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MARKET REACTION TO BUYBACK OF SHARES: NSE LISTED COMPANIES

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ABSTRACT
This paper is an attempt to examine the market reaction to share buybacks of a sample of 66 buyback announcements made through open market offer for a period from April 2004 to March 2014. The companies chosen for analysis are listed only on the National Stock Exchange of India. The present study uses the market model to analyze the market reaction of buybacks in relation to share price. The net/overall effect is the sum of the all effects at different stages like before buyback price effect (BBB), during the buyback offer price effect (DBB) and the post-buyback price effect (ABB). The analysis has shown that the share price has risen in 62% of buyback cases in all scenarios. Thus, it could be stated that the full positive effect of share buyback on share price is realized before; during and after the buyback process.

KEYWORDS
NSE companies, buyback of shares, market reaction.

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INTRODUCTION
Share buyback (or stock repurchase) is the reacquisition by a company of its own stock. In simple words, Buyback can be considered as the reverse of issuing shares by a company as it offers to take back its shares owned by the investors at a specified price.

Buyback of equity shares is a capital restructuring process. It is a financial strategy that allows a company to buy back its equity shares and other securities. In a changing economic scenario corporate sector demands more freedom in restructuring debt-equity mix in times of favorable business environment.

Capital restructuring is a type of business operational strategy that is employed to make changes to the capital structure of a company, usually as a way to deal with shifts in the marketplace that have impacted the financial stability of the business. Just like renovating a house can make it more attractive, capital restructuring makes companies attractive to potential stakeholders, reduces costs, increases efficiency, increases EPS and gives better returns.

Financial restructuring is the reorganizing of a business' assets and liabilities. The process is often associated with corporate restructuring where an organization's overall structure and its processes are revamped. Financial restructuring involves either internal or external restructuring (i.e. Mergers and Acquisitions). In the internal restructuring an existing firm undergoes through a series of changes in terms of composition of assets and liabilities. Whereas in the external restructuring firm acquires another company or merges with another company to expand its presence.

Share buybacks became popular in the US in 1980's although the concept was introduced in 1960's. The system of buyback was considered to be one of the most liberal one as it allowed companies to repurchase shares by borrowing funds and it wasn't mandatory that repurchase has to be made only out of the undistributed profits or reserves. In UK share repurchases were introduced in 1980's and in other European countries shares repurchases became popular in mid 1990's as government had either prohibited buybacks or the tax laws were very stringent. The restrictions were gradually released in late 1990's. The period between 1995 to 2000 witnessed lot of share buybacks in European countries like Finland, Germany, France, Denmark and Sweden. Even in Asian countries share buybacks became popular in late 1990's (Japan-1995, Malaysia 1997 followed by Singapore and Hong Kong in 1998 and Taiwan in 2000).

In India till 1998 share buybacks were prohibited. Section 68, 69 and 70 of the Companies Act, 2013 and Rule 17 of Companies (Share Capital and Debentures) 2014 deal with buy back of Securities. The Act and the Rules both prescribe the permitted resources and the permitted methods for buy back of Securities. Both the Act and the Rules not only list out various criteria to be fulfilled for a buy back but also the rules to be followed for buy back. Section 69 deals the accounting treatment on account of Buy back of Securities and Section 70 gives the list of things that the Company should not have done in order to make them eligible to go for a buy back. The provisions regulating buyback of shares are contained in Section 77A, 77AA and 77B of the Companies Act, 1956. These were inserted by the Companies (Amendment) Act, 1999. The Securities and Exchange Board of India (SEBI) framed the SEBI(Buy-back of Securities) Regulations,1999 and the Department of Company Affairs framed the Private Limited Company and Unlisted Public company (Buy-back of Securities) rules,1999 pursuant to Section 77A(2)(f) and (g) respectively. The SEBI Buy Back of Securities (Amendment) Regulations, 2012 has introduced a few significant changes in buy-back guidelines regulating Indian companies contained in:

- Companies Act, 2013
- Companies (Share Capital and Debentures) Rules, 2014
- Securities and Exchange Board of India (Buy-back of Securities) Regulations, 1998 and Securities and Exchange Board of India (Buy-back of Securities) (Amendment) Regulations, 2013

LITERATURE REVIEW
Share buybacks have become a common phenomenon worldwide in recent years. Global increase in repurchase activity seems to be a result of deregulation, tax changes, shareholder value maximization as a growing corporate objectives and the growth of employee stock ownership plans. Financial literature shows too much return subsequent to stock buyback program in developed market. There are three methods of buyback of shares in India namely tender offer, open market buyback and targeted buyback in the U.S. market.

