

PEYTO Energy Trust

President's Monthly Report

October 2009

From the desk of Darren Gee, President & CEO

I have to say that I have never quite understood the concept of *market sentiment*. It is described as the *general feeling or mood* of the investment community as to the anticipated movement of a particular stock or sector based on a variety of factors. I guess the engineer in me is far too analytical, expecting that most investors are basing their decisions on sound analysis or empirical evidence, not their "mood." But the mood of the market right now seems to be solidly behind natural gas, as evidenced by both the rally seen in natural gas prices and the even greater rally seen in natural gas companies, especially the un-hedged ones, over the last few weeks. A recent trip to Toronto and New York to visit investors caught me off guard as to the extent of this positive market sentiment, especially in light of the currently depressed spot natural gas price.

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

2009 Capital Summary (millions\$ CND)*

	Q1	Apr	May	Jun	Q2	July	Aug	Sept	Q3
Land & Seismic	0	0	0	0	0	1	0		
Drilling	7	1	1	2	3	6	7		
Completions	4	0	0	0	0	2	3		
Tie ins	2	0	0	0	0	0	1		
Facilities	1	0	1	1	1	0	0		
Other	0	0	0	0	0	0	0		
Total	13	1	1	3	5	9	10		

*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

2009 Production ('000 boe/d)*

	Q1 09	Apr	May	June	Q2 09	Jul	Aug	Sept	Q3 09
Sundance	15.9	15.6	15.1	15.0	15.2	15.1	14.5	15.0	
Kakwa	2.0	1.9	1.7	1.6	1.7	1.7	1.9	1.8	
Other	1.3	1.1	1.2	1.0	1.1	1.2	1.2	1.3	
Total	19.1	18.6	18.0	17.6	18.1	18.0	17.6	18.0	

*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.

The Tale of Two Technologies

I have had the opportunity of late to talk to many unitholders and industry investors about the potential use of horizontal multi-stage fracture (MSF) technology in the Deep Basin reservoirs that Peyto develops. In doing so, I, along with my fellow CEOs, have come to refer to it as "new technology." But the fact of the matter is that it really isn't new technology.

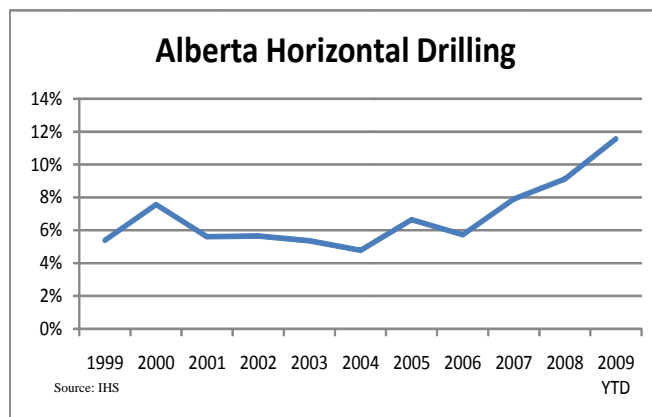
The reality is both horizontal drilling and fracture stimulations are relatively old technologies. It is only the combination of the two that is comparatively new.

Horizontal Drilling

Even horizontal drilling, when you look at the evolution, is all about the combination of technologies. Whether it was the development of mud pulse and electromagnetic surveys, bent bottomhole drilling assemblies or mud motors, each in isolation wouldn't necessarily have resulted in the ability to confidently drill horizontally to a known location. But combined, the technologies have allowed horizontal drilling to advance from the first well in 1929 to today where it is common oilfield drilling practice. Now, with the recent advances in motors, drill bits, mud designs and steerable drilling tools, drilling deep long horizontal holes is possible, even in some of the most challenging rock or strata in the basin.

This wasn't always the case of course. I remember back to the start of my career in the drilling department at Petro Canada (R.I.P.) in the late 1980s. At that time we were setting records with the longest and deepest horizontal well in Canada at 3,500 meters. Of course, that type of well is commonplace today. Even Peyto's first horizontal well was over 4,300 meters and not considered all that unique.

Put in perspective however, horizontal drilling is still only used for a small fraction of overall drilling activity and petroleum development. Figure 1 shows the percentage of horizontal wells spud in Alberta over the last ten years.



