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Devon Energy Corp. (DVN)

Q3 2025 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Devon Energy's Third Quarter 2025 Conference Call. At this time, all participants are in listen-only mode. This call is being recorded.

I'd now like to turn the call over to Mr. Chris Carr, Director of Investor Relations. You may begin.

Christopher Carr
Director-Investor Relations, Devon Energy Corp.

Good morning and thank you for joining us on the call today. Last night, we issued Devon's third quarter earnings release and presentation materials. Throughout the call today, we will make references to these materials to support prepared remarks. The release and slides can be found in the Investors section of the Devon website.

Joining me in the call today are Clay Gaspar, Chief Executive Officer; Jeff Ritenour, Chief Financial Officer; John Raines, SVP, Asset Management; Tom Hellman, SVP, E&P operations; and Trey Lowe, SVP and Chief Technology Officer.

As a reminder, this call will include forward-looking statements as defined under US securities laws. These statements involve risk and uncertainties that may cause actual results to differ materially from our forecast. Please refer to the cautionary language and risk factors provided in our SEC filings and earnings materials.

With that, I'll turn the call over to Clay.

Clay M. Gaspar

President, Chief Executive Officer & Director, Devon Energy Corp.

Thank you, Chris. Good morning, everyone, and thank you for joining us. Let's begin with slide 2. With outstanding execution and innovation from every part of our organization, Devon delivered another outstanding quarter. I'm proud of our team's performance. We exceeded the midpoint of guidance on every key metric including production, operating costs and capital.

These results mark our strongest performance of the year, highlighting the exceptional quality of our assets and our unwavering commitment to operational efficiency and cost control. Building on this performance, we continue to advance our business optimization plan, firmly on track to generate an incremental $1 billion of annual pre-tax free cash flow.

As we enter the fourth quarter, we have already achieved more than 60% of our target, underscoring both the effectiveness and urgency of our approach. These initiatives go beyond cost reductions. They are fundamentally reshaping our business by enhancing margins and boosting capital efficiency across our portfolio.

The output of these compounding efforts show up in our strong preliminary outlook for 2026, which Jeff will discuss in more detail. Despite persistent macro headwinds, these achievements directly contributed to our resilient free cash flow, as we returned over $400 million to shareholders in the quarter and retired $485 million of debt, demonstrating our focus on delivering meaningful value to our shareholders.

Beyond business optimization, we continue to unlock significant value throughout our portfolio. While getting into the details on a later slide, our teams have capitalized on a multitude of opportunities to drive additional value for the organization. Collectively, these achievements reinforce Devon's momentum and position us exceptionally well for the remainder of 2025 and into 2026.

Let's flip to slide 4 and take a deeper look at the quarter. Our relentless focus on production optimization continues to drive our outperformance. With oil production exceeding the midpoint of guidance by 3,000 barrels per day, the outstanding efforts of our teams to reduce artificial lift failure rates and improve workover efficiencies resulted in a 5% reduction in operating costs compared to the start of the year.

Additionally, effective cost management drove our capital investment 10% below the first half run rate. These accomplishments, combined with other ongoing initiatives, led to robust free cash flow of $820 million in the third quarter and enabled us to deliver substantial cash returns to our shareholders.

Moving to slide 5, our consistent track record of disciplined execution and tireless pursuit of capital efficiency is evident. Quarter after quarter, we drive meaningful improvements to our outlook. This momentum is reflected in our updated guidance, where we've raised our full year production expectations every quarter this year while reducing capital by $400 million since our preliminary guidance. These are not isolated wins. They result directly from our steadfast commitment to operational excellence, our culture of continuous improvement, and a rapid adoption of leading-edge technologies across our portfolio.

Now, looking at slide 6, this continuous improvement is also resulting in top-tier performance versus our competitors. Our well productivity stands in the upper echelon of our peers, reflecting the strength of our asset portfolio and the execution of our teams across every basin. On the right-hand side, our disciplined approach to capital allocation is evident in our industry-leading capital efficiency, setting us apart in a highly competitive space.

These achievements highlight the power of our advantaged portfolio and the rigor of our capital allocation process, and the ability of our people to drive superior results. And with our extensive inventory, we are well-positioned to continue this strong performance moving forward.

Turning to our business optimization initiative highlighted on slide 7, our teams are outperforming expectations and delivering results well ahead of schedule. We have already captured more than 60% of our ambitious $1 billion target. When we originally launched this initiative, our focus was – for year-end 2025 was $300 million in value uplift. As shown on the left side of the slide, we are on pace to double that milestone this year alone.

This exceptional progress is highlighted this quarter by our significant progress in capital efficiency and production optimization on the right side, and we are fully confident in our ability to deliver these substantial cash flow improvements as we advance towards 2026. Driving this rapid progress is our outstanding execution.

With greater visibility and confidence in our 2025 full year production volumes, we anticipate a sustainable increase in free cash flow of $150 million resulting from incremental 20,000 Boe per day above our initial baseline when this initiative began. This reflects further acceleration from our outlook from last quarter, highlighting the urgency of our efforts.

