CHAPTER II
REVIEW OF LITERATURE

2.1 INTRODUCTION

Buyers of shares called shareholders or stockholders and they were the legal owners of the firm whose share they hold. Shareholders invested their money in the share of the company in the expected of a return on their invested capital. Pandey (2013)

The companies can buyback or repurchase their own shares for several reasons. Companies can use their profits in two ways that was a portion of profit can be distributed to shareholders in the form of Dividends or buyback of shares and the other portion of profit can be utilized for investing in the further growth of the company. Buyback of shares in India was restricted till 1998 and after which it was believed that the Buyback of shares might encourage the promoters to strengthen their holding in the company by utilizing the financial resources of the company.

Companies announced their buyback as a substitute to dividends. Once a company repurchases their own shares, it decreases the shares held by the public. Once announced the buyback of shares that the companies were able to profitably repurchase share when the company was held by trade investors and added likely to sell their shares to the company after those shares were undervalued.

Buyback of shares have been popular in many other countries like United States of America, Canada, Germany, Japan and United Kingdom. In the year 1980-1990, started the Buyback of shares program in their countries. Under the Securities and Exchange Commission (SEC) procedures, buy back of shares by US corporations can be done in four different methods, namely, open market repurchases, fixed price tender offer, Dutch auction tender offers and privately negotiated repurchase.

The Law and Rule of buyback of shares was enforced in the UK and the USA in 1980s. Since then buyback has enabled a company to pay off its surplus cash especially when the marginal return on its funds was relatively lower, the solvency and liquidity position of the company was bound to get affected by buyback as well.

2.2 Purpose of Review of Literature
A literature review was an evaluate report of studies found in the literature related to a select area. In this case, the researcher has reviewed the literature made by other authors across the globe. In terms of a literature review, "the literature" means the works you consulted in order to understand and investigate your research problem.

According to Cooper (1988)' the literature review used as its database reports of primary or original scholarship, and did not report on new primary scholarship itself. The primary reports used in the literature may be verbal, but in the vast majority of cases reports were written documents. The types of scholarship may be empirical, theoretical, critical/analytic, or methodological in nature. Second a literature review seeks to describe, summarize, evaluate, clarify and/or integrate the content of primary reports.'

The purposes of literature review in the research work a very important component. The previous studies help to analyse and interpret the findings in the current study. This chapter will give a broad idea and will cover the all historical research and events on buyback of shares in both India and other countries. There was an impact of Buyback of shares activity in India and other countries. The literature review has shown lights on the phenomena of buyback of shares of the countries. These reviews have given the perception of company participated in the buyback of shares.

2.3 Purpose of Buyback of shares in India

Financial Markets were not able to correctly measure the meaning of repurchase announcements, because companies were very often announce the repurchase. The main purpose of Share Repurchase was Companies can use their profits in two ways.

- One part of profits can be distributed to shareholders in the form of dividends or stock repurchase.
- Remaining profit called Retained Earnings are set aside for further investments in future growth for the company.

2.4 Definition of Terms used in Research Review of Literature

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Share Repurchase or Buyback of Shares

A Company can repurchase their own outstanding shares.

Signaling

Repurchase announcement serves as a signal from more informed managers that the firm was undervalued. (Janas Rosbran, 2011)

Undervaluation

An Undervalued stock or share that selling price was below the intrinsic value.

Abnormal Returns

Abnormal returns has the difference between actual returns of a shares and expected returns of a shares

Dividend

Dividend is a portion of company profit and it is distributed to company shareholders.

Liquidity

The Capability of convert an asset or security into a cash easily.

Event Window

A Period over which event occurs

Announcement Day

The date announced about buyback of shares (Commencement date of buyback)


2.5 Effects of Abnormal Returns on Buyback of Shares

Alice et al (2013) explained the abnormal returns of repurchasing firms with net insider buying versus net insider selling in a given quarter were significantly higher for the quarter immediately after the repurchase and the three subsequent years. For repurchases accompanied by net insider selling, abnormal returns were negligible after only one year. Share repurchases associated with net insider selling were positively related to illiquidity, option exercises by insiders and pre-repurchase returns and negatively correlated with industry-adjusted book to market ratios when compared to other repurchases.

Andreas and Alexandre (2006) studied on abnormal returns for the period from May 1998 to April 2003. This author that found positive abnormal returns of 5 percent around the statements to seek approval by the annual general meeting of shareholder (AGM), and abnormal returns of almost 7 percent at the time of the repurchases. By taking these two
events together, the valuation effects sum up to about 12 percent. These reports announcement effected four times higher for Germany than reported in studies for the U.S.

Amedeo et al (2012) showed that companies tend to buyback of shares when the share price was slopes down. And also showed that there were negative abnormal returns in preceding months of buyback and positive abnormal returns in periods of following months with repurchase activity. Samples were only 4795 companies in the U.S Companies of the Whole Universe (listed on NYSE, NASDAQ and AMEX).

Balachandran and Faff (2004) conducted a study in Australian firms, and reported an average mean abnormal return of 2.72 percent for the three days surrounding the announcement of an on market buyback over the period 1996-1999, and also the abnormal returns of 3.3 percent for the same window over 1996-1998 using a sample of on and off market buybacks over the period 1996-2000.

Bayer, et al (2007) concentrated on the announcement effects of open market repurchases in Germany covered a period from 2000 to 2005. The authors found on average positive and significant cumulative abnormal returns (CARs) of 5.4 percent around the announcement date.

Born et al (2004) collected samples from the year 1981 to 1997 in New York stock exchange. Data collected on the basis of 49 open market share repurchase in Insurance Companies The study examined that abnormal returns around the buyback announcement date and finds the positive wealth of the share repurchase announcements in both non-financial and financial firms.

Bradford and Bruce (2008) sample taken from US firms was identified used purchase of common preferred stock from the cash flow provided by the Compustat 723 samples were open market repurchase announcements in U.S firms. The study focused on the post event performance through buy and hold abnormal returns and cumulative abnormal returns of open market repurchase of shares by the U.S firms. Observed open market repurchase as a contingent event where the actual research activity provided significant additional information. The results confirmed that the market may underreact to the repurchase announcements, implying that strict regulation that resolves information uncertainty about stock repurchases does not necessarily prevent under reaction by the market.
Chhachhi, Indudeep and Wallace Davidson (1997) taken a sample of 117 tender offers during 1978-89 and studied abnormal returns the authors found that the sufficient evidence of higher abnormal returns in case of repurchase announcement over specifically designated dividend announcements.

Erkens, et al (2012) revealed that effects of the crisis period on the firm performance can be deducted which was partially relevant to the study. The study with a sample of 296 firms among 30 different countries, found that the transparent corporate governance policy resulted in lower stock returns during the crisis period from 2007 through 2008. The authors asserted that corporate governance had an important influence on firm performance during the crisis because of the firms' risk-taking and financing policies. The author defined firm performance by abnormal returns, calculated as the stock returns minus expected returns based on a market model, assessed over the period beginning in 2004 until the end of 2006. The abnormal returns were defined as the equity offering around the event window. Shortly, in that time frame, firms resorted to raising their equity capital to prevent a regulatory intervention when the author recognized losses associated with mortgage related securities.

Fierkans (2010) examined by taking the sample of firms listed on the Dutch AEX exchange and experienced 91 open market repurchases in the period from 2000 to 2010 revealed an average of 1.34 percent abnormal returns. For the event window, the abnormal returns accumulate to an average value of 1.68 percent. The study stated that the agency cost and the information asymmetric in the Netherland were significantly lower compared to similar US situations, and it was suggested that for this reason the abnormal returns in the Netherland was lower.

Gerke et al. (2003) examined announcements of open market repurchases for the period from 1998 to early 2002. Authors attributed the announcement returns of 6 percent to the inexperience of German firms. In addition, the author partitioned their sample according to the repurchase reasons. The author reported abnormal returns of 8.9 percent at the announcement day providing evidence for undervaluation and for the signaling hypothesis. Authors noted that abnormal returns were higher for the repurchase announcements for the period of dramatically falling stock price between 2000 and 2002.

Guojin et al (2008) studied on the long term operating performance and abnormal returns in the open market share repurchase announcements. Samples Data used in the study were collected from Security Data Company (SDC) in the period of 1984 to 2002. The study found
that negative abnormal returns mostly in open market share repurchase i.e., increased company’s percentage and managers done share repurchase. Manager’s view of the open market share repurchase to deflation earning growth in share repurchase that results indicated artificial improvement and subsequent positive abnormal return share returns.

Ian and Wang (2012) found some similarities between US and UK repurchases. Like US repurchases, UK repurchases attract positive and significant short-term abnormal returns surrounding the announcement and long run abnormal returns following the announcement. Two-year buy-and-hold abnormal returns were particularly high among value firms. The author concluded that different from the market under reaction hypothesis or the market overreaction hypothesis. The author also investigated the impact of different announcement dates on short-term and long-term share performance. The results suggested that share performance of UK share repurchases were not statistically influenced by different kinds of announcement dates.

Isa, Ghani and Lee *et al* (2011) conducted an event study on the Malaysian Stock Exchange of 149 firms between the year period 2001 to 2005 and showed a positive market reaction to the actual repurchase of shares. The study found that the pre-event abnormal returns and the event days abnormal returns clearly suggest the existence of a signaling effect of the repurchase. The author also found that the signaling effect was larger for small firms compared to larger ones. This study authors assumed that was a logical that the management of a firm have superior information about it current value and future prospects than outside investors. Therefore it was seen as a logical decision for management to buy back their own shares as a form of good investment, if the author believed that it was in fact being undervalued by the market. Because outside investors were not inform to same set of information that management has, the management’s decision to repurchase their shares will act as a signal to the market.

Isaac and Ross (2002) examined on share repurchase in Australian firm about the share repurchase announcement. The results revealed that abnormal returns of buyback motivated by the signaling and it abnormal decreases the after announcement date around three days of announcement. In addition to that researcher also finds that shareholder earned after announcement abnormal return increased and competitors firms after share repurchase announcement decreases the abnormal returns.
Jagannathan et al (2003) revealed that three types of share repurchase announcements in companies. Frequent repurchase program, Infrequent repurchase program and Occasional repurchase program. The study was conducted in SDC (Security Depository Centre). The results showed that frequent repurchase program was entirely different from Infrequent and occasional repurchase program. As for frequent repurchase program has been higher dividend payout ratios and the study suggested to buyback as a substitute for increase dividend. Final prediction of the study was infrequent repurchase program there were a two reasons i) more variation in operating income, ii) negative abnormal returns.

James (2006) said about six hypotheses in the study and there were signaling effect, agency cost, personal tax effects, inter security increases by share repurchase and corporate tax shield effect. These reasons were to expect the positive announcement for share repurchase. The study revealed that signaling hypothesis describes the abnormal returns about share repurchase announcements used event study method and regression models. It summarizes share repurchase announced by the company gives the importance of optimistic abnormal returns in their samples.

James (2013) studied on the market reaction to repurchase announcements done by Toronto Stock Exchange (TSX) firms. The announcements result in a significant market reaction as evaluated by abnormal return and volume tests. Further analysis by the indicated that firms that have followed through on past repurchase announcements and have cash on hand experienced greater announcement returns. However, most reasons provided by TSX firms for their repurchase programs were not found to be informative. These results provided and supported for the TSX requirement for firms to disclose a reason for their repurchase programs. The results were support the TSX requirement to disclose repurchases since these disclosures appear to provide investors with useful information when interpreting subsequent repurchase announcements.

Jonas Rasbrant (2011) examined that open market share repurchase initiation, impact of share price and long run abnormal returns. The study based on Swedish firm open market repurchase on daily basis on the Stockholm Stock Exchange taken samples in the year between March 2000 to December 2009. The results showed that 2 percent abnormal returns in open market repurchase announcements in two days. In first year initiation of share repurchase program 7 percent approximately long run abnormal returns. In previous studies the author found long run abnormal stock performance is consistent. An optimistic abnormal
return specifies open market share repurchase initiation assumed investor as a signal of undervaluation of share price.

