is not subject to short-term movements in operating working capital. The most directly comparable GAAP measure is cash flows from operating activities.

RESULTS OF OPERATIONS

Production

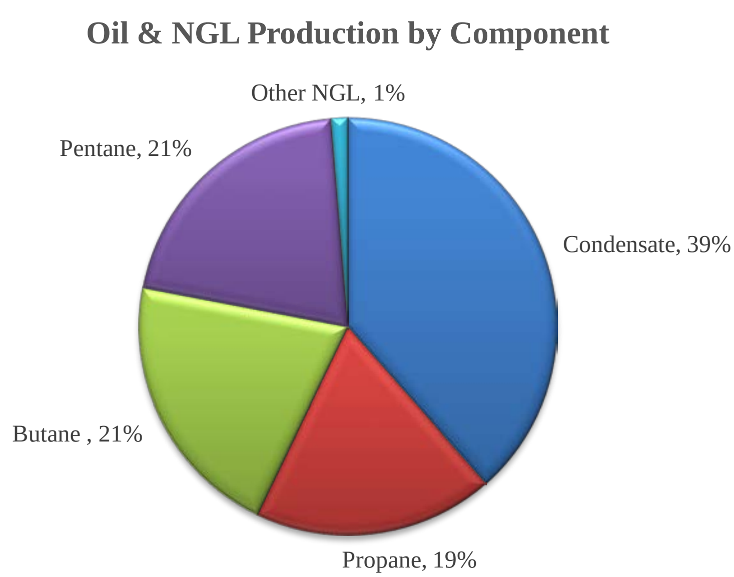
	Three months ended March 31	
	2018	2017
Natural gas (mmcf/d)	**568.5**	549.0
Oil & natural gas liquids (bbl/d)	**10,043**	9,586
Barrels of oil equivalent (boe/d)	**104,793**	101,093
Thousand cubic feet equivalent (mmcfe/d)	**628.8**	606.6

Natural gas production averaged 568.5 mmcf/d in the first quarter of 2018, 4% higher than the 549.0 mmcf/d reported for the same period in 2017. Oil & natural gas liquids production averaged 10,043 bbl/d, an increase of 5% from 9,586 bbl/d reported in the prior year. First quarter production increased 4% from 606.6 mmcfe/d to 628.8 mmcfe/d. Production increases are attributable to Peyto's capital program and resulting production additions.



Oil & Natural Gas Liquids Production by Component

	Three months ended March 31	
	2018	2017
Condensate (bbl/d)	**3,869**	3,846
Propane (bbl/d)	**1,869**	1,638
Butane (bbl/d)	**2,096**	1,929
Pentane (bbl/d)	**2,077**	1,993
Other Oil & NGL'sbbl/d)	**132**	180
Oil & Natural gas liquids (bbl/d)	**10,043**	9,586
Million cubic feet equivalent (mmcfe/d)	**60.3**	57.5



Commodity Prices

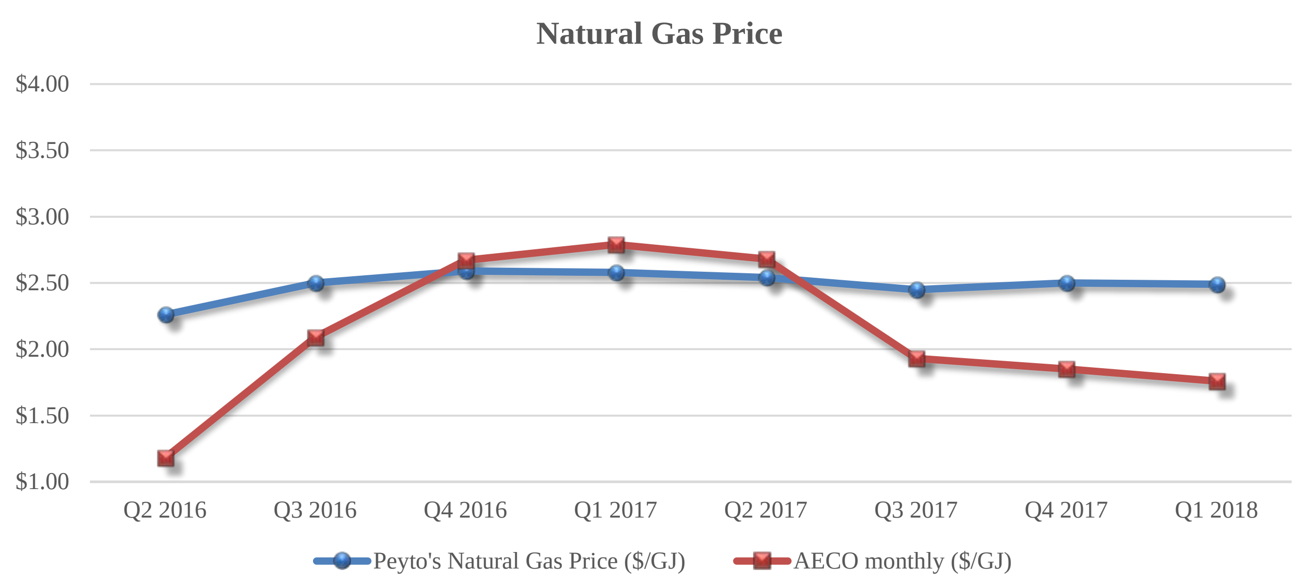
	Three months ended March 31	
	2018	2017
Oil & natural gas liquids ($/bbl)	**59.67**	48.14
Natural gas ($/mcf)	**1.98**	3.14
Hedging – gas ($/mcf)	**0.88**	(0.18)
Natural gas – after hedging ($/mcf)	**2.86**	2.96
Total Hedging ($/mcfe)	**0.80**	(0.17)
Total Hedging ($/boe)	**4.80**	(1.00)

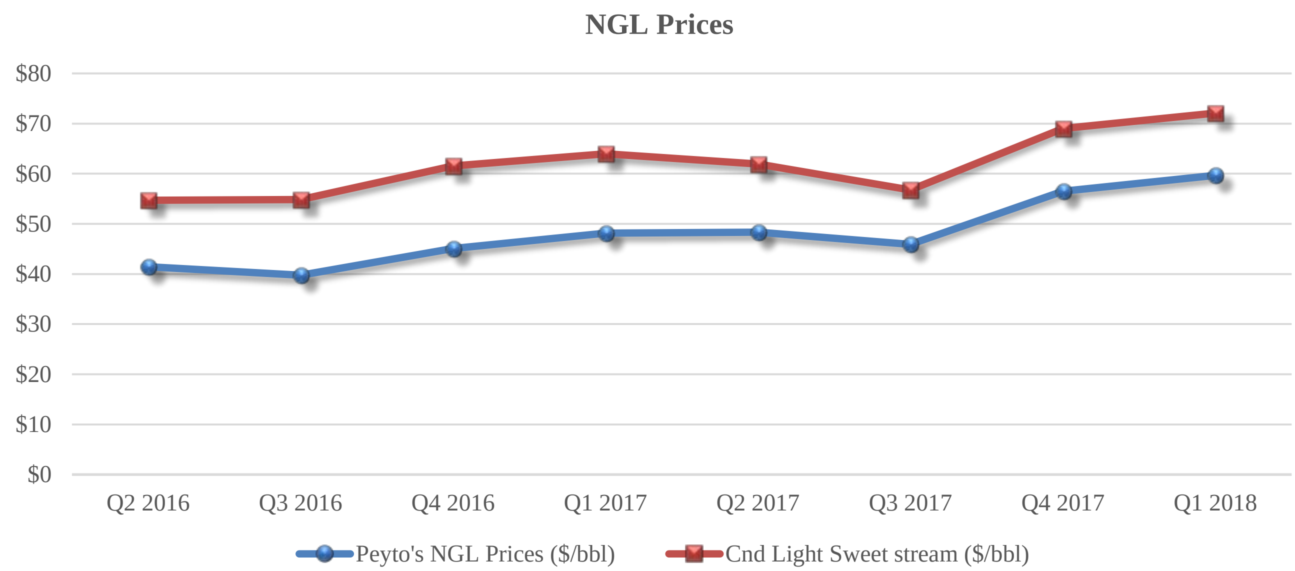
Peyto's natural gas price, before hedging, averaged $1.98/mcf during the first quarter of 2018, a decrease of 37% from $3.14/mcf for the equivalent period in 2017. Oil & natural gas liquids prices averaged $59.67/bbl, an increase of 24% from $48.14/bbl a year earlier.

Commodity Prices by Component

	Three months ended March 31	
	2018	2017
Natural gas – after hedging ($/mcf)	**2.86**	2.96
Natural gas – after hedging ($/GJ)	**2.49**	2.58
AECO monthly ($/GJ)	**1.76**	2.79
AECO daily ($/GJ)	**1.82**	2.55
Natural gas liquids ($/bbl)		
Condensate ($/bbl)	**72.56**	60.91
Propane ($/bbl)	**26.04**	15.19
Butane ($/bbl)	**40.83**	29.12
Pentane ($/bbl)	**79.26**	64.60
Total natural gas liquids ($/bbl)	**59.67**	48.14
Canadian Light Sweet stream ($/bbl)	**72.09**	62.19

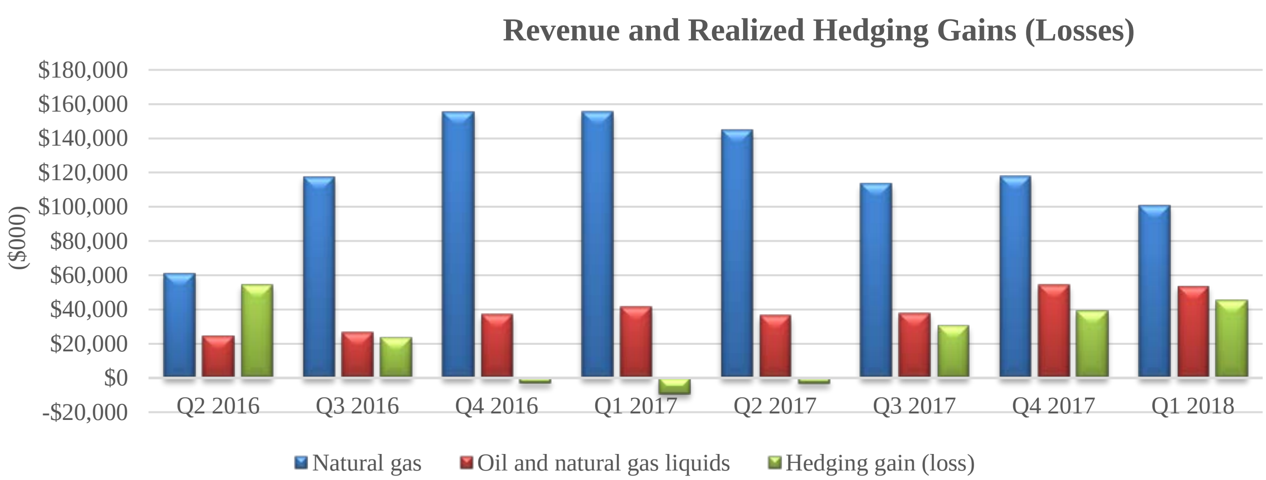
liquids prices are Peyto realized prices in Canadian dollars adjusted for fractionation and transportation.