When we announced the plan in April, we recognized that the market wouldn't immediately price the aspirational $1 billion of incremental free cash flow in our share price. We knew we would have to earn it. While the plan is still in flight, I'm encouraged that Devon's stock is starting to feel a bit of relative appreciation to our peers. That said, I believe that we have much more ground to gain, and I look forward to earning that value in time.

Slide 8 showcases key examples of the initiatives our teams are pursuing to meet targets in each category. These represent some of the most impactful efforts currently underway. As our teams proactively implement these initiatives, we remain confident in our ability to achieve our targets and maintain clear line of sight to our objective.

Turning to slide 9, I'd like to highlight several portfolio optimization actions we've taken on this year, which are delivering an uplift of over $1 billion to enterprise NAV. Importantly, these gains are in addition to the improvements through our ongoing business optimization initiatives. Early in the year, we signed an agreement to dissolve our joint venture in the Eagle Ford, giving us control of our development and the ability to reduce well costs and significantly enhance returns.

In Q2, we completed the sale of the Matterhorn Pipeline and subsequently acquired the remaining interest in Cotton Draw Midstream. Last quarter, we executed two strategic gas marketing agreements that expanded our natural gas sales portfolio into premium markets. In Q3, we acquired approximately 60 net locations in New Mexico for $170 million, increasing our runway of high-return opportunities in Delaware.

And finally, we've benefited from the WaterBridge IPO, which now provides a public marker for our investment, valued at greater than $400 million. These actions showcased our team's initiative and strategic thinking to create shareholder value. As we execute our business plan, we will seek further opportunities to optimize capital allocation, efficiency, costs and asset mix. We remain committed to continuous improvement, innovation and technological leadership, taking decisive steps to strengthen our operations and deliver strong shareholder returns.

With that, I'll hand the call over to Jeff.

Jeffrey L. Ritenour

Executive Vice President & Chief Financial Officer, Devon Energy Corp.

Thanks, Clay. Turning to slide 10, Devon delivered another quarter of strong financial results. In the third quarter, we generated operating cash flow of $1.7 billion. After funding capital requirements, free cash flow totaled $820 million. This robust free cash flow generation enabled us to return significant value to shareholders, including $151 million in dividends and $250 million in share repurchases. We remain committed to our capital allocation framework, balancing high-return investments with substantial cash returns to shareholders.

Moving to slide 11, Devon's financial strength and liquidity continue to set us apart. We ended the quarter with $4.3 billion in total liquidity, including $1.3 billion in cash. Our net debt-to-EBITDA (sic) [net debt-to-EBITDAX] (00:10:13) ratio remains low at 0.9 times, underscoring our commitment to a strong balance sheet. As part of our disciplined capital return framework, we accelerated the retirement of $485 million in debt this quarter, completing the repayment ahead of schedule and generating approximately $30 million in annual interest savings.

With this action, we've now achieved nearly $1 billion towards our $2.5 billion debt reduction target. Looking ahead, our next maturity is our $1 billion term loan due in September of 2026. We remain focused on executing our debt reduction strategy and maintaining the financial flexibility that supports Devon's value-enhancing growth.

Beyond debt reduction, we also used cash on hand to acquire all outstanding noncontrolling interest in Cotton Draw Midstream, saving $50 million in annual distributions, and secured additional resources in the Delaware, as Clay mentioned earlier. These timely transactions reinforce the value of maintaining an investment grade balance sheet and ample liquidity. As we approach 2026, we're determined to accelerate our operational momentum, prioritizing per share growth, maximizing free cash flow and making targeted reinvestments for sustained success.

Slide 12 highlights the key attributes supporting our strong preliminary outlook for 2026. Given ongoing commodity price volatility, we're taking a disciplined approach to capital planning. We intend to maintain consistent activity levels to keep production around 845,000 Boe per day, with oil production at approximately 388,000 barrels per day. With macroeconomic uncertainty and an appearance of a well-supplied oil market, we do not plan to add incremental barrels to the market at this time.

To support this production profile in 2026, we anticipate capital investment of $3.5 billion to $3.7 billion, a reduction of $500 million compared to our maintenance capital levels just one year ago. Importantly, we can fund this program below $45 WTI, including the dividend, providing significant flexibility. This disciplined plan positions us to generate strong free cash flow at current prices and deliver a free cash flow yield that exceeds the broader market.

Regarding free cash flow allocation, our financial framework provides flexibility to deliver market-leading cash returns to shareholders and achieve our debt reduction objectives. We will continue to target share repurchases of $200 million to $300 million per quarter and will retain free cash flow beyond share repurchases on the balance sheet to efficiently reduce net leverage. Complete 2026 guidance will be provided on our February call after the budget is finalized with our board.

