

PEYTO

Exploration & Development Corp.

3



*Interim Report
for the three and nine months ended September 30, 2016*

HIGHLIGHTS

| | Three Months ended September 30 | | | Nine Months ended September 30 | | |
|---|---------------------------------|-------------|----------|--------------------------------|-------------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Operations | | | | | | |
| Production | | | | | | |
| Natural gas (mcf/d) | 534,710 | 455,137 | 17% | 530,441 | 451,829 | 17% |
| Oil & NGLs (bbl/d) | 7,247 | 5,352 | 35% | 6,960 | 6,543 | 6% |
| Thousand cubic feet equivalent (mcf/d @ 1:6) | 578,189 | 487,250 | 19% | 572,199 | 491,084 | 17% |
| Barrels of oil equivalent (boe/d @ 6:1) | 96,365 | 81,208 | 19% | 95,367 | 81,847 | 17% |
| Production per million common shares (boe/d)* | 585 | 511 | 14% | 589 | 521 | 13% |
| Realized Product prices | | | | | | |
| Natural gas (\$/mcf) | 2.88 | 3.57 | -19% | 2.86 | 3.68 | -22% |
| Oil & NGLs (\$/bbl) | 39.76 | 41.69 | -5% | 38.54 | 40.58 | -6% |
| Operating expenses (\$/mcf) | 0.25 | 0.28 | -11% | 0.25 | 0.31 | -19% |
| Transportation (\$/mcf) | 0.16 | 0.16 | - | 0.16 | 0.15 | 7% |
| Field netback (\$/mcf) | 2.63 | 3.21 | -18% | 2.59 | 3.32 | -22% |
| General & administrative expenses (\$/mcf) | 0.04 | 0.02 | 100% | 0.04 | 0.03 | 33% |
| Interest expense (\$/mcf) | 0.19 | 0.19 | - | 0.19 | 0.20 | -5% |
| Financial (\$000, except per share*) | | | | | | |
| Revenue | 168,195 | 170,216 | -1% | 488,437 | 526,230 | -7% |
| Royalties | 6,382 | 6,489 | -2% | 18,241 | 20,356 | -10% |
| Funds from operations | 127,915 | 134,513 | -5% | 370,000 | 414,349 | -11% |
| Funds from operations per share | 0.78 | 0.85 | -8% | 2.29 | 2.64 | -13% |
| Total dividends | 54,328 | 52,456 | 4% | 160,583 | 155,693 | 3% |
| Total dividends per share | 0.33 | 0.33 | - | 0.99 | 0.99 | - |
| Payout ratio | 42 | 39 | 8% | 43 | 38 | 13% |
| Earnings | 22,814 | 37,347 | -39% | 73,859 | 94,154 | -22% |
| Earnings per diluted share | 0.14 | 0.23 | -39% | 0.46 | 0.60 | -23% |
| Capital expenditures | 113,571 | 176,618 | -36% | 339,968 | 431,338 | -21% |
| Weighted average common shares outstanding | 164,630,168 | 158,958,273 | 4% | 161,882,961 | 156,994,934 | 3% |
| As at September 30 | | | | | | |
| End of period shares outstanding | | | | 164,630,168 | 158,958,273 | 4% |
| Net debt | | | | 1,060,355 | 1,021,105 | 4% |
| Shareholders' equity | | | | 1,638,860 | 1,619,916 | 1% |
| Total assets | | | | 3,443,871 | 3,259,579 | 6% |

*all per share amounts using weighted average common shares outstanding

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| (\$000 except per share) | | | | |
| Cash flows from operating activities | 129,057 | 139,275 | 370,299 | 399,724 |
| Change in non-cash working capital | (10,256) | (9,754) | (20,647) | 4,941 |
| Change in provision for performance based compensation | 9,114 | 4,992 | 20,348 | 9,684 |
| Funds from operations | 127,915 | 134,513 | 370,000 | 414,349 |
| Funds from operations per share | 0.78 | 0.85 | 2.29 | 2.64 |

(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 third quarter of the 2016 fiscal year. An ongoing focus on cost control and prudent capital allocation resulted in a 76% operating margin ⁽¹⁾ and a 14% profit margin ⁽²⁾. Additional highlights included:

- **Production per share up 14%.** Third quarter 2016 production increased 19%, 14% per share, from 487 MMcfe/d (81,208 boe/d) in Q3 2015 to 578 MMcfe/d (96,365 boe/d) in Q3 2016. Approximately 5,700 boe/d of new production (not included in the figure above) was deliberately deferred during the quarter due to low commodity prices.
- **Cash costs of \$0.76/Mcfe (\$0.64/Mcfe or \$3.82/boe excluding royalties).** Total cash costs, including \$0.12/Mcfe royalties, \$0.25/Mcfe operating costs, \$0.16/Mcfe transportation, \$0.04/Mcfe G&A and \$0.19/Mcfe interest expense, were down from \$0.80/Mcfe in Q3 2015 despite the deferral of 5,700 boe/d of production. The 5% reduction in cash costs did not fully offset the 17% lower realized commodity prices, and resulted in a cash netback of \$2.40/Mcfe (\$14.43/boe) or a 76% operating margin.
- **Funds from operations per share of \$0.78.** Generated \$128 million in Funds from Operations ("FFO") in Q3 2016 down 5% (8% per share) from \$135 million in Q3 2015 due to the 17% reduction in realized commodity prices, which was mostly offset by the 19% increase in production volumes.
- **Capital investment of \$114 million.** A total of 38 horizontal wells and 2 vertical wells were drilled in the third quarter. New wells brought on production over the last 12 months were producing 46,000 boe/d at the end of the quarter, which, when combined with a trailing twelve month capital investment of \$502 million, equates to an annualized capital efficiency of \$10,900/boe/d.
- **Earnings of \$0.14/share, dividends of \$0.33/share.** Earnings of \$23 million were generated in the quarter while dividends of \$54 million were paid to shareholders, representing a before tax payout ratio of 42% of FFO. This quarter represents Peyto's 47th consecutive quarter of earnings, totaling over \$2.1 billion in cumulative earnings.

Third Quarter 2016 in Review

Peyto is proud to have achieved two historical milestones during the third quarter. Total Company capital investments have now surpassed \$5 billion, while total dividends and distributions to investors, paid out of cumulative earnings, have exceeded \$2 billion. This historical ratio of profit to investment is unique in the Canadian energy industry and is a direct result of Peyto's strategy to focus on generating returns rather than merely focusing on growth. This focus on returns continued throughout the third quarter as the Company invested \$114 million developing low risk, sweet natural gas resources plays in its traditional Deep Basin areas. Wet weather hampered field operations in July and August requiring a 9th drilling rig to be added in mid-September to catch up to drilling plans for the year. Natural gas price recovery throughout the quarter allowed for the shut-in wells, which were accumulated in previous quarters, to be brought on production. Production climbed from a low of 85,500 boe/d in May to over 100,000 boe/d in September with an average of 5,700 boe/d still offline in the third quarter. Even in a challenging commodity price environment, the financial and operating performance resulted in an annualized 6% Return on Equity (ROE) and 5% Return on Capital Employed (ROCE).

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

Spirit River formations again dominated the drilling targets for the third quarter with Wilrich, Falher and Notikewin formations accounting for 90% of the wells drilled. Peyto drilled its second faulted, vertical, Cardium well in the Brazeau area in the quarter, following up an initial successful well earlier in the year, along with its first vertical Belly River well. The Brazeau area accounted for approximately one quarter of all activity with development taking place across multiple formations.

In total, 40 gross wells were drilled across the land base as shown in the following table:

| Zone | Field | | | | | | | Total Wells Drilled |
|--------------|-----------|----------|----------|----------|---------|-----------------|----------|---------------------|
| | Sundance | Nosehill | Wildhay | Ansell | Berland | Kisku/ Kakwa | Brazeau | |
| Belly River | | | | | | | 1 | 1 |
| Cardium | | | | | | | 1 | 1 |
| Notikewin | | | | 4 | | | 4 | 8 |
| Falher | 11 | | | 2 | | | | 13 |
| Wilrich | 7 | 1 | 1 | 3 | | | 3 | 15 |
| Bluesky | 1 | 1 | | | | | | 2 |
| Total | 19 | 2 | 1 | 9 | | | 9 | 40 |

Third quarter drilling continued to take advantage of lower industry activity levels, lower costs and improved execution as the average horizontal well cost \$1.8 MM for the second quarter in a row. Average completion costs increased 12% due to less pad completions conducted in the quarter. The following table illustrates the trend in drilling and completion costs since Peyto began drilling with horizontal wells in 2010:

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 Q1 | 2016 Q2 | 2016 Q3 |
|-------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|----------------|
| Gross Hz Spuds | 52 | 70 | 86 | 99 | 123 | 140 | 36 | 19 | 38 |
| Measured Depth (m) | 3,762 | 3,903 | 4,017 | 4,179 | 4,251 | 4,309 | 4,231 | 4,269 | 4,238 |
| Hz Length (m) | 1,335 | 1,303 | 1,358 | 1,409 | 1,460 | 1,531 | 1,460 | 1,444 | 1,420 |
| Drilling (\$MM/well) | \$2.763 | \$2.823 | \$2.789 | \$2.720 | \$2.660 | \$2.159 | \$1.916 | \$1.790 | 1,807 |
| \$ per meter | \$734 | \$723 | \$694 | \$651 | \$626 | \$501 | \$453 | \$419 | \$426 |
| Completion (\$MM/well) | \$1.358 | \$1.676 | \$1.672 | \$1.625 | \$1.702 | \$1.212 | \$0.910 | \$0.669 | \$0.750 |
| \$ per meter | \$361 | \$429 | \$416 | \$389 | \$400 | \$281 | \$215 | \$157 | \$175 |

Capital Expenditures

Capital investments in the third quarter of 2016 totalled \$113.6 million, comprised of \$64.1 million for drilling, \$26.9 million for completions, \$13.2 million for wellsite equipment and well connections, \$3.8 million for major pipelines and facilities, and \$5.4 million for new seismic data and undeveloped land.