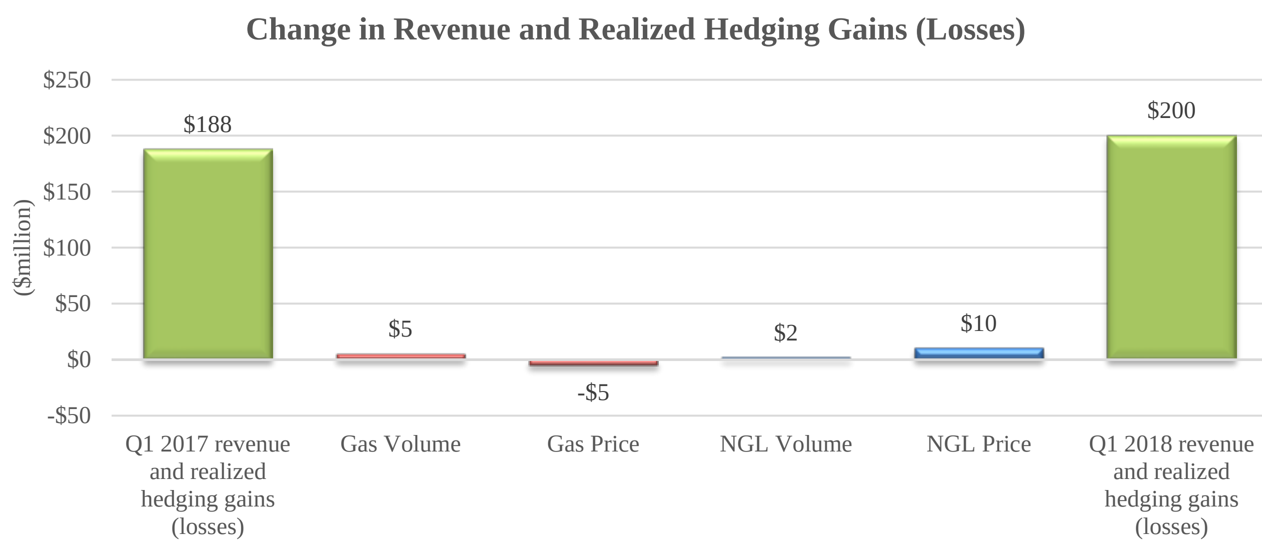
Revenue and Realized Hedging Gains (Losses)

	Three months ended March 31	
($000)	**2018**	2017
Natural gas	**101,231**	155,500
Oil & natural gas liquids	**53,937**	41,536
Hedging gain (loss)	**45,229**	(9,087)
	200,397	187,949



For the three months ended March 31, 2018, revenue and realized hedging gains (losses) increased 7% to $200.4 million from $187.9 million for the same period in 2017. The increase in revenue and realized hedging gains (losses) for the period was a result of increased production volumes and realized oil & natural gas liquids prices, offset in part by a decrease in realized natural gas prices including hedging gains, as detailed in the following table:

	Three months ended March 31		
	2018	2017	**$million**
Revenue and realized hedging gains (losses), March 31, 2017			**187.9**
Revenue and realized hedging gains (losses) change due to:			
Natural gas			
Volume (mmcf)	51,165	49,413	**5.2**
Price ($/mcf)	$2.86	$2.96	**(5.1)**
Oil & NGL			
Volume (mbbl)	904	863	**2.0**
Price ($/bbl)	$59.67	$48.14	**10.4**
Revenue and realized hedging gains (losses), March 31, 2018			**200.4**

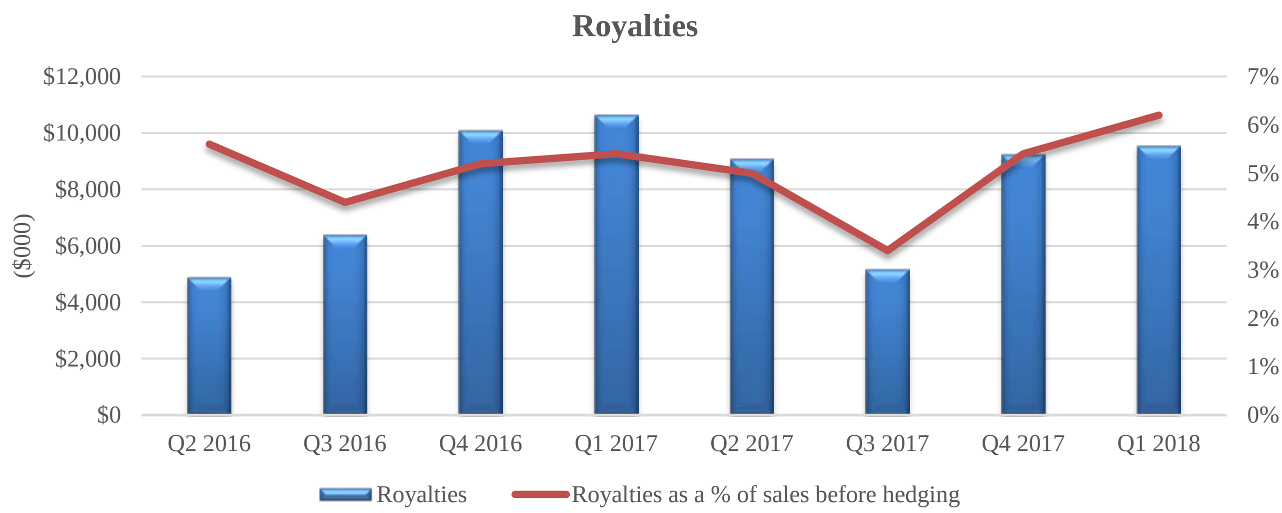


Royalties

Royalties are paid to the owners of the mineral rights with whom leases are held, including the provincial government of Alberta. Alberta Natural Gas Crown royalties are invoiced on the Crown's share of production based on a monthly established Alberta Reference Price. The Alberta Reference Price is a monthly weighted average price of gas consumed in Alberta and gas exported from Alberta reduced for transportation and marketing allowances. All of Peyto's new natural gas wells qualify for the Crown incentive programs which have a 5% initial royalty rate. The royalty rate expressed as a percentage of sales revenue will fluctuate from period to period due to the fact that the Alberta Reference Price can differ significantly from the commodity prices realized by Peyto and that hedging gains and losses are not subject to royalties.

	Three months ended March 31	
	2018	2017
Royalties ($000)	**9,543**	10,635
% of sales before hedging	**6.2**	5.4
% of sales after hedging	**4.8**	5.7
$/mcfe	**0.17**	0.19
$/boe	**1.01**	1.17

For the first quarter of 2018, royalties averaged $0.17/mcfe or approximately 6.2% of Peyto's total petroleum and natural gas sales excluding hedging gains.



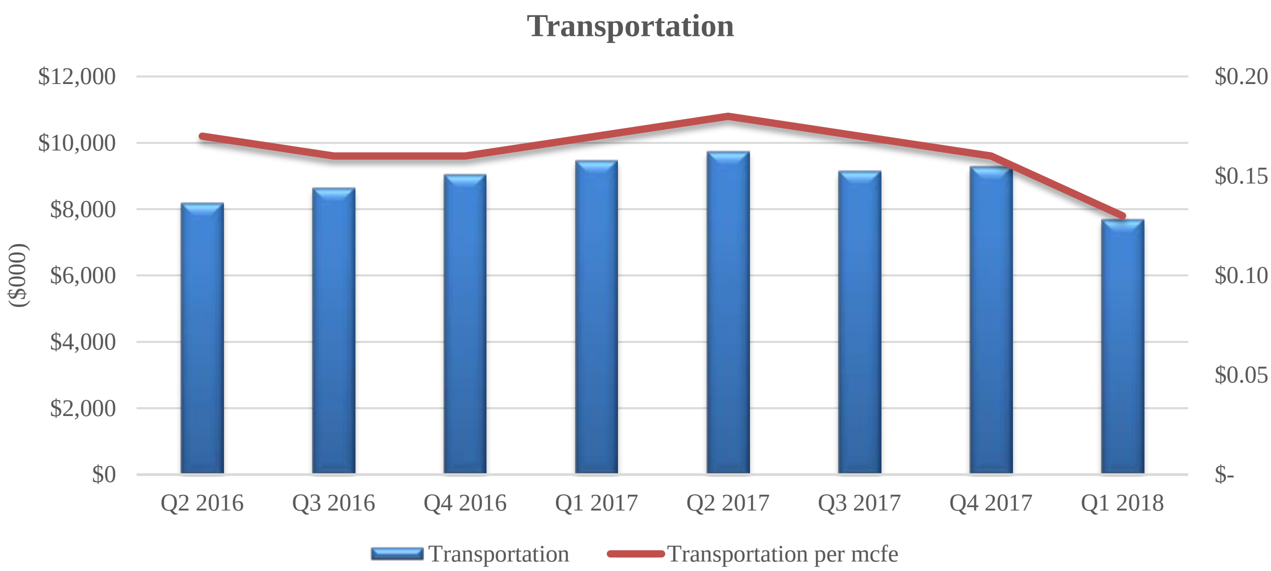
In its 19 year history, Peyto has invested over $5.7 billion in capital projects, found and developed 5.8 TCFe of gas reserves, and paid over $841 million in royalties.

Operating Costs & Transportation
Peyto's operating expenses include all costs with respect to day-to-day well and facility operations.

	Three months ended March 31	
	2018	2017
Operating costs ($000)	**16,454**	15,684
$/mcfe	**0.29**	0.29
$/boe	**1.74**	1.72
Transportation ($000)	**7,686**	9,467
$/mcfe	**0.13**	0.17
$/boe	**0.81**	1.04

For the first quarter, operating expenses increased 5% compared to the same quarter of 2017 primarily due to increase in costs in utilities, chemicals, property taxes and AER Administration fees. On a unit-of-production basis, operating costs remained constant at $0.29/mcfe. Peyto focuses on being the industry leader in operating costs and strives to achieve incremental cost reductions on a continuous basis.

Transportation expenses decreased by 24% from $0.17/mcfe in the first quarter 2017 to $0.13/mcfe in the first quarter of 2018 due to a decrease in TCPL tolls and short term assignment of excess firm service.



