Chapter–8: Miscellaneous

8.1 Corporate Actions

Corporate Actions

Corporate actions tend to have a bearing on the price of a security. When a company announces a corporate action, it is initiating a process that will bring actual change to its securities either in terms of number of shares increasing in the hands on the shareholders or a change to the face value of the security or receiving shares of a new company by the shareholders as in the case of merger or acquisition etc. By understanding these different types of processes and their effects, an investor can have a clearer picture of what a corporate action indicates about a company's financial affairs and how that action will influence the company's share price and performance.

Corporate actions are typically agreed upon by a company's Board of Directors and authorized by the shareholders. Some examples are dividends, stock splits, rights issues, bonus issues etc.

Dividend

Returns received by investors in equities come in two forms a) growth in the value (market price) of the share and b) dividends. Dividend is distribution of part of a company's earnings to shareholders, usually twice a year in the form of a final dividend and an interim dividend. Dividend is therefore a source of income for the shareholder. Normally, the dividend is expressed on a 'per share' basis, for instance - Rs. 3 per share. This makes it easy to see how much of the company's profits are being paid out, and how much are being retained by the company to plough back into the business. So a company that has earnings per share in the year of Rs. 6 and pays out Rs. 3 per share as a dividend is passing half of its profits on to shareholders and retaining the other half. Directors of a company have discretion as to how much of a dividend to declare or whether they should pay any dividend at all.

Dividend yield

Dividend yield gives the relationship between the current price of a stock and the dividend paid by its' issuing company during the last 12 months. It is calculated by aggregating past year's dividend and dividing it by the current stock price.

Example	:	ABC Co.
Share price	:	Rs. 360
Annual dividend	:	Rs. 10
Dividend yield	:	2.77% (10/360)

Historically, a higher dividend yield has been considered to be desirable among investors. A high dividend yield is considered to be evidence that a stock is underpriced, whereas a low dividend yield is considered evidence that the stock is overpriced. A note of caution here though. There have been companies in the past which had a record of high dividend yield, only to go bust in later years. Dividend yield therefore can be only one of the factors in determining future performance of a company.

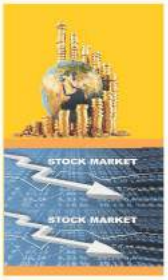
Stock Split

A stock split is a corporate action which splits the existing shares of a particular face value into smaller denominations so that the number of shares increase, however, the market capitalization or the value of shares held by the investors post split remains the same as that before the split. For e.g. If a company has issued 1,00,00,000 shares with a face value of Rs. 10 and the current market price being Rs. 100, a 2-for-l stock split would reduce the face value of the shares to 5 and increase the number of the company's outstanding shares to 2,00,00,000, (l,00,00,000*(10/5)). Consequently, the share price would also halve to Rs. 50 so that the market capitalization or the value shares held by an investor remains unchanged. It is the same thing as exchanging a Rs. 100 note for two Rs. 50 notes, the value remains the same.

Let us see the impact of this on the share holder: Let's say company ABC is trading at Rs. 40 and has 100 million shares issued, which gives it a market capitalization of Rs. 4000 million (Rs. 40 x 100 million shares). An investor holds 400 shares of the company valued at Rs. 16,000. The company then decides to implement a 4-for-l stock split (i.e. a shareholder holding 1 share, will now hold 4 shares). For each share shareholders currently own, they receive three additional shares. The investor will therefore hold 1600 shares. So the investor gains 3 additional shares for each share held. But this does not impact the value of the shares held by the investor since post split, the price of the stock is also split by 25% (l/4th), from Rs. 40 to Rs.10, therefore the investor continues to hold Rs. 16,000 worth of shares. Notice that the market capitalization stays the same - it has increased the amount of stocks outstanding to 400 million while simultaneously reducing the stock price by 25% to Rs. 10 for a capitalization of Rs. 4000 million. The true value of the company hasn't changed.

An easy way to determine the new stock price is to divide the previous stock price by the split ratio. In the case of our example, divide Rs. 40 by 4 and we get the new trading price of Rs. 10. If a stock were to split 3-for-2, we'd do the same thing: 40/(3/2) = 40/1.5 = Rs. 26.60.

2-for-1 Split	Pre-Split	Post-Split
No. of shares	100 mill.	200 mill.
Share Price	Rs. 40	Rs. 20
Market Cap.	Rs. 4000 mill.	Rs. 4000 mill.
4-for-l		
No. of shares	100 mill.	400 mill.
Share Price	Rs. 40	Rs. 10
Market Cap.	Rs. 4000 mill.	Rs. 4000 mill.



Reasons for Stock Split

If the value of the stock doesn't change, what motivates a company to split its stock? Though there are no theoretical reasons in financial literature to indicate the need for a stock split, generally, there are mainly two important reasons. As the price of a security gets higher and higher, some investors may feel the price is too high for them to buy, or small investors may feel it is unaffordable. Splitting the stock brings the share price down to a more "attractive" level. In our earlier example to buy 1 share of company ABC you need Rs. 40 pre-split, but after the stock split the same number of shares can be bought for Rs.10, making it attractive for more investors to buy the share. This leads us to the second reason. Splitting a stock may lead to increase in the stock's liquidity, since more investors are able to afford the share and the total outstanding shares of the company have also increased in the market.

