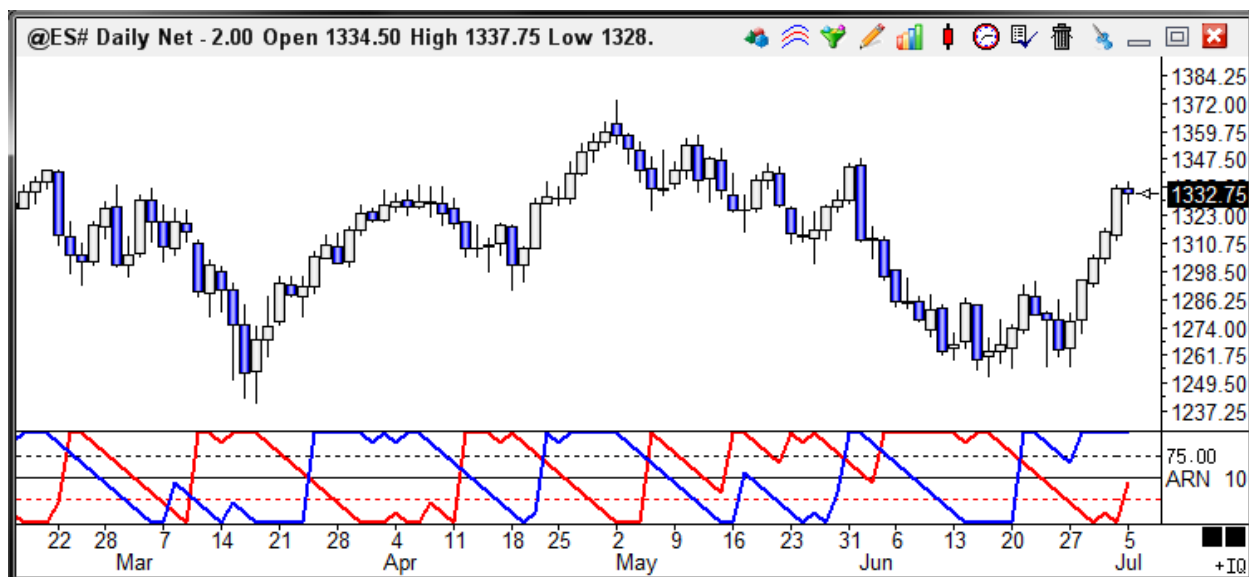


Aroon Indicator

The Aroon Indicator is displayed on a scale of 0 to 100%. Two lines are normally displayed (the Aroon Up line and the Aroon Down line). The study finds the Highest Close and Lowest Close within a specified number of bars (example, within the last 10 bars). If the Highest Close is found in the current bar, then the Aroon Up line will be at 100%. If the Highest Close is found on the first bar of the set, then the Aroon Up line will be at 0. If the Highest Close is found somewhere in the middle of the set, then a percentage between the start and end of the set is calculated. For example, if the Highest Close is exactly in the middle of the set of bars, then the Aroon Up line will have a value of 50. If the Lowest Close is found in the current bar, then the Aroon Down line will be at 100%. If the Lowest Close is found on the first bar of the set, then the Aroon Down line will be at 0. Note: A different Data Point (other than the Close price) can be selected if desired.



If the Aroon Up line goes to the top of the range there is a possibility of an up trend beginning. If the Up line stays between the 100 and the 70 values then an up trend is in motion. The closer it remains to the top, the stronger the trend. If the Up line moves down breaks through the 50% line, then the trend is weakening. If it reaches the bottom of the range, then the up trend is usually over and a downtrend may have started. In summary, a strong trend is likely happening if the Up line goes to the top and stays there. A failing trend is likely if the Up line pulls back to the 50% threshold, and a possible reversal to a down trend if it falls below the 30% threshold. Reverse logic is true for a down trend using the Aroon Down line.

Credits

Developed by Tushar Chande

Aroon Trading System

The Aroon Indicator is supposed to allow you to anticipate changes in price from trending to trading range. At first glance the indicator looks very complicated and seems to make no sense. With a little time, education, and experience I have found it to be most enlightening.