In total, 40 wells (92% Working Interest) were spud in the quarter, 38 horizontal wells and 2 vertical wells, and 37 wells (95% WI) were completed. Despite challenging ground conditions, Peyto was able to install wellsite equipment and pipelines to connect 41 wells (93% WI) and place them on production. Facility and pipeline investments of \$3.8 million included the construction of two water source facilities at Brazeau. Finally, a total of 13 undeveloped sections (96% WI) of land were added in the quarter, acquired from other operators for \$4.8 million or an average of \$596/acre. These lands have an internal estimate of over 40 development locations that will be added to Peyto's existing inventory of Deep Basin locations.

Commodity Prices

US (Henry Hub) natural gas prices continued to climb throughout the quarter finishing above \$3USD/MMBTU. Alberta (AECO) natural gas prices effectively did the same, except for a two week period in the middle of the quarter when prices collapsed due to an interruption in TCPL's mainline service at East Gate. By the end of the quarter however, AECO prices were approaching a high for 2016 at \$2.75CAD/GJ.

The average third quarter 2016 AECO daily natural gas price was \$2.20/GJ up 66% from the previous quarter but down 20% from the same period in 2015, while the average AECO monthly price was \$2.09/GJ, up 75% from the previous

quarter but down 22% from the prior year. As Peyto had committed 87% of its production to the monthly price, Peyto realized a volume weighted average natural gas price of \$2.08/GJ or \$2.39/Mcf, after the TCPL fuel charge and prior to a \$0.49/Mcf hedging gain.

As a result of the Company's hedging strategy, approximately 81% of Peyto's natural gas production received a fixed price of \$2.59/GJ, or \$2.99/Mcf, when including hedges that were put in place over the previous 24 months, while the balance received the blended daily and monthly price of \$2.08/GJ, resulting in an after-hedge price of \$2.50/GJ or \$2.88/Mcf.

Greater competition for fractionation and transportation of natural gas liquids has resulted in realized propane prices improving to the point where extracting propane from the gas stream and condensing it into liquid form is once again profitable. As a result, during the quarter Peyto began adjusting the operating conditions of the refrigeration process at its owned and operated processing facilities in order to recover more liquid propane and butane. The result was a 16% increase in total liquids yield as well a change in the blended realized liquids prices. Peyto realized an oil and natural gas liquids price of \$39.76/bbl in Q3 2016 for its blend of condensate, pentane, butane and propane, which represented 73% of the \$54.82/bbl average Canadian Light Sweet posted price, down from 76% in Q2 2016 and Q3 2015, as shown in the following table.

Commodity Prices by Component

| | Three Months ended | Sept 30 | Jun 30 | Sept 30 |
|--|--------------------|---------|--------|---------|
| | | 2016 | 2016 | 2015 |
| Natural gas – after hedging (\$/mcf) | | 2.88 | 2.60 | 3.50 |
| Natural gas – after hedging (\$/GJ) | | 2.50 | 2.26 | 3.06 |
| AECO monthly (\$/GJ) | | 2.09 | 1.18 | 2.66 |
| Oil and natural gas liquids (\$/bbl) | | | | |
| Condensate (\$/bbl) | | 47.95 | 47.83 | 49.49 |
| Propane (\$/bbl) | | 6.51 | 0.40 | (8.02) |
| Butane (\$/bbl) | | 20.25 | 19.52 | 19.24 |
| Pentane (\$/bbl) | | 49.15 | 50.67 | 50.70 |
| Total Oil and natural gas liquids (\$/bbl) | | 39.76 | 41.46 | 41.69 |
| Canadian Light Sweet postings (\$/bbl) | | 54.82 | 54.70 | 54.70 |

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

Financial Results

Peyto's realized natural gas price combined with realized liquids prices, resulted in unhedged revenues for the third quarter of \$2.71/Mcfe (\$3.16/Mcfe including hedging gains). Royalties of \$0.12/Mcfe, operating costs of \$0.25/Mcfe, transportation costs of \$0.16/Mcfe, G&A of \$0.04/Mcfe and interest expense of \$0.19/Mcfe, all combined for total cash costs of \$0.76/Mcfe (\$4.54/boe). When Q3 2016 total cash costs of \$0.76/Mcfe were deducted from realized revenues, it resulted in a cash netback of \$2.40/Mcfe or a 76% operating margin.

Depletion, depreciation and amortization charges of \$1.54/Mcfe, along with a provision for deferred tax and market based bonus payments reduced the cash netback to earnings of \$0.43/Mcfe, or a 14% profit margin. Dividends of \$1.02/Mcfe were paid to shareholders.

On October 24, 2016, Peyto closed an issuance of CAD \$100 million of senior unsecured notes. The notes were issued by way of a private placement and rank equally with Peyto's obligations under its bank facility and existing note purchase agreements. The notes have a coupon rate of 3.7% and mature in October 24, 2023. Peyto now has CAD \$520 million of outstanding senior unsecured notes, representing approximately 50% of the Company's net debt, at coupon rates ranging from 3.7% to 4.88%.

Natural Gas Marketing

As a result of increased Alberta natural gas price volatility, caused in part by continued transportation constraints on the NGTL/TCPL systems in the form of both periodic curtailments of take-away capacity and dramatic price impact through mainline capacity interruptions, Peyto's Board of Directors has approved an increase to the hedging limit for future natural gas sales from 65% to 85% for the forecasted winter 2016/17 and Summer 2017. As a result, Peyto has been and will be increasing the frequency of future sales to achieve this new target.

The following table summarizes the remaining hedged volumes and prices for the upcoming years as of November 9, 2016.

| | Future Sales | | Average Price (CAD) | |
|-------|--------------|-------------|---------------------|--------|
| | GJ | Mcf | \$/GJ | \$/Mcf |
| 2016 | 31,200,000 | 27,130,435 | 2.62 | 3.02 |
| 2017 | 167,685,000 | 145,813,043 | 2.58 | 2.96 |
| 2018 | 58,820,000 | 51,147,826 | 2.50 | 2.87 |
| Total | 258,164,411 | 224,091,304 | 2.56 | 2.95 |

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

Activity Update

Peyto is continuing its aggressive 2016 development program with 9 drilling rigs and 5 completion spreads active across its core areas. Four rigs are drilling in the heart of Sundance while 2 rigs are drilling on the east side of Sundance in the Edson and Ansell areas. The remaining 3 rigs are drilling in the Brazeau area.

So far, 18 wells (93% WI) have been drilled in the fourth quarter with another 16 wells (92% WI) expected to be drilled by the end of the year. Fifteen wells (90% WI) have been completed and 10 wells (87% WI) have been brought on production. Pad drilling has resulted in a backlog of completions (15 wells on 8 pads) which will to be resolved by December with the expectation that essentially all Q4 drills will be completed and on production by year end.

Production is currently fluctuating between 100,000 and 105,000 boe/d level with approximately 3,000 boe/d of additional volume behind pipe. Ongoing firm service curtailments on the NGTL system and anomalously high NGTL pipeline pressures are negatively affecting Peyto's ability to take full advantage of its production capability. Peyto expects production to grow to the 110,000-115,000 boe/d level by year end with the completions that lie ahead and with reliable take away performance on the NGTL system.

Propane prices continue to recover with further price improvements occurring in mid-October giving rise to additional enhancements to plant propane recovery levels including the resumption of the Oldman deep cut plant operation. Total company liquids recovery has been increased from a Q3 average of 13.6 bbl/MMcf sales gas to a present level above 16.0 bbl/MMcf.

The original 2016 budget announced last November projected the drilling of 130 to 145 wells (95% WI) for approximately \$600 to \$650 million. Peyto is currently on track to drill 131 wells (95% WI) for total capital investment of approximately \$475 million, approximately 20% less than originally planned.

2017 Budget

The Board of Directors of Peyto has approved a preliminary 2017 budget which includes a capital program expected to range between \$550 and \$600 million. The capital program involves drilling between 145 and 160 wells (average of 94% working interest), along with associated pipeline and facility investments to accommodate the growing production base. The 9 drilling rigs currently contracted are deemed sufficient for this level of activity and are expected to be split with 5 rigs in the Greater Sundance area and 4 rigs drilling in Brazeau.

The 2017 drilling locations will be selected from Peyto's large, internal inventory of profitable drilling locations and, based on the current strip price for natural gas and liquids, are all forecast to achieve the Company's strict rate of return hurdle. These locations are expected to add between 47,500 and 52,500 boe/d of new working interest production, for a cost of approximately \$11,500/boe/d, based on anticipated service costs and activity levels. A portion of the new production will offset an internal forecast of 36% base decline, while a portion will grow overall 2017 production from an expected 2016 exit level of 112,000 boe/d to exit between 120,000 boe/d and 125,000 boe/d.

