



STOCK SPLITS AND LIQUIDITY

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ABSTRACT

This study has been carried out to identify the impact of stock splits on liquidity of a share. Therefore, this study seeks to address the question of, what is the liquidity behavior of a share after a stock split. Effect of stock split on liquidity of a share compared to the period before the split is analyzed in this study and furthermore, this study identifies the change of liquidity behavior of a share after the split in relation to the market. This study expands the horizons of liquidity measures of a share by using three dimensions to determine the liquidity behavior after the split. Share price, trade volume and trade frequency is used in this study to determine the liquidity behavior compared to the period before the split. Overall Liquidity of the share is determined based upon all three dimensions and Relative Market Ratio is used to determine the market liquidity of a share.

This study is based on 20 share splits which had been undertaken in Colombo Stock Exchange in the years of 2009 and 2010. In accordance with the results it can be generalized that liquidity of a share after undertaking a stock split has been increased compared to period before the split and also the market liquidity of a share increases after undertaking a stock split. Therefore, this study suggests to undertake stock splits, to reduce cost of capital of corporations and to increase the liquidity of a share.