Empirical Survey on Benefits of Stock Splits in India

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Abstract:
A stock split is a decision by company's board of directors to increase number of outstanding shares of the company without changing shareholders equity but by changing face value of equity shares. An empirical survey was carried out on 55 respondents. It was inferred from the analysis that the stock split conveys positive signal about the company in the market. It helps the company to create a positive impact in the market; the continuous splitting of stocks is not advisable for the company. Stock splits made by the company are beneficial to the stockholders in the way that the stock splits add value to the shares of the common investor. The stock splits help the companies to bring down the share prices to medium range so that the common investor can easily trade with those shares.

Keywords: *Stock Split, Shares of the Company, Shareholders, Equity*

1. Introduction

A stock split increases the number of shares outstanding by reducing the face value of equity shares, without affecting the equity. It must be noted that stock splits is different from stock dividend and bonus issues. In case of stock dividend equity share capital of company increases and there is no actual cash outflow.

Some studies suggest that stock splits are done by managers to communicate positive information about future prospects of their company. This hypothesis is termed as signalling hypothesis or information hypothesis. It was first offered by Fama, Fisher, Jenson and Roll (1969).It was later encouraged by researchers like Brennan and Copeland (1988), McNichols and Dravid (1990), and Brennan and Hughes (1991).

Lakonishok and Lev (1987) analyzed corporate performances by examining earnings growth and cash dividend growth. They constructed a sample of splitting companies and a control sample with matching companies with same industry code, similar asset size and used chi-square test to test differences in growth rates. They found that splitting companies exhibited higher growth in earnings and dividends than control companies after split announcement. They also found three to four percent abnormal share price return around announcement day.

Angel et al.(1997), Pilotte and Manuel (1996), and Pilotte (1997) were some of the scholars who studied multiple splits after first stock split. Pilotte and Manual (1996) concluded that market reaction to subsequent splits was smaller than the reaction to first split announcement.

Baker and Gallagher (1980), Lakonishov and Lev (1987), and Lamoureux and Poon (1987) were of opinion that executives utilized stock split as an instrument to increase their shareholder base which makes it tougher for probable acquirers to control. Baker and Gallagher (1980) after interviewing Chief Financial Officers reported that majority of them were of opinion that stock splits are done to attain optimal trading price range which improves liquidity. They also stated that small investors buy at lower share prices and do not like to invest their money when share prices are high. A stock split according to them broadens ownership base of investors.

Dravid (1987), Lakonishok and Lev (1987), Conroy et al. (1990), Dubofskey (1991),Muscarella and Vetsuypens (1996)using American Depositary Receipts, Desai et al.(1998) and Koski (1998) noted an increase in share turnover after stock splits.

The need to conduct a study on stock splits arises because existing empirical researches have prompted a series of debates regarding significance and role of stock splits. The present study discusses the results of the empirical analysis conducted in relation to stock splits.

2. Objectives of the study

The current study aims at studying the behaviour of share prices around stock splits.The research objectives framed and the research issues examined by the survey are:

1. To investigate the effect of stock splits on share prices.
2. To consider how the stock splits add value to theorganization.
3. To examine how the stock splits help the common investor.

3. Research hypotheses

To attain research objectives of the current study (restricted to India) following research hypotheses are developed:

HYP: 1-Stock split conveys a positive signal to the marketabout the company.
HYP: 2-Multiple stock splits are advisable for the company.
HYP: 3-Stock splits add value to the share of the ordinaryinvestor.
HYP: 4-Stock splits increase the value to the companyand help in increasing its market capitalization.

4. Rationale of Research Hypotheses

The hypotheses relating to share prices try to analyze the behaviour of share prices around stock splits by carrying out a survey in which respondents are the corporate professionals, CEOs, and Managers of the different companies who have announced the Stock split.The survey is conducted to establish the opinion about Stock splits by interviewing the professionals who are responsible for taking a decision for the announcement of stock splits.

5. Research methodology

To test the hypotheses enumerated above following research methodology has been designed.

a. For conducting this study, data was collected from the primary sources (data collected directly from the respondents with the help of a self-administered questionnaire).
b. The study was conducted in various cities of India, viz., Delhi, Mumbai, Gurgaon and Faridabad. The following discussion relates to the sampling process: sample size, characteristics, research setting and sampling technique. Questionnaires were distributed to 55 respondents. Of these 35 usable questionnaires were collected indicating a response rate of 64% approximately.

Respondents included in the sample were selected to meet specific criteria like:

1. They should be a professional or any other person working on a managerial post and

directly involved in decision–making relating to the announcement of stock splits.
2. They could be male or female.
3. They should be willing to participate.