In summary, Devon has all the key attributes to thrive in today's environment and create value well into the future. Our high-quality portfolio provides a solid foundation, while our disciplined strategy keeps us focused on growing per share value and generating free cash flow. With a strong balance sheet, we're positioned to deliver lasting value and confidently navigate whatever the market brings.

With that, I'll now turn the call back over to Chris for Q&A.

Christopher Carr
Director-Investor Relations, Devon Energy Corp.

Thanks, Jeff. We'll now open the call to Q&A. Please limit yourself to one question and a follow-up. With that, operator, we'll take our first question.

QUESTION AND ANSWER SECTION

Operator: Thank you. Our first question comes from Neil Mehta with Goldman Sachs. Neil, please go ahead. Your line is now open.

Neil Mehta
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Thanks so much for the visibility as we look into 2026, and I think the capital efficiency and the cost savings is really starting to materialize, including in the guidance. So, maybe that's where we start off, which is where we are in the business optimization program and the $1 billion. You give us a little bit of color on slide 8, but kind of unpack what's left to do in the journey, and if you end up surprising to the upside relative to the initial guide, where could that be?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah, Neil. Appreciate it. This is Clay. We're incredibly proud. This was a big hairy audacious goal, when Jeff and I started first contemplating, one, what was the metric we want to focus on, and that was sustainable free cash flow, and then how audacious should it be and what kind of timeframe should we put it around. I can tell you there was a tremendous amount of discomfort around the organization and just amongst Jeff and I on how do we get there from here.

But what we knew, I mean, deep in our soul was that you get the flywheel starting to turn, and there's so much that continues to come our way. Right now, we have over 80 parallel workstreams on different ideas. So, the progress that we made essentially in a third of the time to accomplish 60% of the results, I can tell you I'm even more encouraged about what this leads to. The most important measure of success will be locking these earnings in and building into the culture of the organization, benchmarking, hunger for more, creative ways of creating value. And like I said, there is much more to come from this. Trey, you may jump in and just throw a couple of pieces of color of ideas that you have.

Trey Lowe
Chief Technology Officer & Senior Vice President, Devon Energy Corp.

A

You bet. Appreciate the question, Neil. Clay mentioned the 80 workstreams that we have ongoing. The early results that we saw, a lot of them showed up very quickly in the capital side of our business on the drilling and completions operations. Over the last quarter – last four, five months, we've seen a lot of new ideas arriving from our production department, and we continue to see those starting to show up now in our forecast and what's going forward.

One of the examples I mentioned even a quarter ago was our focus on automating and using our technology stack to help us with our downtime. We've made a ton of progress over the last three months on that one and scaled that across the organization. And now, we're working on the next phase of using even more kind of AI to underpin what we're trying to do to continue to look at our faults and what causes those faults, and we're going to see those type of examples show up. [ph] We're estimating over (00:16:35) $10 million on that workstream in 2026, but that shows up and that's sticky, like Clay said, and we'll see that in our base production.

And those are the types of things that we're looking forward to in the future. All of that is underpinned by really a desire across our employee base to use technology. At this point, essentially all of our office-based employees are using AI to help them with productivity gains, and we're right now on the very tip of what we call wave two, and wave three is where you're implementing that AI in our work processes. So, a lot of momentum there, a lot of excitement across all of our organization to continue to move the ball down the field, and everything is looking good.

Neil Mehta
Analyst, Goldman Sachs & Co. LLC

Q

I appreciate the color, guys. And then, as you think about setting that CapEx budget for 2026, you probably took a view on different product lines on the services side. And just talk about – we're trying to isolate the structural cost improvements, which you talked about in the answer to the first question, versus more of the cyclical stuff. So, can you talk about the service environment right now and which product lines you're seeing deflation and which ones – which of the cost items you're seeing flat to inflation?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Neil, we feel really good about our positioning ahead of what could be a really challenging 2026. We look like the market is exceptionally well-supplied, maybe potentially oversupplied. And so, as a kid that grew up on the Gulf Coast, we know how to prepare for a hurricane. And when the storms come and you make sure you got your balance sheet right, you got your operations really buckled down, you got the teams focused on the right things, and then that helps drive through those troubling times.

So, when I think about what could come from 2026 and how we think about this preliminary guide, we've taken out any assumptions of inflation or deflation, really kind of timestamped where we're at today. We don't know where commodity prices are going to go and subsequent activities, and therefore, subsequent deflation. So, just consider that flat to where we're at today, and then we're prepared for whatever comes our way from a macro standpoint.

Neil Mehta
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's very clear. Thanks, Clay. Thanks, team.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Thank you, Neil.

Operator: Thank you. Our next question comes from Arun Jayaram with JPMorgan. Please go ahead. Your line is now open.

