Stock splits are a corporate action in which a company divides its existing shares into multiple new shares.The primary goal of a stock split is to make the stock more affordable to a broader range of investors and potentially increase liquidity. When a stock split is approved and announced by the board of directors of a public company, they decide the ratio of the split, which can be anything from 2:1 to 5:1 and beyond. The company announces the split and specifies the effective date when the split will take place. This is when the new shares will be distributed to shareholders.On the effective date, the stock price is adjusted based on the split ratio. For a 2-for-1 split, each old share is divided into two new shares, and the stock's price is halved. If a stock was trading at $100 per share before the split, after a 2-for-1 split, it would trade at $50 per share.Effects On Existing ShareholdersIt must be noted that stock splits have little to no noticeable effect on existing shareholders, which is an integral part of any stock split. When a stock is split by a certain ratio, the existing shareholders also increase their shares by the same ratio, without incurring additional costs. This is to ensure the satisfaction of existing shareholders and avoid diluting their investments in the company. Reverse Stock SplitsOn the other hand, companies may also go through a reverse stock split, where they decrease the number of available shares on the market by a factor decided by the board of directors. For example, in a 1:5 reverse split, every five existing shares are combined into one new share.The primary goal is to increase the stock's price per share. This is often done to meet minimum price requirements for stock exchange listings or to boost investor confidence. While a reverse split can raise the stock price, it typically reflects financial difficulties or low market confidence, and it doesn't change the company's market value or fundamentals.Stock Split Example - Tesla Inc (TSLA)A notable example of a stock split was Tesla in 2022, when the stock was trading between the $800-$1,000 range, which was deemed too expensive for traders. Therefore, the company initiated a 3:1 stock split, increasing the shares of existing shareholders by a factor of 3 and decreasing the share price by the same ratio. While traders can buy and sell Tesla shares easily using fractional shares, this is not universally available. Therefore, Tesla managed to make its shares more accessible to a much broader group of investors by going through with the stock split. Frequently, management teams decide to do a stock split. A stock split is the exchange of existing shares of stock owned by an investor for new shares from the same company. Stock splits don’t increase or decrease the company’s capitalization; they just change the number of shares available in the market and the per-share price. Typically, a company may announce that it’s doing a 2-for-1 stock split. In this situation, the price of the stock is cut in half, and current shareholders double the number of shares they own. Companies do other splits, such as a 3-for-2 or 4-for-1, but 2-for-1 is the most common split. Qualifying for a stock split is similar to qualifying to receive a dividend — you must be listed as a stockholder as of the date of record. Keep good records regarding your stock splits in case you need to calculate capital gains for tax purposes. Ordinary stock splits An ordinary stock split — when the number of stock shares increases — is the kind investors usually hear about. If you own 100 shares of Dublin, Inc., stock (in certificate form, at $60 per share) and the company announces a stock split, you receive in the mail a stock certificate for 100 more shares. Each share of the stoc is adjusted to a $30 value. Not all stock is in certificate form. Stocks held in a brokerage account are recorded in book entry form. Most stock, in fact, is in book entry form. If you keep the stock in your brokerage account, check with your broker for the new share total to make sure you’re credited with the new number of shares after the stock split. An ordinary stock split is primarily a neutral event, so why does a company bother to do it? The most common reason is that management believes the stock is too expensive, so it wants to lower the stock price to make the stock more affordable and therefore more attractive to new investors. Studies have shown that stock splits frequently precede a rise in the stock price. Although stock splits are considered a non-event in and of themselves, many stock experts see them as bullish signals because of the interest they generate among the investing public. Reverse stock splits A reverse stock split usually occurs when a company’s management wants to raise the price of its stock. Just as ordinary splits can occur when management believes the price is too expensive, a reverse stock split means the company feels that the stock’s price is too cheap. If a stock’s price looks too low, that may discourage interest by individual or institutional investors. Management wants to drum up more interest in the stock for the benefit of shareholders (some of whom are probably insiders). The company may also do a reverse split to decrease costs. When you have to send an annual report and other correspondence regularly to all the stockholders, the mailings can get a little pricey, especially if you have lots of investors who own only a few shares each. A reverse split helps consolidate shares and lower overall management costs. Technically, a reverse split is considered a neutral event. However, just as investors may infer positive expectations from an ordinary stock split, they may have negative expectations from a reverse split because a reverse split tends to occur for negative reasons. One definitive negative reason for a reverse split is if the company’s stock is threatened to be delisted. If a stock is on a major exchange and the price falls below $1, the stock will face delisting (basically getting removed from the exchange). A reverse split may be used to ward off such an event. Share — copy and redistribute the material in any medium or format for any purpose, even commercially. Adapt — remix, transform, and build upon the material for any purpose, even commercially. The licensor cannot revoke these freedoms as long as you follow the license terms. Attribution — You must give appropriate credit , provide a link to the license, and indicate if changes were made . You may do so in any reasonable manner, but not in any way that suggests the licensor endorses you or your use. ShareAlike — If you remix, transform, or build upon the material, you must distribute your contributions under the same license as the original. No additional restrictions — You may not apply legal terms or technological measures that legally restrict others from doing anything the license permits. You do not have to comply with the license for elements of the material in the public domain or where your use is permitted by an applicable exception or limitation . No warranties are given. The license may not give you all of the permissions necessary for your intended use. For example, other rights such as publicity, privacy, or moral rights may limit how you use the material. Editorial Note: We earn a commission from partner links on Forbes Advisor. Commissions do not affect our editors' opinions or evaluations. When a company is concerned that its share price is too high or too low, it can opt for a stock split or a reverse stock split. A stock split can help a company lower its share price to appeal to new investors, while a reverse stock split can boost its share price and help preserve its listing on a major stock exchange. What Is a Stock Split? A stock split is when a company’s board of directors issues more shares of stock to its current shareholders without diluting the value of their stakes. A stock split increases the number of shares outstanding and lowers the individual value of each share. While the number of shares outstanding change, the overall market capitalization of the