Hitting our stride.

PARAMOUNT ENERGY TRUST
Canada’s only 100% natural gas royalty trust

PARAMOUNT ENERGY TRUST (PET) is a natural gas focused Canadian energy royalty trust which commenced operations in February 2003. PET’s operating practices are conservative, targeting maximum distributions and premium after-tax returns at an acceptable risk for all stakeholders.

When the Trust was formed, it acquired the vast majority of the shallow natural gas properties in Northeast Alberta owned by Paramount Resources Ltd. Those assets are well suited to a Trust. They are characterized by long production histories, a predictable production profile, high field netbacks, minimal ongoing capital requirements and strategic infrastructure ownership. PET operates over 90 percent of this extremely focused asset base, which permits hands-on asset management of capital programs, operating costs, debt and natural gas price volatility.

**PET will grow through prudent investments in three areas:**

- **Optimizing** the value of its asset base through low-risk exploitation and infrastructure management;
- **Proactively** managing its extensive undeveloped land base;
- **Pursuing** value-adding corporate and property acquisitions for both maintenance of production and growth.

PET’s state of the art trust structure features high management ownership and no external management fees or contracts. This directly aligns management with Unitholders in a common objective – receiving superior returns from an investment in the Trust.

*PET’s Trust Units are listed on the Toronto Stock Exchange under the symbol PMT.UN.*
Managing the Trust as a low-risk investment that delivers high returns.
What differentiates Paramount from the numerous other trusts?

PET is the only Trust to be created through a dividend-in-kind from a parent corporation – and this approach had several advantages. The formation of PET was virtually seamless from an operations perspective, and the technical professionals who have worked on the properties came with us. From an investor’s standpoint, it was a closed system where all shareholders of Paramount Resources Ltd. (PRL) became PET Unitholders.

Our asset base is also rather unique. PET is currently the only 100% gas-focused Canadian royalty trust. Further, virtually all of our assets were originally located in a concentrated geographic area. That presents a lot of opportunities for cost control and operating efficiencies. The nature of our current properties, particularly the predictability, is well suited to a trust – long production histories, predictable production profiles, high field netbacks, strategic infrastructure ownership and the fact that they require modest capital investment to mitigate production declines. All of those characteristics have allowed PET to maintain a very high level of distributions since inception.

We also have a state of the art trust structure. The high management ownership coupled with completely internalized management with no fees or contracts creates perfect alignment between management and the Unitholders. The trust-on-trust architecture has proved to be particularly valuable in lending maximum efficiency in areas such as taxation and acquisitions, both property and corporate.

Why the focus on natural gas?

The natural gas focus was the legacy of PET’s then-parent corporation, PRL. The assets that we acquired were discovered and delineated by PRL in its formative years 25 years ago. Many of the technical staff managing the Trust’s assets have worked on these properties for years, so we have substantial technical expertise in shallow natural gas.

We are unlikely to remain 100% natural gas focused forever, but there are certain attributes of that commodity, besides familiarity, that we find attractive. Much of the incremental energy demand in North America is based on gas-fired capacity, which is environmentally-friendly relative to alternative energy supply feedstocks. Furthermore, gas is in increasingly short supply on the continent with production from new wells declining more rapidly – and new discoveries more difficult to make. Unlike oil, gas remains a North American rather than a world-wide commodity. In short, scarcity breeds opportunity. And opportunity coupled with expertise and experience is a powerful advantage.

PET stepped up to be the spokesperson for gas producers during the gas over bitumen issue? How did that come about?

The motivation for industry leadership on this issue resulted from the material impact on our Trust and PET’s culture of accountability. PET was the publicly traded entity that
The challenges of the gas over bitumen issue have been greater than any team should ever have to face, let alone in its first year of existence. But it has strengthened our resolve to succeed — and it also put a public face on PET and its people that is perhaps greater than almost any of the established trusts.
was most affected by this issue as the vast majority of our assets fall within the Athabasca Oil Sands Area, and almost 50 percent of our production was initially targeted for shut-in. The magnitude of the impact on our Trust dictated ongoing comprehensive public disclosure as the issue unfolded. The scale of this issue, the manner in which the Alberta Energy and Utilities Board has approached it with disregard to the principles of fairness and reason and the lack of responsiveness to our concerns by the Government of Alberta, left us with no alternative but to take a multi-faceted approach to this issue, including public communication.