Arun Jayaram
Analyst, JPMorgan Securities LLC

Q

Yeah. Good morning. I was wondering if you could maybe elaborate on what you're doing to kind of manage your base production. You highlighted in the release that it's leading to maybe 20 MBoe per day of production uplift and a pretty meaningful improvement in cash flow from those efforts. And maybe talk about your views on the sustainability as we think about [ph] go-forward 2026, beyond (00:19:37)?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Thanks for the question, Arun. This, I think, is really important for us to spend a little time on. So, I really appreciate the angle on this one. It's pretty easy to quantify savings on that side of the equation. It's harder to quantify these wins. And we've been very clear from the beginning, this is not just a cost reduction program. This is a value enhancement program, and that should come on both sides of the ledger. This – what you're talking about is more value enhancement. And I can be honest with you, it's really hard to measure how much downtime would we have had theoretically, how much are we gaining incrementally from the actions. But that's exactly what this attempt is. We're trying to be exceptionally credible. At the same time, we know that this is a hard number to precisely quantify. I'll ask John to dig in on a couple of things that we're doing to measure this, quantify this, and then how we're seeing wins.

John Raines
Senior Vice President-E&P Asset Management, Devon Energy Corp.

A

Yeah. Arun, appreciate the question. I think Clay hit it well. When you look at the full year, we've had a really strong production beat. And the first thing I would say on that is when you look at that production beat and you break it down, we certainly beat on our wedge. We've had some outperformance on our wells. We've had a little bit of acceleration. But overall, the biggest part of that production beat comes from our base, and we feel that that's very measurable. Now, we've got, and I think Clay said earlier, over 80 workstreams on our business optimization. We've got a ton of these that go towards the base.

I'm going to talk about a few that I think have contributed the most this year. We've got a combination of technology and good blocking and tackling. I'll start with a project that I'm very proud of that we've deployed in the Delaware Basin. Really, this deployed some next-generation technology. You've heard me talk about it before. But this is our smart gas lift project in the Delaware Basin. What we're seeking to do here is essentially to deploy AI models that continuously optimize the optimal rate of gas injection for gas lift wells that sit on centralized gas lift systems.

This is a project that we piloted back in Q2. We saw tremendous results here. We saw a 3% to 5% uplift, and we talked about moving to [ph] the pilot two (00:21:54) on that. We saw success that was so good that we moved essentially into full deployment of that in the Delaware Basin, and we expect to be complete roughly by year-end on that. The beauty of this project is we also have application in the Williston Basin. We have application in the Eagle Ford. And so, this is going to be a project that's going to have ongoing sustainable results to our base production, and we're super excited about that.

Probably a couple other projects I'll hit on, and Clay mentioned this in our opening remarks. But we've had a tremendous focus on workover optimization this year. I say this year, this really started last year. We're looking at every which way that we can get better on our workover operations from operational efficiency all the way to safety. We took advantage early in the year. We made some changes in the organization to focus on this. We've got leads that work together to look at best practices across our basins. And when you look at what we've done there operationally, we've looked at advanced KPIs to manage our rig fleet. We've looked at design optimization. We've looked at equipment standardization, and really we've looked at planning optimization.

Not only have we been able to pull a ton of cost out of the system, but we've been able to lower the amount of time that we're spending on pad with these workovers. And essentially, what we've seen is we're getting our wells back quicker. And when we try to break down how much base contribution this had or the contribution to the base beat, we think it's over 2,000 barrels a day net production that we're seeing so far this year, and importantly, we think that's sustainable.

I think it may be the last example I'll provide. We've had a really tremendous focus on failure rate reduction and optimization. We've had this throughout the portfolio. I'll brag on the Rockies team a little bit here. Over the course of the last 18 months, we really looked at our artificial lift failures. We did some very intensive look-backs on that front. We did some proactive redesign there. And when we look back at the reduction in failure rate, we're tracking towards something that's 25%. And so, again, that's a good example of a project that takes cost out of the system, but it also increases our uptime pretty significantly. And so, a lot of really good projects in the queue like that. But we think these are all importantly very sustainable to the base production overall.

Arun Jayaram
Analyst, JPMorgan Securities LLC

Q

Thanks for that fulsome answer. Maybe just to follow up, your Rockies production has been trending maybe a little bit better than we had been modeling. In fact, if you look, you grew your oil 7,000 barrels a day sequentially, and you're relatively flat versus the 4Q 2024 number. So, maybe talk to us a little bit about what's been driving that and maybe how the overall integration with Grayson Mill assets has been going.

John Raines
Senior Vice President-E&P Asset Management, Devon Energy Corp.

A

Yeah. I'll start with the integration of the Grayson Mill assets. That integration is roughly complete. It's gone really well. We've had a lot of bidirectional lessons learned there, everything from midstream to the base operations, to learning more and more about the reservoir, how to drill these wells, how to complete these wells. So, I can't say enough good things about how that integration has gone.

When you talk specifically about the production, you're seeing a few things there. One, again, on the wedge, we're seeing well results that meet or exceed our expectation. And so, we've continued to be very pleasantly surprised with the good production we've seen, the good well results, especially as we focused on the western side of the play. But Neil – or excuse me, Arun, a lot of what I just said around the base is really what's driving that sequential improvement.

