

A THEORETICAL DISCUSSION ON THE INFORMATION CONTENT OF OPEN MARKET SHARE REPURCHASES IN MALAYSIA

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ABSTRACT

In this paper, we undertook a theoretical discussion on the Malaysian stock market reactions to open market share repurchase programs. Share repurchases have become more frequent in Malaysia since the legalization of share repurchase activities in 1998 as a result of the Asian Financial Crisis. The study proceeds to focus on the information content of open market share repurchases, particularly on the information signaling hypothesis, the market undervaluation signaling and the free cash flow hypothesis of firms' share repurchase programs. We found that the most dominant motivation behind companies' share repurchases programs follow the information signaling hypothesis and the free cash flow hypothesis.

Keywords: *Open market share repurchase, positive short term market reaction of share repurchases, information signaling hypothesis and the free cash flow hypothesis*

1. Introduction

Share repurchase is a corporate event which basically refers to a company buying back its own shares from the marketplace, thereby reducing the number of the firm's outstanding shares. It has now become a common and popular alternative to the conventional dividends as a form of corporate payout where firms distribute excess cash in returning capital to their shareholders. Its popularity began in the United States (US) market in the early 1980s, particularly fueled by open market repurchases (OMRs) and this surge in activity soon spread across to other developed countries like United Kingdom (UK) and Canada in the 1990s. In fact, globally, a host of other countries that formerly prohibited share repurchases also started to legalize share repurchase activities, for example Japan in 1995, Finland and Malaysia in 1997, Germany, Singapore and France in 1998, India, Norway and South Africa in 1999, Denmark, Sweden and Taiwan in 2000.

Globally, many companies have grown to appreciate the value of share buybacks as a tool for capital management and to enhance shareholder returns. Some past research has shown that repurchases can provide economic benefits to both shareholders and firms and as an example, repurchases help improve liquidity

through the reduction of costs incurred by shareholders in the buying and selling shares (Cook et al., 2004 and Franz et al., 1995). Fried (2005) argued that with the increase in trading volume caused by repurchasing activities, it is much easier for the market makers to make a reverse position in the stock when the need arises, hence reducing stock holding costs which in turn lowers bid-ask spread, and ultimately increases shareholders' net returns (Singh et al., 1994 and Cook et al., 2004).

Other than improving stock liquidity, share repurchases could also provide firms with a more efficient method of distributing transient (non-recurring) excess cash flows, especially in relatively small amounts (Jagannathan et al., 2000). Fried (2005) proposes that managers seeking to distribute transient cash flows would not wish to initiate regular dividends or increase the firm's current dividend as it may inadvertently signal a commitment by managers to continue paying dividends (or larger dividends) in the future. Share repurchasing could avoid sending such a commitment signal, especially OMRs as repurchase programs once announced still depends on managements' discretion on whether or not to undertake share buybacks. The author posited that in times when firms only wish to make small payouts, a share repurchase would be more advantageous as compared to dividends. When a firm distributes cash through a repurchase, both the firm and the selling shareholders incur brokerage fees and as share trading is mediated through a market maker, both the parties would bear the cost of the bid-ask spread. Hence, if the amount distributed is sufficiently large, a dividend is likely to involve lower per-dollar transaction costs than a repurchase. However, for small amounts, a repurchase would be a more cost-effective method of distributing transient excess cash flows than a dividend.

Another advantage of repurchases over dividends is it also enables firms to provide shares for increasingly popular employee stock option programs (Fenn et al., 2001 and Kahle, 2002). Fried (2005) proposes that a large portion of executive compensation comes in the form of stock options. Options are also widely used to compensate and motivate lower-ranking employees. Under these plans, employees are given options to buy the firm's stock at a certain strike price (usually equal to the grant-date market price). The options cannot be exercised until the end of their investing period. Upon exercise, the firm sells share to the employee for the strike price, and the employee then typically sells those shares in the market for a profit. Employee stock option programs thus require a steady supply of shares. Unlike dividends, repurchases can provide those shares.