Buyback of Shares

A buyback can be seen as a method for company to invest in itself by buying shares from other investors in the market. Buybacks reduce the number of shares outstanding in the market. Buy back is done by the company with the purpose to improve the liquidity in its shares and enhance the shareholders' wealth. Under the SEBI (Buy Back of Securities) Regulation, 1998, a company is permitted to buy back its share from:

a) Existing shareholders on a proportionate basis through the offer document.

b) Open market through stock exchanges using book building process.

c) Shareholders holding odd lot shares.

The company has to disclose the pre and post-buyback holding of the promoters. To ensure completion of the buyback process speedily, the regulations have stipulated time limit for each step. For example, in the cases of purchases through stock exchanges, an offer for buy back should not remain open for more than 30 days. The verification of shares received in buy back has to be completed within 15 days of the closure of the offer. The payments for accepted securities has to be made within 7 days of the completion of verification and bought back shares have to be extinguished within 7 days of the date of the payment.

8.2 Index

The Nifty index

S&P CNX Nifty (Nifty), is a scientifically developed, 50 stock index, reflecting accurately the market movement of the Indian markets. It comprises of some of the largest and most liquid stocks traded on the NSE. It is maintained by India Index Services &. Products Ltd. (IISL), which is a joint venture between NSE and CRISIL. The index has been co-branded by Standard & Poor's (S&P). Nifty is the barometer of the Indian markets.

8.3 Clearing & Settlement and Redressal

Clearing Corporation

A Clearing Corporation is a part of an exchange or a separate entity and performs three functions, namely, it clears and settles all transactions, i.e. completes the process of receiving and delivering shares/funds to the buyers and sellers in the market, it provides financial guarantee for all transactions executed on the exchange and provides risk management functions. National Securities Clearing Corporation (NSCCL), a 100% subsidiary of NSE, performs the role of a Clearing Corporation for transactions executed on the NSE.

Rolling Settlement

Under rolling settlement all open positions at the end of the day mandatorily result in payment/ delivery *n' days later. Currently trades in rolling settlement are settled on T+2 basis where T is the trade day. For example, a trade executed on Monday is mandatorily settled by Wednesday (considering two working days from the trade day). The funds and securities pay-in and pay-out are carried out on T+2 days.

What is Pay-in and Pay-out

Pay-in day is the day when the securities sold are delivered to the exchange by the sellers and funds for the securities purchased are made available to the exchange by the buyers.

Pay-out day is the day the securities purchased are delivered to the buyers and the funds for the securities sold are given to the sellers by the exchange.

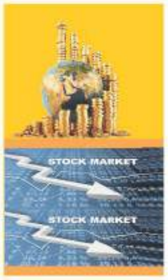
At present the pay-in and pay-out happens on the 2nd working day after the trade is executed on the stock exchange.

Auction

On account of non-delivery of securities by the trading member on the pay-in day, the securities are put up for auction by the Exchange. This ensures that the buying trading member receives the securities. The Exchange purchases the requisite quantity in auction market and gives them to the buying trading member.

Book-closure/Record date

Book closure and record date help a company determine exactly the shareholders of a company as on a given date. Book closure refers to the closing of the register of the names of investors in the records of a company. Companies announce book closure dates from time to time. The benefits of dividends, bonus issues, rights issue accrue to investors whose name appears on the company's records as on a given date which is known as the record date and is declared in advance by the company so that buyers have enough time to buy the shares, get them registered in the books of the company and become entitled for the benefits such as bonus, rights, dividends etc. With the depositories now in place, the buyers need not send shares physically to the companies for registration. This is taken care by the depository since they have the records of investor holdings as on a particular date electronically with them.



No-delivery period

Whenever a company announces a book closure or record date, the exchange sets up a no-delivery period for that security. During this period only trading is permitted in the security.

However, these trades are settled only after the no-delivery period is over. This is done to ensure that investor's entitlement for the corporate benefit is clearly determined.

Ex-dividend date

The date on or after which a security begins trading without the dividend included in the price, i.e. buyers of the shares will no longer be entitled for the dividend which has been declared recently by the company, in case they buy on or after the ex-dividend date.

Ex-date

The first day of the no-delivery period is the ex-date. If there is any corporate benefits such as rights, bonus, dividend announced for which book closure/record date is fixed, the buyer of the shares on or after the ex-date will not be eligible for the benefits.

Recourses available to investor/client for redressing his grievances

You can lodge complaint with the Investor Grievances Cell (IGC) of the Exchange against brokers on certain trade disputes or non-receipt of payment/securities. IGC takes up complaints in respect of trades executed on the NSE, through the NSE trading member or SEBI registered sub-broker of a NSE trading member and trades pertaining to companies traded on NSE.

Arbitration

Arbitration is an alternative dispute resolution mechanism provided by a stock exchange for resolving disputes between the trading members and their clients in respect of trades done on the exchange. If no amicable settlement could be reached through the normal grievance redressal mechanism of the stock exchange, then you can make application for reference to Arbitration under the Bye-Laws of the concerned Stock exchange.

Investor Protection Fund

Investor Protection Fund (IPF) is maintained by NSE to make good investor claims, which may arise out of non-settlement of obligations by the trading member, who has been declared a defaulter, in respect of trades executed on the Exchange. The IPF is utilised to settle claims of such investors where the trading member through whom the investor has dealt has been declared a defaulter. Payments out of the IPF may include claims arising of non payment/non receipt of securities by the investor from the trading member who has been declared a defaulter. The maximum amount of claim payable from the IPF to the investor (where the trading member through whom the investor has dealt is declared a defaulter) is Rs. 10 lakh.