Introduction

A great deal has happened since my initial discoveries of exact pattern alignments. My understanding of specific patterns and repeating cycles quantified by Fibonacci ratios has led to the refinement of unique technical events that can be studied as specific entities.

Technical Entities Continued:

In *Harmonic Trading of the Financial Markets: Volume One*, I discussed the importance of specific pattern alignments that represent defined "technical entities." According to the prescribed set of ratios, each pattern has been differentiated, analyzed and refined to develop the best strategies for each situation. Although I will not review it in this book as I extensively covered it in *Harmonic Trading of the Financial Markets: Volume One*, "The Great Gartley Controversy" which emphasized the importance of pattern differentiation underscores the essential argument that not all patterns (Gartleys) are the same.

New patterns such as the 5-0, the alternate Bat and the Reciprocal AB=CD define further the concept of specific technical entities. These new patterns build upon the foundation of several existing patterns presented in *The Harmonic Trader* and *Harmonic Trading of the Financial Markets: Volume One*. Furthermore, this material broadens the existing pattern identification techniques to encompass the basic understanding and perspective of harmonic structures.

New Ideas in Harmonic Trading

Confirmation: Indicators

Technical Patterns vs. Price Patterns

Candlesticks

Why?

Candlestick Patterns

Alternate Bat Pattern

BAMM Theory

In my first book, *Harmonic Trading of the Financial Markets: Volume One*, and I presented a number of basic strategies for pattern identification as quantified by Fibonacci ratios. Although *The Harmonic Trader* presented many of the basic techniques, it was not until *Harmonic Trading of the Financial Markets: Volume One* was released in 2004 that culled together the gamut of strategies to thoroughly outline the Harmonic Trading methodology from start to finish. *The Harmonic Trader* was essential in that it was the first material to emphasize the importance of exact alignments and pattern differentiation. Since its release in 1999, many have tried to lay claim to the ideas that were first espoused in that work. Despite others lacking interpretations, *Harmonic Trading of the Financial Markets: Volume One* separated Harmonic Trading from the often misguided and misappropriated use of basic Fibonacci announcements.

Harmonic Trading of the Financial Markets: Volume Two Harmonic Trading takes the to a new level. Most of the ideas outlined in this material are unprecedented and not previously released in any of my prior material. *Harmonic Trading of the Financial Markets: Volume Two* advances the comprehensive methodology of pattern identification presented in *Volume One* to incorporate new technical measures that refine and filter the best trading opportunities. Advanced techniques such as the RSI BAMM, represent my most sophisticated trading techniques to date. I firmly believe that this material clearly separates my work with from all others in his field of market discipline.

If you are familiar with my work, you know that Harmonic Trading is much, much more than general Fibonacci analysis. In this book, I have put together is a substantial advancement of the basic Harmonic Trading approach encompassed within the first two books. *The Harmonic Trader* and *Harmonic Trading of the Financial Markets: Volume One* represent over 500 pages of the most comprehensive pattern identification techniques as quantified by Fibonacci ratio measurements. Both books dedicate a considerable portion of reading material that covers most aspects of pattern identification techniques that provide strict rules to validate a potential opportunity.

Released in 2004, *Harmonic Trading of the Financial Markets: Volume One* was a major advancement for the basic principles of the Harmonic Trading approach. The inclusion of new Fibonacci ratios, new patterns and comprehensive strategies for dealing with the violation of patterns expanded the gamut of new technical ideas within the Harmonic Trading approach which have advanced many basic theories to shed new light old studies. *Harmonic Trading of the*

Financial Markets: Volume One was comprehensive in that the material laid out the entire trading process. From initial identification to trade execution to money management, each aspect was thoroughly reviewed and a comprehensive methodology was presented, defining rules for every step of the process. In this regard, I'm very pleased and confident that the development of the Harmonic Trading approach provides a solid framework of probable answers for all possible questions that might arise during the trading process. The entire procedure from identification of a pattern to the eventual execution of a trade is completely outlined. But, there's always room for improvement and there's always room for other studies to challenge the prevailing knowledge.

It is important to note that I have always said that Harmonic Trading and the pattern identification techniques specifically within this approach are merely a starting point. It is important thing to remember that this is a basic framework to measure and analyze price action. The ultimate objective in this analysis is the identification of specific situations within the course of trading that will yield a high degree of reward while minimizing risk. At a minimum, these techniques can offer technical information regarding the potential state of price action unlike any other methodology. When combined with other technical studies and analyzed within the predominant trend, Harmonic Trading strategies can pin point the potential "hot spots" where reversals may develop or important continuations of the prevailing direction may occur. This understanding of critical technical levels of harmonic support and resistance is essential to gauge price action and to identify profitable trading opportunities.

The combination of pattern identification techniques and the utilization of Fibonacci ratios to quantify price action are the greatest assets of the Harmonic Trading approach. But as this methodology has become more refined, I've realized that there are many other technical indicators that form repetitive patterns in the same way that price action forms repetitive patterns. As I mentioned previously, I used to be exclusive in the application of measurement techniques of harmonic price patterns. I wasn't interested in looking at other indicators. However, as time went by, I notice to frequently the confirmation signals that many of these indicators provided. Although many are simple applications of standard indicator techniques, the combination of these existing measures with the Harmonic Trading strategies yields improved confirmation of the precise areas defined by a pattern's Potential Reversal Zone (PRZ), resulting is more precise reversal points.

At first, the simple integration of many of these indicator readings were extremely beneficial. As I expanded the use of other technical indicators, I noticed many similar traits that formed in the indicator readings as did in the actual price action itself. For example, I noticed that certain indicator readings formed similar patterns in setups that possessed distinct price patterns. Even more compelling were situations such as where a price pattern might indicate a Bearish Gartley on daily chart while the Stochastic reading was showing a Bearish Three Drives, each completing at the same relative point within their own charts. Once I began to see these relationships, I thoroughly explored dozens of indicators to find those that correlated the best with the Harmonic Trading techniques and provided the most accurate confirmation signals to validate patterns.

In this book, I discuss the best of these advanced techniques and I have devised strategies that compliment the basic elements of Harmonic Trading. Most of these techniques are completely original in that their application and in combination with the Harmonic Trading approach have never been presented before in any methodology - let alone pattern recognition within the area of technical analysis. I'm sure there are other indicator strategies that I am overlooking that you may find work extremely well in your trading. For example, you may be a Trader who utilizes MACD analysis with some type of Moving Average crossover strategies. Perhaps you are new to the Harmonic Trading approach and after reading this material you realize that harmonic price patterns work well with this type of analysis. Although I don't cover MACD with Moving Average crossover strategies in this book, I'm sure you will find many relationships that are very clear. In fact I've seen many trend continuation strategies that possessed bullish patterns all converging in the same area that are extremely effective methods to complement the basic approach. But, there has to be at least 100 people whom have discussed simple technical strategies like these. Not to mention the number of people who will cite any one of a number of indicator readings to enhance their analysis.   But not here! No.

My goal in this book is to present to you a significant advancement beyond the typical interpretation of technical measures. I am presenting only the best of my best strategies beyond the simple identification of harmonic price patterns. This book will take you to a new level and comprehension of Harmonic Trading and technical analysis in general. This material will expand your perspective of harmonic price patterns and advance your trading to the next level.

The strategies that are presented in this material - in particular BAMM Theory and the RSI BAMM – are practically a trading system unto itself. And this could be a costly fact for me to mention. Why trade harmonic patterns when the RSI BAMM work so well on its own? There's no doubt that both harmonic price pattern recognition strategies and the RSI BAMM approach can be effective in their own right. But, their true effectiveness can be seen when they work in concert with one another. When techniques of multiple approaches come together and yield the same result, the probability for a successful trading opportunity is extremely high.

Imitators and Agitators

Although it might take a few years, there is no doubt that there will be others down the line that will present these techniques, utilize similar indicators and teach these ideas in seminars to other people without any credit to me. Unfortunately, this has been my experience since I first launched my website, my books, and no doubt this will happen again. From a personal standpoint, it has been frustrating to offer this information to the general public, only to see the material reproduced without citation or proper credit. In fact, many people now offering these techniques are only in the business of selling products and not really trading. Although many of the original pattern identification techniques seem to be common knowledge at this time, it was not long ago that many of these techniques were unprecedented strategies. In the same manner, the material in this book will be accepted in the same manner. I do not doubt that in the years to come concepts such as the 5 0 pattern, the harmonic impulse wave strategies and the RSI BAMM, will be copied and presented as others' original ideas. This is an inevitable price of selflessly giving away my discoveries from years of research. But, I'm willing to except that price in exchange for the advancement of trading knowledge and to contribute what I can to those who are in search of the answers to trading the markets.

When I first began discussing Harmonic Trading on various web sites in the 1990s, I was admittedly quite naive. I openly presented the strategies that were the result of years of research that advanced the existing basic Fibonacci trading techniques. In the utopian vein that the emerging internet espoused, it was my desire to help traders, to freely exhibit the most pertinent ideas and to share with others in the hope that they would provide feedback that would ultimately further in this discipline. Although I received fantastic feedback from a n overwhelming number of traders, I realized that other Fibonacci-related web gurus were picking up on the ideas, as well. I welcomed their response and actively sought to “talk shop” with these guys. Unfortunately, I quickly learned that most of the so-called web gurus who were just teaching basic Fibonacci techniques were/are primarily in the business of selling investment products. I realize that I needed to exercise greater discretion and strive to establish Harmonic Trading as a distinct methodology apart from basic Fibonacci analysis.

I frequently scan the internet to review various Harmonic Trading discussion groups to gauge the public reaction to these methods. Although most of the response is overwhelmingly positive, there are a number of individual who see fit to claim these techniques as their own. More discouraging is the blatant theft of copyrighted material. For example, an individual posted a message in a particular Harmonic Trading forum that discussed currencies. He generously offered a pdf file of my first book *The Harmonic Trader* to everyone in the chat discussion. One problem – I never have sold a digital copy of the book anywhere. So, someone ordered a copy, ripped out each page, scanned the entire book and created a pdf file. I have to say that I am flattered that someone would take the time to do such a thing but stealing is stealing. I’m sorry but that is inexcusable.

Another internet search led me to a guy who gave an interview to a notable traders magazine, discussed many of the important concepts of Harmonic Trading and credit another individual for all of the discoveries. Classic plaguerism! But, when I see things like this, I am absolutely ap[alled.”

"**Shrouded In Mystery For The Last 76 Years...**You Are 15 Minutes and 23 Seconds Away From Turning $7,800 Into $76,824 Using The 10 Most Powerfully Profitable Proven Chart Setups Known To Man….If you are deadly serious about making a killing - week in and week out - you will want to indulge me for the next few minutes. In that short time I will reveal to you 10 simple to use trading patterns used by the most sought after money managers in the world. And, if you'll read this entire letter, I will show you exactly how you can make money from them ALL absolutely FREE…. Here's why I am giving away a "secret trading system" for FREE:… Because my clients can make money with it (some as much as $346,000.00 - some as little as $69,200.00) and… Because I enjoy teaching what really works – not some cooked up theory. Here's how it works: I'm not just going to hand you a 'black box' system and send you on your merry way. With my help you will develop a trading method that develops your confidence and consistency, you will literally force yourself to win. ….That's because you'll be training your brain to react to patterns – patterns that have proved themselves to be upwards of 80% reliable. **….The "Holy Grail"? Almost. … once you learn these "Harmonic Zones"**……Learn To Trade Like a Pro... In Just 4 Minutes!"…. Once you've identified the geometric patterns, match the Harmonic Zones to it – <u>all you have to do is sit back and wait for the profits to roll in</u>….Since our patterns are successful 60% of the time (even 70% or 80% in some cases) you can trade on a three to 1 (3:1) reward to risk ratio. That way you can concentrate on fewer symbols to trade, reduce your risk, and maximize your profits. "

This is the biggest farce ever! No holy grail, total bullshit
I will not even dignify the persons name but here is the l

Unfortunately, most of these web gurus are just wanna-be traders who spend all of their time producing article content for naïve subscribers. When I wrote for websites several years ago, I never had enough time in the day to produce articles on a regular basis and trade full-time. Eventually, I had to stop writing altogether, as my trading and Registered Investment Advisory business required all of my time.

Then Why Give It Away

Why do this? I could simply retain these techniques for my own research and trading. However, knowledge not shared is worthless. It does not matter that I have taken the necessary legal precautions that need taken to protect my intellectual property. Although it is my desire to prevent being plaguerized by others, it is my greatest desire to encourage a frank discussion of this material while openly sharing this information with the public. And that's why I'm releasing this book. I was set myself apart. I want a show people that there's another level of Harmonic Trading that will further the accuracy and increase your ability to make money. Because that's what it's all about. Making money.

Like many individual traders, I started as an online day Trader. Sitting at home in front of my computer screen, I spent countless hours researching the best techniques. From these humble beginnings, I've been able to enjoy financial success and move ahead in my career. It is always been my belief that those who can do, and those who can't teach. This quotation defines the trading educators and information available of these so-called web gurus.

It is incredible the number of people who have come to me after spending thousands - if not tens of thousands of dollars – trying to learn how to trade. Many of these people have been swindled out of their money while not learning any meaningful trading strategies. I was there. Years ago, I struggled to find the best systems, spent thousands of dollars on books and software, and lost even more money attempting to trade these fantastic systems that held no real trading value.

It can be difficult to know who is the real deal on who is the shyster selling products just to make money offer people who don't know when he better. After thoroughly investigating many of these professionals either going to their seminars are reading their books even talking with them personally you quickly realize who's really trading and who is not. It's unbelievable that many of these individuals get so much exposure in the media yet they rarely trade and derive most of their income from selling products. Many of these guys haven't executed a trade in years! If you want to find the most pertinent material on successfully trading the markets, you must seek out the people that have or are in the business of trading.

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Harmonic Trading produced from the people that are truly the n the guys said really know how to make the money are the money managers, the floor traders, the successful hedge fund managers. These guys don't many time to teach seminars or, with a variety of products because they're making so much money actually trading the market. It is the frustration of mine since inception my website HarmonicTrader.com.

The At first, I use the website to present ideas, sell my first book "The HarmonicTrader" and to develop forum where others could share their ideas on the entire technical approach to trading the markets. After receiving the enormous amount requests, I develop an online advisory service through the website. Before I knew it, I was in the financial products industrY without really wanting to sell products and services. I just a trade and develop my skills to one day become professional adviser.
Now I am a registered investment advisor.
Xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx

The Content Within…

This is the reason why it's taking the so long to write this third book. Each book represents years of research and endless hours devoted to studying the financial markets. If I didn't love researching the market and studying technical analysis, there's no way I would've had the motivation nor the desire to compile this information and present my research. Books are not easy to write. At best, I'm probably good to write about one book every three to four years. So, I am on track with this book although it was my greatest desire to have released it in 2005. This book like the others has been years in the making and represents a collection of my best ideas. I'm proud of this book because the techniques that I present in this material are unique. They are original. While combining the basic approach of several technical methodologies, I believe the underlying principles within Harmonic Trading are clear. That is, a technical approach that defines profitable trading opportunities in the financial markets from a pattern recognition perspective as quantified by Fibonacci ratios while incorporating pertinent other studies that confirm the information.

I have put together a series of books and a software program that is very affordable and sufficient enough to help an individual learn the dynamics of price action. In fact, I've purposely offered my products at a reduced rate to make them accessible to all people. Whether you are a hedge fund manager with $1 billion to trade, a retiree trying to maximize your IRA or a novice Trader starting out with $10,000 or less, I'm confident that these tools will help you manager and analyze price action better than any other system. I've dedicated a substantial portion of my life studying the financial markets and discovering the best techniques that are consistently reliable.

Although I've given seminars several years ago, I since backed away from the financial products industry. Specifically, I no longer write for website columns, give seminars, teach students because I am now a registered investment adviser. My ultimate goal in this industry as a career was to become professional money manager. I believe my experience has been positive as a financial commentator but my first objective has always been real trading. In the last few years, I've transitioned away from the online articles and seminars to actually trading for myself and for other clients. This is very important because I'm not writing this book to sell you a product. I'm writing this book share in the ideas and research to help you help yourself. The money for selling the book itself is not my motivation.

I want you, the reader, to know that I have been there, sitting in your shoes, wanting to know the answers to the market. At times, either willing to pay anybody out of desperation to look at any approach that proclaims that have the Holy Grail to the market. I have to tell you that searching for the Holy Grail to the financial markets is just not realistic approach to be consistently successful. What is real is finding the order within the chaos in the financial markets, defining that order and being willing to take some risk in return for financial reward.

I believe that the Harmonic Trading approach is extremely accurate defining such order within the chaos the financial markets. The measurement techniques within this methodology provide extensive information regarding state of potential price action. I have said it before, in fact I have said it in every book I've ever written - "This is not the Holy Grail methodology to trading financial markets!" Furthermore, anyone who proclaims that Fibonacci analysis is 80 percent accurate “across the board” must be cautiously regarded.

New Ideas in Harmonic Trading

We will address many new topics with particular emphasis on the Harmonic Impulse Waves, Trend trading strategies and wrap up with the BAMM Theory, in particular the entire RSI BAMM step-by-step approach. I will present new patterns such as the 5-0, the Reciprocal AB=CD, the Alternate Bat and spend some time looking at the classic Head and Shoulders pattern from a harmonic perspective.

In closing, I want thank you for taking time to read my material, your genuine feedback and simply being interested in what I have to say. I want you to know that I'm using these techniques every day to make financial decisions for my clients and myself. As Registered Investment Adviser, I have a fiduciary responsibility to my clients to serve their best interests to the best of my ability. I seek to extend that level of dedication and commitment to all areas of my life. This book reflects such dedication and commitment. I just want to know that are getting the real deal here and that I'm grateful to share this information with you. Let's get started!

CH a P 1: Harmonic Trading as an Integrative Approach

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Although many of the same patterns that were yielding tremendous success the year prior continue to develop and form, the overwhelming bearish trend of the markets made many of these patterns seem futile. This forced me to step back and take a hard look at the effectiveness of this methodology. The overwhelming failure of many patterns during this time truly showed that a pattern is more a signpost of potential future action and not an end all be all signal for trading. Many people who initially embraced this methodology quickly became disparaged with this approach and claimed that harmonic Price patterns did not work in all markets. Instead of getting locked in to this mentality, I realized that the pattern failures of the time were indicating a substantial decline in the financial markets.

For example, in my analysis with this S&P 500 I examined several potential long-term areas where this bear market might end. From a pure harmonic pattern perspective, I realized that the index was headed much lower after it violated key support in the 1300 area. At that point, the next convergence of numbers from long-term standpoint did not complete until the 800 level. My initial report calling for this completion was nearly a year a half before its realization.
The the NASDAQ composite offer similar price action to. As this index continue to slide sharply through the critical support in the 3500-3700 area, I realized the next convergence of weekly projections indicated that the index was headed for the 2200 area. I believe this would be a substantial low for the NASDAQ composite index. However, this was a brief stop in a further slide that would take the index as low as possibly 1700. Although I did not one believe it the time, I knew that is severe violation of the 2000 level would trigger this further decline. The the price action lagged severely in this area. Although a minor balance was experienced, the eventual continuation of the decline marked a severe bearish condition that would require much more time to stabilize had reversed the downtrend.

The Dow Jones industrial average took longer to reach its ultimate low. After violating critical support in the 9000 area, the only harmonic pattern formation left to consider was a substantial bullish ABCD pattern that completed 6800. In fact, I was interviewed on a Quebec AM radio station in July of 2003 asking my opinion on the markets. Although the index had been following sharply for most of the year, the host of the program was quite dismayed when I explain my reasons for the index to continue lower. In fact, after I offered my projections, my interview was abruptly ended. Simply stated, these guys did not want to face reality.

It was these experiences that changed my perspective on the entire Harmonic Trading approach. I realized that the patterns were not ultimate buy or sell signals. Moreover, the patterns were signposts of potential future action. This was a difficult admission for me because it devalued the significance and potential for the strategies to be a trading methodology. I learned a great deal during this time. In the long run, this was an important learning process. It made me focus on price action in the completion area of harmonic patterns more than the patterns themselves. Furthermore, it opened a new attitude towards these techniques. It led to the evolution of utilizing these patterns within the context of price action as they related to overall trend and other technical measures.

XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX

This material is different from my first two books in that it combines several disciplines to refine the simple pattern identification techniques. Although simple pattern identification is a powerful approach to the financial markets, there are many other technical tools that provide significant information to define the best opportunities. I must admit when I first began outlining Harmonic Trading strategies and pattern identification techniques, I ignored the information offered by these measures. This was during the time when the market was going straight up. I believe most traders are inclined to be bullish most of the time, buying much more than selling. I was not immune to this. Although the pattern techniques help me define many successful profitable opportunities, it was the overwhelming bullish bias of the time that made the strategy worked so effectively. However, the lessons of the 2000 bear market severely challenged the integrity of the patterns. It was a matter of evolve or die. Although many of the same patterns that were yielding tremendous success the year prior continue to develop and form, the overwhelming bearish trend of the markets made many of these patterns seem futile. This forced me to step back and take a hard look at the effectiveness of this methodology. The overwhelming failure of many of patterns during this time truly showed that a pattern is more a signpost of potential future action and not an end all be all signal for trading. Many people who initially embraced this methodology quickly became disparaged with this approach and claimed that harmonic Price patterns did not work in all markets. Instead of getting locked in to this mentality, I realized that the pattern failures of the time were indicating a substantial decline in the financial markets.

Pattern Analysis in the Broader Markets for 10 years

As a part of my advisory service for HarmonicTrader.com, I wrote market reports for the three main U.S. indices - the Dow Jones industrial average, the S&P 500 and the NASDAQ composite. As the bear market 2000 progressed and many initial bullish patterns were violated, I realized that the extent of this decline was manifested by these violations. Furthermore, the other possibilities of harmonic patterns in the indices were indicating much lower levels well in advance other ultimate realization.

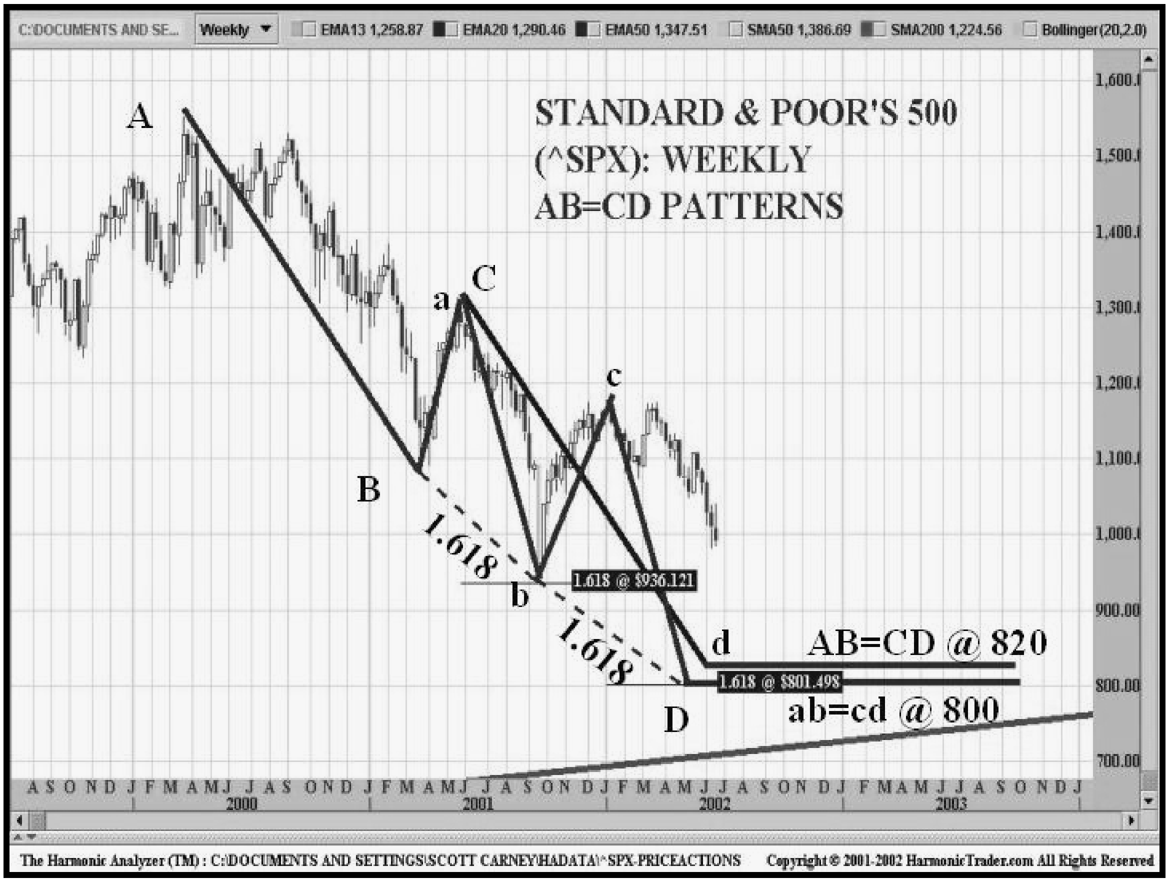
I would like to

Standard and Poor's 500 2000-2005 Review

n my analysis with this S&P 500 I examined several potential long-term areas where this bear market might end. From a pure harmonic pattern perspective, I realized that the index was headed much lower after it violated key support in the 1300 area. At that point, the next convergence of numbers from long-term standpoint did not complete until the 800 level. My initial report calling for this completion was nearly a year a half before its realization.