Kai Li and William (2007) in their study analyzed trade analysis was possible because of a unique Canadian data set. The highest abnormal returns were earned by companies on their own repurchase trades which benefits the non-tendering shareholders. As for the public investor, their study found no strategies that, in practice, would earn abnormal returns to buying after program announcements. However, there was a qualified evidence of abnormal returns to a limit order strategy following publication of individual repurchase trades.

Open Market Repurchase (OMR) played an important role in financial strategy in any firm similar study made by Kirch et al (1998) who observed the announcement of share repurchase experienced negative Cumulative Abnormal Returns prior to announcement and also positive market response to the announcement of open market repurchase program gain the value after one year of announcement. The author have analyzed the NYSE firms open market repurchase program during the year 1980-1990. Findings made by the researcher was from simple financial statement analysis which provide some insights into the market reaction to the actual repurchase of shares as well as for investment in firms announcing open market repurchase plans.

Lee, Jung and Thornton Jr. (2005) studied the long term performance in open market share repurchase announcement firms. Their study showed that for the first two years results were negative abnormal returns for 296 buyback announcements made during 1994 to 1998 in South Korea. Lack of abnormal returns in South Korean Stock Exchange indicated high efficiency of prices.

Leonce, Manoj and Thomas (2011) found that strong evidence consistent with the costs of lost where flexibility and the benefits of Accelerated Share Repurchase (ASR) implement in the companies. In addition Accelerated Share Repurchase announcement showed positive abnormal stock returns. The study results were suggested that ASRs, on average, value-increasing events and add incremental value when announced subsequent to a repurchase program announcement.

Miller et al (2005) explained the market reaction to buyback of shares announcements in Insurance firms. The author found that open market share repurchase announcement leads the
positive abnormal returns and substantial excess returns. Insurance firms react to share repurchase announcements as related to other industries to compete with others.

Mitchell and Watson (2004) created evidence within and outside the U.S and supported the idea that on average the capital market views repurchases (both on- and off-market) as a positive signal and also initiated cumulative abnormal returns of 2.61 percent over the five days surrounding the announcement for on-market (equal access) buybacks.

Netter and Mitchell (1989) took the data of 598 stocks for year 1987, the year of great market crash and evaluated the repurchase announcements made between October 19-30, 1987. Using an event window of 40 days post announcement, researcher found a positive abnormal return and also revealed continuous outperforming of markets by such stocks. The event window of (0,40) revealed maximum abnormal returns for all stocks.

Pierre, Quintana and Hege (2006) explained that the conditions of the recent development of share buybacks in France, focusing on open-market repurchases. The author observed that share buybacks have become a common practice for the French companies, and found a positive correlation between the relative amount spent on buyback programs and the long-run share price performance, tending to suggest a positive impact of buybacks on shareholders’ value, in conformity with corporate governance principles. However, the author have found that immediate effect of buyback announcements was much smaller than in other countries, with an average abnormal return of 0.32 percent only. The author explained the quasi-universal and optional character of buyback programs announced in France.

Rajagopalan and Shankar, (2013) conducted during a 10-year period between 2001 to 2010 by taking the S&P CNX 500 index companies. By using event study methodology their studies analyzed the buyback information impact on stock returns. The author introduced an inefficient market and revised the open market share repurchase strategy and share price behavior. His model predicted and established signaling equilibrium without that assumption companies cannot commit the open market share repurchase.

Raju (2009) examined the excess returns of share repurchase in India. In announcement days of share repurchase reaction on cumulative abnormal returns and average abnormal returns were increased but it was only temporary did not continued for long time i.e., cumulative abnormal returns were decreased after the announcement and pre announcement date only
increases the cumulative abnormal returns. The study was based on 500 Index in BSE period in the year of 2000 to 2006.

Ramsay and Asjeet (2000) studied 62 buyback of shares undertaken announced by US companies found that the share market reacted positively to announcement not made as a part of takeover defense and it reacted negatively to those buy backs used by companies to prevent takeovers and suggested the management entrenchment hypothesis whereby, managers seek to retain their positions by employing a range of defensive tactics against hostile takeovers and share buy-backs which not only increased the debt-equity ratio but also reduced the number of shares available to the public. The study was concluded by the author that while a share buyback has a positive influence on the stock price, a difference exists in the performance between the methods of the buyback.

Robin and Wilber (2007) investigated firms that repurchase their stock to finance an acquisition. The samples were taken from Securities Data Corporation Mergers and Acquisition Database and Repurchase Database samples used for the study were 96 repurchase announcements between 1995 to 2002. The author found these firms were well compensated for their efforts, especially in the long run. On average, these firms have negative abnormal returns prior to their repurchase announcements and thus may choose repurchasing to signal undervaluation.

Sheng et al (2013) examined how the financial constraints of repurchasing firms affect their post-buyback performance. The authors displayed significantly poorer post-buyback abnormal return and operating performance than unconstrained firms. Financial constraints were more important in explaining the performance of share buybacks for firms with high actual repurchase ratios. Constrained firms, especially those with high actual repurchase ratios, experience a significantly greater increase in post-buyback distress risk than unconstrained firms.

Thomas et al (2008) found that firms undertaking ASR (Accelerated Share Repurchase) programs were significantly larger than those undertaking OMR (Open Market Repurchase) programs, and that ASR programs have a larger median dollar amount of deal values than OMR programs. Further, ASR firms have significantly smaller cash holdings, higher dividend payout ratios, higher pre-announcement industry-adjusted leverage ratios, and similar probabilities of being takeover targets compared to OMR firms, and ASR firms grant fewer stock options to their employees than OMR firms. Option exercise by executives not
increases following buyback announcements in either ASRs or OMRs. Stock liquidity increases following both ASRs and OMRs. Although their univariate tests reveals that ASR firms were more likely to tie the CEO bonus to EPS, their multivariate analysis does not find that EPS manipulation is a significant factor in firms chooses an ASR over an OMR program. Finally, firms undertaken ASR programs have lower pre-announcement market valuations, greater positive announcement effects, and better post-announcement operating and stock return performance, compared to those undertaking OMR programs.

Vibha Dua et al (2010), investigated the impact of buyback of shares on share prices in India. Discussed about share buyback in the literature was that the announcement has a positive impact on the stock returns before and after the event. Their study examined that the impact on stock prices, event study model has been used. This study has empirically examined the informational efficiency of the Indian stock market with regards to buy-back of shares. The results of their study showed very negligible reaction on or before the announcement date and also supported to the implications of efficient stock market in its semi-strong form. By and large market is near to efficiency in its semi-strong form. Abnormal returns around the announcement date were not significant.

Victoria, Paul and Warfield (2011) evaluated the representational faithfulness of the accounting treatment of a recent and well-established type of structured transaction—accelerated share repurchases (ASRs). ASRs were popular because accretive earnings per share benefits were recognized immediately, while any gains or losses on the forward contract used to execute an ASR bypass income, and were reported directly in equity. The author study reports showed lower value relevance for the liabilities of ASR companies compared with a size- and industry-matched sample. Finally, documented significant abnormal returns to a trading strategy based on unrealized gains or losses on ASR transactions. Their study results indicated that the current accounting for ASRs does not result in representative reporting of these transactions. As a result, financial statement users might benefit from recognition of ASR elements in financial statements.

Vithessonthi (2008) measured the whether share repurchase program contribute to long run abnormal returns. The sample on the buyback program announced in Thailand were taken in the year between 2001 and 2005 and explained about abnormal returns and how stock price influences in share repurchase program. To detect long run abnormal returns in share repurchase using buy and hold abnormal returns rather than cumulative abnormal returns to
control long run abnormal returns in share repurchase program. The results of this study mean of cumulative returns and mean of cumulative abnormal returns for the three years of share repurchase announcement was positive to stock price. Samples of the study cumulative returns and cumulative abnormal returns were greater than zero.

William, McNally and Smith (2007) found that repurchasing companies stated that share prices showed abnormal losses before the event date and abnormal gains after the event date. Significant abnormal return should be observed in a period after the repurchase announcement. When the market reacts efficiently, shares would not be undervalued anymore (on the announcement day) and the original argument for managers to repurchase shares was eliminated.

Wiyada and Aekkachai (2013) mentioned that common stock repurchase has been allowed since 2001 in Thailand. Eighty-six repurchase announcements from 69 companies listed on Stock Exchange of Thailand (SET) have been made during December 14, 2001 to May 22, 2012. The authors investigated whether repurchase announcement has any effect on the abnormal return of the listed firms or not. Event study methodology is used. Sample covers 78 announcements excluding six illiquid stocks and two recent announcements. The announcement date was set as the same date of the board of director meeting because the company must disclose the resolution to SET within the date of resolution or within 9:00 a.m. of the next business day. The result showed the positive abnormal return of 2.23 percent, on average, at 1 percent significance level. Their Graph clearly indicated that cumulative abnormal returns were significant starts before 2 days of announcement date. This was consistent with the arguments that repurchase was done when stock was underpriced and management knows about this information.

Yook (2010) studied the repurchase programs in firms that were listed on the NYSE, AMEX or the NASDAQ was conducted with the samples consisted of 9,551 repurchase programs that were announced between 1994 and 2007 by 5,014 firms. The study found strong evidence of significant abnormal long-term performance of infrequent repurchasers who actually repurchase shares during the first four quarters following their announcements versus frequent repurchasers. The researcher indicated that the market does not react to announcements of repurchase programs because the market does not necessarily view the announcement as a firm commitment to actually repurchase the shares. The researcher concluded that the extent to which the market does not fully incorporate the effect of the
repurchase announcement in a short period, the residual value of the announcement would be revealed over a longer time period.

Zhang (2005) investigated the stock price performance after actual share repurchases. On the average, repurchasing firms do not exhibit strong superior abnormal performance either initially or over long horizons. However, the performance varied across firm size and book-to-market value ratios, and showed a clear and consistent pattern. The market responded most favourably to repurchases that were made by small and value firms. The study revealed that relation between size of offer and announcement returns.

2.6 Impact of Free Cash Flow on Buyback of shares

Adri De Ridder (2014) found showed that firms with multiple repurchase programs have returns that exceed the return on stocks in firms with fewer programs by 79 basis points per month and that firms with the high cash flows have higher returns, than firms with low cash flows. The study used data from December 19, 2000 to December 2012, The author collected data from the SSE the sample consists of 145 firms with a total of 411 activated repurchase programs in the Swedish Central Security Registrar Euroclear Sweden. The author founds out that firms with frequent programs, i.e., those with three or more programs, have returns that exceed the return on stocks in firms with infrequent programs by 79 basis points per month using the four-factor model and that a portfolio of firms with high cash flow out performs a portfolio with low cash flow by 66 basis points per month.

Ben, Vishaal and Brain (2014) their study showed that dual class companies pay out less cash dividends and repurchase fewer shares and that cash distributions decrease as the divergence of voting and cash flow rights widens. This was consistent with both the private benefits and family legacy hypotheses. However, an examination of executive compensation and family participation on the board indicates that lower dividends were consistent with the private benefits hypothesis.

Bhattacharya sudipto (1979) argued that distribution of cash can be used to signal future cash-flow prospects. However, it has important to bear in mind that there was a difference between the signalling of management’s expectations of the firms’ cash-flows or earnings and the presumed incongruence in opinion of the market versus management about the company’s performance and assumed that outside investors have imperfect information about firms' profitability and that cash dividends were taxed at a higher rate than capital gains. It
was showed that under these conditions, such dividends function as a signal of expected cash flows. By structuring the model so that finite-lived investors turn over continuing projects to succeeding generations of investors, the author derived a comparative static result that relates the equilibrium level of dividend payout to the length of investors' planning horizons.

