

ADX

Wells Wilder developed the ADX, and outlined it in his classic book "New Concepts in Technical Trading Systems". The ADX indicator indicates the strength of the trend without telling you the direction of the trend (upward or downward). It's not a bullish/bearish signal generator.

Determining the Strength of the Trend

The ADX is a momentum indicator, which aims to measure the strength of the trend - and attempts to determine if the market is trending, or is trading sideways.

How to use ADX

ADX is a follow-up indicator but it complements other indicators effectively. Once given a signal from ADX, waiting for a current price bar to close to avoid some few misleading interpretations. If you want to use it put a 20 & 40 line on the tool. Reading the Average Directional Index below 20 indicates a weak trend or no trend and above 20/25 a gaining upcoming strength in the trend. An extremely strong trend will be seen by values over 40 and when it goes over 40 and then turns back down the trend are getting weaker or is over. Although the ADX fluctuates from 0 to 100 it's rarely to score values above 60. You can use the reading of the ADX with your trend trading as the following: Readings above 25 indicate the strength of the trend. You can use the crossing of +DI and -DI to determine the trend direction; when +DI crosses -DI upward it's a bullish signal. Conversely, when +DI crosses -DI downward it's a bearish signal. You can return to your trend follower indicator (e.g. EMA Lines) to decide where to go. Readings below 20 indicate range movement and flat period. When ADX moves from 40 (or above) downward to 20. You can decide to close your trend follower position or tighten your stop loss.



<http://forex-indicators.net/adx>

Trading with ADX indicator involves the following signals:

ADX staying below 20 level — there is no trend or the trend is weak.

ADX moving above 20 level — trend is strong.

ADX passing 40 level — trend is extreme.

ADX value rising — trend is going stronger, falling — trend is weakening.

+DI stays on top of -DI — uptrend is in place.
 -DI stays on top of +DI — downtrend is in place.
 Two DI cross — trend is changing.



<http://www.actionforex.com/articles-library/technical-analysis-articles/what-is-the-average-directional-index-%28adx%29?-2008032439253/>

You see that the EUR/USD was moving up strongly, so you bought this pair on the last pullback. But now after another move up, the pair has pulled off of the highs and is moving down and you wonder if there is a way to measure the strength of the move so you could have exited earlier to protect more of your profits. There is and it is called the Average Directional Index (ADX). Developed by J. Welles Wilder, the ADX is meant to evaluate the strength of a current trend, be it up or down. **The important point is that this technical indicator will not give you the direction of the trending move, but rather will tell you if that move is gaining or losing strength.** A simple look at the ADX plotted on a daily chart of the EUR/USD shows the value of this tool. We can see that the market was moving up strongly as the ADX was moving up. The drawn lines on the chart with an arrow show the ADX peaks and and market price start to move down. We can also see that this change in trend of the ADX was also a change in the direction of the EUR/USD. If the market was in a downtrend, the ADX would also rise as the market was selling off and peak as the market started to change direction back to the upside. But the key is to remember that this indicator only measures the strength of the trend and does not tell us the direction of that move. As a trend trader, this change in momentum can be a valuable tool to help you determine the end of a strong move. If trading with the trend, a trader using the ADX on EUR/USD trades would exit as the ADX peaked and started to move down. This way the trader would be able to time their exit and keep more of the profits in the trade.

Practical needs in scalping

You can use the crossing of +DI and -DI to determine the trend direction; when +DI crosses -DI upward, it's a bullish signal, on the other hand, when +DI crosses -DI downward it's a bearish signal. If trading at M1 or M5 you need ADX (14) also ADX (20) settings.

Scalping might be better to do at forex market if ADX is greater than 20 (ADX > 20; 20 is here a value not a setting variable like ADX (20)). So enter a trade if ADX is over 20 and is rising toward the 40 score. You can often monitor when ADX is rising above 40 the trend starts going down and ADX goes down too - although ADX hovering above 40 suggests a strong trend, it is probably better to avoid opening new trades in the direction of the current trend. If using ADX as a helping tool, a confirmation indicator that could give more confidence by entering a trade – rewording if other primary indicators or methods provide a strong signal and ADX contradicts in value, may be it's better to ignore then the ADX signal.