General and Administrative Expenses

	Three months ended March 31	
	2018	2017
G&A expenses ($000)	**4,985**	4,693
Overhead recoveries ($000)	**(717)**	(2,380)
Net G&A expenses ($000)	**4,268**	2,313
$/mcfe	**0.08**	0.04
$/boe	**0.45**	0.25

For the first quarter, general and administrative expenses before overhead recoveries was $5.0 million compared to $4.7 million for the same quarter of 2017. Overhead recoveries were 70 per cent lower in Q1 2018 compared to Q1 2017 due to a reduction in capital expenditures. General and administrative expenses averaged $0.09/mcfe before overhead recoveries of $0.01/mcfe for net general and administrative expenses of $0.08/mcfe in the first quarter of 2018 ($0.08/mcfe before overhead recoveries of $0.04/mcfe for net general and administrative expenses of $0.04/mcfe in the first quarter of 2017).

Performance Based Compensation

The Company awards performance based compensation to employees and key consultants annually. The performance based compensation is comprised of market and reserve value based components.

The reserve value based component is 4% of the incremental increase in value, if any, as adjusted to reflect changes in debt, equity, dividends, general and administrative expenses and interest expense, of proved producing reserves calculated using a constant price at December 31 of the current year and a discount rate of 8%. An estimate of reserve additions is made quarterly and is used to calculate an accrued reserve value based expense for the period. This methodology can generate interim results which vary significantly from the final compensation paid. Compensation expense of $Nil was recorded for the first quarter of 2018.

Under the market based component, rights with a three year vesting period are allocated to employees and key consultants. The number of rights outstanding at any time is not to exceed 6% of the total number of common shares outstanding. At December 31 of each year, all vested rights are automatically cancelled and, if applicable, paid out in cash. Compensation is calculated as the number of vested rights multiplied by the total of the market appreciation (over the price at the date of grant) and associated dividends of a common share for that period.

Based on the weighted average trading price of the common shares for the period ended March 31, 2018, compensation costs related to 5.2 million non-vested rights (3.1% of the total number of common shares outstanding), with an average grant price of $16.92, are $1.2 million for the first quarter of 2018. Peyto records a non-cash provision for future compensation expense over the life of the rights calculated using a Black-Scholes valuation model (refer to Note 8 of the condensed financial statements for the more details). This methodology can generate interim results which vary significantly from the final compensation paid. The cumulative provision totals $10.4 million ($10.2 million current liability and $0.1 million long term liability.

Rights Outstanding Under Market Based Compensation Plan

	Valued but Not Vested			To be Valued December 31, 2018	
Vesting Date	**Number of Rights**	**Value ($)**		**Number of Rights**	**Average Grant Price ($)**
December 31, 2018	1,257,400	13,866,813	*	1,314,133	14.68
December 31, 2019	-	-		1,314,133	14.68
December 31, 2020	-	-		1,314,133	14.68

*Valued on December 31, 2016 at $33.80

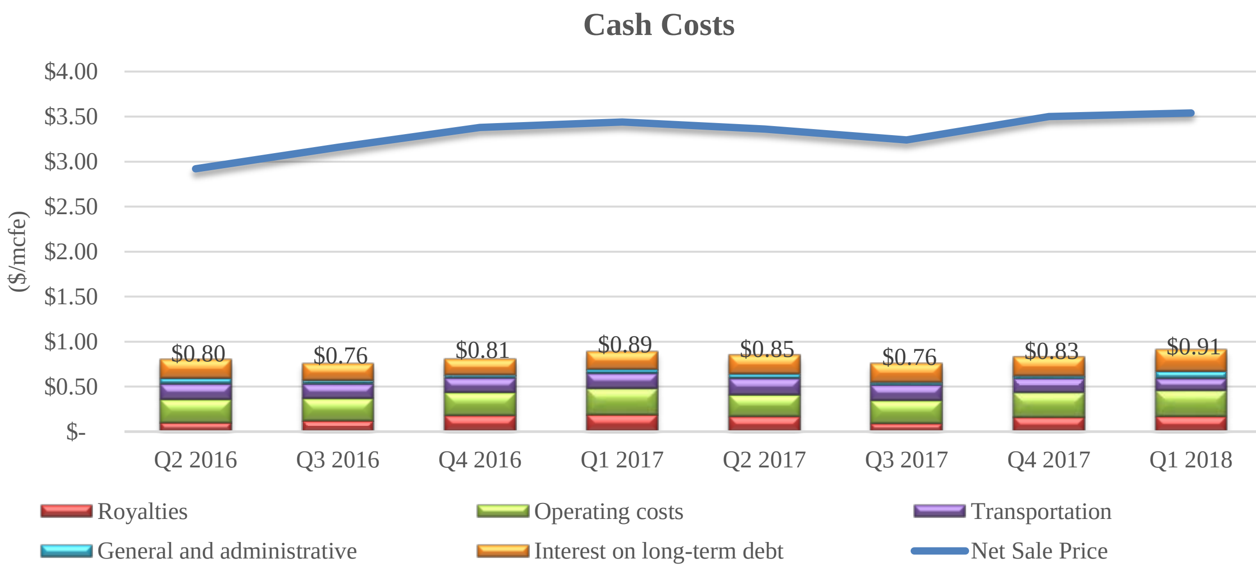
Interest Expense

	Three months ended March 31	
	2018	2017
Interest expense ($000)	**13,460**	10,544
$/mcfe	**0.24**	0.20
$/boe	**1.43**	1.16
Average interest rate	**4.2%**	3.8%

First quarter 2018 interest expense was $13.5 million or $0.24/mcfe compared to $10.5 million or $0.20/mcfe for the first quarter 2017. The average interest rate in the first quarter of 2018 was 4.2% compared to 3.8% in the first quarter of 2017 due to Bank of Canada interest rate increases.

Netbacks

	Three months ended March 31	
($/mcfe)	**2018**	2017
Gross Sale Price	**2.74**	3.61
Hedging gain (loss)	**0.80**	(0.17)
Net Sale Price	**3.54**	3.44
Less: Royalties	**0.17**	0.19
Operating costs	**0.29**	0.29
Transportation	**0.13**	0.17
Field netback	**2.95**	2.79
General and administrative	**0.08**	0.04
Interest on long-term debt	**0.24**	0.20
Cash netback ($/mcfe)	**2.63**	2.55
Cash netback ($/boe)	**15.80**	15.28



Netbacks are a non-GAAP measure that represents the profit margin associated with the production and sale of petroleum and natural gas. Netbacks are per unit of production measures used to assess Peyto's performance and efficiency. The primary factors that produce Peyto's strong netbacks and high margins are a low cost structure and the high heat content of its natural gas that results in higher commodity prices.

Depletion, Depreciation and Amortization

Under IFRS, Peyto uses proved plus probable reserves as its depletion base to calculate depletion expense. The 2018 first quarter provision for depletion, depreciation and amortization totaled $81.6. million compared to $80.0 million in the first quarter 2017. On a unit-of-production basis, depletion and depreciation costs averaged $1.44/mcfe compared to $1.47/mcfe in the first quarter of 2017. As finding and development costs decrease, associated depletion and depreciation costs also decrease.

Income Taxes

The current provision for deferred income tax expense is $17.6 million compared to $14.9 million in the first quarter of 2017. The corporate income tax rate in Alberta remained unchanged at 27%. Resource pools are generated from the capital program, which are available to offset current and deferred income tax liabilities.

Income Tax Pool type ($ millions)	**March 31, 2018**	December 31, 2017	**Annual deductibility**
Canadian Oil and Gas Property Expense	202.7	211.2	10% declining balance
Canadian Development Expense	787.4	848.0	30% declining balance
Canadian Exploration Expense	51.2	76.0	100%
Undepreciated Capital Cost	388.1	406.3	Primarily 25% declining balance
Other	25.8	27.2	Various, 7% to 20% declining balance
Total Federal Tax Pools	**1,455.2**	1,568.7	
Additional Alberta Tax Pools	46.3	46.3	Primarily 100%

MARKETING

Commodity Price Risk Management

The Company is a party to certain derivative financial instruments, including fixed price contracts. The Company enters into these forward contracts with well-established counterparties for the purpose of protecting a portion of its future revenues from the volatility of oil and natural gas prices. In order to minimize counterparty risk, these marketing contracts are executed with financial institutions which are members of Peyto's banking syndicate. During the first quarter of 2018, a realized hedging gain of $45.2 million was recorded as compared to a $9.1 million loss for the equivalent period in 2017. A summary of contracts outstanding in respect of the hedging activities are as follows:

Natural Gas Period Hedged - Monthly Index	Type	Daily Volume	Average Price (CAD)
April 1, 2016 to October 31, 2018	Fixed Price	35,000 GJ	$2.38/GJ
May 1, 2016 to October 31, 2018	Fixed Price	20,000 GJ	$2.29/GJ
July 1, 2016 to October 31, 2018	Fixed Price	20,000 GJ	$2.38/GJ
August 1, 2016 to October 31, 2018	Fixed Price	25,000 GJ	$2.43/GJ
April 1, 2017 to October 31, 2018	Fixed Price	10,000 GJ	$2.67/GJ
November 1, 2017 to October 31, 2018	Fixed Price	5,000 GJ	$2.92/GJ
January 1, 2018 to December 31, 2020	Fixed Price	20,000 GJ	$2.02/GJ
April 1, 2018 to October 31, 2018	Fixed Price	105,000 GJ	$2.05/GJ
April 1, 2018 to March 31, 2019	Fixed Price	185,000 GJ	$2.34/GJ
April 1, 2018 to March 31, 2020	Fixed Price	10,000 GJ	$1.44/GJ
November 1, 2018 to March 31, 2019	Fixed Price	75,000 GJ	$1.84/GJ
November 1, 2018 to March 31, 2020	Fixed Price	5,000 GJ	$1.57/GJ
April 1, 2019 to October 31, 2019	Fixed Price	20,000 GJ	$1.30/GJ
April 1, 2019 to March 31, 2020	Fixed Price	80,000 GJ	$1.76/GJ
November 1, 2019 to March 31, 2020	Fixed Price	15,000 GJ	$2.03/GJ
April 1, 2020 to October 31, 2020	Fixed Price	15,000 GJ	$1.30/GJ
April 1, 2020 to March 31, 2021	Fixed Price	10,000 GJ	$1.65/GJ

Natural Gas Period Hedged -Daily Index	Type	Daily Volume	Price (CAD)
April 1, 2018 to October 31, 2018	Fixed Price	15,000 GJ	$1.59/GJ
April 1, 2018 to March 31, 2019	Fixed Price	40,000 GJ	$1.54/GJ

As at March 31, 2018, Peyto had committed to the future sale of 217,525,000 gigajoules (GJ) of natural gas at an average price of $2.03 per GJ or $2.33 per mcf. Had these contracts closed on March 31, 2018, Peyto would have realized a net gain in the amount of $129.4 million.