June 2002

"The longer-term perspective is becoming much clearer, as recent technical action points to much lower levels - well below last year's low. There are some interesting signs of a potential downside target for the index. Although the recent decline has been sharp, the price action is indicating the 800 area may provide some longer-term support…The three- year chart shows two potential AB=CD patterns that complete just above 800. There is a green line that appears just under this area. The green line represents the longer-term bullish trend from the mid-1980s. This can be seen more clearly on the following chart."



"Clearly, the S&P 500 is headed to test the 15-year bullish trend line that converges at 800. Not to mention, the AB=CD patterns complement this area nicely. The 800 level represents a critical long-term support for the index that could develop over the next few months. It is important to focus on the 970 area in the short-term, although this seems unlikely that it will hold. The overall position remains bearish until these lower levels have been reached."

Jan 2002

June 2002 – 800 call

Reiterqate 800 in 11/02
It is important to note that the S&P 500 possesses the most harmonic scenario of all of the indices. The historic retracements and the distinct bullish AB=CD patterns defined the 800 area as a major potential bottom. The critical element to validate this long-term Potential Reversal Zone (PRZ) is time. If the index can hold these levels and move higher, the stronger the support at 800 will become. Although I favor the bullish side for the next several weeks, especially with a breakout above these recent highs, the index still needs more time to resolve the larger bearish trend. The index is close to challenging the three year downtrend and decisively changing its course. But, it must provide more constructive bullish action before ending the downtrend. For these reasons, the official position remains bearish.

http://www.harmonictrader.com/members/dow/harmonic/markets/spx1102.htm

march 2003

Without question, the next two weeks will be a historically defining time period for the markets. The Standard and Poor's 500 has been the Harmonic bell-weather for all of the indices. The index has consolidated for the past nine months in a considerable Harmonic support zone at the 800 level.

It is important to briefly review the 800 scenario to underscore the importance of the current action in the index. I first outlined this support zone in the June 2002 market report. The index was trading just under 1000 and it was threatening to breakdown - again. The index was clearly heading to much to lower levels to test the convergence of multiple Bullish AB=CD patterns…….It is amazing to consider the significance of the 800 area and the price action of the S&P 500 for the past 9 months. The clear Bullish AB=CD patterns and the longer-term trend line support are defining this area as a historic point for the index.

http://www.harmonictrader.com/members/dow/harmonic/markets/spx0303.htm

APR '03

The "tea leaves" of the entire Harmonic convergence at 800 says that the bottom has completed for the index. The impending breakout of the bear market channel will be significant and it will confirm this 800 as a historic low. For these reasons, the official position is now NEUTRAL with a bias to the upside. Although the index still needs to take out some resistance levels - namely a strong move above the 950 area - the index has resolved this long-awaited Potential Reversal Zone (PRZ).

I believe it's important to review the long-term perspective of the overall market position throughout the past several years. This S&P 500 Market Positions chart shows the overall view of the past four years. Although HarmonicTrader.com has been providing market commentary since 1998, all market reports listed on this website begin with January 2000. Each report has been written on a monthly basis detailing the official position. The website was bullish until September 2000, where I issued an official sell signal on the index, and I reconfirmed the stance October 2000. After a brief switch to a "bearishly" neutral position (temporary state of insanity) in June 2001 and switch back 2 months later, I have been bearish until April of this year. In the April report, I stated that the significant Potential Reversal Zone at 800 of the long-term AB=CD patterns (originally outlined in the November 2001 report) was confirmed. Now, the index is poised to take out the first substantial bear market retracement target.


^SPX 13-JUN-03
Weekly
EMA13 931.54
EMA20 918.02
EMA50 930.17
SMA50 892.80
SMA200 1,183.04
Bollinger(20,2.0)
0.382 @ $1,068.2
1.618BC @ $828.909
1.27AB=CD @ $827.316
0.886xA @ $789.79
0.5XA
0.886XA @ $789.794
1,100.
1,050.
1,000.
950.00
900.00
850.00
800.00
750.00
J A S O N D J F M A M J J A S O N D
2003
The Harmonic Analyzer (TM) : ^SPX
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NASDAQ composite 2000-2005 Review

The the NASDAQ composite offer similar price action to. As this index continue to slide sharply through the critical support in the 3500-3700 area, I realized the next convergence of weekly projections indicated that the index was headed for the 2200 area. I believe this would be a substantial low for the NASDAQ composite index. However, this was a brief stop in a further slide that would take the index as low as possibly 1700. Although I did not one believe it the time, I knew that is severe violation of the 2000 level would trigger this further decline. The the price action lagged severely in this area. Although a minor balance was experienced, the eventual continuation of the decline marked a severe bearish condition that would require much more time to stabilize had reversed the downtrend.

MARCH 2000

"The NASDAQ formed another clear pattern, as the bearish Gartley that completed recently has yielded a nice reversal. The pattern was projected to complete around 5000 – just past the .786 off the high. "
http://www.harmonictrader.com/members/dow/harmonic/markets/nasd0300.htm

note: I had not released the bat yet and was calling this a Gartley

OCT 2000 " If the index breaks below these lows at 3000, the NASDAQ will most likely fall quickly in crashing fashion. Although this is a haunch, technically speaking, there is "nothing but air" below this area. The index may temporarily bounce at 2800. But, the overwhelming convergence of harmonic numbers is in the 2200 area. This would be an extreme target on the downside and represent a significant buying opportunity. "

http://www.harmonictrader.com/members/dow/harmonic/markets/nasd1000.htm

dec 2000

"the NASDAQ sold off sharply through this area without any sign of a reversal. An update was sent out regarding the weakness of the price action and the downside target was moved to 2200. Although it looks very bad, the index is close to the extreme 2200 target. Ideally, I would like to see some type of capitulation in this area. Capitulation would be composed of a 300-400 point down day on 3 billion shares. This is a generalization but it would represent a climax of selling. The index is poised to test this very soon and could represent a significant low for a strong bear market rally at a minimum.

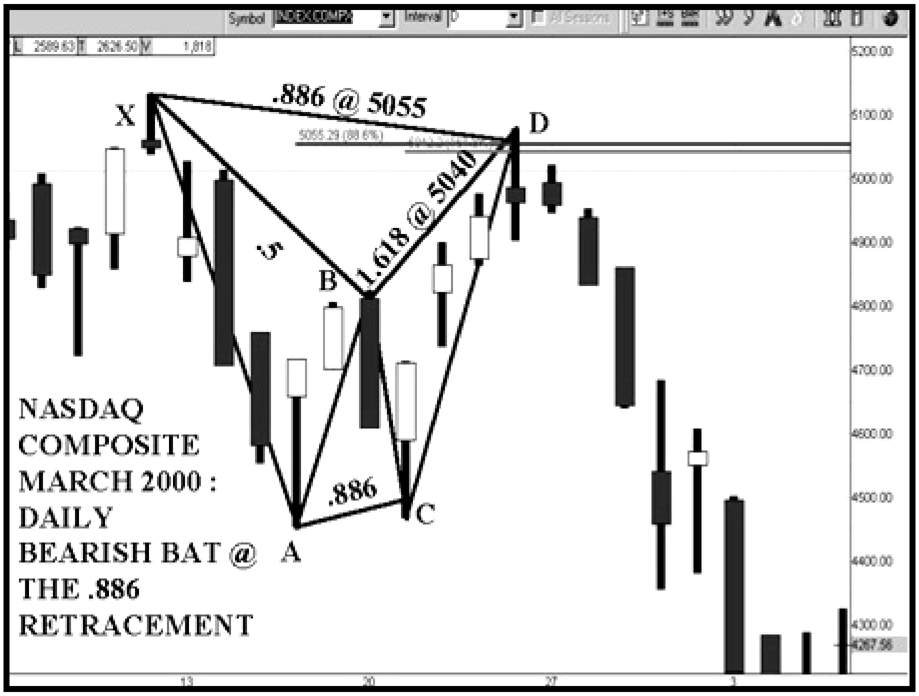
The following chart shows the overwhelming convergence of harmonic numbers in the 2200 area. This scenario was outlined in the October report and is the most likely target for a bounce. The numbers are between 2165 and 2275. Until this area is tested, I remain bearish on the index. "

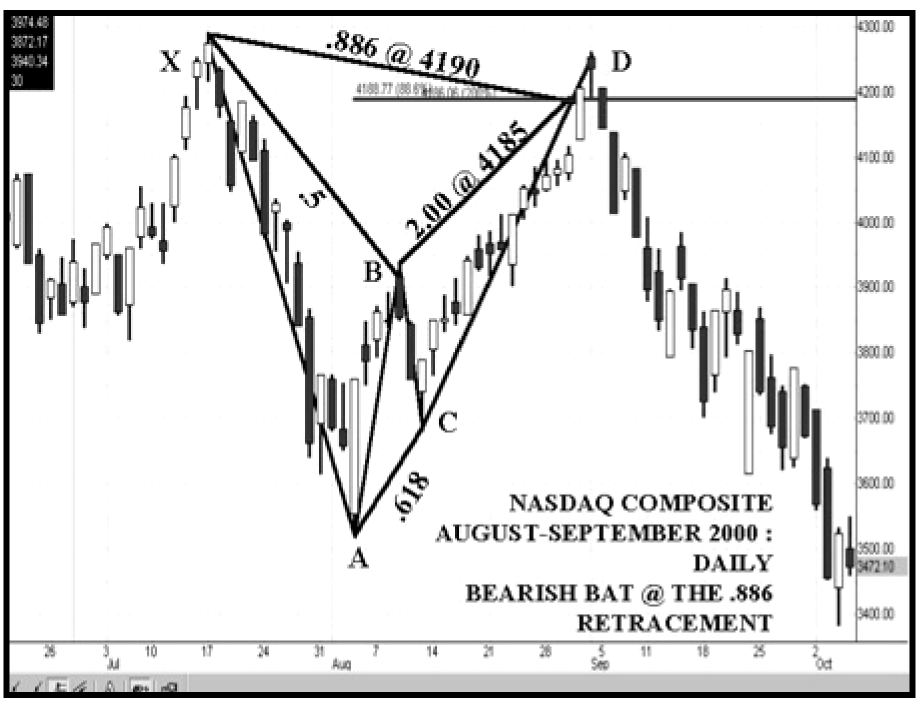
NASDAQ BATS

"Another interesting aspect of this recent bottoming action is the development of yet another new pattern (to be unveiled next month) – 'The Bat.' The Bat resembles a Gartley but uses a .886 retracement for the Potential Reversal Zone (PRZ) at the D point - not the .786! The distinguishing element of this pattern is the B point, which is LESS THAN a .618. The best Bat patterns have a B point at a .382 or a .5 retracement.

The NASDAQ has formed consecutive bearish Bat patterns throughout the past year. Although I have previously identified these as Gartley patterns, they are Bat patterns because they each reversed at the .886 - not the .786. The current bearish Bat pattern is projected to complete at 2930. This area is complemented by the aforementioned .236 and .382 retracements at 2930 and 3020, respectively. Since these numbers converge closely, the index should rally up to this level before retracing.

Here are the other bearish Bat patterns from earlier this year.





In the short-term, the NASDAQ Composite has some room to run. Therefore, I am changing my market position from bearish to short-term Bullish, long-term

Neutral (officially Neutral.). It is still a wait-and-see game beyond this point. But, this 2200 level contains the greatest convergence of harmonic numbers in years and it must be respected."

Dow Jones industrial Average 2000-2005 Review

"The Dow Jones industrial average took longer to reach its ultimate low. After violating critical support in the 9000 area, the only harmonic pattern formation left to consider was a substantial bullish ABCD pattern that completed 6800. In fact, I was interviewed on a Quebec AM radio station in July of 2003 asking my opinion on the markets. Although the index had been following sharply for most of the year, the host of the program was quite dismayed when I explain my reasons for the index to continue lower. In fact, after I offered my projections, my interview was abruptly ended. Simply stated, these guys did not want to face reality.

June 2000 : "The action in the Dow Industrials continues to trade in a tighter range. Sooner rather than latter it is going to break in a direction that will define the trend for the next few months. As the chart illustrates, the index has traded in a downward trending channel, where it has continually rallied to the 78.6% retracement of each the prior sell-off. This channel began with the all-time high in January and the first 78.6% retracement in early April.

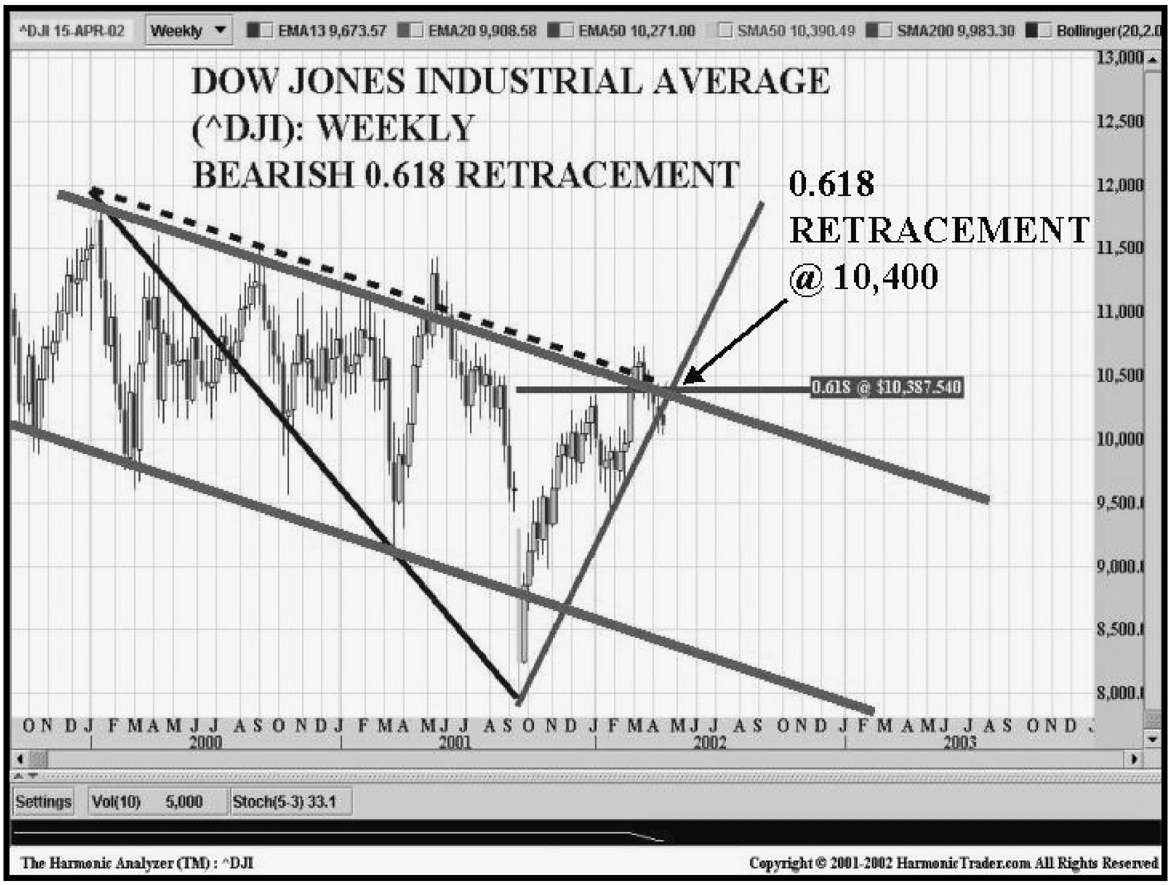
April crash low at 10, 250. If the market is going to rally in the next few months, it must hold these lows. Otherwise, a breakdown past the 10, 250 level would suggest further downside for another 350-400 points before turning bullish. The following chart shows the patterns and Fibonacci numbers that all complete within approximately a 150 points.

The next week or two will clearly dictate the short-term direction of the Dow Industrials. Currently, the previous retracement is consolidating in a very tight, 500 point trading range for the index. If the Dow can hold the lows at 10, 250 and rally through the next 78.6% retracement at approximately 10, 700 (assuming the 10,250 lows hold), the market could see new highs before the end of the year. But, it is important to focus on the 10, 250 area because a breakdown beyond this level would be very bearish for the Dow. "

March 2002: "For now, the index is trading above its current downtrend channel but must crack the 11,300 area for me even to consider moving to neutral position. The whole scenario appears to be another monster bear trap. Also, the impulsive action off the September lows does not represent a "stable" and "maintainable" trend. In fact, the 1974 and 1987 collapses required years to recover its losses – which is a more favorable technical scenario than the current recovery. In addition, the existence of many bearish patterns that have yet to completely resolve their action suggests that the index needs time, if it is going to assert itself to new highs. For these reasons, I remain bearish on the index. "

http://www.harmonictrader.com/members/dow/harmonic/markets/dow0302.htm

April 2002:



"The Dow Industrials have chopped around quite a bit in the past month without much net result. The index has sold off recently, closely testing the 10,000 mark. The action has been lackluster, as most of the rallies are one-day phenomenon, while the declines have slowly dragged. … The index has held up well, despite recent breakdowns of GE (mentioned in last month's report) and Microsoft. It is interesting to note that both of these stocks are approximately 50% off their all-time highs, while the overall Dow Jones Industrial index is not even 20% from its all-time high. Yes, these two stocks were the most important big cap leaders of the" blow off" bull run that started in 1995 and ended early 2000. If we are in a new bull market - as many are claiming, why are these two stocks still languishing within their respective bearish trends? …. There are many market analysts making claims of the beginning stages of the first bull market of the 21st century. I've heard overly bullish targets anywhere from 15,000 to recent call by a well-known money manager for 30,000 in six years. I think these claims warrant caution. Technically, these price targets can not be even considered until certain resistance levels are breached. …. The "Line in the Sand" for such a break out is above the 11,300 area - the all-time 0.886 retracement from the January 2000 high to the September 2001 low. It is a number that I have in the back of my mind and I have mentioned it in a few past reports. But, I continue to stick with my bearish overall position for several reasons. Let's look at the chart."

- **First of all, the trend is still down.** It is amazing that some analysts are calling for a new bull market when there are no technical signs that would support such an argument. As noted by the red channel, the Dow Industrials have failed to break out of the two-year down trend.

- **Lower highs and lower lows.** Each successive critical high and low since the January 2000 peak has continued to trade at lower levels.

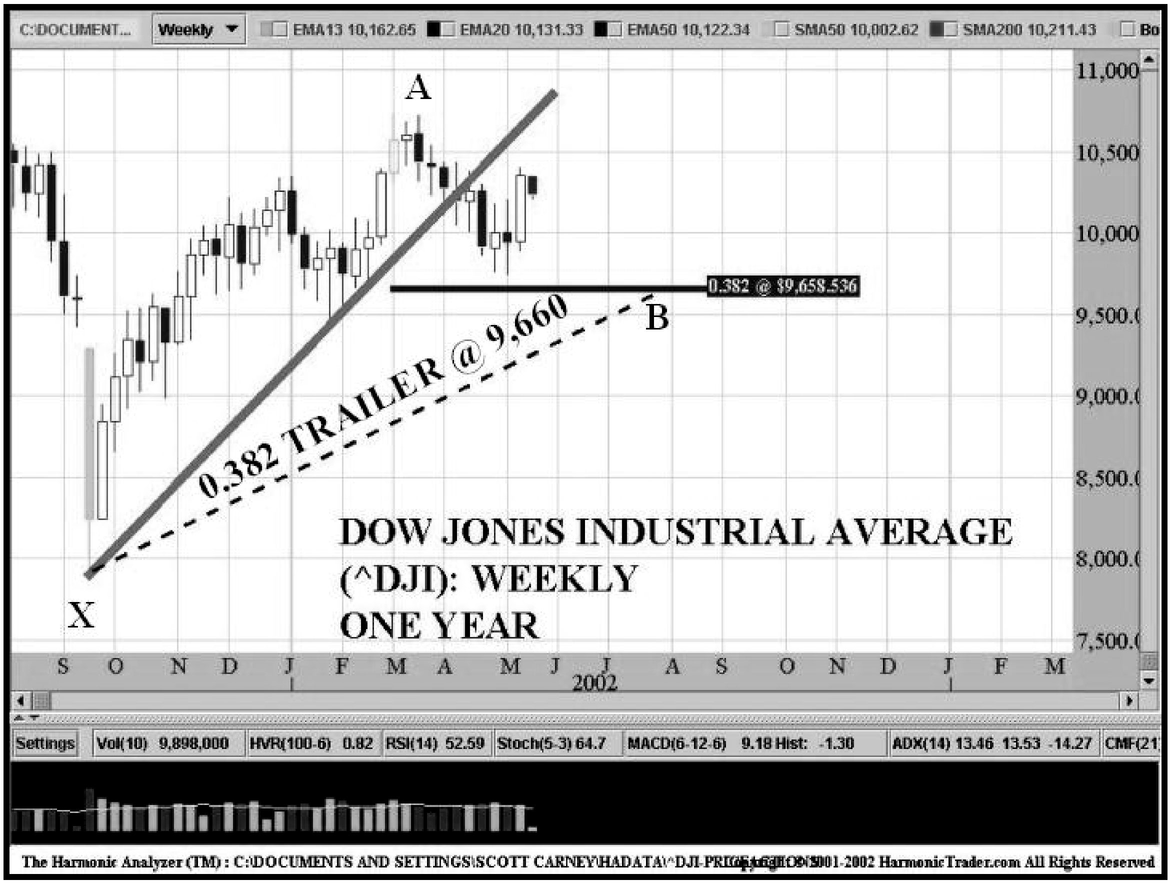
- **Lack of clear pattern.** Throughout the Dow's history, the index has signaled new market up trends with distinct bullish patterns, including distinct secondary tests of prior critical lows. The rally since September has been more impulsive than constructive. This impulsive action can be observed in the Dow Jones Transports, as well. Essentially, the index must provide a significant retest of the September low to establish a constructive and stable base.

… I will outline my longer-term downside targets over the next few Dow Industrial reports. Although it is a long way down from current levels, my first target for the Dow Jones Industrial Average is 6800. There I said it. In May's report, I will explain my reasons. In the short-term, the Industrials have declined after testing an important 0.618 retracement at 10,400, serving as the critical resistance. I favor a continuation of the recent selling and I'm looking for the index to begin to break under 10,000 to as low as the 9500 level. Remember, the longer-term trend remains bearish and unless convincing upside action materializes, the Industrials will continue to slide."

