Announcement Effects of Share Buyback: Study of IT Companies Listed on NSE

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Abstract— **This paper examines the reaction of market share prices on announcement of share buyback, as a tool of restructuring of shares and the regulation of buyback practices in India. Companies announce buyback of shares either to increase the value of issued shares or to eliminate any fear by shareholders who may be looking for a controlling stake. The effect of announcement of buyback is always revealed on share prices. The Information Technology companies are chosen for study which is listed on the National Stock Exchange of India. The provisions regulating buyback of shares are enclosed in Section 77A, 77AA and 77B of the Companies Act, 1956. These sections were inserted by the Companies Amendment Act, 1999. The paper reveals the previews of the buyback of shares by IT companies and its impact on financial performance of the company.**

Index Terms— **Buyback, capital restructuring, Securities and Exchange Board of India (SEBI), tender offer, shareholding**

I. Introduction

A Share buyback refer to the repurchasing of shares by the issuing company itself. A buyback occurs when the issuing company pays shareholders the market value per share and re-absorbs that portion of its ownership that was previously circulated among public and private investors. With stock buyback, also denoted to as share buyback, the company can buy the stock in the open market or buy it back from its shareholders directly. Subsequently companies raise equity capital through the sale of common and preferred shares, it may seem counter-intuitive that a business might choose to give that money back. However, there are many reasons to provide a repurchase of shares by the organizations to improve their financial ratios. In most of the countries, a company can repurchase its own shares by offering cash to existing shareholders in exchange for a fraction of the company's outstanding equity; that is, cash is exchanged for a lessening in the number of shares outstanding. The company also retires the repurchased shares or keeps them as treasury stock, available for re-issuance.

Share repurchases started later in Europe than in the United States, but now a common exercise around the world. India recognized of share buyback system in late 1998. Till then, the Companies Act in India had harshly prohibited for buying back own shares to the companies. Under Section 77 (1) of the Act stated: “No company limited by shares, and no company limited by guarantee and having a share capital, shall have power to buy its own shares to the shareholders, unless the resultant lessening of capital is effected and endorsed in pursuance of Sections 100 to 104 or of Section 402.” Such decreasing of capital could be effected only after shareholders’ agreement finished a special resolution and also the creditors’ consent and the court’s sanction. There were some special factors which impelled the Indian authorities to consider introducing the share buyback system. Around 1996, the Indian government and business houses became greatly concerned about the extended depression in the stock market. All the efforts of the government to recover the market had proved in unprofitable. The stock market’s revitalization had become a subject of wide public debate. The business houses ready a case for share buyback as a possible way of refreshing the capital market. Share buyback are believed to insert some elasticity into share prices because share buyback price is invariably higher than the market price prevalent before the buyback announcement by a company. Business houses promoted for it with the Government which readily accepted it and decided to implement it on urgent basis through a Regulation. The Regulation was announcement on 31st October, 1998, adding new Sections 77A, 77AA and 77B in the Companies Act. We thus find that international acceptance of share buyback had emerged well before India decided to jump on the buyback craze in 1998. In the chapters that follow we shall study how this has worked in actual practice in India.

After the passing of resolution but before making buy-back, announcement of solvency needs to be filed and signed by at least two directors of the company with the Registrar and the SEBI. A company shall not directly purchase its own shares or other specified securities through subsidiary company including its own subsidiary companies.

SEBI guidelines for repurchase of shares are as follows:

1. **Notice of special resolution:** The notice of special resolution to be passed by the members should contain in descriptive details of buyback program as prearranged in Schedule I of SEBI Regulations.
2. **Buying from Members through Tender offer:** Under this method, the maximum price of share at which the company expects to repurchase shares should be indicated in the notice of the general meeting. If the promoters aim to offer their shares for repurchase, details should be given in the notice in the general meeting. The company should make a public announcement of the buyback of shares through the one English National Daily, One Hindi National Daily and One regional newspaper daily,

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all with wide movement giving details prescribed in Scheduled II of SEBI Regulations.

The public announcement about the 'specified date' for the purpose of responsible the names of shareholders to whom letters of offer shall be sent. Draft offer letter giving prearranged details should be submitted to SEBI along-with prearranged fees, at least 20 days before dispatch of letters of offer to shareholders. Offer for buyback will remain open for minimum 14 days and maximum 28 days.