The 2017 plan includes approximately \$100 million in major gas plant and pipeline investments that will increase Peyto's capacity in owned and operated infrastructure to over 950 mmcf/d. This includes a \$60 million investment in a new, sweet gas plant at Brazeau East. This plant will be constructed in two phases; the first phase will include the installation of a refrigeration train and 6 compressors capable of 70 mmcf/d, while the second phase will include a second refrigeration process and 4 additional compressors. There will be the option to add additional compression in the future as required. Phase 1 of the Brazeau East gas plant is expected to be installed during the first quarter and operational by June 2017. Phase 2 is planned for later in the year as drilling plans progress.

In the Greater Sundance area Peyto has plans to install a liquids pipeline system in Q1 2017 for \$15 million. This dual pipeline system will link the Oldman, Oldman North, Nosehill and Swanson gas plants for collection and transportation of both condensate and LPG production. The proposed pipeline will effectively eliminate expensive trucking costs while achieving a reduction in greenhouse gas emissions associated with trucking these products to sales. Liquids product pricing is also expected to be enhanced as a result of this pipeline system.

The future strip for Alberta natural gas prices is currently forecast to average approximately \$2.55/GJ in 2017, along with Canadian Light Sweet oil prices of approximately \$65/bbl. In accordance with Peyto's historical hedging practice, the Company has already forward sold approximately 63% of 2017 forecast gas production at an average price of \$2.58/GJ. These prices, when adjusted for Peyto's historic NGL and heat content premiums of approximately 130% and combined with the Company's industry leading cash costs of approximately \$0.75/Mcfe (\$4.50/boe), should yield cash netbacks of approximately \$16/boe, and give Peyto the ability to fund its dividend and the majority of the capital program from internally generated FFO. For the remainder of the funding requirements for the capital program, Peyto has available capacity within its bank lines and working capital, while continuing to maintain a strong balance sheet.

Outlook

Peyto remains committed to its strategy as a leading natural gas explorer and producer especially as demand for natural gas in North America continues to grow each year. With a strict focus on maximizing returns, the Company is encouraged that it has more opportunities for profitable investment today than ever before. While the competition for traditional gas markets has increased, Peyto remains confident it can compete as one of a select few operators that can demonstrate real and consistent profitability at current market prices. In many ways, the challenges of today are no different than those that have been successfully navigated in the past with a consistent focus on execution, risk management and cost control.

(signed) "*Darren Gee*"

Darren Gee
President and CEO
November 9, 2016

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, 2015 and 2014. The financial statements have been prepared in accordance with the International Accounting Standards Board ("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 November 8, 2016. 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.

Certain information set forth in this MD&A, including management's assessment of Peyto's future plans and operations, contains forward-looking statements. By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond these parties' control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other industry participants, the lack of availability of qualified personnel or management, stock market volatility and ability to access sufficient capital from internal and external sources. 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 that Peyto will derive there from.

All references are to Canadian dollars unless otherwise indicated. Natural gas liquids and oil volumes are recorded in barrels of oil (bbl) and are converted to a thousand cubic feet equivalent (mcf) 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).

OVERVIEW

Peyto is a Canadian energy company involved in the development and production of natural gas in Alberta's deep basin. As at December 31, 2015, the Company's total Proved plus Probable reserves were 3.5 trillion cubic feet equivalent (590 million barrels of oil equivalent) as evaluated by its independent petroleum engineers. Production is weighted approximately 93% to natural gas and 7% to natural gas liquids and oil.

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 to shareholders paid 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 eighteen years indicate that these strategies have been successfully implemented. This business model makes Peyto a truly unique energy company.

QUARTERLY FINANCIAL INFORMATION

| (\$000 except per share amounts) | 2016 | | | | 2015 | | | 2014 |
|----------------------------------|----------------|---------|---------|---------|---------|---------|---------|---------|
| | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 | Q4 |
| Total revenue (net of royalties) | 161,813 | 136,017 | 172,366 | 184,943 | 163,727 | 166,327 | 175,820 | 205,125 |
| Funds from operations | 127,915 | 102,178 | 139,907 | 151,123 | 134,513 | 135,195 | 144,643 | 173,437 |
| Per share – basic and diluted | 0.78 | 0.63 | 0.88 | 0.95 | 0.85 | 0.86 | 0.94 | 1.13 |
| Earnings | 22,814 | 9,102 | 41,943 | 43,406 | 37,347 | 12,295 | 44,513 | 68,597 |
| Per share – basic and diluted | 0.14 | 0.06 | 0.26 | 0.27 | 0.23 | 0.08 | 0.29 | 0.45 |
| Dividends | 54,328 | 53,735 | 52,520 | 52,456 | 52,456 | 52,456 | 50,781 | 49,181 |
| Per share – basic and diluted | 0.33 | 0.33 | 0.33 | 0.33 | 0.33 | 0.33 | 0.33 | 0.32 |

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 September 30 | | Nine Months ended September 30 | |
|--|---------------------------------|--------|--------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Natural gas (mmcf/d) | 534.7 | 455.1 | 530.4 | 451.8 |
| Oil & natural gas liquids (bbl/d) | 7,247 | 5,352 | 6,960 | 6,543 |
| Barrels of oil equivalent (boe/d) | 96,365 | 81,208 | 95,367 | 81,847 |
| Thousand cubic feet equivalent (mmcfe/d) | 578.2 | 487.3 | 572.2 | 491.1 |

Natural gas production averaged 534.7 mmcf/d in the third quarter of 2016, 17 percent higher than the 455.1 mmcf/d reported for the same period in 2015. Oil and natural gas liquids production averaged 7,247 bbl/d, an increase of 35 percent from 5,352 bbl/d reported in the prior year. Third quarter production increased 19 percent from 487.3 mmcfe/d to 578.2 mmcfe/d. The production increases are attributable to Peyto’s capital program and resulting production additions as well as changes to the plant processing to recover more propane and butane from the gas stream.

Summer Production Strategy

The decline of Alberta natural gas (AECO) prices at the beginning of 2016 prompted Peyto to defer production from newly drilled wells, commencing in April and extending over the second quarter. This production deferral strategy was paired with an increase in hedging to a target volume level of 85% for the winter of 2016. Over the second quarter of 2016, Peyto left approximately 17,400 boe/d of production shut in from newly drilled wells. During the third quarter, these newly drilled deferred wells were gradually placed on production as gas prices recovered from the low summer levels. Peyto no longer has any wells shut in for the purpose of deferring production. This strategy has been very successful shifting new well flush production from a period when gas would have sold at less than \$1.30/GJ to the current price environment of greater than \$2.50/GJ.

Oil & Natural Gas Liquids Production by Component

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--|---------------------------------|-------|--------------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Condensate (bbl/d) | 2,944 | 2,398 | 3,227 | 2,732 |
| Propane (bbl/d) | 735 | 289 | 447 | 896 |
| Butane (bbl/d) | 1,337 | 950 | 1,282 | 1,243 |
| Pentane (bbl/d) | 2,096 | 1,561 | 1,850 | 1,507 |
| Other NGL's (bbl/d) | 135 | 154 | 154 | 165 |
| Oil & natural gas liquids (bbl/d) | 7,247 | 5,352 | 6,960 | 6,543 |
| Million cubic feet equivalent (mmcf/d) | 43.5 | 32.1 | 41.8 | 39.3 |

The recovery of propane in liquid form was re-instituted in June in response to increased propane prices. Peyto had previously been operating plants in propane rejection mode to achieve superior value by selling propane in the sales gas stream. Liquid values recovered sufficiently to justify recovering liquid propane. The return to propane recovery operations and ongoing optimization of liquid recovery is expected to drive further improvements for the fourth quarter. The company's ownership and control of its facilities allow it to respond very quickly to market price conditions and achieve optimal value for its produced products.

Commodity Prices

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--------------------------------------|---------------------------------|-------|--------------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Oil and natural gas liquids (\$/bbl) | 39.76 | 41.69 | 38.24 | 40.58 |
| Natural gas (\$/mcf) | 2.39 | 3.02 | 2.02 | 3.01 |
| Hedging – gas (\$/mcf) | 0.49 | 0.55 | 0.84 | 0.67 |
| Natural gas – after hedging (\$/mcf) | 2.88 | 3.57 | 2.86 | 3.68 |
| Total Hedging (\$/mcf) | 0.45 | 0.52 | 0.77 | 0.62 |
| Total Hedging (\$/boe) | 2.70 | 3.11 | 4.65 | 3.69 |

Peyto's natural gas price, before hedging, averaged \$2.39/mcf during the third quarter of 2016, a decrease of 21 percent from \$3.02/mcf reported for the equivalent period in 2015. Oil and natural gas liquids prices averaged \$39.76/bbl, a decrease of 5 percent from \$41.69/bbl a year earlier.

