

Peyto Exploration & Development Corp.

President's Monthly Report

November 2013

From the desk of Darren Gee, President & CEO

On October 23, Peyto celebrated its 15th birthday and the completion of 15 years of successful operations in the Canadian oil and gas industry. A lot can be said about the changes that we've seen over that time, both in the industry and especially at Peyto. On that date 15 years ago, natural gas prices in Alberta were \$2.56/GJ while oil prices were \$19.79/bbl. Companies like Crestar, Renaissance and Canadian 88 were all in the news and over 60% of the capital being invested in the WCSB was for natural gas development. Peyto was just getting going. Don Gray, Peyto's founder and current chairman, was the President, CEO, Chief Engineer, and Receptionist all in one - the proverbial chief cook and bottle washer. "Buck" Braund was his co-founder and consultant landman in charge of securing that first opportunity and a chance to invest some "family and friends" money. Those were meager beginnings to be sure, and no one would have suggested that one day 15 years later Peyto would be one of the larger sized producers leading the industry. Shareholders willing to take a chance on an unproven management team could have bought stock then for \$0.075/share. What a buy that would have been! \$1000 invested back then would have bought you 13,333 shares that, including all the distribution and dividend payments, would be worth almost \$600,000 today! I think that statement alone sums up well the success that Peyto has enjoyed over those 15 years. Let's hope the next 15 are just as fruitful.

As in the past, this report includes an estimate of monthly capital spending, as well as our field estimate of production for the most recent month (see Capital Investment and Production tables below).

Capital Investment*

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

	Q1	Q2	Q3	Q4	2012	Q1	Apr	May	Jun	Q2	Jul	Aug	Sep	Q3
ONR Acq./other acq.			205	-21	184	0				0				0
Land & Seismic	3	1	2	6	12	2	3	2	1	6	1	1	1	3
Drilling	52	23	59	78	211	76	9	3	20	32	32	30	25	86
Completions	31	14	35	47	127	41	9	0	1	10	20	19	15	54
Tie ins	8	5	11	22	46	33	2	1	4	7	3	5	6	14
Facilities	4	3	6	25	37	17	6	6	6	18	7	9	9	24
Total	99	46	317	157	618	169	29	13	32	73	62	63	56	181

Production*

2012/13 Production ('000 boe/d)*

	Q3 12	Q4 12	2012	Q1 13	Q2 13	Jul	Aug	Sept	Q3 13	Oct	Nov	Dec	Q4 12
Sundance	35.7	36.0	35.4	39.7	41.6	38.1	42.1	44.5	41.5	43.7			
Kakwa	3.6	3.1	3.7	3.3	3.0	2.7	2.5	2.7	2.6	2.6			
Ansell	2.9	6.8	2.4	8.8	10.7	10.3	10.5	9.0	9.9	11.7			
Other	3.6	3.6	3.0	3.3	2.9	2.4	2.5	2.4	2.4	2.3			
Total	45.9	49.5	44.5	55.2	58.2	53.5	57.6	58.6	56.5	60.3			

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

That much better?

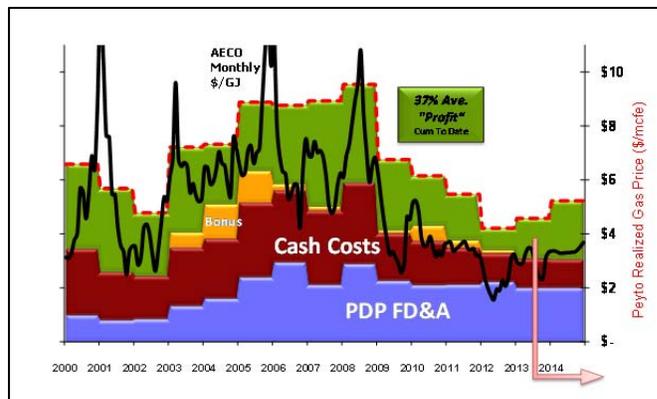
Last month I wrote about how the Marcellus shale play in the NE US was expected to single handedly eclipse that of the entire WCSB and threaten to push Canadian gas out of the US marketplace. While our Western Canadian gas is disadvantaged by location, is the Marcellus really that much better, that much more profitable that it could really do that?

So, I thought this month I would try to dig into the Marcellus a little and see just how profitable it really is. Unfortunately, I don't have access to all of the well data in the Marcellus, and relying on companies that operate there to disclose the real truth is sometimes challenging. Most are inclined to show you their best well or wells as an indication of how good it CAN be, but rarely will any of them show you ALL the wells to show how good, or not, the entire play really is.

So I thought instead, I would look at the financial performance, or the "profitability" of a few of the pure play Marcellus producers to see if I can determine the real profitability of a business in this play. Corporate reports are much more standardized and you can't selectively ignore your failures. Companies like Range Resources and Cabot Energy, for example, are as close to active, pure play Marcellus producers as you get, with over 80% of their reserves and production coming from that play.

The methodology I'll use is a simple one. The same as I would use to show Peyto's profitability over time. Basically, what does it cost them to build reserves, and produce them, relative to what their selling them for. For building costs, I'll use actual Proved Developed FD&A each year (*they don't readily report PDP reserves, so I'll have to include their Proved Developed Non Producing reserves too*). For producing costs, I'll use all of the cash costs at the field level and corporately – direct lease operating costs, transportation, gathering and processing, production and ad valorem taxes, G&A and interest expense.

