MODELING STOCK BUYBACKS USING A REVERSE REPO MODEL

Khaled Abdou, Pennsylvania State University, Berks College, Tulpehocken Road, Reading, PA 19605, 610-396-6173, kka1@psu.edu
Pia Gupta, California State University, Long Beach, 1250 Bellflower Blvd, Long Beach, CA 90840, 562-985-2466, pia.gupta@csulb.edu

ABSTRACT

In this paper, we go beyond the stock repurchase event and investigate what companies do with acquired treasury stock in the long-term. The study follows a “reverse repo” decision-based model rather than “a corporate event transaction” model. Our model follows the structure of a reverse repo (repurchase) transaction, where the company uses its “call option” to buy back equity, which, it can then “sell” or “use” to fund corporate events in the future. Our research integrates the buyback announcement and level of execution (completed, partial completion or no buybacks executed) with how companies make use of the repurchased shares. We analyze the different uses such as SEOs, acquisitions/swaps, and stock options using empirical data. Our study addresses several questions involving long-term company value and thus, has important implications for stockholders.

Keyword: Stock repurchase, Event study, Reverse repo