The description of how the Aroon Indicator works is fascinating stuff. It 'measures the number of periods that have passed since the most recent x-period high and x-period low. Therefore, the Aroon indicator consists of two plots; one measuring the number of periods since the most recent x-period high (Aroon Up) and the other measuring the number of periods since the most recent x-period low (Aroon Down).' Now I am almost sure that most of the people reading this article are just eagerly awaiting a further discussion of how the indicator is plotted in a Stochastic like scale etc, etc, etc. Yeah sure. Just in case you are really interested, a more complete discussion of the indicator can be found on the Internet using a Google search.

We are traders, and as such it is extremely important to know how to use indicators to our advantage. I have never felt the need to be thoroughly educated on how the thing works. Just give it to me and let me play with it long enough and I will either make it work or throw it away because it is impossible to figure out. Right? Ok, I have been playing with the Aroon for a few days and I think I have figured out a way to use it which I will share with you.

As you can see below the Aroon consists of two lines. One red (the Up line), and one blue (the Down line). In the system description there is a discussion about three thresholds. Those being the 70, 50, and 30 thresholds. I have discovered that if I pay attention primarily to the red line's relationship to these thresholds I can determine what the market is telling me about trend. It also begins to become clear that I can use this indicator to trade. In fact I can almost make a complete system out of the indicator.

Rule #1: If the red up line goes to the top of the range (Window) there is a possibility of an up trend beginning. If the red up line stays generally between the top of the window (100) and the 70 threshold marked by the orange line on the example chart, the up trend is in motion. The closer it remains to the top the stronger the trend.

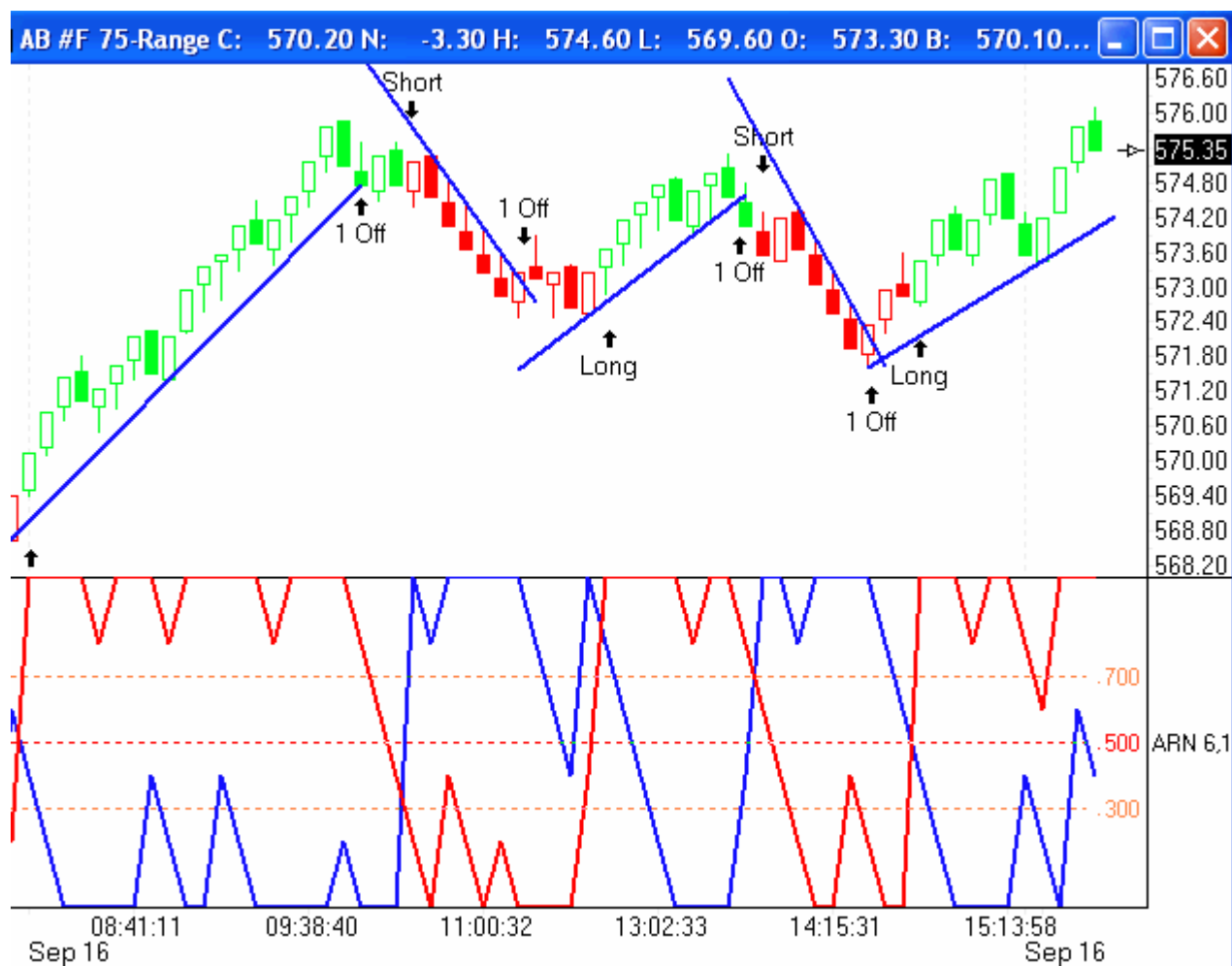
Rule #2: If the red up line retraces to and breaks through the 50% line (red dashed line) the trend is in serious trouble. If it reaches the bottom of the scale/window, the trend is usually dead and a down trend may be beginning.