All in all, the phenomenal growth in share repurchases as a form of corporate payout and its growing significance has attracted much attention and interest, as well as produced numerous studies on its impact on corporate security prices and earnings performance in developed countries such as US, UK and Canada. Unfortunately, the history of this transaction is rather short with respect to developing countries, particularly in Asia with only some recent evidence from Korea, Hong Kong, Taiwan and Japan. More international evidence, particularly from the emerging markets is required, and at present, documented empirical evidence on share repurchases is scarce in Malaysia. Zainudin et al. (2003) explored companies' stated motivations for share repurchases in the Malaysian capital market through companies' circulars to their shareholders. Although Zainudin et al. (2003) had attempted to document the various motivations behind form's share repurchase programs, the results obtained merely involves extracting what firms had stated their motivations were from the circulars issued to the shareholders. Their studies are neither empirically driven nor rigorous and therefore require caution in the interpretation of their results. Lim et al. (2002) and Mohamed et al. (2001) studied the price reaction of share repurchase announcements in the Kuala Lumpur Stock Exchange, which showed positive market

reaction which is consistent with the market undervaluation signaling hypothesis. Abdul Latif et al. (2013) also posited positive market reaction around announcements of repurchase implementation, although the study did not find any significant immediate price reactions surrounding intention dates.

2. Share Repurchase in Malaysia

Before 1st September 1997, companies in Malaysia were not allowed to buy back their own shares. Such prohibition (Lim et al., 2002) was probably premised on the potential conflicts of interests that could arise in that if stock prices reflect the collective judgment of markets on management, this would enable management to engage in price support which in turn could lead to value destruction.

It was after the 1997 financial crisis that the Registrar of Companies (ROC) allowed the Malaysian companies to engage in share buybacks. The 1997 Asian financial crisis adversely affected the Malaysian ringgit which led to a 30% devaluation of the currency against the US dollar, and which subsequently led to the collapse of the stock market and asset prices in which the Kuala Lumpur Composite Index (KLCI) plunged almost 60% from its high for that year (Zainudin et. al., 2003), falling from a level of 1277 in February 1997 to 512.41 in November 1997. It was viewed that the government interference in the Malaysian stock market through the legalization of repurchase activities was one of the recovery strategy to revive and stabilize the stock market which was put in force within three months when share prices in the Kuala Lumpur stock exchange fell sharply in June, 1997. In fact, Grullon et al. (2000) found evidence that repurchasing program announcements are inversely related to market movements; implying that when stock prices fall, repurchase announcements rise, as reflected in the US 1987 market crash as well as the 1998 market disturbance stemming from trouble in the global bond markets.

Since the passing of the Malaysia's share repurchase regulations under Section 67A of the Companies (Amendment) Act 1997, there has been a tremendous growth in the volume of share buyback activities among the Malaysian listed firms. Share repurchasing is still considered a new phenomenon in that the buyback mechanism did not catch on until much later as it has not always been the norm for companies to repurchase their shares and that firms in the initial stage were probably vague about the benefits of share repurchases. Over the years, as firms began to learn about the significance of share repurchases based on the activities in more mature markets such as the US where buybacks have been ongoing for about two decades since 1982, there has been a spree of buyback activities among the Malaysian listed firms ever since.

Sabri (2003) shows that until 1999, out of 171 companies that had received approval for share repurchases, 16 companies had implemented the targeted repurchased shares (ROC, 1999). Lim et al. (2002) showed that until 2001, 43 companies, consisting of 38 main board companies and 5 second board companies had actually repurchased their shares (Refer to Tables 1 and 2).

Table 3 presents a longer-time frame report on firms' share repurchase activities compiled from Bloomberg and the Bursa Malaysian website. It reports the number of firms involved in actual repurchases, the number shares repurchased and the value of shares repurchased from 1999 to 2007. Based on the data presented in table 3, Malaysian share repurchase activities in terms of number and values of shares repurchased has ever since been on a rising trend since 1999 except for the year 2002 and 2006, which witnessed a decrease in the number and the value of shares

repurchased. With regards to the number of firms that actually executed its OMR programs, it has also been on a rising trend which witnessed a total of 667 firms that exercise OMRs from 1999 to 2007.

