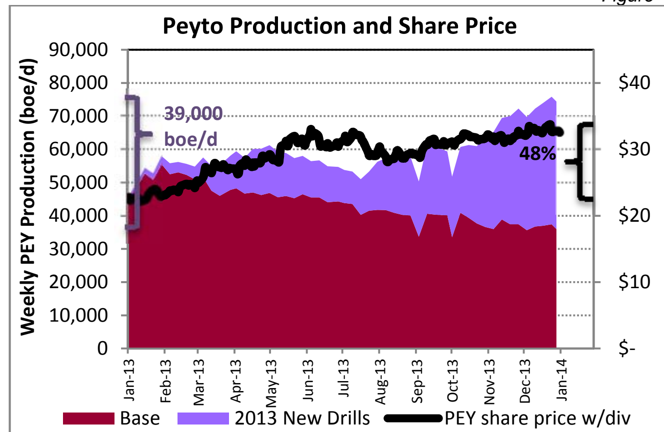
Peyto Exploration & Development Corp.
President's Monthly Report

January 2014 — From the desk of Darren Gee, President & CEO

So much for 13 being unlucky. 2013 was one of Peyto's best years ever. Our largest ever capital program resulted in our largest production build, at almost 39,000 boe/d (75,200 boe/d exit rate, 77,000 boe/d peak rate on Dec. 25). In response, Peyto stock was up over 48% in 2013 when you include the dividend return. See figure 1.

Figure 1



It becomes really exciting then, to consider that 2014 could be even better. With an even larger capital program, we have even grander production results in mind.

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)**

	Q1	Q2	Q3	Q4	2012	Q1	Q2	Jul	Aug	Sep	Q3	Oct	Nov	Dec	Q4	2013
ONR Acq./other acq.			205	-21	184	0	0				0				0	0
Land & Seismic	3	1	2	6	12	2	6	1	1	1	3	1	1		2	12
Drilling	52	23	59	78	211	76	32	32	30	25	86	22	24		46	239
Completions	31	14	35	47	127	41	10	20	19	15	54	15	17		32	137
Tie ins	8	5	11	22	46	33	7	3	5	6	14	5	4		9	64
Facilities	4	3	6	25	37	17	18	7	9	9	24	19	10		29	88
Total	**99**	**46**	**317**	**157**	**618**	**169**	**73**	**62**	**63**	**56**	**181**	**61**	**57**		**118**	**540**

Production*

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

	Q4 12	2012	Q1 13	Q2 13	Jul	Aug	Sept	Q3 13	Oct	Nov	Dec	Q4 12
Sundance	36.0	35.4	39.7	41.6	38.1	42.1	44.5	41.5	43.7	48.1	50.3	47.4
Kakwa	3.1	3.7	3.3	3.0	2.7	2.5	2.7	2.6	2.6	2.5	2.4	2.5
Ansell	6.8	2.4	8.8	10.7	10.3	10.5	9.0	9.9	11.7	14.6	15.4	13.9
Other	3.6	3.0	3.3	2.9	2.4	2.5	2.4	2.4	2.3	4.0	4.5	3.6
Total	**49.5**	**44.5**	**55.2**	**58.2**	**53.5**	**57.6**	**58.6**	**56.5**	**60.3**	**69.2**	**72.6**	**67.3**

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.

To Err Is Human…

"I never made a mistake in my life; at least, never one that I couldn't explain away afterwards."
Rudyard Kipling

They say that we learn more from our mistakes than our successes. But in this business we never seem to talk about the mistakes or problems that happen in pursuit of our goals. Instead we assume that those costly mistakes are always a thing of the past with no mind to future consideration.

Nowhere in a company's investor presentation materials is there consideration that mistakes may happen in the selection of a drilling location or the operations of drilling, completion, tie in, or producing a well. And yet we all know that they happen. And when they happen, it results in higher costs that inevitably erode returns for investors. So it is misleading to suggest that hypothetical economic returns can ever be achieved over and over again without error.

It is more truthful to explain that in the execution of any operation, there are risks. The effective mitigation of those risks is what really differentiates successful companies from unsuccessful ones. As I have said many times in the past, it's not what assets or lands you own, it's what you can do with those assets or lands that determines your success or failure. And a company's ability to mitigate risks and execute operations, will directly impact the return they can deliver to their shareholders.

So while looking back on the activity in the Alberta Deep Basin to see what our competitors are doing, I was interested to note the number of times wells didn't necessarily go as planned. Or put another way, didn't necessarily cost as AFE'd (Authorized For Expenditure). Figure 2 shows the 2013 non-oil well hz spuds (max. possible gas wells), and the number of events classified as either whipstocked & abandon or junked & abandon.

To be fair, there are a few reasons for a whipstock. One may be that the drilling ran into difficulty and the hole needed to be plugged back and re-drilled along a different trajectory. Another could be that a vertical stratigraphic test and log evaluation needed to be conducted before a horizontal lateral could be drilled. Either way, though, the drilling cost is higher than the optimal case where everything goes perfectly. Neither situation is ever captured in type well economics that are modeled on a go forward basis.