Letters of offer should be sent or mailed to the shareholders well in advance so as to reach them before the opening date of the offer. If the approved shares more than the number of shares offered to them for buyback by the shareholders, the actual buyback will be on prearranged proportionate basis. The company should transfer the amount of buyback the shares in shareholders account. Within 16 days of closure of offer for buyback, payment should be complete or regret letters should be sent to the shareholders.

3. **Buyback through Stock Exchange:** In case of buyback of shares through stock exchange route, the members of special resolution should decide maximum price at which shares can be bought and the buybacks should not be made for promoters or persons having control in the company. There is no specified date. Such persons should not deal in shares in stock exchanges when offer for buyback is open.

The company should appoint a merchant banker for the buyback program. Public announcement should be made at least 7 to 8 days earlier to commencing of buyback. A copy of public announcement is to be filed with SEBI along-with prearranged fee within 2 days of such announcement. Companies buying back via stock exchange route must disclose purchases daily. Details of shares purchased every day should be informed to the stock exchanges. Payment will be made as per rules of trading in the stock exchanges.

II. Review of Literature

Ikenberry and Vermaelen (1996) found that announcement returns are directly related to the volatility of the stock and the fraction of shares to be purchased. They also found that the market reaction is negatively related with the correlation co-efficient between stock returns and market returns.

Ishwar (2010) studied approx. 105 BSE listed companies, which announced buy-backs during the period from 1999 to 2006 and found an average abnormal return around of 2.22 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.

Skjeltorp (2004) analyses the market response to share repurchases by Norwegian companies for 19982001 period and finds statistically significant two-day CAR of 0.88% for 100 companies announcing first repurchase. For subsequent repurchases, the CAR shows a declining trend. The CAR for second buyback of 81 companies is 0.39%. The CAR becomes negative when 22 Norwegian companies announce 10th buyback. Howe and Jain (2006) study share repurchase programs of banks in US and find a CAR of 1.86% for first buyback, 2.15% for second buyback and 0.50% for third buyback, which is statistically irrelevant.

Andoain, Bacon, and Frank (2009) studied whether the shareholder can make an above normal return by relying on public information impounded in a stock split announcement. Results suggested that the firms' public stock split announcements did not affect stock price on the announcement day of results, buyback, dividend, bonus, ESOP, etc.

Purnima P. Jariwala (2011) analyzed the effect of share price variations in share repurchase program or announcement of opening date to closing date. 67% of the companies increase their share price after buyback than before buyback. Raju (2013) share repurchase is not observed as an important mechanism of distributing excess cash in India, it is very difficult to arrive relating to dividend substitution effect in India compared to US. Voss 2012, the main aim of this paper why companies are going for share repurchase program several reasons are behind that buyback. This author focused mainly undervaluation of shares. Firms and internal investors knows that share price than outside investors so firms gets informational advantage for buyback it share price is below the true value.

Andriosopoulos and Hoque (2013) reported that firm size, cash dividend, and ownership concentration have a significant impact on the repurchase decision of the firms in all these countries (UK, Germany and France). The results show that large and widely held firms are more likely to make share buyback announcement and also found a complementary relationship between dividend payment and share repurchase in UK and Germany.

Objectives of study

The objectives of Share buyback in India include the following:

1. To find out trend of share prices pre and post buyback announcement.
2. To help shareholders earn greater return out of their investment in IT companies coming with buyback of shares.
3. To suggest on improve of financial health of investors after buyback.
4. To suggest exit route to the shareholders from the shareholdings.

III. Study Period

Samples are collected from Securities Exchange Board of India (SEBI) and National Stock Exchange (NSE) and selected the companies which announced buyback between August 2016 and March 2018. It resulted in a sample of 9 IT companies.

IV. Data Analysis and Interpretation

These IT companies are announced for the buyback of shares. See in table 1. Public announcement of floor price of the share, starting date and end date, buyback size though the NSE, SEBI, or newspapers.