While PET has often been quoted as the spokesperson for the gas producers, we continue to work closely with a consortium of numerous gas and bitumen producers who have been remarkably united in their approach to this issue.

Accountability to PET stems from continually asking the question, “What more can we do to achieve the results we desire for Unitholders?” The gas over bitumen issue has brought that aspect of PET’s culture into clear focus. We are committed to provide our Unitholders nothing less than our total commitment to preserving and enhancing the value of their investment. As part of that accountability, we realized early that our Unitholders would be better served through industry alignment so that was initiated.

**What impact has the gas over bitumen issue had on the Trust?**

Our management, technical, operational and administrative team became a team in the true sense of the word. It is often said that a group needs to go through adversity before it can truly function as a team. PET saw more than its fair share of adversity in 2003 and early 2004. The complexities of our structuring process led to a protracted birth for the Trust – and then, as soon as we got out of the gate, the gas over bitumen issue erupted.

Technically, our detailed knowledge of the properties specifically under review in the gas over bitumen issue has increased exponentially in a very accelerated time frame. Knowledge breeds opportunity and PET will be proactive in generating these opportunities.

**How would you describe your management team?**

Our Trust was formed as a hybrid of management and staff from two predecessor companies – and that brought the perfect mix of something old and something new. We benefited from both the comfort of continuity and familiarity with the assets, as well as the rejuvenation of a new and vibrant environment. Our team has a lot of experience, and there is significant involvement by our Board of Directors in the management of the Trust.

As a team, we are looking for opportunity to be innovative and creative. If I look a little deeper, I would say that everyone has tremendous perseverance, and there is respect and camaraderie. We are always mindful of one thing – accountability to all stakeholders – our Unitholders, employees, partners, suppliers, the community and the environment.

**Every company has a “personality” – a certain style of doing business. What is the Trust’s style?**

We have a very strong focus on individual accountability at every level in PET. Everyone’s opinion matters. It is important that we always focus on adding value for our fellow Unitholders, and that is best accomplished in a dynamic environment of opportunity, individual responsibility, flexibility, creativity, respect and fun.

**What is the major weakness of the Trust?**

In hindsight, with the gas over bitumen issue in the rear-view mirror, I would say that it is a lack of
geographic diversity in our asset base. But that is something we have already moved on to improve through two acquisitions. We will be looking to add assets that still fit well with our technical expertise, but provide more geographic diversity. With that, we may expose ourselves to some oil production, which may provide some balance in terms of commodity price cycles.

**You have a reserve life index under six years, which is low compared with other trusts. Is that a concern?**

Rather than a concern it is a mathematical fact. We believe that our initial assets were ideally suited for a Trust due, in part, to their predictable production profile, high netbacks and particularly that the production declines can be mitigated with modest capital investment. The Northeast Alberta assets have consistently outperformed the production predicted by the independent engineering reports on which the reserve life index is calculated.

In a present value sense, a short reserve life is an advantage in two pools of equal size. The faster the cash flow comes, the more it is worth in real dollars. We are, however, mindful that we must constantly be looking for investment opportunities in our existing asset base and high quality assets to add to our portfolio to offset the declines in our base properties.

**Distributions are uppermost in the minds of investors? What are your plans for maintaining distributions?**

We continue to focus on every step in the value equation to absolutely maximize total return to Unitholders, including distributions. We concentrate on production optimization, cost control, land stewardship and accretive acquisitions. What we cannot control are gas prices and the dramatic effect that they have on the cash flow of a heavily gas-weighted Trust. We do, however, manage gas prices through our proactive and opportunistic hedging and marketing programs – and this is a major focus area for us.

