Research Report

Introducing our 2025 S&P 500 use of cash forecasts

Nurture Enduring Wealth, Embrace Insightful Change

2024/10/24

Reporter: Miranda

NEW EIC

Executive Summary

Objective

- The research aims to forecast S&P 500 **cash spending** trends for 2025, covering areas like CapEx, R&D, buybacks, dividends, and cash M&A, with a focus on earnings growth driving cash spending.

Scope

- The research analyzes S&P 500 companies, comparing spending patterns between the **largest firms** and the **broader market**, with data from **1H 2024** and **forecasts for 2025**.

Key Findings

- The largest stocks have been boosting aggregate cash spending in 2024, but **a broadening is expected in 2025**. (S&P 500 cash spending is expected to accelerate from +8% in 2024 to +11% in 2025, driven by strong earnings growth.)
- In 2025, **the gap in earnings growth should narrow** between the largest stocks and the median stock. (The top 10 S&P 500 spenders increased cash spending by 36% year/year in 1H 2024, while the other 490 stocks saw a more modest 7% growth)
- The forecasts suggests **a roughly even split** between returning cash to shareholders and investing for growth. (A balanced growth of cash allocation is projected for 2025, with 15% growth in buybacks, 7% in dividends, 8% in CapEx, 9% in R&D, and a 20% rebound in cash M&A)

