Analysis of Motivation and Financial Effects of Stock Repurchase by Listed Companies Based on Tencent Holdings

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Abstract. With the gradual improvement of various systems in China's securities market, the advantages of stock buybacks have emerged, and the research object of this paper is the stock buyback event of Tencent Holdings in 2022. Through a comparative study of the financial data of Tencent Holdings, it is found that the motivation of Tencent Holdings' share repurchase includes (mainly potential motivation) the following, i.e., to improve the stock price, to improve the earnings per share, to optimize the capital structure of the enterprise, and to make full use of the cash flow. Tencent Holdings attempts to signal to investors that the company's share price is severely undervalued through share repurchases, attracting the attention of market investors, stabilizing and enhancing the share price, and increasing the overall market value of the enterprise. After analyzing the relevant financial indicators, this paper finds that share buybacks have no impact on Tencent Holdings' good solvency and profitability, which can enhance its operating capacity, and have not affected its shareholding structure. Against this background, this paper focuses on the motivation of Tencent Holdings' large-scale share buybacks on the Hong Kong Stock Exchange, as well as the chain reaction after the buybacks, and whether it can bring a positive financial effect to the enterprise is of significant significance to the maintenance of the listed company's market capitalization.

Keywords: Tencent Holdings; Stock buyback; Buyback motivation; financial effect.

1. Introduction

1.1. Background and Objective

Stock repurchase refers to the use of cash or other means by a listed company to purchase its issued and outstanding shares from the stock market. Stock repurchase originated in the U.S., the U.S. securities repurchase system, on the one hand, greatly enhanced the return of investors, on the other hand, strengthened the price discovery function of the securities market, and in many market fluctuations for the stabilization of the market has played an important role. Compared with the United States, China's stock repurchase started later, the early introduction of stock repurchase means the consideration of the equity distribution reform, in the domestic capital market gradually developed and matured, and enterprises also pay more attention to the use of the means. However, due to China's lack of experience in stock repurchasing, and the development of the domestic financial market being too short, the relevant laws and regulations were temporarily unable to meet the requirements of the market development, before 2005, listed companies were in principle not allowed to repurchase their shares, to January 2019, the policy has been clear support for listed companies to actively implement the share repurchase. Therefore, this paper will take the annual report data published by Tencent Holdings and the information published on the financial website as the basis for analysis, and conduct an in-depth study on the motivation of Tencent Holdings' stock repurchase and the impact of stock repurchase on the enterprise's financial indexes and stock price, to arrive at the complete motivation for stock repurchase, and to determine whether the stock repurchase can effectively optimize the company's stock price and the various financial indicators, and provide more feasible and practical solutions for the subsequent development of China's listed companies. It also determines whether stock repurchase can effectively optimize the company's stock price and various financial indicators, to provide more feasible suggestions for the subsequent development of Chinese-listed companies.

1.2. Structure and Methodology

1.2.1. Content

This paper focuses on the real motivation of Tencent Holdings to implement share buybacks and the financial effects that buybacks will have on the company. The introduction introduces the background of the research on stock buybacks, the purpose and significance of the research, the literature review, research ideas, and research methods. Next, it gives a brief introduction of Tencent Holdings' basic situation and business condition and summarizes Tencent Holdings' share repurchase situation through four perspectives: repurchase program, information disclosure, repurchase process, and repurchase results. The motivation for repurchase is mainly analyzed from the aspects of external repurchase motivation and potential repurchase motivation; the financial effect analysis will study the impact of Tencent Holdings' stock repurchase on the financial indicators and stock price, in which the impact on the financial indicators will be analyzed from the four aspects of operating capacity, growth capacity, solvency and profitability in comparison with other enterprises in the same industry; and finally, the research conclusions of the Tencent Holdings' share buyback are summarized, combined with the results of this case study. Finally, we summarize the conclusions of Tencent Holdings' stock buyback and combine the conclusions and inspirations of this case study to give better suggestions for the implementation of stock buyback by listed companies in China.

