

# Peyto Exploration & Development Corp.

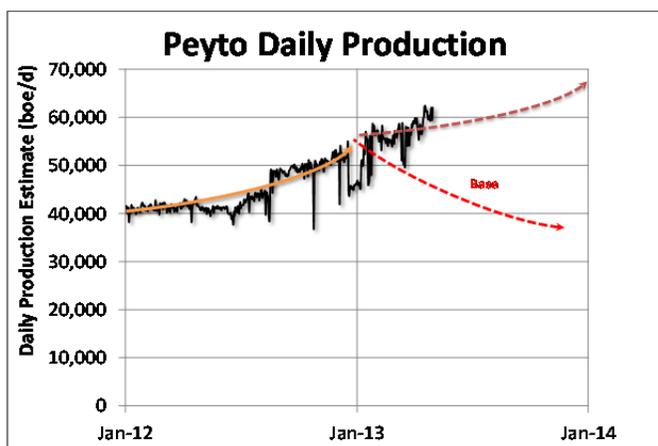
## President's Monthly Report

May 2013

From the desk of Darren Gee, President & CEO

Apparently, some new pens are in order. Back in December 2010 we had pens inscribed marking the 30,000 boe/d production milestone. Since then we've ordered new pens each time we hit the next 10,000 boe/d milestone. With this month, we hit the 60,000 boe/d mark. As a testament to our success I'm amassing quite the collection of writing instruments. Perhaps when we get to 100,000 boe/d we'll have to do something special – like pencils.

Figure 1



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

### Capital Investment\*

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

	2011	Q1	Q2	Q3	Oct	Nov	Dec	Q4	2012	Jan	Feb	Mar	Q1
ONR Acq./other acq.				205			-21	-21	184				0
Land & Seismic	28	3	1	2	4	0	2	6	12	0	1	1	2
Drilling	178	52	23	59	26	30	23	78	211	24	23	28	76
Completions	104	31	14	35	11	15	21	47	127	9	16	16	41
Tie ins	32	8	5	11	8	5	9	22	46	6	11	16	33
Facilities	40	4	3	6	2	3	20	25	37	9	5	4	17
<b>Total</b>	<b>379</b>	<b>99</b>	<b>46</b>	<b>317</b>	<b>50</b>	<b>53</b>	<b>54</b>	<b>157</b>	<b>618</b>	<b>49</b>	<b>56</b>	<b>65</b>	<b>169</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\*

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

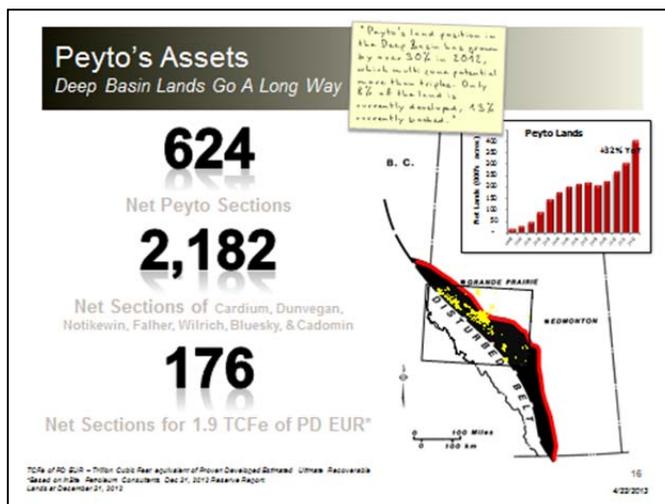
	Q1 12	Q2 12	Q3 12	Q4 12	2012	Jan	Feb	Mar	Q1 13	Apr	May	June	Q2 13
Sundance	35.4	34.3	35.7	36.0	35.4	36.4	40.7	42.1	39.7	43.2			
Kakva	3.8	4.2	3.6	3.1	3.7	3.2	3.1	3.6	3.3	3.2			
Ansell	-	-	2.9	6.8	2.4	9.2	9.0	8.3	8.8	10.2			
Other	2.0	2.8	3.6	3.6	3.0	3.2	3.2	3.6	3.3	3.4			
<b>Total</b>	<b>41.2</b>	<b>41.3</b>	<b>45.9</b>	<b>49.5</b>	<b>44.5</b>	<b>52.0</b>	<b>56.0</b>	<b>57.6</b>	<b>55.2</b>	<b>60.0</b>			

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### Expiring NAV

I believe that Peyto has often been misunderstood in the marketplace with respect to the future potential contained in our Deep Basin land base. Many investors and industry analysts have trouble reconciling our decade-plus drilling inventory assessment from a land base that is just over 400,000 net acres in size. In the past I've attempted to explain how it's the three dimensional nature of the many stacked horizons that provides so much potential. If you add up all the various producing and potential layers of our land base, it grows from around 400,000 net acres, to close to 1.4 million net acres, or almost 2,200 net sections (see Figure 2 from our Corporate presentation). Couple that with the tenure rules in Alberta that allow deeper producing zones, to hold shallow undeveloped rights, and you have a large, very retainable resource that can provide decades of drilling inventory. This is quite a bit different than an areally extensive land base that requires constant drilling and continuous validation. (Further to that, the Alberta Government recently announced it was shelving any efforts force shallow rights reversions held by deeper production.)

Figure 2



A quick survey of company filings this spring reveals that undeveloped land holdings for many producers are down year over year, likely due to expiries. The Annual Information Forms ("AIF") that public companies are required to file by March 31 each year contain some interesting tidbits that provide insight into the future potential of a company's land position (and by proxy, their drilling inventory position) and perhaps even industry issues as a whole.