NEW EIC

Market Overview - Capex

Context

- This session focuses on **capital expenditures (capex)** of the S&P 500 companies, with a particular emphasis on technology companies (hyperscalers) and the energy sector.

Trends

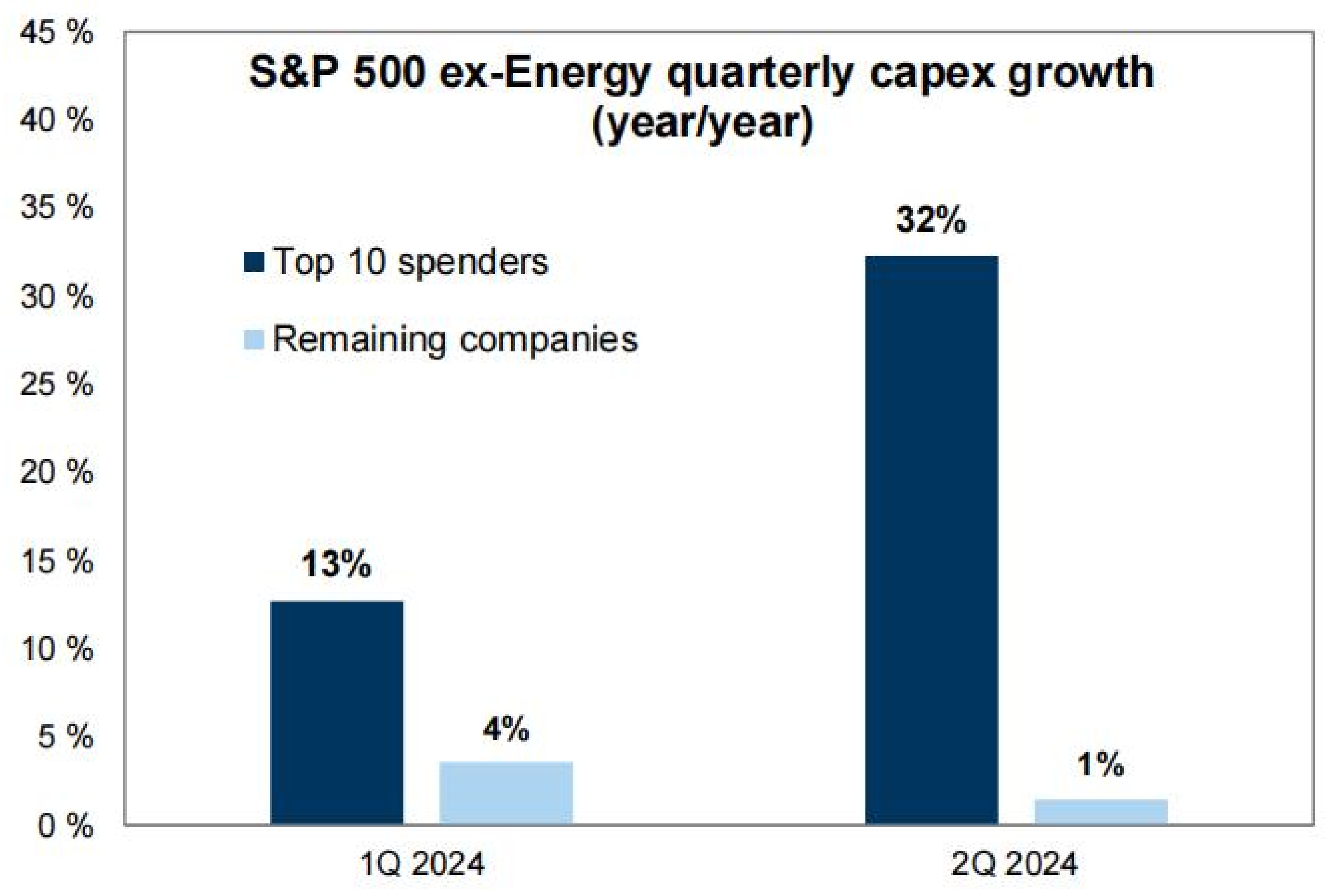
- **Capex Growth**: Capex is expected to grow by 11% in 2024 and **8% in 2025**, driven by strong **economic growth**, **earnings**, and significant **AI investments** from hyperscalers like Amazon, Google, Meta, Microsoft, and Oracle.
- **Sector Disparity**: The top 10 S&P 500 spenders increased capex by 22% in 1H 2024, while the remaining companies grew by only 2%, highlighting the significant role of AI-related investments.
- **Energy Sector**: Energy capex is forecast to grow by 6% in 2025, with cash flow growth expected to rebound from -7% in 2024 to **16% in 2025**.
- **Macroeconomic Conditions**: Slowing GDP growth in 2025 and a deceleration in capex from hyperscalers are anticipated. However, a favorable macroeconomic environment and improving earnings outlook should support broader capex growth in the coming years.

