

Share splits and share price changes: the case of share splits on the Nairobi Stock Exchange

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Abstract:

Stock splits in stocks of companies listed at the Nairobi Stock exchange market have in the recent years gained importance that cannot be underestimated. This has been brought about by the tremendous increase in stock market activity which has resulted in high priced stocks, leading to illiquidity of stock and reduction in the investment momentum of the split shares on the NSE. Stock splits have greatly contributed to an increase in the affordability of stocks and also led to an increase in the volatility of the split stocks at the NSE. It is not clear whether a share split has a positive or negative impact on share prices and whether it improves the liquidity of shares and market efficiency in general. This study, whose objectives were to find out the effect of stock splits on the market prices and to determine other factors that may influence the prices of stocks, provides information on the effect of stock prices and the policy implications of stock splits. This study employed the Event Study Methodology to examine the effect of share splits on share prices. This methodology has been used by economists to measure the impact of a specific event on the value of the firm. The usefulness of such a methodology came from the fact that, given rationality in the marketplace, the effect of an event is reflected immediately in security prices. Published data on dividends, stock prices and the stock market indices for companies that split their shares were collected from the Nairobi Stock Exchange. The data was analysed using multiple linear regression to estimate the coefficients of the variables used with particular emphasis on the split action variable. The main findings of the study were that the stock split action had a significant positive effect on the market prices of the stocks. The current cash dividends per share relative to current share price, change in dividends per share relative to current price per share, change in the stock market price index and current stock market price index, were found to be insignificant in determining stock prices. The recommendation to the management of listed companies is that if they intend to increase the number of transactions along with the number of shares traded, which increases the volatility of the price series, they might split in order to achieve this objective and also increase total market value of the common stock at that particular time. This, of course, assumes that they are in a position to split their stock and it ignores any costs associated with a split.