Non-probability method of sampling was used along with quota and convenience sampling methods. The questionnaires were administered both in person as well as through personalised e-mails with attached questionnaire in HTML format, which could be filled and submitted online to the researcher. Respondents were assured of their anonymity throughout the conduct of the research. Respondents were approached in corporate offices and banks with the questionnaires for data collection. Those respondents to whom the questionnaires were mailed were requested via phone call also to participate in the survey. To increase the response rate, the respondents were repeatedly reminded to complete the questionnaire.

6. Sample Description

From the following table can observe that about 48.6% of the respondents belonged to 22 – 24 years age group. Following bar chart also shows the same.

Age

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	17	48.6	48.6	48.6
25 – 34	7	20.0	20.0	68.6
35 – 40	6	17.1	17.1	85.7
40 - 60	5	14.3	14.3	100.0
Total	35	100.0	100.0	

From the following table we can observe that about 71.4% of the respondents were males.

Gender

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	25	71.4	71.4	71.4
Female	10	28.6	28.6	100.0
Total	35	100.0	100.0	

From the following table we can observe that about 45.7% of the respondents were graduates.

Qualification

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Graduate	16	45.7	45.7	45.7
	Post-graduate	7	20.0	20.0	65.7
	Masters	8	22.9	22.9	88.6
	Other	4	11.4	11.4	100.0
Total		35	100.0	100.0	

From the following table we can observe that about 54.3%of the respondents answered that their organization is a large organization with 200 employees or over.

Organization size

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	8	22.9	22.9	22.9
Medium-size organization (60-199 employees)	8	22.9	22.9	45.7
Large-size organization (200 employees or over)	19	54.3	54.3	100.0
Total	35	100.0	100.0	

7. Research Instrument

Data were collected with a help of undisguised questionnaires. The scale items were taken from the previous research work and adapted to make them appropriate to the Indian context. Structured undisguised questionnaire was used for data collection. Five-point Likert-scale anchored at both extremes to 1 (strongly disagree) and 5 (strongly agree) was chosen to represent the degree of consumer responses. Likert-type or frequency scales use fixed choice response formats and are designed to measure attitudes or opinions. These ordinal scales measure levels of agreement/disagreement. Respondents were offered a choice of five pre-coded responses with the neutral point being neither agree nor disagree. Chi- square method was used to analyse the results.

8. Reliability Testing

Reliability is the degree of consistency with which an instrument measures the attribute it is designed to measure. Cronbach's Alpha test was used in the research to test the reliability of the scales used. A Cronbach Alpha coefficient equal or greater than 0.6 indicates that the scale is reliable (Nunnally, 1978). Cronbach's Alpha coefficients for all the scales except recreation orientation, experience orientation and convenience orientation are far above the threshold limit of 0.6 and hence, were found to be highly reliable.

9. Pretesting the Questionnaire

A pretest refers to a trial administration of the questionnaire to determine whether questions and directions are clear to subjects and whether they understand what is required of them. The questionnaire was pretested on 5 respondents meeting the sample criteria. The results of the pre-test were found to be satisfactory enough to continue withthe main survey.

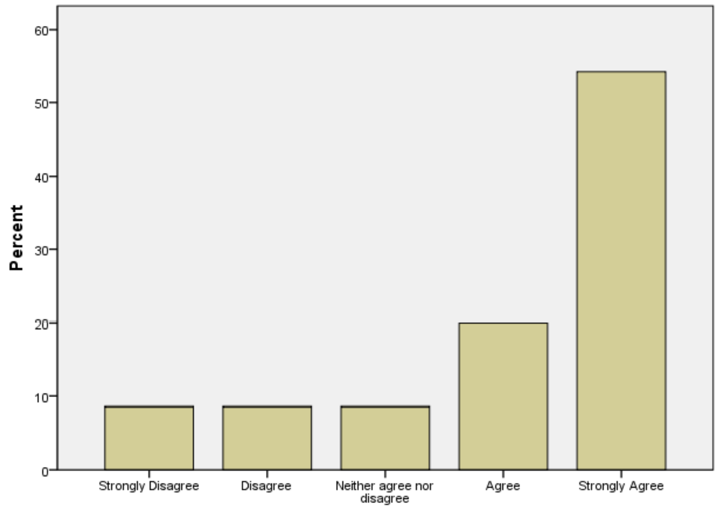
10. Empirical results of the statistical analysis

From the following table we can observe that about 54.3% of the respondents strongly agreed that stock split conveysa positive signal to the market about the company.

Table 1.: Stock split conveys a positive signal to the market about the company.

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	3	8.6	8.6	8.6
Disagree	3	8.6	8.6	17.1
Neither agree nor disagree	3	8.6	8.6	25.7
Agree	7	20.0	20.0	45.7
Strongly Agree	19	54.3	54.3	100.0
Total	35	100.0	100.0	

Stock split conveys a positive signal to the market about the company.