1.2.2. Research method

Case study method. This paper selects the 2022 Tencent Holdings stock repurchase as the research object and analyzes the motivation for stock repurchase and the financial effects caused in depth. Tencent Holdings is a group that is a leading provider of Internet services and mobile value-added services in China and owns the largest real-time communication community in China. The Group currently has three main businesses: Internet value-added services, mobile and telecommunications value-added services and online advertising. The data in this article is sourced from public reports in the stock market, which are legally binding, accurate and reliable. By analyzing Tencent Holdings' various financial reports and underlying information, we objectively analyze whether the buyback has achieved its intended purpose and provide a reference for other listed companies to carry out share buybacks.

1.3. Literature Review and Grounded Theory of Stock Buybacks

1.3.1. Literature review

In the study of stock repurchase motivation, foreign scholars from different perspectives on the motivation of stock repurchase found that the motivation of repurchase is diversified, and with the continuous development of the securities market, the motivation of repurchase is still increasing.

Based on the signaling theory, scholars have drawn their conclusions through the study of stock repurchases in different periods. Li and Nally studied the stock repurchase events in the Canadian market, and the results show that if the stock price of listed companies continues to be low, then managers are more likely to carry out stock repurchases in the hope of sending a signal to the stock market that the stock price is undervalued [1]. Lee et al. found that listed companies issuing cash to the public are more likely to buy back the shares of the company. They found that cash dividends or share repurchases by listed companies are two different positive signals to outside investors. Paying cash dividends indicates that the company's capital flow is sufficient, and implementing stock buybacks indicates that the company's share price is undervalued [2].

Based on the principal-agent theory, foreign scholars focus on the free cash flow of listed companies that implement stock buybacks. Stephens and Weisbach found that listed companies with sufficient free cash flow are more willing to implement stock buybacks to reduce the company's liquidity and reduce the cost of principal-agent and that the scale of stock buybacks is positively correlated with the company's free cash flow [3]. Dittmar analyzed and found that the implementation of stock buybacks by listed companies can circumvent excessive idle capital costs [4]. Almeida et al. found through their study that listed companies with a large amount of free cash weigh two situations, one is to hire more employees to expand the size of the company, and the other is to use the free cash to implement stock buybacks thereby increasing the market capitalization of the company. Most companies will choose to implement stock buybacks to enhance the overall value of the company [5].

Based on the financial efficiency theory, foreign scholars mainly focus on whether stock buybacks will have an impact on the financial leverage of listed companies. Opler and Titman concluded that companies can implement stock buybacks to achieve the optimal financial leverage ratio [6]. Bonaimé AA found that listed companies can adjust and optimize the capital structure and achieve the optimal level of financial leverage by using share buybacks. Capital structure to achieve the optimal level of financial leverage [7]. Campbell and Johnson studied the real motivation of listed companies to implement stock buybacks through case studies and found that at the same time, with the continuous development of the securities market, more and more motivation hypotheses will appear [8]. Wen, categorizing the motivation of stock repurchase in China between 2005 and 2015, found that not all of the real repurchase motives of listed companies were reflected in the Company Law, such as the release of pledge financing and the repurchase of foreign shares [9]. Wu and Yu synthesized and analyzed the motives of stock buybacks through case studies, such as improving earnings per share, enhancing investor confidence, improving share price, improving financial leverage, implementing equity incentives, and reducing idle funds [10, 11].