NEW EIC

Market Overview - Capex

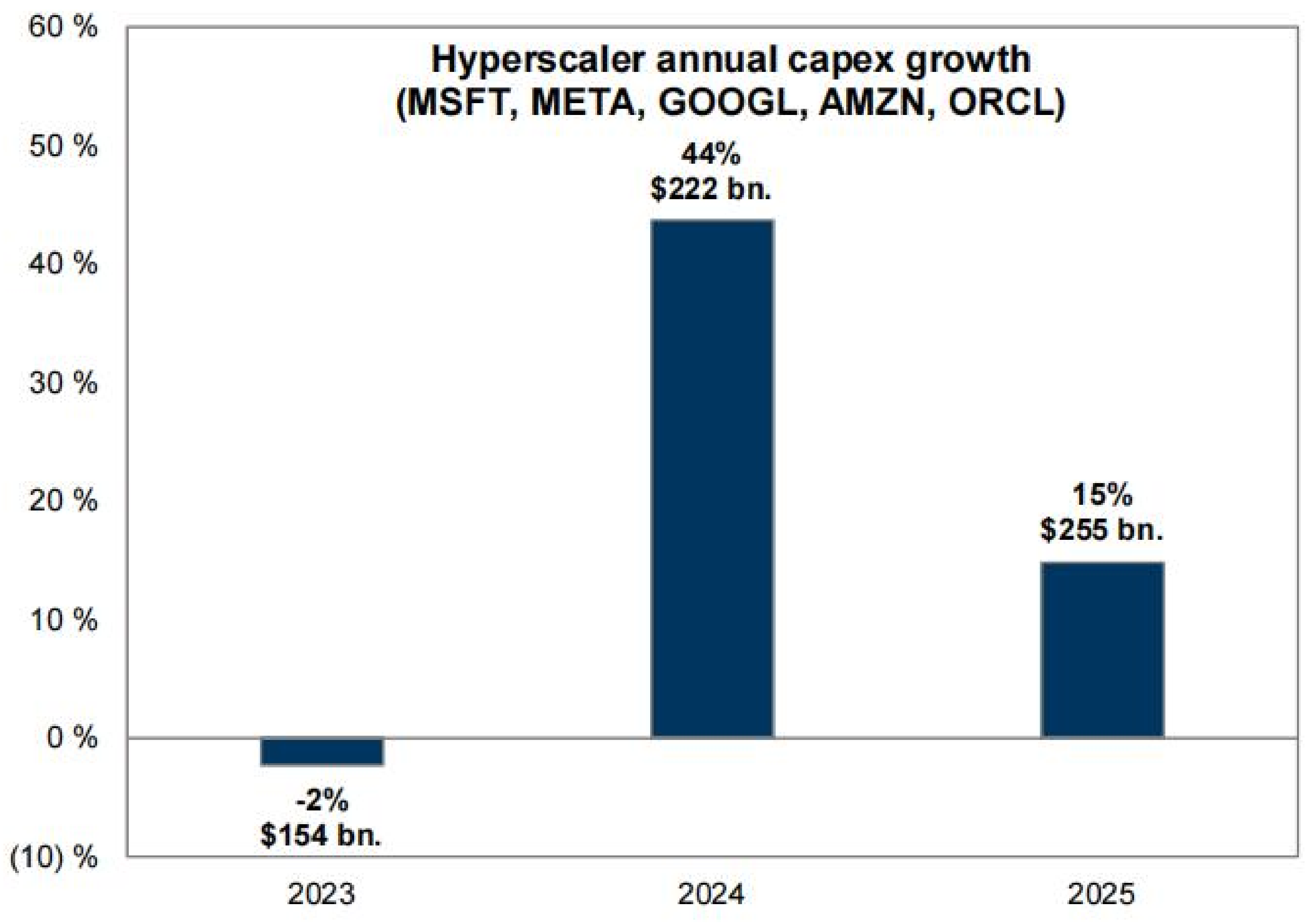
Chart

Exhibit 14: Capex growth has been concentrated among the largest spenders



Source: Compustat, Goldman Sachs Global Investment Research

Exhibit 15: Consensus expects hyperscaler capex growth to slow in 2025



Source: FactSet, Goldman Sachs Global Investment Research

NEW EIC

Market Overview - R&D

Context

- This session focuses on the trends in **R&D (Research & Development)** spending within S&P 500 companies, particularly focusing on sectors like Information Technology and Health Care.