And I would say the Rockies team has really led the way on that. That artificial lift failure reduction that I talked about is a huge driver for us in the Rockies. And specifically, we've seen our workover rig count in the Rockies come down the most, and probably the biggest contribution to the base come from the Rockies. So, really proud of the work they've done, and I can't emphasize enough how important that base uplift has been for us there.

Arun Jayaram
Analyst, JPMorgan Securities LLC

Q

Great. Thanks a lot.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. Arun, I just want to jump in on John's comments. As we talk about the workover rigs especially, a lot of this motivation, I can tell you, was around safety. The workover rigs was something the industry was really struggling with. And with this hyper-focus, we found incremental value, cost savings, production efficiency, and maybe most importantly, safety improvement as well. So, really proud of all the teams that are working on that, and that's been kind of around the industry focus. So, great progress on that. Thanks again for the questions, Arun.

Arun Jayaram
Analyst, JPMorgan Securities LLC

Q

Thanks, gentlemen.

Operator: Thank you. Our next question comes from Neal Dingmann with William Blair. Please go ahead. Your line is now open.

Neal Dingmann
Analyst, William Blair & Co. LLC

Q

Good morning, all. Clay, nice quarter. Clay, my first question just on M&A specifically. I couldn't help but notice, I mean, you guys did a great job on the ground game, being active on New Mexico lease sales. So, I'm just wondering, with that said, do you all anticipate the ground game such as this maybe in New Mexico or other states around other plays continuing to represent a significant portion of your M&A?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Hey. Thanks for the question, Neal. Yeah, I would say this is very important. We've done a lot of this work quietly kind of on the backs of trades, 40 acres in, 40 acres out. I mean, just hard work every single day that can be incredibly value-creative. We've had some more opportunities with state lease sales and upcoming federal lease sales. That's definitely something we want to participate.

We'll look at it objectively as we do all incremental investments, but really excited about that opportunity, and definitely, something we want to play an active role in. Clearly, we have, and we think we have – with the flywheel, the machine that we have running in the Delaware Basin in particular, I think it's a great opportunity for us to leverage not just the skill sets, the momentum that the team has, the technology, the benefit from the business optimization, all of those things, but also the mechanics of being there, boots on the ground every single day as a great ability to scale. So, we think we have every right to be on the front-end of that, and successful thus far.

Neal Dingmann
Analyst, William Blair & Co. LLC

Q

Great point. And then, that leads me to my second question, Clay. I can't help but notice just how much you continue to advance the Delaware, not only just better wells, but you continue to recognize more resource just on developing – kind of developing more rock. So, I guess with that said and just how well you're doing there, does that cause you to think about differently maybe one of your other plays like the Anadarko or PRB, where you have less scale and one rig, and I'd suggest investors are not giving you full credit? I mean, why – any thought about potentially reallocating – selling something and reallocating into the – even more in the Delaware where you continue to see all this upside?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Yeah. Neal, as you know, we look at this stuff all of the time. Our board – this is an imperative that our board has for us to be thinking about all of the art of the possible. And that certainly means we're not going to be in these five basins exactly as constructed for the indefinite future. Objectively, we need to think about what's the right opportunity for us, for how these positions would fit given the market demands, but also thinking about what the opportunities are to continue to scale and grow and make sure that we've got a sustainable value-creating business going forward.

When you look back at the 50-plus-year history of Devon, and I would say any organization that survived 50 years in this very tough business, man, we have reinvented ourselves a number of times along the way. We always will remain objective about what that could mean going forward. And again, this is regular conversations that we have with our board, as we should, about thinking the longevity of creating long-term shareholder value. It's just fundamental to what we do.

Neal Dingmann
Analyst, William Blair & Co. LLC
Q

A great optionality to have. Thanks, Clay.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Thank you, sir.

Operator: Thank you. Our next question comes from Doug Leggate with Wolfe Research. Doug, please go ahead.

Doug Leggate
Analyst, Wolfe Research LLC
Q

Thank you. Good morning, Clay. Good morning everybody. Clay, I wonder if I could come back to the business optimization for a second. I think I've maybe been confused about something, and I'm looking for some clarity. You have some of the legacy midstream contracts rolling off. But my understanding is it's beyond the timeline of the $1 billion target. So, I'm thinking EnLink specifically. So, can you tell us what's included in the remaining $400 million? And it sounds like there might be an upside case for that based on some of these longer dated contracts. Sorry if I'm getting that wrong.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

No, that's – I think you're exactly right, Doug. I think there is upside. One of the things that we debated early – I can tell you, the original construction from the team that was presented to Jeff and I as we were thinking about what could this look like, it was actually a three-year look that includes some other things that we know we're going to have in kind of year three of this opportunity. I can tell you there's additional wins in years three, four, five and for the foreseeable future. We've really focused on 2025 and 2026 wins. And as you pointed out, there's some really material, specifically in the gas contract world, that comes out further than that. I'll ask Jeff to dig into some of those opportunities.