company and the value of each shareholder’s stake remains the same. Say you have one share of a company’s stock. If the company opts for a 2-for-1 stock split, the company would grant you an additional share, but each share would be valued at half the amount of the original. After the split, your two shares would be worth the same as the one share you started with. What Is a Reverse Stock Split? A reverse stock split reduces a company’s number of shares outstanding. If you owned 10 shares of stock in a company, for example, and the board announced a 1-for-2 reverse stock split, you’d end up with five shares of stock. The total value of your shares would remain consistent. If the 10 shares were valued at $4 per share before the reverse split, the five shares would be valued at $8 per share after the reverse split. In either case, the total value of your investment remains $40. Why Do Companies Split their Stock? In many cases, a stock split is a strategy used by companies to meet a specific goal, says Amanda Holden, a former investment counselor and the founder of Invested Development, a course aimed at helping women learn about investing. Companies often like the idea of creating more liquidity by making a price more attractive and attainable for a larger number of people. “You might not be able to buy Apple at $500, but you could buy it at $125,” she says. On the other hand, a reverse stock split is often aimed at helping a company meet the minimum requirements to remain listed on an exchange. “You can get kicked off an exchange if your price drops too far,” Holden says. “A reverse stock split consolidates your shares in a way that results in a higher per-share price that can keep you trading on a public and accessible exchange.” This helps ensure more people can access the shares and keeps existing shares liquid. While a reverse stock split is often thought of as a red flag for investors, in the long run, it can help a company survive and recover from a rough patch. What Is a 2 for 1 Stock Split? A 2-for-1 stock split grants you two shares for every one share of a company you own. If you had 100 shares of a company that has decided to split its stock, you’d end up with 200 shares after the split. A 2 for 1 stock split doubles the number of shares you own instantly. Two-for-one and 3-for-1 stock splits are relatively common, says Holden. While Apple (AAPL) and Tesla (TSLA) have gotten a lot of publicity for their 2020 stock splits, their 5-for-1 or 4-for-1 stock splits were uncommon choices. How Does a Stock Split Affect You? Because a stock split doesn’t change the underlying value of your investment, you may not notice any more substantial changes than the number of shares in your investment account. “There’s no particular advantage for those who already have shares,” Holden says. “Nothing about ownership is going to change. You might have twice as many shares, but they are at half the price, so it balances out.” For those who aren’t already shareholders, though, a stock split can provide motivation to buy. For example, if you couldn’t afford a share of Tesla before its recent stock split, you might be able to get one now. The ability for more people to buy a stock can bump up its price, which in turn may actually increase a company’s value, at least temporarily, Holden says. “With more people able to buy, you see more demand, and the price can go up. If you have more shares, this can be beneficial to you if you hold on,” Holden says. “However, that stock and total value bump is generally temporary. To see long-term gains, you usually need to keep holding that stock to get the benefit over time.” Are Stock Splits Important with Widespread Fractional Share Investing? As fractional investing becomes more popular and widespread, some experts speculate that stock splits will become less important as fractional shares allow you to buy into a company at virtually any price point. Currently, investing apps like Robinhood, Stash, M1 Finance and SoFi Invest, as well as legacy brokerages like Charles Schwab and Fidelity, allow clients to buy fractional shares of certain stocks and exchange-traded funds (ETFs). “It’s hard to say how fractional investing will impact investing and stock splits since there isn’t a lot of data right now,” Holden says. “But I think it will take significant time before fractional investing eliminates the need for stock splits.” And that’s not even considering the psychological aspect of stock splits. “Humans love a round number,” says Holden. “There’s something about knowing you have the money to buy a full share that motivates many investors.” The Bottom Line In the end, a stock split—or even a reverse stock split—doesn’t have a huge practical impact on a company’s current investors. A stock split’s biggest impact is on investors who might be watching a particular stock and hoping to purchase a full share for a lower price. For those investors, a stock split can provide a powerful motivator to get off the sidelines. Big-name companies with lofty stock prices often make waves when they announce stock splits, but these moves may leave investors with questions. What is a stock split? What does it mean? How does it affect me as an investor? How does it affect the company?We cover what investors should know about stock splits and why companies choose to do them.What Happens When a Stock Splits?Simply put, a stock split is exactly what it sounds like. One share gets divided, or split, into multiple shares. Don’t worry, though. The value of your holdings is the same, just in smaller chunks. Think about a stock split like a chocolate bar. Your one big chocolate bar is broken down into multiple bite-size pieces. You still have the same amount of chocolate, just in smaller segments.Similarly, in a stock split, it is very important to remember that the price of the share also is reduced. For example, if a company board announces a 2-for-1 split, then you get one extra share for each share you own--but the share price will be halved. In this example of a 2-for-1 split, if you had one share of Company X at $10 per share, you now have two shares of Company X at $5 per share.This does not mean that the stock has become cheaper. The fundamentals of the company and the stock price have not changed. Sticking with the chocolate bar analogy, after breaking the bar into smaller bits, you have smaller bits of chocolate, not more chocolate overall. Why Does a Company Split Stock?Why do companies announce stock splits? Stock splits are a way for companies to increase their overall liquidity. Liquidity means the ease with which investors can buy or sell shares on a stock exchange. The less each share costs, the less money is needed by even the smallest investor to buy or sell the stock. Plus, having a larger number of cheaper shares can have the psychological impact of making shares more attractive to investors, even though the company’s underlying value hasn’t changed.In most cases, stock splits are undertaken by companies when the share price has gone up significantly, particularly in relation to a company’s stock market peers. If the share price becomes more affordable for smaller investors, it can reasonably be assumed that more investors will participate, and so the overall liquidity of the stock would increase as well.But remember this with stock splits: Though the number of outstanding shares changes, and though the price of each share changes, the company’s overall market cap stays the same. The value of the company doesn’t increase when a split occurs, therefore the value of your stocks, your shares, doesn’t change, either. Take Chipotle CMG for example. When the company announced its upcoming 50-1 split on June 6, 2024, one share sold for about $3,100-$3,200. Many investors (myself included) would not be able to invest in Chipotle, because I do not have $3,000-odd to invest in one share of one company. The split took effect on June 26, 2024, and shares dropped to around $65 a piece, with each existing shareholder receiving 49 additional shares for every share they own. A stock price of $65-odd is much more manageable, both for me and for many others.This is especially true now with more and more investors having access to low-cost trading platforms. Buying and selling stocks is now easier than ever, and for many investors these recent splits might be an entry point into companies they have long admired.All this being said, these recent high-profile splits seem superfluous given that most brokerage platforms now enable trading in fractional shares. Perhaps the psychology of owning at least one whole share is at play in the companies’ decisions.