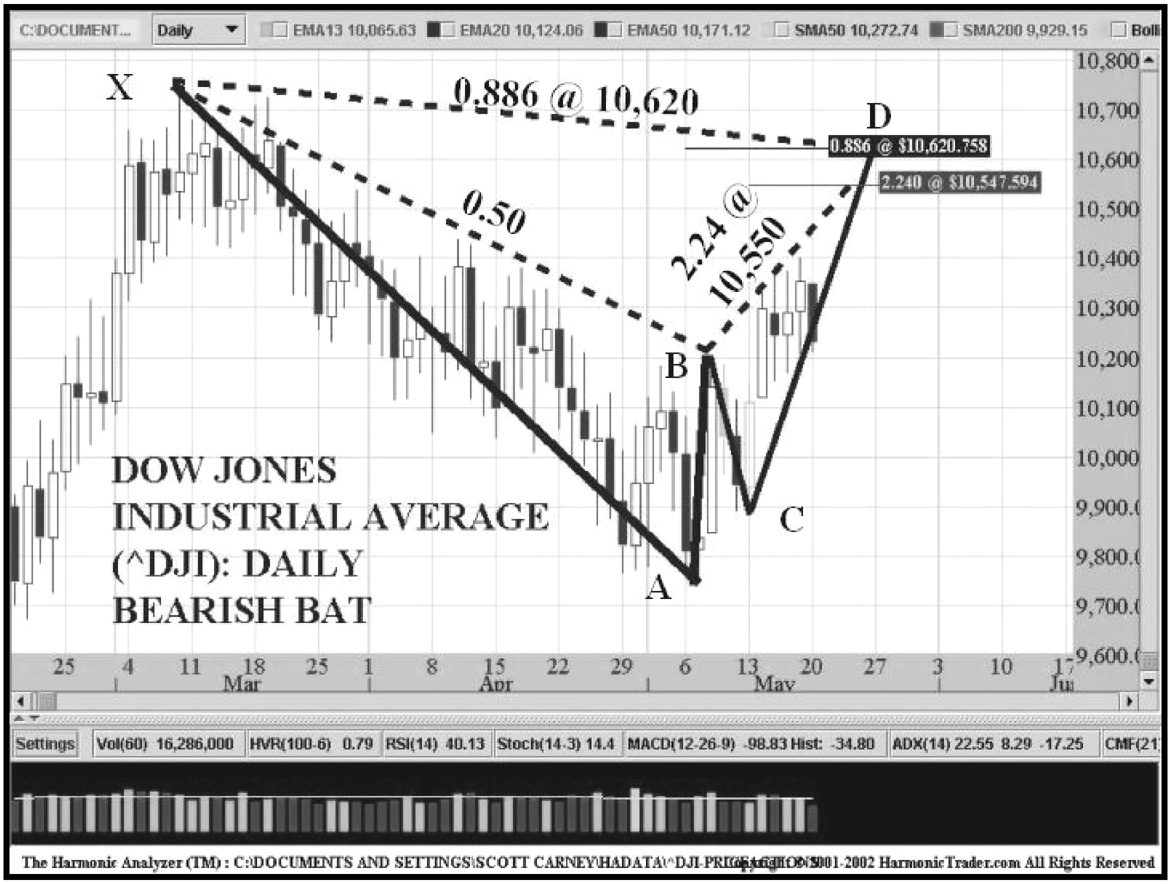
May 2002

" The Dow Jones Industrials sold off last month below the 10,000 level but the index did not quite reach the 9500 level mentioned in last month's report. The

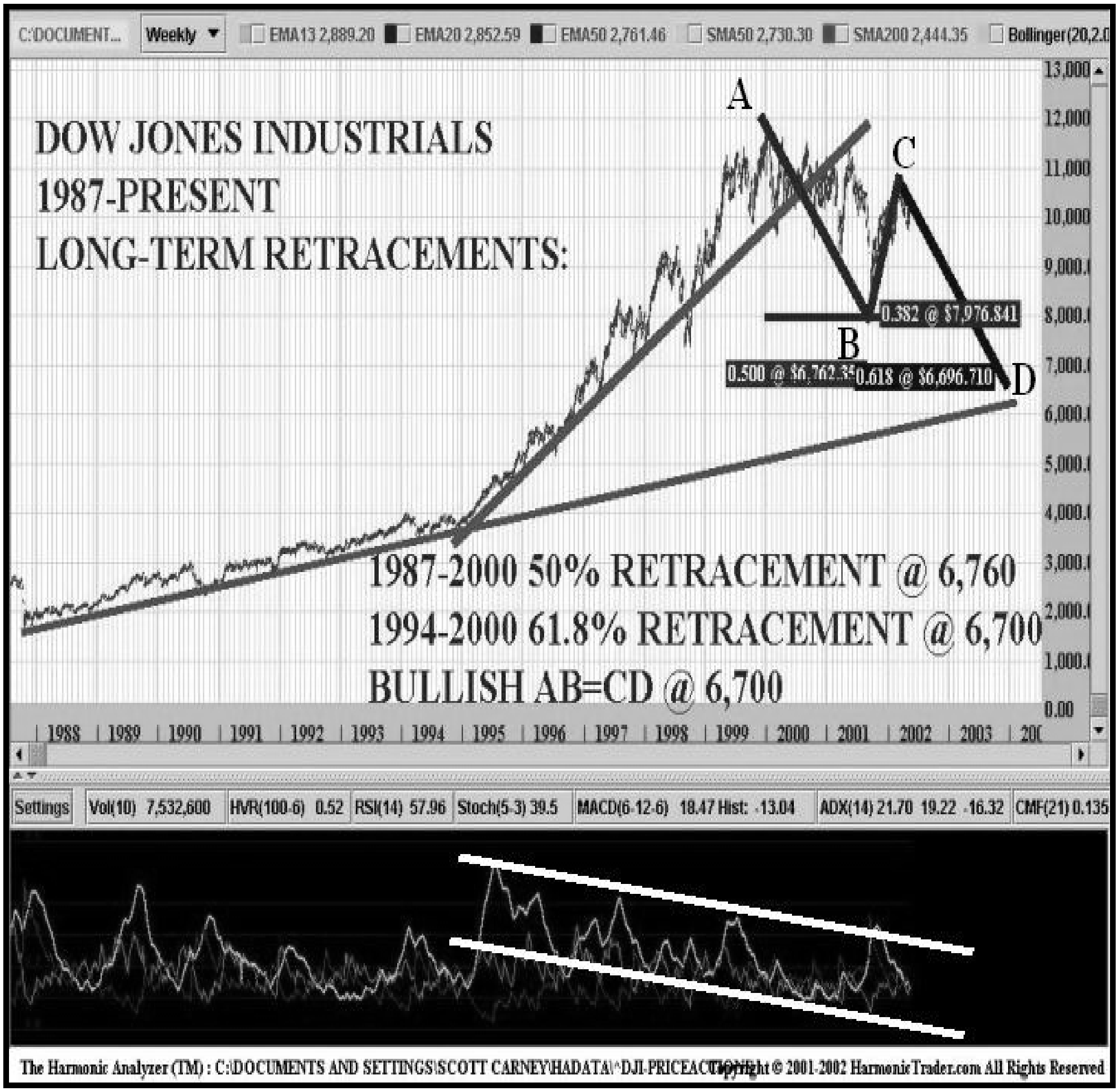
Industrials rallied sharply after nearly testing the 0.382 retracement at 9,660. Despite the rally, the outlook for the index remains bearish.



" On the weekly chart, the index has violated a significant up trend line from last September's low. This breakdown is a sign of longer-term weakness and could signal the resumption of the primary bearish trend. It is important to note that this year's high above 10,700 represents significant long-term resistance. This level was mentioned in March's report, and it represents an important 0.618 retracement. .. The price action on the daily chart is shaping up to reinforce the predominance of the primary bearish trend. The recent rally off of the May low is in the process of forming a Bearish Bat with a Potential Reversal Zone between 10,550-10,620. This area will represent a critical turning point for the index, as the bearish pattern formation and the current year's high will create substantial resistance. In the short-term, the index could experience a small rally, as the price action gravitates towards the completion of the pattern."



"As I mentioned in last month's report, the longer-term picture remains bearish. This 15-year chart – starting from the crash low of 1987 – reveals several interesting aspects of the future action. Clearly, the sharp up trend from the 1994 low to the 2000 high has been violated. Furthermore, the chart shows that the 15-year bull trend from the 1987 low is quite a distance from the current level.



It is important to be mindful of these two trend realities.

1. Obviously, the 1994-2000 rally, as defined by the sharp up trend is over.
2. The 15-year trend line represents substantial support and defines the lower limit of any significant potential correction.

The Dow Industrials are consolidating – more aptly termed distributing – below the bull market up trend of the second half of the 1990s. ..The Harmonics of the long-term price action confirm the potential support of the long-term up trend. Assuming the current year's high will remain untested, a potential Bullish AB=CD completes at 6,700. This area is complemented by two critical retracements from the 1987 low and the 1994 low, a 50% retracement at 6,760 and a 61.8%

retracement at 6,700 respectively. These levels converge with the 15-year trend line and would represent a correction worthy of resuming the long-term bullish trend… The overall market position for the Dow Jones Industrials remains bearish. It is important to focus on the short-term bearish scenario, illustrated in the daily chart. However, I felt compelled to outline the larger scenario that I have been monitoring for quite some time. I have been officially bearish on this index for two years and I will not change this position until one of two things happen:

1. A significant correction to the aforementioned long-term levels or
2. A clear and substantial violation of the primary bearish trend.
   For now, it is important to focus on the short-term daily set up and the resistance at 10,600.

FEB 2003: The 7000 test

"Time and time again throughout the past three years the failure of the Dow Jones Industrial Average to make any progress within the overall bearish trend presents further technical difficulties for the index. The 6800 target remains as the MINIMUM objective for this bear market. The next two weeks will be critical for the index, as the Dow attempts to hold the 7000 area. As I said in last month's report, 'the Dow could decline sharply after sinking below the 8000 mark.' We are seeing the initial developments of this year's double-digit dip. The next two weeks will define the extent of this sell-off and provide greater indication of degree of this bear market. The official position remains bearish, as the index approaches the minimum bear market objective, while the possibility of a larger downside scenario becomes more likely. "

The Bullish Bat


^DJI 18-OCT-02
Daily
EMA13 8,809.36
EMA20 8,965.23
EMA50 9,377.32
SMA50 9,542.07
SMA200 9,819.43
Bollinger(20,2.0)
DOW JONES INDUSTRIALS
(^DJI): DAILY
PRICE ACTION IN THHE
POTENTIAL REVERSAL ZONE
The Harmonic Analyzer (TM) : ^DJI
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The Lessons from the Bear Market of 2000

It was these experiences that changed my perspective on the entire Harmonic Trading approach. I realized that the patterns were not ultimate buy or sell signals. Moreover, the patterns were signposts of potential future action. This was a difficult admission for me because it devalued the significance and potential for the strategies to be a trading methodology. I learned a great deal during this time. In the long run, this was an important learning process. It made me focus on price action in the completion area of harmonic patterns more than the patterns themselves. Furthermore, it opened a new attitude towards these techniques. It led to the evolution of utilizing these patterns within the context of price action as they related to overall trend and other technical measures.

It's not the Pattern's Fault…

It's easy to say that all of the monster bullish setups failed from '00-'02. So ht does not work. No. In fact, the numerous pattern bullish failures were screaming that the predominant trend in many of these equity markets would remain bearish for quite some time. Therefore, the system did not fail. The demonstrative price action in many cases clearly signaled the continuation in many markets, as most of the significant bullish patterns on daily and even weekly timeframes yield little to no support at these harmonic zones. As the price action in the S&P500 index exemplified, the violation of the long-term support at 1300 indicated that the next harmonic possibility was at 800. As the market continued to decline for most of 2002, I continually monitored the price action. Honestly, I was skeptical that these targets could be reached at first. But, the violation of critical harmonic support levels was enormous evidence of a serious continuation of the predominant bearish trend.

My point is that the bear market of 2000-2003 was a severe challenge to the Harmonic Trading methods and the approach as a profitable trading system. But, these difficulties inspired a more integrative approach. Although Harmonic Trading of the Financial Markets: Volume One presented unprecedented strategies that have expanded the application of the basic techniques, this book reflects a greater integrative foundation to define potential reversal areas that are confirmed by multiple methods.

Chp 2: The importance of bias

Bias

The Magnet Effect

Are you gravitating to a pattern completion or failing a distinct structure tht points to a continuation of the predominant trend

The concept of bias can be measured in a variety of technical means.

Indicators, oscillators and overall trend analysis are critical to analyze the relevant position of harmonic patterns.

Anticipation vs. Reaction, Expectation

Positioning a Position – letting the patterns indicate your relative spot on the chart

Anticipation vs. Reaction

The difference between these two general approaches to the market entails the varying degrees strategies and represents two distinct perspectives of interpreting the information. I believe most traders execute trades based upon a series of reactive responses with regard to the set of circumstances within their trading realm. Furthermore, it seems that more mistakes are made as a consequence of reacting to market conditions rather than guiding trading behavior based upon an anticipated set of circumstances. In my own experience, many of mind worst mistakes were as a result of reacting without thinking. The

Anticipation involves a greater degree of patience, experience and skill. From from a Harmonic Trading perspective, anticipation is required for pattern completions, trade management and overall consistency of trading performance.

For example, to anticipate the completion of the pattern, all elements of the setup must be met in order to generate a valid trade signal. Although all traders must react appropriately to current market conditions in order to consistently profit, I believe it is essential to properly anticipate your trading behavior based on a sound set the of rules. Anticipation requires an element of preparation when executing a trade.

