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The Impact of Stock Splits on Price and Liquidity on the Stock Exchange of Thailand

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Abstract

This paper explores the impact of stock splits on stock price and various aspects of liquidity using daily and intraday data from the Stock Exchange of Thailand between 2002-2004. We provide evidence that reductions in trade frictions and increases in split-adjusted price levels are associated with the size of split factors and post-split trading range. Stocks with high split factors have better post-split adjusted price performance and lower trade bid-ask spreads and price impact. The empirical findings lend support to the trading range hypothesis of stock splits.

Keywords: Stock splits; Liquidity; Trading range
JEL Classification Codes: G12; G14; G35

1. Introduction

Stock splits remain one of the puzzling anomalies in the behaviour of stock prices and stock liquidity since they are only numeraire changes in stock price denominations that has no impact on investors' fraction of equity ownership. However, previous research has documented positive price performance subsequent to splits. Grinblatt et al. (1984) and Lamoureux and Poon (1987) support the signaling hypothesis that firms use stock splits to signal future positive earnings. The alternative liquidity and trading range hypothesis comes from management claims that the motivation for split activities is to bring stock prices down to a preferred trading range and improve liquidity.[1] Yet existing empirical research, finds that the impact of split on liquidity is mixed. Copeland (1979), Conroy, Harris, and Benet (1990), and Desai et al (1998), find that bid-ask spreads, increase, indicating worsened liquidity. Other authors, such as, Lamoureux and Poon (1987), Muscarella and Vetsuypens (1996) show that the number of trades per day, increase subsequent to splits. Lakonishok and Lev (1998) finds splits have no impact on split-adjusted trading volume. The inconclusive evidence reflects the challenge in the selection and in the interpretation of the liquidity proxy.

Using daily and intraday data from the Stock Exchange of Thailand (SET) over 2002-2004, this paper examines the impact of stock splits on price and liquidity as well as the determinants of an

[1] See for example, Baker and Gallagher (1980) and Baker and Powell (1993) in their surveys of US firms.