Notes on Corporate Actions

Qiao Zhou

July 10, 2016

1 Introduction

Corporate actions are typically agreed upon by a company's board of directors and authorized by the shareholders. Some examples are stock splits, dividends, mergers and acquisitions, rights issues and spin offs.

2 Types of Corporate Actions

2.1 Stock Splits

It's a non-event in the sense that it will not affect the company's equity or its market capitalization. A firm may issue a stock split in order to increase its share's liquidity in the market. The drop in price and increase in liquidity make the stock more attractive to a wider range of investors and interested buyer, and thus may push the prices up. At times, companies may decide to issue a reverse split to increase its price range and to drive out small investors.

2.2 Dividends

There are two types of dividends a company can issue: cash and stock dividends. After the issuance of dividends, the distributable equities of a company are reduced. In case of a stock dividend of x%, for each 100 shares you will receive x additional shares. The increase in outstanding shares, however will reduce the earning per share, and will thus reduce the share price. The distribution of a cash dividend can signal to an investor that the company has substantial retained earnings from which the shareholders can directly benefit. If it was a rapidly growing company, a newly declared dividend may indicate that the company has reached a stable level of growth that it is sustainable into the future.

2.2.1 How Dividends are distributed

Stocks that pay dividends set three important dates around the determination, announcement, and distribution of dividends: the ex-dividend date, the record date and the payment date. The last one is straight-forward, while the first two dates always confuse people.
In brief, the payment date is the day the dividends will be booked and appear in your brokerage account.However, you might receive the dividends a few days before or after the payment day, depending on whether the payment day falls

in a holiday or weekend. The ex-dividend day is set to remind the investors that you need to purchase the stock before the ex-dividend date and hold the positions till at least the ex-dividend date in order for you to be qualified as a shareholder on the record date. This is due to the fact that, under the "T+2/3" convention, any single stock purchase or transaction can take up to three stock business days in order to "settle" in your account. If you sell the position before the ex-dividend day, you will not receive the upcoming dividends. The record date is the date that actually matters. It is the date on which you must be a holder of the stock in order to receive the dividends in the upcoming payment. In sum, if you have positions of a dividend stock before the ex-dividend day, you will be qualified as holder of stock in the record date and will be entitled to receive dividends in the upcoming payments. And the dividend will actually be booked in the payment day.

2.3 Rights Issues

A company implementing a rights issue is offering additional and/or new shares but only to already existing shareholders. The existing shareholders are given the right to purchase or receive these shares before they are offered to the public. A rights issue regularly takes place in the form of a stock split, and can indicate that existing shareholders are being offered a chance to take advantage of a promising new development.

2.4 Mergers and Acquisitions

If a company undergoes a merger, it may indicate to shareholders that the company has confidence in its ability to take on more responsibilities. On the other hand, a merger could also indicate a shrinking industry in which smaller companies are being combined with larger corporations. In the case of an acquisition, however, a company seeks out and buys a majority stake of a target company's shares; the shares are not swapped or merged.

2.5 Spin Offs

A spin off occurs when an existing publicly-traded company sells a part of its assets or distributes new shares in order to create a newly independent company. Often the new shares will be offered through a rights issue to existing shareholders before they are offered to new investors (if at all). Depending on the situation, a spin-off could be indicative of a company ready to take on a new challenge or one that is restructuring or refocusing the activities of the main business.