Alignment vs. Position

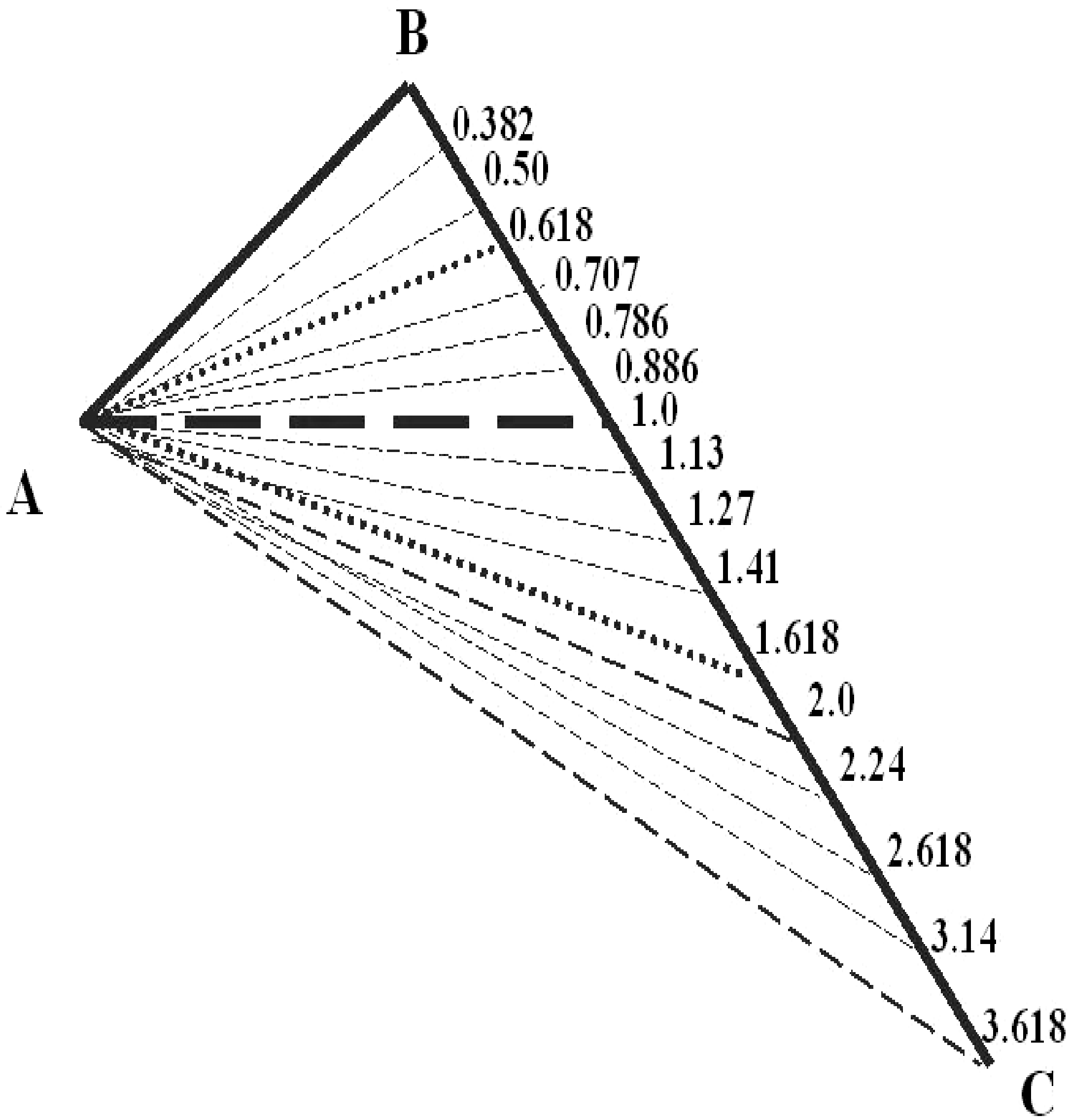
Chp 3: Harmonic Impulse Waves

IMPULSE MOVES 1618;2.0 AND 886

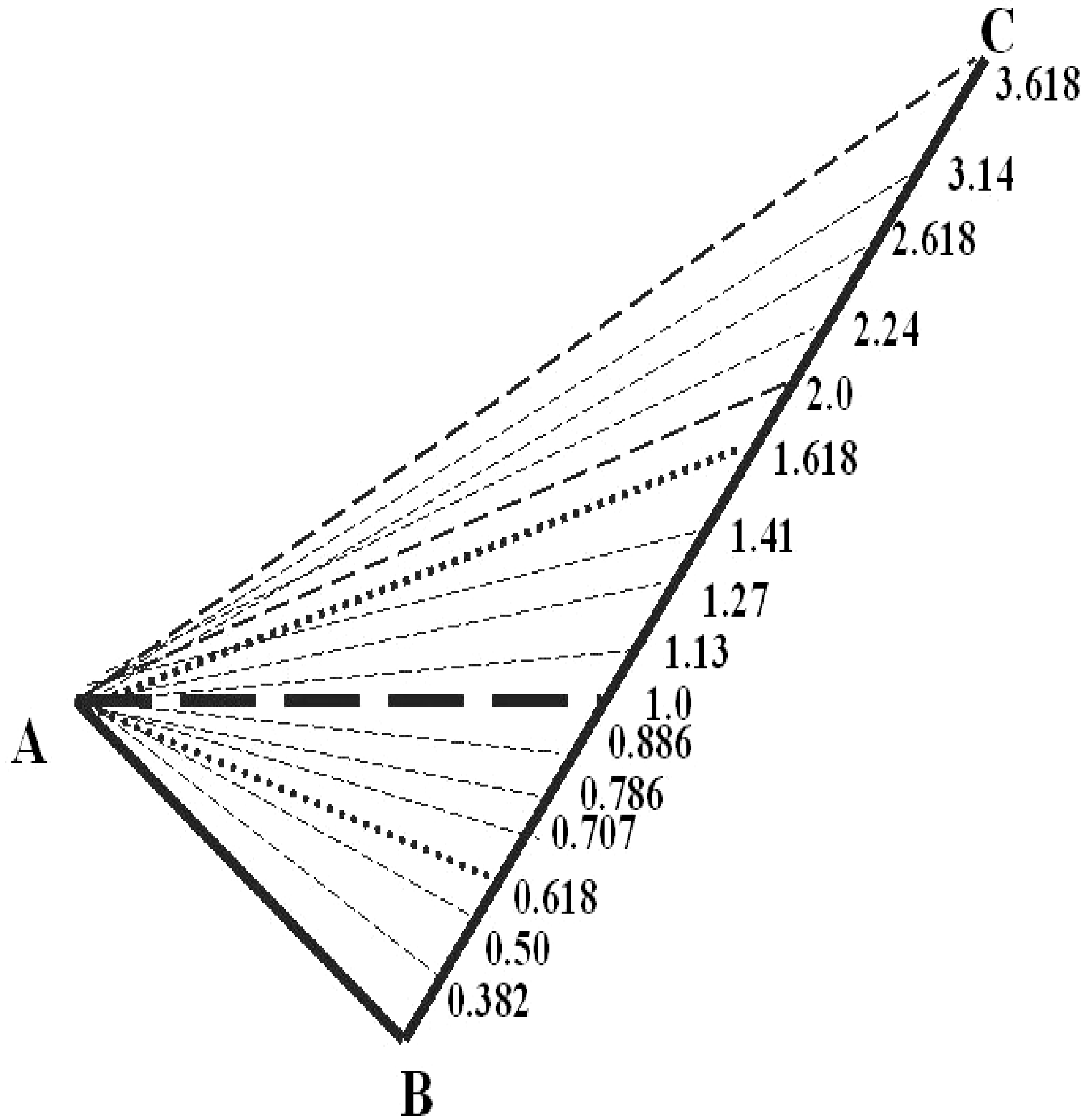
Harmonic Ratio Progression

The need for some model

Bullish Harmonic Ratio Progression

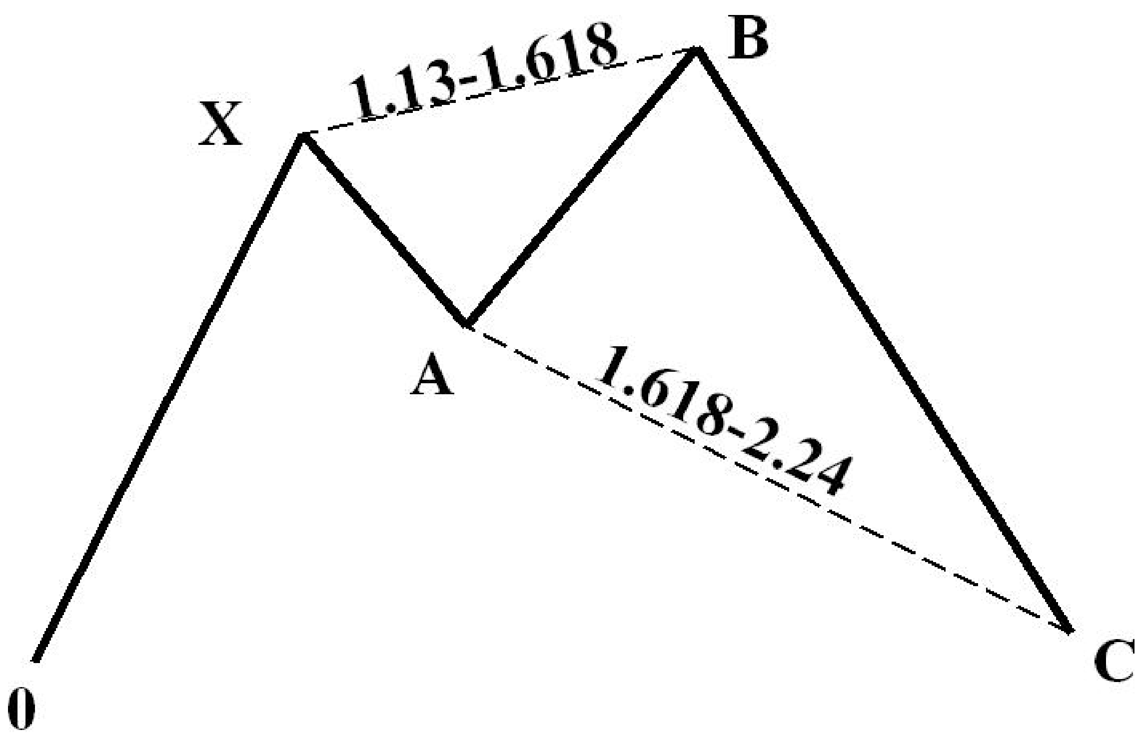


Bearish Harmonic Ratio Progression



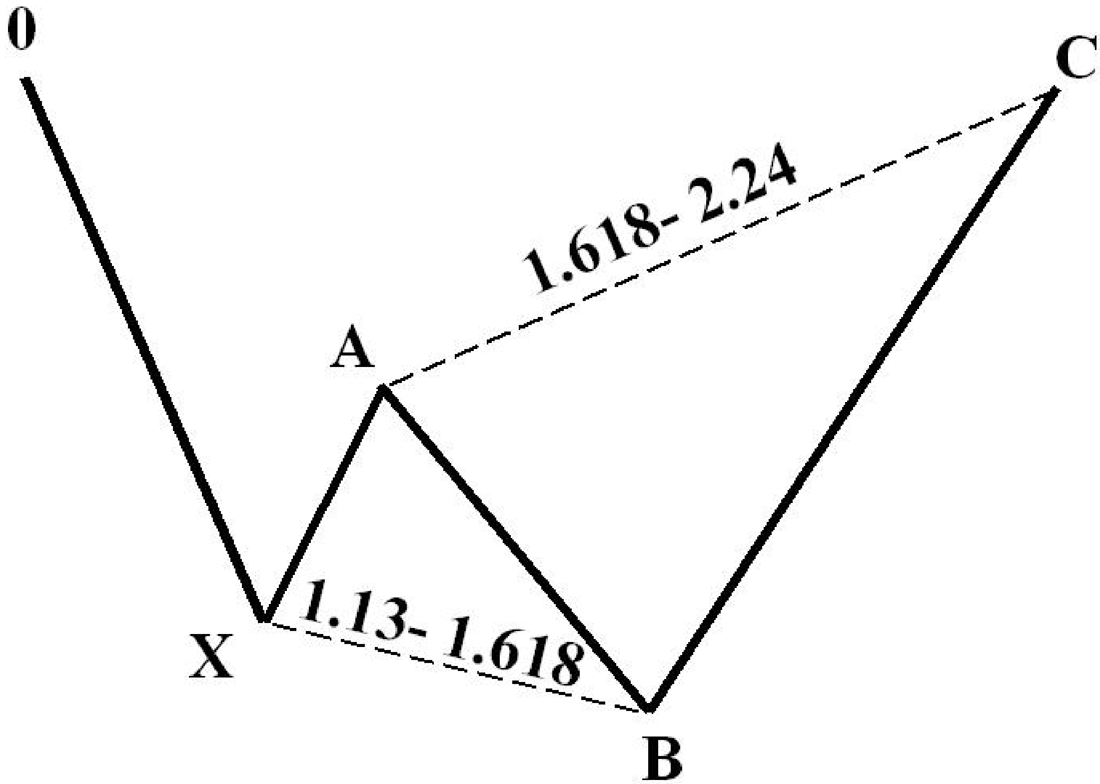
Harmonic Impulse Waves

Bullish Harmonic Impulse Wave



Example

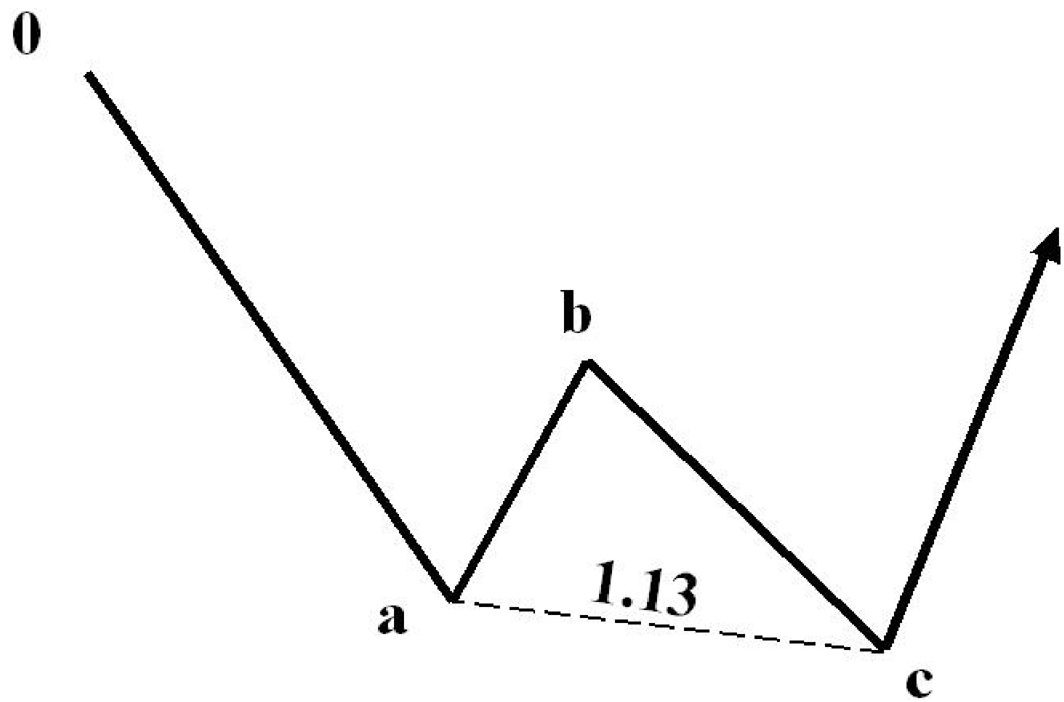
Bearish Harmonic Impulse Wave



Example

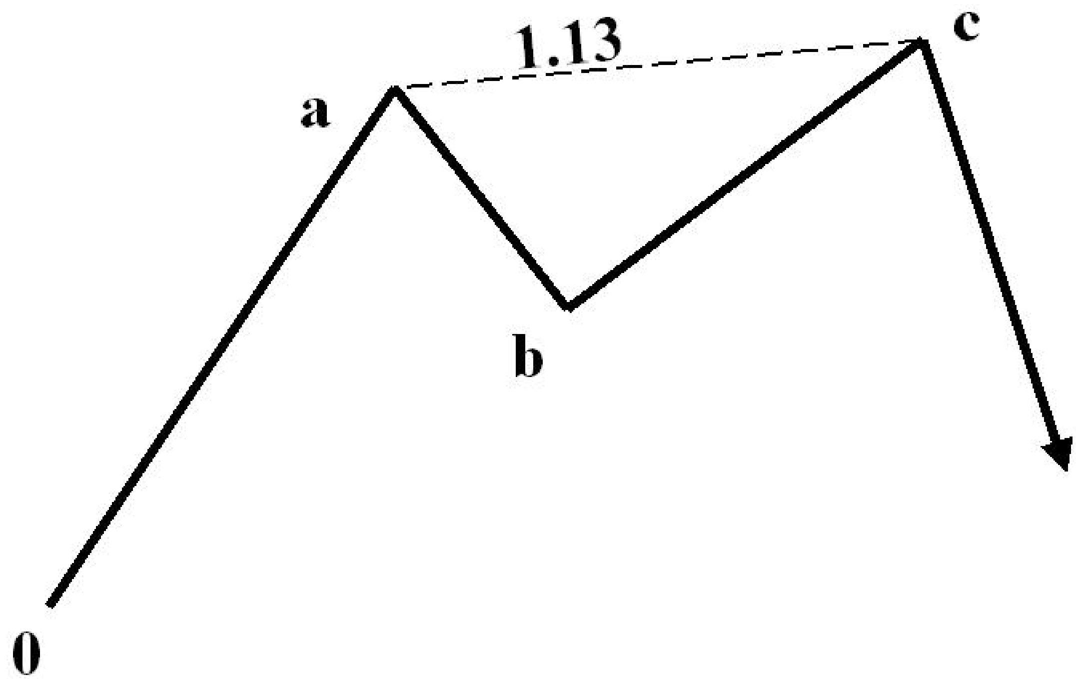
Failed 1.13 Wave

Bullish Failed 1.13 Wave



Example

Bearish Failed 1.13 Wave



Example

Chapter 4: Patterns within the Trend

Two types:

1. **Patterns with the Trend**
2. **Violation of Patterns against the Trend**

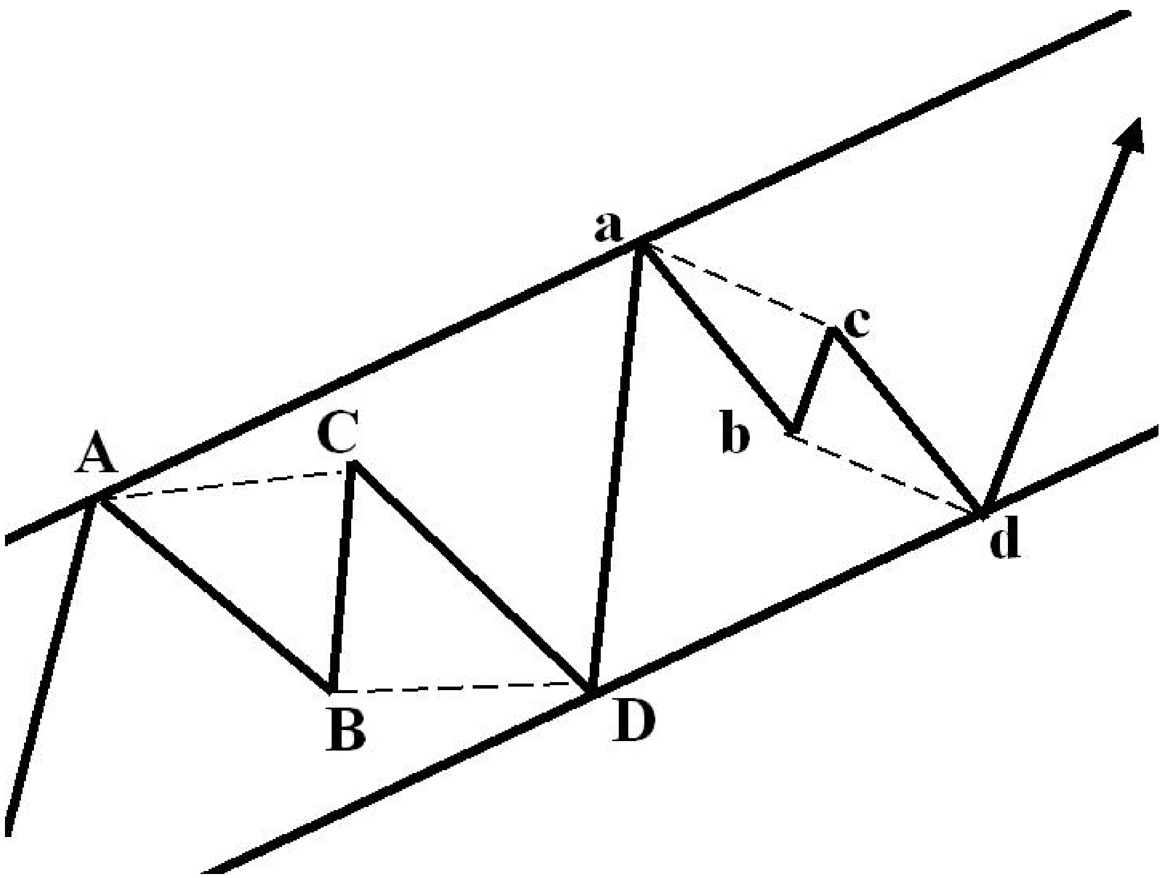
Patterns with the Trend

AB=CD Patterns within Trend Channels

Use as an approximate target in conjunction with other measurement techniques to define the entire area with the constraints of the trend channel.

Bullish AB=CD Patterns within Trend Channels

Bullish AB=CD patterns acting as a continuation signal within the bullish trend.



NASDAQ Composite ($COMPQ): Daily

Throughout 2004-2005, the NASDAQ Composite formed 3 distinct Bullish AB=CD patterns on the daily chart within the context of the predominant bullish trend.

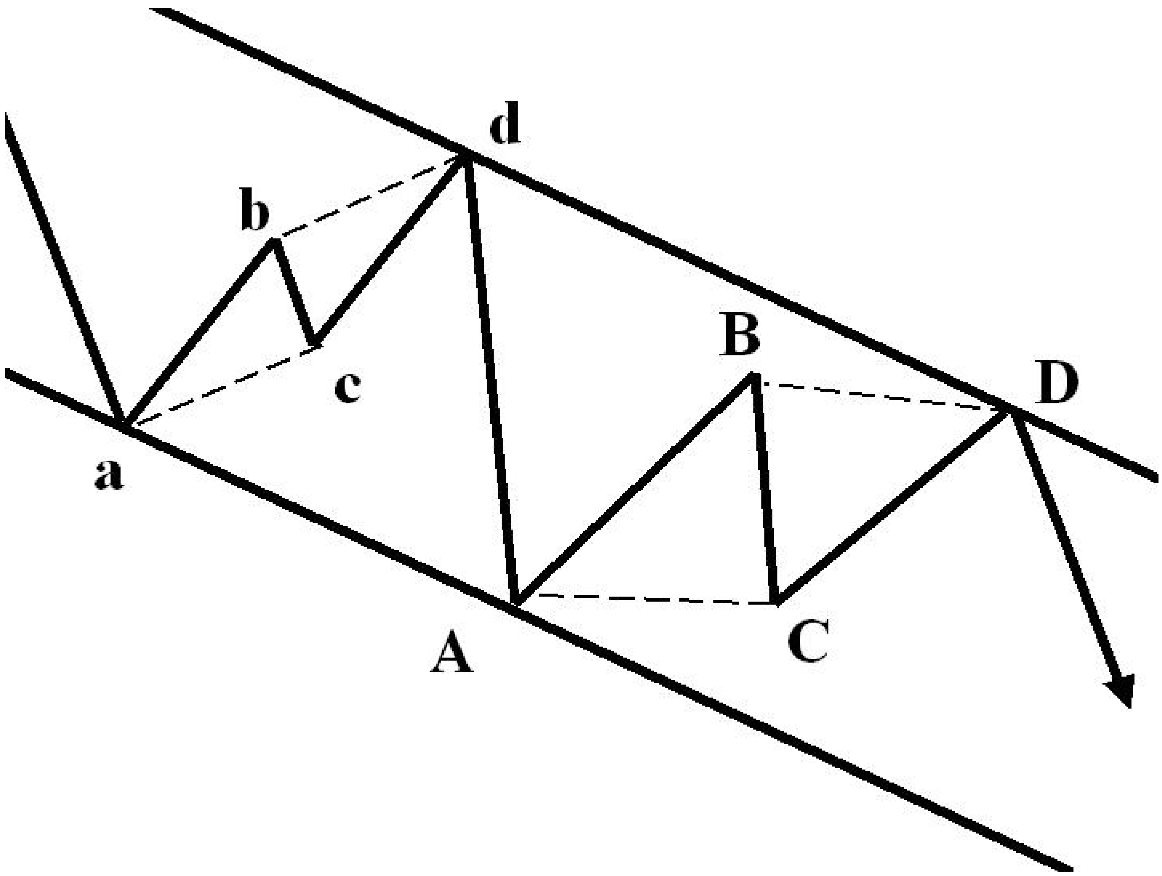
NASDAQ Composite ($COMPQ): Daily
Bullish AB=CD #1: Completed August 2004

NASDAQ Composite ($COMPQ): Daily
Bullish AB=CD #2: Completed April 2005

NASDAQ Composite ($COMPQ): Daily
Bullish AB=CD #3: Completed October 2005

Bearish AB=CD Patterns within Trend Channels

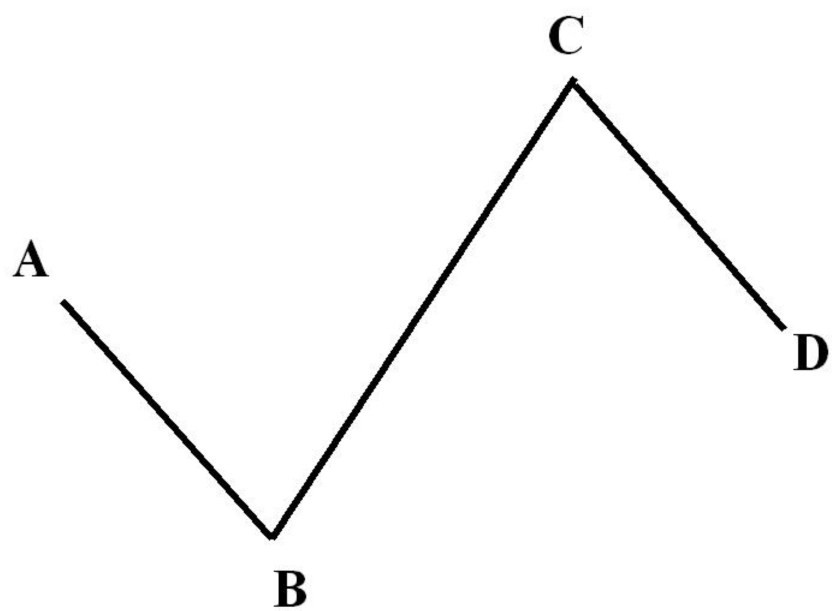
Bearish AB=CD Patterns acting as a continuation signal within the bearish trend.



Reciprocal AB=CD:

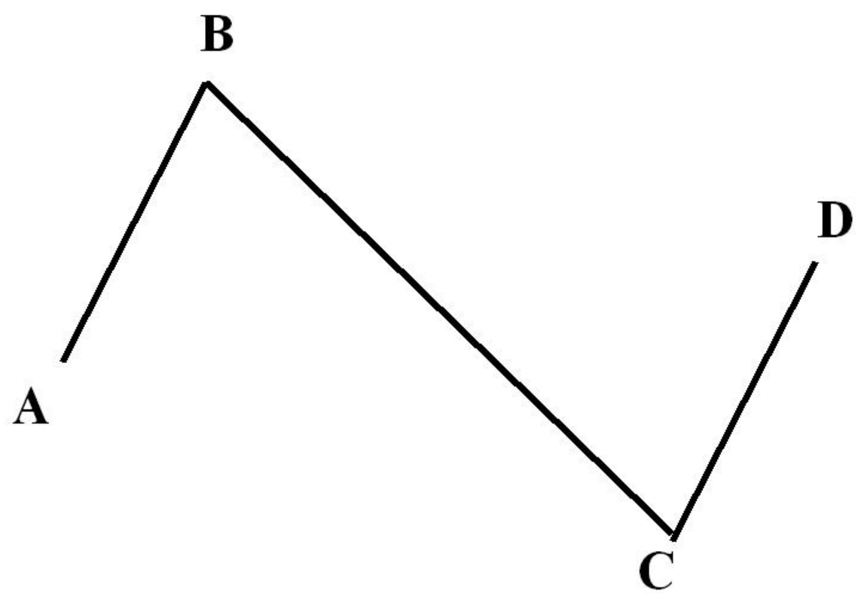
A Reciprocal AB=CD pattern is typically a shorter counter move of equal length within a longer trend. They look like a lazy "Z" or "S."

