MTPredictor™

Software & training for Risk/Reward trading with Elliott wave

MTPredictor Help File

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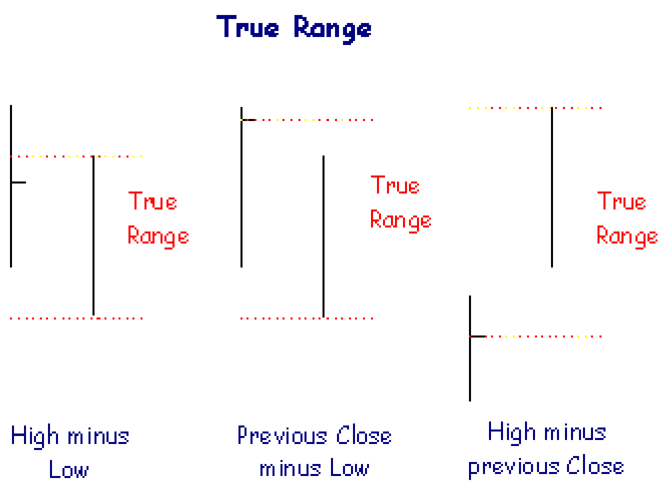
ATR Stop

This help file introduces the ***ATR Stop***.

The ATR stop is based around the average true range (atr), which is a concept that was introduced by Wells Wilder, where the average true range is calculated as being the true range averaged over the last x periods.

First we need to calculate the true range which is as the largest of the following three numbers:



This is then calculated as an average over the last x periods, typically 10.

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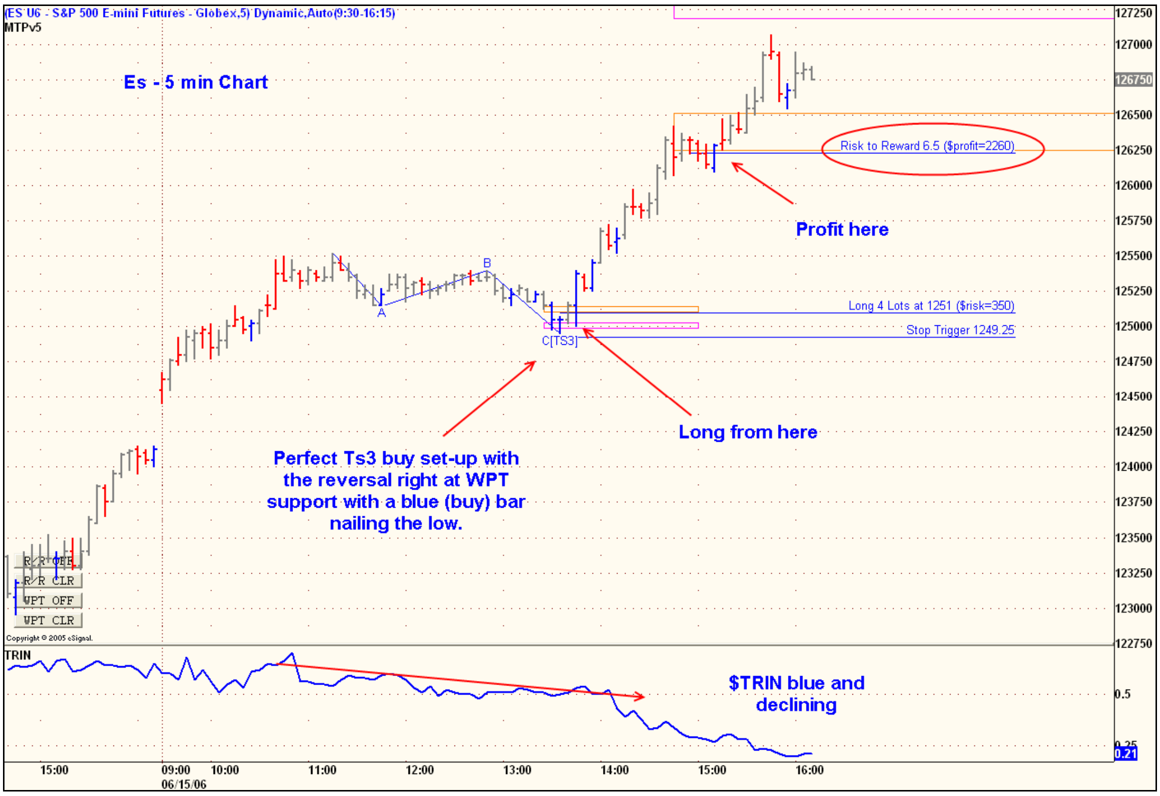
The basic concept is that this then gives you an indication of how volatile the market has been over the last 10 periods.