Scrip name	AD of buyback	Starting date	Closing date	Floor price	Buyback size
ECLERX SERVICES LTD	22-Dec-17	22-Feb-2018	8-Mar-2018	2000	1290000
INFOSYS LTD	21-Aug-17	30-Nov-2017	14-Dec-2017	1150	113043478
WIPRO LTD	20-Jul-17	29-Nov-2017	13-Dec-2017	320	343750000
MINDTREE LTD	28-Jun-17	18-Aug-2017	1-Sep-2017	625	4224000
NUCLEUS SOFTWARE EXPORTS LTD	25-Apr-17	16-Aug-2017	31-Aug-2017	350	3343000
HCL TECHNOLOGIES LTD	20-Mar-17	12-Jun-2017	23-Jun-2017	1000	35000000
TATA CONSULTANCY SERVICES LTD	20-Feb-17	18-May-2017	31-May-2017	2850	56140351
MPHASIS LTD	14-Mar-17	12-May-2017	25-May-2017	635	17370078
HEXAWARE TECHNOLOGIES LTD	25-Oct-16	2-Feb-2017	15-Feb-2017	240	5694835
ECLERX SERVICES LTD	29-Aug-16	28-Nov-2016	9-Dec-2017	2000	1170000
Note: **AD :**Announcement Date					

During the period of buyback offer, i.e., from opening day of the offer to its closing day, the post-buyback outcome has been studied and it has been noted that share price of more than 15% of the firms announcing buyback has gone up. The similar movement can also be noticed in the longer period from start to finish, i.e., on comparing share price on the closing day of the offer and the price before two months of announcement is made is also positive.

Table2. Variation from announcement date

Scrip Name	Price on AD	Price on CD	Price 3 months post CD	Buyback premium over AD price	Price changes from AD to CD	Price changes from AD to 3 month post CD
ECLERX SERVICES LTD	1400.1	1357.2	1297.2	600	(42.9)	(102.9)
INFOSYS LTD	924	1013.1	1180.8	226	89.1	256.8
WIPRO LTD	270.75	287.2	296.6	49.5	16.45	25.85
MINDTREE LTD	525	460	530.5	100	(65)	5.5
NUCLEUS SOFTWARE EXPORTS LTD	286.9	286.75	567.45	63	(0.15)	280.55
HCL TECHNOLOGIES LTD	871.95	851.85	874.05	128	(20.1)	2.1
TATA CONSULTANCY SERVICES LTD	2425	2546.6	2496.35	425	121.6	71.35
MPHASIS LTD	580	574.15	614.45	45	(5.85)	34.45
HEXAWARE TECHNOLOGIES LTD	197.5	210.2	255.35	42.5	12.7	57.85
ECLERX SERVICES LTD	1640	1488.3	1387.25	360	(151.7)	(252.75)
Note: **AD :**Announcement Date **CD :**Closing Date						

The announcement of a share buyback by the firm should lead the share price due to shareholder heterogeneity. The announcement of share buyback manages to prop up the shares for few sessions. These companies have been able to achieve greater returns for the shareholders. From the Table2, one can also probe the relationship between the premium offered and share price behaviors. The company's share prices have rather fallen over the prices that were prevailing at the time of announcement of buyback, thus completely missing the target of giving a push to share prices.

These findings are in direct disparity with many past studies, where the announcement effect is pronounced and leads to knowingly high and low returns. However, this may be an inspiring sign for the Indian Stock market. The effect of buyback announcement on share price is positive with reference to IT companies. When buyback of shares is announced then the share price goes up means the buyback news gives good return. Buyback of shares is fundamentally a method of readjusting the capital structure of the company and as such does not reverse the warning of shareholder wealth maximization. The fact that the announcement of buyback is not having a significant effect on the share price implies that the information is quickly listed in the share price and thus the market is moving towards being informational efficient.

SUGGESTIONS

1. If shareholders buy shares for the buyback, at least hold for the 3 months after closing the buyback program. It may be high profitable in mostly cases.
2. An Investor shall purchase shares on the date of announcement for repurchase because the price of shares tends to increase for once definitely.

CONCLUSION

Buyback of shares as a process of capital restructuring which allows a company to buyback its own shares, which were issued by it earlier. Companies' buyback shares either to increase the value of shares. It also signals undervaluation of the Company's shares in relation to its intrinsic value. It appears that only financially sound companies should be able to resort to buy-back. Companies should follow the principles of model corporate governance and there should be transparency in buy-back deals. In a one and half year the IT companies buyback offer size is 581025742 shares and good returns before opening dates of buyback. In the year ahead, the business environment will continue to remain challenging and competitive intensity is likely to remain high. IT companies delivered healthy results.

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