

Peyto Exploration & Development Corp.

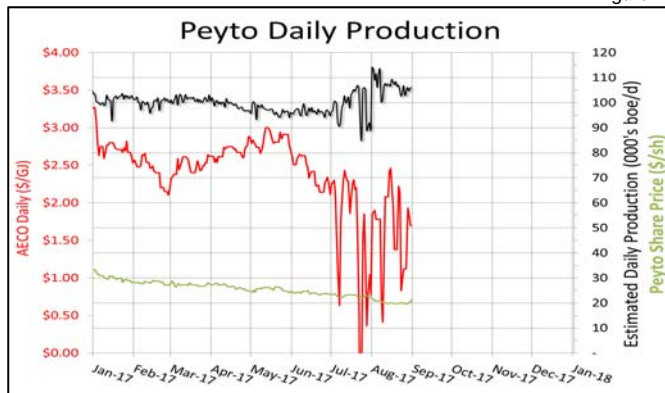
President's Monthly Report

September 2017

From the desk of Darren Gee, President & CEO

Well, I guess that's it for summer. Not a particularly good one in my opinion, punctuated by one of the most severe hurricanes to hit Texas in the last 50 years. Our thoughts are with those most severely affected. Back here in the Western Canadian gas industry we are still struggling with volatile natural gas prices caused by TCPL's Firm and IT service curtailments. It makes maintaining any sort of steady production level difficult when we are constantly turning our daily spot volumes on and off (Figure 1). Thankfully it is a very small portion of our total production. With the latest interruptions to IT delivery service in Eastern Alberta (EGAT) still front and center, we are reminded of the importance of storage reservoirs and their ability to buffer the supply-demand imbalances from summer to winter. Particularly as it relates to the price Albertans receive for their royalty volumes.

Figure 1



Source: Peyto

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) as well as any production deferrals.

Capital Investment*

2016/17 Capital Summary (millions\$ CND)*

	Q1 16	Q2 16	Q3 16	Q4 16	2016	Q1 17	Apr	May	Jun	Q2 17	Jul
Acq.	28	0	5	1	34	4	0	0	0	0	0
Land & Seismic	4	1	1	4	9	9	1	1	0	2	0
Drilling	63	30	64	63	219	67	10	13	26	48	25
Completions	33	8	27	37	105	36	4	5	12	21	15
Tie ins	12	3	13	14	42	13	2	3	4	9	7
Facilities	37	9	4	11	60	25	8	5	4	17	4
Total	176	50	114	130	469	154	25	28	45	98	51

Production*

2016/17 Production ('000 boe/d)*

	2015	Q1 16	Q2 16	Q3 16	Q4 16	2016	Q1 17	Apr	May	June	Q2 17	Jul	Aug
Sundance	59	61	54	58	59	58	59	58	55	55	56	54	57
Ansell	17	25	20	21	22	22	21	20	19	21	20	20	23
Braceau	7	12	11	14	17	14	18	18	20	18	19	21	22
Kakva	2	2	2	2	2	2	2	2	2	2	2	2	2
Other	2	2	1	1	1	1	1	2	1	1	1	1	3
Total	86	101	88	96	102	97	101	100	98	97	98	99	107

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

Things Can Only Get Better

The level of despondency that has befallen the Canadian oil and gas industry lately is unlike any I've ever experienced in my almost 30 year career. People across all facets of the industry from producing companies, to oilfield service providers, to financial supporters, to capital markets participants are all lamenting the current state of the business.

In fact, there are industry historians that are likening this current environment to the time of the National Energy Program and its ultimate effects on the health of the Western Canadian petroleum industry. What's particularly ironic, despite that it was also a time with a Canadian Prime Minister named Trudeau, is that it had the effect of:

1. Delaying development of the oilsands and other major resource development projects
2. Causing American and foreign oil companies to sell off Canadian assets
3. Hitting Alberta hard with heavy job losses.

The effect was further exacerbated by a global recession and by an oil price that dropped in half from \$30/bbl to \$15/bbl. Looking at the industry today, there is a reminiscent chill that runs down one's spine.

Notwithstanding all the "darkest before the dawn" idioms, I do believe there is hope for our industry. Such hope can be found by looking back at our Canadian history and how times like this in the past were followed by much happier and fruitful periods.

Politically, for instance, a strong provincial voice on behalf of our industry and the Western Canadian provinces, particularly Alberta, brought about the end of the NEP. There is no reason to believe that Alberta cannot again elect a political leader to be such a voice, and advocate for the Alberta people and the industries that provide our high standard of living. A leader that fights to reduce the regulations and high taxes that are driving the much needed capital and talent from our most important resource industries.