Beverly Hirtle (2003) observed the relationship between stock repurchases and financial performance for a large sample of bank holding companies. The sample includes both publicly-traded and non-publicly traded banking companies. The main result was that higher levels of repurchases in one year were associated with higher profitability and a lower share of problem loans in the subsequent year. Their results of the study revealed that driven primarily by bank holding companies with publicly-traded stock, especially those companies whose stock was traded on major exchanges. In assessing the source of the repurchase-performance link, the author found and suggested that it may be driven by different factors for different types of bank holding companies. In particular, the evidence was consistent with free-cash-flow considerations for banks traded on major stock exchanges, but only weakly supports this explanation for smaller, closely-held companies.

Blundell and Roulet, (2013) in their study focused on the US economy was improving very soberly and unemployment remains at high levels. In Europe, the recession appears to have made a leap in early 2013; banks were still eager to lend money and there was doubtfully any sign of surprise in business investment. As a whole, corporate borrowing has been strong, equity issuance has not been very durable, and firms have frequently decided to payback cash flow to shareholders in the form of dividends and buybacks.

Bozanic (2010) stated that there was a direct relation between the level of manager’s holdings, degree of negative earnings management and volume of repurchases, thereby suggesting manager’s own interest as the causa proxima for such actions. Interestingly, the level of abnormal returns was correlated to the negative earnings reported, thereby supporting temporary earnings management around repurchases by managers of such firms. There was timing factor involved whereby managers announce repurchases to match perceived undervaluation and the presence of discretionary cash flow.

Chay and Suh (2008) explained the document evidence on cash flow uncertainty, measured by stock return volatility, affecting the payout policies of companies. The managers value flexibility and place significant utility on that flexibility, the author were likely to be reluctant to distribute large cash holdings as dividends or share repurchases. The author also found that
cash flow uncertainty in explaining payout policy was independent of the firm’s life-cycle, which was important, because the fact that mature companies tend to have more stable cash flows and vice versa could cause the impact of cash flow volatility to be a result from mere correlation with the life-stage effect.

Choi, Park and Sangsoo (1997) studied and revealed that benefits of targeted share repurchase a joint hypothesis that targeted buy back decrease excess cash and reduction of the excess cash positively viewed by the market. The results of their study on the share repurchase announcement were positively related to pre-announcement of free cash flow. In addition to that most of the share repurchases forced by the management the author were not willing to buy back of share voluntarily, whereas there may be a valid reason because corporate resources, real value enhancing etc. The final consequences recommend that a share repurchase was a feasible i.e., reduce excess cash and that such decision could increase wealth of shareholders by reduces agency cost of free cash flow.

D’Mello, Krishnaswami and Larkin (2008), study the corporate cash holdings using data from corporate spin-offs. Studying spin-off’s allows for the observation of cash holdings without the aggregation of past decisions, because spin-offed companies can be considered newly established companies. In newly spinned-off companies the management can decide at the point of establishment, what the optimal cash holding level should be. Researcher found that spin-offs with high sales growth, R&D expenditures and lower access to capital markets tend to be allocated larger portions of cash.

Evans et al, (2003) studied changes of cash flow assumed with the samples of 381 companies of United States of America, that listed in NYSE,AMEX and NASDAQ in the year January 1980 to December 1997. Researcher examined that relationship between free cash flow and share repurchase. Several reasons for buyback of shares in company were deferred but free cash flow was the primary driver of share repurchase program.

Nai and Chan (2012) studied open market share repurchase in Taiwan that motivation of share repurchase was signaling effect but some of the price variation during repurchasing that contributes the ambiguous signal for share repurchase. That the reason the information conveyed to investors repurchases program long run abnormal returns after the repurchasing. And also this study examined that share repurchase program with the purpose of maintain the shareholders wealth and improves the share price during repurchasing in short period and also said short term returns affected by free cash flow of the company.
Oswald and Young (2007) argued on existence of strong evidence for low managerial stronghold as reflected in lower insider stock ownership and stronger board monitoring as support for free cash flow hypothesis. Rejecting existence of lower growth opportunities or reduced cost of external financing as suggested for free cash flow hypothesis, the characterized of repurchasing firms by being under stronger board monitoring. Such firms display better post repurchase operating performance, fewer disciplinary corporate control contests and very little failures. Hence, this study attributed lower insider ownership as a new dimension of agency problems of decision insider and outsider shareholders to be potentially important determinant of decision to distribute transitory cash surpluses by repurchasing shares.

Paul, Griffin and Ning (2010) found that CEO stock options influence the choice, amount, and timing of funds distributed as a buyback. These results favor a managerial opportunism motive for buybacks over other theories and support two key research expectations – that buybacks impose option-induced agency costs on outside shareholders, and that manager’s benefit from weak governance and unclear accounting in this choice. The author concluded that the popular use of stock buybacks as a form of cash distribution derives significantly from a strong contemporaneous relation between buybacks and CEOs’ use of stock options as additional compensation.

Salim Chahine et al (2011) argued that corporate governance affects the ability of a buyback of share to improve the agency cost which is related to free cash flows. This study collected data from open-market share repurchase programs during the period 1990–2004 using Thomson One Banker online database. The authors observed the relationship between stock market reaction and corporate governance is stronger during the post Enron crisis, and this was particularly the case in cash constrained companies that were less likely to face the agency problem of free cash flow. Stock market reaction was not good for governed firms its indicated the improve of agency problem more than signaling effect.

Sheng et al (2012) their studies have examined the life cycle explanation for share repurchase in the previous research studies. The authors mostly point of the signaling and free cash flow for buyback. But the researchers found out that a motive of share repurchase depends on the life cycle stages of companies. In life cycle of companies in growth stage of the companies were like to announce buyback program to signal the undervalued stock to market after that mature stage buyback of share to dispense the excess free cash flow.
Shrimpton et al (1998) observed that buyback of shares can prove to be a useful application of surplus cash because it can have a positive impact on some of the performance ratios, namely, earning per share (EPS) and operating income which were commonly used by analysts and investors to assessed how well companies were done.

Vafeas (1997) presented an empirical examination of the determinants of the choice between share repurchase methods. Researcher showed that the likelihood of selecting a self-tender offer over an open market share repurchase increased with the repurchasing firm's agency costs of free cash flow, inside ownership percentage, leverage, pre repurchase stock performance, and the magnitude of cash involved in the transaction. The evidence was consistent with the impact of free cash flow and signaling hypotheses on the choice of repurchase methods among firms. The author found that the firm’s choice of repurchase method would depend on the duration and size of prior market underperformance.

Walter et al (2013) examined the over-investment motivation for share repurchases used a sample of 139 Real Estate Investment Trusts (REITs) between 1996 and 2010. By combining a REIT's property portfolio data with project ROAs from the underlying real estate market, the author were able to create a unique measure of the firm's investment opportunity set and finds that poor investment opportunities were related to higher levels of share repurchases. Conditioning on investment opportunities, the author found that the level of cash was positively related to repurchases only for low investment opportunity set firms. In addition the negative relationship between shares repurchases announcement returns and investment opportunities.

Wansley, Lane and Sarkar (1989) surveyed CFO’s (Chief Finance Officer) of 620 large United States corporations identified in the 1986 Institutional Investor’s CFO roster and by Merrill Lynch, and obtained usable responses from 98 repurchasing and 42 non-repurchasing firms. The respondents of the study cited undervaluation of stock and signal to market as the primary motives for engaging in repurchases. Both repurchasing and non-repurchasing groups agreed that repurchases were used as a signal of confidence in the level of future earnings and stock prices, but not as a substitute for dividends. The author disagreed on lack of investment opportunities or availability of excess cash being the motivators for share repurchases.

2.7 Effects of Signaling on Buyback of shares
Adams et al. (2007) observed that if a company announces a repurchase program with the purpose to create an exchange option, a plausible expectation was that many repurchase options should not be exercised. Proposed that abnormal performance for repurchasing firms can be explained by the exchange option hypothesis. Asymmetric information between insiders (management) and outside investors can be exploited by announcing a coming repurchase program, which creates an option, but not an obligation, to repurchase shares. This option increases possible investment opportunities for the company by authorizing management to in the future execute the repurchase program if their inside information signals repurchase benefits for their shareholders.

Alice Bonaime (2008) showed that generally share repurchase view as signaling effect or information conveyed to investors that a firm’s share value is below the intrinsic value or market value that means the undervaluation of share price. The samples of data taken in Security Data Corporation (SDC) year between January 1 1984 to December 31 2004.

Amitabh Gupta (2006) found that announcement of share buybacks significantly increases the prices of shares around the time of announcement and large companies generate lower abnormal returns than small companies because of low information asymmetry between the management and investors of large companies. Managements can make used of equity buybacks as on important tool to convey information about its shares being undervalued, and about its future profitability and earnings.

Andreas and Alexandre (2006) in their study tested why managers buyback their shares in Germany and US. In both German and US the reasons was buyback of shares were to signal the firm share value was undervalued.

Asquith and Mullins (1986) studied about the important motive of buyback is undervaluation signaling. Managers used buyback of shares announcement as a News Bulletin to investors that indicated their value of shares is undervalued. Generally buyback announced for continuous decreases the share price in the company.

Monica, et al (2008) examined the financial institutions throughout the crisis period. Their finding is that firms’ repurchase activities during the crisis period coincide with findings from other studies of complying, non-financial firms. The aforementioned study confirms the excess capital and undervaluation theories. The author assert that their sample firms show an increased number of share buybacks from the start of the crisis forward. Their study focuses
on the financial institutions and was not comparable to this thesis since financial firms were regulated firms and therefore capital structures were different than for the non-financial firms.

Bhana (2007) analysed the long-term performance of South African companies involved in open market share repurchases has showed that despite managers’ frequent claims of undervaluation when announcing share repurchases, the return in the immediate days following the announcement was relatively small and the author conducted a small study consisted of 117 share repurchase announcements of firms list on the JSE during the period October 2000 to March. The study found that using the buy-and-hold strategy, three-year abnormal returns following the announcement is 14.35 percent. Companies with high book-to-market ratios that announced buyback programs provided the three year abnormal returns of 32.78 percent. This study suggested that either the managers were being overly optimistic relative to the market about the firm’s value or alternatively the market was wrong in responding and is thus underreacting to the repurchase signal. The possibility also exists that the market was slow in responding to the undervaluation signal contained in the repurchase announcements.

Additional investigations of the asymmetrical information theory were conducted by Barth and Kasznik (1999), who hypothesized that firms with more intangible assets were likely to repurchase shares, along with having more positive returns following the announcement to buy back shares. Their study acknowledged that intangible assets were generally unrecognized as accounting assets in a firm's financial statement, although such assets were of substantial importance for generating economic value. Investors outside the firm were assumed to have less valuable information about intangibles than managers at the firm. The study predicted that firms with more intangible assets were more likely to repurchase shares on the open-market. These predictions were tested using logit estimation on a sample of firms making their first repurchase between the years of 1990 and 1994. The sample was compared with firms that did not announce any type of repurchase. Several proxies were utilized for intangible assets, general information asymmetry, and idle cash, with constructed variables as the explanatory variables. The findings of Barth and Kasznik (1999) suggested that intangible asset variables were significantly and positively related to share repurchases; idle cash produced similarly positive results. In contrast, however, the generally asymmetrical information was significantly negatively related to share repurchases. The findings lent support to both the signaling theory and the asymmetrical information theory, while also
demonstrating that free cash flow and undervaluation cannot be definitively distinguished as explanations for the findings concerning intangible assets.

Bartov (1991) examined 185 open market repurchases from 1978 to 1986, and found that the announcement effects on EPS were mixed and weak, but the market risk of the sample declined substantially from the previous year. Overall, the above studies provided further support for the signaling hypothesis by showing that there were significant positive earnings surprises and declines in systematic risk of the repurchasing firms after repurchases, indicating change in investor perceptions.

