

Stock Splits and Capital Markets : Why They Constitute a Material Fact Under Insider Trading Regulations

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This paper examines the basis for classifying stock splits as material facts under Japanese insider trading regulations by empirically analyzing their impact on stock prices.

First, the paper demonstrates that under the Financial Instruments and Exchange Act, stock splits occupy a unique position, distinct from facts that alter a company's operations or financial status, such as mergers or business alliances. The legislative rationale for this classification lies in stock splits' effect of increasing stock prices. The paper reveals that the mechanism by which stock splits influence stock prices has evolved over time. Drawing on prior research, it first discusses the possibility that small-scale splits before the Companies Act reform functioned as "signaling of dividend increases" and examines the possibility of a "split bubble" due to institutional distortions until 2006. The paper then empirically analyzes the impact on stock prices of "pure stock splits" after October 2018, when the standardization of trading units was completed. The results show statistically significant positive returns on announcement days, confirming that stock splits indeed constitute information that boosts stock prices.

Next, the paper analyzes reverse stock splits, which are the inverse of stock splits. With the exception of cases aimed at standardizing trading units, reverse stock splits tend to depress stock prices. This can be considered the flip side of stock splits' price-boosting effect. The paper questions whether the current situation, in which reverse stock splits are not classified as material facts under insider trading regulations, creates a logical inconsistency.

In conclusion, this paper proposes that subjecting both stock splits and reverse stock splits to insider trading regulations would be rational and logically consistent, as both are facts that impact stock prices. However, this paper's scope is limited to elucidating the function of stock splits; fundamental questions regarding how insider trading regulations should be structured are left for future research.