In a commodity-based trust sector such as ours, investors need to think in terms of whom can best maximize distributions rather than maintaining them.

**What risks do investors face?**

The risk of gas markets is by far the greatest risk to our future cash flow. We believe that the risk of the gas over bitumen issue to PET has now been fully quantified and assessed as to the recommendations of the AEUB Staff Submission Group.

Other significant risk factors related to PET include interest rates and foreign exchange rates. None of these risks, other than gas over bitumen issue and our weighting to gas, are unique to PET.

**Can you give investors a sense of what Paramount will look like in one, even five years?**

We are here to grow this Trust. While 2003 had more than enough distractions, we have nevertheless shown an ability to consummate accretive transactions. That will not stop. With the ever-growing number of royalty trusts in the sector, there are likely to be some that exit and some that become consolidators of assets. We see ourselves as the latter.

Five years is an eternity in this industry. If we could be more than twice as big with a market cap of more than $1 billion much sooner – that would be great. Adding value for Unitholders will remain our driving force.

**What is your biggest challenge?**

The Canadian oil and gas industry, and its royalty trust sector in particular, is extremely competitive. There are more players than good opportunities. One must remain diligent, persistent and creative to continue to add value and access capital. We are up for the challenge.
Value is always uppermost in our minds. Every day, our efforts, whether in our head office or in the field, are concentrated on increasing value in the Trust for our Unitholders. It is a philosophy, but it is also a concrete way of doing business. At PET, we empower our employees and the benefits have been far-reaching. Our people have a level of dedication and professionalism that continues to yield opportunities, efficiencies, cost reductions – and added value for our Unitholders. We have a culture of execution, driven by strategies, developing ideas with rigorous attention to detail then translating these ideas into results. We call it the value equation, and it is a major focus in everything we do.

**Marketing**

Proactive management of the price side of the revenue equation is inclusive in our business process.

Our opportunistic hedging strategy utilizes numerous predictive tools.

Price management tools vary depending on where we are in a particular commodity cycle.
unitholders

Maximizing distributions is a top priority.

PET's gas focus gives investors a "pure play" on natural gas prices.

The strength of our asset base allows for a high level of both distributions and payout ratio due to high netbacks and low capital requirements.

Completely internalized management means no fees or contracts.

The Distribution Reinvestment Plan (DRIP) provides Unitholders the largest discount to market in the sector.

Two-way communication directly with Unitholders is an important part of our role as managers of the Trust.

head office

Employees are compensated through salary, bonus and Unit ownership or incentive options, which is part of our empowerment philosophy.

Our staff complement is very lean with general and administrative expenses at $0.15/Mcf.

We are committed to improving our efficiencies through technological advancements. We are moving toward a paperless office environment.

Significant tax planning and structuring are integral to all activity.

Ongoing exploitation programs on our existing properties continue to add value with production and reserve additions.

Proactive land stewardship is driven by the risk-reward profile of opportunities in our asset base.

acquisitions

Our unique trust-on-trust structure provides flexibility for both corporate and property acquisitions.

Our team is dedicated to negotiating accretive acquisitions. When assessing transactions, we focus on growth in cash flow per Unit and net asset value per Unit.

We cultivate strategic alliances with exploration and development companies which aid in effectively searching out strategic acquisitions.

Our land stewardship program for PET's extensive undeveloped acreage base lends flexibility to the acquisition program.
PET operates over 90% of its production at an average wellhead gas price of $9.79/Mcf

**West Side**
- Including Marten Hills
  - Production: 47 MMcf/d
  - Reserves: 82 Bcf
  - Average Working Interest: 84%
  - Undeveloped Land: 129,000 net acres
  - Infrastructure: six operated plants

**East Side**
- Production: 46 MMcf/d
- Reserves: 74 Bcf
- Average Working Interest: 82%
- Undeveloped Land: 201,000 net acres
- Infrastructure: four operated plants

