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## Share Repurchases and Employee Stock Options and Their Implications for S&P 500 Share Retirements and Expected Returns

*Board of Governors of the Federal Reserve System Finance and Economics Working Paper No. 99-59*

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### Abstract


We estimate the effects of share repurchases and employee stock option exercises on net share retirements for large S&P 500 companies. We find that, over the past five years, gross repurchases have reduced shares outstanding 2 percent annually; but, owing to the exercise of employee stock options, only about half of those shares were actually retired. Given the recent pace of employee stock option grants, and assuming that equities continue to be priced at about 30 times earnings, our analysis suggests that the pace of net share retirements will fall well below the pace of the last few years, unless corporations use nearly all their earnings to fund shareholder payouts. Moreover, over the long haul, assuming corporations need to retain 40 to 50 percent of their earnings to invest and grow at historical rates, the long-run average pace of net share retirements is likely to fall to 1/2 percent or less.

**Keywords:** Share repurchases, stock options, expected returns

**JEL Classification:** G10, G35

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