Commodity Prices by Component

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--|---------------------------------|--------|--------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Natural gas – after hedging (\$/mcf) | 2.88 | 3.50 | 2.86 | 3.73 |
| Natural gas – after hedging (\$/GJ) | 2.50 | 3.06 | 2.49 | 3.25 |
| AECO monthly (\$/GJ) | 2.09 | 2.66 | 1.76 | 2.66 |
| Oil and natural gas liquids (\$/bbl) | | | | |
| Condensate (\$/bbl) | 47.95 | 49.49 | 44.19 | 55.14 |
| Propane (\$/bbl) | 6.51 | (8.22) | 2.30 | (1.64) |
| Butane (\$/bbl) | 20.25 | 19.24 | 18.81 | 23.92 |
| Pentane (\$/bbl) | 49.15 | 50.70 | 47.22 | 54.09 |
| Total Oil and natural gas liquids (\$/bbl) | 39.76 | 41.69 | 38.24 | 40.58 |
| Canadian Light Sweet postings (\$/bbl) | 54.82 | 54.70 | 50.15 | 58.64 |

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

Revenue

| (\$000) | Three Months ended September 30 | | Nine Months ended September 30 | |
|-----------------------------|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Natural gas | 117,794 | 126,467 | 294,033 | 371,287 |
| Oil and natural gas liquids | 26,507 | 20,526 | 72,914 | 72,487 |
| Hedging gain (loss) | 23,894 | 23,223 | 121,490 | 82,456 |
| Total revenue | 168,195 | 170,216 | 488,437 | 526,230 |

For the three months ended September 30, 2016, revenue decreased 1 percent to \$168.2 million from \$170.2 million for the same period in 2015. The decrease in revenue for the period was a result of decreased realized commodity prices offset by an increase in production volumes, as detailed in the following table:

| | Three Months ended September 30 | | | Nine Months ended September 30 | | |
|-----------------------------------|---------------------------------|---------|-----------|--------------------------------|---------|-----------|
| | 2016 | 2015 | \$million | 2016 | 2015 | \$million |
| Total Revenue, September 30, 2015 | | | 170.2 | | | 526.2 |
| Revenue change due to: | | | | | | |
| Natural gas | | | | | | |
| Volume (mmcf) | 49,193 | 41,873 | 26.1 | 145,341 | 123,349 | 80.9 |
| Price (\$/mcf) | \$2.88 | \$3.57 | (34.0) | \$2.86 | \$3.68 | (119.2) |
| Oil & NGL | | | | | | |
| Volume (mdbl) | 667 | 492 | 7.2 | 1,907 | 1,786 | 4.9 |
| Price (\$/bbl) | \$39.76 | \$41.69 | (1.3) | \$38.24 | \$40.58 | (4.4) |
| Total Revenue, September 30, 2016 | | | 168.2 | | | 488.4 |

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.

| (\$000 except per share amounts) | Three Months ended September 30 | | Nine Months ended September 30 | |
|----------------------------------|---------------------------------|-------|--------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Royalties | 6,382 | 6,489 | 18,241 | 20,356 |
| % of sales before hedging | 4.4 | 4.4 | 5.0 | 4.6 |
| % of sales after hedging | 3.8 | 3.8 | 3.7 | 3.9 |
| \$/mcf | 0.12 | 0.15 | 0.12 | 0.15 |
| \$/boe | 0.72 | 0.87 | 0.70 | 0.91 |

For the third quarter of 2016, royalties averaged \$0.12/mcfe or approximately 4.4% of Peyto's total petroleum and natural gas sales excluding hedges.

Substantially all of Peyto's production is in the Province of Alberta. Under the Alberta Royalty Framework ("ARF") the Crown royalty rate varies with production rates and commodity prices. The royalty rate expressed as a percentage of sales revenue will fluctuate from period to period as 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.

In addition to the basic underlying royalty structure (the ARF), Alberta has instituted additional features that impact the royalty paid on gas and gas liquids for new wells drilled subsequent to January 1, 2009. These additional features include:

1. A one year flat 5% royalty period (18 months for horizontal wells) for each new well but capped at a cumulative production level of 500 MMcf for each new well, and
2. A Natural Gas Deep Drilling Holiday program that provides a royalty holiday value for new wells based on meterage drilled. This holiday feature further reduces the royalty for new wells to a minimum of 5% for a maximum 5 year period from on-stream date. This benefit sequentially follows the benefit under point (1) above.

Alberta's Modernized Royalty Framework

On January 9, 2016 the Alberta Government released a report of its Royalty Review and Advisory Panel. The report sets forth a new Modernized Royalty Framework (MRF) that is scheduled to commence for wells drilled starting January 1, 2017. In general, the MRF looks to reward those companies who continuously innovate, strive to reduce their costs and environmental footprints. Peyto is already an industry leader in this regard. Peyto does not expect that the latest royalty framework will pose any significant additional burden to the Company's well investment economics over a reasonable commodity price range expected in the foreseeable future.

In its 18 year history, Peyto has invested over \$5.1 billion in capital projects, found and developed 4.6 TCFe of gas reserves, and paid over \$779 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 September 30 | | Nine Months ended September 30 | |
|-------------------------|---------------------------------|--------|--------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Operating costs (\$000) | 13,254 | 12,665 | 38,526 | 40,672 |
| \$/mcf | 0.25 | 0.28 | 0.25 | 0.31 |
| \$/boe | 1.49 | 1.70 | 1.47 | 1.82 |
| Transportation (\$000) | 8,647 | 7,085 | 25,506 | 20,302 |
| \$/mcf | 0.16 | 0.16 | 0.16 | 0.15 |
| \$/boe | 0.98 | 0.95 | 0.98 | 0.91 |

Operating expenses increased by 5% for the third quarter of 2016 as compared to the same quarter of 2015 due to an increase in production volumes. On a unit-of-production basis, operating costs decreased 11% averaging \$0.25/mcf in the third quarter of 2016 compared to \$0.28/mcf for the equivalent period in 2015. These continued strong results were achieved despite increases in municipal taxes and the Alberta Energy Regulator fee levy. Peyto focuses on being the industry leader in operating costs and strives to achieve incremental cost reductions on a continuous basis.

Transportation expenses were unchanged at 0.16/mcf.

General and Administrative Expenses

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|----------------------|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| G&A expenses (\$000) | 4,053 | 3,862 | 12,154 | 12,323 |
| Overhead recoveries | (1,920) | (3,040) | (5,311) | (7,992) |
| Net G&A expenses | 2,133 | 822 | 6,843 | 4,331 |
| \$/mcf | 0.04 | 0.02 | 0.04 | 0.03 |
| \$/boe | 0.24 | 0.11 | 0.26 | 0.19 |

For the third quarter, general and administrative expenses before overhead recoveries was \$4.1 million compared to \$3.9 million for the same quarter of 2015. Capital overhead recoveries declined as a result of reduced drilling and completion costs on a per well basis. General and administrative expenses averaged \$0.08/mcf before overhead recoveries of \$0.04/mcf for net general and administrative expenses of \$0.04/mcf in the third quarter of 2016 \$0.09/mcf before overhead recoveries of \$0.07/mcf for net general and administrative expenses of \$0.02/mcf in the third quarter of 2015.

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 \$2.8 million was recorded for the quarter ended September 30, 2016. The cumulative provision totals \$6.3 million.

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 September 30, 2016, compensation costs related to 4.8 million non-vested rights (3.0% of the total number of common shares outstanding), with an average grant price of \$25.84, are \$11.1 million for the third quarter of 2016. 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 7 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 \$26.8 million.

Rights Outstanding Under Market Based Compensation Plan

| Vesting Date | Valued but Not Vested | | To be Valued December 31, 2016 | |
|---------------------|------------------------------|-------------------|---------------------------------------|---------------------------------|
| | Number of Rights | Value (\$) | Number of Rights | Average Grant Price (\$) |
| December 31, 2016 | 1,003,718 | 3,104,296* | 1,261,833 | 24.09 |
| | - | - | | |
| December 31, 2017 | - | - | 1,261,833 | 24.09 |
| December 31, 2018 | - | - | 1,261,833 | 24.09 |

*Valued on December 31, 2014 at \$34.34

Interest Expense

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--------------------------|---------------------------------|-------|--------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Interest expense (\$000) | 9,864 | 8,642 | 29,320 | 26,221 |
| \$/mcf | 0.19 | 0.19 | 0.19 | 0.20 |
| \$/boe | 1.11 | 1.16 | 1.12 | 1.17 |
| Average interest rate | 3.7% | 3.6% | 3.6% | 3.6% |

Third quarter 2016 interest expense was \$9.9 million (\$0.19/mcfe) compared to \$8.6 million (\$0.19/mcfe) for the third quarter 2015.

Netbacks

| (\$/mcf) | Three Months ended September 30 | | Nine Months ended September 30 | |
|----------------------------|---------------------------------|-------|--------------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Gross Sale Price | 2.71 | 3.28 | 2.35 | 3.31 |
| Hedging gain | 0.45 | 0.52 | 0.77 | 0.62 |
| Net Sale Price | 3.16 | 3.80 | 3.12 | 3.93 |
| Less: Royalties | 0.12 | 0.15 | 0.12 | 0.15 |
| Operating costs | 0.25 | 0.28 | 0.25 | 0.31 |
| Transportation | 0.16 | 0.16 | 0.16 | 0.15 |
| Field netback | 2.63 | 3.21 | 2.59 | 3.32 |
| General and administrative | 0.04 | 0.02 | 0.04 | 0.03 |
| Interest on long-term debt | 0.19 | 0.19 | 0.19 | 0.20 |
| Cash netback (\$/mcf) | 2.40 | 3.00 | 2.36 | 3.09 |
| Cash netback (\$/boe) | 14.43 | 18.00 | 14.16 | 18.54 |

Netbacks are a non-IFRS 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 2016 third quarter provision for depletion, depreciation and amortization totaled \$82.2 million as compared to \$76.6 million in 2015. On a unit-of-production basis, depletion and depreciation costs averaged \$1.54/mcfe as compared to \$1.71/mcfe in 2015.