Jeffrey L. Ritenour
Executive Vice President & Chief Financial Officer, Devon Energy Corp.
A

Yeah. Doug, just to be clear, so in the business optimization guidance that we rolled out to get to the $1 billion of free cash flow starting in January of 2027, the bulk of that that relates to the commercial opportunities is what we talked about in the previous quarters, which is reduced fees on gathering, processing and transportation and fractionation. Most of that's on gas and NGLs specific to the Delaware Basin.

So, the lion's share and bulk of that really resides in the Delaware. That's where you're going to get this incremental uplift, if you will, of the commercial opportunities that we highlighted specific to the $1 billion. As Clay just said, 2027 and beyond, there'll be other opportunities across our portfolio where we could see some incremental benefit. But in the $1 billion, the real driver of that is what we're seeing in the Delaware specific to our gas and NGL contracts.

Doug Leggate
Analyst, Wolfe Research LLC
Q

That's very helpful. I guess it would be a bit of a stretch to ask you to quantify the upside at this point, but I think maybe that's for another call. My follow-up is a little self-serving, I'm afraid, and I just want to make sure I'm not misinterpreting or overstating this. But if I look back to the legacy commitment from when you were still COO, Clay, you used to talk about 70% of your free cash flow coming back to shareholders. It seems that your presentation deck has adjusted that a little bit to now include debt reduction in your shareholder returns. Is that the right interpretation? Because obviously we're big fans of that. I just wanted to clarify with you if that's how you're thinking about it.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Yeah. Appreciate that. I mean, I think it is a fundamental piece of how we think about returning value to shareholders. And certainly, ahead of what could be a pretty choppy year in 2026, I think we want to make sure that we are thinking about debt, debt structure, how we capitalize the company, and that we're prepared for anything that comes ahead. So, there was an opportunity for us to take the $485 million down. We certainly consider that part of, again, returning cash in various forms to shareholders. And obviously, we had an illustration this time that included that.

So, yeah, appreciate your support over the years for debt reduction. This is a very – it's a challenging business. We think the more that you can be prepared for the storms, the storms turn into real opportunities. And I think that's where Devon is positioned today that, when these challenges come ahead, we're going to be front footed and on the – have an opportunity to really be – to turn them into a value-creating opportunity rather than just a defensive posture.

Doug Leggate
Analyst, Wolfe Research LLC
Q

This sounds like an M&A question, Clay, but I'll leave it there. Thanks very much indeed.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Thank you, Doug. Appreciate it.

Operator: Thank you. Our next question comes from Scott Gruber with Citigroup. Please go ahead, Scott.

Scott A. Gruber
Analyst, Citigroup Global Markets, Inc.

Q

Yes. Good morning. I want to come back to the production optimization bucket. Great gains there. I think though the bulk of that effort hits production, and therefore, a reduction in maintenance CapEx needs. But I think there's also an LOE benefit as well. How does that split? And we see your LOE rolling lower. How should we think about the LOE cost in 2026?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. Scott, that's a great question, and it is – this manifests in a few different categories and some of them are cost reductions. As you mentioned, LOE, we've seen a significant improvement quarter-over-quarter. We'll continue to see benefits there. It shows up obviously in the maintenance capital, requiring us to drill fewer wells. I think our original plan versus the plan we're executing now, we're actually drilling 20 fewer wells this year because of these kind of benefits, essentially lowering that burden of maintenance capital, and as a side benefit, prolonging the really high quality portfolio that we have. I might ask John to see if he has anything else to add to that.

John Raines
Senior Vice President-E&P Asset Management, Devon Energy Corp.

A

Yeah. As we originally contemplated this, you're absolutely right, there's a component of our production optimization target that's LOE. There's a component that is production uplift. There's even a little bit there that is pulling capital out of the system. But I'll tell you right now, the way that we're looking at the $150 million, that's essentially all of the production uplift at this point in time.

We have had some success on LOE over the course of the year. I think if you look back to our Q1 and you break it out from the number we disclosed, LOE plus [ph] GP&T, we're sitting at (00:36:44) about $6.50 a barrel. I want to say this quarter, we're sitting just above $6.10 a barrel. So, about a 6% improvement year-over-year. LOE is pretty sticky and it lags. So, as we go into 2026, we expect ongoing reductions on LOE, and you'll see more LOE contributions show up within production optimization. But essentially, what we're taking credit for up to this point is that base uplift that I mentioned earlier.

Scott A. Gruber
Analyst, Citigroup Global Markets, Inc.

Q

I appreciate that color. And with the efforts reducing your [ph] well count needs, how do we think about the TIL count (00:37:15) that's embedded in your 2026 preliminary guide here?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. I think that's obviously contemplated as we get both more efficient on how quickly we can execute drilling, completion, building facilities, and then the effectiveness of those completions and how they contribute. Again, we're in a base capital mode – excuse me, a base oil production mode, and the lower maintenance capital is certainly reflected by that preliminary $3.6 billion guide, which again is a substantial improvement from where we were 12 months ago when we were providing a preliminary guide for 2025. So, we're winning significantly on that. That's showing up in the numbers. I continue to be encouraged by the work that we're doing and the great efforts of the team and how this is showing up and will continue to show up in time.