Bullish Reciprocal AB=CD



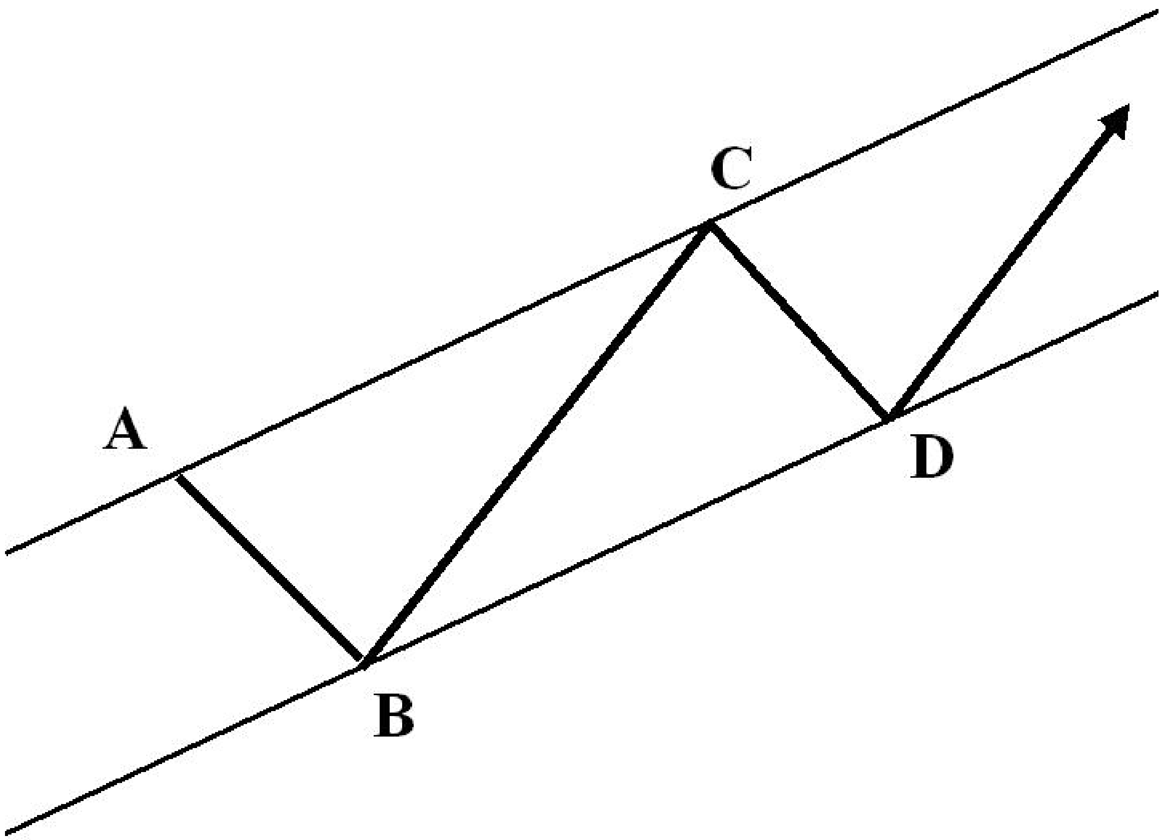
example

Bearish Reciprocal AB=CD

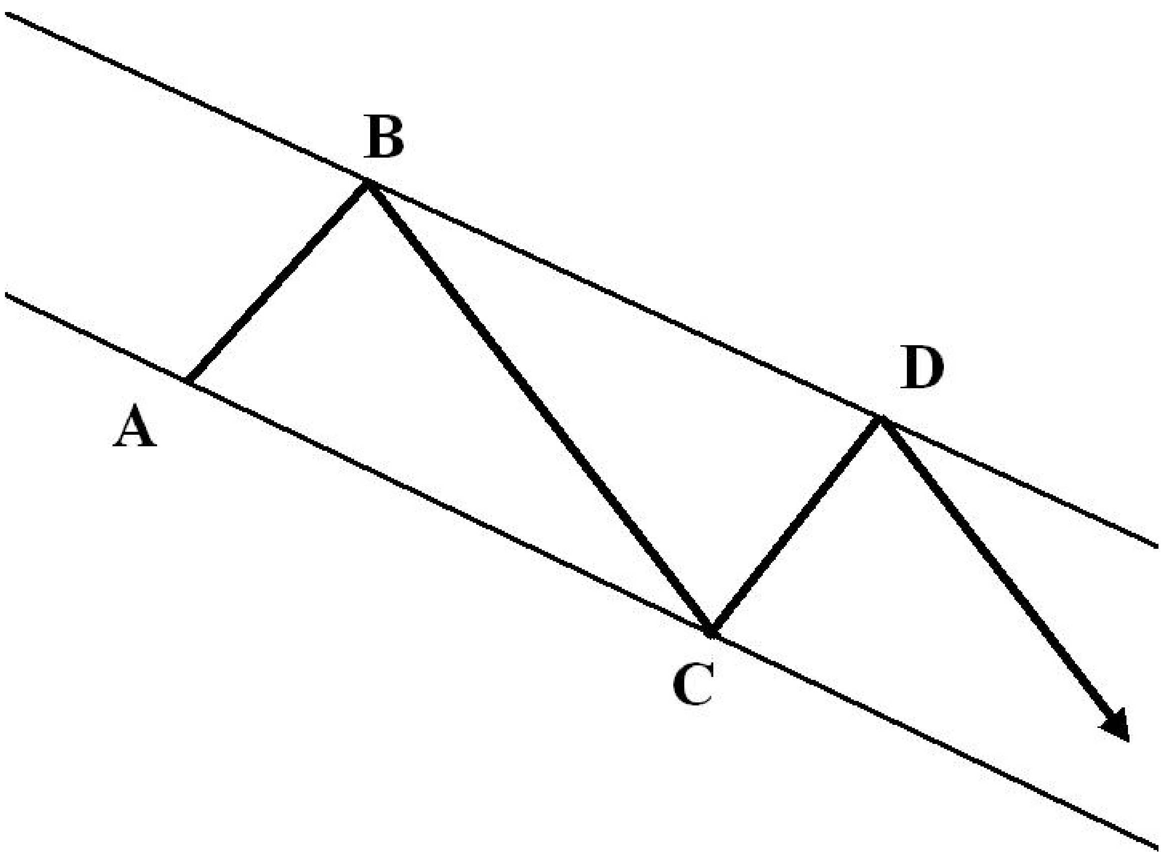


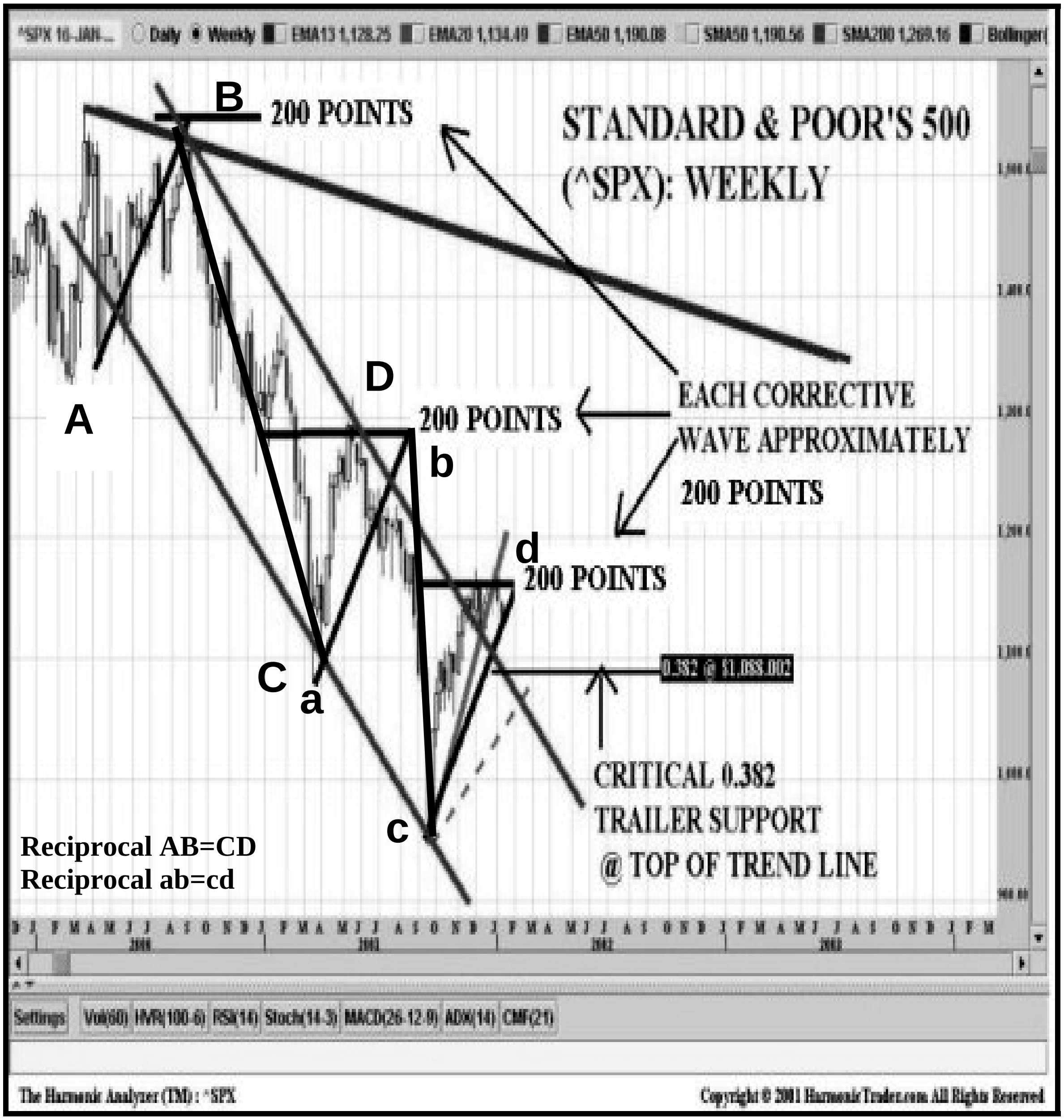
BEARISH EXAMPLE

Bullish Reciprocal ABCD Patterns within Trend Channels



Bearish Reciprocal ABCD Patterns within Trend Channels




B
200 POINTS
STANDARD & POOR'S 500
(^SPX): WEEKLY
D
200 POINTS
EACH CORRECTIVE
WAVE APPROXIMATELY
200 POINTS
A
b
d
200 POINTS
0.382 @ $1,088.002
C
a
CRITICAL 0.382
TRAILER SUPPORT
@ TOP OF TREND LINE
c
Reciprocal AB=CD
Reciprocal ab=cd
The Harmonic Analyzer (TM) : ^SPX
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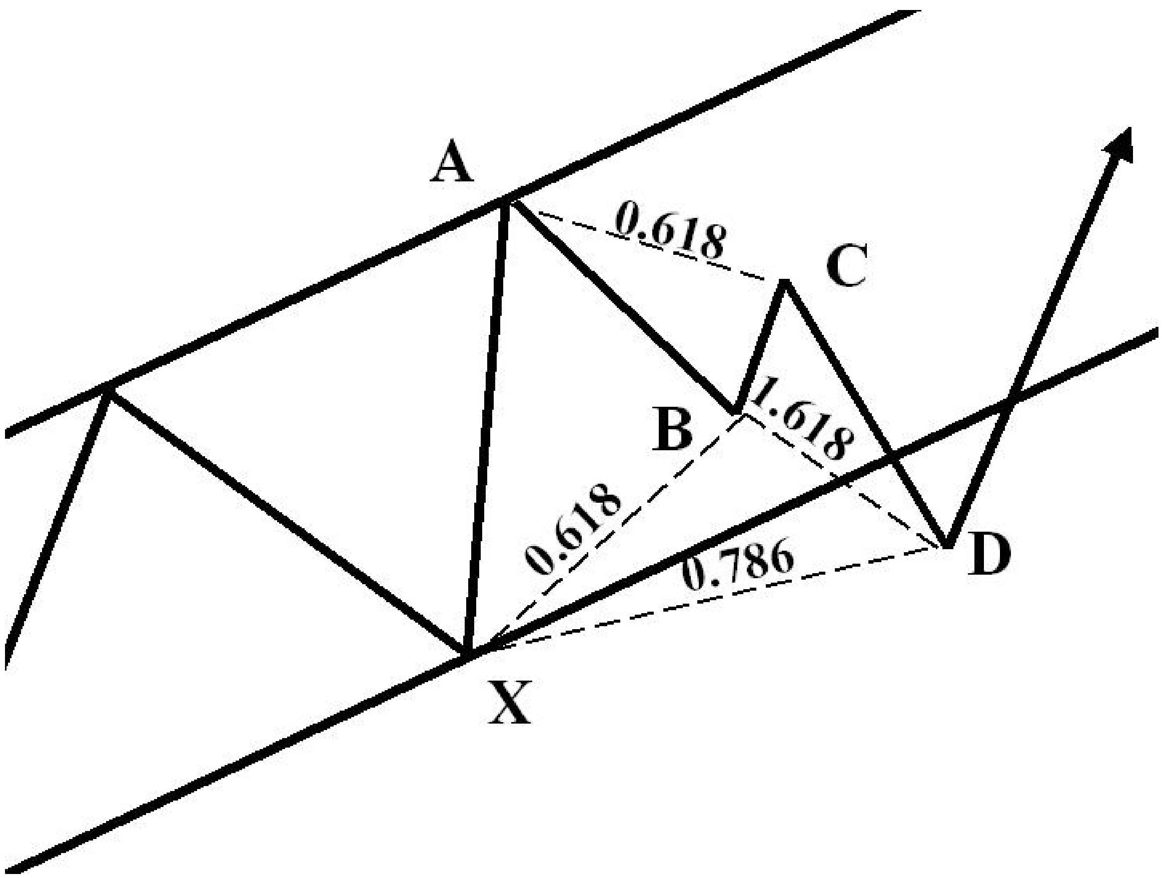
Complex Patterns within Trend Channels

Bullish Complex Patterns with the Trend Channels

Bullish Pattern acting as a continuation signal within the bullish trend.

Outside the bottom trend channel

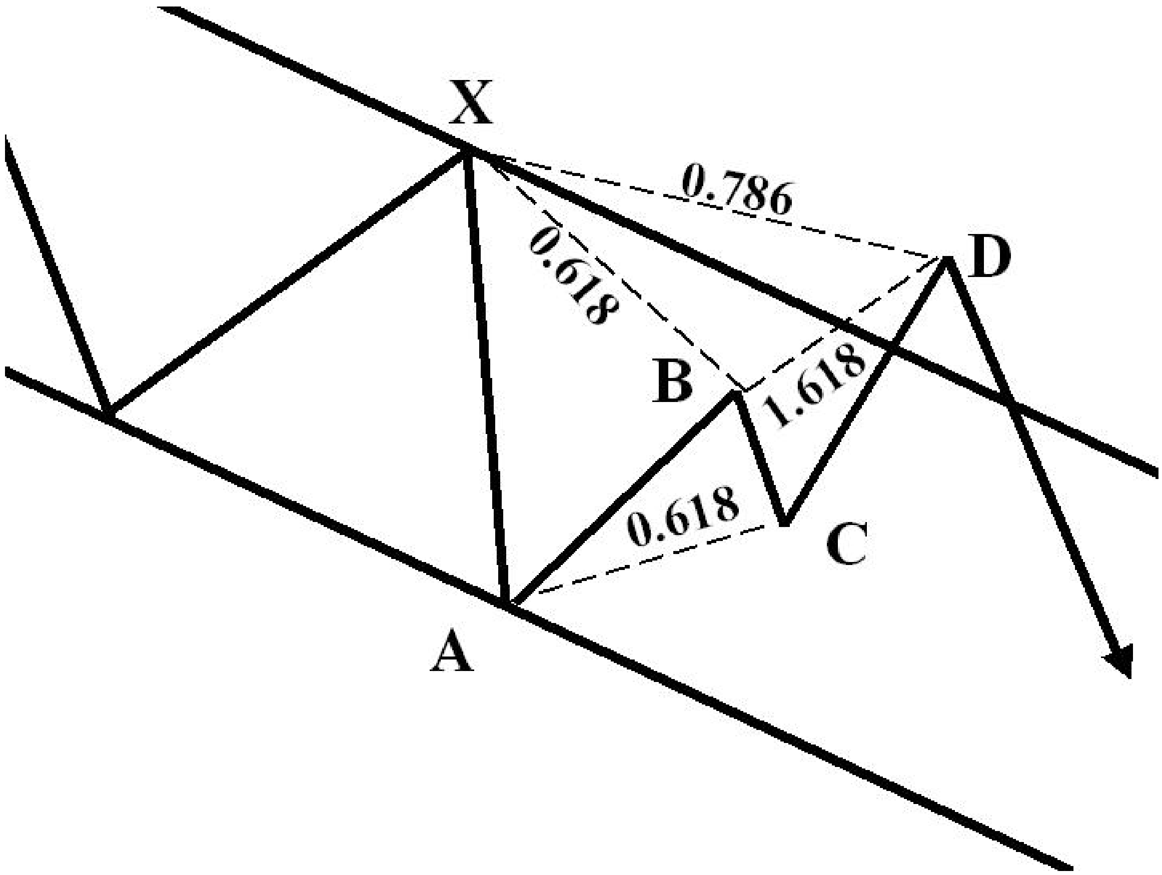
Principle of Harmonicity emphasizes alignment over position with the sequence triggering the pattern completion within the larger trend.



EXAMPLE

Bearish Complex Patterns with Trend Channels

Bearish Pattern acting as a continuation signal within the bearish trend.



EXAMPLE

Violation of Patterns against the Trend

Failed ABCDs within Trend Channels

Bullish Failed ABCDs within Trend Channels

Edit ...
MLNM
tide
$tran
BOT
vlo
sbux
es_z5
$xoi
ES_H6
NQ_H6
siri
biph
RIMM
ERTS
$indu
$spx
$compq
yhoo
eur_a0-fx
siri
$sox
EXPE
NG_f6
sndk
EUR_A0-FX 20-DEC-05_09:45
15min
EMA13 1.20
EMA20 1.20
EMA50 1.20
SMA50 1.20
SMA200 1.20
Bollinger(20,2.0)
zz 0.0010
zz 0.01318
zz 0.1
zz 1.0
zz 10.0
A
0.786AB
C
D
1.270BC @ $1.194
AB=CD @ $1.194
1.2075
1.2050
1.2025
1.2000
1.1975
1.1950
1.1925
1.1900
1.1875
1.1850
14 Dec
15 Dec
16 Dec
19 Dec
20 Dec
The Harmonic Analyzer (TM) : EUR_A0-FX-15MIN
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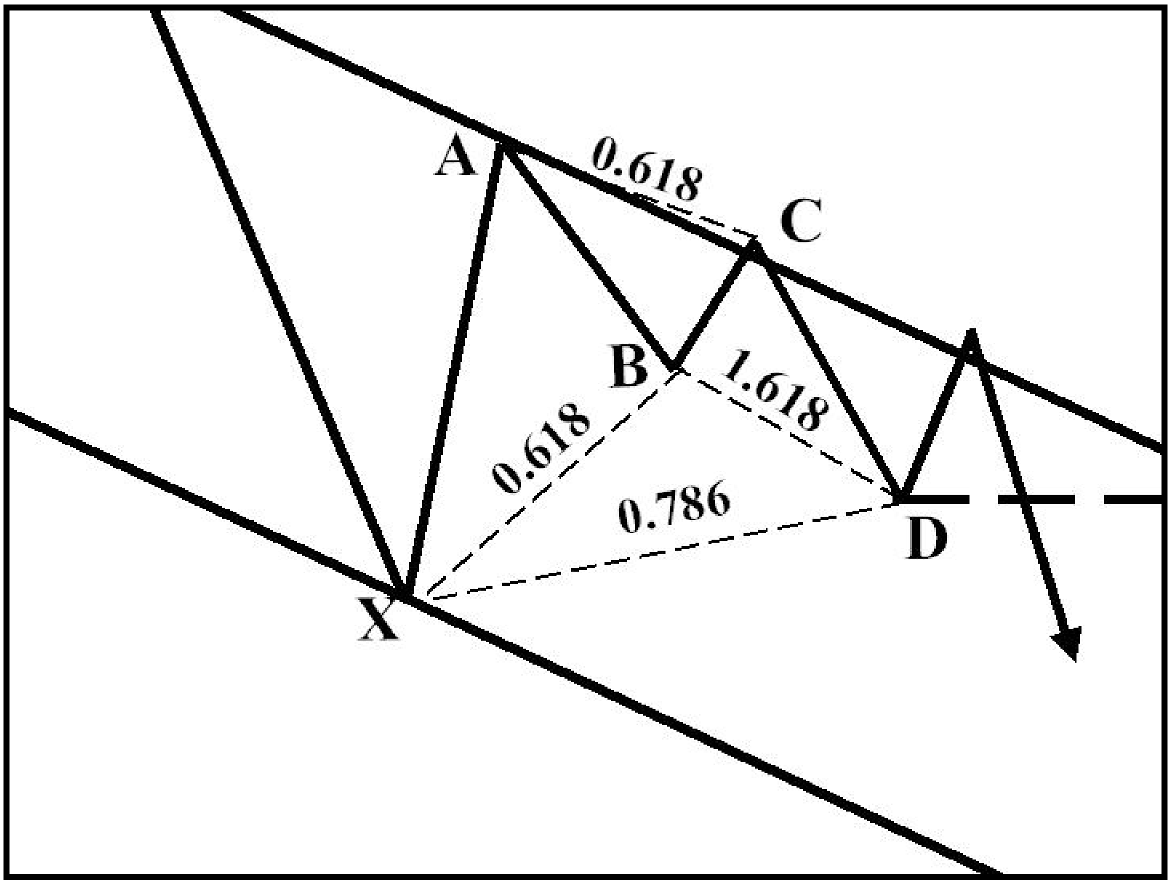
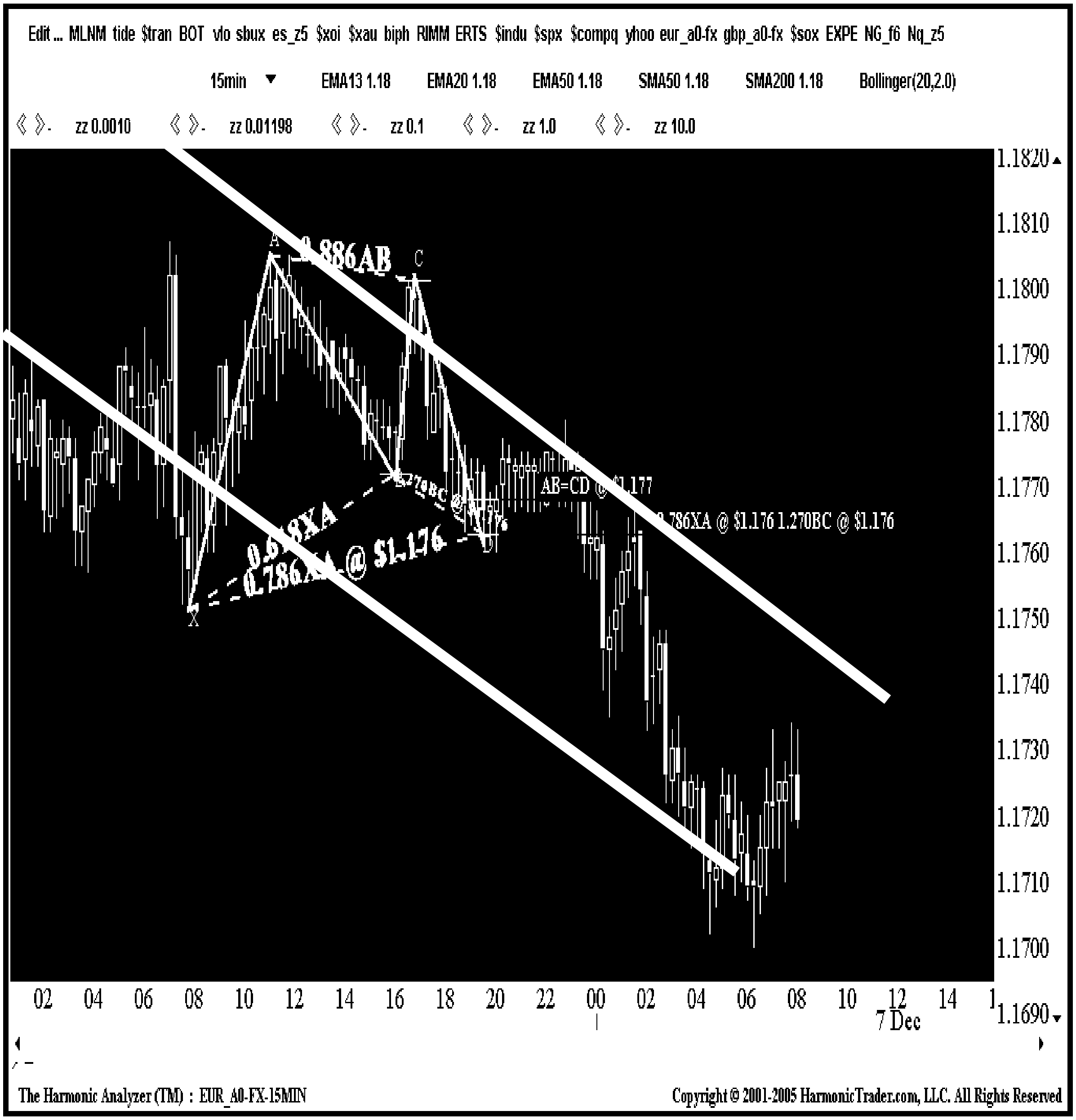
Bearish Failed ABCDs within Trend Channels

Failed Patterns Against the Trend

Bullish Failed Complex Pattern Against the Trend




Edit ... MLNM tide $tran BOT vlo sbux es_z5 $xoi $xau biph RIMM ERTS $indu $spx $compq yhoo eur_a0-fx gbp_a0-fx $sox EXPE NG_f6 Nq_z5
15min
EMA13 1.18
EMA20 1.18
EMA50 1.18
SMA50 1.18
SMA200 1.18
Bollinger(20,2.0)
zz 0.0010
zz 0.01198
zz 0.1
zz 1.0
zz 10.0
A
0.886AB
C
AB=CD @ $1.177
0.786XA @ $1.176 1.270BC @ $1.176
0.618XA
0.786XA @ $1.176
X
D
1.1820
1.1810
1.1800
1.1790
1.1780
1.1770
1.1760
1.1750
1.1740
1.1730
1.1720
1.1710
1.1700
1.1690
02 04 06 08 10 12 14 16 18 20 22 00 02 04 06 08 10 12 14
7 Dec
The Harmonic Analyzer (TM) : EUR_A0-FX-15MIN
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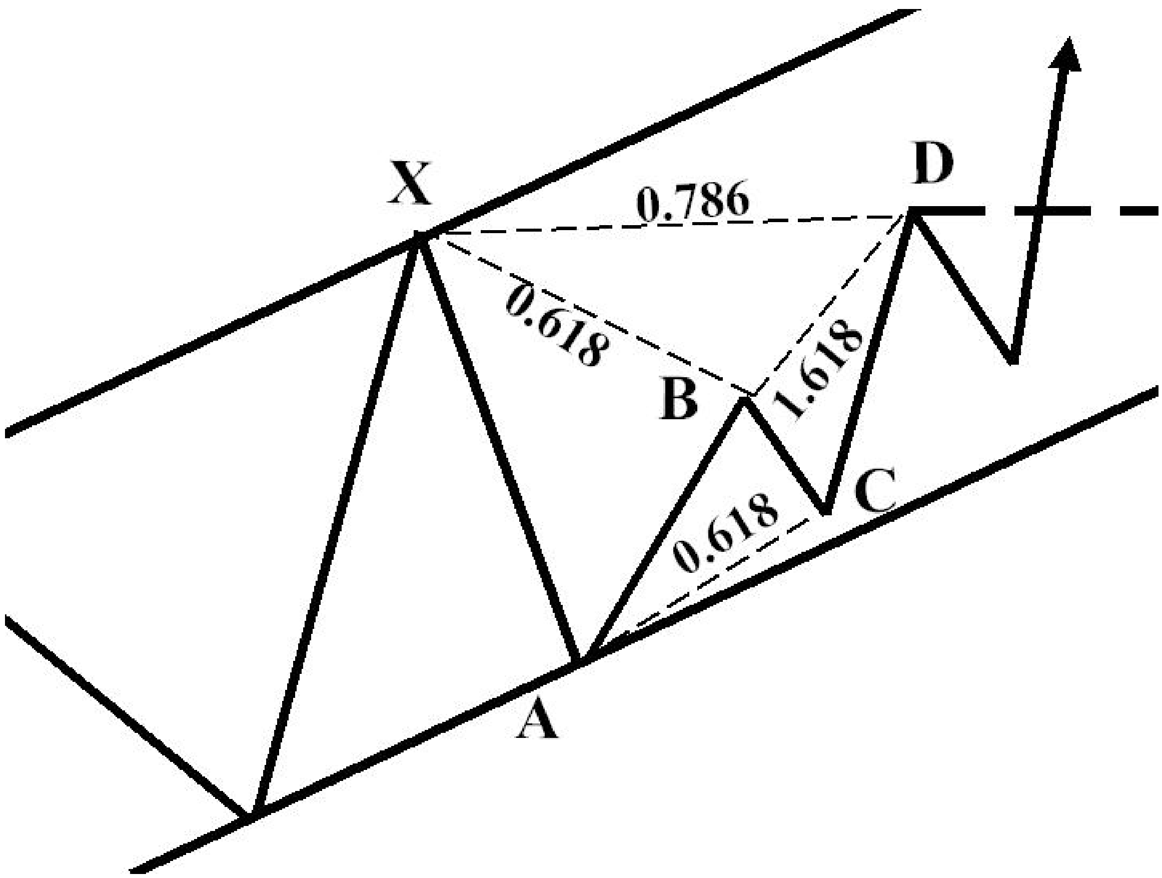
Failed Bearish Patterns within the Trend