“When we look at a company like Chipotle and strictly observe the value of an investment immediately after a stock split, there really isn’t a discernable pattern in the change in wealth. What is noticeable is the trading volume of the stock which might be attributed to news flow. All this said, for long-term investors in a stock, a stock split (or reverse split) really doesn’t affect the fundamental value of the company or the wealth in your pocket,” points out Morningstar Canada’s director of Investment Research Ian Tam.The value of the company doesn’t increase when a split occurs, therefore the value of your stocks, your shares, doesn’t change, either. Does the Company Change After a Stock Split?Not at all. Stock splits do not alter the fundamentals of the company in any way, apart from the short-term price increases we described earlier. There’s no harm done in this regard if the stock doesn’t split either.Recent high-profile stock splits include Chipotle, Broadcom AVGO, Nvidia NVDA, and Walmart WMT. Alphabet GOOGL/GOOG, Tesla TSLA, and Amazon AMZN split shares in 2022. What Is a Reverse Stock Split?The opposite of a stock split, which is technically called a forward stock split, is a reverse stock split.In the case of reverse stock splits, the company divides the number of shares that investors own, rather than multiplying them. As a result, the price of the shares increases.For instance, if you own 10 shares of Company X at $10 per share, and the company announces a 1-for-2 reverse stock split, you end up owning five shares of Company X at $20 per share. Usually, reverse stock splits are announced by companies that have low share prices and want to increase them--often to avoid being delisted.Is a Reverse Stock Split a Bad Sign?You may think that reverse stock splits are bad news for the company, but this is not always the case. One of the most famous examples of reverse stock splits is Citigroup C. Its share price declined to under $10 during the 2008 global financial crisis and stayed there, so in 2011 the Citigroup board decided to do a reverse split of 1-for-10. The split took the price from $4.50 per share to $45 per share. The company--and the stock--survived and is now trading at around $61 per share.See, just math!The author or authors do not own shares in any securities mentioned in this article. Find out about Morningstar’s editorial policies. Investing in stocks means you have to stay on top of how your investments are trending. When a company wants to appeal to more investors, they might issue a stock split. Here’s what a stock split is and how they matter to your investments. $0 stock & ETF trades; $0.65/contract options trades; $0 mutual funds tradesGet up to $700 when you open & fund an account with qualifying new money. Offer expires 4/15/2025. What is a stock split? A stock split is when a company divides and increases the number of shares available to buy and sell on an exchange. A stock split lowers its stock price but doesn’t weaken its value to current shareholders. It increases the number of shares and might entice would-be buyers to make a purchase. The total value of the stock shares remains unchanged because you still own the same value of shares, even if the number of shares increases. How does a stock split work? A stock split gets issued by a company’s board of directors in an effort to become more affordable to potential investors. The announcement tends to come a few weeks before the stock split goes into effect so current investors aren’t caught off guard and potential investors can make plans to buy shares. The type of stock split can impact the total number of shares available. For instance, if a company issues a 2/1 stock split, the value of each share is cut in half. So if you own 50 shares of a stock that trades at $50 per share, you’ll now have 100 shares that trade at $25 a share. Types of stock split The type of stock split matters because it can tell you how a company is performing. A regular stock split might occur when a company believes the value of the stock is too high, which means a company is performing well and is looking to increase the number of shareholders in the company. If you are unsure about how a stock split will affect your investments, it may be helpful to consult with a financial advisor to assist you with your individual financial goals and risk tolerance. 0.50%-0.60% based on portfolio sizeEducation, home purchase, retirement, travel and more Reverse stock split A regular stock splits the existing number of shares into a bigger number of shares. A reverse stock split takes a large number of shares and reduces the number. For instance, in a 1-2 reverse stock split, a stock that was trading for $10 is now worth $20 a share and if you had 10 shares, you now have five. A reverse stock split might be made to bring up the share price and in some cases, avoid being delisted as some exchanges have a minimum share price requirement. 2/1 stock split This common stock split is when one share is divided in half. So if you have 50 shares of a stock valued at $50 each, a 2/1 split means you’ll have 100 shares valued at $25 each. This is one of the most common stock splits. 3/1 stock split A 3/1 stock split is when a company splits a stock three ways rather than two. So if you have 100 shares of a stock valued at $30 each, you’ll have 300 shares valued at $10 each. Examples of a stock split Stock splits are not uncommon. In 2022, Alphabet — the parent company of Google — had a 20-for-1 stock split. This is one of the biggest splits in recent history. Amazon also had a 20-for-1 stock split in 2022 and GameStop had a 4-for-1 stock split. Tesla had a 3-for-1 stock split last year as well. Why do companies split their stocks Companies might split their stocks when they believe the share price is too high for most people. By splitting stocks and cutting the price per share, they’re opening up the opportunity for more potential investors to buy into the company. When a company does a reverse stock split, that might be a sign of trouble. This brings the stock price back up and means there are fewer available shares for people to buy. Pros and cons of stock splits Pros More buying opportunities. With the drop in stock price, a stock split can create more buying opportunities for potential investors. It’s more affordable to buyers who would otherwise not be able to afford it. Increase awareness. There might be more attention brought to a company that wasn’t there before the announcement of the stock splitting. Cons Could become volatile. As some investors drop their shares and others start buying, stock splits can cause increased volatility. If you’re playing the long game, it’s important to remember that this is part of the risk involved in investing. Doesn’t increase value. Getting more shares doesn’t mean the value of those shares increase. But if you plan to stay in it for a while, the value could increase as more investors become shareholders. How to watch out for stock splits Stock splits are announced a few weeks before they go into effect. You can explore stock split calendars like this one from Nasdaq. Your broker might also offer a stock split calendar so you can see what the split ratio is and when they become payable. Sometimes these are only available to account holders. Stock splits and fractional investing Fractional investing is when you own a portion of one singular share of a stock. How you buy a fraction of a share depends on what’s offered. You might buy up to a certain dollar amount or you can buy up to a certain amount in fractional