Income Taxes

The current provision for deferred income tax expense is \$8.4 million compared to \$14.4 million in 2015. Resource pools are generated from the capital program, which are available to offset current and deferred income tax liabilities.

| Income Tax Pool type (\$ millions) | September 30, 2016 | December 31, 2015 | Annual deductibility |
|---------------------------------------|-----------------------|----------------------|--------------------------------------|
| Canadian Oil and Gas Property Expense | 226.8 | 211.2 | 10% declining balance |
| Canadian Development Expense | 840.1 | 857.6 | 30% declining balance |
| Canadian Exploration Expense | 79.8 | 98.3 | 100% |
| Undepreciated Capital Cost | 393.1 | 398.3 | Primarily 25% declining balance |
| Other | 35.1 | 32.8 | Various, 7% declining balance to 20% |
| Total Federal Tax Pools | 1,574.9 | 1,598.2 | |
| Additional Alberta Tax Pools | 44.9 | 44.9 | Primarily 100% |

MARKETING

Commodity Price Risk Management

The Company is a party to certain off balance sheet 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 third quarter of 2016, a realized hedging gain of \$23.9 million was recorded as compared to a \$23.2 million gain for the equivalent period in 2015. A summary of contracts outstanding in respect of the hedging activities are as follows:

| Natural Gas Period Hedged | Type | Daily Volume | Price (CAD) |
|------------------------------------|-------------|--------------|----------------|
| April 1, 2015 to October 31, 2016 | Fixed Price | 5,000 GJ | \$2.855/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.83/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.90/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.97/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.98/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$3.05/GJ |
| May 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.82/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.84/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.88/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.92/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.925/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.95/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.975/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.975/GJ |
| December 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.55/GJ |
| January 1, 2016 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.54/GJ |
| April 1, 2016 to October 31, 2016 | Fixed Price | 5,000 GJ | \$2.40/GJ |
| April 1, 2016 to October 31, 2016 | Fixed Price | 5,000 GJ | \$2.45/GJ |
| April 1, 2016 to October 31, 2016 | Fixed Price | 5,000 GJ | \$2.50/GJ |
| April 1, 2016 - October 31, 2016 | Fixed Price | 5,000 GJ | \$3.05/GJ |

| | | | |
|-----------------------------------|-------------|----------|-------------|
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.50/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.52/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.53/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.5775/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.60/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.605/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.64/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.65/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.665/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.6725/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.6725/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.70/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.74/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.80/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.845/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.65/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.70/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.715/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.8225/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.825/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.825/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.835/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.85/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.85/GJ |

As at September 30, 2016 Peyto had committed to the future sale of 262,455,000 gigajoules (GJ) of natural gas at an average price of \$2.56 per GJ or \$2.94 per mcf. Had these contracts closed on September 30, 2016, Peyto would have realized a loss in the amount of \$31.6 million.

Subsequent to September 30, 2016, Peyto entered into the following contracts:

| Natural Gas Period Hedged | Type | Daily Volume | Price (CAD) |
|--------------------------------------|-------------|---------------------|------------------------|
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.60/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.67/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.86/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 5,000 GJ | \$2.70/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.75/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.92/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.955/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$3.025/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.80/GJ |
| April 1, 2017 to October 31, 2018 | Fixed Price | 5,000 GJ | \$2.40/GJ |
| April 1, 2017 to October 31, 2018 | Fixed Price | 5,000 GJ | \$2.535/GJ |
| April 1, 2017 to October 31, 2018 | Fixed Price | 5,000 GJ | \$2.565/GJ |

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 September 30 2016, 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 \$1.6 million per quarter. Average debt outstanding for the quarter was \$1,045 million (including \$420 million fixed rate debt).

LIQUIDITY AND CAPITAL RESOURCES

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

| (\$000) | Three Months ended September 30 | | Nine Months ended September 30 | |
|--|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Cash flows from operating activities | 129,057 | 139,275 | 370,299 | 399,724 |
| Change in non-cash working capital | (10,256) | (9,754) | (20,647) | 4,941 |
| Change in provision for performance based compensation | 9,114 | 4,992 | 20,348 | 9,684 |
| Funds from operations | 127,915 | 134,513 | 370,000 | 414,349 |
| Funds from operations per share | 0.78 | 0.85 | 2.29 | 2.64 |

For the third quarter ended September 30, 2016, funds from operations totaled \$127.9 million or \$0.78 per share, as compared to \$134.5 million or \$0.85 per share during the same quarter in 2015 due to decreases in commodity prices offset in part by increases in production and decreases in cash costs.

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.

Long-Term Debt

| (\$000) | September 30, 2016 | December 31, 2015 |
|-----------------------------------|--------------------|-------------------|
| Bank credit facility | 625,000 | 625,000 |
| Senior unsecured notes | 420,000 | 420,000 |
| Balance, end of the period | 1,045,000 | 1,045,000 |

The Company has a syndicated \$1.0 billion extendible unsecured revolving credit facility with a stated term date of December 4, 2019. An accordion provision has been added that allows for the pre-approved increase of the facility up to \$1.3 billion, at the Company's request, subject to additional commitments by existing facility lenders or by adding new financial institutions to the syndicate. The bank facility is made up of a \$30 million working capital sub-tranche and a \$970 million 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 September 30, 2016 – 1.9:1.0

- 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 September 30, 2016 – 1.9:1.0

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

as at September 30, 2016 – 14.4 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 per cent 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 September 30, 2016 – 39 per cent

Peyto is in compliance with all financial covenants and has no subordinated debt as at September 30, 2016.

On April 26, 2016, the amended and restated note purchase and private shelf agreement dated January 3, 2012 and restated as of April 26, 2013 was amended to increase the shelf facility from \$150 million to \$250 million.

On October 24, 2016 Peyto closed an issuance of CDN \$100 million of senior unsecured notes. The notes were issued by way of private placement pursuant to the amended and restated 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 3.7% and mature in October 24, 2023. Interest will be paid semi-annually in arrears. After the issuance of these notes, the shelf facility is fully drawn at \$250 million.

Peyto's total borrowing capacity after the issuance of the senior, unsecured notes on October 24, 2016 is \$1.52 billion of which the credit facility is \$1.0 billion.

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 \$550 to \$600 million for 2017. The total amount of capital invested in 2017 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 September 30, 2016 | As at December 31, 2015 | As at September 30, 2015 |
|---|-----------------------------|----------------------------|-----------------------------|
| Bank credit facility | 625,000 | 625,000 | 540,000 |
| Senior unsecured notes | 420,000 | 420,000 | 420,000 |
| Current assets | (124,304) | (167,455) | (144,103) |
| Current liabilities | 178,523 | 163,886 | 171,942 |
| Financial derivative instruments | (16,516) | 65,169 | 51,174 |
| Provision for future performance based compensation | (22,348) | (1,998) | (17,908) |
| Net debt | 1,060,355 | 1,104,602 | 1,021,105 |

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, 2015 | 158,958,273 | 1,467,264 |
| Common shares issued by private placement | 281,270 | 7,644 |
| Equity offering | 5,390,625 | 172,500 |
| Common share issuance costs, (net of tax) | - | (5,409) |
| Balance, September 30, 2016 | 164,630,168 | 1,641,999 |

On December 31, 2015, Peyto completed a private placement of 149,030 common shares to employees and consultants for net proceeds of \$3.8 million (\$25.29 per share). These common shares were issued January 6, 2016.

On March 15, 2016, Peyto completed a private placement of 132,240 common shares to employees and consultants for net proceeds of \$3.9 million (\$29.30 per common share).

On May 18, 2016, Peyto completed a public offering for 5,390,625 common shares at a price of \$32.00 per common share, for net proceeds of \$165.6 million.

Capital Expenditures

Net capital expenditures for the third quarter of 2016 totaled \$113.6 million. Exploration and development related activity represented \$91.1 million (80% of total), while expenditures on facilities, gathering systems and equipment totaled \$17.0 million (15% of total) land, seismic, leaseholds and acquisitions totaled \$5.5 million (5% of total). The following table summarizes capital expenditures for the period:

| (\$000) | Three Months ended September 30 | | Nine Months ended September 30 | |
|----------------------------|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Land | - | 4,185 | 1,003 | 5,451 |
| Seismic | 682 | 90 | 4,554 | 4,372 |
| Drilling | 64,121 | 88,052 | 156,654 | 216,972 |
| Completions | 26,939 | 43,742 | 68,089 | 119,565 |
| Equipping & Tie-ins | 13,176 | 14,512 | 27,239 | 32,494 |
| Facilities & Pipelines | 3,838 | 32,027 | 49,204 | 55,463 |
| Acquisitions | 4,765 | 54 | 32,640 | 3,107 |
| Dispositions | - | (6,102) | (28) | (6,282) |
| Leasehold Improvements | 50 | 58 | 613 | 196 |
| Total Capital Expenditures | 113,571 | 176,618 | 339,968 | 431,338 |

Dividends

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|---------------------------------------|---------------------------------|---------|--------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Funds from operations (\$000) | 127,915 | 134,513 | 370,000 | 414,349 |
| Total dividends (\$000) | 54,328 | 52,456 | 160,583 | 155,693 |
| Total dividends per common share (\$) | 0.33 | 0.33 | 0.99 | 0.99 |
| Payout ratio (%) | 42 | 39 | 43 | 38 |

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 September 30, 2016:

| (\$000) | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter |
|----------------------------------|--------|--------|--------|--------|--------|------------|
| Interest payments ⁽¹⁾ | 4,830 | 18,385 | 18,385 | 16,190 | 13,995 | 27,840 |
| Transportation commitments | 8,704 | 35,651 | 39,309 | 31,930 | 24,602 | 98,700 |
| Operating leases | 265 | 2,279 | 2,032 | 2,032 | 2,032 | 12,567 |
| Methanol | - | 1,582 | - | - | - | - |
| Total | 13,799 | 57,897 | 59,726 | 50,152 | 40,629 | 139,107 |

⁽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 contains various claims relating to alleged misrepresentations in disclosure documents of Poseidon (not New Open Range), which claims are 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 seeks 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.

