

The Outcome of Prior Stock Repurchase Decisions and its Effect on Future Stock Repurchasing Decisions

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ABSTRACT

Stock repurchases are risky investments made by management on behalf of current shareholders. My study asks to what extent the outcome of prior repurchasing activity influences future repurchasing decisions. Prior gains and losses are measured relative to actual repurchase prices, which are referred to as reference points. I find that the size of past gains has a significant impact on repurchases, even after controlling for variables previously shown to affect repurchase activity. When losses and gains are included separately the entire effect is driven by the sensitivity of repurchases to past losses. I find that over very short horizons (one- and two-years), large gains and large losses both increase the firm's repurchase activity. However, as the horizon lengthens into an intermediate range (three- to five-years) a distinct shift occurs. For firms with prior losses, subsequent increases in losses lead to less repurchasing; for firms with past gains, further gains tend to produce small additional increases in repurchases. Both CEO tenure and age affect repurchases in a manner consistent with managerial loss aversion.