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Repurchases, Reputation, and Returns

Alice Adams Bonaimé*

Abstract

This paper examines whether a firm's reputation is a determinant of repurchase completion rates (the ratio of actual to announced repurchases) and whether the stock market discounts announcements made by less reputable firms. Prior completion rates are positively correlated with current completion rates and announcement returns, suggesting consistency in repurchases and implying a reputational effect. Further, a nascent literature regarding accelerated share repurchases (ASRs) finds them to be more credible than open market repurchases. I show that the probability of announcing an ASR is greater for firms likely to be concerned about reputation because of low past completion rates.

I. Introduction

Firms signal material information to the stock market through corporate announcements, which include news pertaining to events such as mergers and acquisitions, earnings, and changes in payout policy. This paper asks whether firms establish a reputation with respect to releasing accurate information and whether the stock market considers past behavior when evaluating new corporate announcements. Specifically, I study a method by which firms voluntarily disclose information to investors: open market share repurchases.

Share repurchases are an increasingly popular form of corporate payout, and open market share repurchases are the most common form of repurchase (Grullon and Michaely (2004)). An open market repurchase occurs in 2 steps: i) the announcement, which includes the intended size of the repurchase plan as a dollar value or a number or percent of shares outstanding; and ii) the actual repurchase, which generally occurs over several years after the announcement.[1] Managers

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