

# PEYTO Energy Trust

## President's Monthly Report

September 2008

From the desk of Darren Gee, President & CEO

The hurricane season has begun and the National Hurricane Center is calling for an 85% chance of an above average season with 3-6 major hurricanes. It will be interesting to see if the new production platforms that were reconstructed after the 2005 hurricane season (Katrina and Rita) will better withstand another onslaught. The most recent storm, Gustav, while causing some volatility to spot prices, didn't seem to affect natural gas futures much. Fortunately, Peyto operations in west central Alberta aren't affected by such weather events. We only have to deal with the odd rainstorm or lightning strike that causes temporary power outages and production disruptions.

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

### Capital Investment

2008 Capital Summary (millions \$ CND)\*

	Jan	Feb	Mar	Q1	Apr	May	Jun	Q2	July
Land & Seismic	0	0	0	1	0	0	1	2	1
Drilling	6	5	6	17	1	1	8	10	10
Completions	2	3	4	9	2	0	5	7	7
Tie ins	1	2	3	5	1	0	2	3	2
Facilities	0	0	0	0	0	0	0	0	0
Other	0	0	0	0	0	0	0	0	0
<b>Total</b>	<b>10</b>	<b>10</b>	<b>13</b>	<b>33</b>	<b>3</b>	<b>2</b>	<b>16</b>	<b>21</b>	<b>20</b>

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

### Production

2008 Production ('000 boe/d)\*

	Q1 08	Apr	May	June	Q2 08	Jul	Aug	Sept	Q3 08
Sundance	16.4	16.3	16.0	15.6	16.0	16.1	16.5		
Kakwa	2.6	2.5	2.3	2.2	2.3	2.4	2.2		
Other	1.4	1.4	1.2	1.2	1.3	1.2	1.2		
<b>Total</b>	<b>20.4</b>	<b>20.2</b>	<b>19.5</b>	<b>19.0</b>	<b>19.6</b>	<b>19.7</b>	<b>19.9</b>		

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### Cashflow is King

One of the strengths of the Peyto strategy is the strict focus on value creation. Like most successful businesses, "it's all about the money." We spend capital to drill a well, and we measure the return we get on that capital by how much money we get back when we sell the production. The absolute production at any given time, for instance, is of less significance than the total cashflow that is being delivered over the life of the well. If operating costs, for example, that may be low today, rise dramatically in the future, they will choke off that cashflow stream and erode our return. It is critically important to understand and optimize those cashflow variables that can be controlled, and minimize the risk of those that can't.

Take Crown Royalties for example: the new Alberta Royalty framework, to take effect January 2009, outlines equations that determine natural gas royalties using both a price component and a production rate component. The price component is somewhat outside of our control, although we can attempt to manage the risk by ensuring that the Crown's share is sold at or above the Reference Price. The production rate component, however, is completely within our control and we can manipulate the production rate to produce the desired result of lower royalties. Lower royalties means greater cashflow. And we all know, cashflow is king.

If we look at a tight gas well example, we can see how, by choking back early time production, we can actually reduce royalties and increase the amount of cashflow we obtain.

Typical Tight Gas Well

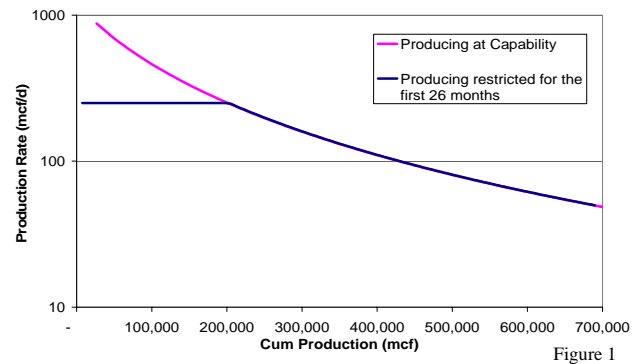
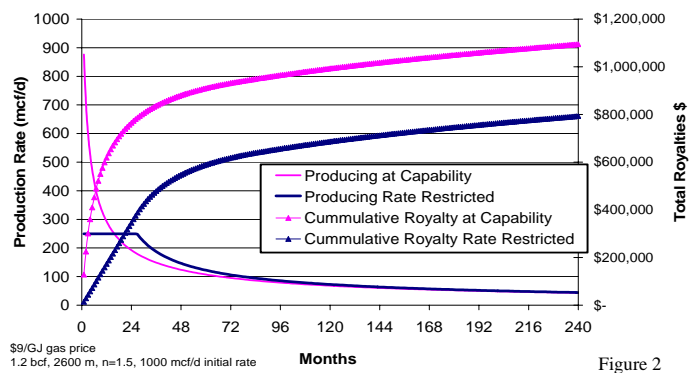


Figure 1 shows the production rate versus cumulative production for a tight gas well producing at capability and for one that is choked back for the first 26 months of its producing life. Both producing profiles come together once the well has recovered approximately 200 mmcf because the wells are no longer capable of producing at greater rates. Both wells also recover the same amount of ultimate reserves.

