Buybacks eat into equity float

Since 2016, ₹1.3 trillion worth of fresh equity has been issued while ₹1.1 trillion has been repurchased

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Share buybacks in the domestic market have skyrocketed in the past three years, following the increase in dividend tax and impetus from government disinvestment.

This has been to the extent that they are beginning to eat into the domestic equity float. Since 2016, shares worth ₹1.1 trillion have been extinguished through share repurchase programmes. This is 85 per cent of the new equity paper that has entered the market during the same period.

Around ₹1.3 trillion worth of fresh equity paper was issued in the past three years through rights offerings, qualified institutional placements (QIPs), and initial public offerings (only fresh issuance considered).

The shares extinguished through buybacks are still a miniscule portion of India's total market capitalisation of ₹145 trillion. However, experts say the trend of buybacks offsetting new shares entering the market is worrying.

Even the capital markets regulator has taken a note of this issue. In a speech last year, Securities and Exchange Board of India (Sebi) chairman Ajay Tyagi had expressed concerns over the high amount of share buybacks relative to fresh capital raising in the domestic market. "More money is being returned to investors against money raised," he had said in September 2017 at an industry event.

Market participants say the levying of additional tax on dividend income, buybacks by software exporters, and use of repurchase as a disinvestment tool by the government are reasons behind the sharp spurt in buybacks.

"The government is getting PSUs to do a buyback instead of selling shares in the market for disinvestment. The technology players are also seeing a lot of value in returning money to shareholders. Buybacks have become more tax efficient compared to dividends," said Ajay Saraf, executive director of ICICI Securities.

A buyback is a process by which a company repurchases its own shares from its stakeholders. The shares repurchased are extinguished, resulting in a smaller equity base.

Effective 2016-17, the government started levying an additional 10 per cent tax on dividend income at the hands of recipients. The move saw a lot of companies reward their shareholders, including promoters, through buybacks instead of dividends.

"Volatility and overall fall in markets have made buyback attractive for companies as a means for rewarding shareholders in addition to regular dividends. Further many promoters and large HNI investors are preferring buybacks due to better tax treatment," said Pranajal Srivastava, independent capital markets professional.

Moreover, there has been a lot of shareholder pressure on technology services companies to return cash to shareholders, said market participants.

The share repurchase of TCS, the largest IT company by market capitalisation and revenue, which concluded in September 2018 was the biggest in the past two decades. The IT major repurchased shares worth ₹160 billion. TCS had repurchased shares worth the same amount in 2017.

Infosys, Wipro, Mphasis, Nucleus Software, HCL Technologies and Mindtree are some other companies to have bought back shares in the last three years.

Experts said buyback is the most tax-efficient method of rewarding the shareholder. Those companies which have substantial cash balances, and have no plans of organic or inorganic growth and want to pay shareholders are the ones who typically come with a buyback, market participants said. And the trend of buybacks will continue in 2019 as well.

SHARP RISE

Equity shares extinguished through the buyback route have almost offset new issuances

in ₹ bn	Fresh equity issued*	Shares extinguished via buyback
2016	158	279
2017	744	553
2018	414	288
Total	1,316	1,120

Note: *includes IPOs (only fresh component), QIPs and rights offerings Source: Prime Database