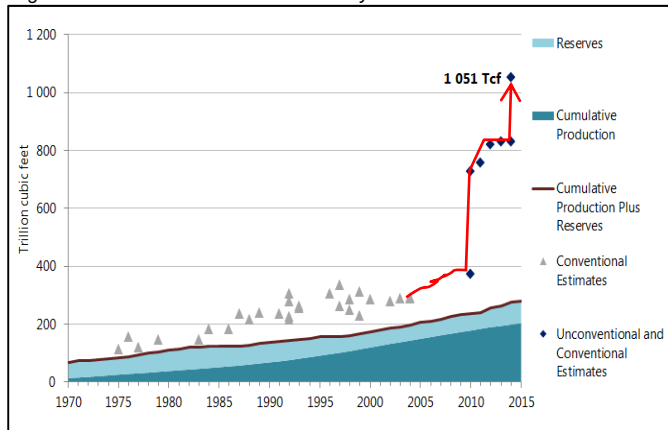
Speaking of resources, I can't recall a time in my career when we've had such an abundance of known potential in the WCSB. Looking at the history of developable natural gas reserves in Western Canada, 2016 was the largest assessment of unconventional and conventional ultimate recoverable reserves so far (Figure 2), while global consumption of natural gas is also at its highest level ever. And since we do a superior job of sustainable and environmentally responsible resource development, when fairly compared to any other jurisdiction, we should be promoting ourselves as the logical choice to provide those resources and be justifying why capital should be invested here versus elsewhere.

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Figure 2 Published Estimates for Ultimately Recoverable Natural Gas in WCSB

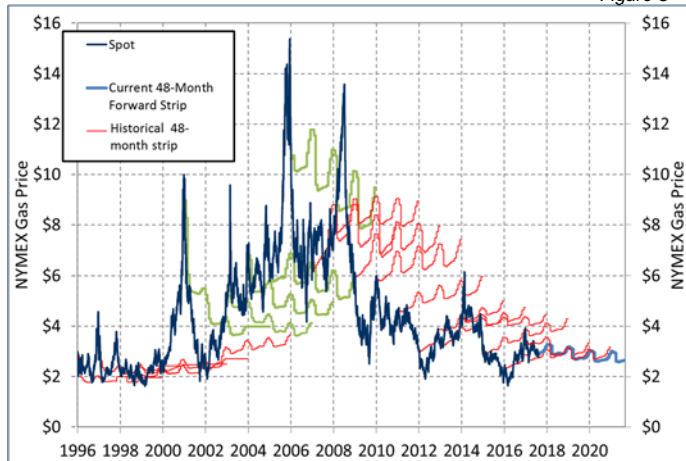


Source: NEB

Our timing might be quite fortuitous, especially when it comes to natural gas development. Looking at the current forward curve for natural gas prices both here and in the US, it's interesting that for the first time in almost a decade the future strip is in backwardation. Figure 3 below shows the NYMEX futures curve on January 1 for the last 20 years superimposed on the actual spot price history.

"Backwardation", or an inverted futures curve is when the future price of a commodity is forecast to fall, while a rising futures curve is said to be in "Contango". As you can see over the last 20 years, when the futures curve was in backwardation, spot prices actually rose. The reverse was also true. When the futures curve was in contango the spot prices fell. This is interesting because the current sentiment creating a falling future price must be that we have an unlimited amount of cheap supply that can be brought to market at an ever decreasing cost.

Figure 3



Source: RBC

The reality, however, may be that when we've had backwardated pricing in the past, companies stopped hedging and were therefore less motivated to outspend their cashflow and grow production into a falling commodity price. The result of lower spending was a shortage of new supply and the reversal of a supply driven marketplace to a demand driven marketplace. Perhaps we are at the beginning of just such a reversal.

Strong, supportive political leadership removing roadblocks and encouraging investment. An abundance of undeveloped resources primed for efficient and responsible development. An annual North American replacement requirement of almost 25 BCF/d driving a decade of rising commodity prices. It's not so far-fetched. And it's definitely a future that my fellow Albertans and I can begin to get excited about.

Activity Levels and Commodity Prices

The current spot price for Natural Gas at the Dawn Hub in Ontario is around \$3.50/GJ which I find rather astonishing. Especially when you consider that it currently costs well over half that amount to ship the gas from Alberta to that market (which Peyto doesn't actually pay, this is just for illustration with our costs). Even under the newly proposed TCPL Mainline deal, producers will be paying more than a third of the value of the commodity to get it to market (Figure 4). That seems rather ridiculous to me. Would the oil business be content to spend a third of the value of a barrel getting it to market? Over \$20/bbl in transport? I suspect we'd find another way if that were the case for oil so maybe we should be looking for one for gas.

Figure 4

	Current Structure	Proposed Structure	Sold at AECO	
	1-Sep-17	1-Sep-18	1-Sep-18	1-Sep-18
Dawn Spot Price \$/GJ	\$ 3.50	\$ 3.25		
Dawn Spot Price \$/mcf	\$ 4.03	\$ 3.74		
AECO Spot Price, \$/mcf			\$ 2.58	
Empress to Dawn toll	\$ 1.41	\$ 0.77	\$ -	
AECO to Empress toll	\$ 0.20	\$ 0.20	\$ -	
PEY plantgate to AECO toll	\$ 0.16	\$ 0.16	\$ 0.16	
NGTL/TCPL fuel @ 5.5%	\$ 0.11	\$ 0.11	\$ 0.03	
Total shipping cost \$/GJ	\$ 1.88	\$ 1.24	\$ 0.19	
Total shipping cost \$/mcf	\$ 2.16	\$ 1.43	\$ 0.22	
	54%	38%	8%	
2016 PEY (roy, opex, g&a, int), \$/mcf	\$ 0.60	\$ 0.60	\$ 0.60	
2016 PEY capital cost (PDP FD&A), \$/mcf	\$ 1.44	\$ 1.44	\$ 1.44	
What's left, \$/mcf	\$ (0.18)	\$ 0.27	\$ 0.32	

Source: Peyto, TD, TCPL