Table 1. Breakdown of KLSE Listed Companies involved in Open Market Repurchases (OMRs) 1997 - 2001#

Breakdown by Type	Main Board Companies	Second Board Companies	Total
Announced/Obtained shareholders' approval at EGM/AGM	112	19	131
Actually repurchased shares	38	5	43

(Sources: Data from KLSE).

indicates the period from January 1 up to June 30, 2001

Table 2. Breakdown by Year of Companies that Executed Open Market Repurchases (OMRs)

Breakdown by Year	Main Board Companies	Second Board Companies	Total	Cumulative Total
1997	1	0	1	1
1998	11	3	14	15
1999	11	0	11	26
2000	9	1	10	36
2001#	6	1	7	43
Total	38	5	43	

(Sources: Data from KLSE).

indicates the period from January 1 up to June 30, 2001.

Table 3. Firms' Actual Open Market Share Repurchase (OMR) Activities from 1999 to 2007

Year	No. of Firms	Cumulative No. of Firms	Actual No. of Shares Repurchased	Value of Shares Repurchased (RM)
1999	17	17	45,890,400	226,594,232.79
2000	20	37	127,407,600	592,054,744.37
2001	33	70	203,598,800	521,160,676.02
2002	36	106	119,375,000	291,361,735.18
2003	64	170	283,348,045	567,400,363.65
2004	69	239	545,403,400	1,774,231,869.54
2005	127	366	1,049,151,490	2,359,669,999.88
2006	149	515	754,174,007	1,229,778,437.24
2007*	152	667	853,986,000	2,816,100,393.25
Total number of shares repurchased from 1999 to 2007			3.98 billion shares	
Total Value of Shares Repurchased from 1999 to 2007 (RM)				RM 10.38 billion

(Sources: Data compiled from Bloomberg and Bursa Malaysian website).

There are various methods of share repurchases such as tender offer repurchase (where the company specifies a price at which the company will buy back its shares, the number of shares it intends to buy and the period of time for which the offer will be kept open), Dutch-auction tender offer (where the firm specifies a range of prices from which the shares would be repurchased), privately negotiated repurchase (where the company buys back shares from a large shareholder(s) at a negotiated price) and the open market repurchase (OMR) where the company buys back shares in the open market at the prevailing market price. Malaysian listed firms apply the OMRs as stipulated by Bursa Malaysia's Chapter 12 Share Buy-backs Listing Requirements, which allows only the OMR option where repurchases must only be effected on the market of the exchange. "On the market" refers to transactions that are to be made through the Automated Trading System of the Bursa Malaysia and excludes any forms of direct business transactions.

3. The Economic Motivations for Share Repurchases

As mentioned earlier, the motivation for share repurchase in Malaysia was predominantly to stabilize share prices during the financial crisis. Zainudin et al. (2003) examined 40 companies' circulars to shareholders between October 1999 and May 2002 and found the five widely stated motivations for share repurchases are to stabilize stock prices, pay stock dividend, investment opportunity, use surplus cash and increase shareholder returns. Now that almost two decades have passed and that Malaysia is over with the 1997 Asian financial crisis, the increasing popularity of share repurchase among the present Malaysian companies might most probably be motivated by other reasons other than to stabilize share prices.