Vermaelen (1981) formalises the signaling theory of share repurchase to explain the stock price reactions associated with share repurchase. The information signaling theory has more predictive explanation for the post repurchase abnormal returns. Repurchase at a premium using tender offers signifies that the future prospects are more likely to improve. The author also reported that the quantum of premium offered to shareholders was positively associated with the percentage of outstanding shares bought back and the fraction of shares owned by managers. This may be taken as the signaling explanation.

Asquith and Mullins (1986) emphasized on proving the superiority of share repurchases over dividends in market signaling. The support provided by announcement of share repurchases to an otherwise falling stock is unquestionably better and for longer duration than dividends. Managers take interest in sending bigger signals through repurchases, as managerial incentives are related to stock performance. Hence, higher the managerial interest, bigger the signals being sent to shareholders.

Inkberry et al., (1996) made a comprehensive examination of US Open Market repurchase programs during the 1980s. In their study, they have found that the market's initial response to repurchase announcements is not complete in nature. They have actually reported abnormal performance of 2.9% over a four-year period following the announcement. For value stocks where a stronger case can be made for under valuation, the annual abnormal return was reported to be 6.4% over the same post announcement period.

Stephens and Weisbach (1998) assert that repurchase is negatively related to the prior stock price performance. In other words, undervalued shares perform better subsequent to a share repurchase announcements.

Grullon and Michaely (2004) took a sample of 4443 open market repurchase announcements falling between 1980 to 1997 in this regard. They reported the predictions of market experts and found expectations of incremental improvements in EPS following repurchase announcements.

Unlike US the rules for share buybacks in India are quite stringent. There were very fewer studies on buybacks when compared to developed countries due to the reason that until 1998 Share buybacks were prohibited in India.

Mohanty (2002) in the study of 12 buybacks in India found a 3.86 percent return on the announcement day to document the first evidence of positive signalling in Indian context. In a study of 25 buybacks between 1999 and 2001, **Mishra (2005)** found short term gain for the shareholders.

Sunitha (2005) examined market reaction to announcements of stock repurchases and dividends of 22 firms in the BSE 500 index during 2002-2004, and choice between the two-payout methods (i.e stocks repurchases and dividends) and found that stock repurchase programs recorded a high cumulative abnormal return of 3.2 percent within two days of the event, whereas dividend announcement recorded a high cumulative abnormal return of 2.1 percent within one day of the event. There was no significant difference in abnormal returns as result of various repurchase levels.

Gupta (2006) studied 46 buybacks between 1999 and 2005 and documented further evidence for the positive signalling by having observed a significant abnormal return of 1.66 percent.

Hyderabad (2009) showed a statistically significant average abnormal return of 2.76 percent on the announcement day for the 70 corporate buyback announcements made during the period 1999 to 2007 to support undervaluation hypothesis and documented non sustainability of abnormal returns in the post event period.

Ishwar (2010) studied 106 BSE listed companies, which announced buybacks during the period from 1999 to 2006 and found an average abnormal return of 2.23 percent, but that was not statistically significant on the event day to signal the under-pricing of securities. The author opined that the market has not found any news in the announcement as revealed by the continuing trend that started before the announcement and the market anticipate the information and incorporated into prices before the announcements.

Dhatt (2010) suggested a statistically significant abnormal return of 2.55 percent on the event day for 40 cases listed in BSE for a period between 2004 and 2009, thereby signalling undervaluation. All the above studies were taken up in different time horizon and except one study all the other supported the undervaluation assumption or positive information signaling.

S.Narayan Rao (2010) examined the effects of announcement of offer of open market buyback in India. The sample consists of 64 open market share buybacks offer during 2003-June 2010. The evidence suggested that significant sustainable increases in firm values occur around the announcement of buyback offer. The results support information signaling hypothesis of share buyback.

Kaur Karamjeet and Singh Balwinder (2010) in their paper analyzed the market reaction to the share buy-back announcements of companies listed on BSE for the year 1999-2004 by employing event study methodology with Sensex as the market index and found that market reacts positively to the buy-backs. Further, abnormal returns are tested for information signaling, free cash flow and leverage hypotheses. Results reveal that only leverage and under-valuation hypotheses were found valid whereas signaling and free cash flow hypotheses were rejected.

Kaur Karamjeet (2012) reported out that the impact of open market share buy-back announcements on share prices of BSE listed companies. A total of 172 events of share buy-backs through open market have been found during March 2001 to March 2012. About 55% of open market share buy-back events experience positive returns on the announcement day. Returns are positive even before the announcements Further, it is seen that post-announcement returns are very small, insignificant and mostly negative.