Trends

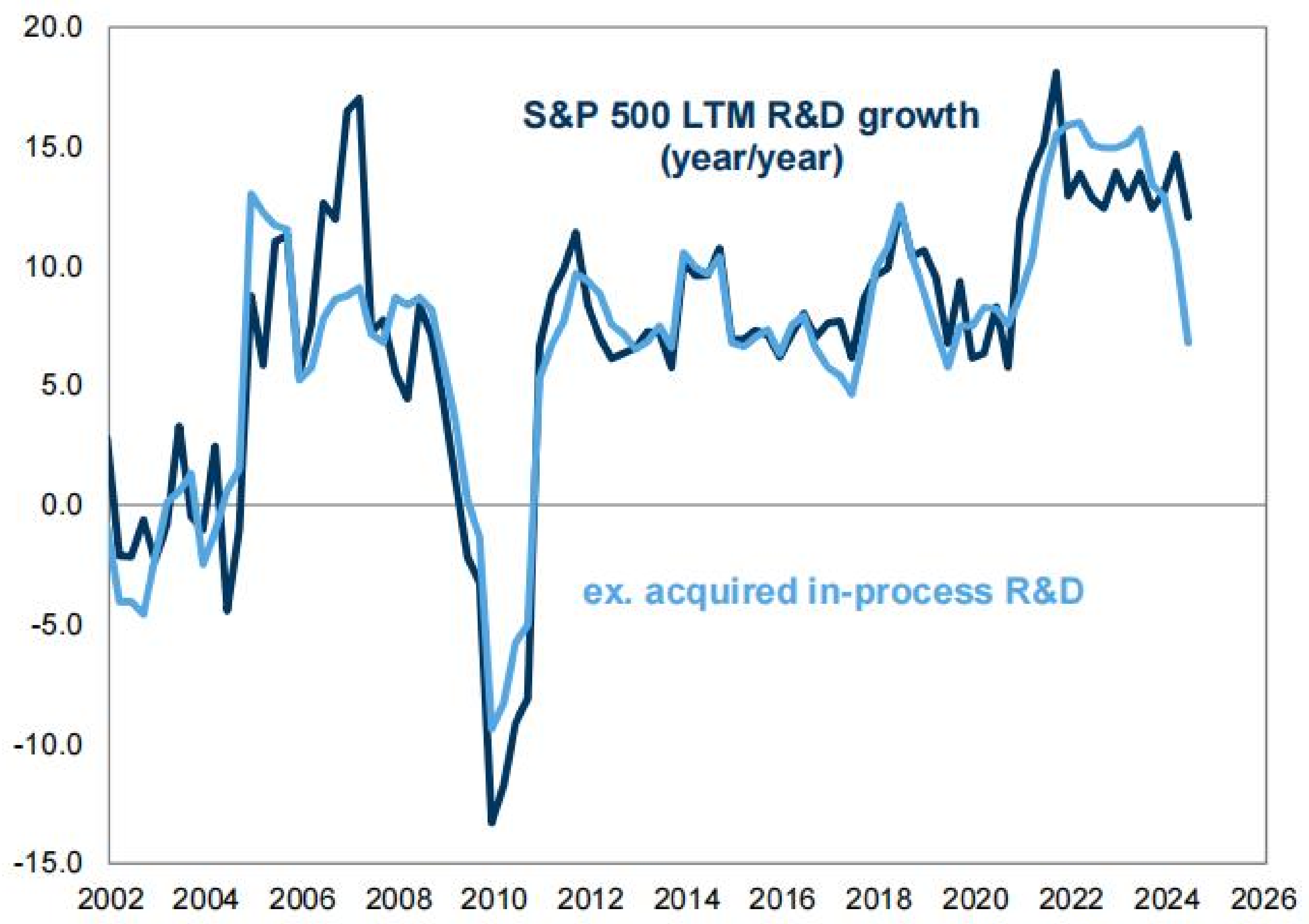
- **R&D Growth Rate**: R&D growth is projected to slow down from 13% in 2023 to 10% in 2024 and 9% in 2025, gradually normalizing toward pre-pandemic levels of around 8%.
- **Sector-Specific Drivers**: R&D spending is highly concentrated in a few sectors, notably Info Tech and Health Care, which are expected to continue driving slightly elevated growth beyond what is implied by broader economic conditions.
- **Impact of Acquisitions**: In 2024, large Health Care companies like Bristol-Myers Squibb (BMY), Gilead Sciences (GILD), and Vertex Pharmaceuticals (VRTX) contributed to a boost in R&D spending through acquired in-process R&D (IPRD), totaling $27 billion in the first half of the year. Excluding these acquisition-related expenses, R&D growth would appear closer to its historical average.

