

Devon Energy: Funding the Next Barrel

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On August 6, Devon Energy reported its second-quarter results. The company had generated \$1.535 billion in operating cash flow and \$587 million in free cash flow during the quarter. It had also agreed to spend \$5 billion to acquire Grayson Mill Energy's Williston Basin business. The deal was still pending. Devon's board had expanded its share-repurchase authorization, while management described a plan to reduce debt and maintain its regular shareholder-return framework.

The figures left a practical question for Devon's leaders: how should the company allocate cash once the transaction closed? More drilling could develop a larger inventory and capture operating benefits. Debt repayment could protect flexibility in a volatile commodity business. Dividends and buybacks could return cash to shareholders. Each use had a claim on the same uncertain future cash flows.

This case is set immediately after Devon's August 6 results filing and before its scheduled August 7 earnings call. A capital-allocation committee is a **hypothetical classroom role**; no public record establishes that Devon held such a meeting at this time. Students should recommend a policy for the first two years after closing, state the conditions that would change it, and identify what evidence management should monitor.

A larger Williston position

Devon had built a multi-basin U.S. oil and gas portfolio, with major operations in the Delaware Basin, Eagle Ford, Anadarko Basin, Powder River Basin and Williston Basin. Its strategy emphasized operating efficiency, disciplined reinvestment, a conservative balance sheet and shareholder distributions. In July, it announced an agreement to acquire Grayson Mill's Williston Basin business.

The announced transaction value was \$5.0 billion: \$3.25 billion in cash and \$1.75 billion in Devon shares, valued at 37 million shares at announcement. Devon said it expected to fund the cash portion from cash on hand and debt. The agreement remained subject to closing conditions and customary purchase-price adjustments. It was not yet a completed acquisition as of the case cutoff. (Exhibit 1.)

Management said the acquired position included approximately 307,000 net acres, production expected to be near 100,000 barrels of oil equivalent per day in 2025, 500 gross drilling locations and 300 refracturing candidates. Devon estimated up to \$50 million in annual operating and marketing synergies and a 15% free-cash-flow yield at \$80 per barrel WTI. It projected about 1.0 times net debt to EBITDAX at closing and said it intended to direct up to 30% of annual free cash flow toward \$2.5 billion of debt reduction over two years. These figures were estimates and plans supplied by Devon, not results already achieved. (Exhibit 1.)

The deal also expanded Devon's options. A larger Williston operation could increase scale, add drilling inventory and connect more production to infrastructure Devon said it could operate. But the package required substantial cash financing, brought new assets to integrate, and added development opportunities whose returns would depend on oil prices, well performance, costs and timing.

The cash-generation baseline

Devon entered the second half of 2024 with a \$3.3 billion to \$3.6 billion full-year capital-expenditure range. In the second quarter, it spent \$828 million on upstream capital and reported total capital expenditures, excluding acquisitions, of \$890 million. The company maintained its annual capital range and expected spending in the upper half. It raised its production guidance to 677,000-688,000 barrels of oil equivalent per day, citing well performance and shorter cycle times. The updated 2024 guidance did not include Grayson Mill, which had not closed. (Exhibits 2 and 3.)

At June 30, Devon reported \$1.169 billion in cash, including restricted cash, and \$6.140 billion of debt. The resulting \$4.971 billion net debt and 0.6-times net-debt-to-EBITDAX ratio were company calculations using its stated definitions. The quarter's cash generation and leverage gave Devon room to act, but the acquisition would change the balance sheet and future cash needs. Devon projected approximately 1.0-times leverage at close; that projection was not a reported post-close result. (Exhibit 2.)

The quarter also showed why the definition of "free cash flow" mattered. Devon's reported \$587 million of free cash flow equaled operating cash flow of \$1.535 billion less \$948 million of cash capital expenditures. Its \$765 million of adjusted free cash flow instead used operating cash flow before balance-sheet changes of \$1.736 billion less \$971 million of accrued capital expenditures. The measures differed in both working-capital treatment and capex timing. (Exhibit 3.)

Devon said it was committed to returning approximately 70% of adjusted free cash flow through fixed and variable dividends and share repurchases. In the second quarter, it declared a \$0.22-per-share fixed dividend and a \$0.22-per-share variable dividend, and repurchased 5.2 million shares for \$256 million. Separately, the July acquisition announcement described directing **up to** 30% of annual free cash flow to debt reduction. The two statements used different terminology, definitions and timing. They do not establish complementary 70% and 30% slices of one cash pool. (Exhibits 1-3.)

The board also raised the repurchase authorization by 67% to \$5 billion through mid-2026. An authorization permitted repurchases; it did not require Devon to spend the full amount or specify a quarter-by-quarter pace. (Exhibit 1.)

A capital-allocation choice

Devon's leaders could frame the next two years around different priorities. An integration-first approach could protect the announced capital plan while funding acquired-asset evaluation, operating integration and projects that met the company's investment criteria. A balance-sheet-first approach could use more cash for debt reduction until leverage or liquidity met stated conditions. A shareholder-return-first approach could maintain distributions and use repurchases when management judged the shares attractive, while continuing selected development.

These approaches need not be all-or-nothing. A policy could set minimum liquidity, leverage triggers, return hurdles or a sequence of uses. However, Devon had not disclosed a single

reconciled post-close cash waterfall that specified how these capital uses would interact under different oil-price or operating scenarios. Students must make the definitions, timing and conditions explicit rather than infer a precise allocation from the public statements.