Bunny Singh Bhatia (2013) empirically examined the effect of share repurchases on stock price. They found out negative abnormal returns prior to the announcement of buy-back during 2011-2012 indicating undervaluation of shares and positive abnormal return post announcement, indicating signaling effect of share repurchases. Besides, a small company tends to have higher price reaction than larger companies due to higher information asymmetry faced by small companies. The results are similar to the study of open market repurchases in Developed countries.

Harikrishna M (2014) studied the effect of share buyback on stock price of Reliance industries. It was found out that RIL has underperformed the benchmark with poor returns prior to the announcement of buyback, indicating undervaluation of shares and positive abnormal return in the post announcement indicating signaling effect of share buyback during 2011-2013.

OBJECTIVE OF THE STUDY
The objective of the study is to analyze the 'Market reaction to buyback of shares in NSE Listed Companies'.

DATABASE & METHODOLOGY
Share buy-back announcements for the period from April 2004 to March 2014 in National Stock Exchange only were considered. For the study, NSE Top 500 listed companies with the market capitalization as on March 31, 2013, were considered for inclusion in the sample. The sample of 66 buyback announcements was framed for usage on the basis of aggregate buyback amount.

Everyday closing price of shares in NSE is taken for the study. The public announcement dates of share buybacks are available on www.sebi.gov.in. The study is based on secondary data which is collected from published Annual Report; Journals; and Magazines and from various websites - sebi.com, nse.com, etc. For the purpose of study, MEAN has been used to examine the market reaction to share buyback. An attempt is made to investigate the difference in market reaction to share buyback between pre-buyback, Announcement buyback, during buyback and post-buyback phases.

Before (Pre) buyback	–	BBB
After Announcement buyback	–	AaBB
During the buyback	–	DBB
After (Post) buyback	–	ABB

The method of measuring the price effect of share buyback involves a comparison of the share price at three different points of time, as shown below:

POINTS OF TIME DISTINGUISHED

CHART 1

PRE-BUYBACK (BBB)

Mean share price (3 months **before** the buyback offer opening date)

ANNOUNCEMENT BUYBACK (AaBB)

Closing share price on the buyback offer **announce-ment** date

DURING BUYBACK (DBB)

Mean share price (**Actual** period of buyback offer)

POST-BUYBACK (ABB)

Mean share price (3 months **after** the buyback offer clo-sure date)

ANALYSIS & FINDINGS

Impact of share buy-backs on company's share price movements are a result of a bundle of factors such as company fundamentals, demand and supply of particular scrip and various corporate announcements and unpredictable global factors. The sensitive National Stock Exchange in India etc. reacts to these factors. Buy-back of shares an important event also affects the share price movements. The impact of share buy-back on company's share price movements is analyzed for four different stages i.e. pre-buy-back phase, announcement buyback, during buy-back and post buy- back phase.

EFFECT OF SHARE BUYBACK ON SHARE PRICE

TABLE 1

Points of Time Distinguished	No. of Cases (%age)		
	Positive	*Negative*	*Total*
AaBB Vs BBB Effect	36 (54.5)	30 (45.5)	**66 (100.0)**
BBB Vs DBB Effect	41 (62.1)	25 (37.9)	**66 (100.0)**
DBB Vs ABB Effect	46 (69.7)	20 (30.3)	**66 (100.0)**
BBB Vs ABB Effect	40 (60.6)	26 (39.4)	**66 (100.0)**
Sum of Effect	**61.7**	**38.3**	**100.0**

**Figures in parentheses are percentages.*

AaBB Vs. BBB Effect

From the viewpoint of measuring the effect on share price, the greatest importance attaches to the net change between the (a) two months pre - buyback price (BBB) and (b) the price on announcement day of buyback (AaBB). As regards (a), the closing share price of two months before the announcement date of the offer. As regards (b), the closing share price on announcement date of the offer.

Data showed the magnitude and direction (upwards or downwards) of price movement due to the announcement effect. The price rise was in 55% cases and the share price dropped in 45% cases. It was noted that the effect on share price was positive and the increase was up to 10% in about 38% of the total number of cases analyzed. Another 11% of the cases showed increase more than 17%. However, there are also about 17% of the cases which showed a fall up to 10% in share price due to the buyback announcement and 29% of them showed a more than 10% decrease. Hence, it could be stated that there is a meager effect on share prices due to the announcement as 45% cases were showed negative impact as well.

