

STOCK PRICE REACTION TO SCRIP DIVIDEND ANNOUNCEMENT AND MARKET EFFICIENCY: STUDY FROM THE CSE IN SRI LANKA

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1. Introduction

The scrip dividend announcement is a corporate action in which a company offers its shareholders the choice to receive shares instead of a cash dividend. The main objective of the study is to test the stock price reaction on scrip dividend announcements and market efficiency within CSE.

2. Research Methodology

The study selected 22 scrip dividend announcements using purposive sampling from 2012 to 2022. This study utilize the event study method by incorporating the stock volatility clustering phenomenon into the Market Model. Additionally, it is expanded through the application of time series modeling techniques. The event window is 31 days, comprising fifteen days before and fifteen days after the scrip dividend announcement.

3. Findings and Discussion

The market and time series models indicate that the AAR and CAAR on the day of the scrip dividend announcement are statistically insignificant at the 5 % level. Therefore, the researcher accepted the null hypothesis stating that stock prices do not show significant abnormal returns due to scrip dividend announcements. A possible explanation is that some market insiders may be engaging in trading activities on this information prior to its public disclosure. Thus, the dividend announcement that is ultimately released does not provide the market with any novel information.

4. Conclusion and Implications

The overall results confirm that emerging markets, such as Sri Lanka, do not respond significantly to scrip dividend announcements. This suggests that these announcements do not contain price-sensitive information, implying that the Colombo Stock Exchange does not adhere to the semi-strong form efficiency hypothesis. It is imperative for regulatory entities to priorities the reinforcement of legislation pertaining to the prohibition of insider trading while concurrently ensuring the implementation of severe penalties for any violations.

Keywords: Abnormal Return, Event Study, Scrip Dividend, Semi-Strong Form Efficiency and Time Series Modelling.