Dow Jones Transportation Average ($TRAN): Daily


Edit ... CELL $SPX F NG_f7~ng_V6 NG_V6 NG_U6 NG_X6 NG_F7 NG_H7 NG_Z6 NG_M7 ng_V6~ng_u6 ng_z6~ng_u6 ng_z6~ng_x6 ng_v6~ng_u6 ng_x6~ng_u6
$TRAN 10-MAR-06
Daily
EMA13 3,702.90
EMA20 3,707.85
EMA50 3,679.80
SMA50 3,661.79
SMA200 3,638.24
Bollinger(20,2.0)
zz 9.0E-4
zz 0.01174
zz 0.11
zz 1.0
zz 10.0
D
1.414BC @ $3,790.291
0.786XA @ $3,774.065
AB=CD @ $3,704.570
Aug
Spt
Oct
Nov
Dec
The Harmonic Analyzer (TM) : $TRAN
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Edit ... CELL $SPX F NG_f7~ng_V6 NG_V6 NG_U6 NG_X6 NG_F7 NG_H7 NG_Z6 NG_M7 ng_V6~ng_u6 ng_z6~ng_u6 ng_z6~ng_x6 ng_v6~ng_u6 ng_x6~ng_u6 ng_x6~ng
$TRAN 10-MAR-06
Daily
EMA13 2,898.50
EMA20 2,895.96
EMA50 2,845.03
SMA50 2,848.38
SMA200 2,515.90
Bollinger(20,2.0)
zz 9.0E-4
zz 0.01174
zz 0.11
zz 1.0
zz 10.0
4,500.
4,250.
4,000.
3,750.
3,500.
3,250.
3,000.
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Oct Dec Feb Apr Jun Aug Oct Dec Feb Apr Jun Aug Oct Dec Feb Apr Jun Aug Oct Dec Feb Apr
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CL_U6 15-AUG-06
Daily
EMA13 62.13
EMA20 61.80
EMA50 62.08
SMA50 61.92
SMA200 59.12
Bollinger(20,2.0)
zz 9.0E-4
zz 0.01174
zz 0.099
zz 1.0
zz 10.0
1.618XA @ $75.725
2.618BC @ $75.000
0.618XA
X
A
B
C
D
2.618BC @ $75.000
1.618XA @ $75.725
80.00
77.50
75.00
72.50
70.00
67.50
65.00
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CL_U6 15-AUG-06
Daily
EMA13 65.86
EMA20 66.27
EMA50 65.62
SMA50 65.43
SMA200 62.11
Bollinger(20,2.0)
zz 9.0E-4
zz 0.01174
zz 0.099
zz 1.0
zz 10.0
1.618XA @ $75.725
2.618BC @ $75.000
0.618XA
1.618AB=CD @ $72
X
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B
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23 30 6 13 21 27 6 13 20 27 3 10 17 24 1 8 15 22 30 5 12 19 26 5
Feb
Mar
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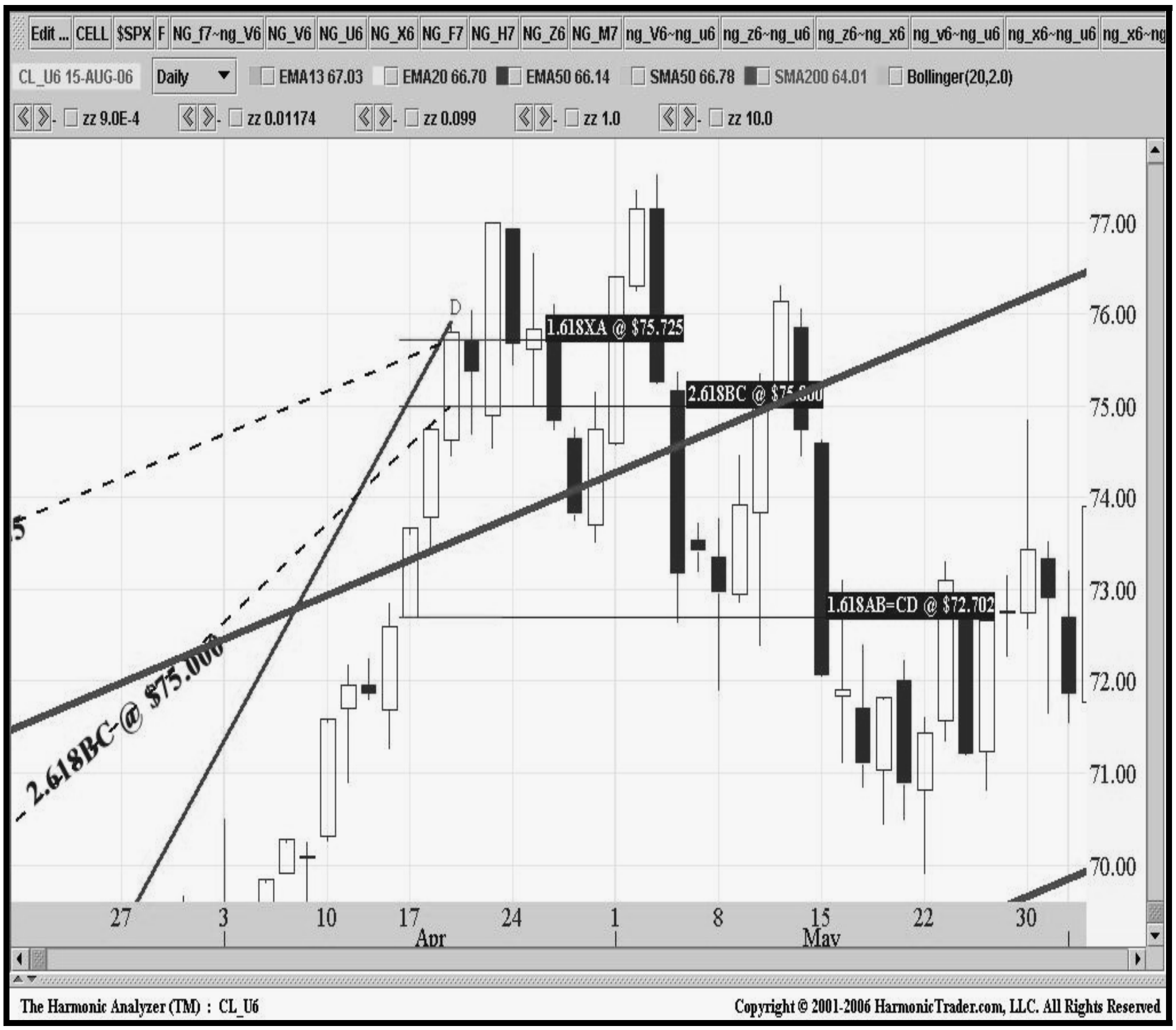

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CL_U6 15-AUG-06
Daily
EMA13 67.03
EMA20 66.70
EMA50 66.14
SMA50 66.78
SMA200 64.01
Bollinger(20,2.0)
zz 9.0E-4
zz 0.01174
zz 0.099
zz 1.0
zz 10.0
D
1.618XA @ $75.725
2.618BC @ $75.000
2.618BC @ $75.000
1.618AB=CD @ $72.702
77.00
76.00
75.00
74.00
73.00
72.00
71.00
70.00
27
3
10
17
Apr
24
1
8
15
May
22
30
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CHP 5: The 5-0 Pattern

Although I have been aware of the structure for quite some time, the 5-0 Pattern is a relatively new discovery within the Harmonic Trading approach that I have refined immensely over the past year. I have studied hundreds of cases to define the best 5-0 structures. In this article, I will outline the basic identification techniques for the pattern. Although I will not cover execution or trade management strategies, the principles are the same as for all harmonic patterns and can be found in my 2004 book, *Harmonic Trading of the Financial Markets: Volume One*. I wanted to release the pattern with the intention of providing a thorough review of the principles of the 5-0 in my next book, *Harmonic Trading of the Financial Markets: Volume Two* – which will be published in June 2005. Although this new pattern possesses many characteristics that are consistent with all harmonic structures, there are several traits that truly differentiate it from the rest.

The 5-0 Pattern is a unique structure that possesses a precise alignment of Fibonacci ratios to validate the pattern. Although the 5-0 is considered a retracement pattern, as the 50% retracement is the most critical number within the Potential Reversal Zone, the measurements of the various price legs are slightly different than the Bat or the Gartley. The 5-0 is within the family of 5-point harmonic reversal structures and is primarily defined by the structure's B point – as is mandatory for all harmonic patterns. However, the 5-0 requires a reciprocal AB=CD measurement to define the pattern's completion.

The basic premise of the pattern is to identify distinct reactions following the completion of a contrary trend. A valid 5-0 patterns typically represent the first pullback of a significant trend reversal. In many instances, the AB leg of the structure is a failed final wave of an extended trend. Within Elliott Wave terms, the AB leg may be a failed wave 3 of a corrective "abc" or a failed wave 5 of an entire completed trend. Although these are obvious similarities, from the Harmonic Trading perspective, it is important to examine the structure via its relative Fibonacci measurements to satisfy the pattern requirements.

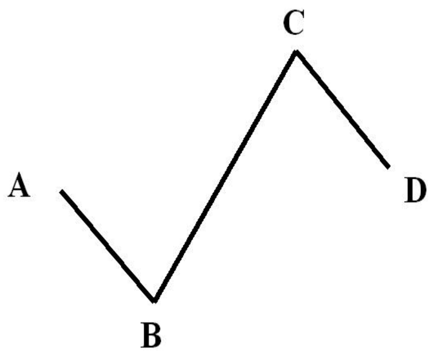
The 5-0 is an incredibly precise pattern that possesses only two numbers – the 50% retracement of the BC leg and the Reciprocal AB=CD. It is important to note that the measurements utilized to define the Potential Reversal Zone (PRZ) are different from all other harmonic patterns in two distinct ways.

50% BC Projection Defines the Pattern’s Completion Point:

In most cases, the XA leg is the defining measurement of the pattern’s completion, while the BC projection is normally a complimentary number. But, the 5-0 pattern utilizes the 50% BC retracement as the defining limit in the set up.

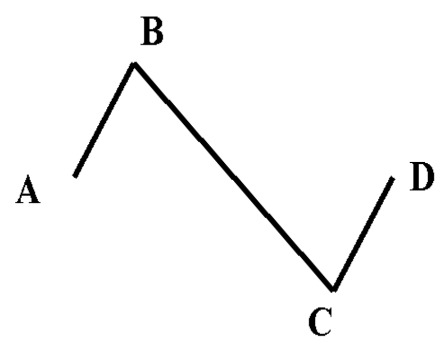
Reciprocal AB=CD

To recall from the previous chapter, the Reciprocal AB=CD pattern is an important harmonic structure in specific situations. In the 5-0 set up, it is a crucial element that compliments the 50% retracement and defines the Potential Reversal Zone (PRZ) for the pattern. Please review these illustrations for the Reciprocal AB=CD patterns.



BULLISH RECIPROCAL AB=CD

BUY @ D!



BEARISH RECIPROCAL AB=CD

SELL @ D!

Basic 5-0 Requirements

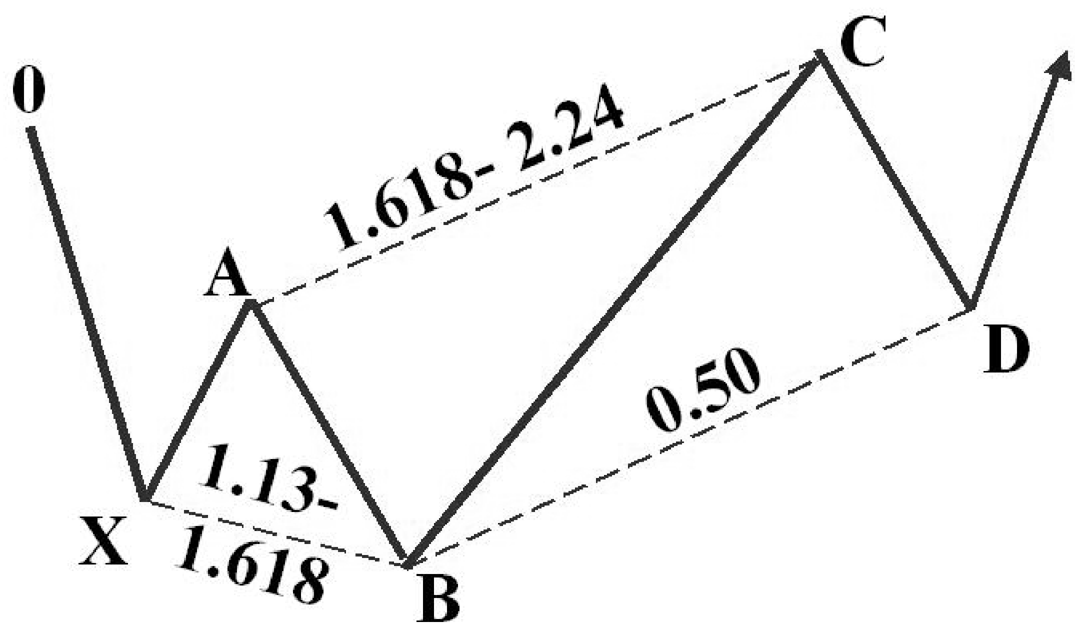
Although the pattern incorporates 5 points within the structure (X, A, B, C, D), the starting point of the structure (0) can be the beginning of any extended price move. However, the initial point X must possess a specific alignment with respect to the A and B point. The X, A , B formation of the structure is usually some type of impulse move. The XA projection that defines the B point can not exceed a 1.618. Any extension greater than a 1.618 will negate the structure, as smaller impulse moves are preferred. Again, this is the failed wave 3 or wave 5 – in Elliot Wave terms – that establishes the rest of the structure.

The BC leg is the longest price length of the structure and must be at least a 1.618 extension of the AB length but it must not exceed 2.24. This tight range of 1.618-2.24 is a defining element of the structure. If the 1.618 minimum limit is not reached, the structure is not a valid 5-0.

After the BC leg has reversed from that zone, the 50% retracement is measured from the B point to the C point. In addition, the Reciprocal AB=CD is projected from the C point (an equivalent length of the AB leg) to compliment the Potential Reversal Zone (PRZ). The following illustrations and examples will clearly explain these concepts.

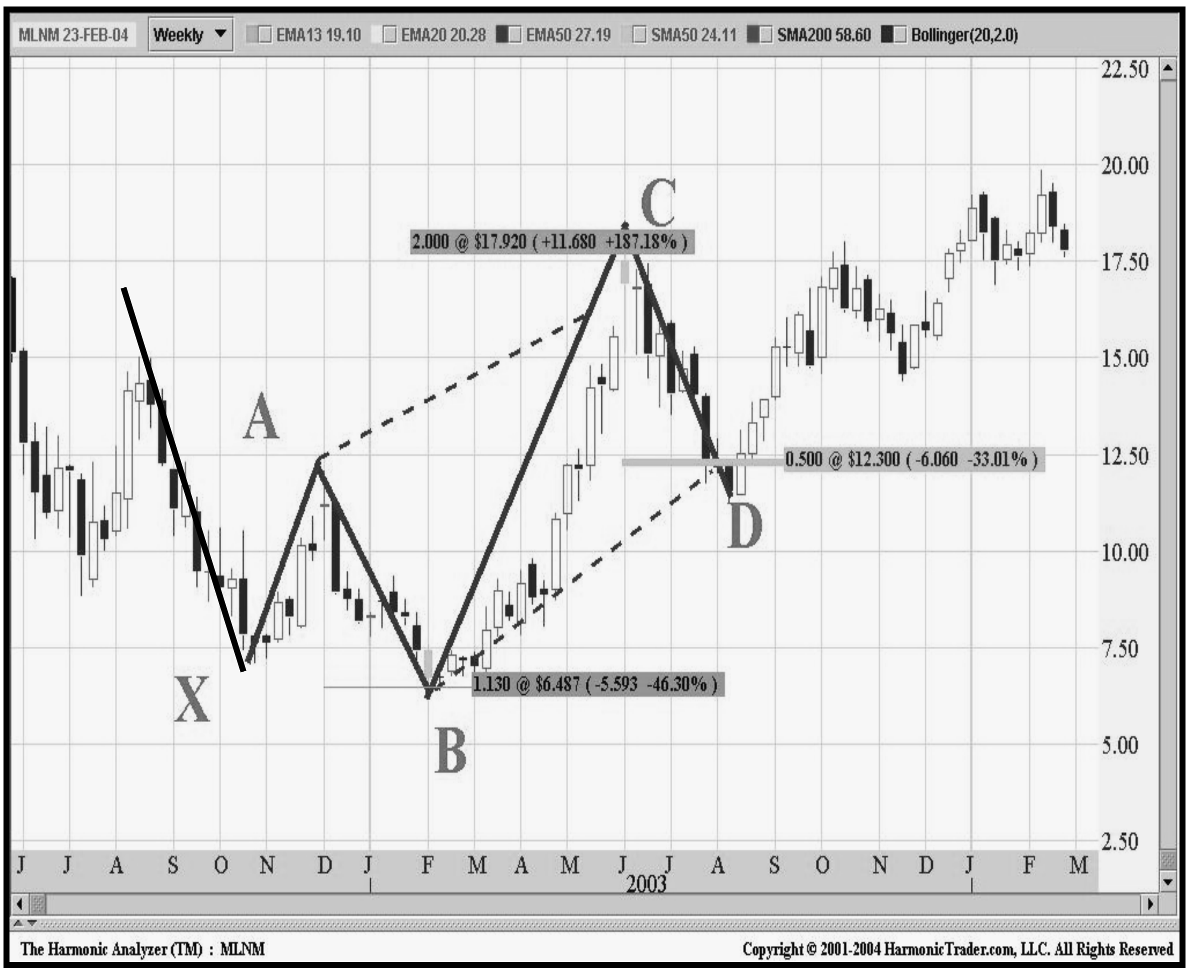
The Bullish 5-0 Pattern

The Bullish 5-0 starts at the 0 point, representing an extended down leg to begin the pattern at X. The initial point X acts as the low of this prior substantial decline. After a quick reactive bounce to the A point, the structure abruptly continues the decline, only to find support slightly past the prior low at X. This is the failed wave 3 or wave 5 – in Elliot Wave terms – that establishes the rest of the structure.



The important limits from a Harmonic Trading perspective requires that this X, A extension be at least a 1.13 but not greater than a 1.618. After that impulsive failed wave is established, the BC leg rallies to at least a 1.618 extension of the AB length but it does not exceed 2.24. Again, this tight range of 1.618-2.24 is a defining element of the structure. If the 1.618 limit is not reached, the structure is not a valid 5-0. After the BC leg has reversed from that zone, the *bullish* 50% retracement is measured from the B point to the C point. In addition, the Reciprocal AB=CD is projected from the C point (an equivalent length of the AB leg) to compliment the Potential Reversal Zone (PRZ). It will take some time to begin to identify this structure but the obvious characteristic is the failed down wave followed by a precise 1.618-2.24 extension. At that point, it is important to calculate the 50% retracement level with the Reciprocal AB=CD and study the price action in the PRZ.

Millennium Pharmaceutical
(MLMN): Weekly



This chart of Millennium Pharmaceutical demonstrates the effectiveness of the pattern in longer-term situations. After declining steadily in through 2002, the stock completed a failed down wave that nominally took out the prior low in early 2003 before rallying sharply to the 2.0 projection of the AB leg. The stock rolled over to retest the 50% level before resuming the up trend. The Reciprocal AB=CD complimented the 50% retracement just under the $12 level, defining a precise area between 11.50-12.30 to buy the stock.

Dow Jones Industrial Average ($INDU): 5-Minute

This intra-day chart of the Dow Jones Industrial Average exemplifies an ideal 5-0 structure. After an extended decline from 9855, the index bounced (A) and then declined a bit further taking out the prior low (X) in an intra-day shake out to the 1.13 extension, before rallying in the mid-afternoon to the C point. After rolling over at the 2.0 extension, the 5-0 was set up with the 50% retracement at

9838 and the Reciprocal AB=CD at 9839. The index reversed sharply after exceeding this area slightly.

Adobe Software
(ADBE): Daily

Standard and Poor's 500 September 2004 Mini-Contract (ES_U4): 15-Minute

Edit ... $INDU $INDU-15min $COMPQ $COMPQ-15min XLNX XLNX-60min XLNX-15min CSCO
ES_U4 07-SEP-04_12:15
15min
EMA13 1,117.28
EMA20 1,117.39
EMA50 1,117.48
SMA50 1,117.76
SMA200 1,116.10
Bollinger(20,2.0)
2.000 @ $1,121.750 (+8.500 +0.76%)
D
0.500 @ $1,117.625 (-4.375 -0.39
06
08
10
12
14
16
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Standard and Poor's 500 Trust (SPY): Daily

Reebok (RBK): Weekly

Eurodollar
(EUR_A0-FX): 5-Minute

Standard and Poor's 500 June 2004 Mini-Contract (ES_M4): 60-Minute

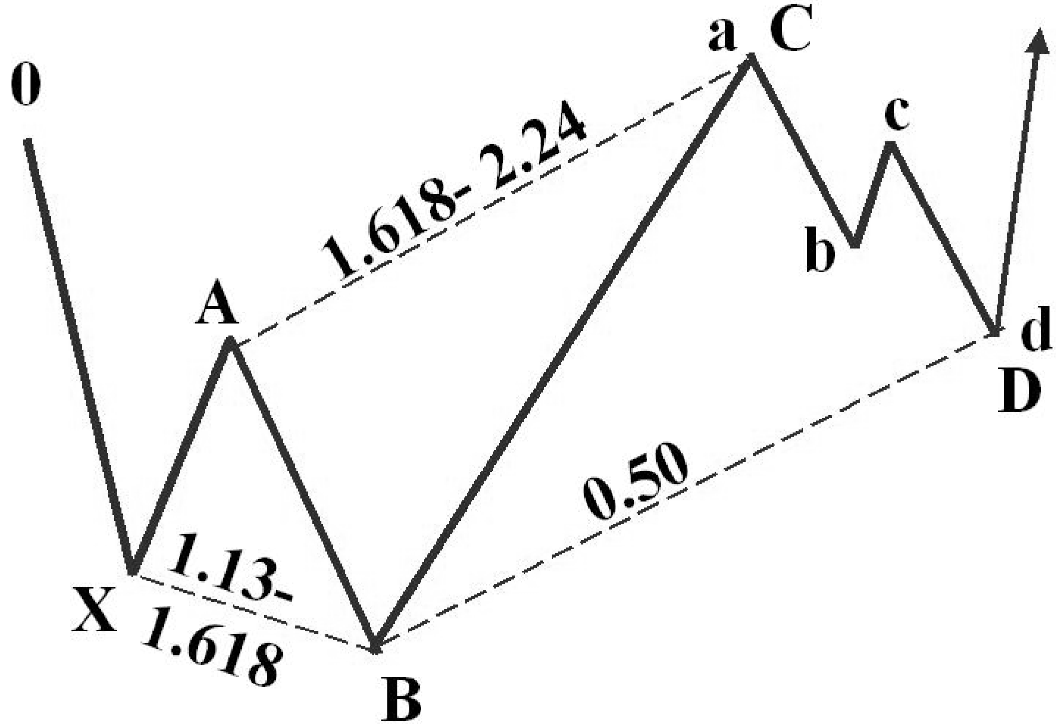
This chart of the ES was illustrated in advance. The structure was quite distinct and the 50% retracement was calculated at 1113. In addition, the Reciprocal Bullish AB=CD was projected to complete in the same exact area.

This 60-minute chart exemplifies the ideal structure for the 5-0, especially with the sharp reversal at the 2.0 projection (red line). This pattern formed over the course of the prior week. Like a magnet, the price action steadily declined to test this support. The following chart shows the price action, as the ES approached the Potential Reversal zone (PRZ) at 1113.

The black line represents the Bullish Reciprocal AB=CD completion point and it converges at the same level as the 50% retracement. After a sharp decline into the PRZ, the price action was able to stabilize.

After exceeding the 1113 level slightly, the ES reversed sharply within a brief time following the initial test. This is an excellent example that truly reveals the ideal price action of a valid Bullish 5-0. The structure was distinct, the alignment of Fibonacci numbers was satisfactory and the price action reversed in the zone. Although it will take time to identify these situations, 5-0 opportunities like these occur frequently in the financial markets. Although a "clean" reversal from a single test of a Potential Reversal Zone (PRZ) is ideal, it is more common for price action to retest this pivot area a second or even multiple times before reversing significantly.

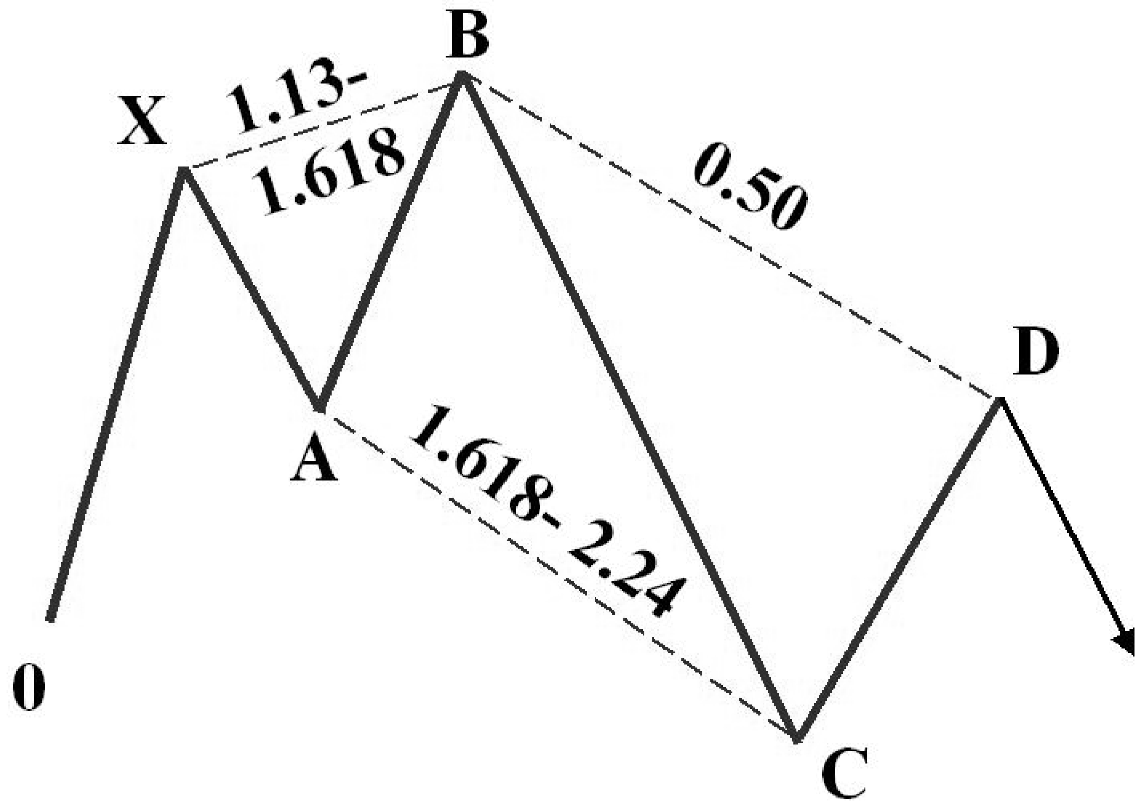
Bullish ab=cd within CD leg of 5-0 Pattern



Burlington Resources (BR): 15-Minute

The Bearish 5-0 Pattern

The Bearish 5-0 starts at the 0 point, representing the low of an extended rally up to the initial point of the pattern at X. The initial point X sets up the failed break out area, where the rally from the A point to the B peak, nominally takes out the prior high at X. Again, this is the failed wave 3 or wave 5 – in Elliot Wave terms – that establishes the rest of the structure.