BBB Vs. DBB Effect

From the viewpoint of measuring the effect on share price, the greatest importance attaches to the net change between the (a) pre - buyback price (BBB) and (b) the price of the period during buyback offer (DBB) (i.e. 'from start to finish' of the buyback process). As regards (a), the mean share price of three months before the opening date of the offer. As regards (b), the mean share price during the buyback period from the opening date of the offer till the closure date of the offer.

The price rise was in 62% cases and the share price dropped in 38% cases. It was noted earlier that the effect on share price was positive and the increase was up to more than 10% in about 35% of the total number of cases analyzed. Another 27% of the cases showed increase up to 10%. However, about 24% of the cases showed a fall of more than 10% in share price after buyback announcement and 14% of them showed a fall up to 10%.

DBB Vs. ABB Effect

Regarding the actual post buyback effect, it needs to compare the share prices at the following two points of time: (a) the price during the period of the buyback offer (DBB) and (b) the price after 3 months from buyback closure date (ABB). As regards (a), the mean share price during the buyback which is the period from the opening date of the offer till the closure date of the offer. As regards (b), the mean share price of three months immediately after the closure date of the offer. The price rise was in 70% cases and the share price dropped in 30% cases.

It was noted earlier that the effect on share price was positive and the increase was more than 10% in about 45% of the total number of cases analyzed. Another 25% of the cases showed increase up to 10%. However, there are also about 20% of the cases which showed a fall of more than 10% in share price after buyback announcement and 10% of them showed a fall up to 10%.

BBB Vs. ABB Effect

From the viewpoint of measuring the effect on share price, the greatest importance attaches to the net change between the (a) pre - buyback price (BBB) and (b) the price after three months from buyback closure date (ABB). As regards (a), the mean share price of three months before the opening date of the offer. As regards (b), the mean share price of three months immediately after the closure date of the offer.

Data showed the magnitude and direction (upwards or downwards) of price movement after the buyback. The price rise was in 61% cases and the share price dropped in 39% cases. It was noted earlier that the effect on share price was positive and the increase was up to more than 10% in about 50% of the total number of cases analyzed. Another 11% of the cases showed increase up to 10%. However, about 26% of the cases showed a fall of more than 10% in share price after buyback announcement and 13% of them showed a fall up to 10%.

Overall Effect

The net/overall effect is the sum of the all effects like before buyback price effect (BBB), during the buyback offer price effect (DBB) and the after-buyback price effect (ABB). It is the change in share price measured from the pre-announcement date (three months before the buyback announcement) including up to the closing day of the buyback offer and after three months from the closing day of the offer. The analysis has shown that measured in this way, the share price had a rise by more than 64% (40 cases) buyback cases in all scenarios. Thus, it may be said that the full positive effect of share buyback on share price is realized before; during and after the buyback process is completed.

OVER-ALL EFFECT OF SHARE BUYBACK ON SHARE PRICE

TABLE 2

Points of Time Distinguished	No. of Cases (%)		
	Positive	*Negative*	*Total*
BBB Vs DBB Effect	41 (62.12%)	25 (37.88%)	**66 (100.0%)**
DBB Vs ABB Effect	46 (69.70%)	20 (30.30%)	**66 (100.0%)**
BBB Vs ABB Effect	40 (60.60%)	26 (39.40%)	**66 (100.0%)**
Sum of Effect	*64.14%*	*35.86%*	*100.00%*

CONCLUSION

The present paper investigated the impact of open market share buybacks on share prices of NSE listed Companies. It was found out that the shares are quite undervalued before the announcement of share buyback programs. Further, Positive mean of share prices after the share repurchase program completion indicate that market reacts positively to the news of share buybacks. It is necessary that market should have more reliability and confidence in the buyback programs of corporate. The results of share price movements has shown that buyback effect resulted in a rise in price three months before announcement date of the offer (pre buyback period) thereby, supporting management's contention of undervaluation of shares. Besides, an analysis of the mean share prices shows that there was an increase in the mean share prices after buyback as compared to the mean share prices for pre buyback period. However, the overall effect of buyback on the share prices is the algebraic sum of the pre buyback effect, announcement effect, during the buyback program effect and the post buyback effect. The analysis has shown that measured that the share price had risen more than 62% of buyback cases in all scenarios except in announcement effect i.e. 55% only. Thus, it may be said that the full positive effect of share buyback on share price is realized before; during and after the buyback process is completed. These results lead to acceptance of both undervaluation and signaling hypothesis. Share repurchase becomes stronger signaling tool.

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