Beverly Hirtle (2003) examined the relationship between stock repurchases and the financial performance for a large sample of bank holding companies between 1987 and 1998. The study finds that large banking firms showed better financial performance after the repurchases, raising the question on impact of firm size and/or information asymmetry on the effect of the repurchase. The study tests to see if the signaling hypothesis was confirmed in the banking sector over the study period of 13 years.

Block (2006) explained that premium paid over market value is higher, than in open market purchases which were less than fixed price tender offer. The researcher has collected the data from 473 companies listed in Fortune 1000 companies. Out of 473 companies 372 companies responded to the questionnaires. The study used for research is descriptive in nature. Results of the study revealed that the Dutch auction buyback offers 9.8 percent which falls between open market repurchase and tender offers. In his study the researcher finds that the fixed price tender offer method for buyback to increase their stock performance. It also finds that in the open market repurchase method stock return in share repurchase shows positive. The study also pointed out that share repurchases program increase the cash dividends and signaling of share was undervalued.

Brockman and Chung (2001) identified the important determinants of this market timing ability to be short interest rate, the firm’s cash flow and frequency of repurchases. The author studied of the bid-ask spread analyzed more than 5,000 share repurchases in 181 different firms on the Hong Kong Stock Exchange between 1992 to 1999, established that managers acquire shares at lower cost than a simple accumulation strategy, but their findings were also consistent with either opportune timing based on insider information or price support and also the author indicated that repurchasing firms have market timing ability.
Buyback of shares in Australia increased very well after 1995 large number of shares was repurchases on that time. Brown and Christine, (2007) in their study have conducted an examination of stock price and trading behavior announcements of equal access repurchase in Australian firms. The author found out that the Australia firms provides announcement effects because equal access repurchase occur at a discount to the market price and significant abnormal returns on announcement of buyback of shares for signaling undervaluation.

Carol and Wang, (2007) in their study found out that the signaling power of UK Open Market Share repurchases, and also identify the relationship between short term abnormal returns and the characteristics of repurchasing firms. Their study conducted a sensitivity analysis of announcement for abnormal returns. The author also found that there was no evidence for signaling hypothesis but UK share repurchases were not interested to motivated by share undervaluation.

Carol et al, (2007) revealed that the essential obstacle of share repurchases is undervaluation or signaling managers considered share repurchase as a good investment opportunity of excess cash in the company or firm. And companies were choosing Accelerate Share Repurchase is immediate effect of shares and very strong signal to the market about the firm. The results of their study reveals that strong controlling signaling effect in share repurchases decision in share repurchase announcements.

Charles and Choi (2001) examined the impact of share repurchase tender offers on the market microstructure. Their sample comprises of 65 fixed-price and 72 Dutch auction offers that were conducted between 1983 and 1992 for firms listed on the NYSE and AMEX. The study suggested that the bid ask spread was asymmetric during the offer period with the bid-side spread smaller than the ask-side spread.

Chun et al (2010), argued that signaling information to correct the share valuation and evade outside takeover attempts of undervalued firms was more apparent under conditions of strong market monitoring circumstances. If there is no market monitoring, management may not be under pressure to release private information and share price may not respond to actions such as repurchase announcements. In this instance, the raider may also not benefit from taking over the undervalued firm since share price may not increase in the absence of market monitoring and that if the share is undervalued, potential raiders may also be attracted to take over the company. Management may then decide to repurchase shares so that the share price will adjust upwards to the correct level for the benefit of shareholders or to dismay the raider.
Comment and Jarrell, (1991) analyzed 1197 open market buyback announcement between 1984 and 1988. The author studied three methods of buyback open market, tender offer and Dutch auction. These three methods Tender offer usually signaling information to investors than open market repurchase. The open market repurchase was very low compared with Tender offer price. The studies finds that signaling hypothesis effect was happens when the stock price is undervalued firm going for buyback to get maximum advantage. Comment and Jarrell (1991) analysed the abnormal returns for three types of repurchases and reported a 11% average excess returns for self tender offers and Dutch auction repurchases and just 2% for open market repurchases. This is mainly attributed to the price offers made under the different methods. The excess returns have also been shown to be related significantly to firm specific returns which clearly support the market signaling hypothesis.

Damien, Michael and Alfred (2011) examined the impact of different business conditions on the frequency of share repurchase programs using Australian Data. The authors segmented Data into three categories infrequent, occasional and frequent share repurchase program in Australian company which were listed in Australian Stock Exchanges in the year of 1996 to 2009. The results of their studies indicated positive response from the market as companies reduce their free cash holding that sends a signal to the market and the author believe their share value was undervalued.

Dann (1981) examined the effects of a common stock repurchase on the values of the repurchasing firms common stock, debt and preferred stock, and attempted to identify the dominant factors underlying the observed value changes. The evidence indicated the significant increases in firm values occur within one day of the stock repurchase announcement. The value changes appear mainly to be due to an information signal from the repurchasing firm.

David et al (1995) examined long-run firm performance following open market share repurchase announcements, 1980–1990. The author found that the average abnormal four-year buy-and-hold return measured after the initial announcement is 12.1%. For ‘value’ stocks, companies more likely to be repurchasing shares because of undervaluation, the average abnormal return is 45.3%. For repurchases announced by ‘glamour’ stocks, where undervaluation is less likely to be an important motive, no positive drift in abnormal returns
is observed. Thus, at least with respect to value stocks, the market errs in its initial response and appears to ignore much of the information conveyed through repurchase announcements.

Dimitris et al (2013), showed that information disclosure and CEO overconfidence were significant determinants of the share buyback completion rate. In addition, the author found that large and widely held firms that conduct subsequent buyback programs and have a past buyback completion reputation exhibit higher completion rates. An open market share buyback is not a firm commitment, and there is limited evidence on whether firms repurchase the intended shares. In addition, observed some evidence in France and Germany that a firm's likely undervaluation has a significant impact on the decision to announce a share repurchase.

Dixon et al (2008), in their study have shown a main motivation of optimizing the capital structure of the firm. An explanation for the different findings could be the different business culture in different countries. However, that was hard to decided, as the studies took place in different periods. There were more share buybacks in the 90’s than in the period 1983 – 1985. Consequently, the change in motivation from undervaluation to optimizing capital structure could be explained by the increasing importance of the capital structure during the time. A more recent study in the UK exists about the motivations for a buyback. Their study has published in 2008 and involved a survey of UK top 200 firms, which execute a share buyback. The study contains share buyback deals in UK from 1981, when it was legislated. Their results showed of the study that the main motivation is to create the optimal capital structure.

Fried, (2000) in his study revealed that normally cash was distributed to public shareholders in the form of dividend, but large portion of cash used in the form of repurchase. Predicted share repurchase announcements in tender offer method for signal underpricing of shares. Managers use the repurchase tender offer insider trading for insider signaling.

Grullon and Ikenberry (2000) explained two different types to the signaling. The first type stated that repurchases were intended to convey a firm’s expectation of future increases in earnings and cash flow. It was also called as a positive signal, indicating that management has correctly forecasted future cash flow and does not need the excess cash to cover future commitments such as capital expenditures or interest payments. The author second type developed a theory on Signaling hypothesis explain that management was not attempting to convey new information to the market about a company’s future and hence its share price. This was management’s view that the share was undervalued. It may also indicated that
managers were not attempted to convey new information to the market, but were instead expressed their disagreement with how the market is pricing their current performance.

Guay and Harford (2000), their study reveals that indication of both a share repurchase and a dividend payment conveyed positive information about the value of the firm, along with positive stock price reactions that reflected information signaling and support for the signaling theory. Additional research observed the cash flow of a firm to investigate the hypothesis that stock buybacks reflected a more transient cash flow position for the firm, while dividend payments reflected a more permanent cash flow level. The study found that, on average, dividend increases tended to occur with more permanent cash flow changes.

Healy and Palepu (1990) developed the framework to examined the role of both accounting and non-accounting disclosures on firm valuation. Their framework suggested that if the market viewed the financial disclosures as credible, it would alter the interpretation of previously released accounting information. The author argued that a cash payout using dividends or repurchases would be the managerial response available to undervalued firms to signal their confidence in the level of future earnings to the investors.

Ho, Liu and Ramanan (1997) examined 335 open market repurchases during 1978 to 1992, and found that the market reaction to the announcement was significantly associated with the firm's sales growth and accounting profitability in prior periods, after controlling for 2 known correlates of the market response: size of the repurchase and prior returns. This result was consistent with the market reinterpreting previously released accounting information of the firm due to subsequent repurchase announcement. The association between the market response and prior accounting information was more pronounced for smaller firms, and for firms that have few analysts following them suggesting that the degree of reinterpretation of prior accounting information is proportional to the information asymmetry between managers and investors. The author included alternative proxies for information asymmetry (size of the firm, number of analysts following, dispersion in analysts' forecasts of earnings) to test the relation between the market response to the announcement and prior accounting information.

Howe, et al (1992) in their study found that an average 15 percent return on combining announcements and long run returns which is consistent with managers’ claims. The study in order to distinguish undervaluation from all other motivations, sort the sample firms on basis
of book-to-market ratios. Repurchases by high book-to-market companies were more likely to be driven by undervaluation, while those with low ratios were motivated primarily by other reasons. Besides, a more substantial post announcements drift in stock prices of high book-to-market ratios was observed supporting the undervaluation claims.

Ian and Wang (2012) indicated that the UK market reacts slowly to actual repurchases made by value firms. UK repurchases on average do not suffer from share undervaluation prior to the announcement. Value firms perform just as well as glamour firms during the authorization period but outperform glamour firms significantly 2 years following the announcement. It turns out that value firms repurchase over 6 percent more shares than glamour firms during the authorization period.

James (2006) in his study explained about six hypothesis i.e., signaling effect, agency cost, personal tax effects, inter security increases by share repurchase and corporate tax shield effect these six hypothesis or reasons were to expect the positive announcement for share repurchase. In the study, it was observed the open market repurchase announcements more undervaluation and also it included the signaling effect of share repurchase. Low stock price announced could lead management signal of the stock was undervalued.

Jain, et al (2009), discussed about the decision to dividend payout was driven by life cycle factors and investor preference to dividend, while the decision to buyback of shares was extra for undervaluation signaling purpose.

John, Howe and Ravi Jain (2006) studied two motivations behind open-market share repurchases by banks. Their first hypothesis was the signaling hypothesis – banks use share repurchase announcements to signal higher future performance and second hypothesis is the “optimal capital ratio” hypothesis – banks use share repurchases to manage their capital ratios, and the positive announcement effect is the result of an increased value of the deposit insurance. The author found that banks announcing share repurchases have a positive industry-adjusted change in ROA during the two years following the announcement, consistent with the signaling hypothesis. In addition find evidence in support of second hypothesis: banks announcing share repurchase programs experience a reduction in their capital ratios subsequent to the repurchase announcement. The reduction in capital ratios occurs without a change in the asset growth rate or dividend payout ratio. The study also reveals that the announcement effect is positively related to the growth in capital ratios prior
to the announcement and to a decrease in capital ratios subsequent to the announcement, supportive of the optimal capital ratio hypothesis.

Jiang and Koller (2011) argued a different explanation to “signaling” theory stating that a negative signal, i.e. management’s view that the share is undervalued, could indicate a failure of management to find enough value-creating investment opportunities.

Jordan Voss, (2012) explained that signaling hypothesis in share repurchases was similar to the undervaluation of share price. When the companies were buyback their shares on the basis of open market it means that signaling and sending a signal to the market for their future prospectus. Signaling assumes that the market strongly inefficient form because there was asymmetric information between company investors and themselves.

Kadiyala and Rao (2002) in their study have observed the behavioural pattern of investors following the announcement of 4 different events, namely, share buyback, seasoned equity offerings, stock financed acquisitions. While none of the previous studies measure investor reactions to different events differently, this study made an attempt to bring all the events on the same platform whereby the author were categorized into either under reaction or over reaction response by the investors. However, the findings clearly supported the under reaction hypothesis for all corporate events.