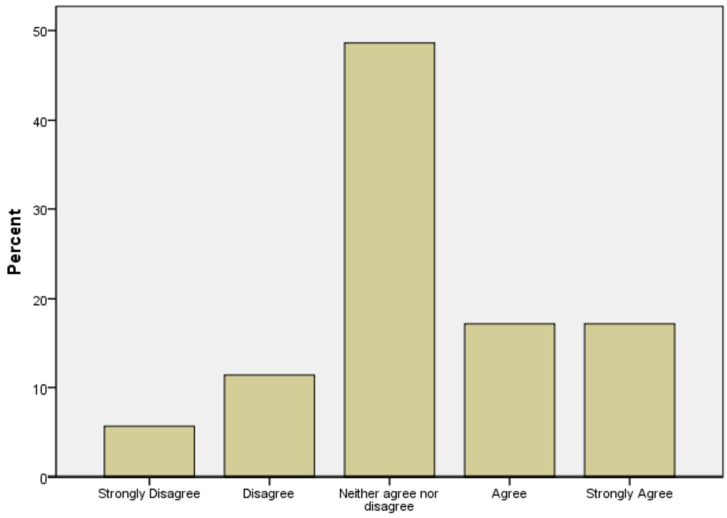


From the following table we can observe that about 48.4% of the respondents neither agreed nor disagreed that multiple stock split is not advisable for the company. Following bar chart also shows the same.

Table 2: Multiple stock split is not advisable for the company

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	5.7	5.7	5.7
	Disagree	4	11.4	11.4	17.1
	Neither agree nor disagree	17	48.6	48.6	65.7
	Agree	6	17.1	17.1	82.9
	Strongly Agree	6	17.1	17.1	100.0
	Total	35	100.0	100.0	

Multiple stock split is not advisable for the company

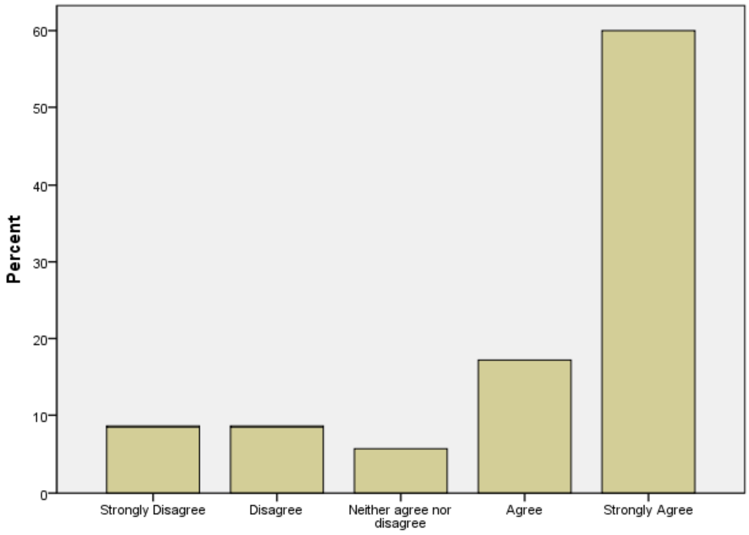


From the following table we can observe that about 60.0% of the respondents strongly agreed that stock splits add value to the share of the common investor. Following bar chart also shows the same.

Table 3: Stock splits add value to the share of the common investor.

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Strongly Disagree	3	8.6	8.6	8.6
Disagree	3	8.6	8.6	17.1
Neither agree nor disagree	2	5.7	5.7	22.9
Agree	6	17.1	17.1	40.0
Strongly Agree	21	60.0	60.0	100.0
Total	35	100.0	100.0	

Stock split add value to the share of the common investor.

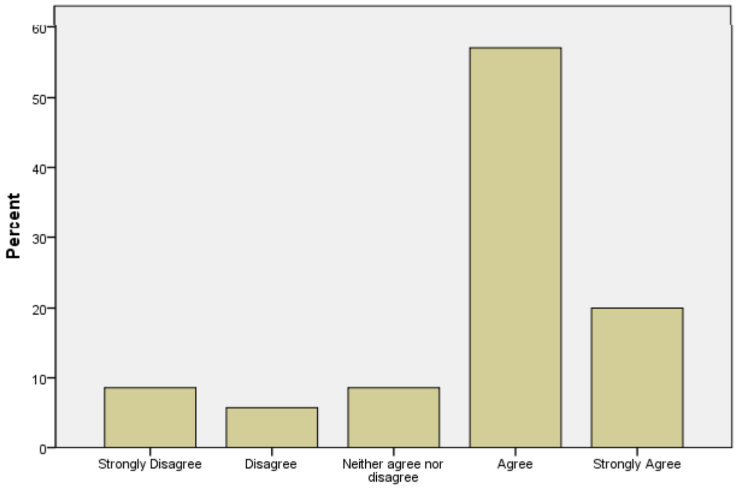


From the following table we can observe that about 57.1% of the respondents agreed that stock splits add value to the company and help in increasing its market capitalization. Following bar chart also shows the same.