Subsequent to March 31, 2018 Peyto entered into the following contracts:

Natural Gas Period Hedged - Monthly Index	Type	Daily Volume	Price (CAD)
November 1, 2018 to March 31, 2019	Fixed Price	20,000 GJ	$1.97/GJ
April 1, 2019 to October 31, 2019	Fixed Price	15,000 GJ	$1.30/GJ
April 1, 2021 to October 31, 2021	Fixed Price	5,000 GJ	$1.64/GJ

Crude Oil Period Hedged	Type	Daily Volume	Price (CAD)
July 1, 2018 to December 31, 2018	Fixed Price	100 bbl	$84.03/bbl
July 1, 2018 to June 30, 2019	Fixed Price	100 bbl	$85.34/bbl

Commodity Price Sensitivity

Peyto's earnings are largely determined by commodity prices for crude oil and natural gas including the US/Canadian dollar exchange rate. Volatility in these oil and gas prices can cause fluctuations in Peyto's earnings. Low operating costs and a long reserve life reduce Peyto's sensitivity to changes in commodity prices.

Currency Risk Management

The Company is exposed to fluctuations in the Canadian/US dollar exchange ratio since commodities are effectively priced in US dollars and converted to Canadian dollars. In the short term, this risk is mitigated indirectly as a result of a commodity hedging strategy that is conducted in a Canadian dollar currency. Over the long term, the Canadian dollar tends to rise as commodity prices rise. There is a similar correlation between oil and gas prices. Currently Peyto has not entered into any agreements to further manage its currency risks.

Interest Rate Risk Management

The Company is exposed to interest rate risk in relation to interest expense on its revolving credit facility while interest rates on the senior notes are fixed. Currently there are no agreements to manage the risk on the credit facility. At March 31 2018, the increase or decrease in earnings for each 100 bps (1%) change in interest rate paid on the outstanding revolving demand loan amounts to approximately $1.7 million per quarter. Average debt outstanding for the quarter was $1.3 billion (including $620 million fixed rate debt).

LIQUIDITY AND CAPITAL RESOURCES

Funds from operations is reconciled to cash flows from operating activities below:

	Three months ended March 31	
($000)	**2018**	2017
Cash flows from operating activities	**143,995**	121,137
Change in non-cash working capital	**3,913**	16,160
Change in provision for performance-based compensation	**1,078**	2,008
Funds from operations	**148,986**	139,305
Funds from operations per share	**0.90**	0.85

For the first quarter ended March 31, 2018, funds from operations totaled $149.0 million or $0.90 per share, compared to $139.3 million or $0.85 per share during the same quarter in 2017. The increase in funds from operation on a per share basis was due to an increase in production volumes and in Oil & NGL prices.

Peyto's policy is to balance dividends to shareholders with earnings and cash flow, and to balance funding for the capital program with cash flow, equity and available bank lines. Earnings and cash flow are sensitive to changes in commodity prices, exchange rates and other factors that are beyond Peyto's control. Current volatility in commodity prices creates uncertainty as to the funds from operations and capital expenditure budget. Accordingly, results are assessed throughout the year and operational plans revised as necessary to reflect the most current information.

Revenues will be impacted by drilling success and production volumes as well as external factors such as the market prices for commodities and the exchange rate of the Canadian dollar relative to the US dollar.

Current and Long-Term Debt

($000)	**March 31, 2018**	December 31, 2017
Current senior unsecured notes	100,000	-
Long-term senior unsecured notes	520,000	520,000
Bank credit facility	650,000	765,000
Balance, end of the period	**1,270,000**	1,285,000

The Company has a syndicated $1.3 billion extendible unsecured revolving credit facility with a stated term date of October 13, 2021. The bank facility is made up of a $40 million working capital sub-tranche and a $1.26 billion production line. The facilities are available on a revolving basis. Borrowings under the facility bear interest at Canadian bank prime or US base rate, or, at Peyto's option, Canadian dollar bankers' acceptances or US dollar LIBOR loan rates, plus applicable margin and stamping fees. The total stamping fees range between 50 basis points and 215 basis points on Canadian bank prime and US base rate borrowings and between 150 basis points and 315 basis points on Canadian dollar bankers' acceptance and US dollar LIBOR borrowings. The undrawn portion of the facility is subject to a standby fee in the range of 30 to 63 basis points.

Peyto is subject to the following financial covenants as defined in the credit facility and note purchase agreements:

- Long-term debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 3.0 times trailing twelve month net income before non-cash items, interest and income taxes;

  as at March 31, 2018 – 1.98:1.0

- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 4.0 times trailing twelve month net income before non-cash items, interest and income taxes;

  as at March 31, 2018 – 1.98:1.0

- Trailing twelve months net income before non-cash items, interest and income taxes to exceed 3.0 times trailing twelve months interest expense;

  as at March 31, 2018 – 12.5 times

- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 55% of shareholders' equity and long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items.

  as at March 31, 2018 – 42%

Peyto is in compliance with all financial covenants and has no subordinated debt as at March 31, 2018.

On January 2, 2018, the Company closed an issuance of CDN $100 million of senior unsecured notes. The notes were issued by way of a private placement, pursuant to a note purchase agreement and a note purchase and private shelf agreement, and rank equally with Peyto's obligations under its bank facility and existing note purchase agreements. The notes have a coupon rate of 3.95% and mature on January 2, 2028. Interest will be paid semi-annually in arrears. Proceeds from the notes were used to repay a portion of Peyto's outstanding bank debt.

Outstanding senior notes are as follows (includes notes due within one year):

Senior Unsecured Notes	**Date Issued**	**Rate**	**Maturity Date**
$100 million	January 3, 2012	4.39%	January 3, 2019
$50 million	September 6, 2012	4.88%	September 6, 2022
$120 million	December 4, 2013	4.50%	December 4, 2020
$50 million	July 3, 2014	3.79%	July 3, 2022
$100 million	May 1, 2015	4.26%	May 1, 2025
$100 million	October 24, 2016	3.70%	October 24, 2023
$100 million	January 2, 2018	3.95%	January 2, 2028

Peyto's total borrowing capacity after the issuance of the senior, unsecured notes on January 2, 2018 is $1.92 billion of which the credit facility is $1.3 billion.

Senior unsecured notes in the amount of CAD $100 million with a coupon rate of 4.39% mature on January 3, 2019 and have therefore been classified as a current liability. It is Peyto's intention to re-finance these notes with long term debt at a comparable interest rate.

Peyto believes funds generated from operations, together with borrowings under the credit facility will be sufficient to maintain dividends, finance current operations, and fund the planned capital expenditure program of approximately $200 to $250 million for 2018. The total amount of capital invested in 2018 will be driven by the number and quality of projects generated. Capital will only be invested if it meets the long-term objectives of the Company. The majority of the capital program will involve drilling, completion and tie-in of lower risk development gas wells. Peyto's rapidly scalable business model has the flexibility to match planned capital expenditures to actual cash flow.

Net Debt

"Net debt" is a non-GAAP measure that is the sum of long-term debt and working capital excluding the current financial derivative instruments and current provision for future performance-based compensation. It is used by management to analyze the financial position and leverage of the Company. Net debt is reconciled below to long-term debt which is the most directly comparable GAAP measure:

($000)	**As at March 31, 2018**	As at December 31, 2017	As at March 31, 2017
Bank credit facility	**650,000**	765,000	615,000
Senior unsecured notes	**620,000**	520,000	520,000
Current assets	**(211,161)**	(243,489)	(100,703)
Current liabilities	**77,119**	160,078	198,395
Financial derivative instruments	**117,577**	135,017	(19,842)
Provision for future performance-based compensation	**(10,244)**	(9,166)	(8,862)
Net debt	**1,243,291**	1,327,440	1,203,988

Capital

Authorized: Unlimited number of voting common shares

Issued and Outstanding

Common Shares (no par value)	**Number of Common Shares**	**Amount ($000)**
Balance, December 31, 2017	**164,874,175**	**1,649,537**
Common shares issued	-	-
Common share issuance costs, (net of tax)	-	-
Balance, March 31, 2018	**164,874,175**	**1,649,537**

Capital Expenditures

Net capital expenditures for the first quarter of 2018 totaled $35.5 million. Exploration and development related activity represented $31.1 million (88%), while expenditures on facilities, gathering systems and equipment totaled $7.5 million (21%) and land, seismic, and dispositions totaled $(3.2) million (-9%). The following table summarizes capital expenditures for the period:

	Three months ended March 31	
($000)	**2018**	2017
Land	**650**	5,623
Seismic	**182**	3,592
Drilling	**14,236**	67,061
Completions	**16,901**	36,111
Equipping & Tie-ins	**3,818**	12,924
Facilities & Pipelines	**3,669**	25,089
Acquisitions	**-**	3,474
Dispositions	**(4,002)**	-
Total Capital Expenditures	**35,454**	153,874

Dividends

	Three months ended March 31	
	2018	2017
Funds from operations ($000)	**148,986**	139,305
Total dividends ($000)	**29,677**	54,387
Total dividends per common share ($)	**0.18**	0.33
Payout ratio (%)	**20**	39

Peyto's policy is to balance dividends to shareholders with earnings and cash flow; and funding for the capital program with cash flow, equity and available bank lines. The Board of Directors is prepared to adjust the payout ratio levels (dividends declared divided by funds from operations) to achieve the desired dividends while maintaining an appropriate capital structure.

Contractual Obligations
In addition to those recorded on the Company's balance sheet, the following is a summary of Peyto's contractual obligations and commitments as at March 31, 2018:

($000)	2018	2019	2020	2021	2022	Thereafter
Interest payments [1]	18,710	23,840	21,645	16,245	16,245	36,075
Transportation commitments	27,420	30,702	19,475	18,655	26,265	245,944
Operating leases	1,682	2,242	2,242	2,242	2,317	9,269
Total	47,812	56,784	43,362	37,142	44,827	291,288

(1) Fixed interest payments on senior unsecured notes

LITIGATION

On October 1, 2013, two shareholders (the "Plaintiffs") of Poseidon Concepts Corp. ("Poseidon") filed an application to seek leave of the Alberta Court of Queen's Bench (the "Court") to pursue a class action lawsuit against the Company, as a successor to new Open Range Energy Corp. ("New Open Range") (the "Poseidon Shareholder Application"). The proposed action contained various claims relating to alleged misrepresentations in disclosure documents of Poseidon (not New Open Range), which claims were also alleged in class action lawsuits filed in Alberta, Ontario, and Quebec earlier in 2013 against Poseidon and certain of its current and former directors and officers, and underwriters involved in the public offering of common shares of Poseidon completed in February 2012. The proposed class action sought various declarations and damages including compensatory damages which the Plaintiffs estimate at $651 million and punitive damages which the Plaintiffs estimate at $10 million, which damage amounts appear to be duplicative of damage amounts claimed in the class actions against Poseidon, certain of its current and former directors and officers, and underwriters. An application seeking leave to commence a class action lawsuit against the Company making the same allegations was also made by two Poseidon shareholders in Ontario (the "Ontario Poseidon Shareholder Action"). No steps were taken to advance these actions against the Company.