Several hypotheses have been advanced in the empirical literature to explain what motivate firms to initiate share repurchase programs. Among them are the information signaling hypothesis where firms repurchase to signal optimistic information about their future operating and cash performance prospects (Dann, 1981; Vermaelen, 1981 and 1984; Ofer and Thakor, 1987 and Constantinies and Grundy, 1989), the market undervaluation signaling hypothesis where firms repurchase to signal that their current stock price is below their true intrinsic value (Comment and Jarrell, 1991 and Ikenberry et al. 1995), the agency costs of the free cash flow hypothesis where firms repurchase to mitigate potential problems of unmonitored spending of excess cash on unprofitable projects (Easterbook, 1984 and Jensen, 1986), the capital structure adjustment hypothesis where firms repurchase shares to adjust their financial leverage towards an optimal leverage ratio, thereby allowing firms to benefit from tax advantages of debt financing (Bagwell and Shoven, 1989 and Hovakimian, Opler and Titman, 2001), the takeover deterrence hypothesis (Brown and Ryngaert, 1991; Bagwell, 1991) where firms repurchase to fend off unwanted takeover attempts, the dividend substitution hypothesis where firms substitute dividends with repurchases as a form of corporate payout to benefit from tax savings through capital gains tax of repurchases which is usually lower than the ordinary dividends tax (Black, 1976; Barclay and Smith, 1988), where firms distribute temporary cash flows to the shareholders through repurchases and would increase dividends only when earnings is believed to have increased permanently (Jagannathan, Stephens and Weisbach, 2000) and, where firms repurchase shares to counter the dilution effects of employee and management stock option plans (Fenn and Liang, 2001).

Among the prominent explanations given by most findings for share repurchases are the “signaling” hypothesis and the free cash flow hypothesis. With respect to the “signaling” hypothesis, there are two different versions of the signaling theory i.e. the information-signaling and the market undervaluation signaling theories, which a number of past academic researchers have overlooked (Grullon et al., 2000) and at times, mistake one for the other. The authors asserted that the former reflects as an attempt by the management to signal new information relating to unexpected improvements in its future earnings and cash flow position while the latter is not about conveying new information, but instead is about expressing management’s disagreement with how the market is pricing its current performance, believing that their current stock prices have been mispriced, particularly underpriced by the market. Still, the authors view that in both cases, management of firms signal that their stock is undervalued in which the former reflects the inability of a company (without the repurchase) to convey its prospects convincingly to the market whereas the latter reflects the market’s inability to project publicly available information in the current stock price.

With respect to the free cash flow hypothesis, firms repurchase their shares to mitigate potential over-investment by management (Jensen, 1986) which argues that firms with excess cash and a poor portfolio of investment opportunities will face sizeable agency costs if the excess cash is not distributed to shareholders. Barring such a distribution, managers have incentives to invest the excess cash in perquisites, empire building (entrenchment), and other negative net present value (NPV) projects (Nohel et. al., 1998). Stock repurchases allow a firm to distribute its excess free cash flow, thereby eliminating the incentive for wasteful investment and increasing firm value.

Despite the above theoretical explanations for firms’ repurchases, these hypothesized effects are not mutually exclusive given that the above theories all predict the same positive stock price reaction to repurchase announcements. Hence, to verify if the two signaling theories and the free cash flow theory explain significantly the Malaysian OMR programs, it is important to distinguish between each of these theories and one of the ways to disentangle the competing hypotheses is to examine the market assessment of OMR repurchase announcements that includes both OMR market performances in the short and in the long term basis.

Positive short term market reactions of OMR program announcements, involving an event window of 41 days i.e. “20 days before” to “20 days after” the event day 0, may represent information-signaling hypothesis of firms’ OMR programs where managers attempt to convey optimistic information about its future earnings and cash flows prospects (Vermaelen, 1981 and 1984). It can also represent market undervaluation signaling hypothesis (Comment and Jarrell, 1991), especially in relation to repurchasing firms that have high book-to-market values (BMTV), generally known as “value stocks” and firms that are small in size, having small market capitalization values which are thought to offer greater potential for mispricing (Zhang, 2005). Likewise, firms’ OMR programs can also represent the free cash flow hypothesis, particularly for repurchasing firms that are more likely to over-invest as proxied by the Tobin’s Q of less than 1 which reflects high levels of cash and few investment opportunities in a firm (Lang and Litzenberger, 1989). In addition, superior price performance is also reflective of the free cash flow hypothesis in relation to firms with higher repurchase activity in terms of number of shares bought back with the view that higher volume of repurchases help to reduce agency costs of free cash flows by getting rid of excess cash being invested in unprofitable projects (Jiraporn, 2006).