**Southern Alberta**
- Acquired November 2003
  - Production: 2 MMcf/d
  - Reserves: 2.5 Bcf
  - Average Working Interest: 38%
  - Undeveloped Land: 10,300 net acres
  - Infrastructure: two operated compressor stations

**Marten Hills**
- Acquired February 2004
  - Production: 7.4 MMcf/d
  - Reserves: 8 Bcf
  - Average Working Interest: 83%
  - Undeveloped Land: 23,700 net acres
  - Infrastructure: one operated plant

**Strategic Assets**
While current average daily production is in excess of 90 MMcf/d, up to 16 MMcf/d of PET's gas production is at risk of shut-in as a result of pending AEUB gas over bitumen decisions. Our firm stance on the necessity of decision-making on gas over bitumen demand required an extensive technical evaluation of a significant percentage of our asset base. This led to an intimate understanding of our properties and their potential now and for the future. Our knowledge will translate into maximum recovery of value from shut-in gas and strategic use of assets today and tomorrow.
LIEGE
Paramount Resources Ltd. employed innovative air drilling technology in the severely under pressured Grosvenor reservoir, leading to the discovery of natural gas on the West Side in 1979. Cumulative production to date is over 200 Bcf and the LIEGE field still produces close to 10 MMcf/d net to PET.

LEGEND
The Trust's largest producing property at over 17 MMcf/d, the Legend property commenced production June 29, 1984. Cumulative production to date is in excess of 200 Bcf. Infrastructure is extensive with one gas plant and eight compressor stations totaling 18,500 horsepower. An additional 2.5 MMcf/d of the Trust's East Legend production is also processed through this gas plant.

SALESKI
Production continues from the original Devonian Grosvenor pools discovered and developed in the mid-90s. Saleski has the lowest rate of decline of the Trust's properties, with 9.4 Bcf of reserves and a seven-year reserve life index.

ELLIS
Discovered in 2002 by Paramount Resources Ltd., PET acquired this property in March 2003 as a separate transaction from those associated with the Trust's formation. Current production of over 7.5 MMcf/d provides the highest operating netback in the Trust's portfolio.

CHARD
The Chard discovery well was drilled by Paramount Oil and Gas in 1976, following up two dry holes in a three well farm-in program. Production commenced in November 1982, representing PRL's first production from the East Side.

CORNER
Developed in the mid-90s using 3D seismic bright spot technology, Corner was PET's second largest producing property at over 12 MMcf/d prior to the September 1, 2003 gas over bitumen shut-in.

KETTLE RIVER
Low production declines that continually outperform expectations characterize the Kettle River property. Production is primarily from the upper Cretaceous Clearwater formation since the first gas over bitumen shut-in at Sorrento in May 2000.

LEISMER
Approximately 8 MMcf/d is currently producing through the meter station at Leismer, including new production from the upper Clearwater and Grand Rapids formations. One PET-operated gas plant processes gas gathered from more than seven towns with three booster compressor stations reducing pipeline pressures for optimal reserve recovery.

COLD LAKE
As PET's most southerly property in Northeast Alberta, Cold Lake provides opportunities for capital spending year-round. Production of 6 MMcf/d flows through a combination of PET-owned and operated compressor stations as well as third party processing facilities.

KIRKPATRICK
Acquired through the recent acquisition of Epon Exploration Ltd., Kirkpatrick is PET's most significant Southern Alberta property. A recent upgrade to our 100% owned and operated compressor station will optimize gas production from Cretaceous-aged Belly River and Viking reservoirs.
What makes PET’s assets “high quality”?
It is common in the trust industry to hear references to businesses or groups of assets being “trustable” or well-suited for inclusion in a trust’s portfolio of assets. There are a number of attributes of PET’s present suite of assets that justify just such a description.

Predictable production profile
Trust Unitholders count on stable monthly distributions. The long, stable production history of our Northeast Alberta properties provides a solid basis for PET to predict the performance of our assets. In some cases, wells have been on production over 20 years. We tend to get very few surprises in the production performance of our properties.