shares. Stock splits and fractional investing are a couple of different ways to buy into a company that’s trading at a high dollar amount that’s more than you can afford. But not every company or brokerage offers fractional investing. While you might find this offered at some brokerages, it’s not universally available and at this point. Should you take advantage of stock splits? You might want to think about taking advantage of stock splits if you’re interested in buying into a stock and it’s been too expensive in the past. Stock splitting shouldn’t be the main reason you buy shares of a stock, but it might be a reason to look into investing in one. Frequently asked questions (FAQs) Does it matter to buy before or after a stock split? If you buy a stock before it splits, you’ll pay more per share than what it’ll cost after it splits. If you’re looking to buy into a stock at a cheaper price, you may want to wait until after the stock split. Who benefits from a stock split? Companies who want to expand their shareholders and potential investors both benefit from a stock split. Are stock splits risky? All investments are risky, but some are more risky than others. If you’re looking to buy shares in a stock, you might be taking on more risk compared to other types of investments, like index and mutual funds.The information presented here is created by TIME Stamped and overseen by TIME editorial staff. To learn more, see our About Us page. Companies typically engage in a stock split so that investors can more easily buy and sell shares, otherwise known as increasing the company's liquidity. Stock splits divide a company's shares into more shares, which in turn lowers a share's price and increases the number of shares available. For existing shareholders of that company's stock, this means that they'll receive additional shares for every one share that they already hold."If your current stock is valued at $100 per share and there is a 2-for-1 split, you will have two shares worth $50 each," explains Brian Stivers, investment advisor and founder of Stivers Financial Services.Using Amazon's 20-for-1 stock split as an example, existing shareholders will get 20 shares for each share they currently own. When a company divides each existing share into 20 new shares, that also means that each share is now worth one twentieth of the original value. The market value of the company, however, does not change.In short, Amazon stock is going to become a lot more affordable to the everyday investor who wants in.Though the net value of an existing shareholder's stock doesn't change with a stock split, the new level of demand that can come as more investors purchase the more affordable shares can be beneficial to current investors.The share price would likely increase again as more investors purchase shares, Stivers says, adding that in the long run, current shareholders could see some potential value increases, though perhaps temporary.For current Amazon shareholders, the 20-for-1 stock split also frees up some shares to be sold."With 20 times the share, it would allow you as an investor to diversify further, if you want to liquidate some of the Amazon shares to diversify further into other holdings," Stivers suggests. "This would especially be true if the new split stock increases rapidly in value."It's tempting to want to buy into a pricey stock when it becomes much cheaper to do so; however, eager investors should make sure that stock aligns with their overall investing goals. You shouldn't jump all in just to say you own Amazon stock, for example, unless it's something that has long been a part of your portfolio objectives."If the average investor was attracted to Amazon before the split, then it is probably a good time to invest after the split, as it is more obtainable," Stivers says. "However, you should only do so if it is part of a well-diversified portfolio."A diversified portfolio means that your money is spread out amongst different asset classes (stocks, bonds, real estate, etc.) that react differently to various economic and financial environments. This minimizes volatility while maximizing return opportunity. Robo-advisors can build a diversified portfolio of index funds for you based on factors like your age, risk tolerance and time horizon.Editorial Note: Opinions, analyses, reviews or recommendations expressed in this article are those of the Select editorial staff’s alone, and have not been reviewed, approved or otherwise endorsed by any third party. When Nvidia's (NVDA) stock price soared past $1,200 in 2024, the global chip giant made a change that might puzzle some novice investors: they split their stock 10-for-one, making their stock cheaper. This decision, far from being unique to Nvidia, is typical of firms with highflying stocks that carry out stock splits so their shares are more affordable to a broader range of investors, particularly retail investors who might be deterred by high share prices. Announcing the split, Nvidia said the company wished "to make stock ownership more accessible to employees and investors." A stock split is when a company divides its stock into multiple shares, effectively lowering the price of each share without changing the company's market value. It's akin to cutting a cake into smaller slices; you end up with more pieces, but the total amount stays the same. For instance, in a two-for-one split, an investor who owned one share priced at $100 would end up with two shares, each worth $50 but with the same total value. A stock split is when a company increases the number of its outstanding shares to boost the stock's liquidity.Although the number of shares outstanding increases, there is no change to the company's total market capitalization as the price of each share is split as well.The most common split ratios are two-for-one or three-for-one, which means every share before the split will turn into multiple shares afterward.Reverse stock splits are the opposite, in which a company lowers the number of shares outstanding to raise its stock price. This can increase liquidity (the ability to trade the stock easily) and trading volume. However, a stock split doesn't change the company's value—it simply redistributes ownership into smaller, more affordable units. In addition, some argue that in the age of fractional shares and when so much investing is done by institutions that just look at the total value invested, not the share price, stock splits are becoming obsolete. However, stock splits are still used by companies to make their shares appear more attainable to retail investors. These company actions also tend to signal management's confidence in future growth. Below, we'll explore more about why companies choose this strategy, the mystery behind why the stock's value tends to go up (even as it shouldn't), how this change affects various stakeholders, and what investors should consider when a stock split occurs. When examining historical stock charts, be cautious since many platforms (but not company investor sites) automatically adjust backward the historical prices for stock splits. This means a stock that traded at $1,000 on a specific day historically before a 10-for-one split might show up as $100 in the historical data. Always check if prices are split-adjusted to avoid misinterpreting long-term price trends. Stock splits are labeled reverse or forward, though when used without an adjective, a forward stock split is usually meant. These occur when a company increases the number of its outstanding shares without changing the overall market capitalization. Each shareholder receives additional shares in proportion to their prior holdings, while the value of each share decreases proportionally. The main characteristic of a forward stock split is the increase in the number of shares available in the market. For instance, in a two-for-one split, each share is divided into two, doubling the number of outstanding shares. Similarly, a three-for-one split would triple the number of shares. Along with this increase in share count, the price per share is adjusted downward in line with