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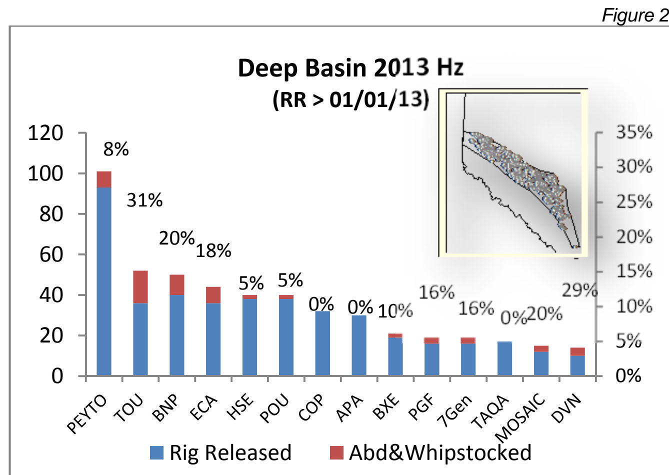
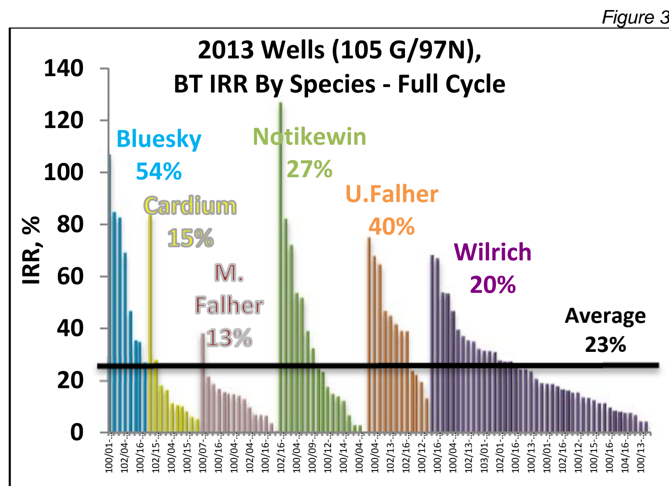
Figure 2



From Figure 2 it's clear that nothing ever goes perfectly and none are really immune to mistakes. Even Peyto had to deal with a few problem wells. And those extra costs factored into the real returns we delivered to shareholders. That is why, rather than report hypothetical future returns we show real actual returns on a "look back" basis for the many plays and areas we're developing. Figure 3 shows our internal economic post mortem evaluation for the 105 wells we drilled in 2013.

Figure 3



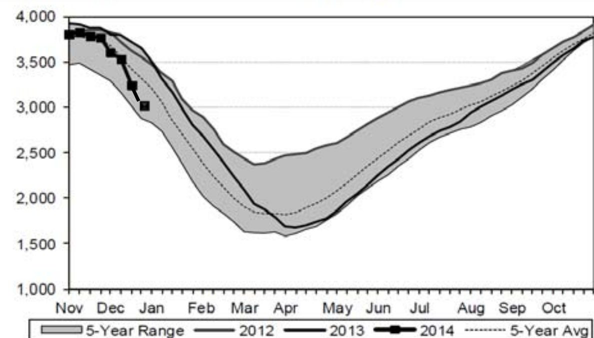
These results include $930,000/well for the land, seismic and facilities capital that was spent in 2013, divvied up per well, to account for full cycle costs. What is interesting to note is the wide distribution of returns. Not only is there actual variability of production performance and reserve recovery, there is also variability in cost, resulting from varying success in the execution of operations. This distribution is true of all plays, despite the template economics you so often see. Wells never cost exactly the same and the results are never exactly the same. Which is why real investor returns are not about what *potentially* could happen but about what *actually* happens, after those operations are executed. And why those, like Peyto, that are proficient in the "doing", rather than the "talking", are the ones making those real returns.

One other little take away from Figure 3 is that out of 105 wells, only 2 wells will not make back their capital. Which is just another reason why we like the Deep Basin, for it's low risk repeatable returns. You definitely won't get those odds in Vegas.

Activity Levels and Commodity Prices

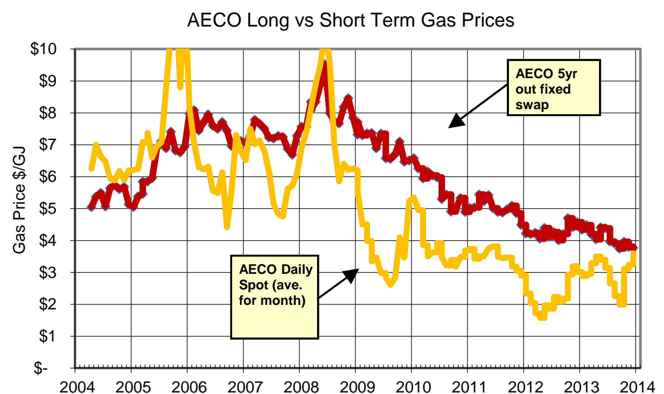
Cold winter and big natural gas storage draws caused remaining storage levels at the end of 2013 to be much lower than average (see Figure 4). This has caused near term natual gas prices to rally.

Figure 4 *Source:Haywood*



Interestingly, farther out future gas prices have not rallied. In fact, the AECO price 5 yrs out is the lowest it's been in over a decade and is even lower than current prices (see Figure 5).

Figure 5



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