Scott A. Gruber
Analyst, Citigroup Global Markets, Inc.

Q

But should we think about the 2025 [ph] TIL count kind of less 20 (00:38:14) as a starting point for 2026? Is that fair?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Look, I don't know if we want to get into details of that. But here's what I would tell you is take the preliminary guide, start with the numbers that we're guiding on 2025 as of today, and I think that's a good kind of relative application and allocation. Again, we've mentioned no additional deflation is baked in. So, I think that's a good starting point for assumptions. And then, obviously, when we come back to you early in the year with firm guidance, we'll have a lot more details to share with you then.

Scott A. Gruber
Analyst, Citigroup Global Markets, Inc.

Q

Okay. I appreciate it. Thank you, Clay.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Thanks, Scott. Appreciate it.

Operator: Thank you. Our next question comes from Kevin MacCurdy with Pickering Energy Partners. Please go ahead, Kevin.

Kevin MacCurdy
Analyst, Pickering Energy Partners LP

Q

Hey. Good morning and thanks for taking my question. I mean, kind of going back to M&A, there's been a lot of industry interest in the Anadarko and specifically M&A in the Anadarko. And maybe a two-part question there. I mean, being located there in Oklahoma, what do you make of the interest in that basin and what do you think is driving kind of the renewed interest? And does the level of interest kind of make you reconsider the Anadarko's place in your portfolio?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. Kevin, I would say on the first question, obviously, it's gas-oriented. It's positioned well. It's not backed up behind Waha. So, there's some structural advantages of the Mid-Continent, the Anadarko Basin that we benefit from today. And certainly, we're very aware of that and we take great pride in that.

I'll go back to my earlier comments. We consider everything all the time. Our board is very inquisitive and very thoughtful about how do we build the right term – right long-term shareholder opportunity value set, how do we think about the portfolio. You have to remember, we're always consuming the front-end of our portfolio. So, how are we backfilling with quantity and quality of the portfolio to make sure that we have a very substantial and solid 10-year runway in front of us. All of those things are considered. And so, as markets change and we see other things, we have interest – we have interest in other things, all of that certainly comes into play, but no additional details to share with you on that today. But appreciate you asking.

Kevin MacCurdy
Analyst, Pickering Energy Partners LP

Q

Got you. Thanks, Clay. And then, as a follow-up, I really liked the details on slide 9. I think that highlights the value creation that you've had that doesn't always kind of show up in the production numbers. I guess a question on WaterBridge. Is there any operational reasons that you would keep that equity interest?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. Kevin, I'd probably put it in the same category that we've done a lot of deals kind of adjacent to our core business. Think about something like Matterhorn, where we entered that opportunity. The key there was really, specific to Matterhorn, making sure that we had gas takeaway from the basin. That was the phenomenal – or the fundamental importance that we did. By underwriting that, we ensured that that pipe was built, we have a significant position on that. We've retained that volume on the pipe. We also benefited from an equity position. We made a very, very substantial return on that. We're very proud of that. But again, the objective was making sure that that pipe was built and making sure that we had our ability to get our gas to market.

Similarly, with WaterBridge, the main objective there is making sure that we're thinking a lot about a super system. [ph] We reserve pour space (00:41:56). That's very proactive in our industry. John will probably tell you a little bit more about that when I hand it to him. But I can tell you, the really fundamental important piece of this was to make sure that we have our water taken care of in the Delaware Basin. And through this JV, this partnership, we've secured that.

Now, as a very beneficial byproduct, we have a substantial ownership in a publicly traded entity that's done very well. There's no reason we have to hang on to it. By the same token, it's a great investment, and I would tell you, we're not – we have to sell either in that position. So, it's option value for us. We have a lot of that in our organization. And we continue to evaluate that, just as we do with other things in our portfolio in this regular part of the conversation we have with our board. John, anything else you wanted to add?

John Raines
Senior Vice President-E&P Asset Management, Devon Energy Corp.

A

Clay, I think you covered it really well. I would say the relationship there remains very important to us. Operationally, we work with those guys every day. We've got a very multi-faceted water management effort in the Delaware Basin. That's both to manage costs, but manage future risk associated with water. I've talked about this before on our calls. But our first call on water is always to go to recycle. We've got a big recycle operation in the basin. In New Mexico, we've got a large water midstream presence we probably don't talk about enough. That gives us a lot of flexibility there. We've got a lot of strategic offloads. Many of those offloads are WaterBridge. And then, when you get into Texas, we really leverage our WaterBridge relationship to give us diversity of options across the play there. So, we feel really good about how that's working operationally.

Kevin MacCurdy
Analyst, Pickering Energy Partners LP

Q

A very detailed answer. Thank you, guys.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Thanks, Kevin.

Operator: Thank you. Our next question comes from Kalei Akamine with Bank of America. Please go ahead. Your line is now open.