the split ratio. Thus, if a company carries out a two-for-one split, a share priced at $100 before the split would be priced at $50 afterward. A $90 share would be $30 post-split in a three-for-one split. Despite these changes, the total value of an investor's holdings remains constant. The decrease in the price per share precisely offsets the increase in the number of shares. This principle extends to the company's market capitalization, which remains unchanged before and after the split (except for market shifts). The total value of shares held by all shareholders should stay the same, maintaining the company's market value. When a company performs a forward stock split, the process is seamless for shareholders. The additional shares are automatically credited to shareholders' accounts by their brokers. While a stock split doesn't inherently change a company's value, it can affect market perception and liquidity. The lower share prices resulting from a split may make the stock more accessible to smaller investors, potentially broadening the shareholder base. In addition, the increased number of shares can improve liquidity in the market, making it easier for investors to buy or sell the stock. In a perfectly efficient market, a stock split shouldn't impact a company's total market value or an investor's wealth. The total market capitalization, individual ownership stakes, and fundamental value of the company are unchanged. It's often compared with cutting a pizza into smaller slices—you have more pieces, but not more pizza. However, research has consistently shown that stock splits often result in short-term abnormal returns, with companies experiencing an average 2% to 4% increase in value around the split announcement. Another way of saying this is that, on average, following a stock split announcement, the stock to be split tends to be overpriced relative to its fundamental value. This phenomenon, known as the "announcement premium," has been studied by financial researchers for decades. For reverse splits, researchers have found the opposite of the announcement premium of forward splits: the stock price tends to fall below fundamental value in the short-term.) Several overlapping explanations have been proposed: The best trading range: Companies split their stock to keep the share price within a perceived best range that balances the needs of different investor types. That is, specific prices might appear strange or outlandish to investors. Lower prices attract more investors: A lower post-split price is more accessible to retail investors. Liquidity hypothesis: As we've seen, many argue that stocks trading at lower prices after a split are more liquid, attracting more investors and increasing trading volume. Signaling theory: Stock splits serve as a signal from company insiders of positive prospects. Executives might be indicating their expectations of continued growth and rising stock prices. Attention hypothesis: Stock splits may attract media and analyst attention, increasing visibility and potentially driving demand for the stock. Tick size hypothesis: In markets with fixed minimum price increments, i.e., ticks, splits can effectively increase the relative tick size, potentially benefiting market makers and improving liquidity. Stock splits can affect option contracts. When a stock splits, the option's strike price and number of contracts are usually adjusted to maintain the same total value. If you're holding options during a stock split, you should carefully review how your contracts are affected. Studies have long shown that investors prefer specific nominal price ranges, which companies may be catering to through splits. This research, which has included surveys of investors, has found that investors generally prefer stock prices from $10 to $50 per share. However, these preferences vary across different markets and periods. Here's a summary of findings that relate to this: Stocks can be priced too low: There's often resistance to prices below $5, as some institutional investors have policies against buying "penny stocks" (generally defined as stocks trading below $5). Stocks can seem too pricey: Prices above $100 are often seen as "too expensive" by retail investors, even though this is not necessarily related to the stock's fundamental value. Historical consistency: The average nominal share price on the New York Stock Exchange remained remarkably constant at around $30 to $40 from the 1930s to the 2000s, suggesting a long-term preference for this range. Market differences: The preferred range varies by market. For example, in some Asian markets, lower nominal prices (even below $1) are more common and accepted. Recent trends: With the rise of fractional share investing, some companies have allowed their share prices to rise well above $1,000 without splitting. However, many companies still aim for the traditional $20-$50 range. Post-split target: When companies split their stocks, they often aim for a post-split price in the $30-$50 range. Reverse splits: Companies often carry out reverse splits to bring their share price above $5 or $10, avoiding delisting and improving institutional investors' perceptions. Lower-priced shares after a split seem to be psychologically more appealing to some investors, even though the company's fundamental value hasn't changed. This relates to the concept of "nominal price illusion"—like the "money illusion"—that investors have a cognitive bias to see lower-priced shares as more of a value, no matter that there's no change in the stock's fundamentals. These preferences aren't rational in a purely economic sense, as the nominal share price shouldn't matter. Behavioral finance researchers have been particularly interested in the stock split anomaly since it challenges the efficient market hypothesis. Behavioral finance asserts that people often make financial decisions based on emotions and cognitive biases rather than being rational in their trading decisions. For instance, loss aversion means that investors often hold losing positions rather than feel the pain of taking a loss. In addition to a slight boost between the announcement and the split, researchers have generally found "post-split drift," with "drift" being a term used for this and other events. This refers to how, after a significant corporate event (stock splits and other company announcements), there's still an effect even though, all things being equal, there shouldn't be. This drift for forward stock splits means a slight bump in stock prices afterward. Traders and experts have wanted to understand why. Specialists in behavioral finance have argued that cognitive biases contribute to the announcement premium: Anchoring bias: Investors might anchor to the pre-split price, perceiving the post-split price as "cheaper." Availability bias: The increased attention from a split may make the stock more "available" in investors' minds, potentially driving demand. "Gambling" preferences: When a company splits its stock, the lower post-split price can make the shares appear more like a "lottery ticket" to some investors. An investor might feel they have more upside potential owning 100 shares at $20 each than one share at $2000, even though the total investment is the same. Overconfidence: Retail investors overestimate their ability to profit from perceived "cheaper" shares post-split. Representative heuristic: Investors might associate stock splits with successful, growing companies, leading to undue optimism. While none of these suggest entirely rational decisions by traders, a more prosaic and far less flattering depiction of investors is just that they don't do math well. For this reason, some may struggle to adjust their valuation models properly for the new share structure enough to produce the anomaly. The frequency of stock splits has decreased significantly since the late 1990s. This decline coincides with the rise of algorithmic trading, the selling of fractional sales, and the acceptance of such prices by institutional investors. The first obvious implication to remember is that while stock splits may