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 claims, 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.

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 Peyto for any liability KPMG is determined to have to Poseidon. Peyto is not required to deliver a defence to this claim at this time.

On July 3, 2014, the Plaintiffs filed a lawsuit with the Court against KPMG LLP, 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 LLP 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 seeks, among other things, an indemnity, or alternatively contribution, from the third party defendants with respect to any judgment awarded against KPMG LLP.

The allegations against New Open Range contained in the claims described above are based on factual matters that pre-existed the Company's acquisition of New Open Range. The Company has not yet been required to defend either of the actions. If it is required to defend the actions, the Company intends to aggressively protect its interests and the interests of its Shareholders and will seek all available legal remedies in defending the actions.

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 | | Accounts Payable | | | |
|---------|-------------|---------------------------------|--------------|--------------------------------|--------------|--------------------|--|
| | | Three Months ended September 30 | | Nine Months ended September 30 | | As at September 30 | |
| (\$000) | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | |
| | 98.6 | 436.2 | 579.1 | 1,327 | 344.3 | 597.6 | |

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 September 30, 2016 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, 2015 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 2016. 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 September 30, 2016.

In July 2014, the IASB completed the final elements of IFRS 9 "Financial Instruments." The Standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 "Financial Instruments: Recognition and Measurement." IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. The Standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 9 will be applied by Peyto on January 1, 2018 and the Company is currently evaluating the impact of the standard

on its financial statements.

In May 2014, the IASB issued IFRS 15 "Revenue from Contracts with Customers," which replaces IAS 18 "Revenue," IAS 11 "Construction Contracts," and related interpretations. The standard is required to be adopted for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 will be applied by Peyto on January 1, 2018 and the Company is currently evaluating the impact of the standard on Peyto's financial statements.

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

| | 2016 | | | 2015 | |
|--|-------------|-------------|-------------|-------------|-------------|
| | Q3 | Q2 | Q1 | Q2 | Q3 |
| Operations | | | | | |
| Production | | | | | |
| Natural gas (mcf/d) | 534,710 | 489,337 | 567,230 | 540,512 | 455,137 |
| Oil & NGLs (bbl/d) | 7,247 | 6,621 | 7,008 | 6,943 | 5,352 |
| Barrels of oil equivalent (boe/d @ 6:1) | 96,365 | 88,177 | 101,546 | 97,028 | 81,208 |
| Thousand cubic feet equivalent (mcf/d @ 6:1) | 578,189 | 529,064 | 609,278 | 582,167 | 487,250 |
| Average product prices | | | | | |
| Natural gas (\$/mcf) | 2.88 | 2.60 | 3.06 | 3.34 | 3.57 |
| Oil & natural gas liquids (\$/bbl) | 39.76 | 41.46 | 33.60 | 39.88 | 41.69 |
| \$/MCFE | | | | | |
| Average sale price (\$/mcf) | 3.16 | 2.92 | 3.24 | 3.58 | 3.80 |
| Average royalties paid (\$/mcf) | 0.12 | 0.10 | 0.13 | 0.13 | 0.15 |
| Average operating expenses (\$/mcf) | 0.25 | 0.26 | 0.23 | 0.25 | 0.28 |
| Average transportation costs (\$/mcf) | 0.16 | 0.17 | 0.16 | 0.16 | 0.16 |
| Field netback (\$/mcf) | 2.63 | 2.39 | 2.72 | 3.04 | 3.21 |
| General & administrative expense (\$/mcf) | 0.04 | 0.06 | 0.03 | 0.05 | 0.02 |
| Interest expense (\$/mcf) | 0.19 | 0.21 | 0.17 | 0.16 | 0.19 |
| Cash netback (\$/mcf) | 2.40 | 2.12 | 2.52 | 2.82 | 3.00 |
| Financial (\$000 except per share) | | | | | |
| Revenue | 168,195 | 140,891 | 179,351 | 191,606 | 170,216 |
| Royalties | 6,382 | 4,874 | 6,985 | 6,663 | 6,489 |
| Funds from operations | 127,915 | 102,178 | 139,907 | 151,123 | 134,513 |
| Funds from operations per share | 0.78 | 0.63 | 0.88 | 0.95 | 0.85 |
| Total dividends | 54,328 | 53,735 | 52,520 | 52,456 | 52,456 |
| Total dividends per share | 0.33 | 0.33 | 0.33 | 0.33 | 0.33 |
| Payout ratio | 42% | 53% | 38% | 35% | 39% |
| Earnings | 22,814 | 9,102 | 41,943 | 43,406 | 37,347 |
| Earnings per diluted share | 0.14 | 0.06 | 0.26 | 0.27 | 0.23 |
| Capital expenditures | 113,571 | 50,634 | 175,763 | 162,442 | 176,618 |
| Weighted average shares outstanding | 164,630,168 | 161,845,999 | 159,142,526 | 158,958,273 | 158,958,273 |

Peyto Exploration & Development Corp.

Condensed Balance Sheet (unaudited)

(Amount in \$ thousands)

| | September 30 2016 | December 31 2015 |
|--|----------------------|---------------------|
| Assets | | |
| Current assets | | |
| Cash | 33,097 | - |
| Accounts receivable | 73,359 | 85,525 |
| Due from private placement (Note 6) | - | 3,769 |
| Derivative financial instruments (Note 8) | - | 65,169 |
| Prepaid expenses | 17,848 | 12,992 |
| | 124,304 | 167,455 |
| <hr/> | | |
| Property, plant and equipment, net (Note 3) | 3,319,567 | 3,190,059 |
| | 3,319,567 | 3,190,059 |
| | 3,443,871 | 3,357,514 |
| <hr/> | | |
| Liabilities | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | 121,550 | 144,402 |
| Dividends payable (Note 6) | 18,109 | 17,486 |
| Derivative financial instruments (Note 8) | 16,516 | - |
| Provision for future performance based compensation (Note 7) | 22,348 | 1,998 |
| | 178,523 | 163,886 |
| <hr/> | | |
| Long-term debt (Note 4) | 1,045,000 | 1,045,000 |
| Long-term derivative financial instruments (Note 8) | 15,051 | 2,299 |
| Provision for future performance based compensation (Note 7) | 10,707 | - |
| Decommissioning provision (Note 5) | 152,020 | 118,882 |
| Deferred income taxes | 403,710 | 403,890 |
| | 1,626,488 | 1,570,071 |
| <hr/> | | |
| Equity | | |
| Share capital (Note 6) | 1,641,999 | 1,467,264 |
| Shares to be issued (Note 6) | - | 3,769 |
| Retained earnings | 16,615 | 103,339 |
| Accumulated other comprehensive (loss) income (Note 6) | (19,754) | 49,185 |
| | 1,638,860 | 1,623,557 |
| | 3,443,871 | 3,357,514 |

See accompanying notes to the financial statements.

Peyto Exploration & Development Corp.

Condensed Income Statement *(unaudited)*

(Amount in \$ thousands except earnings per share amount)

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|---------|-----------------------------------|----------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue | | | | |
| Oil and gas sales | 144,301 | 146,993 | 366,947 | 443,774 |
| Realized gain on hedges <i>(Note 8)</i> | 23,894 | 23,223 | 121,490 | 82,456 |
| Royalties | (6,382) | (6,489) | (18,241) | (20,356) |
| Petroleum and natural gas sales, net | 161,813 | 163,727 | 470,196 | 505,874 |
| Expenses | | | | |
| Operating | 13,254 | 12,665 | 38,526 | 40,672 |
| Transportation | 8,647 | 7,085 | 25,506 | 20,302 |
| General and administrative | 2,133 | 822 | 6,843 | 4,331 |
| Future performance based compensation <i>(Note 7)</i> | 13,969 | 5,518 | 31,057 | 10,596 |
| Interest | 9,864 | 8,642 | 29,320 | 26,221 |
| Accretion of decommissioning provision <i>(Note 5)</i> | 538 | 633 | 1,685 | 1,760 |
| Depletion and depreciation <i>(Note 3)</i> | 82,157 | 76,623 | 248,750 | 237,555 |
| Gain on disposition of assets <i>(Note 3)</i> | - | - | (12,668) | - |
| | 130,562 | 111,988 | 369,019 | 341,437 |
| Earnings before taxes | 31,251 | 51,739 | 101,177 | 164,437 |
| Income tax | | | | |
| Deferred income tax expense | 8,437 | 14,392 | 27,318 | 70,282 |
| Earnings for the period | 22,814 | 37,347 | 73,859 | 94,155 |
| Earnings per share <i>(Note 6)</i> | | | | |
| Basic and diluted | \$0.14 | \$0.23 | \$0.46 | \$0.60 |

See accompanying notes to the financial statements.