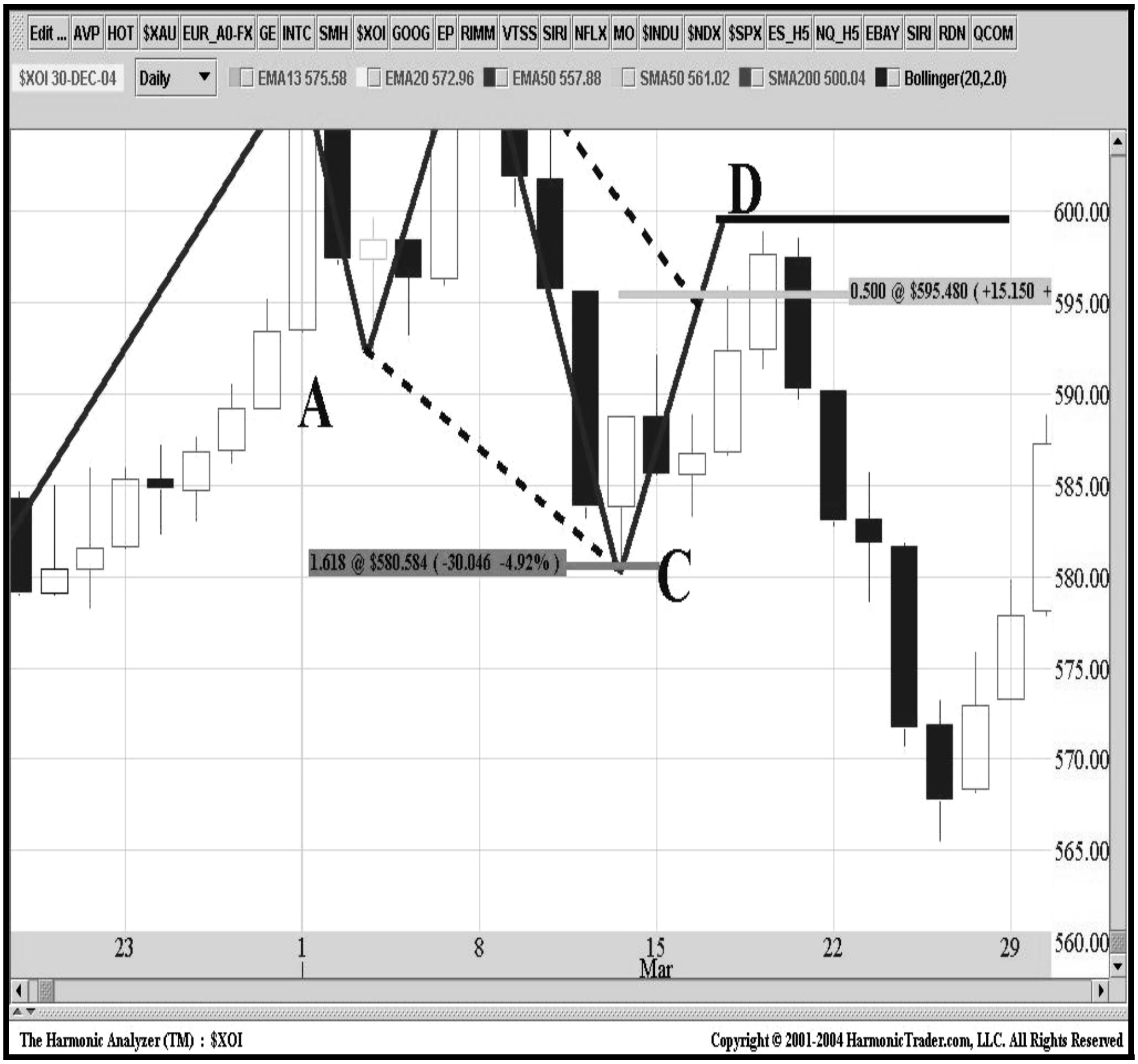


Remember, this X, A extension must be at least a 1.13 but not greater than a 1.618. After that impulsive failed wave is established, the BC leg declines to at least a 1.618 extension of the AB length but it does not exceed 2.24. Again, this tight range of 1.618-2.24 is a defining element of the structure. If the 1.618 limit is not reached, the structure is not a valid 5-0. After the BC leg has reversed from that zone, the *bearish* 50% retracement is measured from the B point to the C point. In addition, the Bearish Reciprocal AB=CD is projected from the C point (an equivalent length of the AB leg) to compliment the Potential Reversal Zone (PRZ).

AMEX Oil Index
($XOI): Daily

This is a fantastic example of a Bearish 5-0 structure that possessed the ideal Fibonacci alignment to validate the pattern. After a long rally, the index made an initial peak at the X point, pulled back to point A and reversed sharply at the B point, establishing the failed wave or triangle of the 5-0 structure.

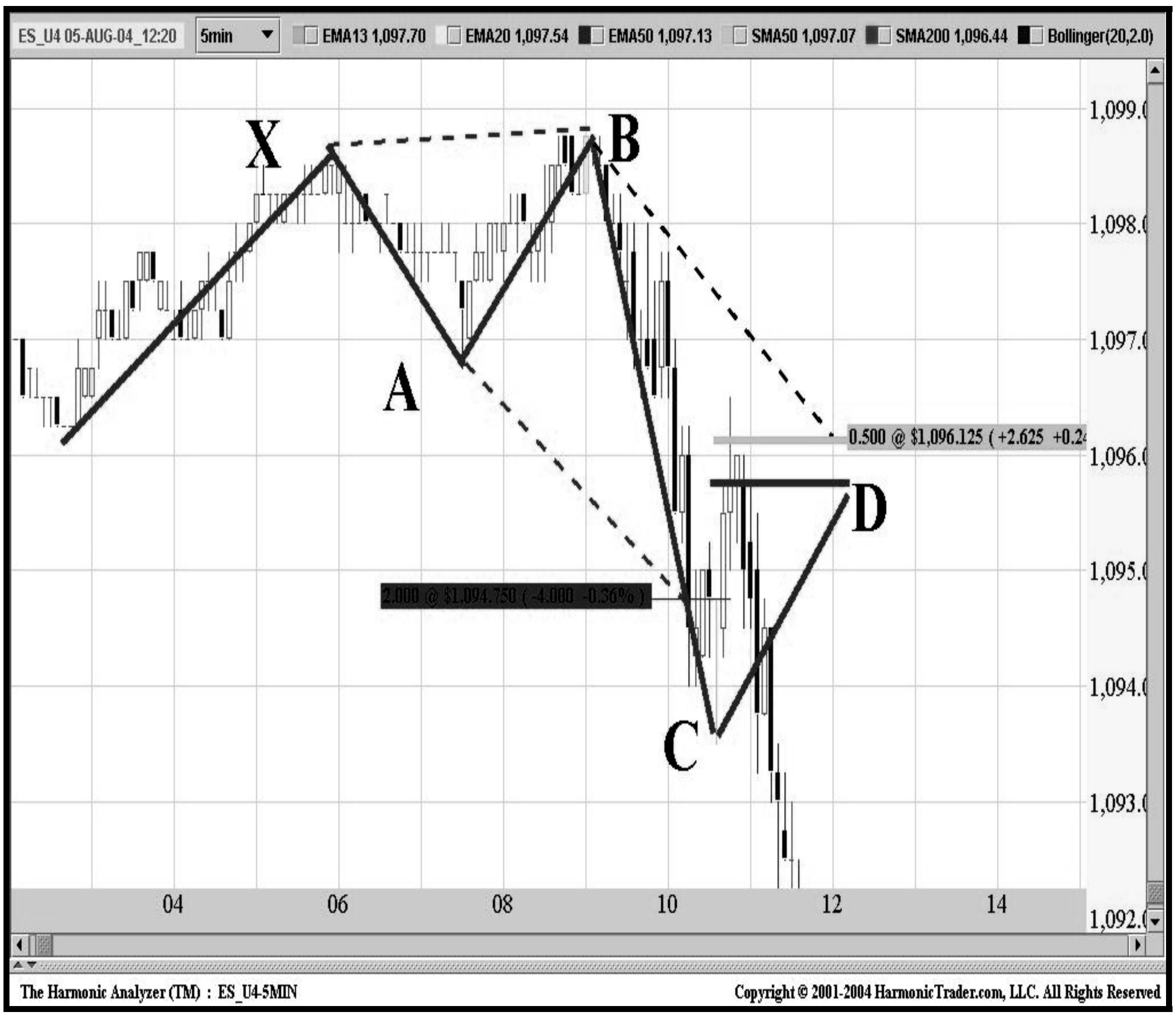
The following chart of the price action in the Potential Reversal Zone (PRZ) clearly shows the sharp reversal following the test of the 50% level. The Bearish Reciprocal AB=CD complimented the 50% retracement and defined a tight range just under the 600 level. The day after the $XOI tested 50% level, it started to reverse.



It is important to point out the C point on this chart. The mandatory 1.618 requirement was met in this case but it was close. If the C point did not test the 1.618 or fell just shy, it would invalidate the structure. It is important to understand that there is no discretion outside the prescribed parameters for the 5-0 pattern. Although such strict application reduces the number of potential trading candidates, it serves to distinguish the best opportunities.

Standard and Poor's 500 September 2004 Mini-Contract (ES_U4): 5-Minute

This 5-minute chart in the ES shows another ideal intraday structure with a perfect 50% retracement, calculated at 1096 with the completion of the Reciprocal Bearish AB=CD slightly below this level.



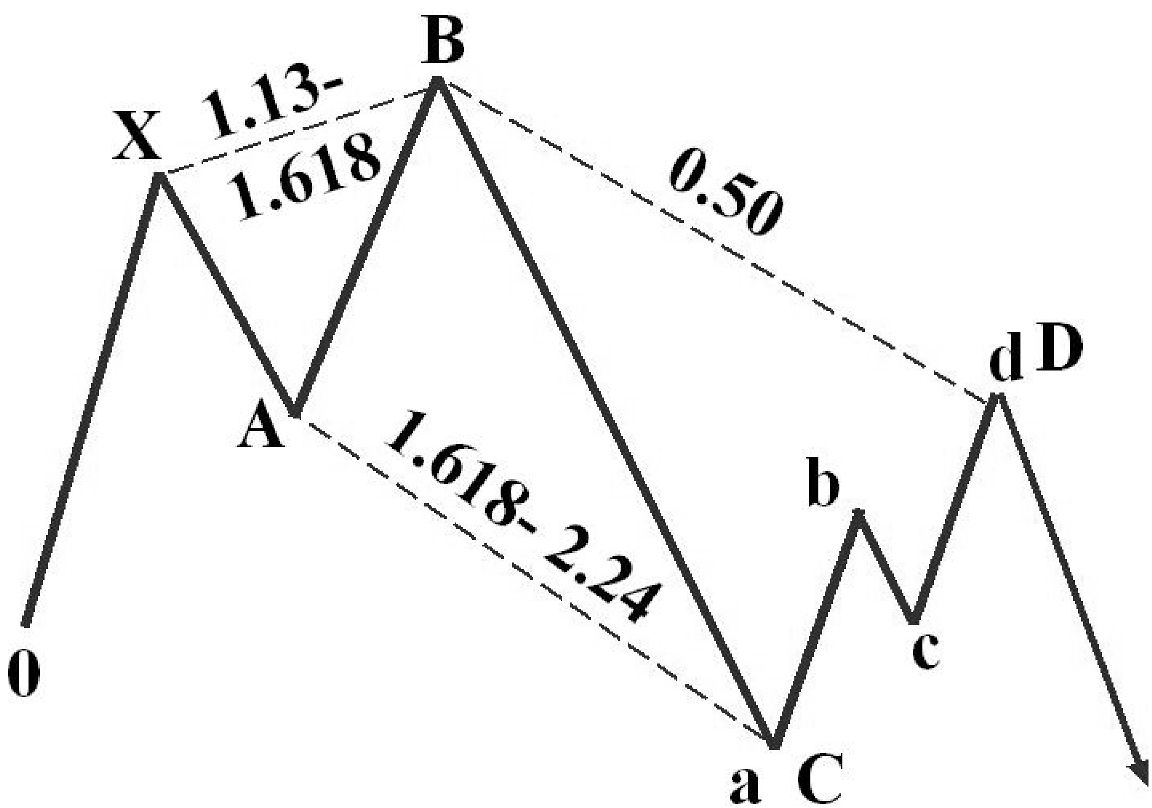
The following chart of the price action in the Potential Reversal Zone (PRZ) clearly shows the sharp reversal following the entire test of the 5-0 resistance. The Bearish Reciprocal AB=CD complimented the 50% retracement and defined a tight intraday range at 1096. The ES rolled over sharply within a few price bars of the resistance.

This Bearish 5-0 possessed an ideal reversal and downside continuation, which is a common trait of valid structures. The best trading opportunities usually provide quick indication of the validity of the reversal.

In this case, the ES stalled exactly at the harmonic numbers and rolled over shortly thereafter. Whether it's a 1-minute, 5-minute, 60-minute, daily or weekly chart, the principles remain the same, as clear opportunities like these will present themselves on all time frames.

Standard and Poor's 500 March 2005 Mini-Contract (ES_H5): 5-Minute

Bearish ab=cd within CD leg of 5-0 Pattern



Edit ... AVP HOT $XAU EUR_A0-FX GE INTC SMH $XOI GOOG EP RIMM VTSS SIRI NFLX MO $INDU $NDX $SPX ES_H5 NQ_H5 EBAY SIRI RDN QCOM
$XOI 30-DEC-04 Daily EMA13 595.47 EMA20 591.19 EMA50 574.16 SMA50 577.63 SMA200 509.95 Bollinger(20,2.0)
B
1.130 @ $609.733 (+17.673 +2.99%)
X
d
b
D
c
0.500 @ $595.480 (+15.150
a
A
1.618 @ $580.584 (-30.046 -4.92%)
C
0
615.00
610.00
605.00
600.00
595.00
590.00
585.00
580.00
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570.00
565.00
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17
23
1
8
15
Mar
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29
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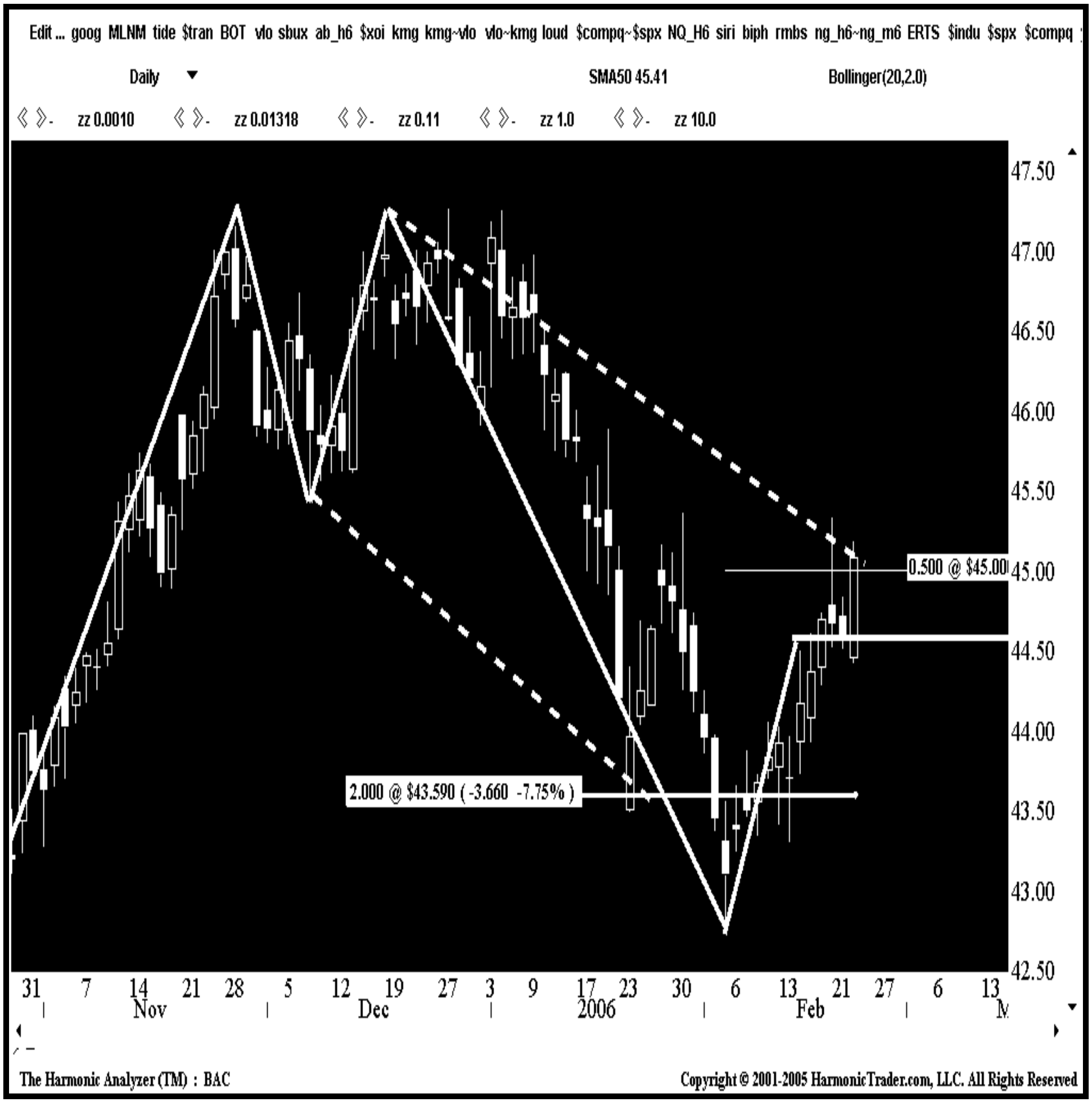
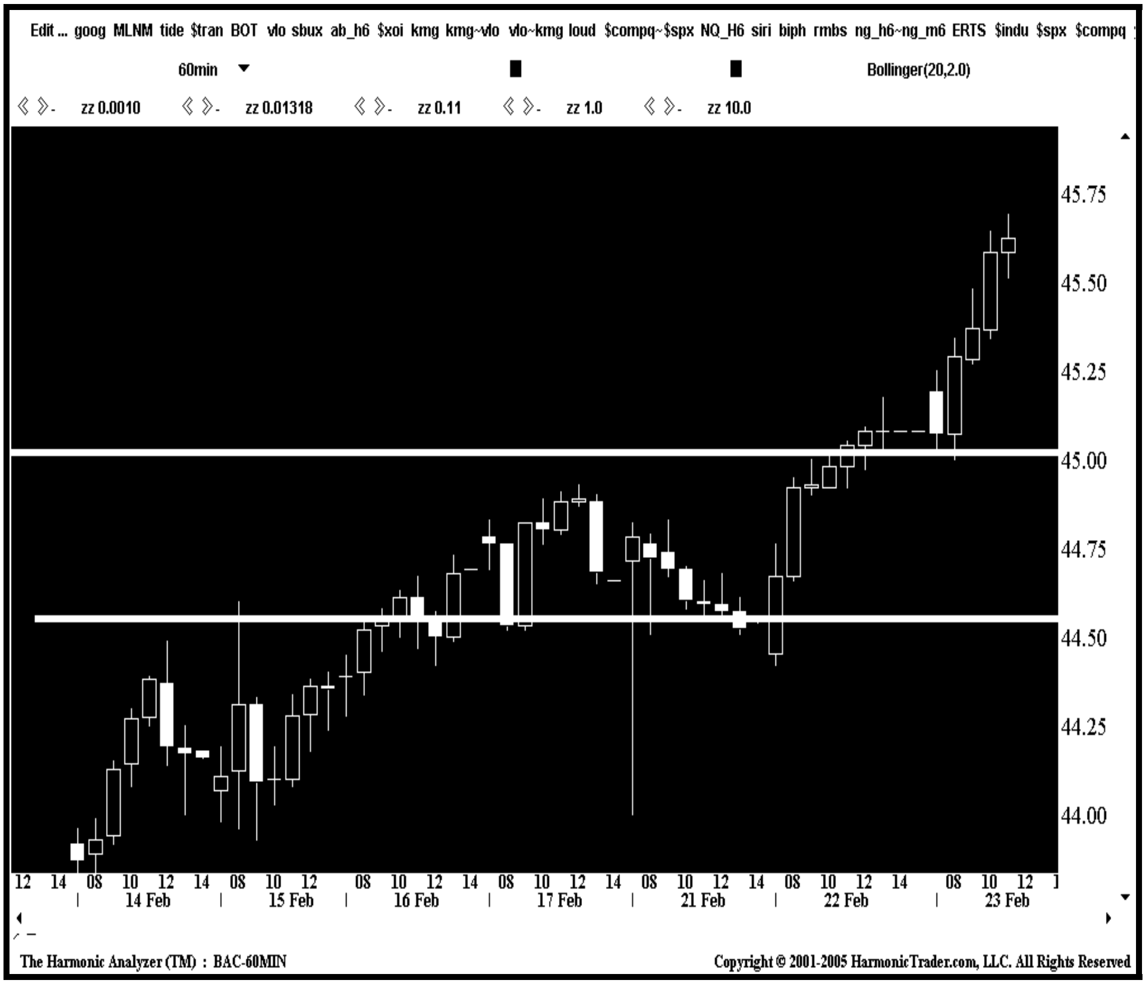
5-0 Pattern Violations

Bank of America (BAC): Daily

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60min
Bollinger(20,2.0)
zz 0.0010
zz 0.01318
zz 0.11
zz 1.0
zz 10.0
45.75
45.50
45.25
45.00
44.75
44.50
44.25
44.00
12 14 08 10 12 14 08 10 12 08 10 12 14 08 10 12 14 08 10 12 14 08 10 12 14 08 10 12
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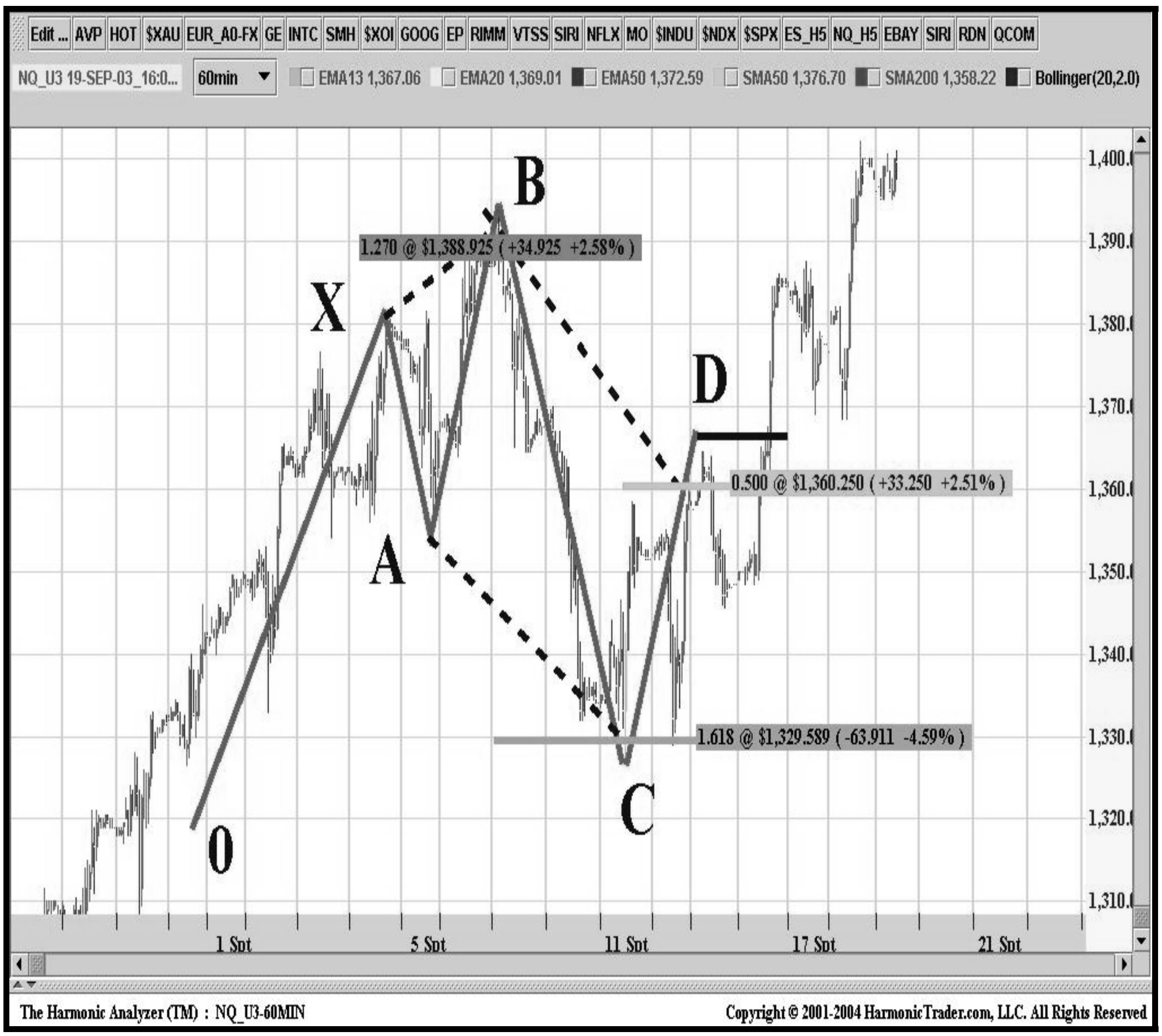
NASDAQ 100 September 2003 Mini-Contract (NQ_U3): 60-Minute