The ATR stop then takes this value and moves it up or down (depending whether you are in a long trade or short trade) by a set multiplier, typically 2, 2.5 or 3. This will then give you a line on the chart that trials the markets but trails the market 2 or 3 times outside the average “true range” over the last 10 periods. The idea being is that as long as the market volatility continues to move as it has done over the last 10 periods you remain in the trade. You will then only be stopped out if any increased volatility (outside what was considered normal for the last 10 periods) occurs. This will allow you to run your trade much further as a trend unfolds.

Let's take a look at an example:



Here is a standard TS3 trade setup that resulted in a profit off approximately 6.5x the initial risk using the standard trade management guidelines.

However let’s now change to using the ATR stop and see what difference it can make.

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Here is the same trade at this time using the ATR stop:

As you can see, it allowed you to stay in this trade much longer.

This is the idea behind the ATR stop, in that it will help you "run" your trades much further when a strong trend unfolds.

However, the key phrase here it is "when a strong trend unfolds", and this will be something I'll be talking about in a bit more detail later in this help file. In that it is important that you only utilize this particular trade management technique when you are in a ***strong*** trend.

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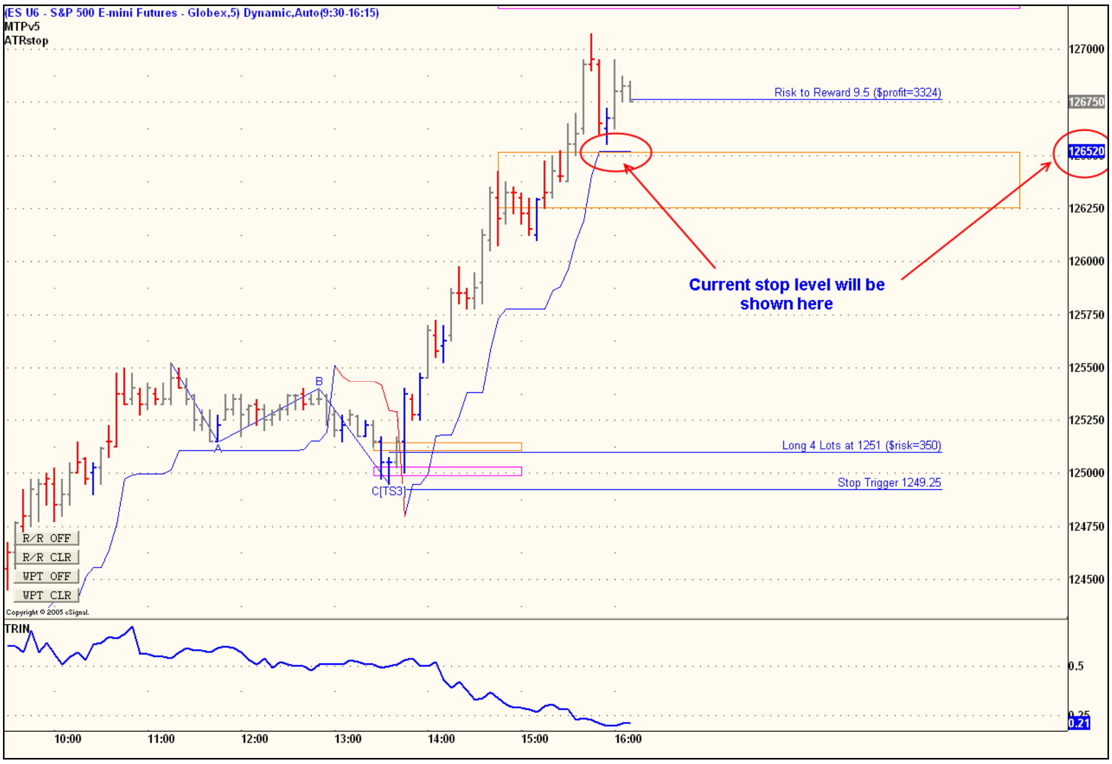
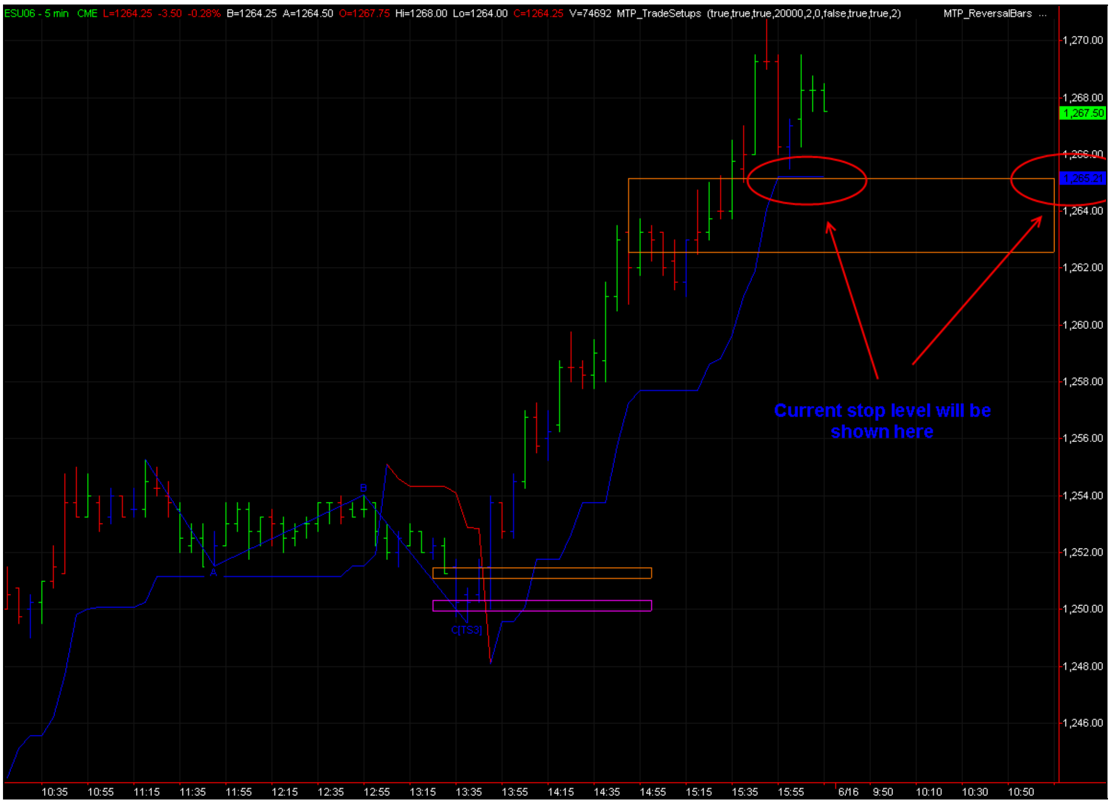
The ATR stop is very easy to use. All you have to do is load it onto either your eSignal or TS8 chart.