High netbacks
Trust Unit distributions are entirely a function of cash flow. The more cash that is left over after royalties and operating costs, which is the netback, the more cash there is for distributions. Our Northeast Alberta gas properties produce some of the highest netbacks in the Western Canadian sedimentary basin.

In 2003, PET’s average netback was $4.33 per Mcf, or almost $26.00 per barrel of oil equivalent, and represented 67 percent of the gross selling price. Our sweet, shallow gas requires little processing or other special handling and so operating costs are very reasonable. The geographic concentration of these assets creates many synergies in PET’s operations through centralized field operations and economies of scale.

Opportunity-rich with modest capital requirements
The oil and gas industry is by nature capital intensive. Everything we do is expensive and more so all the time. This issue is compounded in a trust structure where capital expenditures become a drain on distributable income.

Capital is not just required for new assets. All oil and gas production declines naturally and capital investment is required to mitigate or arrest declines. Yet not all properties require equal reinvestment. In the case of PET’s assets, we are able to offset a significant portion of annual natural production declines with relatively modest capital reinvestment. Historically we have been able to bring on new production in our core areas for an average of $2 to $2.5 million per MMcf/d, or $10 to $15,000 per BOE/d. In addition, annual reinvestment of 10 to 20 percent of cash flow has reduced annual average decline rates to 6 percent. Our assets provide a very solid base for sustainability and growth.

High working interests, operatorship and infrastructure ownership
Another key component of predictability in the oil and gas industry is control. An historic characteristic of this industry has been the sharing of costs and risk with other entities through the joint venture. While this is an effective risk-management strategy, the potential downside is that projects tend to be controlled by the operator and/or those with the largest interests. Given the predictable nature of PET’s assets, the low-risk nature of the development opportunities and the low capital requirements, we benefit greatly from having an average working interest of over 80%
and by operating over 90 percent of our production. PET is able to control the nature, timing and execution of investment in virtually all of its operations. In addition, our significant infrastructure ownership allows for the optimal configuration of all facilities for further cost minimization. Last but not least, the high average working interest means that our share of premium netbacks is not diluted and our people are focused on opportunities that will impact Unitholders.

Focus

PET presently produces one commodity and more than 95 percent of it’s production in one geographic region. This extreme focus allows for tremendous expertise to be amassed and translated into future gains. It also allows for a very efficient organization. PET’s average general and administrative expense in 2003 was only $0.15 per Mcf. With only 85 staff in total, each person at our Trust accounted for an average of almost $1.5 million of distributable income. We are proud of that level of productivity. As we grow, we think we can achieve even greater efficiencies.

Reserve life index

Reserve life is an important aspect of an investment in any trust. At PET, we are cognizant that our reserve life index (RLI) is lower relative to many of our peers. PET’s 2003 year-end independent engineering report suggests a RLI of 5.1 years. That indicates that our reserves would last 5.1 years based on consistent, non-declining production of 29 Bcf per year, which is our production forecast for 2004, and PET’s reserve base of 150 Bcf. Further, it implies an annual production decline of approximately 20 percent.

The situation is much more complex. Reserve life is not a static characteristic of any particular reservoir and furthermore it does not describe the quality of a Trust’s asset base. Operating decisions and capital investment in a particular pool can change both reserves and production rates, and therefore reserve life. What is critical is to optimize the capital investment and production profile, to continually optimize the value of each property in order to maximize distributions to Unitholders over the producing life of the asset. This optimization is central to PET’s business plan.

Factors behind PET’s RLI

▲ PET’s strategic decision to focus on natural gas was based on the commodity’s attractive economics, future prospects for North American natural gas markets and the greater availability of prospects in western Canada when compared to oil.

▲ In general the optimal development plan for natural gas assets, particularly shallow natural gas properties, results in a shorter RLI than for oil assets. This is related to the lower average cost to add gas production and the high component of fixed operating costs associated with shallow gas assets.
All prudent producers strive to achieve the optimal present value of future cash flows on each property. Capital investments to accelerate production and capture of reserves can increase the net present value (NPV) of a property; however, the estimated reserve life will be shortened.