The Bottom Line

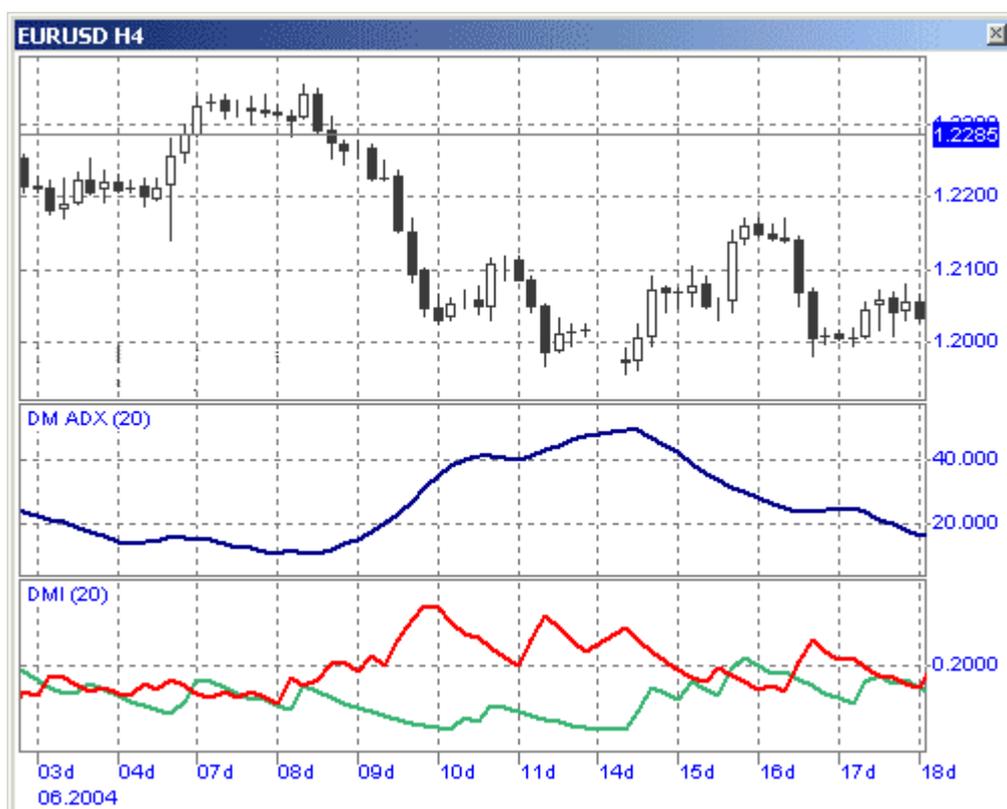
If you want currency trading success, you can't just trade support and resistance levels, and hope they hold or break. You need confirmation of momentum to get the odds on your side - and the ADX indicator will assist you.

Dimensional characteristics

ADX will show different values by using different timeframes. Learn the different ADX values by monitoring 10 sec., M1 or M5 (or M30, H1, H4). The ADX at 10 sec. timeframe in the trading system „Scalping 10 sec., 30, M1“ is used for looking at +DI and -DI crossovers and vice versa and if ADX are rising and signalize a confirmation for a short term trade, whereas at M1 are sending excellent trend signals. May be that an ADX direction is more important than the levels. Basically a rising ADX at M1 timeframe indicates an increasing trend strength. Some of good trades are in situation when ADX value rises from below 15. If you wait till a 20-25 score, the move could be frequently over by then and whatnot when ADX level has risen above the DMI's (+DI, -DI) you can say: „the higher the ADX is above both DMI lines, the more likely the trend could end shortly. Often a reversal is coming and other times just a consolidation.

How to set ADX, -DI, +DI

Different brokers offers different indicators. Some trading platforms quote the Positive Directional Movement Indicator (+DI) and the Negative Directional Momentum Indicator (-DI) with the ADX Indicator and can be set when ADX indicator is applied to charts. On other look for DMI indicator (Directional Movement Index).



<http://www.forexrealm.com/technical-analysis/technical-indicators/average-directional-index.html>

Mathematical Formula

For the boffin's out there, here's the technical bit – don't worry if you don't understand the calculation, its easy to use when visually plotted. The ADX is based on the comparison of two other directional indicators, both of which were also developed by Wilder, and they are:

Positive Directional Indicator (+DI) and the Negative Directional Indicator (-DI) to produce ADX as showed in the following formula:

$$ADX = \text{SUM}[(+DI-(-DI))/(+DI+(-DI)), N]/N$$

Where:

N: Refers to the period of calculation. The formula above produces the ADX line, which oscillates between 0 to 100 values. The +DI and -DI are both present and can be seen to make up the indicator.

You don't need to understand the above calculation to use the indicator – you only need to accept that the indicator works. The indicator is easy to use when it's visually plotted - and you'll find it included, with most of the good forex chart services.

Closing Remarks

The ADX line is a great momentum indicator and like the RSI (also developed by Wells Wilder), the ADX it will help you trade the strongest trends - and give you advance warning of changes in momentum. ADX alone, or Bollinger Bands or RSI etc. can't provide a consistently winning solution. So it would be better to call it „trading ideas“ not „trading system“.

Link

If you are interested in trading with ADX take a look at:

<http://forex-indicators.net/adx>

<http://www.informedtrades.com/4525-how-trade-trends-using-adx-forex-futures-stocks.html>

<http://www.forexrealm.com/technical-analysis/technical-indicators/average-directional-index.html>

Best of luck in scalping the Forex!

Kindest regards
Forexcube

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