

Does the ASX Always Follow the US?

There is a very commonly held belief that the Australian market **almost always** reacts to and therefore follows the direction of the US stock market. For quite some time I have felt that this belief was questionable. I decided to make the time to research it. What I found out may surprise some readers.

An immediate problem was whether this vague belief was based on the opening price or the closing price for the day following trading on the US market. I have reservations about the opening price for ASX indices. I don't really understand exactly how they are calculated. In particular the opening values for the indices are available before the market is fully open. This means that it only reflects changes in the stock(s) that will open first, rather than an across-the-market opening.

I decided that I would use only closing prices in the comparison. If readers are of the view that I made a wrong decision here, they are welcome to do their own research based on the opening index values. However, I feel that the open will always be suspect in the sense that it does not reflect the entire market.

I also decided that I would start my research from January 2007. I chose this as being the last year of the last bull market. Exactly when the bull market ended and the bear market began is thus avoided.

The other problem was what to do when there were public holidays. The decision I made was to compare the ASX direction to the US direction on the last day that the US market traded before the relevant day on the ASX. This might be across more than a two-day weekend at times, but they are fairly rare.

The indices that I chose to compare were:

ASX: The All Ordinaries index

US: The S&P500 index.

I felt that these indices were reasonably comparable. I could have used the ASX200, but my feeling (not tested) is that its direction tends strongly to be the same as the All Ordinaries except on days when the change from the previous day is quite small.

What I have found is this:

1. Over whole the period January 2007 through June 2011, the

Days when XAO closes in the same same direction as the S&P500 on the preceeding day

Month	Same	Different	% Diff	Av %Diff
Jan-07	11	8	42	
Feb-07	9	10	53	
Mar-07	14	8	36	
Apr-07	10	8	44	
May-07	16	6	27	
Jun-07	16	4	20	
Jul-07	14	7	33	
Aug-07	20	3	13	
Sep-07	13	6	32	
Oct-07	16	7	30	
Nov-07	25	6	19	
Dec-07	15	4	21	31
Jan-08	11	9	45	
Feb-08	18	2	10	
Mar-08	17	2	11	
Apr-08	13	8	38	
May-08	10	10	50	
Jun-08	15	5	25	
Jul-08	16	6	27	
Aug-08	16	6	27	
Sep-08	14	7	33	
Oct-08	16	6	27	
Nov-08	16	3	16	
Dec-08	11	10	48	30
Jan-09	15	4	21	
Feb-09	13	6	32	
Mar-09	16	6	27	
Apr-09	15	5	25	
May-09	17	3	15	
Jun-09	19	2	10	
Jul-09	18	4	18	
Aug-09	15	6	29	
Sep-09	16	4	20	
Oct-09	18	4	18	
Nov-09	9	11	55	
Dec-09	18	3	14	24
Jan-10	14	4	22	
Feb-10	14	5	26	
Mar-10	19	4	17	
Apr-10	14	5	26	
May-10	15	6	29	
Jun-10	15	5	25	
Jul-10	16	5	24	
Aug-10	16	6	27	
Sep-10	12	9	43	
Oct-10	15	6	29	
Nov-10	16	5	24	
Dec-10	14	7	33	27
Jan-11	13	5	28	
Feb-11	12	7	37	
Mar-11	15	8	35	
Apr-11	7	11	61	
May-11	14	7	33	
Jun-11	16	5	24	
Average Difference			29	

direction of the ASX was ***different to the US 29% of the time.***

2. The month with the ***lowest*** number of days where the direction was different was June 2009 when only ***10% of days*** saw a different direction on the ASX.
3. The month with the ***highest*** number of days where the direction was different was April 2011 when ***61% of days*** saw a different direction on the ASX.

My general conclusion is that there is a strong correlation in direction, but it is not a certainty by any means. We therefore need to be very careful in basing short term buy and sell timing decisions on the direction of the ASX based on the overnight direction of the US market. The range of likely outcomes is too great for a confident prediction.

Before we finish, let me point out something else. I have only researched direction in the sense that the markets closed up or they closed down. I have not looked at whether days where the US market has moved by more than a certain percentage change is more or less likely to mean the ASX will follow its direction. I readily admit that this is possible, but I have not researched it. The main reason is that I would not use such information myself because of my timeframe as an investor, so it is not worth my time to do the analysis.

However, if any reader is interested to do such an analysis, I would be very interested to know the results and would be willing to publish them if the reader wishes to make the results more generally available.

On the previous page, I have shown the month-by month and overall average results of my research. I have also calculated an average for each of the years, which do not differ hugely (the range is 24% to 31%) from the overall average of 29%.

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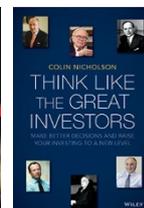
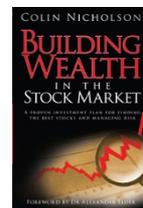
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