Ken et al (2010) examined the wealth effect of stock repurchase announcements, using a sample of 11,862 repurchase programs announced during 1994–2007. The results of several recent industry surveys indicated that managerial motivations for repurchasing shares may have changed in recent years. To better understand the reasons for repurchasing shares the author classify their sample in various ways, by year, by the method used for repurchasing shares, and by the stated purpose of the program. The author find that the median size of firms repurchasing shares has increased dramatically recently, and concomitantly, the announcement returns have declined. Signaling undervaluation of share prices appears to become less important than previously assumed. While smaller firms signal undervaluation using open market repurchases, tender offers were chosen to enhance shareholder values by other means.

Kracher and Johnson (1997) found that the firms deliberately misusing the signal in a repurchase, when the repurchase was announced without an intention to fully execute the buyback. In contrast to their study the author have suggestion of false signals, a which
indicated that approximately 74 percent to 82 percent of share repurchases were substantially completed within 3 years of the announcement, along with 57 percent fully completed within 3 years post announcement. Moreover, their investigation into the magnitude of share repurchases revealed that within 3 years following the announcement date, 30 percent of firms in their study repurchased more than twice the targeted quantity in a sample of open-market buyback programs announced from 1981 through 1990, although 10 percent of the firms repurchased less than 5 percent of the targeted number of shares.

Lee et al., (2005) found that most of the South Korean firm had reported that share repurchase used as a strategic tool for stabilize prices and it is provided strong evidence for undervaluation of share value is the main motivation of buyback of shares.

Michael (1998) examined the relationship between manager’s risk wealth risks in false signaling in self-tender offer repurchase announcements. Signaling assumed that the credibility of signal from a repurchase announcement increased. When managers repurchase the firm were themselves exposed to risk of signaling failure. The study observed pre announcement trading activity by managers could be motivated by managerial belief that the market price of the firm’s stock is at a discount to its true value. The manager also believed their share is undervalued it is motivate to take decision for buyback of shares. The buyback announcements and reaction of stock markets to the same have concentrated on various aspects, including undervaluation signaling, excess cash distribution, substitution for cash dividends, defense against takeover threat and the similar. In foreign and Indian companies it was more undervaluation of signaling.

Naratip Tabtieng, (2013) examined the motivation influenced the share buyback the most cited reason is undervaluation of share price, below the fundamental price and to improve the earnings per share (EPS). The author have analyzed in 27 companies in Thailand in the year July 2001 to December 2009. The results of their studies showed as 12 companies share price increased after the end of share repurchase program and bring firm for attention of the market through repurchase announcements.

Narayan Rao (2010) examined the effects of announcement of offer of open market buyback in India. The study sample consists of 64 open market share buybacks offer during 2003 - 2010. The evidence suggested that significant sustainable increases in firm values occur around the announcement of buyback offer. The results of the study support information signaling hypothesis of share buyback.
Nobuyuki Isagawa (2002) discussed two types of main contribution to open market repurchase signaling. First model established signal equilibrium without the assumption that the firm was committed to an announcement of open market repurchases intention. Second model predicts positive long run stock returns as well as positive announcement effects following open market announcement. The researcher concluded when the market was completely inefficient the outstanding shares of firm would be undervalued after announcing an open market repurchase program.

Nohel and Tarhan (1998) mentioned generally positive investor reaction to an announced repurchase has suggested support for the signaling hypothesis in the findings. If a firm's intention in announcing a share repurchase has been to signal to outsiders of the firm that the company's prospects were improving, then, the signal suggested a tangible improvement in financial operating performance following the announcement. In contrast, if the intention of the firm was to distribute free cash flow, rather than invest in less worthy projects, then the firm may or may not have exhibited improved financial performance following the announcement. The signaling theory suggests that signaling implies an improvement in financial performance, yet improved performance does not necessarily imply signaling.

Peterson et al (2003) said that asymmetric information between management of a firm and investors on the stock market is obvious. Management’s actions will give signals about the operations to investors, and different signals can be interpreted in different ways. According to the signalling hypothesis, an announcement of the start of a share repurchase program is interpreted by investors as the management of a firm is putting its money where its mouth is, i.e. signalling that the stock is undervalued.

Pugh and Jahera (1990) compiled a sample of 45 fixed-price tender offers from 1978 to 1985 by non-financial, non-utility firms with an offer premium of 19.4%. The author reaffirmed the previous studies results that the offer premium is the primary determinant of abnormal returns, and the percent repurchased and insider ownership provided limited but significant information. The author found that small firms and firms with low institutional holdings set higher premiums confirming the effect of information asymmetry.

Ramakrishnan (2007) analyzed open market share buyback effects on share prices with Bursa Malaysia jurisdiction and found positive effects to share prices during buyback and after buyback as compared to before buyback. The study concluded that more managers and shareholders of low capitalized companies undertake share buyback program as a vehicle to
signal information to keep shareholders informed and interested in the firm. The study found support the undervaluation hypothesis praised in the financial literature as the primary motive for share buyback.

Saeyoung and John (2014) their study finds that abnormal returns were positively related to managerial ownership of buyback of shares and it is evidence for higher share price reaction for low and high free cash flow firms. The author have analyzed a samples were 92 convertible preferred stock repurchases over the 1981 to 2005 period. Mutually results were most constant with the signaling hypothesis.

Sang-gyung Jun et al (2008) examined that the signaling hypothesis and wealth transfer of share repurchase announcement the results were positive effect of buyback that provide support for the wealth transfer. The study used the multivariate analysis, it found that wealth changes to shareholders is positively related to bondholder wealth changes. The divisions of share repurchase signaling effect were less likely and positive relationship between shareholder and bondholder is eliminated. If assets reduced through share repurchase was increased risk for bondholders.

Sheng et al (2013) explained the buyback behavior in IPO (Initial Public Offering) firms and motive of buyback initiative in the companies. Using 3614 IPO firms in the US it was indicated that sends false signals to mislead investors by announcing repurchase program. IPO firms announced buyback programs that firm practiced negative abnormal returns in long run. The author found IPO buyback announcement underperform the general IPO firms in profitability measures.

Seifert and Stehle (2003) in their study argued, disagreed and stated that the positive announcement effects and the undervaluation stated as the main reason for the repurchase vanish after several days.

Stephans et al (1998) focused upon the relative performance of repurchasing firms in terms of percentage of share actually bought back as a proportion of total announced. The authors found that only up to 74 to 82 percent of the total announced shares are actually bought back. Hence, buyback is an important tool in the hands of corporate managers whereby the author can control the timing of an investment decision. This flexibility is larger as there is no commitment on part of companies to actually buyback and sometimes the author prefer to go
for overbuying. Besides, the negative correlation between previous quarter and post repurchase quarterly stock return strongly supported presence of information asymmetry.

Tsetsekos and Liu (1991) surveyed Chief Finance Officer (CFO’s) of 1,000 large NYSE firms and based on 183 usable responses to determine the stock repurchase motives, the author found that the primary reason for repurchases was stock undervaluation. Most of the respondents cited changing capital structure as the primary motive, but the responses pointed to signaling the market as the reason. Contrary to the results from Baker et al (1981), the author found that managers of the repurchasing firms view repurchases as a financing rather than investment decision. Vithessonthi (2008) studied share repurchase program announced in Thailand taken 21 samples in the year between 2001 and 2005 reveals that share repurchase programs announcements are only share price was undervaluation in market and superior to future operating performance development. The author concluded with this study the information conveyed through share repurchase announcement to market was this share price was undervaluation.

Woan Lih et al (2010), focused on cases where managers were seemingly under heavy pressure to boost stock prices and might have announced a repurchase only to convey a false signal. Managers in suspect firms have comparatively higher exposure to stock options, a potentially endogenous result suggested greater sensitivity to both stock valuation and to future equity dilution. Overall, the results suggested only a limited number of managers may have used buybacks in a misleading way as “cheap talk.” Yet as theory also suggests, the author find no long-run economic benefit to this behavior. Woon-lih Liang (2012) explained that most of the buyback research study suggested that the underestimation of future intangible value may explain high return associated with the buyback of shares. For better understanding the author finds the repurchase signals an undervaluation of intangible return. In addition the author investigated several potential proxies for intangible information, R&D expenses, intangible assets, and future operating performance.

Wu, Kao and Huang (2007) revealed that in Taiwan where repurchases were introduced in 2000, while ESOs came in the year 2001. Proposing option funding hypothesis to replace the empirical signaling hypothesis, their study measure the short term and long term impact of repurchase announcements on abnormal stock returns. While the short term impact was found to be significant for pre ESOs issuing repurchases with post ESOs issuing repurchasing firms,
the long term impact came out to be insignificant, thereby rejecting the signaling hypothesis (which proposes both short and long term abnormal returns) in favour of option funding hypothesis.

Zhang (2005), explained that firms on the Hong Kong Stock Exchange provides evidence that suggested managers do not exhibit superior performance, when the author make open-market share repurchases. The researcher concluded that at least for high book-to-market value firms, for which undervaluation was more likely to occur, managers can detect and size some of those opportunities when their shares were relatively undervalued and make repurchases to benefit long-term shareholders.

2.8 Dividends Substitution on Buyback of shares

Abe de et al (2003) investigated dividend and share repurchase policies of Canadian firms. The author used a Questionnaire method to collect date from 500 non-financial companies in Canada (Toronto stock Exchange). Their results were consistently with a structure in which the company first decides whether it wants to pay out cash to its shareholders or not. Company decides the payout policy of dividends, share repurchase or both. Payout was predicted by free cash flow. The choice of dividends and repurchase of company depends upon the tax. In addition asymmetric information amongst outsiders was associated with a preference for dividend payment over share repurchase.

Adam Dunsby (1995) examined the empirical determinants of share repurchase policy and to examine the reasons for the increase in share repurchase activity in the mid-1980s. Of most interest was whether firms that repurchase pay less in dividends than comparable firms that do not repurchase. In other words, do firms substitute share repurchases for dividends? The main result was that firms that repurchase do not pay less in dividends than comparable firms which do not repurchase. High profitability and the presence of an ESOP were predictors of share repurchase activity. The increase in share repurchase activity in the mid-1980s appears to be the result, at least in part, of an increased use of share repurchases to distribute earnings.

Allen and Michaely (2003) found that repurchases have captured a large and ever increasing volume of corporate payouts since the 1980’s, when dividends constituted a majority of the payouts. During the 1980’s dividends grew at an average rate of 15 percent, compared to the
6 percent growth rate of the observation period (1980-1999) of their study. In 1999, repurchases represented the same level of magnitude as dividends in terms of absolute value.

Arnott and Asness, (2003) explained the share buybacks were defined as an alternative for dividends. Low payout dividend in many of the studies ratios were defined as good for the growth of the firm. The firm can invest a much to provide for growth. On this manner, the firm creates value for the shareholder. The researcher investigated the dividend payout ratio as a predictor for future growth. The result of the study which central issue, low dividend payout ratios were a strong positive signal for future earnings growth were inconsistent with the historical evidence. Higher payout ratios create higher future earnings growth and profits.

Bagwell and Shoven (1989) carried out a similar analysis of the type of characteristics which differentiate the firms which go for alternative utilization of funds by share repurchases or by mergers and acquisitions rather than paying dividends. The study examined the probability of a firm going for either repurchase or acquisition (both considered as equivalent decisions) by analyzing different variables influential in taking such decisions.

Baker et al. (1981) surveyed CFO’s of 150 randomly selected repurchasing firms and 150 non-repurchasing firms listed on the NYSE (New York Stock Exchange) during the late 1970’s. The majority of the responding managers viewed share repurchases as investment decision, not a financing or dividend decision. The respondents cited investment of excess cash and option funding as the 2 major reasons for initiating a repurchase program. The managers discounted substitution of repurchases for dividends as a motive.

