TRADER ON THE STREET

LEARN TO TRADE

WITH THE

HMA

HISTORY OF THE HMA: AN INTRODUCTION

The HMA, or Hull Moving Average, indicator was developed by Australian trader and leading stock market expert Alan Hull in 2005. The goal of creating this indicator was simple:

“How do we reduce lag in a moving average?”

So, Alan Hull set out to craft an indicator that minimizes the lag often associated with previous indicators. Since we’re talking about it still today, you can see the impact this indicator has had on trading programs and how it essentially became a paradigm shift in terms of how traders approach their strategies.

Why is that? Why is this indicator regularly discussed among rookie and elite traders around the world? Well, it basically solved an old dilemma every trader encountered. The HMA indicator is the answer to how to better see price action while still showing it in smoother curves.

Other moving averages like the SMA (Simple Moving Average) show you too much lag and so, curves are not as smooth. The result? You can’t really see every single movement of the markets, which makes it harder to determine short and long entries.

This is because the market often has a lot of up and down activity, and these moving averages have a hard time keeping up with small price changes.

Alan Hull set out to solve this problem by combining two techniques.

By taking a simple average period, determining the middle point of this period that significantly lags behind the current price point, halving the period to the actual midpoint, applying it to recent data, and taking that result and add it to the difference between the two averages, the result is lag reduction and improved curve smoothing.

There’s a little overcompensation with this formula that works perfectly to better balance the amount of lag created when averaging between time periods.

Essentially, it uses the square root of the desired period rather than go off the base numbers.

This formula seems easy enough, which is why it was able to be adapted to any trading program from that point on.

I bet you’re wondering how you can use it.

The following is a guide you can use to significantly simplify your trading by implementing the HMA.

IT’S ALL ABOUT THE MOMENTUM

The one thing to always remember when you want to use the HMA indicator in your strategy is that it helps you determine one thing:

Momentum.

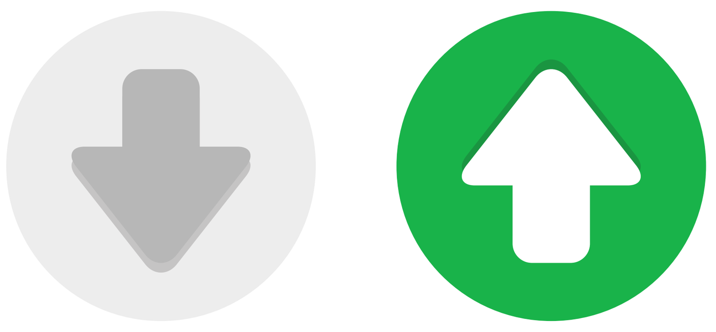
Since, as stated before, other indicators often are delayed and are thus less responsive to price action, having the HMA on your chart will eliminate that concern you may have that you’re not seeing activity as well as you should be, making it harder on you to place trades.

Being able to identify the momentum of the market

The HMA indicator is all about looking at price action to see if the market is bullish or bearish, and it really makes it simple enough if you’re a visual person.

Take this chart as an example. The HMA indicator makes it very obvious as to whether you should buy or sell, using two different colors to INDICATE that. Blue and Red

Blue: Go long
Red: Go short



You can clearly see bullish and bearish movements and entry opportunities with the HMA.

However, once you see a color change, that doesn't necessarily mean you need to immediately place trades heavily.

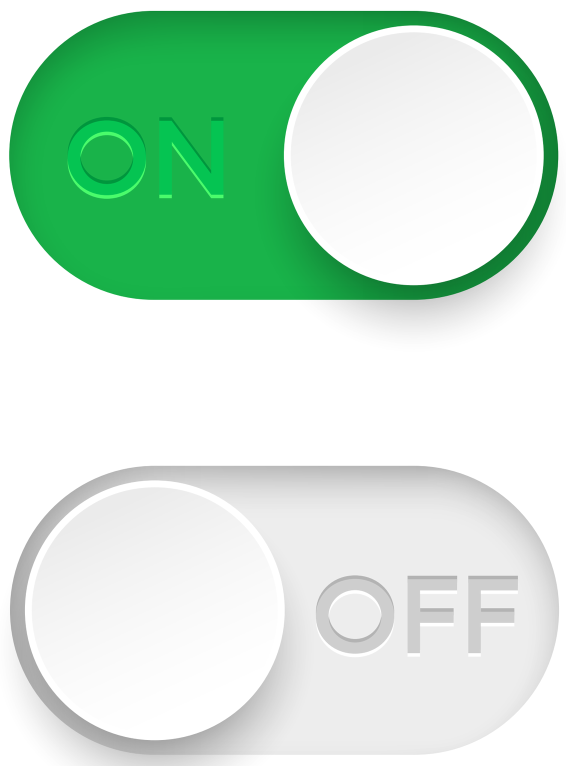
Color changes need to be taken into consideration once a few candles are formed.