Table 5:Stock splits add value to the company and help in increasing its market capitalization.

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Strongly Disagree	3	8.6	8.6	8.6
Disagree	2	5.7	5.7	14.3
Neither agree nor disagree	3	8.6	8.6	22.9
Agree	20	57.1	57.1	80.0
Strongly Agree	7	20.0	20.0	100.0
Total	35	100.0	100.0	

Stock split add value to the company and help in increasing its market capitalization.



11. Interpretations of the Empirical Survey

In this study, almost 36.4 percent of the respondents who participated in the study are in the ages between 25 and 34 years. Around 27.3 percent of the interviewees who participated in the study are in the ages between 35 and 40 years. Around 23.6 percent of the respondents who participated in the study are in the ages between 40 and 60 years. More than half of the total respondents who participated in the study were males, that is, around 54.5 percent of the respondents were males, and 45.5 percent of the respondents were females. Around 47.3 percent of the interviewees who participated in the study were qualified up to masters' degree; around 45.5 percent of the interviewees who took part in the study were qualified up to post graduate degree. This shows that the survey had been done mostly with the highly qualifiedpersons.

Then the respondents who participated in the study were asked about the size of their organization. For that around 49.1 percent of the respondents said that their organizationis a medium sized organization with 60 to 199 employeesand around 34.5 of the respondents who participated in the study stated that their organization is a small size organization with less than 60 employees. This shows that more than 80 percent of the respondents who participated in the study are from the small and medium sized organizations.

When the respondents who participated in the study were asked whether the stock split conveys positive signal about the company in the market, for that around 32.7 percent of the respondents who participated in the study said that they strongly agree that the stock split conveys positive signal about the company in the market. Around 25.5 percent of the respondents who participated in the study said that they agree that the stock split conveys positive message about the company in the market. Thus it is inferred that most of the respondents, that is more than 50 percent of the respondents who participated in the study accept that the stock split conveys positive signal about the company in the market.

When most of the respondents who participated in the study said that the stock expresses positive signal about the company in the market, then they were asked about their opinion for the statement that the multiple stock split is not advisable for a company. For that around 45.5 percent of the respondents who participated in the study said that they strongly agree with the statementthat the multiple stock splits are not advisable for acompany. And 25.5 percent of the respondents who participated in the study said that they agree with the statement that the multiple stock splits are not advisable for a company. That is more than 70 percent of the respondents who participated in the study said that the multiple stock splits are not advisable for a company. Thus it is inferred that any way stock split helps the company to create a positive impact in the market, the continuous splitting of stocks is not advisable for the company.

Once most of the respondents who participated in the study said that the multiple stock splits are not advisable for a company, then the respondents who participated in the study were asked that whether stock splits add value to the share of the ordinary investor. For that, about 41.8 percent of the interviewees who participated in the survey said that they strongly agree that the stock splits add value to the share of the common investor. About 25.5 percent of the respondents who participated in the study said that they agree that the stock splits add value to the share of the common investor. That is more than 60 percent of the respondents who participated in the study accept that the stock splits add value to the share of the common investor. Thus it is understood that the stock splits made by the company are beneficial to the stockholders in the way that the stock splits add value to the shares of the common investor.

Once most of the respondents who participated in the study said that the stock splits add value to the share of the common investor, then they were asked that whether stock split adds value to the company and help in increasing its market capitalization. For that, about 45.5 percent of the respondents who participated in the study said that they strongly agree that the stock split adds value to the company, and also it helps in increasing the market capitalization of the company. About 25.5 percent of the respondents who participated in the study said that they agree that the stock split adds value to the company, and also it helps in increasing the market capitalization of the company. That is, more than 70 percent of the respondents who participated in the study accept that the stock split adds value to the company, and also it helps in increasing the market capitalization of the company. From this, it is inferred that the stock splits made by a company will add value to that company and also with the increasing number of shares in the market it helps in the increase of the capitalization of the company.

12. Conclusion

- The stock split conveys positive signal about the company in the market.
- Stock split helps the company to create a positive impact in the market, the continuous splitting of stocks is not advisable for the company.
- Stock splits made by the company are beneficial to the stockholders in the way that the stock splits add value to the shares of the common investor.
- The stock splits made by a company will add value to that company and also with the increasing number of shares in the market it helps in the increase of the capitalization of the company.
- The stock splits help the companies to bring down the share prices to medium range so that the common investor can easily trade with those shares.

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