

## **Ex-Dividend Day Stock Price Behaviour - Evidence from Colombo Stock Exchange**

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Efficient market is one in which prices fully reflect available information. Implication of an efficient market is that no excess returns can be made since current prices already reflect all available information. Recent research supports the hypothesis that CSE is not a semi-strong market and as a result there is a possibility for investors to make abnormal gains. The objectives of this paper was to identify ex-dividend price behaviour of stocks at the CSE and to identify suitable trading strategies around ex-dividend day to exploit this anomaly.

A sample of 85 listed companies' with 470 ex-dividend events were selected covering the period January 2003 to December 2012. Relative Liquidity Ratio (RLR) was used to divide the sample into two groups to control for liquidity. Initially the stock price behaviour on ex-dividend day was examined using Raw Price Ratio (RPR), Raw Price Drop Ratio (RPDR) and Market Adjusted Price Drop Ratio (MAPDR). Thereafter, the event study methodology was used to examine the abnormal returns and abnormal volumes on and around ex-dividend day using the market model, mean adjusted returns model and market adjusted returns model.

The findings from RPR, RPDR and MAPDR implied that the stock prices drop by less than dividend on the ex-dividend day. The results from the event study implied significant positive abnormal returns and volumes on and around ex-dividend day. This finding is consistent with the short term trading hypothesis, but could not be explained by the taxation hypothesis. Further, the results indicated that for the liquid stocks there are significant negative abnormal returns on cum-dividend day followed by significant positive abnormal returns on ex-dividend day. For the least liquid stocks there are significant positive abnormal returns on ex-dividend day followed by significant negative abnormal returns on the following day. These results also confirm that the CSE is not information efficient and investors have the opportunity to make unusual gains by trading around ex-dividend day.

*Key words: Ex-dividend, price behavior, Sri Lanka*