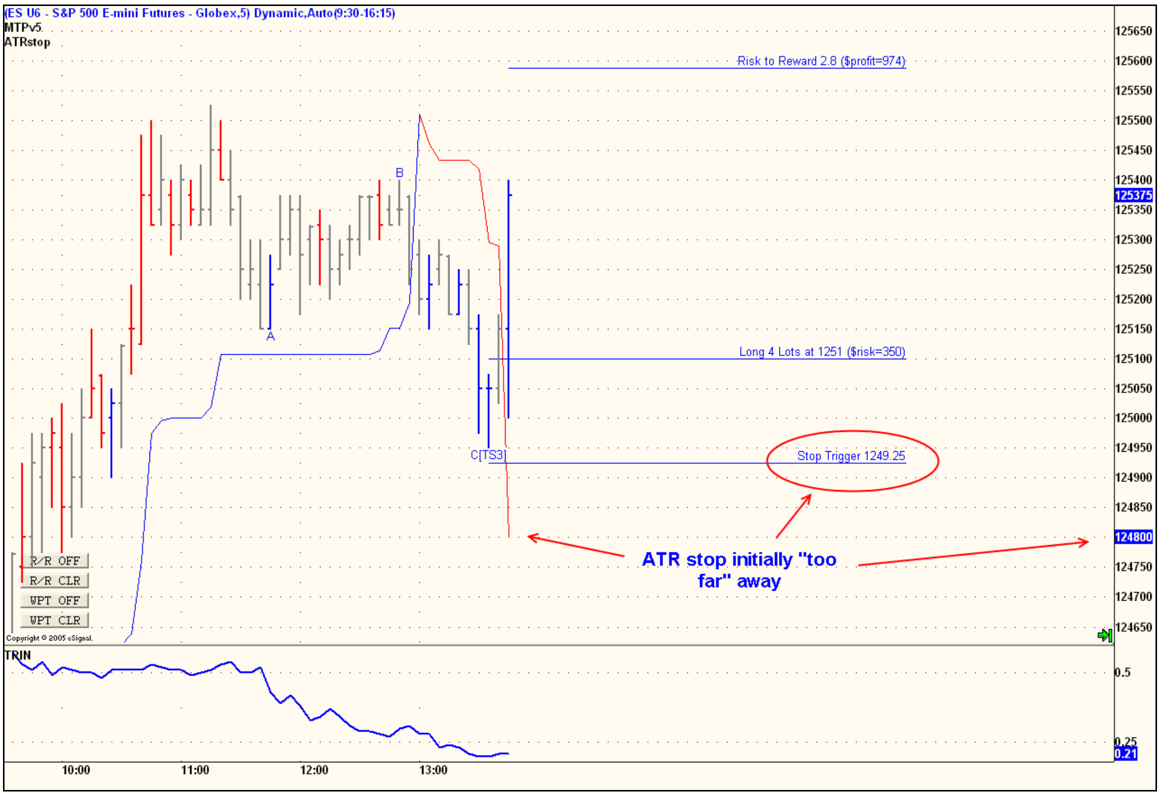


And



As you can see, the current stop level will be shown by the solid line on the chart and so the price level on your price axis. This should be adjusted as each new bar completes.

The only time this can become slightly tricky is right at the start of the trade where the actual value of the ART stop can be slightly further away than your normal initial stop.



As you can see here, the ATR Stop is slightly further away than your normal "initial stop position". You will never want to widen your initial stop and therefore increase your initial risk on the trade, so if this happens then common sense will tell you that you should use the normal initial stop position until the ATR stop catches up and gives you a value that is higher than your initial stop for a long trade, or lower for a short trade. This is just basic common sense.

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Sometimes, the ATR stop can be slightly slow in recognizing the new trend, so you can get a situation like this unfold:

Here it is giving you a sell protective stop value that is currently higher than the current price so is obviously this is incorrect. This is just because the ATR stop is slightly slow in recognizing the new up trend (in this example).

As you can see, common sense should be used at all times and therefore you should initially use the standard stop positions on your trade until the ATR stop level "catches up" and starts to move in the correct direction.