Christine and James (2006) their study examined the relation between share repurchases and dividend changes in a non-classical tax environment, where dividends were not tax disadvantaged relative to capital gains. The author found that repurchase yield was positively related to dividend increases, suggested that Australian firms were not buying back shares with funds generated by altering dividend policy. Finally reveals that have important implications for our understanding of the effect of taxation on firms’ payout policy.

David Gelb (2000) investigated how the composition of the firm’s total payout affects investors’ reactions to dividend and stock repurchase announcements. The author revealed that the market reaction to a cash distribution was mediated by the composition of the total (year-to-date) payout announced during the fiscal year in contrast to their predictions. In
addition to that the market reaction was more favorable when regular common dividends (but not special dividends) comprise a larger proportion of the total payout. The result of the study supports the findings of previous studies that regular dividends were a more positive signal about future cash flows than stock repurchases or special dividends.

Erik and Heidi (1999), their study explained that companies can distribute the excess cash to shareholders in the form of dividends or repurchase their own shares. The author also found out that small capital gains or low dividend yield or payout preceded the tax reform manager more likely to lead the firm the author choose self-tender offer over a special dividend or repurchase program over dividend increase.

Erik Lie (2005) examined the effect of financial flexibility and the level and certainty of operating performance on the choice to change dividends, pay special dividends, and repurchase shares. Firms that increase payouts have excess financial flexibility and exhibit positive concurrent income shocks and decreases in income volatility, but there was limited evidence of subsequent performance improvements. The results were opposite for firms that cut dividends. Thus, the decision to alter payout levels appears to convey information about contemporaneous income and changes in operating risk.

Eva and Daniel (2002) reported empirical results on the determinants of the authorization decision for share repurchases and dividends in Finland. The author used a data set with precise data on share repurchases as well as characteristics for the option programs. Contrary to the U.S., the author use a data set where 41% of the options were dividend protected, which allows us to separate between the "option funding" and "substitution/managerial wealth" hypothesis for the choice of the distribution method. The author find that tax effects in terms of higher foreign ownership was the main determinant for share repurchases in Finland. The author also find evidence in support of both the signalling and agency cost hypotheses for cash distributions, especially in the case of share repurchases. Finally, the author find a significant difference between companies with or without dividend protected options. When options were dividend protected, the relationship between dividend distributions and the scope of the options program turns to a significantly positive one instead of the negative one documented on U.S. data. This gives some support for the substitution/managerial wealth hypothesis as a determinant for the choice of the distribution method.
Fama and French (2001) observed that buyback of shares were utilized at an increasing rate since 1978 by large, profitable firms that were, in turn, decreasing the use of cash dividend payments. The study observed, that the cash dividend payout ratio of the typical dividend paying company did not tend to decline during the years of 1983 through 1998, and the author inferred that this suggested a want by the large, profitable firms to increase their overall payout ratios. The study also noted a surge in non-profitable publicly owned firms that did not meet the financial profile of a firm likely to pay dividends, and that this profile, as well as more profitable firms that had never paid dividends, accounted for part of the decline in number of firms that paid dividends. The study concluded that dividend payments continued to have unexplained determinants, with some empirical evidence that determinants reflected financial characteristics of the firm.

Fenn and Liang (2001) in their study, provide evidence that top management’s stock options are positively correlated with stock repurchases and negatively correlated with dividend payments, suggesting that executive stock options reduce the attractiveness of dividends to the managers.

Ferran (1999) opined that a company, whose shares were not actively traded, was not an attractive investment prospect to external investors because of the risk of being permanently locked into that investment. Also, the income that would be derived from such an investment may be low, if not minimal, with the bulk of the profits being re-invested in the business instead of paying a higher dividend.

Gaspar et al. (2004) had used a sample from US firms in the period ranging from 1984 through 2000, concerning the pay-out policy with respect to share repurchases from investors used for their research. The study was cross-sectional study of the average investment horizon of a firm’s shareholder with respect to its pay-out policy and how the market reacts to this effect. The finding was firms were more likely to repurchase shares if the author were held by short-term investors, than if the author were distributing their cash by dividends. The author found an average of 2.9 percent abnormal returns, for the event window.

Grullon and Michaely (2002) has studied that the share repurchase not only a payout tool in US Companies nonetheless companies used cash to invest in share repurchase for improve their dividends. Undeveloped companies more propensity to pay cash through buyback. Modigliani Miller dividend irrelevancy theory the basic level implies that buyback and dividends were perfect substitute. The main aim of this study evidence for dividends
substitutes the share repurchases. Most of the companies paying dividends and initiates the share repurchases. Established companies distribute more cash through buy back and less through dividends.

Grullon and Michaely (2004) found that firms reduced their current levels of capital expenditures and research and development expenses to be able to repurchase shares. Firms decrease their level of cash reserves on the balance sheets and the market even overreacts to repurchasing firms that were more likely to overinvest. When firms evolve to a maturity phase, their set of investment prospects become smaller with less room to grow and the author used samples from US firms in the period from 1980 through 1997 in which the data emphasizes the repurchase pay-out method. Whereas the cumulative average abnormal return was 2.7 percent for 1 day surrounding the announcements, no indication has been found that the firms involved in repurchase programs show progress in their future lucrativeness with respect to peer firms.

Gryglewicz (2004) examined that market response for share repurchase announcement and dividends. And also finds that buyback and dividend decision firms were conclude that buyback and dividends were alternatives and not perfect substitute. Canadian firms also substitutes the share repurchase and dividends but Australian firms were not substitutes the buyback and dividends.

Hribar, et al (2004) analysed the similar situation and reported EPS enhancement for nearly 20 percent of repurchasing firms. However, this trend was found to be more visible, prominent and permanently sustainable among firms with small negative pre repurchases earnings surprises. Moreover, repurchasing strategy was expected to yield better results vis-à-vis dividend payments and cash accumulation in terms of EPS enhancements primarily due to two reasons Reduction in zero return assets with cash distributed among shareholders and Changes in mix of risky assets to total assets thereby yielding higher return on investments in the future. Besides, repurchases allow individual shareholders to invest the money received in risk free government bonds and bank deposits, thereby increasing their return on investment which was not possible in case of dividends payments.

Hsieh and Wang (2008) reported that firms prefer repurchases to dividends when the level of insider ownership was high or increases, especially in years when dividends were more tax disadvantaged relative to capital gains. And previous studies reported that the decision to
repurchase share can also be related to the impact of liquidity on share prices rather than tax effects.

Jonchi Shyu (2007) studied the listed electronics firms in Taiwan that have announced stock repurchases and changes in cash dividend policy over the period from January 1, 2001 to December 31, 2004. The author compared the effects of announcements regarding stock repurchases and increases in cash dividends, and then examined the impact of stock repurchases on the announcement effect of dividend changes. The empirical results found that the price of a stock tends to fall before a firm announces a stock repurchase and generates significantly positive abnormal returns after such an announcement. Firms that increase cash dividends tend to see their stock prices rising in the pre-announcement period and experience positive abnormal returns after the announcement. Based on the market reaction to an announcement, a stock repurchase tends to convey more positive information than does a dividend increase. This study also observed the positive impact of stock repurchases on the announcement effect of changes in cash dividends, which verifies the value added effect of the stock repurchase on the announcement effect of change in cash dividend policy.

Kai and Peter (2007) said that buyback and dividends announcements are send the management information about share price that will be impact of shareholders wealth. This was a theoretical view which implicitly assumed efficient markets. The study reveals that paying out free cash flow and dividends reinvestment plan (DRIP) has a positive impact of share price. DRIP or buyback increased the current shareholders wealth. Perhaps buyback of shares or free cash flow were equivalent for shareholder expected wealth.

Kahle (2002) found that managers decided to repurchase shares because executive options create an incentive not to pay dividends, since the payments of dividends reduces the value of both exercisable and unexercisable options held by managers. This was commonly called the substitution hypothesis. As high technology firms have higher levels of managerial options and such options provide additional incentives beyond employee options for firms to repurchase.

Kenji Wada (2002) analyzed the stock performance of the Japanese firms listed in TSE around all of their share repurchase announcements between 1995 and 2001. Because of the stringent regulation on stock repurchase, The study showed that the average size and value of the program and the announcement date excess return was much smaller than, but the long-
term excess return was comparable to those in the United States., an announcement for retirement purpose followed a decline in excess stock returns, an announcement for stock option purpose followed an increase in excess returns which was never reported in the U.S. or Canada, excess stock returns increased after the repurchase announcements, the excess returns were higher when the motive of the repurchase announcement was stock option, this was the first repurchase announcement there was actual repurchase, the dividends of the firms making repurchase announcements slightly increased and the total payout (dividends plus the actual value of shares repurchased) of these firms increased so that the growth in actual share repurchases in Japan represented an increase in total payout instead of the substitution between dividends and the share repurchase.

Marc and Daniel (2002) discussed the important reason for increase in share buyback was the flexibility of repurchase program as compared to distribution of dividends there was a significant advantage to buyback program. In some countries cash dividends was more taxed than buyback of shares. In such situations shareholders not received the cash dividends. Share repurchase announcements in India basically follow three methods, through open market share repurchase, Fixed Tender offer method and Dutch auction. The study revealed that relationship between repurchase and dividends was unresolved when the author were used simultaneously. When Manager used Dutch auction announce the acceptable price at which shareholder can tender, while managers used fixed tender offer announcement in buyback fixed price at which shares were repurchased.

Masulis (1980), in his study of 199 announcements of tender offers covered during 1963-78, revealed a 17% return for common stock over a period of 2 days post repurchase announcement. It was attributed mainly to the tax advantage of repurchases over dividends and to wealth transfer from tendering to non-tendering shareholders.

Moser (2007) distinguished between tax advantaged institutional ownership such as charitable endowments and pension funds and tax disadvantaged institutional ownership such as mutual funds and investment advisors with respect to dividends. With an increasing tax penalty on dividends and a higher ownership level of tax disadvantaged shareholders, firms were more likely to distribute cash through repurchases rather than dividends. However, with an increasing tax penalty on dividends and a higher ownership level of tax advantaged
shareholders, firms were more likely to distribute cash in the form of dividends.

Paul *et al* (2008) stated that once a firm initiates a payout, the higher stock market liquidity increases the profitability of a repurchase relative to paying dividends.

Raju (2013) examined the dividend substitution effect of share repurchase decision in Indian firms. In the share repurchase announcements showed that Indian firms were do not buy back their share by sacrificing dividends, and motive of share repurchase was free cash flow in the company and finds that Indian firms do not buybacks, its shares by sacrificing dividends. High levered and small sized firms in minor valuation in share repurchase in India but not the dividends. Meanwhile share repurchase was not observed as an important mechanism of distributing excess cash in India, it was very difficult to arrive relating to dividend substitution effect in India compared to US.

Renneboog and Trojanowski, (2008), in their study explained that the UK has a corporate governance system that was broadly similar to the US system  i.e. the Anglo- American model, however the taxing of the share repurchases and the dividends were determined differently for both countries. In the UK, managers seem to prefer dividend increases since shareholders were found to enjoy tax benefits from dividends. As a result, the managers in the UK were less likely to buy shares back than their US counterparts.

Skinner (2008) analyzed the changing corporate payout decisions over three decades. Specifically studying dividends and repurchase behavior of 345 firms who have regularly paid dividends over a period of last 16 years and have repurchased shares over a period of last 11 years, these firms continue to pay dividends largely because of compulsion that the author have been paying dividends for many years and were essentially obliged to continue this practice. The study reported adaptability and flexibility of repurchases to adjust quickly to earnings changes as the main reason for their preference over dividends.

