

Share Splits



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Retail conglomerate Amazon recently announced a 20:1 stock split. This is the fourth share split for the company, the last one occurring over twenty years ago. The split is accompanied by a \$10 billion share buyback. Based on the present price of Amazon stock at \$3250, the post-split price will be approximately \$160 per share. The split is expected to occur in June.

There is corporate prestige in having a lofty share price. It creates an air of exclusivity. Institutional investors tend to favor stocks in a higher price range which are then regarded, often mistakenly, by their clients as less-speculative. How a high price affects employee morale is another question. A high share price inhibits broad employee participation through stock options and bonuses. It also inhibits family members giving at least a board lot (100 shares) to their offspring.

So why should a company like Amazon choose to go to the bother and expense of a stock split? First, a stock split is to some extent a celebration. It is a celebration of corporate success which also includes an increased dividend. The timing of the celebration usually occurs when the economy is growing, when earnings per share achieve a new high and sometimes in anticipation of an additional direction for the company. Most important, it is hoped the share split will eventually broaden the shareholder base.

In the case of Amazon, the stock buyback has a dual purpose. It is in lieu of a dividend increase and to provide market liquidity for those shareholders who want to take some profits on their stock. Why sell when the company is doing so well? Basically, because the price is up. Amazon stock rose over 5% on the day of the announcement.

In deciding whether to sell, some stockholders will ask themselves: Why not take advantage of the premium the split announcement has put on the stock price? Years ago, Fortune Magazine made a study of stock performance post-split. They concluded that the time around a stock split is, more often than not, a good time to sell. In the case of Amazon, the \$10 billion buyback should counter any unwarranted sell-off in the stock. On the other hand, how much is the buffer of \$10 billion when it represents less than .65% percent of the market value of shares issued.

There are at least two more reasons for the Amazon 20:1 stock split. At a price of \$3250 per share, most retail investors had lost interest in directly owning Amazon shares. Amazon's core business is retail. Individual investors tend to be loyal to their investments. A Loblaw investor will likely feel guilty about shopping at Metro. If a client owned Bank of Montreal stock, they will likely bank there. If they own two bank stocks, they will likely have accounts at both. Publicly owned stocks are a form of advertising the company's business.

A second reason for a more modest share price is it gives the company more flexibility when making takeover offers, purchasing corporate services as well as imbursing employees and prospective talent.

If the Amazon share split is a harbinger of more splits to follow, it is most welcome. Share splits bolster public interest in the investment business, and equity markets are far healthier with a more equal balance between the institutional and retail investor.

The views as articulated in this article are those of Briar Foster alone and do not necessarily reflect the opinion of Foster & Associates.

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