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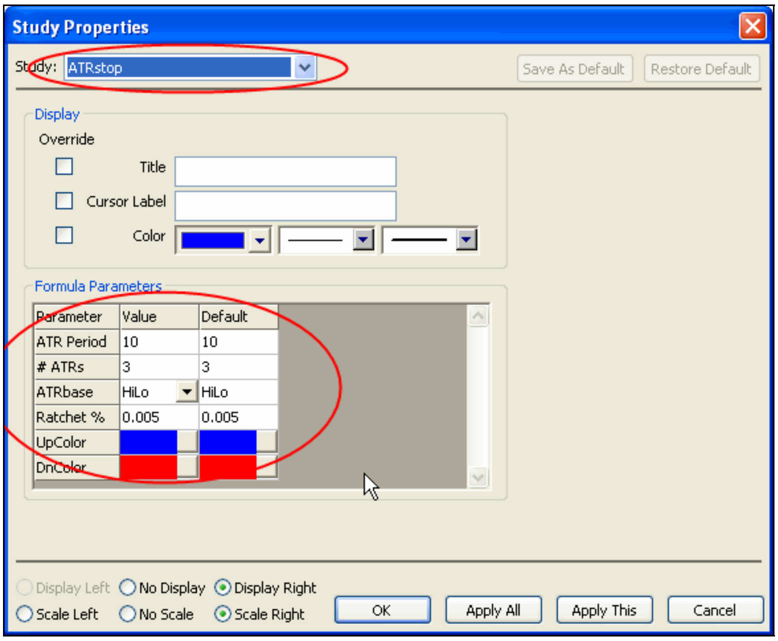
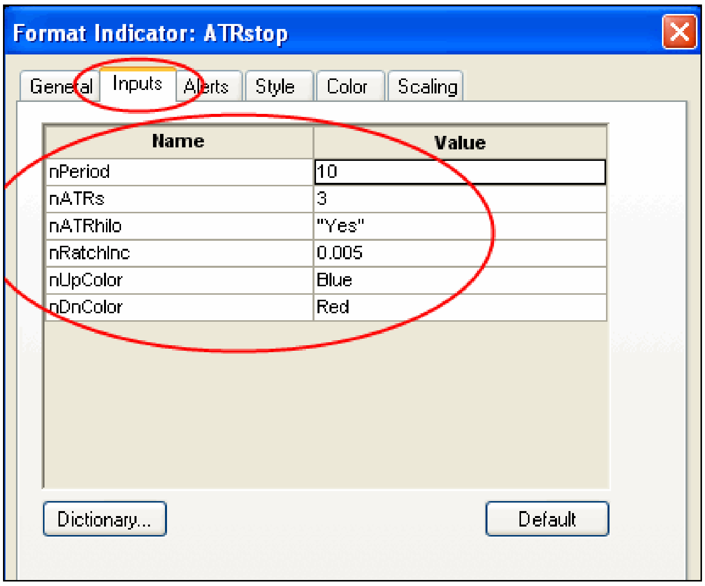
eSignal options:



TS8 options:



As you can see, the standard settings have a period of 10, and then use a ATR multiplier of 3, and a ratchet value of 0.005.

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I have already discussed the period of 10, but the ATR multiplier of 3 is the level "up or down" that the ATR stop tracks at. A value of 3 means that this will be 3x the ATR value below the recent Highs for a long trade OR this will be 3x the ATR value above the recent lows for a short trade. Obviously a value of 2 will mean that the stop is closer to the market. Normal values for this are either 3, 2 or 2.5, But I have found that 3 Is a good value to use.

