Stock Market Anomalies: What Can We Learn From Repurchases and Insider Trading?

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In this paper, we examine whether managers’ trading decisions (both at a firm and personal level) are correlated with trading strategies suggested by the operating accruals anomaly and the post-earnings announcement drift (also known as the standardized unexpected earnings, or SUE) anomaly.

The use of managerial trading activity to infer managers’ private valuation about their own securities is a unique feature of this research design and we discuss advantage and disadvantage of this approach in the paper.

We argue that if managers are skilled at identifying equity mispricing and an anomaly accurately captures situations where stock prices deviate from firms’ fundamental value, then managers’ marginal trading decisions through repurchase programs and on personal accounts will be correlated with the anomaly trading strategy. On the other hand, restrictions on the managers’ ability to take advantage of temporary mispricing due to insider trading restrictions, prohibitive trading costs or risk associated with trading strategy may render the interpretation of null results inconclusive.

We provide corroborative evidence for the accruals anomaly — that is, managers’ repurchase and insider trading behavior varies consistently with the information underlying the operating accruals trading strategy. Low (high) accruals firms repurchase more (less) shares, and managers of low (high) accruals firms buy more (less) shares on their personal accounts.

On the other hand, we do not find corroborative evidence for the SUE anomaly, suggesting that trading on information embedded in SUE is costlier to managers than trading on information embedded in accruals.
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