There were also limits to what the public data could answer. The acquisition announcement did not provide well-level type curves, decline rates, full-cycle costs, maintenance-versus-growth capital requirements or realized post-close synergies. The \$80 WTI free-cash-flow yield was a company estimate under a stated price assumption; it did not independently establish a return for each investment or the value of the whole package. Devon's second-quarter operating performance described its existing portfolio and did not isolate Grayson Mill's incremental economics.

Exhibits

Exhibit 1. Announced Grayson Mill transaction and stated plans

Item	Devon announcement
Stated transaction value	\$5.0 billion
Cash consideration	\$3.25 billion
Stock consideration	\$1.75 billion, or 37 million shares at announcement value
Acquired net acreage	Approximately 307,000 acres
Expected acquired production	Near 100,000 Boe/d in 2025, approximately 55% oil
Gross drilling locations / refrac candidates	500 / 300
Estimated annual operating and marketing synergies	Up to \$50 million
Company-estimated FCF yield	15% at \$80 WTI
Projected net debt / EBITDAX at close	Approximately 1.0x
Stated debt-reduction intent	Up to 30% of annual FCF toward \$2.5 billion over two years
Repurchase authorization	Increased to \$5 billion through mid-2026

Source: Devon's July 8, 2024 acquisition announcement and related 8-K. All operating, synergy, leverage and FCF-yield values above are company estimates or projections. Transaction value and consideration remained subject to customary adjustments and closing conditions. FCF-yield price case is specified by Devon; methodology is not independently reconstructed here.

Exhibit 2. Devon second-quarter 2024 snapshot

Measure	Q2 2024 / June 30, 2024
Net earnings	\$844 million
Operating cash flow	\$1.535 billion
Reported free cash flow	\$587 million
Cash, including restricted cash	\$1.169 billion
Total debt	\$6.140 billion
Net debt	\$4.971 billion
Net debt / EBITDAX	0.6x
Production	707,000 Boe/d
Oil production	335,000 barrels/d
Q2 upstream capital	\$828 million
Q2 total capital excluding acquisitions	\$890 million
FY2024 capital range	\$3.3-\$3.6 billion; company expected upper half
FY2024 production guidance	677,000-688,000 Boe/d

Source: Devon Q2 2024 results release and supplemental tables filed August 6, 2024.

Net-debt/EBITDAX is company-defined. Full-year guidance excluded Grayson Mill before closing.

Exhibit 3. Two free-cash-flow measures and Q2 shareholder returns

Company measure	Q2 2024 calculation / amount
Reported FCF	\$1.535bn operating cash flow – \$0.948bn cash capex = \$0.587bn
Adjusted FCF	\$1.736bn operating cash flow before balance-sheet changes – \$0.971bn accrued capex = \$0.765bn
Fixed dividend	\$0.22 per share
Variable dividend	\$0.22 per share
Share repurchases	5.2 million shares for \$256 million
Stated ongoing distribution commitment	Approximately 70% of adjusted FCF via dividends and repurchases

Source: Devon Q2 2024 results release and supplemental tables. The company's "approximately 70% of adjusted FCF" distribution commitment and its separate "up to 30% of annual FCF" debt-reduction intent are not directly additive; their measures and periods are not reconciled in the disclosed materials cited here.

Exhibit 4. Peer capital-return context: Diamondback Energy

Diamondback reported that its Q2 base and variable dividends totaled \$421 million, approximately 50% of its adjusted free cash flow under its own definition. It made no share repurchases in Q2. The company had issued \$5.5 billion of senior notes in April to fund part of the cash consideration for its pending Endeavor combination. At June 30, Diamondback reported \$12.2 billion of debt and \$5.3 billion of net debt.

Source: Diamondback Q2 2024 results release and shareholder letter, filed August 5, 2024. Diamondback differs from Devon in transaction structure, leverage, assets and metric definitions; the comparison is descriptive, not a target for Devon.

Assignment

Assume you are advising Devon's hypothetical capital-allocation committee immediately after the August 6 Q2 filing and before the August 7 earnings call. Recommend a policy for the first two years after the Grayson Mill transaction closes.

1. How should Devon sequence acquired-asset investment and integration, debt reduction, fixed and variable dividends, and repurchases?
2. What conditions should trigger a change in that sequence? State measurable indicators and define their time horizon.
3. How should the policy respond if oil prices or acquired-asset performance are weaker than Devon's assumptions?
4. Which information should management provide to investors to make the policy and its progress assessable?

Use the exhibits and state your assumptions. Do not treat company projections as realized results, assume the repurchase authorization will be fully used, or add the 70% and 30% statements as though they used one denominator.

Sources and cutoff

Case facts come from Devon's FY2023 Form 10-K; its July 8, 2024 Grayson Mill announcement; its August 6 Q2 2024 results release and supplemental tables; and Diamondback Energy's August 5, 2024 Q2 results release and shareholder letter. Filing details and direct links are recorded in the Devon research source register. The information cutoff is **August 6, 2024, 4:42:54 p.m. ET**, the SEC acceptance time of Devon's Q2 results package. The August 7 call and 10-Q, the presentation with unverified public timing, and all later closing or operating outcomes are excluded.