How to Predict Where the Market Will Open

By LISA SMITH Updated February 14, 2022

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After all, it's the closing price that tells you how much money you have gained or lost in your portfolio for the day. There's more to the behind-the-scenes story than you might expect.

KEY TAKEAWAYS

- Trading stocks takes an abrupt halt each trading afternoon when the markets close for the day, leaving hours of uncertainty between then and the next day's open.
- Predicting where the market will resume trading at the open can help investors both hedge risk and place bets on the next day's price action.

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Full Bio

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Key Takeaways

- Trading stocks takes an abrupt halt each trading afternoon when the markets close for the day, leaving hours of uncertainty between then and the next day's open.
- Predicting where the market will resume trading at the open can help investors both hedge risk and place bets on the next day's price action.
- After-hours trading in stocks and futures markets can provide a glimpse, but these tend to be less liquid and prone to more volatility than during regular trading hours.
- For a better picture, investors look to international markets that are open while the U.S. is closed and to economic data released by countries, or figures released by companies.

Predicting the Likely Direction of the Market Open

Before we get into why some investors closely track the open's likely direction, let’s look at a few indicators that help them with the task.

While the financial markets have clearly stated business hours, developments outside of those hours continue to influence both the value of securities and investor behavior. Geopolitical events and natural disasters, for example, can occur at any time. Events like the assassination of a sitting president or a major terrorist attack are likely to indicate a significantly lower market open.

Corporate data also plays a role. Earnings announcements made after the close or before the open in key companies can influence the market’s direction. During January, April, July, and October, the vast majority of firms release their results for the quarter. Good news from a bellwether firm often leads to a higher stock market open while bad news can have the reverse effect.

Other important news comes out before the markets open. A wide variety of economic releases, including employment data, retail sales, and gross domestic product results, are released at 8:30 a.m.1 Once again, both good news and bad news can sway the market open direction.

After-Hours Trading

After-hours trading activity is a common indicator of the next day's open. Extended-hours trading in stocks takes place on electronic markets known as ECNs before the financial markets open for the day, as well as after they close.

Such activity can help investors predict the open market direction. In fact, gauges such as the Nasdaq-100 Pre-Market and After-Hours Indicators are designed to track extended hours activity specifically for this purpose.

Likewise, trading virtually 24 hours a day, index futures can indicate how the market will likely trend at the start of the next session. S&P 500 futures are often used by money managers to either hedge risk over a certain time period by selling the contract short, or to increase their stock market exposure by buying it.

Unlike the stock market, futures markets rarely close. Futures contracts trade based on the values of the stock market benchmark indexes they represent. S&P 500 futures trade based on the value of the Standard & Poor's 500, just as Dow futures trade based on the value of the Dow Jones Industrial Average.

Since the securities in each of the benchmark indexes represent a specific market segment, knowing the direction of pricing on futures contracts for those indexes can be used to project the direction of prices on the actual securities and the markets in which they trade. If S&P futures are trending downward all morning, it is likely that stock prices on U.S. exchanges will move lower when trading opens for the day. Once again, the opposite is also true, with rising futures prices suggesting a higher open.

In addition to offering market access almost 24 hours a day, a major benefit of futures is their high liquidity level after-hours compared with stocks traded on ECNs. This liquidity affords tighter spreads, which are critical because the wider the spread, the more a trade has to move in your favor just to break even.

How International Markets Can Influence the Open

When domestic markets are closed for the day, international markets are open and trading. A good day in Asian markets can suggest that U.S. markets will open higher. Devastating losses overseas can lead to a lower open at home.

By paying attention to foreign developments, domestic investors can get an idea about what direction they can expect local markets to move when they open for the day. Major stock exchanges in Tokyo, Frankfurt, and London are often used as barometers for what will happen in the U.S.

Serious market watchers wake up early, pull the data, and use these various indicators singly and in combination to predict the direction of the opening moves in the U.S. market. Less ambitious investors just check in on social media sentiment or tune in to the morning financial news broadcasts to hear the talking heads provide an update on expectations for the day. Either way, it is possible to get a fairly solid reading on what to expect when U.S. trading starts for the day.

Why the Direction of the Open Is Important

Market direction presents opportunity. At a broad level, if markets are set to rise, individual stock prices are likely to do so as well. Short-term traders can make buy/sell decisions based on the information. For instance, if markets are set to rise and then a technology company releases good news before the opening bell, that company's stock is likely to rise at the open.

For investors who hold the stock, this could be a signal to sell existing holdings and lock in profits. For investors who don't own the stock, it could be a signal to buy early and sell into a rising market. Keep in mind that if you only have a few dollars to invest, the exercise in tracking market direction may be meaningless.

On the other hand, if you can buy 100,000 shares that rise two cents each, you could make a quick $2,000 (ignoring transaction costs)—not bad for an hour's work. If you can buy 500,000 shares that rise 10 cents, you could make a quick $50,000, and the numbers go up from there. For big institutional traders, there's serious money to be made on these moves. In an era of rapid-fire electronic trading, even price movement measures in a fraction of a cent can result in big gains for deep-pocketed traders who make the right call.

The Bottom Line

Accurately predicting the stock market’s opening moves can be a useful tool. If your projection is accurate, you have an opportunity to profit. Of course, the first step is to correctly gauge the market direction. That step alone isn’t enough to make money.

You also need to select an investment and successfully gauge the resulting impact that the market’s move will have on your investment in order to make money. You may not make the right guess on the market’s direction, and the market may move against you.

Even if you get the direction right, you also need to be correct on your investment to generate a profit. Simply put, there are no guarantees that you will get the direction right or that your investment will pay off.

As with all investment strategies, you should conduct a thorough analysis while understanding your strategy and its implications before you place a bet on the direction of the open.