Peyto Exploration & Development Corp.

Condensed Statement of Comprehensive Income (Loss) (unaudited)

(Amount in \$ thousands)

| | Three months ended | | Nine months ended | |
|--|--------------------|----------|-------------------|----------|
| | September 30 | | September 30 | |
| | 2016 | 2015 | 2016 | 2015 |
| Earnings for the period | 22,814 | 37,347 | 73,859 | 94,155 |
| Other comprehensive income (loss) | | | | |
| Change in unrealized gain (loss) on cash flow hedges | 42,232 | (7,660) | 27,053 | (54,409) |
| Deferred tax (expense) recovery | (4,951) | 2,068 | 25,498 | 14,690 |
| Realized (gain) on cash flow hedges | (23,894) | (23,223) | (121,490) | (82,456) |
| Comprehensive income (loss) | 36,201 | 8,532 | 4,920 | (28,020) |

See accompanying notes to the financial statements.

Peyto Exploration & Development Corp.
Condensed Statement of Changes in Equity *(unaudited)*
(Amount in \$ thousands)

| | Nine months ended September 30 | |
|---|---------------------------------------|-----------|
| | 2016 | 2015 |
| Share capital, beginning of period | 1,467,264 | 1,292,398 |
| Common shares issued by private placement | 7,644 | 7,732 |
| Equity offering | 172,500 | 172,517 |
| Common shares issuance costs (net of tax) | (5,409) | (5,387) |
| Share capital, end of period | 1,641,999 | 1,467,260 |
| | | |
| Shares to be issued, beginning of period | 3,769 | 5,625 |
| Shares issued | (3,769) | (5,625) |
| Shares to be issued, end of period | - | - |
| | | |
| Retained earnings, beginning of period | 103,339 | 173,927 |
| Earnings for the period | 73,859 | 94,155 |
| Dividends <i>(Note 6)</i> | (160,583) | (155,693) |
| Retained earnings, end of period | 16,615 | 112,389 |
| | | |
| Accumulated other comprehensive income, beginning of period | 49,185 | 79,986 |
| Other comprehensive loss | (68,939) | (39,719) |
| Accumulated other comprehensive (loss) income, end of period | (19,754) | 40,267 |
| | | |
| Total equity | 1,638,860 | 1,619,916 |

See accompanying notes to the financial statements.

Peyto Exploration & Development Corp.

Condensed Statement of Cash Flows (unaudited)

(Amount in \$ thousands)

See accompanying notes to the financial statements

| | Three months ended September 30 | | Nine months ended September 30 | |
|---|------------------------------------|------------------|-----------------------------------|------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Cash provided by (used in) | | | | |
| operating activities | | | | |
| Earnings | 22,814 | 37,347 | 73,859 | 94,155 |
| Items not requiring cash: | | | | |
| Deferred income tax | 8,437 | 14,392 | 27,318 | 70,282 |
| Depletion and depreciation | 82,157 | 76,623 | 248,750 | 237,555 |
| Accretion of decommissioning provision | 538 | 633 | 1,685 | 1,760 |
| Gain on disposition of assets | - | - | (12,668) | - |
| Long term portion of future performance based compensation | 4,855 | 526 | 10,708 | 913 |
| Change in non-cash working capital related to operating activities | 10,256 | 9,754 | 20,647 | (4,941) |
| | 129,057 | 139,275 | 370,299 | 399,724 |
| Financing activities | | | | |
| Issuance of common shares | - | - | 180,144 | 180,249 |
| Issuance costs | (10) | - | (7,409) | (7,380) |
| Cash dividends paid | (54,328) | (52,456) | (159,960) | (155,113) |
| Increase (decrease) in bank debt | - | 50,000 | - | (65,000) |
| Issuance of senior unsecured notes | - | - | - | 100,000 |
| | (54,338) | (2,456) | 12,775 | 52,756 |
| Investing activities | | | | |
| Additions to property, plant and equipment | (113,571) | (176,618) | (339,968) | (431,338) |
| Change in prepaid capital | (1,567) | 7,721 | 6,166 | (6,158) |
| Change in non-cash working capital relating to investing activities | 48,059 | 32,078 | (16,175) | (14,984) |
| | (67,079) | (136,819) | (349,977) | (452,480) |
| Net increase (decrease) in cash | 7,640 | - | 33,097 | - |
| Cash, beginning of period | 25,457 | - | - | - |
| Cash, end of period | 33,097 | - | 33,097 | - |
| The following amounts are included in cash flows from operating activities: | | | | |
| Cash interest paid | 9,140 | 9,402 | 28,547 | 24,050 |
| Cash taxes paid | - | - | - | - |

Peyto Exploration & Development Corp.
Notes to Condensed Financial Statements (*unaudited*)
As at September 30, 2016 and 2015
(Amount in \$ thousands, except as otherwise noted)

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 November 8, 2016.

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, 2015 and 2014.

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.

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, 2015 and 2014.

(b) Standards issued but not yet effective

In July 2014, the IASB completed the final elements of IFRS 9 "Financial Instruments." The Standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 "Financial Instruments: Recognition and Measurement." IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. The Standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 9 will be applied by Peyto on January 1, 2018 and the Company is currently evaluating the impact of the standard on its financial statements.

In May 2014, the IASB issued IFRS 15 "Revenue from Contracts with Customers," which replaces IAS 18 "Revenue," IAS 11 "Construction Contracts," and related interpretations. The standard is required to be adopted for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 will be applied by Peyto on January 1, 2018 and the Company is currently evaluating the impact of the standard on Peyto's financial statements.

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. Property, plant and equipment, net

Cost

| | |
|--|--------------------|
| At December 31, 2015 | 4,416,643 |
| Additions | 350,785 |
| Decommissioning provision additions | 31,453 |
| Prepaid capital | (6,166) |
| At September 30, 2016 | 4,792,715 |
| Accumulated depletion and depreciation | |
| At December 31, 2015 | (1,226,584) |
| Depletion and depreciation | (246,564) |
| At September 30, 2016 | (1,473,148) |
| Carrying amount at December 31, 2015 | 3,190,059 |
| Carrying amount at September 30, 2016 | 3,319,567 |

During the nine months ended September 30, 2016, the Company closed an asset swap arrangement. For purposes of determining a gain on disposition, the estimated fair value was based on the fair value of the assets received. The Company recorded a gain of \$12.7 million for the nine months ended September 30, 2016.

During the three and nine month periods ended September 30, 2016, Peyto capitalized \$1.6 million and \$4.7 million (2015 - \$3.0 million and \$6.8 million) of general and administrative expense directly attributable to exploration and development activities.

4. Long-term debt

| | September 30, 2016 | December 31, 2015 |
|-----------------------------------|--------------------|-------------------|
| Bank credit facility | 625,000 | 625,000 |
| Senior unsecured notes | 420,000 | 420,000 |
| Balance, end of the period | 1,045,000 | 1,045,000 |

The Company has a syndicated \$1.0 billion extendible unsecured revolving credit facility with a stated term date of December 4, 2019. An accordion provision has been added that allows for the pre-approved increase of the facility up to \$1.3 billion, at the Company's request, subject to additional commitments by existing facility lenders or by adding new financial institutions to the syndicate. The bank facility is made up of a \$30 million working capital sub-tranche and a \$970 million 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.

Peyto is in compliance with all financial covenants at September 30, 2016.

On April 26, 2016, the amended and restated note purchase and private shelf agreement dated January 3, 2012 and restated as of April 26, 2013 was amended to increase the shelf facility from \$150 million to \$250 million.

On October 24, 2016 Peyto closed an issuance of CDN \$100 million of senior unsecured notes. The notes were issued by way of private placement pursuant to the amended and restated 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 3.7% and mature in October 24, 2023. Interest will be paid semi-annually in arrears. After the issuance of these notes, the shelf facility is fully drawn at \$250 million.

Peyto's total borrowing capacity after the issuance of the senior, unsecured notes on October 24, 2016 is \$1.52 billion of which the credit facility is \$1.0 billion.

Total interest expense for the three and nine month periods ended September 30, 2016 was \$9.9 million and \$29.3 million (2015 - \$8.6 million and \$26.2 million) and the average borrowing rate for the period was 3.7% and 3.6% (2015- 3.6% and 3.6%).

5. Decommissioning provision

The following table reconciles the change in decommissioning provision:

| | |
|--|----------------|
| Balance, December 31, 2015 | 118,882 |
| New or increased provisions | 13,266 |
| Accretion of decommissioning provision | 1,685 |
| Change in discount rate and estimates | 18,187 |
| Balance, September 30, 2016 | 152,020 |
| Current | - |
| Non-current | 152,020 |

Peyto has estimated the net present value of its total decommissioning provision to be \$152.0 million as at September 30, 2016 (\$118.9 million at December 31, 2015) based on a total future undiscounted liability of \$254.1 million (\$239.0 million at December 31, 2015). At September 30, 2016 management estimates that these payments are expected to be made over the next 50 years with the majority of payments being made in years 2040 to 2064. The Bank of Canada's long term bond rate of 1.66 per cent (2.15 per cent at December 31, 2015) and an inflation rate of 2.0 per cent (2.0 per cent at December 31, 2015) were used to calculate the present value of the decommissioning provision.