NEW EIC

Market Overview - R&D

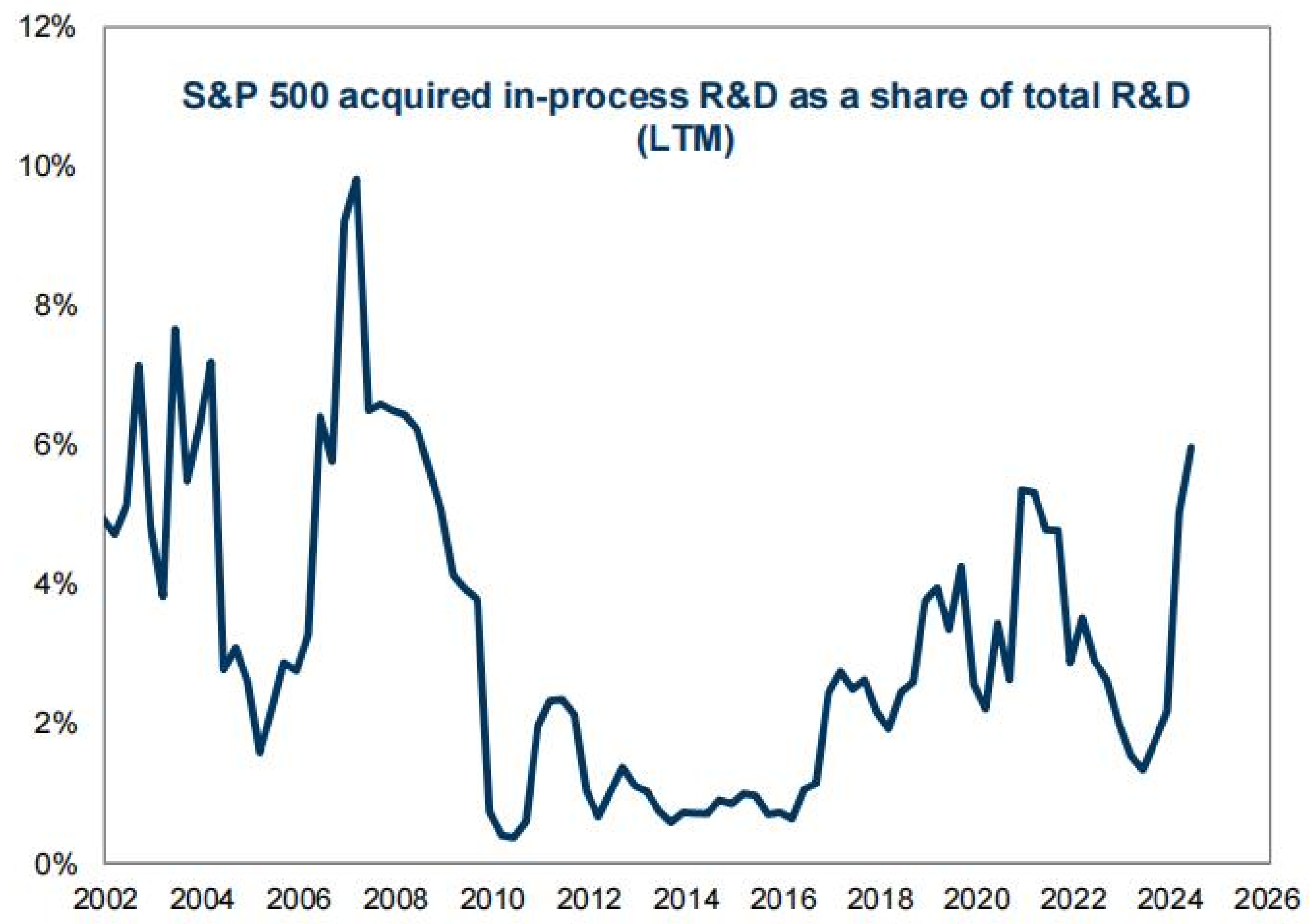
Chart

Exhibit 17: Acquired in-process R&D expensing has supported R&D growth



Source: Compustat, Goldman Sachs Global Investment Research

Exhibit 18: Acquired in-process R&D has comprised a growing share of R&D



Source: Compustat, Goldman Sachs Global Investment Research

NEW EIC

Takeaway(1-2 pages)

Risk Management

- **Policy changes pose two-sided risks to the capital spending forecasts。** Policy uncertainty has constrained corporate cash spending, but it has declined by 14% in 2024. Resolution of uncertainties around the upcoming election and Federal Reserve policy could further reduce uncertainty. Despite this, potential risks such as tariffs, corporate tax reforms, and regulatory changes could cause significant adjustments in capital spending forecasts.
- **Corporate cash balances remain high relative to long-term averages but have deteriorated。** Corporate cash balances are still high compared to long-term averages, with cash-to-assets ratios in the 67th and 65th percentiles for the aggregate index and the median stock, respectively. However, both have sharply declined in recent years, falling below the 10-year average.

Our Idea

- Looking ahead, the outlook for cash spending appears more **positive**. As earnings growth is expected to reaccelerate, companies will generate more cash flow. Additionally, the Federal Reserve's recent decision to cut interest rates has pushed bond yields lower, which could incentivize firms to issue more debt, making it easier for them to raise funds. This improvement in financial conditions is expected to contribute to an increase in corporate cash balances. As a result, businesses may have more liquidity available for capital investments, stock buybacks, or other financial strategies moving forward, reversing the trend of decline seen in recent years.

NEW EIC