As for positive long term market performance of OMR program announcements, involving a 3 year period of analysis following Zhang (2005), this represents market undervaluation signaling hypothesis of firms' OMR programs (Ikenberry et al., 1995 and 2000) while firms that experience a period of price depreciation before the repurchase announcements also represents market undervaluation signaling hypothesis of firms' OMR programs to indicate that the firms' stock prices are trading below intrinsic value

With respect to market assessment of OMR programs, due to regulatory constraints, repurchase activity was for many years concentrated in developed countries, particularly the US and it was in the 1990s that the removal of regulatory restraints allowed repurchases to be employed in many markets around the world. Although the resulting literature has provided many insights, one limitation of the existing studies is the concentration on the short-term market response to the repurchase announcement. For short-term price performance, it is well documented that most studies reported positive abnormal returns for share repurchase programs (Lee, Jung and Thornton Jr, 2005; Zhang, 2005; Lie, 2005; Chan, Ikenberry, and Lee, 2004; Grullon and Michealy, 2004; Ikenberry, Lakonishok and Vermaelen, 1995 and 2000; Comment & Jarrell, 1991; Lakonishok and Vermaelen, 1990; Vermaelen, 1981 and 1984; Dann, 1981 and Masulis, 1980). In fact, Lim et al (2002) as well as Mohamed et al. (2001) also documented positive price reaction from OMR announcements in the Malaysian market.

On the long-term price performance of OMRs, the extant literature is mixed and inconclusive. Ikenberry et al. (1995 and 2000) and Chan et al. (2004) investigate the long-term performance of OMRs in the US and Canada and find positive long-term performance where they interpret their results as being the result of an under reaction or delayed reaction by the market. Ikenberry et al (2000) and Zhang (2005) also found long term positive performance in "value" stocks, but not in "growth" stocks in Canada and Hong Kong respectively.

In contrast, Mitchell and Stafford (2000) and Lee, et al. (2005) found no evidence of long-run abnormal performance after repurchases in the US and Korea respectively, hence providing support for the efficient market hypothesis. Lee et al. (2005) argued that the main contributing factor that ensues differences in results is the potentially confounding effects of ongoing repurchase activity and related information releases in the US where firms take 3 years or more to complete announced repurchases (Cook, Krigman and Leach, 2003), thereby contributing to the difficulty of determining the actual number of shares repurchased by the firm. In Korea, firms are required to complete a repurchase within 3 months of the announcement and are required to report the number of shares actually repurchased at the end of the repurchase period. Lee et al. (2005) reiterated that the above Korean requirements resulted in a much cleaner sample as compared to US and hence provide robustness to the findings of Mitchell et al. (2000) of no long-run abnormal performance after repurchases.

Additionally, controversial issues regarding the various methodologies used by past researchers to determine long term market reaction have also contributed to the inconsistencies of past findings on long term performance of repurchase activities. Barber and Lyon (1996) argued for the simple buy-and-hold return (BHAR) method in measuring long-run abnormal stock returns where they found well-specified test statistics for detecting long-run abnormal stock returns in comparison to the reference portfolio model and the Fama–French three-factor model. Lee, Jung, Thornton Jr. (2005) suggested that based on the evidence in Fama (1998) and Mitchell and Stafford (2000) of misspecification in the event-time methods, the calendar-time

approach with both one-factor and three-factor models instead would produce better results in deriving long-run abnormal stock returns. McNally and Smith (2006), on the other end, however criticize both the BHAR and the calendar-time approach in measuring long term performance which ignores transaction costs and instead proposed using different trading strategies involving market and limit orders that incorporates price impacts and brokerage fees.

To recapitulate, the existing literature on long-term performance after repurchase announcements in the developed markets is inconclusive. In fact, no evidence of long term performance has yet been documented on the repurchases activity in Malaysia. Therefore, evidence of long term performance in this study on Malaysian repurchases would substantiate the documented evidence on this issue and also ascertain whether the market undervaluation signaling hypothesis explain the Malaysian OMR programs.