6. 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, 2015 | 158,958,273 | 1,467,264 |
| Common shares issued by private placement | 281,270 | 7,644 |
| Equity offering | 5,390,625 | 172,500 |
| Common share issuance costs, (net of tax) | - | (5,409) |
| Balance, September 30, 2016 | 164,630,168 | 1,641,999 |

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

| | Three Months ended September 30 | | Nine Months ended September 30 | |
|--|------------------------------------|-------------|-----------------------------------|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| Weighted average common shares basic and diluted | 164,630,168 | 158,958,273 | 161,882,961 | 156,994,934 |

On December 31, 2015, Peyto completed a private placement of 149,030 common shares to employees and consultants for net proceeds of \$3.8 million (\$25.29 per share). These common shares were issued January 6, 2016.

On March 15, 2016, Peyto completed a private placement of 132,240 common shares to employees and consultants for net proceeds of \$3.9 million (\$29.30 per common share).

On May 18, 2016, Peyto completed a public offering for 5,390,625 common shares at a price of \$32.00 per common share, for net proceeds of \$165.6 million.

Dividends

During the three and nine month periods ended September 30, 2016, Peyto declared and paid dividends of \$0.33 and \$0.99 per common share (\$0.11 per common share for the months of January to September 2016, totaling \$54.3 million and \$160.6 million respectively (2015 - \$0.33 and \$0.99 (\$0.11 per common share for the months of January to September 2015), totaling \$52.5 million and \$155.7 million respectively).

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

Gains and losses from cash flow hedges are accumulated until settled. These outstanding hedging contracts are recognized in earnings on settlement with gains and losses being recognized as a component of net revenue. Further information on these contracts is set out in Note 8.

7. 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:

| | September 30, 2016 | September 30, 2015 |
|----------------------------------|---------------------------|--------------------|
| Share price | \$36.82 | \$27.75 |
| Exercise price (net of dividend) | \$23.10 | \$33.35 |
| Expected volatility | 36.1% | 31% |
| Option life | 0.25 years | 0.25 years |
| Risk-free interest rate | 0.51% | 0.52% |

8. Financial instruments

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 September 30, 2016.

The Company's areas of financial risk management and risks related to financial instruments remained unchanged from December 31, 2015.

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 value drivers are observable in active markets.
- Level 3 – valuations derived from valuation techniques in which one or more significant inputs or 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 September 30, 2016, cash and financial derivative instruments are carried at fair value. Accounts receivable, due from private placement, 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 September 30, 2016:

| Natural Gas | | | Price |
|---------------------------------------|-------------|---------------------|----------------------------|
| Period Hedged | Type | Daily Volume | (CAD) |
| April 1, 2015 to October 31, 2016 | Fixed Price | 5,000 GJ | \$2.855/GJ |
| April 1, 2015 to March 31, 2017 | Fixed Price | 50,000 GJ | \$2.83/GJ to \$3.05/GJ |
| May 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.82/GJ |
| November 1, 2015 to March 31, 2017 | Fixed Price | 40,000 GJ | \$2.84/GJ to \$2.975/GJ |
| December 1, 2015 to March 31, 2017 | Fixed Price | 5,000 GJ | \$2.55/GJ |
| January 1, 2016 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.54/GJ |
| April 1, 2016 to October 31, 2016 | Fixed Price | 50,000 GJ | \$2.40/GJ to \$3.43/GJ |
| April 1, 2016 to March 31, 2017 | Fixed Price | 95,000 GJ | \$2.58/GJ to \$3.01/GJ |
| April 1, 2016 to March 31, 2018 | Fixed Price | 60,000 GJ | \$2.42/GJ to \$2.75/GJ |
| 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, 2017 | Fixed Price | 20,000 GJ | \$2.11/GJ to \$2.305/GJ |
| May 1, 2016 to October 31, 2018 | Fixed Price | 20,000 GJ | \$2.20/GJ to \$2.35/GJ |
| June 1, 2016 to October 31, 2016 | Fixed Price | 20,000 GJ | \$1.52/GJ to \$1.63/GJ |
| July 1, 2016 to October 31, 2016 | Fixed Price | 5,000 GJ | \$1.73/GJ |
| July 1, 2016 to March 31, 2017 | Fixed Price | 10,000 GJ | \$2.30/GJ |
| July 1, 2016 to October 31, 2017 | Fixed Price | 10,000 GJ | \$2.375/GJ to \$2.3775/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, 2017 | Fixed Price | 20,000 GJ | \$2.22/GJ to \$2.30/GJ |
| August 1, 2016 to October 31, 2018 | Fixed Price | 25,000 GJ | \$2.3175/GJ to \$2.5525/GJ |
| September 1, 2016 to October 31, 2016 | Fixed Price | 15,000 GJ | \$2.12/GJ to \$2.14/GJ |
| November 1, 2016 to March 31, 2017 | Fixed Price | 175,000 GJ | \$2.34/GJ to \$3.00/GJ |
| November 1, 2016 to March 31, 2018 | Fixed Price | 5,000 GJ | \$2.51/GJ |
| April 1, 2017 to October 31, 2017 | Fixed Price | 115,000 GJ | \$2.23/GJ to \$2.845/GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 60,000 GJ | \$2.65/GJ to \$2.945/GJ |
| April 1, 2017 to October 31, 2018 | Fixed Price | 10,000 GJ | \$2.585/GJ to \$2.745/GJ |
| November 1, 2017 to March 31, 2018 | Fixed Price | 15,000 GJ | \$2.91/GJ to \$3.0425/GJ |
| April 1, 2018 to October 31, 2018 | Fixed Price | 25,000 GJ | \$2.39/GJ to \$2.465/GJ |

As at September 30, 2016, Peyto had committed to the future sale of 262,455,000 gigajoules (GJ) of natural gas at an average price of \$2.56 per GJ or \$2.94 per mcf. Had these contracts been closed on September 30, 2016, Peyto would have realized a net loss in the amount of \$31.6 million. If the AECO gas price on September 30, 2016 were to decrease by \$0.10/GJ, the financial derivative liability would decrease by approximately \$26.2 million. An opposite change in commodity prices rates would result in an opposite impact.

Subsequent to September 30, 2016 Peyto entered into the following contracts:

| Natural Gas Period Hedged | Type | Daily Volume | Price (CAD) |
|--------------------------------------|-------------|---------------------|-------------------------|
| April 1, 2017 to October 31, 2017 | Fixed Price | 20,000 GJ | \$2.60/GJ to \$2.86GJ |
| April 1, 2017 to March 31, 2018 | Fixed Price | 25,000 GJ | \$2.75/GJ to \$3.025/GJ |
| April 1, 2017 to October 31, 2018 | Fixed Price | 15,000 GJ | \$2.40/GJ to \$2.565/GJ |

9. 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 | | Accounts Payable | | | |
|---------------------------------|-------|--------------------------------|-------|--------------------|-------|
| Three Months ended September 30 | | Nine Months ended September 30 | | As at September 30 | |
| 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| 98.6 | 436.2 | 579.1 | 1,327 | 344.3 | 597.6 |

10. Commitments

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 September 30, 2016:

| | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter |
|----------------------------------|--------|--------|--------|--------|--------|------------|
| Interest payments ⁽¹⁾ | 4,830 | 18,385 | 18,385 | 16,190 | 13,995 | 27,840 |
| Transportation commitments | 8,704 | 35,651 | 39,309 | 31,930 | 24,602 | 98,700 |
| Operating leases | 265 | 2,279 | 2,032 | 2,032 | 2,032 | 12,567 |
| Methanol | - | 1,582 | - | - | - | - |
| Total | 13,799 | 57,897 | 59,726 | 50,152 | 40,629 | 139,107 |

⁽¹⁾ Fixed interest payments on senior unsecured notes

11. 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 contains various claims relating to alleged misrepresentations in disclosure documents of Poseidon (not New Open Range), which claims are 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 seeks 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.

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 claims, 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.

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 Peyto for any liability KPMG is determined to have to Poseidon. Peyto is not required to deliver a defence to this claim at this time.

On July 3, 2014, the Plaintiffs filed a lawsuit with the Court against KPMG LLP, 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 LLP 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 seeks, among other things, an indemnity, or alternatively contribution, from the third party defendants with respect to any judgment awarded against KPMG LLP.

The allegations against New Open Range contained in the claims described above are based on factual matters that pre-existed the Company's acquisition of New Open Range. The Company has not yet been required to defend either of the actions. If it is required to defend the actions, the Company intends to aggressively protect its interests and the interests of its Shareholders and will seek all available legal remedies in defending the actions.

Officers

Darren Gee
President and Chief Executive Officer

Scott Robinson
Executive Vice President and Chief Operating Officer

Kathy Turgeon
Vice President, Finance and Chief Financial Officer

Lee Curran
Vice President, Drilling and Completions

Stephen Chetner
Corporate Secretary

Tim Louie
Vice President, Land

David Thomas
Vice President, Exploration

Jean-Paul Lachance
Vice President, Exploitation

Todd Burdick
Vice President, Production

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

Bankers

Bank of Montreal
Union Bank, Canada Branch
Royal Bank of Canada
Canadian Imperial Bank of Commerce
The Toronto-Dominion Bank
Bank of Nova Scotia
Alberta Treasury Branches
Canadian Western Bank

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Stock Listing Symbol: PEY.TO

Toronto Stock Exchange