This serves as a confirmation of where the momentum has shifted, creating chances for shorting or longing.

If you wait for that confirmation, you won't run into any major issues if the market decides to shift momentum out of your favor. You can easily enter and exit trades before momentum shoots up or down.

Remember, look at the direction, wait for confirmation, and once it's in your favor, enter trades.

TRIGGERS



Luckily, trading platforms have many tools you can use to backtest and pinpoint entries and exits.

If you want to backtest the HMA, it's a great opportunity to look at trigger positions you could have taken in the past, so that when you encounter similar movement in the future, you can enter trades quickly.

Say this chart above is your back test. You can use different drawing tools such as lines and rectangles to pinpoint where you could have entered the market. The vertical lines used in this example are what could have been your entry points had you encountered a market in similar momentum shifts.

That first line shows when the HMA turned from red to blue, showing that it's a good time to go long.

As you can see, this is an example of an 200 HMA. If you know your Fibonacci sequence, you know how critical it can be in trading.

For the HMA indicator, the higher the number in the Fibonacci sequence, the smoother the curve will be. A lower number will show quicker, short-term movements, so a more detailed curve.

Luckily you can use any time frame you want as well with the HMA indicator. So, regardless of what number you choose within the Fibonacci sequence, you can implement it into any time frame.

You can also draw out support and resistance levels using horizontal lines to determine exactly where on the chart the price action will continue to test past levels.

Again, wait for a few candles to form and for pull in the desired direction before entering trades.

SETUP

You can use drawing tools, but other indicators can greatly benefit you when trading with the HMA as well. Trigger points in the market can be better determined when using supporting indicators. They can provide additional data and further confirm the trend's direction.

There are a couple you can utilize in your trade setup that will yield a lot of important data.

Here's how we can set up the HMA with the 200 time period. For this one, we'd also be utilizing the 10 period HMA and the MACD in conjunction with the main 200 HMA indicator.

The MACD Indicator stands for Moving Average Convergence Divergence, and it's primarily used to analyze the momentum of a trend. It does this by comparing two moving averages.

It's an oscillating indicator, so it operates within a range of 0 to 100. How can you use this with the HMA? Here are the points to remember about the primary and secondary setup.

Primary Setup

- The 200 HMA must change color and the MACD must be above 0

Secondary Setup

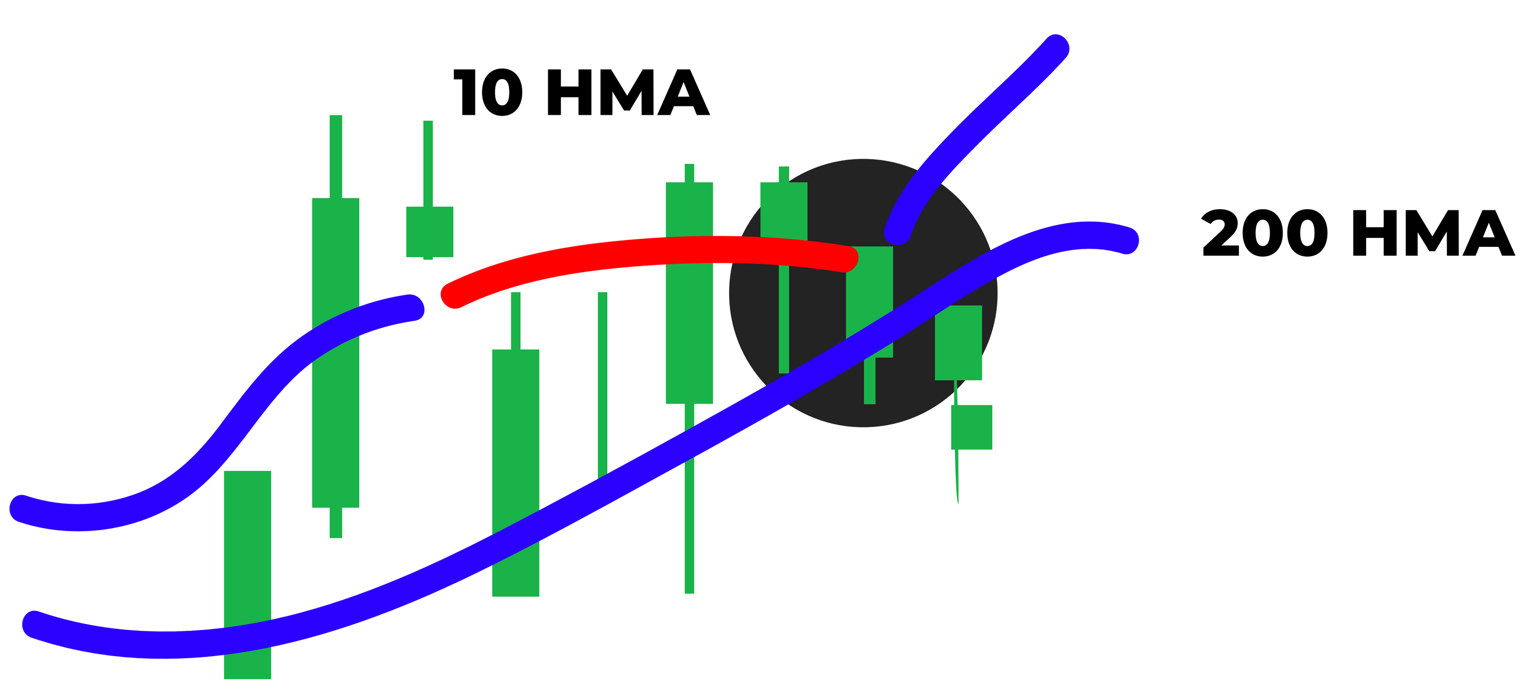
- 10 HMA turns the same color as the 200 HMA and the MACD is greater than 0