TBAR BREAKOUT UP TO 886

BECAUSE THE 5-0 SETS UP A BAT

PRICE BAMM – PLAYING THE BREAK 5-0 TO 886

BAT VS GARTLEY

PLAYING FOR POSITION

HARMONIC PROGRESSION - everyone believes you go from 382, to 618 to 786 to 886…

5-0 TO 886

127 – 1618

Failed Complex Patterns within the Trend

Morephing

Fropm bat to Crab

Chapter 6: Head and Shoulders Pattern from a Harmonic Perspective

Use reciprocal ratios

Look for patterns in the structure

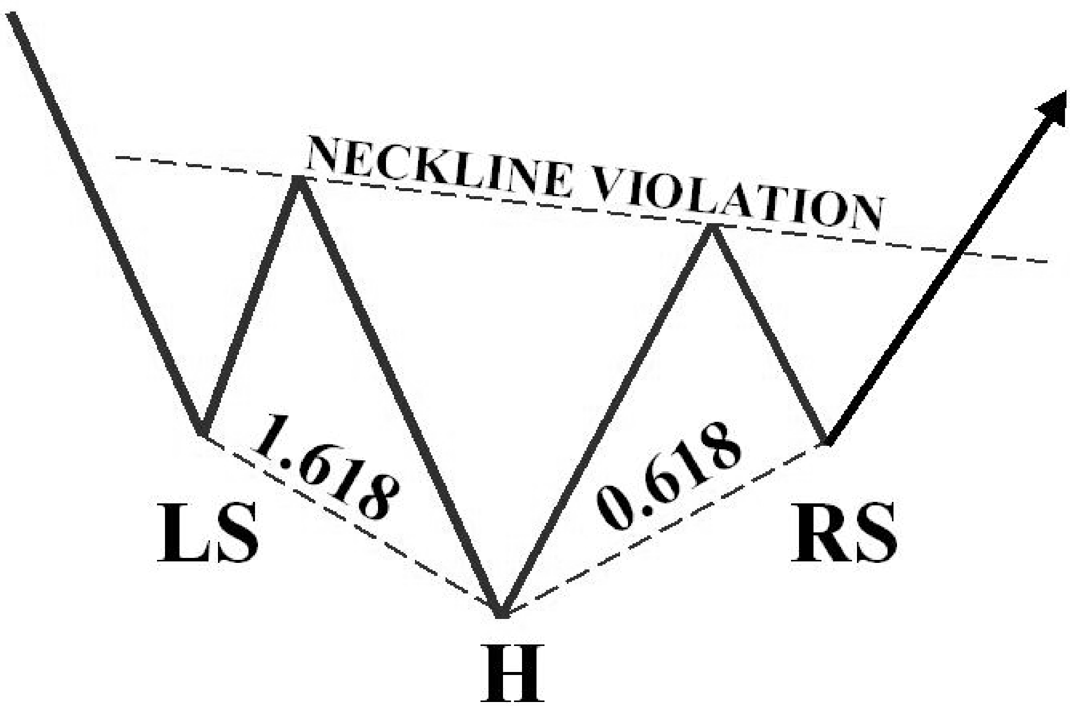
@ the top

@ the right shoulder

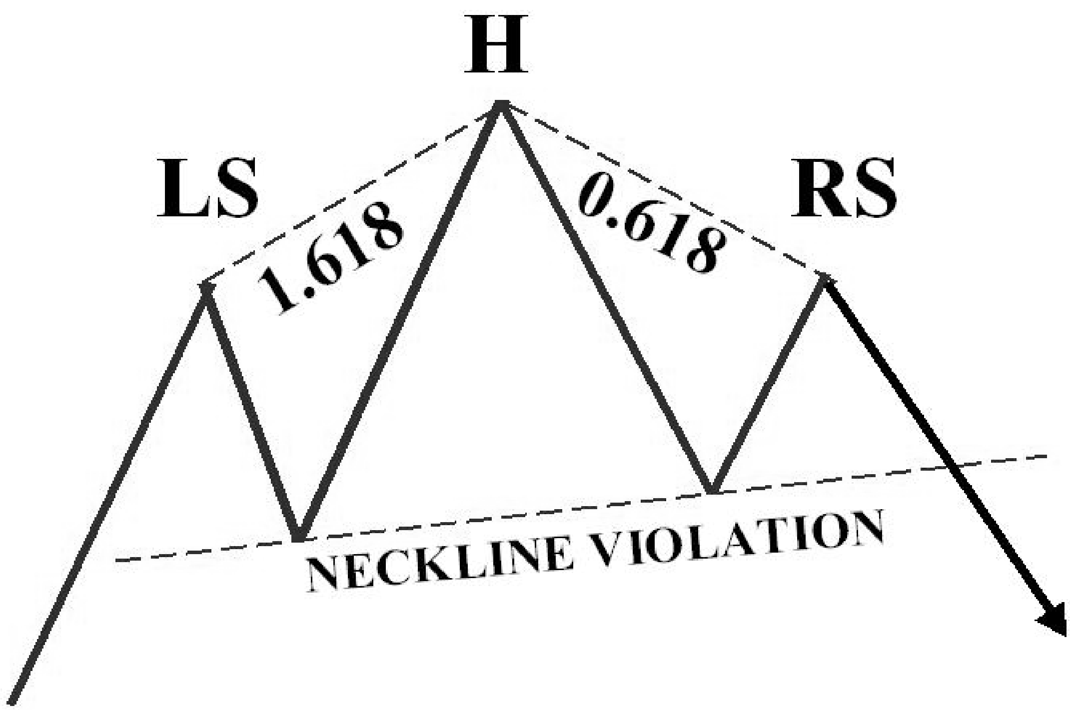
@ a major retracement of higher time frame

Look for symmetry

Bullish Head and Shoulders Pattern

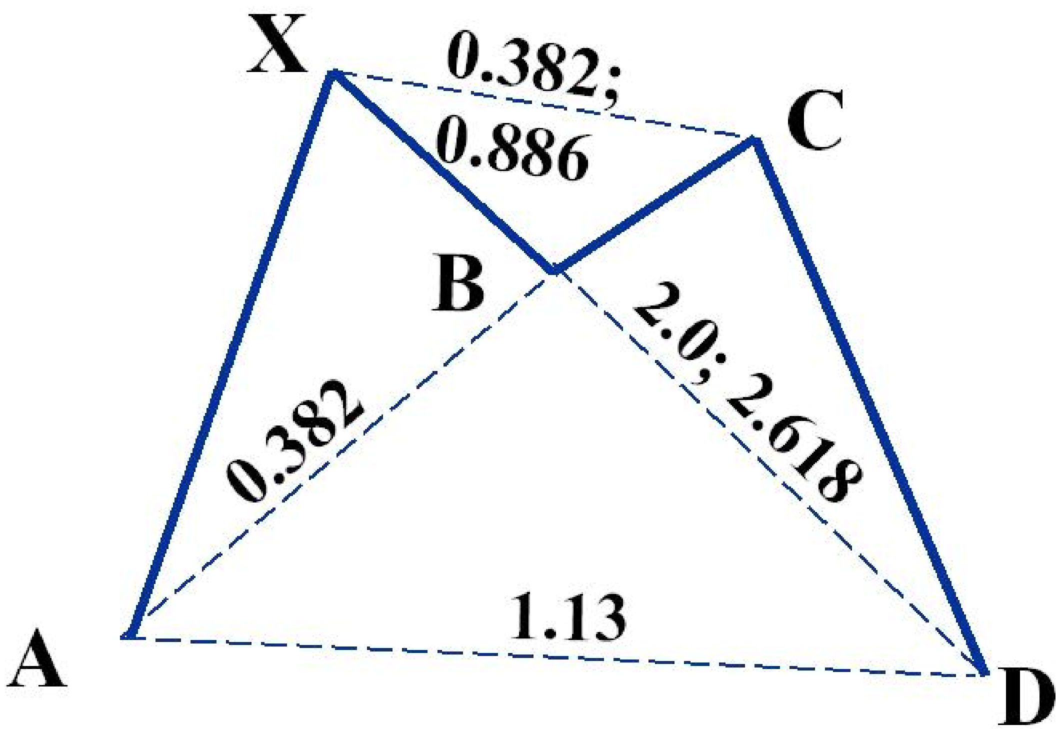


Bearish Head and Shoulders Pattern



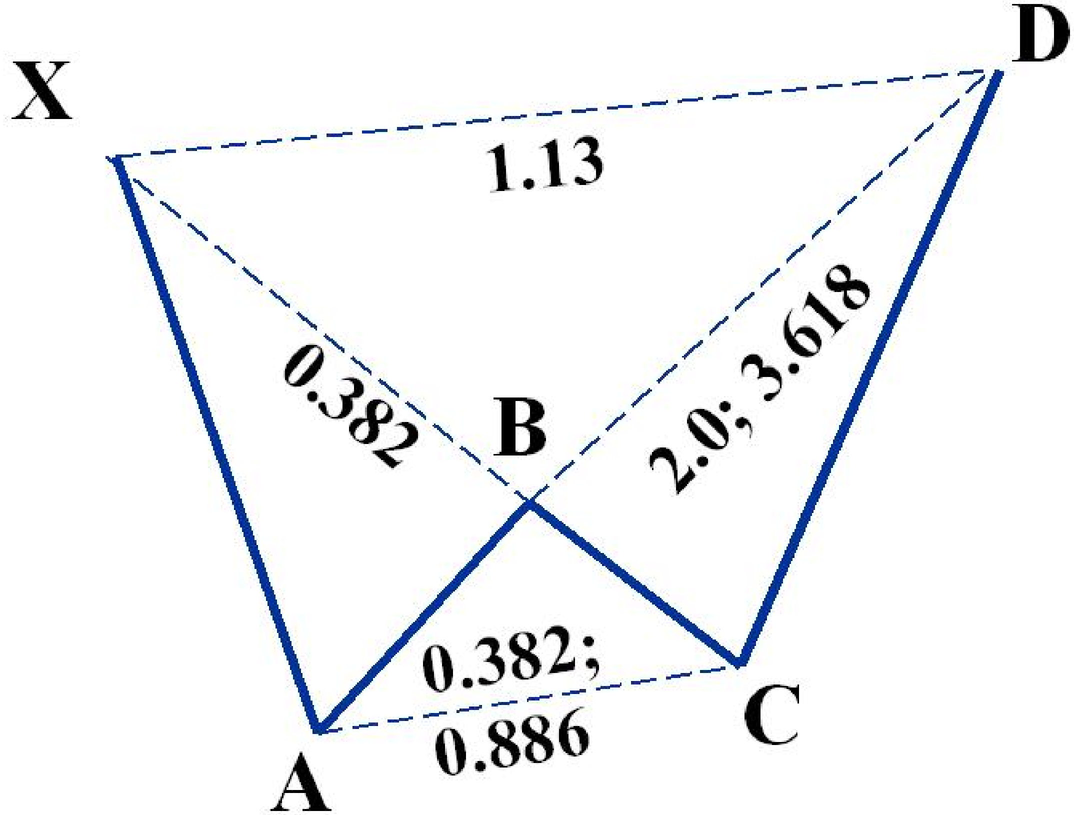
Chp 7: Alternate Bat Pattern

Alternate Bullish Bat Pattern



Example

Alternate Bearish Bat Pattern



Chapter 8: Integrating Technical Indicators with Harmonic Trading

I believe it is important to embrace a gamut of market strategies like these to thoroughly understand market price action. Considering a variety of technical methods can provide greater confirmation of potential price action. In fact, H.M. Gartley in his infamous book, *Profits in the Stock* Market, emphasized such multiple confirmation strategies of technical methods stating,

> **"Patterns must be used in conjunction with other technical working tools. The study of tops and bottoms, to be of greatest value, must be combined, and used in conjunction with the study of other working tools, such as Trend Lines, Moving Averages, Gaps, and particularly Volume, as well as Dow Theory and the general market phenomena which we call 'Breadth-of-the-Market' studies."**

(*Profits in the Stock Market*, Lambert-Gann Publishing.
Pomeroy, Washington. 1932 pg. 221)

The Harmonic Trading approach is not exclusive, and I agree with Mr. Gartley's statement. Patterns, in this case, Harmonic patterns, must be used in conjunction with other technical working tools. In "The Harmonic Trader" and in this book, I outline trading strategies that integrate such standard technical measurements with Harmonic patterns. But, it is important to note that the price measurements utilized exclusively in Harmonic Trading combine many powerful elements of Fibonacci applications to the

The importance of bias

The concept of bias can be measured in a variety of technical means. Indicators, oscillators and overall trend analysis are critical to analyze the relevant position of harmonic patterns.

BAMM

RSI BAMM

As it began to investigate the effectiveness of indicators as they relate to pattern completions, I realized that many of these technical tools formed similar structures as did the price action.

I want to make it clear. I am not the first one, with pattern recognition however I've been able to put together arranges strategies that's worth. In the beginning when the text name is the release became the basis of trading and I had much success, I was somewhat narrowminded regarding the techniques. Although it studied almost everyone's approach to the financial markets, I always focused on the techniques that were and ignored in the other strategies that were not effective for many and my trading. I remember close to 10 years ago when I first met Jim Kane of Kane trading.com, when I told him all I cared about was price. But this was during a time when the market went straight up and you can pretty much by any retracement and make money. In much same way, the 2000 bear market yielded only profits on the sell side and the bearish patterns were the only patterns that work. During that period in the '90s when the market was exploding, I was not concerned with other technical indicators because buying bullish but price patterns was yielding phenomenal results. I even publicly announced certain indicators as irrelevant money came to harmonic Price patterns. But the lessons of the 2000 bear market exposed my in her weakness which was my ability to only buy. Although I was able to maintain despite some initial disappointing results after the market topped in 2000, I was constantly striving to pick the bottom. In so my articles on the Internet by the projected several substantial support levels. But as the market continued to slide for over two years, I realize that there were other signals that I had to look for that would help me gauge the overall state of the price action whether it the bearish or bullish. Outside of the price patterns, it and utilize simple trendline analysis I will look it volume and a few other technical studies. But my main focus is always on the completion of price patterns. What I realize during that bear market was that truly the trend was your friend as it is an all markets. The problem is most of us, myself included, are optimistic people and positive people. We won the bullish. I do. When it comes to the stock market, I want the bullish on businesses, people and progress. In this can sometimes be our tragic flaw. The simple reason is that markets go to markets go down like a living organism breathing, growing and being. So I looked at a number of technical managers including relative strength, stochastics, volatility bands, M. A. C. D. of all these measures, I was looking for the technical indicator that would provide some measure of the extent of buying and selling within one trend. Since price patterns often represent the end of the significant trend, it is critical to understand some type or relative measure that manifests the degree of buying and selling. The from a harmonic pattern perspective it appeared to me that relative strength provided that measure. Although when talking about relative strength sometimes people miss confused the subject as relative to another index, such as the S&P 500. In this case, I'm talking about the relative strength measure that calculates the internal change of price movement, usually comparing the current price action with that of 14 price bars ago. The significance of the relative strength indicator when applied to the completion of harmonic patterns provides greater inside to the extent of the price action. My experience, it is help me differentiate invalid patterns from profitable opportunities. Furthermore, reversals from extreme relative strength areas, that is a positive 70 reading for a bearish signal war below the 30 reading for a bullish signal, were typically more significant price moves, resulting in confirmation of trend change.

Extreme readings @ pattern completions Indicator Patterns with Price Patterns

Although this concept can be applied to structural readings of any indicator reading, such as Stochastics, MACD, etc., impulsive and complex indicator structures trading in extreme areas can provide a great deal of technical information regarding the state of potential future price action.

Patterns in the Indicators

I also noticed that indicators frequently formed the same structure as a Price pattern did. In fact, certain indicators such as stochastics and relative strength form thereby distinct price waves and are clear opportunities than even the price action is retailing. Quite often, such distinct price structures in the indicators can confirm even more so clear harmonic Price patterns. After realizing that I needed to discover strategies that complemented harmonic patterns, I focused on the technical indicators that provided the most information and consistently confirmed or denied clear setups. Although stochastics frequently exhibit this phenomenon and I utilize this measure in my analysis, I found myself focusing primarily on the relative strength indicator. Time and time again, the most valid trading opportunities came from those patterns that exhibited price behavior that was confirmed by the relative strength.

Relative Strength Indicator (RSI)

Harmonic Trading techniques utilize Fibonacci Ratios to quantify the extent of relative price action. The two most important Fibonacci ratios directly derived from the Fibonacci sequence are the 0.618 and the 1.618. These numbers are the primary ratios of Harmonic Trading techniques and are utilized to derive the secondary and tertiary ratios of Harmonic Price Pattern Recognition.

Simple Fibonacci retracement and extension measurements frequently provide precise levels of support and resistance as a means of gauging price action. Although these measurements can be very effective, it is difficult to know exactly which Fibonacci level to examine for a potential reversal. However, Harmonic Trading techniques combined with other technical measures such as basic indicators and oscillators can complement the information provided by Fibonacci measurements of price movements. For this article, I will illustrate a simple technique of utilizing 1.618 extension price movements with Relative Strength Indicator (RSI).

1.618

The 1.618 projection is a significant Fibonacci number, because it usually indicates exhaustive price action. Often, when a stock exceeds the 1.618, it usually represents extreme price action that is difficult to sustain. When the 1.618 projection has been exceeded in this area, I know that a trade set-up is developing. Since the 1.618 represents price action that is too extreme, reversals that occur beyond this area will usually happen quickly. As a rule of thumb, I usually wait for a stock to hit 1.618 projection in a Potential Reversal Zone (PRZ) before accepting a trade.

Stochastics

Relative Strength Indicator (RSI)

"The Relative Strength Index ("RSI") is a popular oscillator. It was first introduced by Welles Wilder in an article in *Commodities* (now known as *Futures*) Magazine in June, 1978… The name "Relative Strength Index" is slightly misleading as the RSI does not compare the relative strength of two securities, but rather the internal strength of a single security. The RSI is a price-following oscillator that ranges between 0 and 100…The RSI usually tops above 70 and bottoms below 30. It usually forms these tops and bottoms before the underlying price chart."

This abbreviated explanation of RSI comes from the eSignal Education section. For a thorough explanation of RSI, please go to:

http://www.esignal.com/education/resources/atoz/default.asp

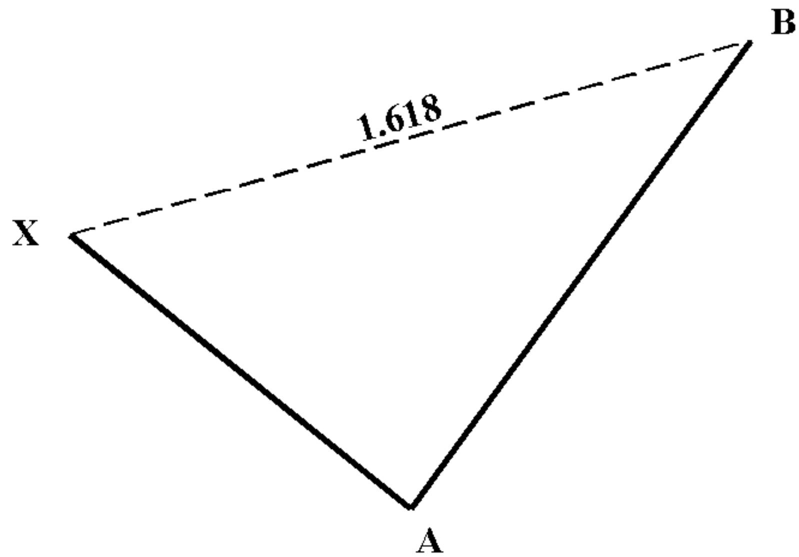
Bullish 1.618 Projection

A bullish 1.618 often occurs in an extreme sell-off. When a stock is declining, the price action can often become over-extended. The 1.618 projection point can identify profitable set-ups, since a stock that reverses off this area frequently provides a nice bounce.

I trade the Standard and Poor's 500 mini-contracts on a daily basis and look for 1.618 extensions confirmed by extreme RSI readings for intra-day opportunities. In this first example, the September contract of the S&P 500 Mini (ES03U) sold off sharply, forming a distinct intra-day 1.618 extension. It is important to note that I prefer to utilize only those 1.618 extensions that form during normal market trading hours (9:30am-4:00pm EST). In this instance, the early sell-off provided a nice reversal and it was confirmed by an oversold RSI reading that was below 30.

Bearish 1.618 Projection

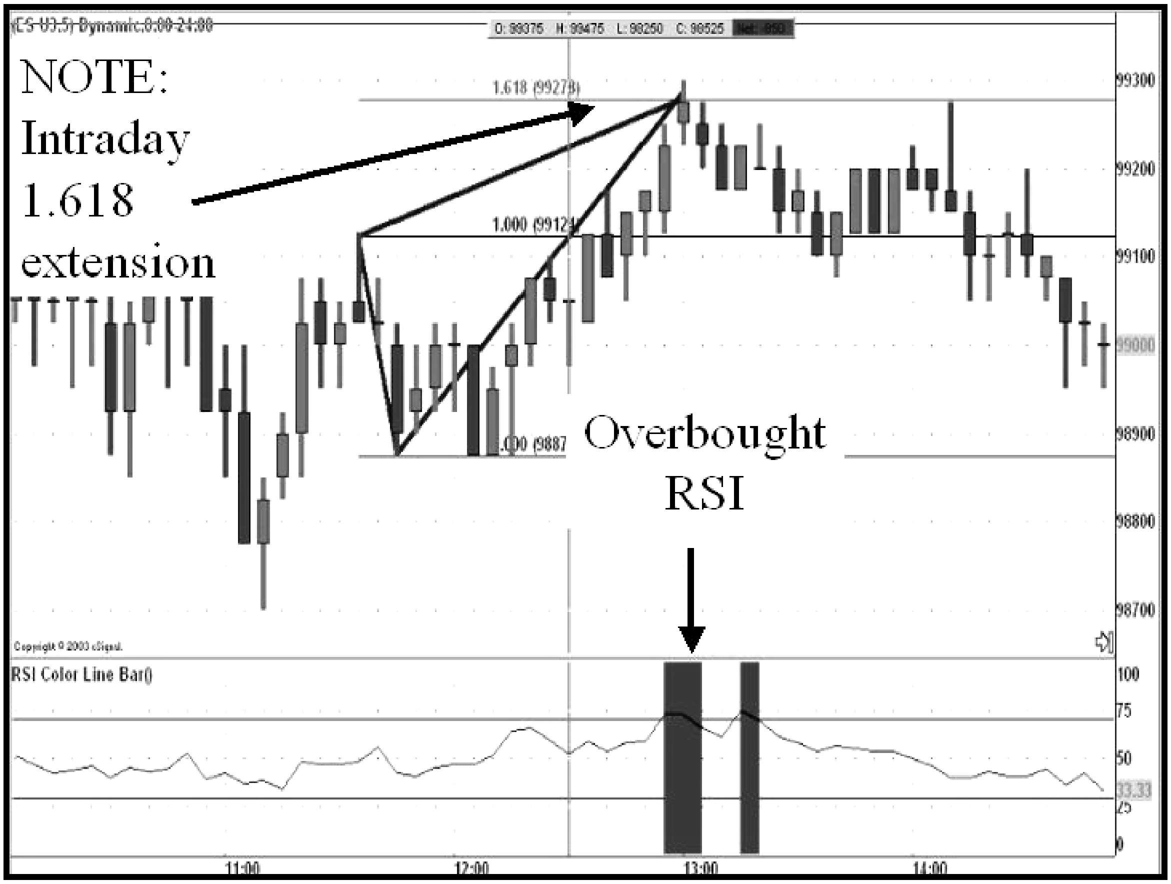
The bearish 1.618 is a very important Fibonacci number because it is an excellent area to take profits or enter a short position. As I have stated previously, the 1.618 represents an extreme price area. Often, when a stock hits this projection, it will encounter substantial resistance. If this happens, the rally usually will reverse. Although the 1.618 area can be exceeded, it is important to understand that such action above this area can be difficult to maintain. In combination with an indicator like RSI, the 1.618 can be an extremely effective Fibonacci measurement. Therefore, it is critical to examine a stock closely in this area and be prepared to sell.



BEARISH 1.618 PROJECTION
SELL AT B!

Examining another intra-day example in the September Standard and Poor's 500 Mini-contract (ES03U), the Relative Strength Indicator confirmed the short-term resistance. