

Share buybacks help boost performance

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Share buybacks are not always popular with investors, who often prefer to see higher dividends, but firms that repurchase shares have outperformed their peers by 25% over the past two years.



Indxis, an index firm, tracked the performance of companies listed on NYSE or Nasdaq that have repurchased more than 5% of its common stock over a 12-month period.

The performance of these firms matched the record of companies in the S&P 500 until the nadir of March 2009, when the S&P 500 hit rock bottom. Since then, firms that have instigated buyback schemes have far outperformed those who have not. The Indxis

BuyBack Achievers Index has almost doubled since March 2009, from 2500 basis points to 4,850, almost 1,000 points above the S&P 500.

This poses a difficult question for firms sitting on sizable war chests. According to research by Morgan Stanley in November, cash levels at US investment-grade companies are at the highest point in two decades, relative to the amount of debt on their balance sheets.

These firms have the choice of increasing dividends, reinvesting the cash, buying other firms or repurchasing their own shares.

Some investors prefer to see the excess capital moved off the balance sheet and paid out as extra dividends. Speaking to Financial News in December, Robert Talbut, chief investment officer at Royal London Asset Management, said: "I believe that, as fund managers, we should be demanding that companies return excess capital to us in the form of dividends."

Share buybacks can issue mixed signals to existing shareholders. Decreasing the pool of available shares helps boost the share price and is regarded as a vote of confidence by the company. It also improves return of equity, but using up too much capital can leave it at risk of missing out on potential deals.

British Tobacco, the world's second largest tobacco firm, highlighted the dilemma at the end of February. The company announced it would continue a share buyback scheme initially postponed in 2009 in the wake of the [financial crisis](#). But analysts were disappointed at the scale of the proposed £750m share buyback after previously forecasting a figure of £1bn.

Chief financial officer Ben Stevens said he hoped to keep firepower available for any potential acquisitions, but shareholders questioned British Tobacco's caution, with shares falling slightly on the announcement, despite the firm posting an increase in pre-tax profits.

While investors may have been desperate for healthy balance sheets in 2009, two years later, good health does not always result in happy investors.