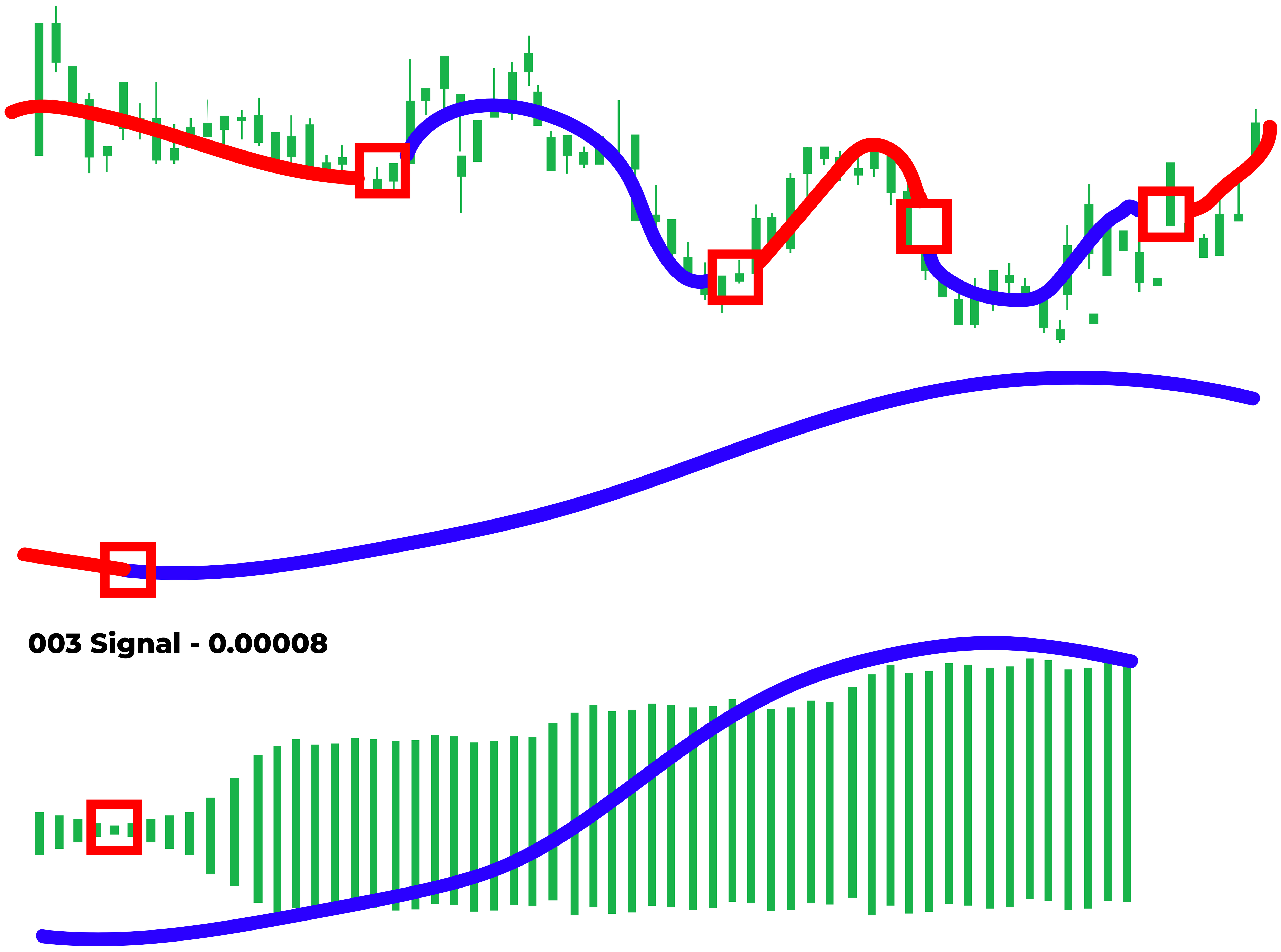
Entry

When all these are in unison, they're your entry signals. It might look a little like this in an uptrending market. The opposite goes for a bearish trend.

So, what does the entry look like? At the close of the candle that confirms the change and the setup, place your trade. This works for both the primary and secondary setups.

If we were to look at the setup as a whole, this is what it would look like.





EXIT

Keep in mind that your profit targets need to be pre-determined based on the time frame you're trading. Normally, it's around the support or resistance level.

For placing your stop loss orders,on the other hand, the junction in which the market transitions into a new trend is your best bet.

With this strategy, you can keep your trades up longer than usual. But if you want to close them for a profit, you need to look for the opposite signal that goes against your current trades.

WORD OF CAUTION

As is often stated in trading circles, nothing is ever an absolute guarantee in the markets. The same goes for using indicators. Often, when things go wrong in your trades, you might find yourself taking a step back and reevaluating your approach or strategy.

That's crucial because it's counterintuitive to continue using a particular strategy if it's always coming back to bite you.

When talking about the HMA, the same applies, considering that depending on market conditions, the indicator will not work the same moving forward.

And if things go wrong while using the indicators, don't continue with that particular strategy.

Trading is an ongoing process. It constantly merits changing quantities, time periods, and the moving averages you use, or simply taking out what's not working.

Take your current approach. Pause and refine it to see what went wrong.

What could go wrong is you see blue and start to go long and all of a sudden, it just tanks. That's less of a dig on the indicator and it's just a matter of unpredictability in the markets.

If that's the case, then you're not necessarily at fault. However, if you're placing trades and your pip count isn't increasing, something could be wrong with your strategy.

It's important to remember that when you're reinventing your technique to not overdo it.