generate short-term price movements, they do not change a company's underlying value or an investor's percentage ownership. The change should be cosmetic. That said, given the findings of an announcement premium, there might be prospects for taking advantage of mispricings around splits. A reverse stock split is when a company reduces its outstanding shares by combining multiple shares into one, resulting in a proportionally higher price per share. This is the opposite of a forward stock split, where a company increases its share count while decreasing the price per share. Here are the most important characteristics of a reverse split: Decrease in outstanding shares: The primary feature of a reverse split is to lower the total number of shares in circulation.Higher share price: Shareholders receive fewer shares than they previously held, but the value of each share increases proportionally.Unchanged market capitalization: All things being equal, the company's total market value should remain the same since the increase in share price offsets the reduction in share count.Ensures compliance with exchange rules: Often used to increase a stock's price to meet the minimum price major exchanges require for remaining listed.Negative perceptions: Reverse splits can sometimes be viewed unfavorably by investors, as they may indicate financial distress or lack of confidence in future growth. For example, suppose a company with 10 million shares outstanding trading at $5 per share carries out a one-for-five reverse split. In this case, the number of shares will be reduced to 2 million (10 million ÷ 5), with each share priced at about $25 ($5 × 5). However, the company's market capitalization should remain at $50 million ($5 × 10 million = $25 × 2 million). A reverse/forward stock split is a special stock split strategy to eliminate shareholders holding less than a certain number of shares. A reverse/forward stock split consists of a reverse stock split followed by a forward stock split. The reverse split reduces the overall number of shares a shareholder owns, causing some shareholders who hold less than the minimum required by the split to be cashed out. The forward stock split then increases the number of shares owned by the remaining shareholders. In a stock split, there are three pivotal dates that investors should be aware of: the announcement date, the record date, and the distribution date (also known as the effective date). The announcement date is when the company publicly declares its intention to split its stock, often causing an immediate market reaction.The record date is the day the company determines which shareholders are eligible to receive the additional shares from the split; investors must own the stock before this date to participate in the split.Finally, the distribution date is when the new shares are actually issued and begin trading at the post-split price. While an investor must own shares by the record date to be eligible for the split, shares typically trade at the pre-split price until the distribution date. The time between these dates can vary, but companies usually provide this information in their split announcement to help shareholders and potential investors plan. Some successful companies have never split their stock. Berkshire Hathaway's Class A shares (BRK.A) have never been split and traded at over $675,000 per share in September 2024. Let's summarize the advantages companies see when going through the hassle and expense of a stock split. First, a company often decides on a split when the stock price is relatively high, making it expensive for investors to acquire a standard board lot of 100 shares. Second, the higher number of shares outstanding can result in greater liquidity for the stock, which facilitates trading and may narrow the bid-ask spread. Increasing the liquidity of a stock makes trading in the stock easier for buyers and sellers. This can help companies repurchase their shares at a lower cost since their orders will have less impact for a more liquid security. While a split, in theory, should have no effect on a stock's price, it often results in renewed investor interest, which can positively affect the stock price. While this effect may wane over time, stock splits by blue-chip companies are a bullish signal for investors. Some may view a stock split as a company wanting a bigger future runway for growth; for this reason, a stock split generally indicates executive-level confidence in the prospect of a company. In the U.K., a stock split is called a scrip issue, bonus issue, capitalization issue, or free issue. However, stock splits have disadvantages. One of the primary drawbacks is the cost involved: legal fees, paperwork, and shareholder communications. These costs can be substantial for smaller companies. Another disadvantage is a potential increase in the stock's volatility. Lower-priced shares resulting from a split may attract more speculative trading, potentially leading to greater price shifts. This increased volatility is often undesirable for all companies or investors. There's also a risk that the positive effects of a stock split may be short-lived. While splits often lead to a brief surge in stock price and trading volume, these effects tend to diminish over time. Any gains will likely be temporary if the underlying business fundamentals don't support the optimism generated. In addition, in an era of fractional share investing, when investors can buy partial shares, the practical benefits of stock splits for increasing accessibility have been reduced. This seems to have made splits less impactful or necessary. Lastly, frequent stock splits might be seen as a form of financial engineering rather than a focus on fundamental business growth. In August 2020, Apple (AAPL) split its shares four-for-one. Right before the split, each share was trading at around $540. After the split, the price per share at the market open was $135 (approximately $540 ÷ 4). An investor who owned 1,000 shares of the stock pre-split would have owned 4,000 shares post-split. Apple's outstanding shares increased to over 15 billion, while the market capitalization continued to fluctuate, rising to over $3 trillion in September 2024. A company may split its stock as many times as it would like. For instance, Apple also split its stock seven-for-one in 2014, two-for-one in 2005, two-for-one in 2000, and two-for-one in 1987. To convert a quantity of pre-split shares to post-split shares across multiple splits, multiply the ratio value of each split together. For example, a single pre-split AAPL share in 1987 would have eventually been split into 224 shares after the 2020 split. This is determined by multiplying four, seven, two, two, and two. Calculating the cumulative effect of a company's stock splits over time begins by identifying each split event to determine its impact on share count and price. Then you apply each split ratio consecutively to the original share count. For example, if a company has had a two-for-one split followed by a three-for-one split, the original number of shares would be multiplied by six (2 × 3). The share price adjusts inversely to maintain the same market capitalization, that is, it would be one-sixth what it was, all else being equal. Let's look at Walmart Inc.'s (WMT) May 1971 stock split as an example. This information is found on Walmart's investor website. We'll suppose you owned 200 shares of the stock on that day: Stock split ratio: Two-for-oneOriginal number of shares: 200Original cost per share: $8.25Market price on the day of the split: $47.00 Step-by-Step Calculation: Note the stock split ratio: A two-for-one stock split means investors will now hold two shares for every share owned. The number of shares doubles while the price per share is cut in half.Calculate the new number of shares: New shares = Original shares × split ratio = 400 (200 × 2).Adjust the share price: New Price = Original Price ÷ Split ratio $23.50 ($47.00 ÷ 2)Verify the values are consistent: Before split: 200 shares × $47.00 = $9,400. After split: 400 shares × $23.50 = $9,400 No. Receiving