To extrapolate the current fever associated with horizontal multi-stage fracture technology to the majority of wells drilled is somewhat impractical. The industry just doesn't have the capability. Perhaps at some time in the future it may indeed represent how most wells are drilled. But that time is a ways away yet.

Fracture Stimulation

Hydraulic fracture stimulations are also not new. In fact this technology was developed in the 1940s by Amoco (now BP)

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by building on the petroleum industry's experimentation with injection techniques. Originally patented in 1953, Halliburton was the first to obtain the license and commercialize the procedure. In the early days, injecting gelled fluid at pressures that were high enough to break or fracture the reservoir rock, and then placing river sand in the crack created, was primarily designed to bypass the near wellbore formation damage caused by the drilling fluids.

As the technology developed, larger and larger fracs were designed, using more sophisticated fluids and stronger proppants so that true enhancement to the native reservoir capability was achieved. Nowadays, fluid technology exists to create gelled fluids from various hydrocarbons bases like oil, diesel, or liquid propane, to water bases, to acid bases, to even super cooled gases. All capable of suspending very high densities of sand or man-made proppants and transporting them down the wellbore to be placed in the fracture created in the reservoir. The specific reservoir characteristics (sands, shales, carbonates, oil or gas, depths, stresses, etc) ultimately determines which design is selected.

At Peyto, every well we drill is hydraulically frac'd. That is because we focus exclusively on the tight gas sands in the Deep Basin. Over the years we have tried different fluids but have come to rely on water based gels as the most reliable and cost effective way to stimulate our reservoirs. Due to the depths and highly stressed reservoirs we're stimulating; we also rely on mostly man made ceramic proppants to hold our fractures open.

Now, instead of large single fractures in vertical wellbores, we're placing multiple fracs along a horizontal wellbore and using one of several options to isolate or divert the various stages.

The idea of combining technologies to get more than the sum of the parts is not unique to the oil and gas industry but perhaps we should not forget the power of such innovation.

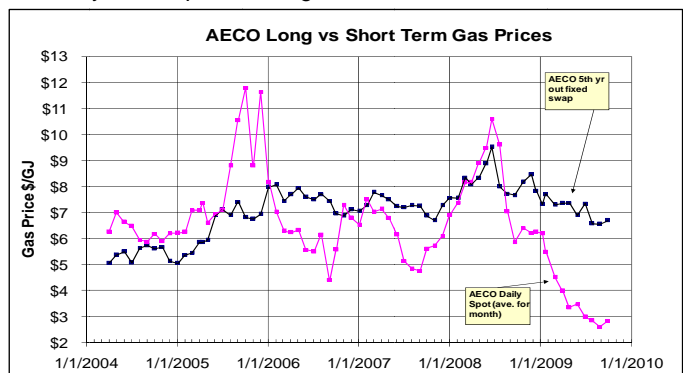
Just as combining technologies like high-intensity ultrasound with ozone technology to eliminate E. Coli in food, or PET scans with CT scans to give a hybrid scan that can properly image cancer cells, horizontal wellbores with multi stage fracture treatments reminds us that sometimes more can be achieved without having to invent something new.

Still, kudos should go out to the likes of Packers Plus and Weatherford and others that are helping execute this combination of old technologies by providing (and in some cases I guess inventing) tools that can be used to do it cheaper and faster.

Sometimes I find it's hard to buy in to the concept that we will eventually run out of non-renewable hydrocarbon fuels. I know it's true at some point, but with continued innovation like we have just seen, it may not be quite as soon as some dire forecasts suggest.

Activity Levels and Commodity Prices

Spot and near term natural gas prices have rallied significantly in the last month. The AECO price on August 28th of \$2.01/GJ had risen to \$3.49/GJ by September 28th, up 74% (not that \$2/GJ was any kind of sustainable price). Future prices are relatively unchanged further out, however, with 5 year out prices rising from \$6.56/GJ to \$6.70/GJ.



The steep contango between \$3 spot and \$6.50 futures is one of the largest we've seen in the last few years as shown in Figure 2.

US natural gas production is finally showing some evidence of the reduced drilling and shut-ins resulting from lower gas prices. As dramatically as the volume has dropped over the last month, if it is driven by shut-ins, it could just as quickly increase. If it is driven more by reduced drilling activity that can't keep up with natural declines in production, then a recovery in supply will take longer to enact. Nevertheless, it is providing the necessary pressure to push both spot and near term futures prices higher.

U.S. Dry Natural Gas Production

Source: CIBC