Typical Tight Gas Well



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If we now look at these same profiles on a rate versus time graph (Figure 2) and we assume a \$9/GJ gas price (*that would be nice!*), we can see that the rate restricted well pays approximately \$300,000 less in royalties over the first 20 years. After this time, both rate curves come together and both wells are paying the same royalties.

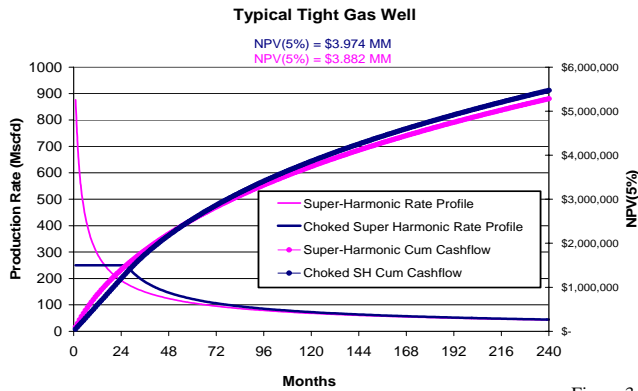


Figure 3

Unfortunately, restricting the production rate also restricts the amount of revenue that is delivered in the first 15 months or so. This means we are giving up cashflow in the early time in order to recover more over the life of the well. When we consider the time value of money and the fact that we need to recover our capital investment as fast as possible, do we still make more?

The answer is still yes. Figure 3 shows both cashflow streams after subtracting royalties and a constant provision for operating costs. The rate restricted well still recovers approximately \$90,000 more value, discounted at 5%, than the well produced at capability. Even at a 10% discount factor, the rate restricted well captures more.

The point of this analysis is not just to show that the new royalty regime in Alberta seems to encourage even longer reserve life, but that generating strong returns for unitholders and creating real value is not solely about building production, it's about making money. Understanding the various attributes of an oil and gas investment and how they contribute to cashflow is how Peyto has always maximized returns for its unitholders.

### Activity Levels and Commodity Prices

Western Canadian drilling activity (Figure 4) is slowly picking up as the stronger commodity price for the year materializes in increased cashflow and increased capital programs. The gap between Alberta activity and the rest of Western Canada continues to widen, illustrating the negative impact of the new royalty regime on conventional oil and gas play economics.

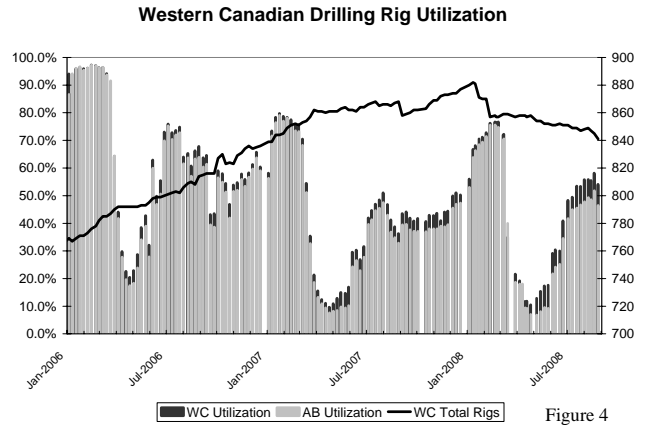


Figure 4

There has been no relief on the horizon with respect to steel costs, however, as "hot rolled coil" is still trading at \$1150/ton (Figure 5).

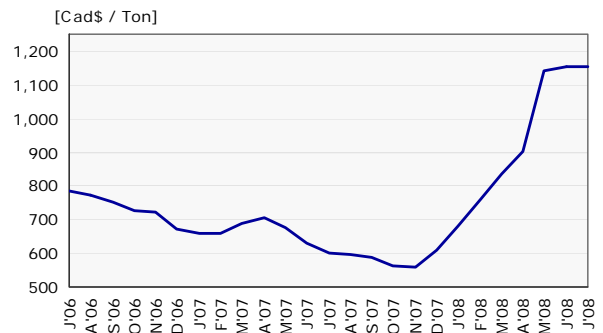


Figure 5

And with Alberta natural gas price having dropped off (blue line in Figure 6), we need to keep a close watch to ensure we are maintaining our high level of returns.

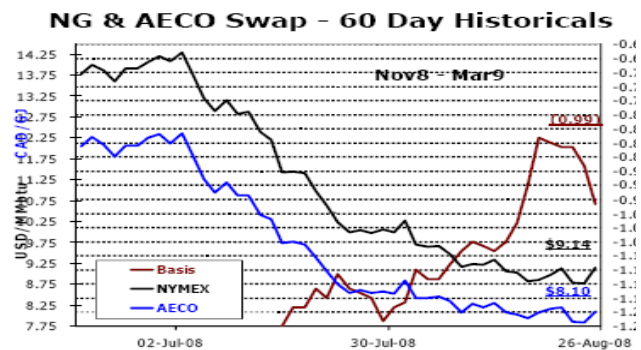


Figure 6