Sohnke Bartram *et al* (2010) investigated the roles of firm and country level agency conflicts in determining corporate payout policies. Based on a large sample of 29,610 firms in 43 countries from 2001 to 2006, The author also find that in high protection countries, investors were able to use their legal powers to extract cash from firms but their ability to do so can be substantially hindered when agency costs at the firm level were high. In poor protection
countries, investors can seek refuge in firm level governance mechanisms to curb agency conflicts, suggesting a substitution between country and firm level investor protection. Finally, compared to repurchases, the author found dividends were more likely to be the sole method of payout in high protection countries and in less closely held firms.

Sung and Ko (2007) examined how control and ownership structure affect share repurchases in an emerging market where controlling families derive large private benefits. Whereas firms with concentrated ownership often pay cash dividends, firms with weak control rights often repurchase shares. The magnitude of repurchase increases with weak control rights, but decreases with strong foreign ownership. These results hold even after controlling for M&A threats and managerial stock options. Additionally, stock returns were lower when share repurchase announcements were made by firms where controlling families have lower ownership and lower control rights. These results suggested that insiders can repurchase shares to protect control positions.

Thirumalvalavan and Sunitha (2006) investigated 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 returns of 2.1 percent within one day of the event. There was no significant difference in abnormal returns as a result of various repurchase levels. These results implied that the strong signaling power of stock repurchases announcements and that the market react more favourably to repurchase compared to dividends announcements.

Vaughan and Williams (1998) developed a multiple regression model to test the relative signaling power and substitution effect of dividends and repurchases. Although repurchases have not been found to give more efficient signals of future income prospects over dividends, yet the study concluded that companies pay dividends to expose shareholders to excessive taxation to create psychologically favourable signal prospects. This study reported clearly makes a strong case for taxation benefits of repurchases over dividends.

2.9 Effects Takeover Deterrence on Buyback of shares
Bagnoli, et al. (1989) discussed the takeover deterrence as a motivation for repurchases for the first time. In this study, the authors developed a signaling model in order to understand the dynamics of share repurchases undertaken in response to takeover bids. The model suggested an increase in cost of acquisition following repurchase announcements. The price paid to repurchase shares has an inverse relation to the value of the firm, thereby making it unattractive for the potential bidder. Hence, the managers of such firm send a strong signal through repurchases to the shareholders regarding future price potential of his firm. The model assumed asymmetric information and relied on signaling by managers to shareholders not to tender shares to any takeover bids in anticipation of future raise in prices.

Bagwell (1991) presented a theory in which share repurchases act as a deterrent against hostile takeovers. The research study showed evidence that a perceived threat of a possible takeover significantly increases share repurchase activities conducted by companies. The underlying rationale of the theory stated that company shareholders have heterogenic perceptions of the intrinsic value of the company, which results in a broad range of reservation prices at which shareholders were willing to tender their shares. When a company repurchases shares, the first shareholders that were willing to tender their shares were ones with lowest reservation prices, leaving the remainder of the shareholder base having a higher average reservation price compared to the pre-repurchase situation. The increase in the average reservation price consequently increases the bid at which an acquirer was able to obtain majority consent from the shareholders. The study cited that the case of Sears, where the company announced the initiation of a share repurchase program, targeting 10 percent of the share base, as a response to circulating rumors regarding a possible takeover.

Davidson and Garrison (1989) used the publicly announced reasons for repurchase to divide the overall sample into 3 sub samples- Takeover defense, Investment repurchases, and ESOP needs. The author found that the market reacted 1) negatively to the takeover defense motive (control); 2) substantially positively to undervalued stock motive (signaling); and 3) neutrally to ESOP motivated repurchase (option funding). Davidson and Garrison (1989) studied 62 tender offers from 1978 to 1983, and measured the abnormal returns for the 181 trading days around the repurchase announcements to see if the announced intents of the repurchases contributed to the market returns. The repurchasing firms that cited investment / stock undervaluation showed significant abnormal gain in line with previous research, and those that cited takeover defense as the motive showed significant abnormal losses. In both of these situations, the market reacted predictably to two opposing signals.
Denis (1990) suggested the effects of two major defensive strategies in response to takeover attempts, i.e., repurchases and special dividends. By taking a sample of 49 such defensive announcements undertaken between 1980 to 1987, the study reported an increase in the concentration of voting power in the hands of managers in both the cases. Yet, the study reported repurchases announcements as highly effective in retaining independence of the target firm.

Hodrick (1996) researcher studied taken to support the takeover deterrence theory by documenting that shareholders were heterogenic in their perception of company value, which results in an upward sloping supply curve for shares. Companies that faced higher price elasticity were found to be those with larger institutional and smaller insider holdings.

Ji Chai et al (2014) analyzed a large sample of Open Market Repurchases (OMRs) and found strong evidence consistent with their hypothesis. The takeover risk factor into asset pricing tests, there were no abnormal returns in the post-announcement period. In particular, the increase in takeover risk in the post-announcement period was larger for smaller firms, for firms with larger negative valuation shocks, and for firms that attract more attentions of market participants. The evidence implies that OMRs, which have been used by many firms to counter undervaluation, could make the firms more sensitive to takeover waves and raise their cost of equity capital.

Miller and McConnell (1995) in their study stated that there was reported lack of any effect of buyback announcements on stock liquidity. However, in order to control the effect of other variable which include stock return volatility, trading volume and level of share price, their study also conducted multivariate analysis, and found no evidence of significant decrease in liquidity following buyback announcements.

Persons (1994) assumed the suitability of different motivations for fixed price tender offers and Dutch auction share repurchases. While fixed price tender offer was used mainly by companies in order to signal undervaluation Dutch auction offer method was used for effective takeover deterrents. The justification for this argument flows from the formation of model which suggests the best utilization of Dutch auction share repurchases for firms who want to use repurchases in order to counter takeover attempts. This study assumes different prices quoted by the tendering shareholders in case of Dutch auction method resulting into huge cash outflows as the main force behind the demotivation of bidders to quote for acquisition of the target company.
Sinha (1991) considered debt along with share repurchases as a combined defensive strategy. In the event of no takeover threat, the manager can afford to allocate all the resources at their disposal towards perquisite consumption. However, in case of any takeover threat, the managers decide to allocate a portion of resources towards investments in the firm. This will increases the value of the firm, thereby making it less attractive for takeover. In order to make these investments observable to outsiders, managers carry out debt financed share repurchases. Thus, with increased debt financing and increased share repurchases, the bankruptcy threat increases while possibility of a takeover threat declines. Favouring debt financed share repurchases over debt financed any other cash outflow including special dividends, the study quoted tax advantage and different valuations by heterogeneous shareholders as the main reason for such preference attached to share repurchases.

2.10 Impact of Share Price on Buyback of shares

Aboody and Kasznik (2000) found evidence that managers tends to time their voluntary disclosures to beneficially coincide with dates on which stock options were awarded. In such instances the management releases negative news on the company, resulting in a negative stock price reaction, which in turn will set the exercise prices of the awarded stock options at lower prices than pre-announcement.

Amy and Laura (2014) analyzed that firms repurchase stock at a significantly lower price than the average market price in all sample years. Less frequent repurchases, firms that repurchase when insiders buy on their own account, and firms that experience low stock returns prior to the repurchase obtain significantly lower prices. After controlling for risk factors, repurchasing firms earn positive returns. Infrequent repurchasers earn a significantly higher return up to three years following the actual repurchase.

Axelsson and Brissman, (2011) focused on the period following 2008, showed an increasing trend in the buybacks and an improved S&P 500 stock index. In summary, the buybacks and borrowing trend was a phenomenon mainly in North America and Europe. Recent news, especially after 2009, indicates an upward trend of share buybacks in the US as well as in the EU. While a boost in the share buybacks may signify profitable returns for the common outstanding shares, there were different visions. If under-reaction was truly occurring in the midst of the crisis in 2009, long-term positive stock price reactions could arise, in combination with increasing stock prices and a buy-high trend by companies.
Bai, et al (2000) on studying the importance of transaction prices, argue that the observed transaction price can be decomposed into efficient one plus a “Noise” due to microstructure effects. The transaction prices were inefficient and incomplete. The author does not reflect the full information of the security. There was a portion of noise in the price of security. The relevance of the microstructure noise, especially when dealing with high frequency data was discussed in this research paper.

Byoun (2008) opined that if a firm faces above-target debt-ratios, financial surplus were used to pay off debt only whereas in case of below-target debt ratios, financial surplus was used to retire both equity and debt to circumvent costly repurchases and re-issuing activities. In addition, share buybacks can often lead to an expropriation of at least one group of stakeholders because repurchases usually result in a decrease in asset value as it reduces the value of debt. This reduction leads to decreasing bond prices and thus results in a wealth transfer from bondholders to shareholders.

Cook Krigman and Leach (2004) studied uses a sample of 64 US firms, investigated the market timing ability and price support motive of repurchase firms. The author found mixed results of New York Stock Exchange and NASDAQ traded firms. In general, the author found no evidence of market timing ability but some firms executed repurchases in a pattern consistent with the price support motive.

De Ridder (2009) conducted a study on repurchase activities of firms listed on the Stockholm Stock Exchange between 2000 to 2004, representing 174 share repurchase programs in 71 firms. Overall, there was strong empirical evidence of managerial timing capabilities for repurchasing firms in Sweden indicating that firms repurchased shares at a price lower than that paid by other investors. Furthermore, the study analysis of repurchase patterns shows no particular pattern during the weekdays, but higher repurchase activity was recorded in February, March and August, which were months when most Swedish firms present their interim reports.

Dielman, Nantell and Wright (1989) discussed the effect of share repurchases on stock prices in short run. Using random coefficient regression model, this study covered a period of 1957-74 for both open market and tender offer repurchases. Although this study didn’t find any significant impact of repurchases on share prices in short run for open market repurchases, yet the impact in case of tender offers has been pretty significant. However, measuring the
return over a very short time period of 2-5 days post announcement period was a question still unanswered.

Ginglinger and Hamon (2007) examined that repurchasing firms have market timing ability; meaning that on average, these firms repurchased shares at a price lower than that paid by other investors since shares were repurchased, after an observable decline in share price, even though the author have no private information about future price developments. Actual share repurchases for 352 firms in France from 2000 to 2002 Their evidence suggest that firms act against market trends, executing their repurchases to take advantage of falling prices. This result was consistent with a price stabilization motive for repurchases. This findings were repeat the importance of timing skills as the repurchase would be expected to occur on trading days, when prices were falling and/or immediately after a fall in the price. Managers, who exercised timing skills, would expect to observe price trends in the trading days after the announcement day.

Hung et al (2013), examined that the enterprise conducts share repurchase to promote the share price of the company. The Manager and other superior shows low shareholding ratio and market appears downturn, a company likely to conduct share repurchase. Data of their study have taken from the Taiwan Listed companies and the author has used Logistic regression and Correlation for analysis. The results of their study reveals that companies were likely to conduct a share repurchase program for promote the share price and that was considered as under estimation or valuation of share price that indicates signaling to the market.

Jaemin Kim (2007) found that daily returns reduced significantly for share repurchase firms and also examined changes in systematic risk as measured by CAPM beta. Active buyback was a tool for buying their own shares when the share price decreases. And CAPM beta does not decrease the firms were not share repurchase program. It provides additional support for the relation between actual buyback and return volatility decrease, which finally indicates to the systematic risk decrease.

Konam et al (2010) explained the share price effects and determinants of share repurchase programs for French, German, Italian, and British firms. Like US firms, the authors found that German and Italian share repurchases were met with a positive and significant share
price response. However, British repurchase announcements exhibit small positive abnormal returns, and abnormal returns for French share repurchases were insignificantly different from zero, both results being quite different from results found in studies of US firms. Their results from their analysis of cumulative abnormal returns were also consistent with the Undervaluation, Takeover Deterrence, and National Investment Opportunity Set Hypotheses. However, the author do not finds support for the Excess Capital Hypothesis, the Intangibility Hypothesis or the Optimal Leverage Ratio.