Despite the well documented evidence on the positive short term market performance of share repurchase programs, most of the documented evidence on short term price performance of OMRs is based on repurchase program announcements rather than actual repurchases. Knowing the fact that OMR program announcements are not obligatory commitments, the question of false signaling may arise in situations where management of firms in actual fact do not intend to buy back their shares from the market but make the repurchase program announcements to boost their stock prices and reap the benefits of short term price improvements (Fried, 2005). The author advocated that in the US, although all major US stock exchanges require firms to announce the board's approval of an OMR program, neither the stock exchanges require an announcing firm to indicate the number or value amount of shares to be repurchased or to indicate the expiration date of its repurchase programs. It was only in 2003 that the Securities and Exchange Commission (SEC) required disclosures of firm's repurchase activities in which in their quarterly public filings, firms are now required to disclose, among other things:

- (1) the total number of shares repurchased during the previous quarter;
- (2) the average price paid for those shares;
- (3) the number of shares that were purchased in the preceding quarter as part of a publicly announced plan; and
- (4) the maximum number of shares, or approximate dollar value, that may yet be repurchased under any share repurchase program.

Despite the new US disclosure requirements, problems arise in that investors may not learn about a firm's repurchases until several months later, which could still lead to misleading repurchase announcements or even enabling managers to buy back shares secretly to profit from bargain repurchases (Fried, 2005). In Malaysia, such possibilities are constrained by the stringent regulations set on matters pertaining to OMRs where companies are required to adhere to a structured pre-repurchase disclosure rules as laid out in appendix 12A, 12B, 12C and 12D of Chapter 12, Bursa Malaysia's Listing Requirements. Based on these requirements, firms are required to announce and disclose all information on the actual repurchasing day with regards to repurchase program authorizations and actual repurchase transactions such as the maximum number of shares that can be bought back (i.e. subject to a maximum of 10 percent of its issued and paid-up capital at the time of announcement), the actual number of shares purchased on each buyback transaction, the minimum and the maximum price paid for each share and the total consideration paid for each buyback transaction.

Moreover, unlike firms in US which usually take about 3 years to complete a repurchase program (Cook et al., 1988), Malaysian firms are required to complete their repurchase programs within a year, which starts immediately from the first initial approval obtained from its shareholders during the Annual General Meeting (AGM) or Extraordinary General Meeting (EGM) to the next. In the forthcoming AGM, the firm merely seeks renewal of its shareholder authorization to repurchase shares and such information is usually incorporated into market expectations. Note that as share repurchase program announcements during the AGM are made together with other announcements, it is rather impossible to separate their effects.

Hence, based on the above nature of legal restrictions on OMRs in Malaysia, the strength of the signaling mechanisms based on share repurchase authorization program announcements may be questionable. In fact, an Australian study by Lamba and Ramsay (2000) argued that due to the strict regulations on repurchasing for Australian firms up to 1995, repurchase authorization announcements are ineffective as signal mechanisms. A more accurate way of evaluating the signaling mechanisms in the Malaysian context would be based on actual repurchase announcements instead of share repurchase authorization program announcements. The existing empirical literatures of OMRs short term market performance with regards to such stringent regulations, especially in relation to reported actual repurchases and not announced repurchase authorizations is acutely limited. Documented evidence from Ikenberry et al. (2000) in the Canadian market, Zhang (2005) in the Hong Kong market and Lim et al. (2002) in the Malaysian market are among the few that relates to OMR market reaction based on actual repurchases. Hence, further attempt to study market reaction based on actual repurchases involving a longer period of time with larger sample size would go a long way to verify if both the signaling theories hold, as well as to ultimately identify which of the two signaling theories is more relevant for the Malaysian OMRs programs.

Other than examining market performance of OMR programs in studying the information content of repurchases, the study of repurchasing firms' operating performance also enables to determine if repurchases are motivated by information signaling hypothesis or by the free cash flow hypothesis of firms' share repurchase programs. According to the former hypothesis, repurchasers' attempt to signal good news about firms' future profitability, hence implying that operating performance, as proxied by return of assets (ROA), would increase after repurchase announcements. The latter hypothesis however justifies that due to firms' entering into maturity stage, investment and growth opportunities decline, thereby resulting in declining profitability or operating performance, to ultimately end up with high free cash flows in a company in which through repurchases could the agency costs of free cash flow be mitigated (Grullon et al., 2004). Indirectly, this implies that repurchasing firms would experience a period of declining operating performance before repurchase announcements.