New Open Range was incorporated on September 14, 2011 solely for purposes of participating in a plan of arrangement with Poseidon (formerly named Open Range Energy Corp. ("Old Open Range")), which was completed on November 1, 2011. Pursuant to such arrangement, Poseidon completed a corporate reorganization resulting in two separate publicly-traded companies: Poseidon, which continued to carry on the energy service and supply business; and New Open Range, which carried on Poseidon's former oil and gas exploration and production business. Peyto acquired all of the issued and outstanding common shares of New Open Range on August 14, 2012. On April 9, 2013, Poseidon obtained creditor protection under the Companies' Creditor Protection Act.

On October 31, 2013, Poseidon filed a lawsuit with the Court naming the Company as a co-defendant along with the former directors and officers of Poseidon, the former directors and officers of Old Open Range and the former directors and officers of New Open Range (the "Poseidon Action"). Poseidon claimed, among other things, that the Company is vicariously liable for the alleged wrongful acts and breaches of duty of the directors, officers and employees of New Open Range. No steps were taken to advance these actions against the Company.

On September 24, 2014 Poseidon amended its claim in the Poseidon Action to add Poseidon's auditor, KPMG LLP ("KPMG"), as a defendant.

On May 4, 2016, KPMG issued a third party claim in the Poseidon Action against Poseidon's former officers and directors and the Company for any liability KPMG is determined to have to Poseidon. The Company was not required to defend KPMG's third party claim.

On July 3, 2014, the Plaintiffs filed a lawsuit with the Court against KPMG, Poseidon's and Old Open Range's former auditors, making allegations substantially similar to those in the other claims (the "KPMG Poseidon Shareholder KPMG Action").

On July 29, 2014, KPMG filed a statement of defence and a third party claim against Poseidon, the Company and the former directors and officers of Poseidon. The third party claim sought, among other things, an indemnity, or alternatively contribution, from the third party defendants with respect to any judgment awarded against KPMG LLP. The Company was not required to defend KPMG's third party claim.

The allegations against New Open Range contained in the claims described above were based on factual matters that pre-existed the Company's acquisition of New Open Range.

On April 6, 2018, the Company entered a global settlement with all parties involved in the Poseidon related litigation. The settlement was presented to the Alberta Court of Queens Bench on May 4, 2018 for approval as part of a plan of compromise and arrangement under the Companies' Creditor Arrangement Act. The Alberta Court approved the settlement and Plan and issued Orders dismissing Alberta actions involving Poseidon including the Poseidon Shareholder Application and the Poseidon Action against the Company. The Ontario, Quebec and United States Courts will now be asked to recognize the Alberta Court's Orders and to dismiss the actions before them (including the Ontario Poseidon Shareholder Action against the Company). Assuming the Alberta Court Orders are recognized, the settlement will be effective and all of the actions involving Poseidon including the Poseidon Shareholder Application, the Ontario Poseidon Shareholder Action and the Poseidon Action against the Company will be dismissed. Although the contributions being made by the different defendants are confidential, Peyto's contribution is immaterial and reflects its belief there was no merit to the claims.

RELATED PARTY TRANSACTIONS

Certain directors of Peyto are considered to have significant influence over other reporting entities that Peyto engages in transactions with. Such services are provided in the normal course of business and at market rates. These directors are not involved in the day to day operational decision making of the Company. The dollar value of the transactions between Peyto and the related reporting entities is summarized below:

Expense ($000)		Accounts Payable ($000)	
Three Months ended March 31		As at March 31	
2018	2017	**2018**	2017
118.0	82.4	**118.0**	78.4

RISK MANAGEMENT

Investors who purchase shares are participating in the total returns from a portfolio of western Canadian natural gas producing properties. As such, the total returns earned by investors and the value of the shares are subject to numerous risks inherent in the oil and natural gas industry.

Expected returns depend largely on the volume of petroleum and natural gas production and the price received for such production, along with the associated costs. The price received for oil depends on a number of factors, including West Texas Intermediate oil prices, Canadian/US currency exchange rates, quality differentials and Edmonton par oil prices. The price received for natural gas production is primarily dependent on current Alberta market prices. Peyto's marketing strategy is designed to smooth out short term fluctuations in the price of natural gas through future sales. It is meant to be methodical and consistent and to avoid speculation.

Although Peyto's focus is on internally generated drilling programs, any acquisition of oil and natural gas assets depends on an assessment of value at the time of acquisition. Incorrect assessments of value can adversely affect dividends to shareholders and the value of the shares. Peyto employs experienced staff and performs appropriate levels of due diligence on the analysis of acquisition targets, including a detailed examination of reserve reports; if appropriate, re-engineering of reserves for a large portion of the properties to ensure the results are consistent; site examinations of facilities for environmental liabilities; detailed examination of balance sheet accounts; review of contracts; review of prior year tax returns and modeling of the acquisition to attempt to ensure accretive results to the shareholders.

Inherent in development of the existing oil and gas reserves are the risks, among others, of drilling dry holes, encountering production or drilling difficulties or experiencing high decline rates in producing wells. To minimize these risks, Peyto employs experienced staff to evaluate and operate wells and utilize appropriate technology in operations. In addition, prudent work practices and procedures, safety programs and risk management principles, including insurance coverage protect Peyto against certain potential losses.

The value of Peyto's shares is based on among other things, the underlying value of the oil and natural gas reserves. Geological and operational risks can affect the quantity and quality of reserves and the cost of ultimately recovering those reserves. Lower oil and gas prices increase the risk of write-downs on oil and gas property investments. In order to mitigate this risk, proven and probable oil and gas reserves are evaluated each year by a firm of independent reservoir engineers. The reserves committee of the Board of Directors reviews and approves the reserve report.

Access to markets may be restricted at times by pipeline or processing capacity. These risks are minimized by controlling as much of the processing and transportation activities as possible and ensuring transportation and processing contracts are in place with reliable cost efficient counterparties.

The petroleum and natural gas industry is subject to extensive controls, regulatory policies and income and resource taxes imposed by various levels of government. These regulations, controls and taxation policies are amended from time to time. Peyto has no control over the level of government intervention or taxation in the petroleum and natural gas industry. Peyto operates in such a manner to ensure, to the best of its knowledge that it is in compliance with all applicable regulations and are able to respond to changes as they occur.

The petroleum and natural gas industry is subject to both environmental regulations and an increased environmental awareness. Peyto has reviewed its environmental risks and is, to the best of its knowledge, in compliance with the appropriate environmental legislation and have determined that there is no current material impact on operations. Peyto employs environmentally responsible business operations, and looks to both Alberta provincial authorities and Canada's federal authorities for direction and regulation regarding environmental and climate change legislation.

Peyto is subject to financial market risk. In order to maintain substantial rates of growth, Peyto must continue reinvesting in, drilling for or acquiring petroleum and natural gas. The capital expenditure program is funded primarily through funds from operations, debt and, if appropriate, equity.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: (i) material information relating to the Company is made known to the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation. Such officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Company's disclosure controls and procedures at the year end of the Company and have concluded that the Company's disclosure controls and procedures are effective at the financial period end of the Company for the foregoing purposes.

Internal Control over Financial Reporting

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, internal control over financial reporting to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Such officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Company's internal control over financial reporting at the financial period end of the Company and concluded that the Company's internal control over financial reporting is effective, at the financial period end of the Company, for the foregoing purpose.

Peyto is required to disclose herein any change in Peyto's internal control over financial reporting that occurred during the period ended March 31, 2018 that has materially affected, or is reasonably likely to materially affect, Peyto's internal control over financial reporting. No material changes in Peyto's internal control over financial reporting were identified during such period that has materially affected, or are reasonably likely to materially affect, Peyto's internal control over financial reporting.

It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

CRITICAL ACCOUNTING ESTIMATES

Reserve Estimates

Estimates of oil and natural gas reserves, by necessity, are projections based on geologic and engineering data, and there are uncertainties inherent to the interpretation of such data as well as the projection of future rates of production and the timing of development expenditures. Reserve engineering is an analytical process of estimating underground accumulations of oil and natural gas that can be difficult to measure. The accuracy of any reserve estimate is a function of the quality of available data, engineering and geological interpretation and judgment. Estimates of economically recoverable oil and natural gas reserves and future net cash flows necessarily depend upon a number of variable factors and assumptions, such as historical production from the area compared with production from other producing areas, the assumed effects of regulations by governmental agencies and assumptions governing future oil and natural gas prices, future royalties and operating costs, development costs and workover and remedial costs, all of which may in fact vary considerably from actual results. For these reasons, estimates of the economically recoverable quantities of oil and natural gas attributable to any particular group of properties, classifications of such reserves based on risk recovery, and estimates of the future net cash flows expected there from may vary substantially. Any significant variance in the assumptions could materially affect the estimated quantity and value of the reserves, which could affect the carrying value of Peyto's oil and natural gas properties and the rate of depletion of the oil and natural gas properties as well as the calculation of the reserve value based compensation. Actual production, revenues and expenditures with respect to Peyto's reserves will likely vary from estimates, and such variances may be material.

Peyto's estimated quantities of proved and probable reserves at December 31, 2017 were evaluated by independent petroleum engineers InSite Petroleum Consultants Ltd. InSite has been evaluating reserves in this area and for Peyto since inception.

Depletion and Depreciation Estimate
All costs of exploring for and developing petroleum and natural gas reserves, together with the costs of production equipment, are capitalized and then depleted and depreciated on the unit-of-production method based on proved plus probable reserves. Petroleum and natural gas reserves and production are converted into equivalent units based upon estimated relative energy content (6 mcf to 1 barrel of oil). Costs for gas plants and other facilities are capitalized and depreciated on a declining balance basis.

Impairment of Long-Lived Assets
Impairment is indicated if the carrying value of the long-lived asset or oil and gas cash generating unit exceeds its recoverable amount under IFRS. If impairment is indicated, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. The determination of the recoverable amount for impairment purposes under IFRS involves the use of numerous assumptions and judgments including future net cash flows from oil and gas reserves, future third-party pricing, inflation factors, discount rates and other uncertainties. Future revisions to these assumptions impact the recoverable amount.

Decommissioning Provision
The decommissioning provision is estimated based on existing laws, contracts or other policies. The fair value of the obligation is based on estimated future costs for abandonment and reclamation discounted at a credit adjusted risk free rate. The liability is adjusted each reporting period to reflect the passage of time and for revisions to the estimated future cash flows, with the accretion charged to earnings. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material.

