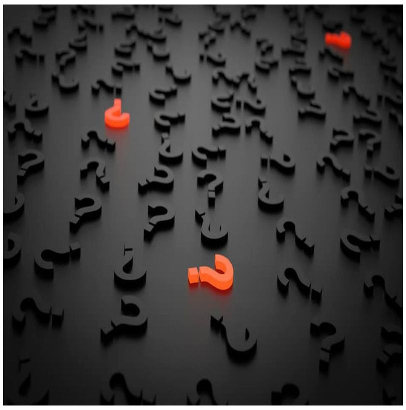

Are Stock Splits Good for Investors?

Description

Dollarama Inc. (TSX:DOL) recently posted another solid quarter. Alongside its quarterly earnings, the company also announced its proposal for a three-for-one stock split. Dollarama shareholders can expect to receive two additional shares for each share they own. As per its press release, only those "shareholders of record at the close of business on June 14, 2018, will be entitled to receive" the two additional shares. Will a split benefit investors?

There is one main reason that companies undergo stock splits, and that is to improve liquidity. When a company's share price gets too high for smaller investors, or if it significantly exceeds that of its peers, a stock split will decrease the value of the company's share price. This can have the psychological effect of being more affordable to smaller investors who, in turn, are expected to buy more shares. However, there is evidence to support that liquidity doesn't actually improve. In a practical world, a two-for-one split should double the number of shares traded if liquidity is to be increased by the split. However, this trend is often not observed.

One study, which looked at the top 30 U.S. companies by current market capitalization that underwent a stock split between 2001 and 2010, revealed no significant benefit. In fact, exactly half of the companies showed a positive return over a one-year period post-split, while the other half showed a negative return.

Between 2015 and 2017, there have been very few large cap TSX-listed companies that have undergone stock splits. **Andrew Peller Ltd.** (TSX:ADW.A) underwent a three-for-one split on October 17, 2016. In the year following, its share price returned 4.65%, which underperformed the market. On May 13, 2015, **Brookfield Asset Management Inc.** (TSX:BAM.A)(NYSE:BAM) underwent a three-for-two split. Brookfield also underperformed the market, just barely posting a one-year return of 0.14%. On April 6, 2015, **Keyera Corp.** (TSX:KEY) underwent a two-for-one split. Did it beat the market? No. Unfortunately, Keyera's share price lost approximately 16% of its value in the year following.

The key aspect for investors to remember is that a stock split has no material impact on the company's financial situation. Its underlying value remains the same. There is a common misconception that a split will result in a share price increase due to increased liquidity. However, there is little evidence to support this notion. In effect, a stock split is intended to be a neutral event.

Don’t chase stock splits

Although they might be alluring, stock splits are neutral events that serve primarily as distractions. First and foremost, investors should always ensure that they invest in a company with solid fundamentals. Don’t be tempted to chase after meaningless events.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:BN (Brookfield Corporation)
2. TSX:ADW.A (Andrew Peller Limited)
3. TSX:BN (Brookfield)
4. TSX:DOL (Dollarama Inc.)
5. TSX:KEY (Keyera Corp.)

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1. Investing

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