Lasfer (2000) observed the event window from 1985 to 1998 and discovered a 1.64 percent return in response to announcements in the UK, including a reaction of 1.06 percent to buybacks for other European countries. Particularly, researcher observed at the French open market repurchases in the same period, but the author can’t find a significant price reaction to announcement of open market purchases in French.

Laurie Simon, (1992) described that fundamental difference for the Dutch auction tender offer was that not one offer price exists. The Dutch auction uses a price range from which shares will be purchased. Shareholders were invited to tender their stock. If the price was stated within the price range, the firm gathers the response and creates a supply curve. The firm pays the lowest price for the desired amount of shares.

Medury et al, (1992) analyzed the differences among repurchasing and non repurchasing firms and also between various repurchasing firms on the basis of the type of repurchasing method utilized by them. The authors taking a sample of 283 repurchasing and 577 non-repurchasing firms over a period of 1983-1986, identified 14 independent variables for differentiation on basis of the basic motivation driving repurchase decisions. The author developed multiple discriminant analysis for purposes of segmenting the firms and also to identify the relative strength of each individual variable. The results were validated using holdout sample, thereby providing sufficient evidence of wide usage of the model and the variables involved. The study reported variables related to share prices, liquidity, dividend payouts and leverage levels as the significant ones to differentiate the firms following either open market operations or tender offer method.

Milano and Cryan (2012), found firms used their cash earnings to buy back shares provide lower total returns in the form of capital gains. The study was done during the period from 2001- 2011. In addition, firms prefer to buyback in good times, and when share prices were high. Adversely, such prospered buybacks falls in bad times, when prices decline and there
wa restricted cash. According to Standard & Poor’s S&P 500 data, firms spent four times more on share repurchases in 2007 as in 2009, when the share prices were much lower. Firms have the intention to buyback when the prices were high, and that in turn restricts the promoted lucrativeness of share buybacks.

Mishra, (2005) investigated share buybacks in India, which took place in the period 1999 till 2001. The announcement of a buyback from the management resulted in an increase in the stock price. This was a short-term phenomenon. The prices of shares had no sustainable basis to stay higher than before the announcement. After the buyback, the price of a share decrease below the price before the announcement of the buyback. The study concludes with the results of quantitative and qualitative research that the buybacks were not successful in India and that a buyback could not ensure a sustained increase of the share prices.

Raisa Beygelam (2005) found that the true option prices were on average closer to bid than to ask quotes indicating that mid quotes were indeed proxies for the true option prices. The market participants adjust their trading strategies in times of high option price asymmetry.

Rainer et al (2011) contributed the provision of a simple deterministic framework for answering the question whether a buyback option should be offered by the Original Equipment Manufacturer (OEM) to the repair shops, and which buyback price should be paid for each returned core. And further high light the impact of remanufacturing performed at the OEM on the profitability of buyback.

Rim (2013) found out the relationship between the share repurchase and ownership (managers) used 77 companies as sample in the year 2003 to 2008. The study also found the investors were negatively affect the buyback of shares and also positive relationship between the shareholding of the owners and the share repurchases. It may be factor for the repurchase by improving the stockholding of owners who repurchase the stocks.

Roosenboom et al (2001) said about the share buybacks, which took place in the period from January 1995 until January 2001. The announcement of a buyback created an average stock performance of 1.4 percent. The structural performances were examined. After 30 trading days, the positive performances had evaporated. The study concluded that buybacks do not create any sustained increase in the share price.
Ye Lu, et al (2011) assumed that a firm has a reservation price for the stock, which was the highest price that the firm was willing to pay to repurchase its own stock. The author characterized the optimal policy for the trader to maximize the total number of shares that the author can buy over a fixed time horizon. Specifically, studied Greedy Policy, which involves in each period buying a quantity that drives stock price to the reservation price.

**2.11 Leverage effect on Buyback of shares**

Armen Hovakimian (2001) suggested “target adjustment hypothesis” consisting of two different subparts. The sub part pertains to findings evidence for deviation from target leverage as the motivation for different financial transactions which include debt issuance, debt significant impact of pre event deviation from target leverage in case of all the events except debt reduction. In the second sub part, segregating debt issuance/reductions and equity issuance/repurchases as separate events, logistic regression results showed market conditions as the main driving force impacting timing of these transactions. Besides, the effects of equity transactions on deviation from target leverage ratio were marginal and transitory as compared to debt transactions which were long lasting and significant. Hence, this study out rightly rejected optimal leverage ratio to be the major motivation for share repurchases/issuances.

Arak (1999) discussed the ineffectiveness of repurchases as a tool for enhancing EPS. Primarily, with repurchases, there was automatic reduction in number of outstanding shares in the denominator, but the automatic increase in numerator was not possible. Maintaining same level of EPS requires high returns on investments on the changed assets as compared to interest foregone on cash used for repurchases.

Buyback of shares as an earnings management tool for the debt financing constraints and affected that the constraints of the growth of real earnings management technique. The author showed the buyback of shares was an instrument to increase the earnings per share. Kathleen Farrell, Emre Unlu and Jin Yu(2014).

Hovakimian, et al (2001) was able to segregate the motivations behind buyback verse share issuances. Researcher suggested the deviation from the target debt ratio, and the main reason
for firms going for share buyback. However, the variables used in the study proved too weak in predicting share issuances.

Kaur and Balwinder (2010) analyzed the market reaction to the share buyback 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 buybacks. Further, abnormal returns were tested for information signaling, free cash flow and leverage hypothesis. Results were revealed that only leverage and under valuation hypothesis were found valid whereas signaling and free cash flow hypothesis were rejected.

Maxwell and Stephens (2003) observed wealth expropriation through reactions in stock prices and bond markets to share repurchases. Researcher found that on average bond returns fall by 18.5 basis points (at 1 percent significance level) around the time of the repurchase announcement, additionally bond ratings, following a repurchase announcement, were more likely to be downgraded than upgraded.

Nidal Rashid Sabri (2003) examined one of the most important issues in the international corporate laws, which has the issue of share repurchases known as treasury shares. This study investigated corporate laws, stock exchange regulations, research literatures and stock trading volume for repurchase activities. The author covered a sample of thirty-five countries developed and emerging markets. Their study also found that there was an increasing movement in the world stock market towards adopting or deregulating the share repurchase activities, More than half of the selected sample witnessed a change in the related laws (especially corporate laws) of share repurchases during the period 1995 to 2000. Moreover, there was a toleration to use the treasury share in enhancing the stock market during stock crises and extraordinary market price volatility. Based on upon findings, a modal has been suggested and articulated to be considered as a stabilization instrument for stock marketing.

Skjeltorp and Seggard (2004) their study proposed that optimum leverage hypothesis to explain abnormal returns during repurchase announcements. If firms were below their optimum capital structure, the share repurchase increase leverage, increases the tax shield and increase firm value.
William and Nelson (1999) reported a 12 percent higher annual return over a period of five years following buyback as compared to share issuance. Inefficiency in the speed with which the market corrects itself has been put forward as the root cause for excess returns in the long run occurring to firms repurchasing shares. Thus, it increases the value of the firm as firms tend to streamline or adopt the discipline of leverage through buyback.

2.12 Liquidity Effects on Buyback of shares


Barclay and Smith (1988) found that an increase in bid ask spread in case of a firm announcing buyback. The study revealed that an increase in cost of capital with a decrease in liquidity which was indicated by an increase in bid ask spread.

Franz et al (1995) conducted an analysis of stocks on NASDAQ. Upon repurchase announcements, the information which was earlier the domain of a few managers becomes widely public, thereby reducing the risk of adverse selection by various active market traders. Decrease in adverse selection cost due to decreased information asymmetry reduces the bid ask spread and hence, increases liquidity.

Guffey and Scheneider (2004) examined a sample of 672 open market repurchase announcements and 49 tender offers during a period 1994 to 1996. A total of 11 independent variables were taken and categorized into 5 broader categories through factor analysis. Subsequently, developing a logistic regression model to compute the differences among repurchasers and non-repurchasers, the authors found profitability as the most important variable followed by size, growth and leverage. However, the liquidity has been reported to be the significant factor in case of companies repurchasing through tender offers.

Hans et al (2012), explained the bond exchanges and buyback operations serve two main purposes. First, by reducing the outstanding amounts of bonds close to maturity, exchanges and buybacks help in reducing roll-over peaks and thus lowering refinancing risk. Second, exchanges and buybacks allow debt managers to increase the issuance of on-the-run
securities above and beyond what would otherwise have been possible. The results more rapid build-up of new bonds enhances market liquidity of these securities. This in turn had be reflected in higher bond prices. Hence, bond exchanges and buybacks were aimed at lowering refinancing risk. In addition these operations may also contribute to lower funding costs for governments.

Hsu, Pao-Chung (2008) investigated the impact of odd lot share repurchase program on liquidity of stock of the buyback firms, and the success of program. The author collected data 204 initial odd lot repurchase program announced in 182 firms during 1985- 2000. The author examined effects of the program on liquidity and volatility of stocks of the repurchasing firms, and number of shareholders.

Huang (2012) explained and initiated the share repurchase program important determination for stock market liquidity. Researcher study was based on Real Estate Investment Trust (REIT) share repurchase initiator and non-initiator by the year 1985 to 2010 but sample taken 1,310 out of this samples only 205 companies for repurchase initiator in the period of after 1998. The result revealed that whether stock market liquidity affects the REIT to initiate the share repurchase program the results are asymmetric information companies will share repurchase only if liquidity was high in stock market.

Nyar (2008) studied that short term and long term impact of buyback program on liquidity. The results suggest that liquidity significant was improved during the tender offer of share repurchase but the liquidity was temporary and limited for short period. Whenever that Dutch auction and Fixed Price Tender offer announced by firm buyback that means firms increased liquidity and this study confirmed that during Dutch auction and Fixed price tender methods increased stock price and showed the short term liquidity during share repurchase program especially tender offer method and the author were carried out the analysis of total of 165 Dutch auction/ fixed price tender offers to establish a relationship between liquidity and share repurchase happening through these two methods. Research noted the changes in liquidity over a period of 30-75 days post expiration of the offer as a measure of effect of repurchases over long term liquidity. However, no significant change could be attributed to liquidity in spite of decrease in relative spreads.

Paul Brockman, et al (2008) studied the impact of stock market liquidity on managerial payout decisions. The study argued that stock market liquidity influences payout policy through a first-order effect on the share repurchase decision, and a second-order or residual
effect on the dividend decision. Managers compare the tax and flexibility advantages of a repurchase against its liquidity cost disadvantage. All else equal, higher market liquidity encourages the use of repurchases over dividends. Their empirical results were confirmed that stock market liquidity plays a significant role in repurchase and dividend initiations, as well as in recurring payout decisions. The previous studies that measure liquidity changes following the repurchase decision, further the study also examined liquidity levels prior to the payout decision. The author showed that managers condition their repurchase decision on a sufficient level of market liquidity, Repurchases have recently become the payout decision of choice in part because of rising stock market liquidity.

2.13 Identification of Research Gap:

None of the studies focused on the variables that indicate the company’s likelihood of share repurchase and whether share repurchase announcements results in abnormal returns. This study pursues to fill this gap besides whether any impact of share repurchase occurred in the company.

2.14 Conclusion:

Review of Literature showed that the Buyback of share activities in different countries like U.S. U.K. Australia and India. The introduction of Buyback of shares in India showed clearly that the main purpose was the profits that can be distributed to shareholders in the form of Dividends or share repurchases. This chapter covered the buyback of shares played an important role in the companies i.e., researchers have explained the share repurchases in all over the world indicated the signaling to the investors or market and it has the substitute or alternative for dividends. Based on literature reviews, it made established that many of the research papers in buyback of shares explained and stated that Signaling hypothesis, Dividend Substitution, Free Cash Flow, optimal capital structure, option funding and managerial wealth and Liquidity. This showed there were many factors influence the company to go buyback of shares.