It's what we call "Over-optimization." When something goes awry, and you want to change your approach, wait to see if it's actually yielding results over time rather than re-optimizing it at the first sign of trouble.

In order for a system to truly see success, it needs to be re-optimized periodically, and it should always be based on past market data and real-time events.

It's important to get accurate information, and shorter time periods between optimizations will often not grant you the exact data you're looking for.

If you're using the HMA indicator and need to find out what's wrong with your past trades, backtests come into play. Look at the mistake you made before and narrow down if your entry was incorrect, and what you should have done instead.

CONCLUSION

After all this information, you might think to yourself: "is this indicator necessary?"

The answer isn't cut and dry. No, you don't need to use it all the time, and it won't have a negative effect on your trades.

However, it will make it ever more simple to look at charts and know EXACTLY what you're looking at. If all the candles and numbers present a problem, something as simple as a moving line with two colors that basically let you know what you should do might do the trick for you.

It's a quick and easy indicator to pull up and analyze further.

That's why it was created: to make trading simplified. It tells you the **momentum, allows you to place buy or sell triggers, and adds certainty to your next positions in the markets.**

You'll be increasing your odds of making profitable trades, and the HMA also adds some flexibility to your entry and grant space for trades to hit your targets.

It's a dynamic indicator that will react properly to constantly shifting market trends, and the data that can be extrapolated from just eyeballing the indicator is of great use.

Again, this indicator reduces lag, so the movement you're seeing is more accurate than other moving averages, and so, you won't be late to an entry when the HMA is in play.

Don't completely rely on this indicator, though. It takes an awareness of all the minutiae in the markets to be considered an elite trader.

HMA works for different kinds of traders, such as swing or longer term traders in conjunction with all the other tools at their disposal.

It's a step above past moving averages.

Go ahead and start using the HMA to see what results it can bring you.