more of the additional shares will not result in taxable income under U.S. law. The tax basis of each share owned after the stock split will be half what it was before the split. Stock splits are generally done when the stock price of a company has risen so high that it might become an impediment to new investors. So, a split is often the result of growth or the prospects of future growth, and it could be a positive signal. In addition, the price of a stock that has just split may see an uptick if the lower nominal share price attracts new investors. Stock splits neither add nor subtract fundamental value. The split increases the number of shares outstanding, but the company's overall value does not change. Immediately following the split the share price will proportionately adjust downward to reflect the company's market capitalization. If a company pays dividends, the dividend per share will be adjusted, too, keeping overall dividend payments the same. Mutual funds can undergo splits, but they work differently than individual stock splits and occur less frequently. Mutual fund splits typically occur when the price per share is too high, making the fund less accessible to smaller investors. In a mutual fund split, the number of shares an investor owns increases while the net asset value per share decreases proportionally, just like a stock split. Stock splits are corporate actions that alter the number of outstanding shares and their price without changing a company's fundamental value or market capitalization. While theoretically neutral events, stock splits often generate a positive market reaction because of increased accessibility, perceived growth signals, and behavioral factors. Companies typically carry out splits to keep share prices within a preferred range, potentially boosting liquidity and broadening their investor base. Meanwhile, reverse splits are often used to avoid delisting or improve institutional appeal. While splits may lead to short-term price movements and increased trading, they don't change a company's underlying worth or an investor's proportional ownership. Investors should focus on a company's fundamental business prospects rather than being swayed by the cosmetic changes of a stock split. However, being aware of split dynamics can provide insight into how market psychology often affects prices. It can also potentially help you locate mispricing opportunities. There are various ways in which companies can manipulate their share price. One of these ways is implementing a corporate action called a stock split. The following guide, illustrated by examples, will look at how this process works, how it is applied, and how it can affect an investor’s portfolio.   Highly Rated Stock Trading & Investing Platform Invest in stocks, ETFs, options and crypto Copy top-performing crypto-traders in real time, automatically. 0% commission on buying stocks - buy in bulk or just a fraction from as little as $10. Other fees apply. For more information, visit etoro.com/trading/fees. eToro USA is registered with FINRA for securities trading. 30+ million Users worldwide eToro is a multi-asset investment platform. The value of your investments may go up or down. Your capital is at risk. Don’t invest unless you’re prepared to lose all the money you invest. This is a high-risk investment and you should not expect to be protected if something goes wrong. Take 2 mins to learn more. A stock split occurs when a company decides to increase the number of shares outstanding to boost the stock’s liquidity. Though the number of shares increases, the overall value of shares outstanding stays the same because the split does not fundamentally change the company’s value. When a company goes through a split, it will use a particular split ratio to indicate how many new shares each outstanding share will be divided into. The most standard forward (or conventional) split ratios are 2-for-1 (2:1) or 3-for-1 (3:1), which means investors will receive two or three shares, respectively, for each share they held beforehand. A company might also decrease the number of outstanding shares, increasing the share price. As the name suggests, this technique is called a reverse stock split. So, in a 2:1 reverse stock split, a company would merge two shares into one, which means investors will receive one share for the two they held before. Read also:Stock Trading for BeginnersDividend Investing for Beginners10 Best Stock Trading Books15 Top-Rated Investment BooksWhat is Investing? Highly Rated Stock Trading & Investing Platform Invest in stocks, ETFs, options and crypto Copy top-performing crypto-traders in real time, automatically. 0% commission on buying stocks - buy in bulk or just a fraction from as little as $10. Other fees apply. For more information, visit etoro.com/trading/fees. eToro USA is registered with FINRA for securities trading. 30+ million Users worldwide eToro is a multi-asset investment platform. The value of your investments may go up or down. Your capital is at risk. Don’t invest unless you’re prepared to lose all the money you invest. This is a high-risk investment and you should not expect to be protected if something goes wrong. Take 2 mins to learn more. A stock split is a way for companies to change the per-share price without changing market capitalization. Market capitalization (cap) refers to the total value of a company’s issued stock. It is calculated by multiplying the price per stock by the total number of shares outstanding. For instance, let’s imagine Company A has 10 million shares outstanding, and the stock is trading at $50 per share. Its market cap will be $500 million (10 million multiplied by 50). Now, the company’s board of directors has decided to split the stock 2-for-1. Immediately after the split is implemented, the number of shares outstanding would double to 20 million. By contrast, the share price would be halved to $25, leaving the market cap unchanged at $500 million (20 million times 25). Therefore, while the number of outstanding shares changes, the company’s overall valuation and the value of each shareholder’s stake remain the same. So if an investor has one share of a company’s stock valued at $10, after a 2-for-1 stock split, they would have two shares of stock at $5 each. The two shares combined are worth the same as the one you started with, and the value of your investment remains unaffected. 4-for-1 stock split vs. 1-for-4 reverse stock split. Source: Finbold.com Many public companies implement a stock split after the share price has exhibited significant growth. Reducing the trading price into a more comfortable range will make their stock look more attractive from a per-share price and encourage investors to buy it. Basically, most investors might be more willing to buy, say, 100 shares of a $10 stock instead of 1 share of a $1,000 stock. This is because 100 shares are considered a board lot, a standardized number of securities defined as a trading unit by a stock exchange. Furthermore, companies will often split their stock to create more liquidity. The higher the number of shares outstanding, the greater the liquidity, facilitating trading and narrowing the bid-and-ask spread. Increasing the liquidity makes it easier for investors to buy and sell the stock without too substantial an effect on the share price. Moreover, it can help companies buy back their own stock at a lower price since their orders would not push up the share price of a more liquid stock as much. A company can decide to split the stock by any ratio. For example, a stock split may be 2-for-1, 3-for-1, 10-for-1, 100-for-1, etc. A 3-for-1 split means there will now be three shares for every one share held by an investor; namely, the number of outstanding shares in the market will triple. However, the cost per share after the 3:1 split will be divided by three, keeping the value of the stock the same.   