Figure 1



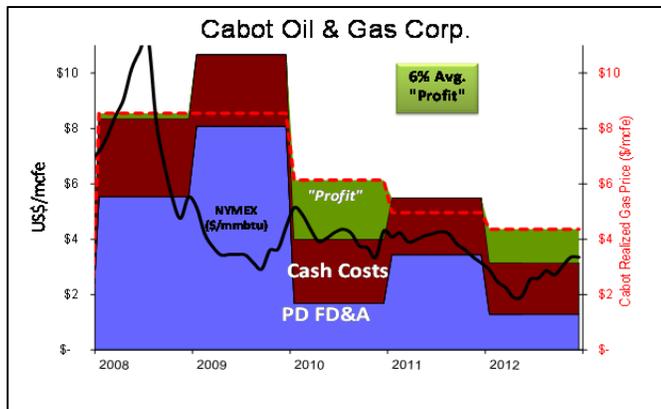
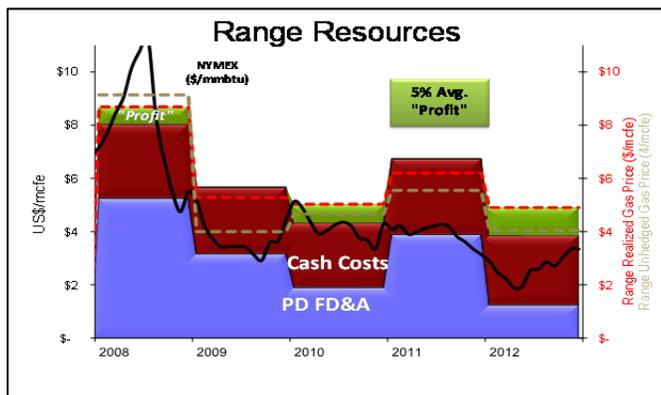
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You'll likely recall seeing a similar analysis of Peyto's profitability, shown in Figure 1, from my previous monthly reports or our corporate presentation. It shows Peyto's average "profit" over the last 14 years at 37%. More recently, or over the last 5 years, Peyto's average "profit" is 31%, even after accounting for the cost of stock based compensation.

So how do the Marcellus producers stack up? Figure 2 and 3 show both Range Resources and Cabot Oil & Gas using that same analysis.



Interestingly, neither company looks to be knocking it out of the park as far as profitability goes. Proved Developed FD&A costs have averaged \$3-\$4/mcfe over the last 5 years (which factors in land purchase costs), while cash costs have averaged \$2.30/mcfe to \$2.60/mcfe, leaving only around 5% average "profit". So it begs the question, how can the Marcellus be growing so dramatically when there is very little true profit being generated? Perhaps it's because US producers have greater access to capital via debt and equity markets that they don't have to rely on reinvestment of profits? Or perhaps their shareholders and the market rewards them for growth rather than returns, so they don't

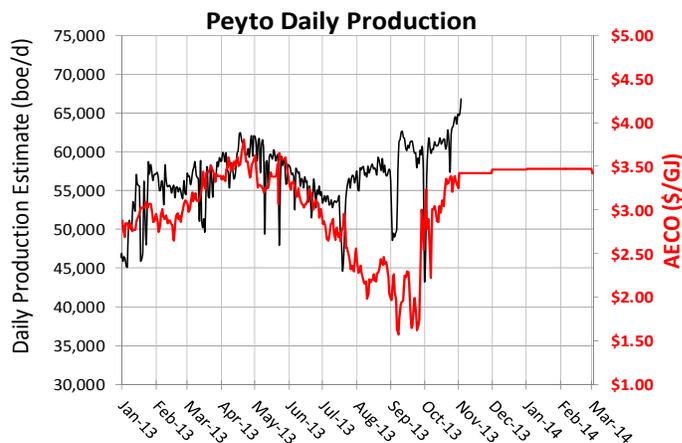
care if the capital they are investing generates a return, as long as it generates growth? Or perhaps they thought the premium price that natural gas was fetching in this part of the country would remain at a premium to justify all this cost? These are two of the lowest cost producers in the US so it's hard to argue that it's the producers themselves that are below average.

While we may never really know the answers to these questions, this comparison gives me a lot more confidence in Peyto's ability to continue to compete in the North American natural gas market.

In the early years, it's the new and exciting plays that attract the attention and capital of the industry, but ultimately, it's the profitability that determines the true longevity and sustainability of any given play (remember the Haynesville?). I think either the play or the Marcellus players still have a long ways to go to rival that of Peyto's profitability.

Activity Update and Commodity Prices

We have officially unleashed the hounds. With the startup of our three new facility projects at Swanson (30mmcf/d), Oldman North (30 mmcf/d) and Brazeau (20 mmcf/d), and the turning on of all the behind pipe production that we had waiting on those facilities, we have recently seen production ramp up. Peyto's daily production is shown below in Figure 4, which we expect will be hitting 70,000 boe/d any day as we work out the startup kinks.



At the same time, natural gas prices are much better than what we saw a month ago. AECO daily average prices of \$2/GJ in September were replaced by over \$3/GJ prices in October, while the current strip for this winter is trading closer to \$3.40/GJ. We are setting up for a strong finish to the year and a great start to 2014!