Motivation theories common to stock buybacks include signaling theory, principal-agent theory, and financial leverage theory and so on. The capital market in foreign countries is more developed, and the theory of wealth transfer as well as the financial flexibility hypothesis has been effectively argued. China's securities market has its own characteristics, and the motivation of domestic listed companies to implement share repurchase also includes the reduction of state-owned shares, improve the shareholding structure, cooperation with the shareholding reform, and realize surplus management. Research on the market effect and financial effect of share repurchase, in the market effect of share repurchase, research scholars generally believe that in the short term, there is a more significant market effect, the long-term effect is not obvious; in the financial effect, research scholars believe that the share repurchase will be in the profitability, debt servicing and other aspects of some of the optimization brought about by the role of the share repurchase, but there is also manipulation of share prices and other issues. This study mainly focuses on the motivation for share repurchase, as well as the implementation of the shares of the company's financial operations after the implementation of the impact of the analysis, the utility of the share repurchase depends more on the listed company's capital operation whether to achieve the purpose of improving the financial situation, the comprehensive use of its own funds and the issuance of debt to obtain funds, so that the listed company to achieve the optimal asset-liability ratio.

1.3.2. Fundamental theory

(1) Signaling Theory

The signaling theory in stock repurchase suggests that stock repurchase is an alternative form of cash dividend. With the continuous development of the securities market and the gradual relaxation of regulatory constraints on stock buybacks, more and more listed companies implement stock buybacks to enhance share price performance. When a listed company releases the news of implementing stock repurchase, it indicates that the management believes that the company's current stock price is undervalued. When investors receive the signal of repurchase, they know that the company's stock price is on the low side, and they can realize the value-address of their assets by buying the stock at a low price on the day of the announcement.

(2) Principal-Agent Theory

The principal-agent theory suggests that due to the separation of ownership and operation of a company, the actions of managers may deviate from the goals of the company's shareholders. When the company has enough free cash, the manager may consume the cash to satisfy his desires or engage in high-risk and low-return investment projects without taking any risk himself, which will ultimately infringe on the interests of shareholders. Implementing share repurchases with own funds can reduce the company's free cash, lower the agency cost, and safeguard shareholders' interests. Through the implementation of the equity incentive program, part of the manager's income is linked to the company's share price, prompting managers to improve operational efficiency, increase the overall value of the company, and effectively serve shareholders.

(3) Theory of financial effect

The implementation of stock buybacks will lead to changes in the company's equity and debt-to-total assets ratio. According to the theory of taxable MM, before reaching the optimal debt ratio, increasing the debt ratio can play the role of a tax shield, and tax avoidance improves the value of the company. After the company implemented the stock repurchase with its own funds, the company's owner's equity decreased and the debt ratio increased, the company's capital structure could be improved, reducing the weighted average cost of capital and increasing the value of the company. However, in the process of repurchasing the outstanding shares, the reduction of free cash flow may affect the short-term solvency and improve the financial risk.

2. Introduction of Tencent Holdings' Stock Buyback Case

2.1. Overview of Tencent Holdings (Tencent Group Overview)

2.1.1. Company Profile

Founded in November 1998, Tencent is currently one of China's largest integrated Internet service providers and one of the Internet enterprises serving the largest number of users in China. Since its establishment more than 15 years ago, Tencent has been adhering to the business philosophy that everything is based on user value and has always been in a state of steady and high-speed development. on June 16, 2004, Tencent was publicly listed on the main board of the Hong Kong Stock Exchange (stock code 700) It is Tencent's mission to enhance the quality of human life with the advanced technology of the Internet.

2.1.2. Company operation

The main businesses of Tencent Holdings are communications and social networking, online games, digital content, online advertising, financial technology, cloud, and other corporate services, which can be categorized into value-added services, financial technology and corporate services, and online advertising (Table 1).

Table 1. Tencent's main business revenue.

Tencent business situation	2020	2021	2022	2023
value-added service	2642	2916	2876	2984
FinTech & Corporate Services	1281	1722	1771	2038
online advertising	822.17	886.66	827.29	1015
other	74.95	76.85	71.94	53.95
Total operating income (in billions)	4821	5601	5546	6090

2.2. Tencent Holdings' Share Buyback Program and Results

2.2.1. Tencent Holdings' share repurchase program

Press release dated 27 June 2022 from Prosus (which is majority-owned by Naspers) and Nasprs, the substantial shareholders of Tencent Holdings, about the commencement of a long-term, open-ended repurchase program by Prosus and Naspers of shares in their respective share capitals from the respective public shareholders of Prosus and Naspers, and the raising of funds for the repurchase program in an orderly manner by way of on-market offer of the Company's shares held by the Naspers Group. The funds for the repurchase program will be raised in an orderly manner by way of an on-market offer of the Company's shares held by the Naspers Group. According to the press release, the Naspers Group expects that the number of shares of the Company to be sold each day will be a small percentage of the average daily trading volume of the Company's shares. For example, if the Naspers Group had executed the repurchase program in the past three months in compliance with the European regulatory restrictions, the number of the Company's Shares sold per day would not have exceeded, on average, approximately 3-5% of the average daily trading volume of the Company's Shares.

2.2.2. Results of Tencent Holdings' Share Repurchases

Statistics show that Tencent Holdings ranked first with a repurchase amount of HK$9,825 million.2024 In the first two months of February Tencent Holdings has repurchased shares a total of 13 times, repurchasing a total of 34.11 million shares, with a repurchase amount of HK$9,825 million. During the period, the company repurchased the lowest price of 274.61 Hong Kong dollars/shares and the highest price of 299.71 Hong Kong dollars/shares. 2023 the same period, the company during the period of the number of repurchases, the amount of repurchases was 7,853,100 shares, respectively, 2,874 million Hong Kong dollars.

3. Analysis of the Motivation of Stock Repurchase of Tencent Holdings

3.1. Analysis of the External Motivation of Stock Repurchase of Tencent Holdings

3.1.1. Investor preferences

In Hong Kong Stock investment, investors prefer enterprises with good development prospects, strong capital, and large industrial scale. Among them, the banking and financial investment industry, state enterprises, energy enterprises, and Internet technology enterprises are particularly prominent, and Hong Kong investors' favorite stocks are usually determined by comparing the value of Hong Kong Stock Connect's stock market. Up to January 3, 2024, the top five shares held by Hong Kong Stock Connect were Tencent Holdings (HK $264 billion), China Mobile (HK $142.9 billion), China National Offshore Oil (HK $111.7 billion), HSBC Holdings (HK $110.7 billion) and China Construction Bank (HK $89.8 billion). Therefore, Tencent Holdings has become the most popular stock for Hong Kong investors with its high stock market value.

3.1.2. Continued volatility in the stock market

Tencent's stock price increases and decreases staggered. For example, on August 26, 2022, the price of the shares was HK $307.918 per share, and the number of shares traded on that day was 79,374,000. After that, the price of the shares was HK $312.097 on September 2, the number of shares traded on that day was 102,068,000. But on September 9th the share price fell to HK $291.582 per share, the number of shares traded on that day was 92,520,000. According to the data, when the market mood is pessimistic, the daily trading volume of stocks will fall, and investors may hesitate to make decisions. But when the mood is positive, daily trading of stocks will rise, and investors may be inclined to chase the rally.

3.2. Analysis of the Potential Motivation of Stock Repurchase of Tencent Holdings

3.2.1. Raise stock prices

Stock repurchases of listed companies can reduce total share capital, to achieve the purpose of raising the stock price as a whole. As shown in Table 2, the stock repurchase amount and stock price of Tencent in late August 2022.

Table 2. Statistics of share repurchase amount and share price of Tencent

Date	Total repurchase amount (RMB 100 million)	Stock Price (HK $)
2022.08.22	3.5	295.001
2022.08.23	3.5	297.001
2022.08.24	3.5	294.431
2022.08.25	3.5	308.678
2022.08.26	3.5	307.918
2022.08.29	3.5	306.778
2022.08.30	3.5	307.438
2022.08.31	3.5	310.767

3.2.2. Increase earnings per share

Share buybacks of listed companies reduce total equity and boost earnings per share, thus giving the company's shares more purchasing power. For example, Tencent repurchased about 10.5 billion RMB of shares in September 2022, with an average repurchase price of about 300 RMB per share. Tencent had a market capitalization of about 3 trillion RMB at the end of September 2022, leading to a theoretical increase in earnings per share of 0.35 percent.