Rule #3: If the red and blue lines separate and remain separated the trend is strong and I aggressively add contracts on price pull backs.

So, in summary, what we have is a strong trend if the red line goes to the top and stays there, a failing trend if it pulls back to the 50% threshold and a possible reversal into a down trend if it falls below the 30% threshold. The reverse is true for a down trend. If the red line breaks up through the 50% line the down trend is weakening, etc.

So how do we trade this thing? I have discovered that if I merely watch the relationship between the red and blue lines I can use their crossovers for entry and exit signals. Look at the chart below which I have marked up with arrows for the entries to trades. This is real data for Sep 16th and the trades worked as advertised. The day produced over 10 points in the AB. You can see that the red line races to the top immediately after the opening, crossing the blue line in the process. That crossing of the blue

line is a long entry. Then the red line stays generally above the 70% threshold and the price continues to rise. Note how the red and blue lines are separated through most of the up move. That indicates a strong trend in progress and I would buy more contracts as the price pulls back and hooks.



When the red line breaks the 50% line you can remove at least one contract if you are trading multiple contracts and if you are trading a single contract, go flat with the crossing of the 50% line. In the example chart, you'll notice that the red line again crosses the blue line on its way to the bottom of the window. You can sell that crossing and go short. As long as the red line stays below the 50% line you can stay in the short trade.

That's it in a nut shell for the Aroon indicator. I do a couple of other things to help with entries and trade management. Look at the chart and you can see I have placed the [Auto Trend](#) lines on the chart example. I think you can see that it is very beneficial to have these on the chart. I trade multiple contracts and I use the Trend lines to 'take one off' when the price closes on the other side of a trend line and I reverse the trade when the Aroon red line crosses the blue line, which when it happens correctly, occurs quickly after the trend line break by the price. Obviously you can reverse the trade if you wish on the trend line break, but I have seen those trend lines do a nasty little adjustment thing on occasion and that's not fun to get caught in one of those, so I generally wait for the Aroon to confirm the

Trend line break and reversal. It is considered aggressive style to reverse the trend line breaks and you may get whipsawed more often doing that than waiting for the Aroon.

When the market is moving normally this system will catch all the winners and cut losers fairly quickly due to the action of the Aroon and the price action around the trend lines. I use a 0.75 range chart to trade with this indicator. I'm sure other time frames will work with the Aroon but the settings should be tailored to the time frame. Give it a try and see if you like it.

Article by Jay West