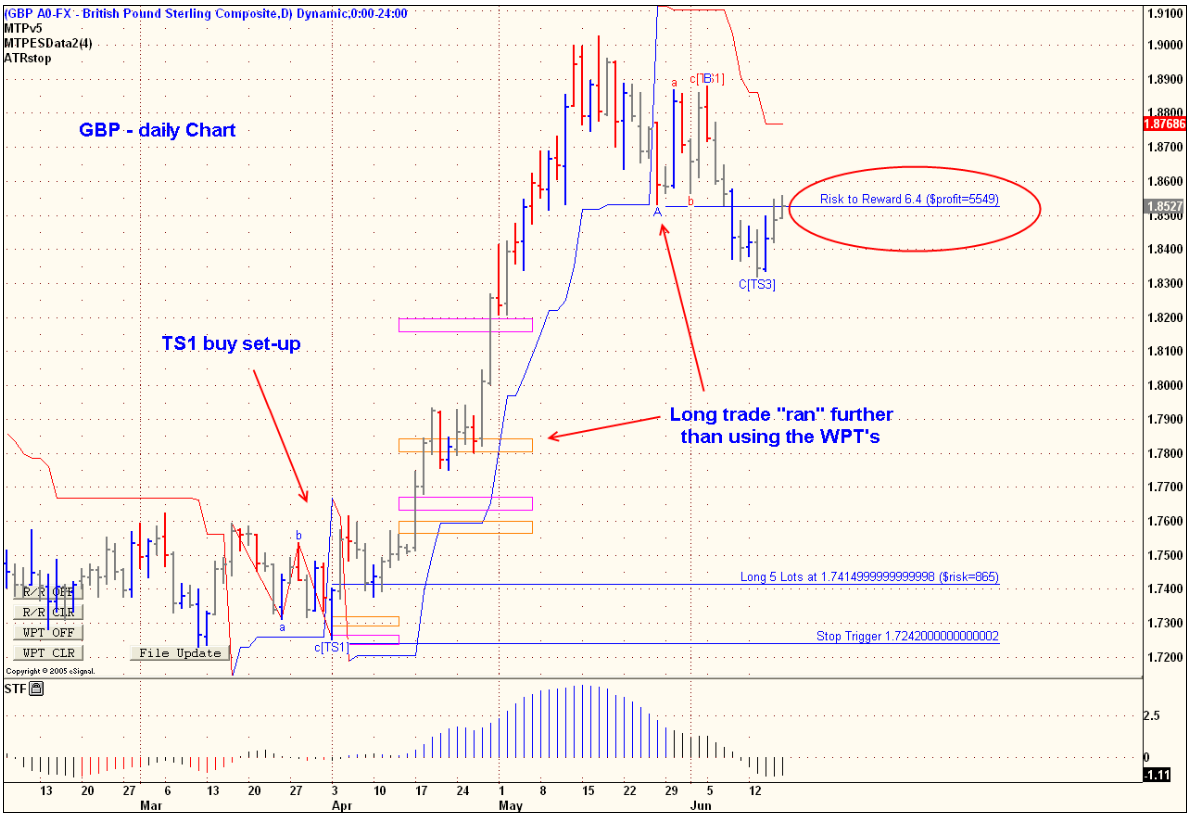
Next the "ratchet" value of 0.005 means that as a trade progresses in your favour, the ATR stop level slowly adjusts closer to the market. The idea being is that the longer you are in a trade the more likely it is that the current trend is nearing an end therefore for you to lock in the most profits; your protective stop should be moving slightly closer to the market. I have found that a value of 0.005, especially combined with an ATR stop multiplier of 3 works well for most markets in most conditions. However, if you do not wish to use this ratchet value please set it to 0.

As I said earlier, the best time to use this particular trade management technique is when you are in a strong trend. For this I would suggest using the STF (strong trend filter) on a high time frame to check that you are indeed moving strongly in a larger degree trend.

For example, on this particular 5min ES set-up the 15min STF was blue and very strongly up:

As such, this was a good time to consider letting your 5min long trade run further using the ATR stop rather than the standard WPT targets……….

This technique can be used on any market and any time frame. Here is recent example on a daily chart of the British pound:



Again, this is a very good technique to use to use when you are already in a strong trend or anticipating that a strong trend will unfold.

Thanks and good trading . . .

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