

White Paper Session

Topic : William's Alligator Indicator

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The legendary trader, Ben Williams introduced the Alligator indicator in 1995, also known as the Williams Alligator.

The Alligator is as much a metaphor as it is an indicator. It consists of three lines, overlaid on a pricing chart, that represent the jaw, the teeth and the lips of the beast, and was created to help the trader confirm the presence of a trend and its direction.

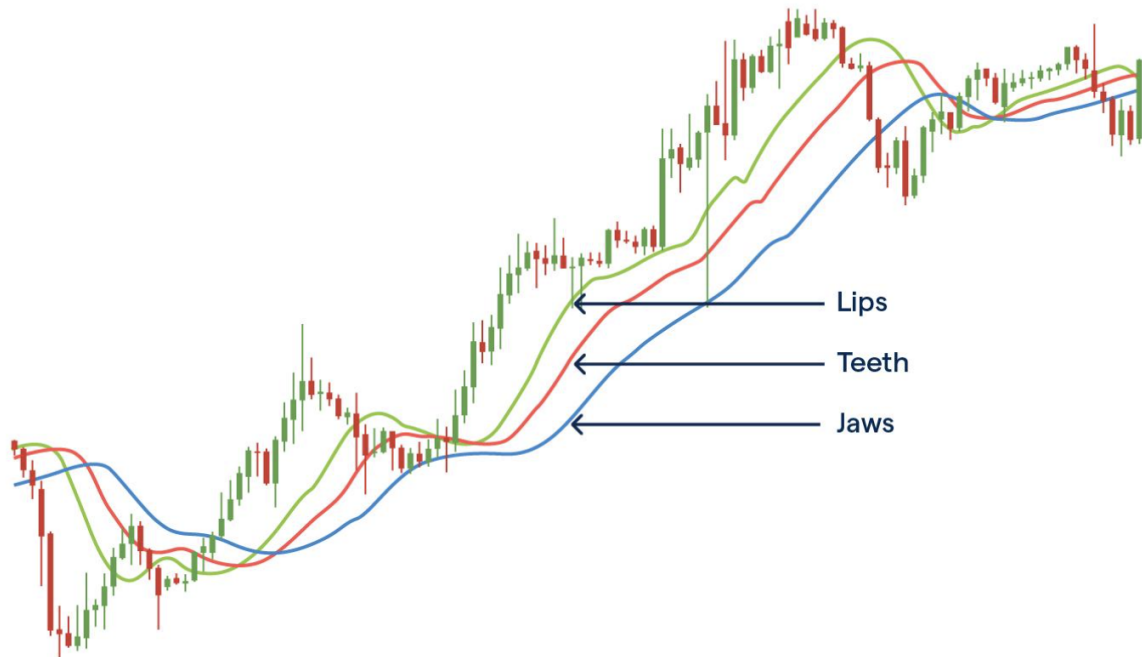
The Alligator indicator follows the premise that financial markets and individual securities trend just 15-30 percent of the time. While grinding through sideways ranges the other 70-85 percent of the time. The developer believed that individuals and institutions collect most of their profits during strongly trending periods.

The Alligator indicator can also help traders designate impulse and corrective wave formations, but the tool works best when combined with a momentum indicator.

The three Moving Averages that are used to comprise the alligator in three major ways: the Jaw, the Teeth, and the Lips/Mouth. These components converge and diverge depending on their subsequent reaction to evolving trends and trading ranges alike. Let's take a deeper look into each element of the Williams Alligator indicator.

- 1) The Alligator's Jaw, the "Blue" line, is a 13-period Smoothed Moving Average, moved into the future by 8 bars;
- 2) The Alligator's Teeth, the "Red" line, is an 8-period Smoothed Moving Average, moved by 5 bars into the future;

3) The Alligator's Lips, the "Green" line, is a 5-period Smoothed Moving Average, moved by 3 bars into the future.



How to make use of this indicator?

The indicator makes use of convergence-divergence relationships to develop trading signals. The Jaw makes the slowest turns and the Lips make the fastest turns.

The Lips crossing down through the other lines indicates an opportunity of a short sale. While crossing upward indicates an opportunity to buy.

A trend only exists when the three lines move in parallel. If the green line is above the red line and the red line is above the blue line, there is an uptrend. If the order of the lines is reversed, (blue top, red middle, green bottom) the market is in a downtrend. When the lines widen, it confirms the trend.

The way the indicator works can be explained using the following analogy. When the alligator's jaw, teeth, and lips are closed (moving average lines are intertwined), it means it is tired or sleeping. This is when many traders avoid taking a position because the trend is too weak.

The longer the alligator sleeps, the hungrier it becomes – when it wakes up, it's ready to hunt bears and bulls. The alligator opens its jaws (lines uncross and move upwards or downwards) and eats until it is sated.

So now, the alligator has lost interest in the food and it closes its mouth to rest (lines move closer together). This is when some traders close their positions if they've made a profit, as the upward or downward trend may have come to a halt.



Limitations:

The Williams Alligator indicator is known for pushing false positive signals when the three lines are criss-crossing amongst each other. This can happen often and is often due to choppy market conditions. This is referred to as “sleeping.”