Kalei Akamine
Analyst, BofA Securities, Inc.

Q

Hey. Good morning, guys. I want to start with the Wolfcamp B drilling program for this year, and maybe this one is for John. So, production in the Delaware has been holding up quite well this year. Can you kind of compare how the Wolfcamp B results are comparing to your expectations? And then, for 2026, do you anticipate [indiscernible] (00:44:14) comprising a similar proportion of the program?

John Raines
Senior Vice President-E&P Asset Management, Devon Energy Corp.

A

Yeah. Kalei, appreciate the questions. I would say Wolfcamp B is performing very well relative to our expectations for the year. You probably heard me mention this on the last call. When you look at 2025, we've got a very diversified program as far as the zones that we're targeting for the full year. We're looking at about 30% Wolfcamp B or Deep Wolfcamp, about 30% Upper Wolfcamp, about 30% Bone Spring, and the remainder in the Avalon.

What you're really seeing – you're going to see some volatility in terms of zone mix each quarter. A lot of our Wolfcamp B wells have come on in the first quarter and really the first half of the year. So, we've had had a little bit of a run at seeing how those wells are performing. And generally speaking, I'd say they're mostly meeting our expectations, with quite a few of those wells beating our expectations.

What I think you can expect from us going forward – for 2026, it's too early to get in and talk specifically about zone mix throughout the year. But I think Clay said earlier, you can expect some stability, some consistency in how we're thinking about our overall Delaware program. And as we shifted more into this multi-zone co-development, from a well productivity standpoint, we took that trade-off to go a little bit lower this year in exchange for better NPV overall and for a longer inventory runway. But I think you can expect that well productivity to be very consistent going forward for the next couple of years.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.

A

Yeah. And if I could add – I'm going to ask Tom just to add a little bit more about our D&C efficiency that we continue to see in the Delaware Basin. I mean, I think it's very important as we think about all of these additional zones. The Wolfcamp B just a touch deeper, but as we start expanding to the geographic edges and up and down the zone, so to speak, that efficiency really contributes as well. So, Tom, just maybe a little bit on how we're thinking about on the efficiency gains there.

Thomas J. Hellman
Senior Vice President-E&P Operations, Devon Energy Corp.

A

Yeah. Clay, it's been really interesting this year. We've been really leaning into benchmarking in the Delaware Basin and using the AI tools on top of that. We have both AI tools that help us on sort of the [ph] new school (00:46:37) where we can predict – like use the AI to look at the parameters – the drilling parameters that really help us predict how to drill faster on the current well. And we're even using AI tools right now to help us [ph] trip faster (00:46:58) and drill curves faster and even running casing faster, all about 30% faster. Each one of those saves us millions of dollars. And now, in the Delaware Basin, we have a new record at about 1,800 feet per day.

That really screens well versus all of our fastest peers. So, Clay, it's looking really good, and I think these AI tools and the benchmarking is really coming through for us.

Kalei Akamine
Analyst, BofA Securities, Inc.
Q

That's awesome. I appreciate that detailed answer. My follow-up is on the lease sales. So, yesterday, that sale was a state sale. But this presidential administration has put federal lease sales back on the table, and they should occur with a pretty steady cadence. How are you guys thinking about those? And do you anticipate that being a part of your cash allocation priorities for 2026?

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Yeah. Great question. And I think as I mentioned earlier, I think this is something we should be able to compete exceptionally well. We've got an existing footprint, the momentum of the organization, the efficiencies Tom was just talking about around D&C, the infrastructure that we have including WaterBridge, the relationships that we have with the gas midstream partners, and then of course the existing infrastructure of the people applying this business optimization, the technology, puts us in a really good position to be super competitive. So, when we look at those, you bet, we'll be participating in the process. There's some really interesting land. We're thrilled to have the BLM open up some of these opportunities, and there's some pretty material lease sales coming up.

So, yeah, we – as we've shown on the last lease sale, we want to be part of the process, and at the same time, we want to be very objective about how do we create value – full-cycle value from these opportunities. So, yeah, count us in as part of the process. And as long as – alongside everything that we're doing on the ground game, including trades, small acquisitions, ground floor leasing in all the basins we're doing, we just see a real interesting opportunity coming in the Delaware. So, definitely leaning that direction.

Kalei Akamine
Analyst, BofA Securities, Inc.
Q

Thanks, Clay. I'll pass it back.

Clay M. Gaspar
President, Chief Executive Officer & Director, Devon Energy Corp.
A

Thank you, sir. Appreciate it.

Operator: Thank you. We have no further questions. And so, I'd like to turn the call back over to Chris for closing comments.

Christopher Carr
Director-Investor Relations, Devon Energy Corp.

Yeah. Thank you for your interest in Devon today. If there are any further questions, please reach out to the Investor Relations team. Have a good day. Thanks.

Operator: Thank you, everyone, for joining us today. This concludes our call, and you may now disconnect your lines.