Future Market Performance Based Compensation
The provision for future market based compensation is estimated based on current market conditions, distribution history and on the assumption that all outstanding rights will be paid out according to the vesting schedule. The conditions at the time of vesting could vary significantly from the current conditions and may have a material effect on the calculation.

Reserve Value Performance Based Compensation
The reserve value-based compensation is calculated using the year end independent reserves evaluation which was completed in February 2018. A quarterly provision for the reserve value based compensation is calculated using estimated proved producing reserve additions adjusted for changes in debt, equity and dividends. Actual proved producing reserves additions and forecasted commodity prices could vary significantly from those estimated and may have a material effect on the calculation.

Income Taxes
The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded.

Accounting Changes
Voluntary changes in accounting policy are made only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impractical to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and changes in accounting estimates are applied prospectively by including these changes in earnings. When the Company has not applied a new primary source of GAAP that has been issued, but is not effective, the Company will disclose the fact along with information relevant

to assessing the possible impact that application of the new primary source of GAAP will have on the financial statements in the period of initial application.

STANDARDS ISSUED BUT NOT YET EFFECTIVE

The IASB issued the following standards and amendments which are not yet effective for Peyto and discussed in further detail in Note 2 to the Financial Statements for the fiscal period ended March 31, 2018.

> In January 2016, the IASB issued IFRS 16 “Leases”, which replaces IAS 17 “Leases”. For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition of assets and liabilities for most leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. The Company is currently evaluating the impact of the standard on the Company’s financial statements.

ADDITIONAL INFORMATION

Additional information relating to Peyto Exploration & Development Corp. can be found on SEDAR at www.sedar.com and www.peyto.com.

Quarterly information

	2018	2017			
	Q1	Q4	Q3	Q2	Q1
Operations					
Production					
Natural gas (mcf/d)	568,496	595,885	557,958	535,274	549,037
Oil & NGLs (bbl/d)	10,043	10,479	8,958	8,319	9,586
Barrels of oil equivalent (boe/d @ 6:1)	104,793	109,793	101,951	97,531	101,093
Thousand cubic feet equivalent (mcfe/d @ 6:1)	628,755	658,759	611,703	585,187	606,556
Average product prices					
Natural gas ($/mcf)	2.86	2.87	2.81	2.92	2.96
Oil & natural gas liquids ($/bbl)	59,67	56.52	45.92	48.33	48.14
$/MCFE					
Average sale price ($/mcfe)	3.54	3.50	3.24	3.36	3.44
Average royalties paid ($/mcfe)	0.17	0.15	0.09	0.17	0.19
Average operating expenses ($/mcfe)	0.29	0.28	0.26	0.24	0.29
Average transportation costs ($/mcfe)	0.13	0.16	0.17	0.18	0.17
Field netback ($/mcfe)	2.95	2.91	2.72	2.77	2.79
General & administrative expense ($/mcfe)	0.08	0.03	0.03	0.05	0.04
Interest expense ($/mcfe)	0.24	0.21	0.21	0.21	0.20
Cash netback ($/mcfe)	2.63	2.67	2.48	2.51	2.55
Financial ($000 except per share)					
Revenue and realized hedging gains (losses)	200,397	211,799	182,226	178,982	187,949
Royalties	9,543	9,232	5,165	9,071	10,635
Funds from operations	148,986	161,672	139,257	133,487	139,305
Funds from operations per share	0.90	0.98	0.85	0.81	0.85
Total dividends	29,677	54,408	54,408	54,408	54,387
Total dividends per share	0.18	0.33	0.33	0.33	0.33
Payout ratio	20%	34%	39%	41%	39%
Earnings	47,749	51,547	44,818	39,957	40,255
Earnings per share	0.29	0.31	0.27	0.24	0.24
Capital expenditures	35,454	134,411	135,187	97,738	153,874
Weighted average shares outstanding	164,874,175	164,874,175	164,874,175	164,874,175	164,800,637

Peyto Exploration & Development Corp.

Condensed Balance Sheet *(unaudited)*

(Amount in $ thousands)

	March 31 2018	December 31 2017
Assets		
Current assets		
Cash	-	5,652
Accounts receivable (*Note 8)*	80,978	90,242
Derivative financial instruments *(Note 10)*	117,577	135,017
Prepaid expenses	12,606	12,578
	211,161	243,489
Long-term derivative financial instruments *(Note 10)*	11,867	16,233
Property, plant and equipment, net *(Note 4)*	3,539,807	3,584,992
	3,551,674	3,601,225
	3,762,835	3,844,714
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	56,983	132,776
Dividends payable *(Note 7)*	9,893	18,136
Provision for future performance-based compensation *(Note 9)*	10,243	9,166
Current portion of long-term debt *(Note 5)*	100,000	-
	177,119	160,078
Long-term debt *(Note 5)*	1,170,000	1,285,000
Provision for future performance-based compensation *(Note 9)*	115	-
Decommissioning provision *(Note 6)*	145,844	143,805
Deferred income taxes	544,626	532,853
	1,860,585	1,961,658
Equity		
Share capital *(Note 7)*	1,649,537	1,649,537
Retained earnings (deficit)	(22,189)	(40,261)
Accumulated other comprehensive loss *(Note 7)*	97,783	113,702
	1,725,131	1,722,978
	3,762,835	3,844,714

See accompanying notes to the financial statements.

Approved by the Board of Directors

(signed) *"Michael MacBean"*
Director

(signed) *"Darren Gee"*
Director

Peyto Exploration & Development Corp.

Condensed Income Statement *(unaudited)*

(Amount in $ thousands)

	Three months ended March 31	
	2018	**2017**
Revenues		
Natural gas and natural gas liquid sales (*Note 8)*	155,168	197,036
Royalties	(9,543)	(10,635)
Natural gas and natural gas liquid sales, net of royalties	**145,625**	186,401
Risk management contracts		
Realized gain (loss) on risk management contracts *(Note 10)*	45,229	(9,087)
	190,854	177,314
Expenses		
Operating	16,454	15,684
Transportation	7,686	9,467
General and administrative	4,268	2,313
Future performance-based compensation *(Note 9)*	1,193	3,370
Interest	13,460	10,544
Accretion of decommissioning provision (*Note 6)*	804	750
Depletion and depreciation *(Note 4)*	81,579	80,043
	125,444	122,171
Earnings before taxes	**65,410**	55,143
Income tax		
Deferred income tax expense	17,661	14,888
Earnings for the period	**47,749**	40,255

Earnings per share *(Note 7)*		
Basic and diluted	**$0.29**	$0.24

Peyto Exploration & Development Corp.

Condensed Statement of Comprehensive Income *(unaudited)*

(Amount in $ thousands)

	Three months ended March 31	
	2018	**2017**
Earnings for the period	**47,749**	40,255
Other comprehensive income		
Change in unrealized gain on cash flow hedges	23,422	131,960
Deferred income tax recovery (expense)	5,888	(38,083)
Realized (gain) loss on cash flow hedges	(45,229)	9,087
Comprehensive income	**31,830**	143,219

Peyto Exploration & Development Corp.

Condensed Statement of Changes in Equity *(unaudited)*

(Amount in $ thousands)

	Three months ended March 31	
	2018	**2017**
Share capital, beginning of period	**1,649,537**	1,641,982
Common shares issued by private placement	-	7,574
Common shares issuance costs (net of tax)	-	(19)
Share capital, end of period	**1,649,537**	1,649,537

Common shares to be issued, beginning of period	**-**	4,930
Common shares issued	**-**	(4,930)
Common shares to be issued, end of period	**-**	-

Retained earnings (deficit), beginning of period	**(40,261)**	776
Earnings for the period	47,749	40,255
Dividends *(Note 7)*	(29,677)	(54,388)
Retained earnings (deficit), end of period	**(22,189)**	(13,357)

Accumulated other comprehensive income (loss), beginning of period	**113,702**	(106,754)
Other comprehensive (income) loss	(15,919)	102,964
Accumulated other comprehensive income (loss), end of period	**97,783**	(3,790)

Total equity	**1,725,131**	1,632,390

Peyto Exploration & Development Corp.

Condensed Statement of Cash Flows *(unaudited)*

(Amount in $ thousands)

	Three months ended March 31	
	2018	**2017**
Cash provided by (used in) operating activities		
Earnings	47,749	40,255
Items not requiring cash:		
Deferred income tax	17,661	14,888
Depletion and depreciation	81,579	80,043
Accretion of decommissioning provision	804	750
Long term portion of future performance-based compensation	115	1,361
Change in non-cash working capital related to operating activities	(3,913)	(16,160)
	143,995	121,137
Financing activities		
Issuance of common shares	-	7,574
Issuance costs	-	(26)
Cash dividends paid	(37,921)	(54,361)
Increase in senior notes	100,000	-
Increase (decrease) in bank debt	(115,000)	65,000
	(52,921)	18,187
Investing activities		
Additions to property, plant and equipment	(35,454)	(153,874)
Change in prepaid capital	295	(6,598)
Change in non-cash working capital relating to investing activities	(61,567)	19,046
	(96,726)	(141,426)
Net (decrease) in cash	**(5,652)**	(2,102)
Cash, beginning of period	**5,652**	2,102
Cash, end of period	**-**	-

The following amounts are included in cash flows from operating activities:

Cash interest paid	**11,044**	9,432
Cash taxes paid	**-**	-

1. Nature of operations

Peyto Exploration & Development Corp. ("Peyto" or the "Company") is a Calgary based oil and natural gas company. Peyto conducts exploration, development and production activities in Canada. Peyto is incorporated and domiciled in the Province of Alberta, Canada. The address of its registered office is 300, 600 – 3rd Avenue SW, Calgary, Alberta, Canada, T2P 0G5.

These financial statements were approved and authorized for issuance by the Audit Committee of Peyto on May 7, 2018.

2. Basis of presentation

The condensed financial statements have been prepared by management and reported in Canadian dollars in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting". These condensed financial statements do not include all of the information required for full annual financial statements and should be read in conjunction with the Company's financial statements as at and for the years ended December 31, 2017 and 2016.

Significant Accounting Policies

(a) Significant Accounting Judgments Estimates and Assumptions

The timely preparation of the condensed financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies, if any, as at the date of the financial statements and the reported amounts of revenue and expenses during the period. By their nature, estimates are subject to measurement uncertainty and changes in such estimates in future years could require a material change in the condensed financial statements.

Except for the impact of adoption of new accounting standards as discussed in note 3 below, all accounting policies and methods of computation followed in the preparation of these financial statements are the same as those disclosed in Note 2 of Peyto's financial statements as at and for the years ended December 31, 2017 and 2016.