A stock split is normally an indication that a company is thriving and its stock price has increased. Though theoretically, it should not affect a stock’s price, it often results in renewed investor interest, which can positively influence the stock price. While this effect may wither over time, splits by blue-chip companies (established, stable, and well-organized corporations) are a bullish signal for investors. There is no particular advantage for those that already own stock at a company that has split its stock; the value of their shares will not change. Nevertheless, a stock split can motivate those interested in becoming shareholders to buy. And while the ability for more investors to buy in can bump up the stock price, this usually is only a temporary change driven by the increase in demand.   In August 2020, Apple (NASDAQ: AAPL) split its shares 4-for-1. Right before the split, each share was trading at around $540. Post-split, the share price was $135 (approximately $540 divided by 4). As a result, Apple’s outstanding shares grew from 3.4 billion to about 13.6 billion, while the market capitalization remained practically unchanged at $2 trillion. A shareholder would hold four shares of AAPL for each previously held share. In another stock split example, in July 2022, Alphabet Inc. (NASDAQ: GOOGL), the parent company of Google, executed a 20-for-1 stock split. Prior to the split, each share was trading at approximately $2,400. Following the split, the price of each share adjusted to around $120 (approximately $2,400 divided by 20). As a result, Alphabet’s outstanding shares increased significantly, while its market capitalization stayed essentially the same. This meant that for every share of Alphabet stock an investor held before the split, they would then hold 20 shares post-split, although the total value of their holdings remained unchanged. In June 2024, NVIDIA (NASDAQ: NVDA) executed a 10-for-1 stock split. Prior to the split, NVIDIA’s stock was trading at approximately $1,200 per share. After the split, the share price adjusted to around $120 ($1,200 divided by 10). As a result, shareholders received nine additional shares for every share they previously owned. A reverse stock split is the opposite of a stock split (also known as a forward stock split). A reverse stock split occurs when a company consolidates the number of existing shares of stock into fewer higher-priced shares. Like with a forward split, the market value of a company after a reverse split stays the same. A company would primarily pursue this corporate action to bump its per-share price. Firstly, to avoid being delisted from a stock exchange for not meeting the minimum bid price required for a listing. Secondly, to attract big investors, as many institutional investors and mutual funds have policies against investing in stocks priced below a preset minimum per share. Another reason a company might opt for a reverse split is to make its stock look more appealing to investors who may regard higher-priced shares as more valuable. A reverse stock split can often signify a company in distress and is not perceived positively by market participants. It is usually an indicator that the stock price has plummeted, and the company’s board of directors is attempting to inflate the prices artificially without any fundamental business proposition. Furthermore, as the number of shares is reduced on the market, the stock’s liquidity is generally also affected, making the stock more volatile for traders. Ultimately, a stock split or a reverse split does not affect the company’s intrinsic value, so it won’t have a substantial practical impact on its current investors. Nonetheless, a stock split can indicate to investors that a company is thriving, in contrast to a reverse split which often suggests a company is experiencing some turbulence.   A stock split’s most significant impact is on new investors, eyeing up a particular stock and hoping to purchase a round lot of shares at a lower cost. Thus, a stock split can provide a powerful motivator to get in the action. Disclaimer: The content on this site should not be considered investment advice. Investing is speculative. When investing, your capital is at risk. After a split, the stock price will decline since the number of outstanding shares has increased. This, however, does not change the market capitalization of a company, and the value of your held shares will remain the same. The most standard stock splits are traditional stock splits, such as 2-for-1 and 3-for-1. For example, in a 2-for-1 stock split, a shareholder receives two shares after the split for every share they owned before the split. In a 3-for-1 split, they receive three shares for every share. However, split ratios can go various ways, including 20-for-1, 100-for-1, etc. A frequent reason for a stock split is toto make shares more affordable for investors. This can increase liquidity, broaden the shareholder base, and make the stock more attractive to small investors. It doesn’t change the company’s overall value, but it can promote more active trading and accessibility of the stock. A stock split makes the stock more accessible and appealing, particularly to small investors, and is often seen as a positive sign reflecting the company’s growth or potential for future growth. Additionally, the post-split lower nominal share price can attract new investors, possibly leading to an uptick in the stock’s value due to increased demand. Indeed, a 2-for-1 stock split increases the marketability of the stock because it usually occurs after the company’s stock price has risen significantly, potentially deterring new investors with higher per-share costs. Stock splits can lead to increased administrative costs, create potential investor confusion, possibly result in perceived lower company value due to reduced share price, and might increase stock volatility without adding real value to the company. A reverse split reduces a company’s outstanding shares increasing per-share value. It is typically done to avoid being delisted from an exchange if the stock is nearing the minimum share price allowed on that exchange. As a result, it might be wise to steer clear of investing in a stock that has recently undergone a reverse split. A stock split increases the number of shares by splitting each existing share into multiple shares, reducing the share price but not changing the total value of holdings. A stock dividend is a payment made in additional shares based on the number of shares already owned, reflecting a distribution of earnings. Both increase the number of shares but have different implications and reasons. Warren Buffett has avoided splitting Berkshire Hathaway’s Class A shares (NYSE: BRK.A) because he believes their high price discourages short-term trading and aligns with his focus on attracting long-term investors committed to building intrinsic value. However, to make the company more accessible, he introduced Class B shares (NYSE: BRK.B) in 1996, which have been split in the past to accommodate retail investors while preserving the core philosophy of the company. Highly Rated Stock Trading & Investing Platform Invest in stocks, ETFs, options and crypto Copy top-performing crypto-traders in real time, automatically. 0% commission on buying stocks - buy in bulk or just a fraction from as little as $10. Other fees apply. For more information, visit etoro.com/trading/fees. eToro USA is registered with FINRA for securities trading. 30+ million Users worldwide eToro is a multi-asset investment platform. The value of your investments may go up or down. Your capital is at risk. Don’t invest unless you’re prepared to lose all the money you invest. This is a high-risk investment and you should not expect to be protected if something goes wrong. Take 2 mins to learn more. A stock split is the act of dividing a company's outstanding commons shares into a larger number of shares. If a company had a three-for-one-split, for example, and a shareholder held 100 shares before the split, they would own 300 shares after the split. But the value of the company equity owned by the shareholder would remain the same, only the number of units held would differ as the share price changes accordingly. Share splits are subject to the approval of the company's shareholders.