With respect to the operating performance of repurchasing firms after repurchase announcements, the existing evidence has thus far produced results that are inconclusive. Studies from Vermaelen (1981), Bartov (1991), Jaganathan and Stephens (2003) and Grullon et al. (2004) do not provide support for any robust improvements in future earnings after OMR announcements whereas Lie (2005) provide evidence of operating performance improvements and the positive earnings announcement returns of firms that actually repurchase shares during the same fiscal quarter, suggesting that actual repurchases, and not announcements per se, signify future performance improvements. Grullon et al. (2004) find only weak evidence of a performance improvement around OMRs announcements and to the extent that there

is a performance improvement, it occurs during the announcement year, and not in subsequent years. Jaganathan et al. (2003), on the other end however provide evidence that operating performance of repurchasing firms actually decline in the years following repurchase announcements.

The existing evidence with respect to future operating performance of repurchasing firms is limited and inadequate, hence the findings of this study on Malaysian repurchases would substantiate further the evidence documented in the developed and the developing markets. Ultimately, this would also ascertain whether the information signaling hypothesis or the free cash flow hypothesis explain the Malaysian OMR programs.

Finally, in studying the information content of repurchases, an analysis on the repurchasing firms' capital expenditures and cash reserves will be undertaken to verify if the information signaling hypothesis or the free cash flow hypothesis explain the Malaysian OMRs programs. In relation to the former hypothesis, Grullon et al. (2004) argues that there will be an increase in firms' capital expenditures as well as research and development (R&D) expenses following share repurchase announcements as firms attempt to convey information about the good investments they are undertaking where future earnings and cash flows from those investments would be realized in the distant future. As for the latter hypothesis, the author postulates that if repurchases are being used to reduce free cash flows in times when cash is least needed i.e. when investment opportunities are scarce; a reduction in financial slack will be observed. In their findings, it showed that repurchasing firms significantly reduce their cash reserves over the three years following repurchase announcements, supporting the idea that repurchasing firms face a shrinking investment opportunity set. In fact, their findings on the repurchasing firms' capital expenditures that includes R&D expenditures also declines during the year of event as well as three years after the event.

Based on the existing literatures, Nohel et al., (1998) and Grullon et al., (2004) showed that capital expenditures do not increase significantly following repurchases, hence providing support for the free cash flow hypothesis over the information signaling hypothesis. The latter author also showed that the level of cash reserves significantly declines, which also supports the free cash flow hypothesis.

The existing evidence with respect to repurchasing firms' capital expenditures and cash reserves is also limited and inadequate in studying the information content of firms' OMR programs. Hence, the findings of this study on Malaysian repurchases would also aid to build up the existing literatures on OMRs, thereby ascertaining whether the information signaling or the free cash flow theories explain the Malaysian OMR programs.

4. Conclusion

The phenomenal growth in share repurchases as a form of corporate payout and its growing significance has attracted much attention and interest among researchers and findings have been documented on the impacts on corporate security prices and earnings performance in the developed countries such as US, UK and Canada (Masulis, 1980; Dann, 1981; Vermaelen, 1981 and 1984; Lakonishok and Vermaelen, 1996; Comment and Jarrell, 1991; Ikenberry et al. 1995 and 2000; Grullon et al., 2004; and Lie 2005), Lim et al. (2002) and Mohamed et al. (2001) and Abdul Latif et al. (2013).

Unfortunately, most of the share repurchase studies in Malaysia are based on small sample size and short-time period of analysis since share repurchase was only initiated in 1997 and that as mentioned earlier, the buyback mechanism did not catch on until much later. Now that two decades have passed, it would be a substantive attempt to study share repurchase issues on a longer time frame to substantiate further the economic motivations behind OMRs.

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