Biderman on Markets: Does the $93 Billion of Bank New Stock Buybacks Mean the Corporate Buying Slowdown is Reversing?

July 11 , 2017

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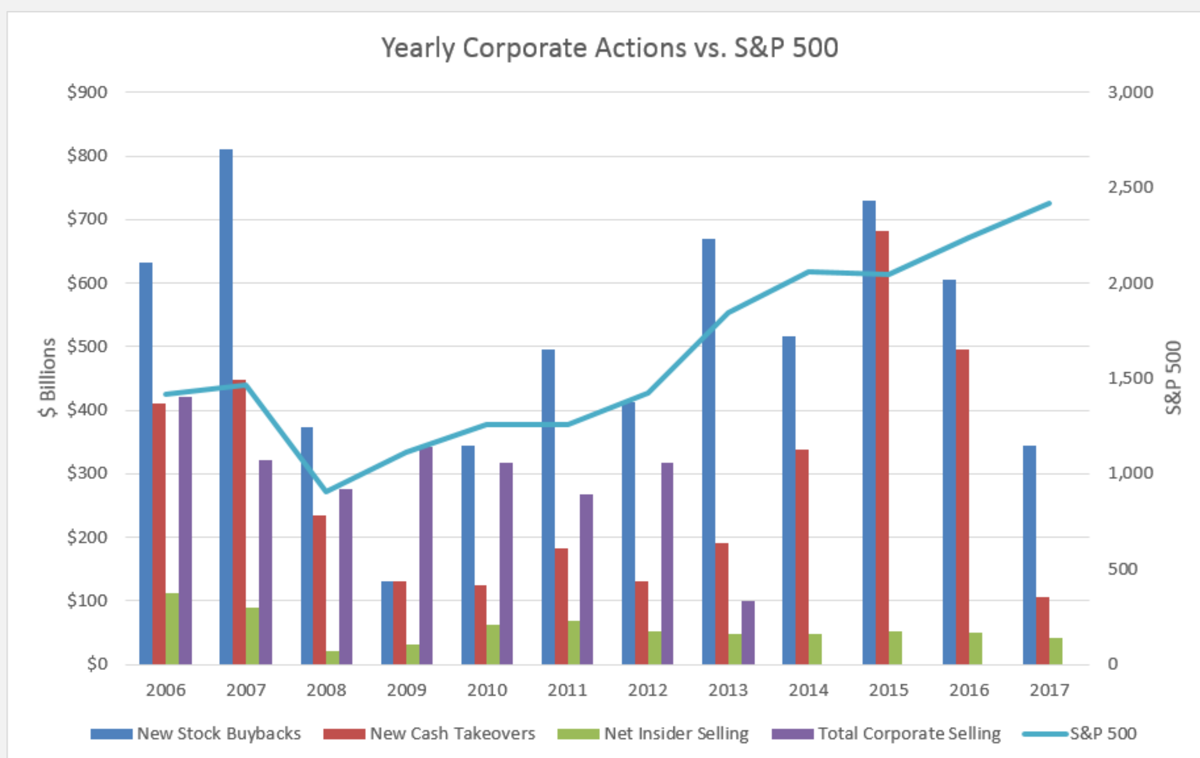
US banks announced a record $93 billion of stock buybacks on June 28 after the Fed reported that virtually all US banks passed the “stress test”. Prior to that deluge there had been only $8 billion of new stock buybacks announced in June and that meager amount would have been the smallest month in several years.

The pace of new stock buyback announcements had been steadily slowing since the 2015 peak, down by more than 20% in 2016 and just under 20% so far this year before the bank spike.

Not only are buybacks slumping but newly announced cash takeovers of already public companies are down by over 40% this year compared with overall 2016 pace. And again the 2016 pace was down by about 25% from the 2015 peak.



Source: Informa Trim Tabs Investment Research

So, does the big spike in buybacks sourced by the Fed approving almost all US banks stress tests mean that the slump in corporate buying is reversing? I do not think so.

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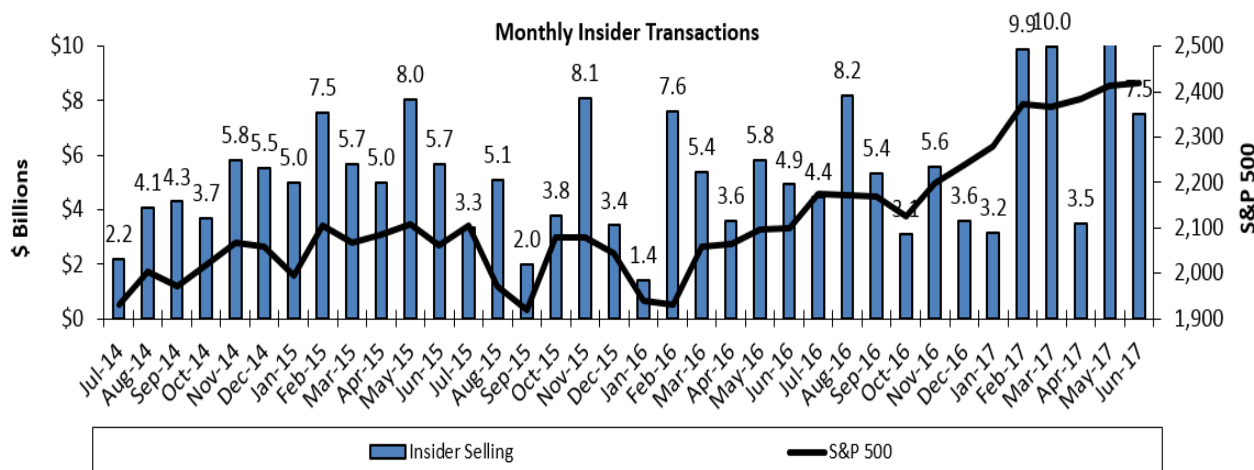
Why Not?

Three reasons:

First, overall stock prices could have gotten so high that companies are reluctant to use cash to reduce share count.

Second, to buttress the first point, net insider selling (all insider selling minus all insider buying) is running 40% faster than the pace of previous years. Insiders are selling monthly an average of $7 billion more shares than they are buying so far this year compared with $4 billion per month in 2016.

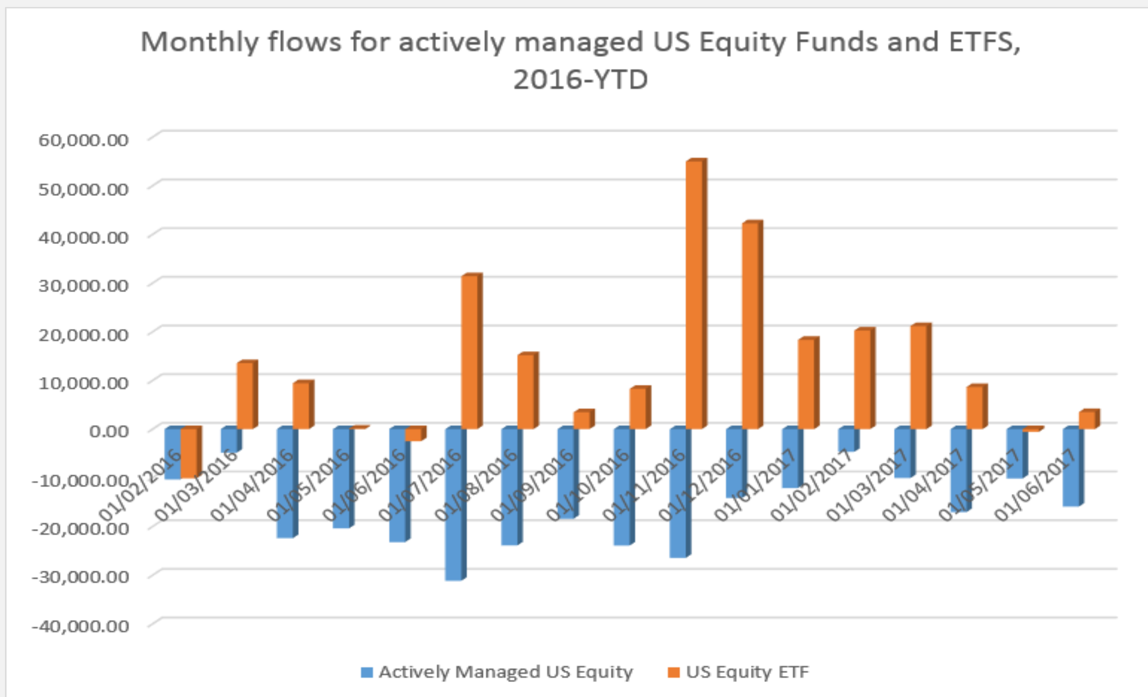
To be sure, insiders historically always have sold more than they buy. Why? Many insiders, particularly here in the US, receive stock grants as part of their compensation and those shares get sold sooner or later. However, when insider selling spikes to many times the recent pace, that is of obvious concern when it happens at the same time as corporate buying slumps.



Source: Informa Trim Tabs Investment Research

Third, perhaps corporate managements are losing interest in new buybacks for performance reasons? Several recent research reports have commented that buybacks have not been working as well as they have in prior years in terms of boosting stock price. Therefore, why borrow to reduce share count when that is not having the desired impact?

Why is the slump in corporate buying so important? Since the end of 2011 the overall US stock market capitalization has risen by about $10 trillion. But, over that same time frame, there has been on net, no new money flowing into US equity ETFs and US equity mutual funds combined. Yes, US equity ETFs have seen healthy inflows, but US equity mutual funds have had outflows roughly equal to the ETF inflows, netting both to virtually zero.



Source: EPFR, Informa Financial Intelligence

Over that same time frame companies have reduced the total share count by over $3 trillion as a result of buybacks and cash takeovers topping all new share sales by both companies and insiders.

Besides the $3 trillion in net corporate buying the Federal Reserve, the ECB and the Bank of Japan have all printed new money some of which has flowed into equities.

In other words, stocks always go up in aggregate when more money chases fewer shares. The more money came from the $3 trillion given to shareholders by companies who either reduced their own share count or used cash to buy already public US companies. In addition some of the trillions printed by the central banks for the purpose of buying financial assets also added to the more money. Fewer shares came about by the same share reduction that generated more cash.

The $3 trillion from share reduction plus an unknown amount financed by central banks explains why the US stock market is up by about $10 trillion in market cap since the end of 2011.

Bottom line:

The ability of stock prices to keep climbing is in major danger if the two sources of new money for the stock market, net corporate buying and central bank money printing, are both likely to slow.

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Charles Biderman is founder of Informa TrimTabs, an Informa Financial Intelligence business. Charles' market insights are widely cited in financial media including Barron's, Associated Press, Bloomberg, Thomson Reuters, the Financial Times, Forbes, Wall Street Journal and others. Charles can also be seen regularly on CNBC's Santelli Exchange, typically discussing what supply and demand data tells us about today's stock market.

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