(b) Recent Accounting Pronouncements

Standards issued but not yet effective

In January 2016, the IASB issued IFRS 16 "Leases", which replaces IAS 17 "Leases". For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition of assets and liabilities for most leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. The Company is currently evaluating the impact of the standard on the Company's financial statements.

3. Changes in Accounting Policies

IFRS 9 "Financial instruments"

On January 1, 2018, Peyto adopted IFRS 9 "Financial Instruments" as issued by the IASB. IFRS 9 includes a new classification and measurement approach for financial assets and a forward-looking 'expected credit loss' model.

Peyto has revised the description of its accounting policy for financial instruments to reflect the new classification approach as follows:

Financial instruments

On initial recognition, financial instruments are measured at fair value. Measurement in subsequent periods depends on the classification of the financial instrument as described below:

• Fair value through profit or loss: Financial instruments under this classification include cash and derivative assets and liabilities.
• Amortized cost: Financial instruments under this classification include accounts receivable, accounts payable, accrued liabilities, dividends payable, and long-term debt.

The standard also provides a simplified approach to measuring expected credit losses using a lifetime expected loss allowance for all trade receivables and contract assets. The credit loss model groups receivables based on similar credit risk characteristics and days past due in order to estimate bad debts. The adoption of this approach did not result in a material impact to the Peyto’s financial statements due to the high credit quality of Peyto's customers.

IFRS 15 "Revenue from contracts with customers"

On January 1, 2018, Peyto adopted IFRS 15 "Revenue from Contracts with Customers". IFRS 15 establishes a comprehensive framework for determining whether, how much, and when revenue from contracts with customers is recognized. Peyto's revenue relates to the sale of natural gas and natural gas liquids to customers at specified delivery points at benchmark prices. Peyto adopted IFRS 15 using the modified retrospective approach. Under this transitional provision, the cumulative effect of initially applying IFRS 15 is recognized on the date of initial application as an adjustment to retained earnings. As a result of applying the requirements of IFRS 15, including the application of certain practical expedients such as the right to invoice method of measuring the Company’s progress towards complete satisfaction of its performance obligations, no changes or adjustments to the comparative financial statements were required. Refer to Note 8 for more information including additional disclosures required under IFRS 15.

As a result of this adoption, Peyto has revised the description of its accounting policy for revenue recognition as follows:

Revenue associated with the sale of natural gas and natural gas liquids is measured based on the consideration specified in contracts with customers. Revenue from contracts with customers is recognized when Peyto satisfies a performance obligation by transferring a promised good or service to a customer. A good or service is transferred when the customer obtains control of that good or service. The transfer of control of natural gas and natural gas liquids usually coincides with title passing to the customer and the customer taking physical possession.

Peyto principally satisfies its performance obligations at a point in time. Joint venture partners are not considered customers and therefore processing and gathering recoveries related to joint operations are netted against operating expenses.

4. Property, plant and equipment, net

Cost	
At December 31, 2017	**5,453,072**
Additions	35,454
Decommissioning provision additions	1,235
Prepaid capital	(295)
At March 31, 2018	**5,489,466**
Accumulated depletion and depreciation	
At December 31, 2017	**(1,868,080**
Depletion and depreciation	(81,579)
At March 31, 2018	**(1,949,659**
Carrying amount at December 31, 2017	3,584,992
Carrying amount at March 31, 2018	**3,539,807**

During the period ended March 31, 2018, Peyto capitalized $0.6 million (2017 - $2.1 million) of general and administrative expense directly attributable to production and development activities.

5. Current and Long-term debt

	March 31, 2018	December 31, 2017
Current senior unsecured notes	100,000	-
Long-term senior unsecured notes	520,000	520,000
Bank credit facility	650,000	765,000
Balance, end of the period	**1,270,000**	1,285,000

The Company has a syndicated $1.3 billion extendible unsecured revolving credit facility with a stated term date of October 13, 2021. The bank facility is made up of a $40 million working capital sub-tranche and a $1.26 billion production line. The facilities are available on a revolving basis. Borrowings under the facility bear interest at Canadian bank prime or US base rate, or, at Peyto's option, Canadian dollar bankers' acceptances or US dollar LIBOR loan rates, plus applicable margin and stamping fees. The total stamping fees range between 50 basis points and 215 basis points on Canadian bank prime and US base rate borrowings and between 150 basis points and 315 basis points on Canadian dollar bankers' acceptance and US dollar LIBOR borrowings. The undrawn portion of the facility is subject to a standby fee in the range of 30 to 63 basis points.

Peyto is subject to the following financial covenants as defined in the credit facility and note purchase agreements:

- Long-term debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 3.0 times trailing twelve-month net income before non-cash items, interest and income taxes;
- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 4.0 times trailing twelve-month net income before non-cash items, interest and income taxes;
- Trailing twelve months net income before non-cash items, interest and income taxes to exceed 3.0 times trailing twelve months interest expense;
- Long-term debt and subordinated debt plus the average working capital deficiency (surplus) at the end of the two most recently completed fiscal quarters adjusted for non-cash items not to exceed 55 per cent of the book value of shareholders' equity and long-term debt and subordinated debt.

Outstanding senior notes are as follows (includes notes due within one year):

Senior Unsecured Notes	Date Issued	Rate	Maturity Date
$100 million	January 3, 2012	4.39%	January 3, 2019
$50 million	September 6, 2012	4.88%	September 6, 2022
$120 million	December 4, 2013	4.50%	December 4, 2020
$50 million	July 3, 2014	3.79%	July 3, 2022
$100 million	May 1, 2015	4.26%	May 1, 2025
$100 million	October 24, 2016	3.70%	October 24, 2023
$100 million	January 2, 2018	3.95%	January 2, 2028

On January 2, 2018, the Company closed an issuance of CDN $100 million of senior unsecured notes. The notes were issued by way of a private placement, pursuant to a note purchase agreement and a note purchase and private shelf agreement, and rank equally with Peyto's obligations under its bank facility and existing note purchase agreements. The notes have a coupon rate of 3.95% and mature on January 2, 2028. Interest will be paid semi-annually in arrears. Proceeds from the notes were used to repay a portion of Peyto's outstanding bank debt.

Peyto is in compliance with all financial covenants at March 31, 2018.

Total interest expense for the period ended March 31, 2018 was $13.4 million (2017 - $10.5 million) and the average borrowing rate for the period was 4.2% (2017 – 3.8%).

6. Decommissioning provision

The following table reconciles the change in decommissioning provision:

Balance, December 31, 2017	**143,805**
New or increased provisions	778
Accretion of decommissioning provision	804
Change in discount rate and estimates	457
Balance, March 31, 2018	**145,844**
Current	-
Non-current	145,844

Peyto has estimated the net present value of its total decommissioning provision to be $145.8 million as at March 31, 2018 ($143.8 million at December 31, 2017) based on a total future undiscounted liability of $291.3 million ($289.7 million at December 31, 2017). At March 31, 2018 management estimates that these payments are expected to be made over the next 49 years with the majority of payments being made in years 2046 to 2067. The Bank of Canada's long term bond rate of 2.23 per cent (2.26 per cent at December 31, 2017) and an inflation rate of 2.0 per cent (2.0 per cent at December 31, 2017) were used to calculate the present value of the decommissioning provision.

7. Share capital

Authorized: Unlimited number of voting common shares

Issued and Outstanding

Common Shares (no par value)	Number of Common Shares	Amount $
Balance, December 31, 2017	**164,874,175**	**1,649,537**
Common shares issued by private placement	-	-
Common share issuance costs, (net of tax)	-	-
Balance, March 31, 2018	**164,874,175**	**1,649,537**

Earnings per common share has been determined based on the following:

	Three Months ended March 31,	
	2018	2017
Weighted average common shares basic and diluted	**164,874,175**	164,800,637

Dividends

During the period ended March 31, 2018, Peyto declared and paid dividends of $0.18 per common share or $0.06 per common share per month, totaling $29.7 million (2017 - $0.33 or $0.11 per common share per month, $54.4 million).

Comprehensive income

Comprehensive income consists of earnings and other comprehensive income ("OCI"). OCI comprises the change in the fair value of the effective portion of the derivatives used as hedging items in a cash flow hedge. "Accumulated other comprehensive income" is an equity category comprised of the cumulative amounts of OCI.

Accumulated hedging gains and losses

Gains and losses from cash flow hedges are accumulated until settled. These outstanding hedging contracts are recognized in earnings on settlement. Further information on these contracts is set out in Note 10.

8. Revenue and receivables

	Three Months ended March 31,	
	2018	2017
Natural Gas Sales	**101,230**	155,499
Natural Gas Liquid sales	**53,938**	41,537
Natural gas and natural gas liquid sales	**155,168**	197,036

	March 31, 2018	December 31, 2017
Accounts receivable from customers	**51,010**	67,294
Accounts receivable from realized risk management contracts	**19,706**	10,746
Accounts receivable from joint venture partners and other	**10,262**	12,202
	80,978	90,242

A substantial portion of the Company's accounts receivable is with petroleum and natural gas marketing entities. Industry standard dictates that commodity sales are settled on the 25th day of the month following the month of production.

9. Future performance-based compensation

Peyto awards performance-based compensation to employees annually. The performance-based compensation is comprised of reserve and market value-based components.

Reserve based component
The reserves value-based component is 4% of the incremental increase in value, if any, as adjusted to reflect changes in debt, equity, dividends, general and administrative costs and interest, of proved producing reserves calculated using a constant price at December 31 of the current year and a discount rate of 8%.

Market based component
Under the market-based component, rights with a three-year vesting period are allocated to employees. The number of rights outstanding at any time is not to exceed 6% of the total number of common shares outstanding. At December 31 of each year, all vested rights are automatically cancelled and, if applicable, paid out in cash. Compensation is calculated as the number of vested rights multiplied by the total of the market appreciation (over the price at the date of grant) and associated dividends of a common share for that period.

The fair values were calculated using a Black-Scholes valuation model. The principal inputs to the option valuation model were:

	March 31, 2018	March 31, 2017
Share price	$10.80- $33.80	$27.35 - $33.80
Exercise price (net of dividends)	$14.40- 22.77	$22.77 - $33.47
Expected volatility	37.09%	27.39%
Option life	0.75 year	0.75 year
Risk-free interest rate	1.8%	0.8%

10. Financial instruments and Capital management

Financial instrument classification and measurement

Financial instruments of the Company carried on the condensed balance sheet are carried at amortized cost with the exception of cash and financial derivative instruments, specifically fixed price contracts, which are carried at fair value. There are no significant differences between the carrying amount of financial instruments and their estimated fair values as at March 31, 2018.

The Company's areas of financial risk management and risks related to financial instruments remained unchanged from December 31, 2017.

The fair value of the Company's cash and financial derivative instruments are quoted in active markets. The Company classifies the fair value of these transactions according to the following hierarchy.