As you can see in figure 3, the average amount of undeveloped land that is set to expire in 2013 is rather material, averaging 12% or around 180,000 net acres per company. Replacement cost for that land could also be

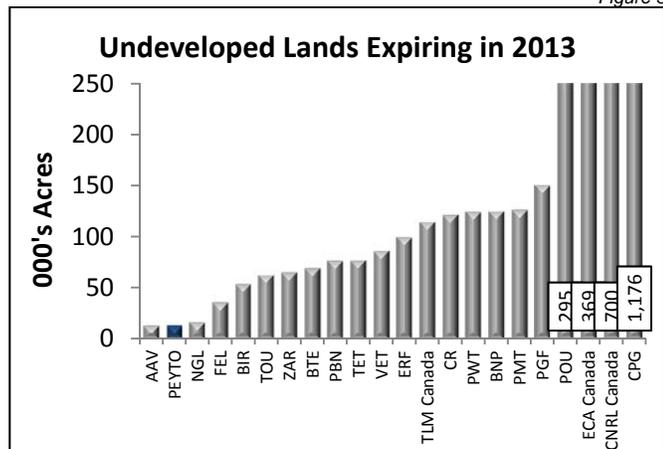
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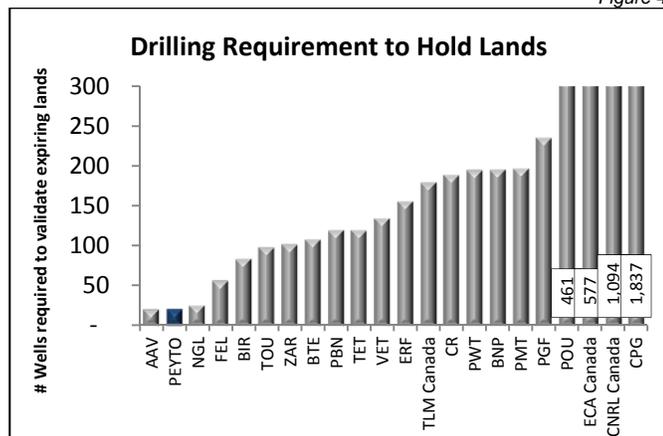
material at bid prices, in Alberta at least, that averaged greater than \$250/acre over the last 3 years. If all these lands were repurchased at \$250/acre that would equal more than \$1B for the provincial coffers.

Figure 3



The other way to look at all this expiring land is to see how many wells would have to be drilled to retain it all. The average number of new wells required to hold the expiring land - 282, (worse case scenario one well per section) would be a lot more than most producers are budgeting to drill this year (Figure 4).

Figure 4



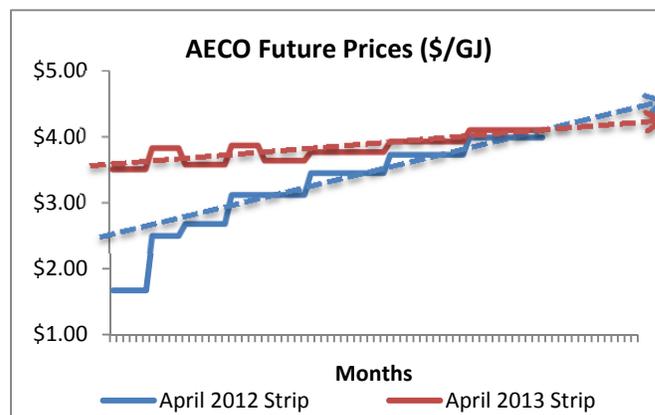
Considering the above, it is worth doing some due diligence on land expiries before blindly crediting some companies with undeveloped drilling inventory that may not be indefinitely in their possession. By contrast, Peyto's stacked Deep Basin land base has very little tenure issues, meaning we can direct drilling to where we want to drill today, rather than where we have to drill.

## Activity Update and Commodity Prices

"Natural gas prices are way better today than last year."

Most people would agree with that statement. When you compare the futures curve today to one from last summer, when spot prices in Alberta had hit a 15 year low, we see that the short term prices are definitely better today, but the long term prices aren't really better (Figure 5 – gasalberta.com). What does that say about the sentiment for Alberta and North American natural gas prices? And how does that flattening of the future price curve change the economic results of new drilling?

Figure 5



The implication of a cap on Alberta gas prices at \$4/GJ (or around \$4.50/MMBTU NYMEX) is that there is sufficiently cheap supplies of North American natural gas that can be brought on for less than that price, in order to satisfy any future demand. This belief comes from the most recent behaviour of the industry to continue to over supply the North American market when prices were falling below \$4/GJ the first time around. Looking at actual costs and profitability, many have shown that the price needs to be higher, but as the strip above indicates, the market doesn't believe it. So the price continues to be range bound between \$2/GJ and \$4/GJ based on historical behaviours to oversupply above \$4 and over consume (last summer's power generation) below \$2.

So how does a range bound price affect our future drilling economics? If we run an average Deep Basin tight gas well production profile, say a Wilrich well in Sundance, against those two gas strips above, the effect is pretty dramatic. The IRR doubles from 20% BT to 40% BT (on \$4.7MM for D/C/E/T) and the value increases between 25-30% just by the improvement in gas price for those first few years. That's because of the shape of the decline profile and the current royalty incentives in place that apply to the first few years of production. So, yes, prices are WAY better today.