3.2.3. Optimize the capital structure of enterprises

The capital structure of enterprises is formed by various financing methods adopted by enterprises to raise funds, and the combination types of various financing methods determine the capital structure of enterprises and their changes. The proper use of debt can help reduce the cost of capital and gain financial leverage benefits, but transition debt creates financial risks. Generally speaking, the problem of capital structure is actually a problem of the proportion of debt capital. Reasonable debt can improve the interests of the company and shareholders, oppositely, it will increase the risk of bankruptcy.

3.2.4. Make good use of cash flow

Enterprises can use cash flow analysis to find a balance between reducing risks and increasing returns and achieve the goal of optimal capital utilization. Cash flow analysis enables the enterprise managers to have a clear understanding of the financial situation of the enterprise to discover financial problems that may be overlooked in daily operations, predict the future financial development of the enterprise and effectively adjust or change the current business strategy according to the predicted situation. It is very important to analyze the cash flow, whether it is the enterprise operator or the enterprise investor. Especially for modern enterprises, cash flow analysis, which directly affects the survival and development of enterprises, plays an important role in enterprise management.

4. Financial Effect Analysis of Stock Repurchase of Tencent Holdings

4.1. Impact of Stock Repurchase on Operating Capacity

Hong Kong stocks stipulate that shares bought back by listed companies must be canceled. Therefore, shares bought back by Tencent cannot directly use equity incentives, but reward employees in the form of new shares issued. In this way, it can improve the enthusiasm of employees, attract more talent and improve the operation ability of the company.

Table 3. Statistics of share awards granted by Tencent in recent ten years

Years	Number of share awards (ten thousand shares)
2014	3252
2015	7430.9
2016	5237.1
2017	1907.2
2018	2094
2019	5309.7
2020	3729.7
2021	7705.5
2022	6517.5
2023	6460.4

4.2. The Influence of Stock Repurchase on the Growth Ability of the Company

Company stock repurchases can reduce the agency cost of the company. Stock repurchase can improve the earnings per share of the company's stock, thus making the company's stock more attractive and establishing a good corporate image in the stock market. Increase their value in the minds of investors and attract them to invest.

According to Tencent Holdings' third-quarter financial report released in 2022, the company's revenue in the third quarter was 140.1 billion RMB, including a net profit of 39.94 billion RMB. A year-on-year increase of 1%, and a net profit of 32.25 billion RMB under non-international financial reporting standards, a year-on-year increase of 2%.

Table 4. Statistics of partial stock repurchase at the end of the third quarter of Tencent in 2022.

Date	Total repurchase amount (RMB 100 million)
2022.09.16	3.5
2022.09.17	3.5
2022.09.18	3.5
2022.09.19	3.5
2022.09.20	3.5
2022.09.21	3.5
2022.09.22	3.5
2022.09.23	3.5
2022.09.24	3.5
2022.09.25	3.5
2022.09.26	3.5
2022.09.27	3.5
2022.09.28	3.5
2022.09.29	3.5
2022.09.30	3.5

5. Conclusion

By continuing to buy back the company's shares, Tencent is sending a signal to the market that it is confident in the company's future development and is willing to demonstrate its recognition and support of the company's value by buying back shares. At the same time, large buybacks also indicate that these companies have sufficient cash flow and financial strength to invest and return to shareholders.

This paper puts forward the following suggestions in response to the findings of the case study: companies need to clarify the purpose of share repurchases in light of their circumstances before conducting share repurchases, and managers should make professional judgments about future uncertainties and risks; securities regulators should establish and improve standards for evaluating disclosure of information, and require listed companies to disclose all important information related to share repurchases promptly by the relevant regulations; and investors need to learn to correctly interpret the share repurchase announcements by listed companies reasonably predict market changes and make rational investment decisions.

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