- Level 1 – quoted prices in active markets for identical financial instruments.
- Level 2 – quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.
- Level 3 – valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The Company's cash and financial derivative instruments have been assessed on the fair value hierarchy described above and classified as Level 1.

Fair values of financial assets and liabilities

The Company's financial instruments include cash, accounts receivable, financial derivative instruments, due from private placement, current liabilities, provision for future performance-based compensation and long-term debt. At March 31, 2018 cash and financial derivative instruments are carried at fair value. Accounts receivable, current liabilities and provision for future performance-based compensation approximate their fair value due to their short-term nature. The carrying value of the long-term debt approximates its fair value due to the floating rate of interest charged under the credit facility.

Commodity price risk management

Peyto uses derivative instruments to reduce its exposure to fluctuations in commodity prices. Peyto considers all of these transactions to be effective economic hedges for accounting purposes.

Following is a summary of all risk management contracts in place as at March 31, 2018:

Natural Gas **Period Hedged – Monthly Index**	**Type**	**Daily Volume**	**Price** **(CAD)**
April 1, 2016 to October 31, 2018	Fixed Price	35,000 GJ	$2.10/GJ to $2.60/GJ
May 1, 2016 to October 31, 2018	Fixed Price	20,000 GJ	$2.20/GJ to $2.35/GJ
July 1, 2016 to October 31, 2018	Fixed Price	20,000 GJ	$2.28/GJ to $2.45/GJ
August 1, 2016 to October 31, 2018	Fixed Price	25,000 GJ	$2.3175/GJ to $2.5525/GJ
April 1, 2017 to October 31, 2018	Fixed Price	10,000 GJ	$2.585/GJ to $2.745/GJ
November 1, 2017 to October 31, 2018	Fixed Price	5,000 GJ	$2.92/GJ
January 1, 2018 to December 31, 2020	Fixed Price	20,000 GJ	$2.00/GJ to $2.040/GJ
April 1, 2018 to October 31, 2018	Fixed Price	105,000 GJ	$1.30/GJ to $2.565/GJ
April 1, 2018 to March 31, 2019	Fixed Price	180,000 GJ	$1.54/GJ to $2.625/GJ
April 1, 2018 to October 31, 2019	Fixed Price	5,000 GJ	$1.90/GJ
April 1, 2018 to March 31, 2020	Fixed Price	10,000 GJ	$1.43/GJ to $1.44/GJ
November 1, 2018 to March 31, 2019	Fixed Price	70,000 GJ	$1.75/GJ to $1.9525/GJ
November 1, 2018 to March 31, 2020	Fixed Price	5,000 GJ	$1.5725/GJ
April 1, 2019 to October 31, 2019	Fixed Price	15,000 GJ	$1.30/GJ
April 1, 2019 to March 31, 2020	Fixed Price	75,000 GJ	$1.45/GJ to $2.50/GJ
November 1, 2019 to March 31, 2020	Fixed Price	15,000 GJ	$2.02/GJ to $2.05/GJ
April 1, 2020 to October 31, 2020	Fixed Price	15,000 GJ	$1.30/GJ
April 1, 2020 to March 31, 2021	Fixed Price	5,000 GJ	1.64/GJ

Natural Gas Period Hedged – Daily Index	Type	Daily Volume	Price (CAD)
April 1, 2018 to October 31, 2018	Fixed Price	15,000 GJ	$1.54/GJ to $1.63/GJ
April 1, 2018 to March 31, 2019	Fixed Price	40,000 GJ	$1.40/GJ to $1.67/GJ

As at March 31, 2018, Peyto had committed to the future sale of 217,525,000, gigajoules (GJ) of natural gas at an average price of $2.03 per GJ or $2.33 per mcf. Had these contracts been closed on March 31, 2018, Peyto would have realized a gain in the amount of $129.4 million. If the AECO gas price on March 31, 2018 were to increase by $0.10/GJ, the unrealized loss would increase by approximately $21.6 million. An opposite change in commodity prices rates would result in an opposite impact on other comprehensive income.

Subsequent to March 31, 2018 Peyto entered into the following contracts:

Natural Gas Period Hedged	Type	Daily Volume	Price (CAD)
November 1, 2018 to March 31, 2019	Fixed Price	20,000 GJ	$1.91/GJ to $1.99/GJ
April 1, 2019 to October 31, 2019	Fixed Price	15,000 GJ	$1.285/ to $1.32/GJ
April 1, 2021 to October 31, 2021	Fixed Price	5,000 GJ	$1.64/GJ

Crude Oil Period Hedged	Type	Daily Volume	Price (CAD)
July 31, 2018 to December 31, 2018	Fixed Price	100 bbl	$84.03/bbl
July 1, 2018 to June 30, 2019	Fixed Price	100 bbl	$85.34/bbl

11. Related party transactions

Certain directors of Peyto are considered to have significant influence over other reporting entities that Peyto engages in commercial transactions with. Such services are provided in the normal course of business and at market rates. These directors are not involved in the day to day operational decision making of the Company. The dollar value of the transactions between Peyto and each of the related reporting entities is summarized below:

Expense		Accounts Payable	
Three Months ended March 31		As at March 31	
2018	2017	**2018**	2017
118.0	82.4	**118.0**	78.4

12. Commitments

Following is a summary of Peyto's contractual obligations and commitments as at March 31, 2018.

	2018	2019	2020	2021	2022	Thereafter
Interest payments [(1)]	18,710	23,840	21,645	16,245	16,245	36,075
Transportation commitments	27,420	30,702	19,475	18,655	26,265	245,944
Operating leases	1,682	2,242	2,242	2,242	2,317	9,269
Total	47,812	56,784	43,362	37,142	44,827	291,288

(1) Fixed interest payments on senior unsecured notes

13. Contingencies

On October 1, 2013, two shareholders (the "Plaintiffs") of Poseidon Concepts Corp. ("Poseidon") filed an application to seek leave of the Alberta Court of Queen's Bench (the "Court") to pursue a class action lawsuit against the Company, as a successor to new Open Range Energy Corp. ("New Open Range") (the “Poseidon Shareholder Application”). The proposed action contained various claims relating to alleged misrepresentations in disclosure documents of Poseidon (not New Open Range), which claims were also alleged in class action lawsuits filed in Alberta, Ontario, and Quebec earlier in 2013 against Poseidon and certain of its current and former directors and officers, and underwriters involved in the public offering of common shares of Poseidon completed in February 2012. The proposed class action sought various declarations and damages including compensatory damages which the Plaintiffs estimate at $651 million and punitive damages which the Plaintiffs estimate at $10 million, which damage amounts appear to be duplicative of damage amounts claimed in the class actions against Poseidon, certain of its current and former directors and officers, and underwriters. An application seeking leave to commence a class action lawsuit against the Company making the same allegations was also made by two Poseidon shareholders in Ontario (the “Ontario Poseidon Shareholder Action”). No steps were taken to advance these actions against the Company.

New Open Range was incorporated on September 14, 2011 solely for purposes of participating in a plan of arrangement with Poseidon (formerly named Open Range Energy Corp. ("Old Open Range")), which was completed on November 1, 2011. Pursuant to such arrangement, Poseidon completed a corporate reorganization resulting in two separate publicly-traded companies: Poseidon, which continued to carry on the energy service and supply business; and New Open Range, which carried on Poseidon's former oil and gas exploration and production business. Peyto acquired all of the issued and outstanding common shares of New Open Range on August 14, 2012. On April 9, 2013, Poseidon obtained creditor protection under the Companies' Creditor Protection Act.

On October 31, 2013, Poseidon filed a lawsuit with the Court naming the Company as a co-defendant along with the former directors and officers of Poseidon, the former directors and officers of Old Open Range and the former directors and officers of New Open Range (the “Poseidon Action”). Poseidon claimed, among other things, that the Company is vicariously liable for the alleged wrongful acts and breaches of duty of the directors, officers and employees of New Open Range. No steps were taken to advance these actions against the Company.

On September 24, 2014 Poseidon amended its claim in the Poseidon Action to add Poseidon’s auditor, KPMG LLP (“KPMG”), as a defendant.

On May 4, 2016, KPMG issued a third party claim in the Poseidon Action against Poseidon’s former officers and directors and the Company for any liability KPMG is determined to have to Poseidon. The Company was not required to defend KPMG’s third party claim.

On July 3, 2014, the Plaintiffs filed a lawsuit with the Court against KPMG, Poseidon's and Old Open Range's former auditors, making allegations substantially similar to those in the other claims (the “KPMG Poseidon Shareholder KPMG Action”).

On July 29, 2014, KPMG filed a statement of defence and a third party claim against Poseidon, the Company and the former directors and officers of Poseidon. The third party claim sought, among other things, an indemnity, or alternatively contribution, from the third party defendants with respect to any judgment awarded against KPMG LLP. The Company was not required to defend KPMG’s third party claim.

The allegations against New Open Range contained in the claims described above were based on factual matters that pre-existed the Company’s acquisition of New Open Range.

On April 6, 2018, the Company entered a global settlement with all parties involved in the Poseidon related litigation. The settlement was presented to the Alberta Court of Queens Bench on May 4, 2018 for approval as part of a plan of compromise and arrangement under the Companies’ Creditor Arrangement Act. The Alberta Court approved the settlement and Plan and issued Orders dismissing Alberta actions involving Poseidon including the Poseidon Shareholder Application and the Poseidon Action against the Company. The Ontario, Quebec and United States Courts will now be asked to recognize the Alberta Court’s Orders and to dismiss the actions before them (including the Ontario Poseidon Shareholder Action against the Company). Assuming the Alberta Court Orders are recognized, the settlement will be effective and all of the actions involving Poseidon including the Poseidon Shareholder Application, the Ontario

Poseidon Shareholder Action and the Poseidon Action against the Company will be dismissed. Although the contributions being made by the different defendants are confidential, Peyto’s contribution is immaterial and reflects its belief there was no merit to the claims.

Officers

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President and Chief Executive Officer

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Executive Vice President New Ventures & Director

Kathy Turgeon
Vice President, Finance and Chief Financial Officer

Lee Curran
Vice President, Drilling and Completions

Todd Burdick
Vice President, Production

Tim Louie
Vice President, Land

David Thomas
Vice President, Exploration

Jean-Paul Lachance
Vice President, Engineering & COO

Stephen Chetner
Corporate Secretary

Directors

Don Gray, Chairman
Stephen Chetner
Brian Davis
Michael MacBean, Lead Independent Director
Darren Gee
Gregory Fletcher
Scott Robinson

Auditors

Deloitte LLP

Solicitors

Burnet, Duckworth & Palmer LLP

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Royal Bank of Canada
Canadian Imperial Bank of Commerce
The Toronto-Dominion Bank
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