Due to the nature of PET’s Northeast Alberta assets, the production declines suggested by the independent engineering report can be mitigated by modest capital investment. PET has been able to achieve production additions for less than $3 million per MMcfd, highlighting the efficiency of the capital program. By comparison, the costs to mitigate declines on longer reserve life properties are often greater or, in many cases, the opportunities do not exist at all. Risk of investment must be factored in as well.

In the Canadian royalty trust sector, production is split almost equally between oil and gas on a barrel of oil equivalent basis. Therefore, with PET’s assets comprised of 100 percent shallow natural gas, it follows that PET has a shorter average RLI than the more oil-weighted peer group.

**Typical 1.75 Bcf PET Gas Pool**

NPV@10% (000$) including upfront capital for production additions

PET is focused on the rigorous analysis of its development plans for individual properties in order to optimize the value of each asset for PET Unitholders. Optimization of individual properties is a key component of PET’s business plan and its application is integral to the Trust’s commitment to maximizing distributions.
Acquisitions

Oil and gas properties are a declining asset. Without capital investment reserves, production and cash flow will decline. This is inconsistent with the preeminent desire of an oil and gas royalty trust to sustain or increase distributions to Unitholders. Consequently, acquisitions are the life blood of the sector. In today’s highly competitive marketplace good acquisitions are very difficult to do. As a result PET has instituted detailed criteria and developed multiple strategies to source and consummate effective acquisitions of properties or corporations.

Preferred Criteria

Above all else, in order to have a positive effect on Unitholder value, as is PET’s goal, acquisitions must be accretive to cash flow and net asset value on a per unit basis. Growth for growth’s sake is pointless if it comes at the cost of ultimate Unitholder dilution. The competition for and cost of the current acquisition market mean that acquirers must look diligently for hidden opportunities for accretion such as development upside and tax structuring.

PET has a full-time team dedicated to the screening of acquisition opportunities. We prefer opportunities with the following characteristics:

▲ Natural gas focused assets
▲ The majority of the recognized reserves are ideally in the Proved Producing category
▲ Properties with exploitation opportunities and development upside
▲ Assets in which PET’s technical teams have particular expertise (ie. shallow to medium-depth natural gas, geological play understanding, etc.)
▲ Operated properties with high working interests allow for greater control of costs and project timing as well as opportunities for synergies and consolidation
▲ Opportunities must fit within the Trust’s financing capacity (debt and/or equity)
▲ PET is not averse to properties with shorter reserve lives as the sales process on them is often less competitive

Strategies

In order to gain a competitive advantage in the acquisition & divestiture (A&D) market, PET employs multiple strategies including:

▲ Seeking consolidation opportunities in its core areas of operation in Northeast and Southern Alberta
▲ Sourcing new operating areas to provide geographic diversity to the asset base and year round access to spread out the Trust’s capital expenditure program
▲ Forming strategic alliances with exploration and production companies which may allow for preemptive acquisitions which might be less competitive than a public sales process
▲ Cultivating relationships with all players in the A&D market including property brokers, investment bankers and A&D groups in other companies.
A team dedicated to excellence.

Management
Clayton H. Riddell
Chief Executive Officer
Susan L. Riddell Rose
President and
Chief Operating Officer
Cameron R. Sebastian
Vice President, Finance and
Chief Financial Officer
Gary C. Jackson
Vice President,
Land, Legal and Acquisitions
Kevin J. Marjoram
Vice President,
Operations
Brett Norris
Vice President,
New Ventures & Geoscience
Myra Jones
Corporate Secretary

Directors
Clayton H. Riddell
Chief Executive Officer and
Chairman of the Board
Paramount Energy Operating Corp.
Susan L. Riddell Rose
President and
Chief Operating Officer
Paramount Energy Operating Corp.
Karen A. Genoway
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