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Why do Firms Undertake Accelerated Share Repurchase Programs?

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Abstract


Using a sample of accelerated share repurchase (ASR) program announcements from 2004 to 2020, we analyze firms' rationale for undertaking ASR programs rather than the more traditional open market share repurchase (OMR) programs. Based on the notion that ASR programs are faster but more costly for the firm to execute and involve a greater commitment by the firm to complete the repurchase of the entire number of shares announced, we develop and test several hypotheses regarding firms' choice between ASR and OMR programs. The three most prominent of these hypotheses are the signaling or undervaluation hypothesis, whereby firms with more severely undervalued equity (relative to intrinsic value) are more likely to undertake ASR rather than OMR programs; the EPS manipulation hypothesis, where firms with CEO compensation more closely tied to EPS are more likely to choose ASR over OMR programs; and the liquidity reduction hypothesis, where the reduction in stock liquidity following the repurchase announcement is expected to be smaller for firms announcing ASR rather than OMR programs. Our multivariate analysis results show that, compared to those announcing OMR programs, firms announcing ASR programs have lower market-to-book ratios, have larger positive abnormal stock returns upon repurchase announcement, and have better post-announcement operating performance, thus providing strong support for the signaling or undervaluation hypothesis. Our results are also consistent with the EPS manipulation hypothesis but inconsistent with the liquidity reduction hypothesis. Finally, we do not find any support for the predictions of several other hypotheses that have been advanced to rationalize stock repurchases, such as the takeover avoidance, employee stock option dilution, and managerial opportunism hypotheses.

Keywords: Accelerated Stock Repurchase (ASR), Open Market Stock Repurchase (OMR), Signalling, Undervaluation, EPS Manipulation

JEL Classification: G32; G35; G14

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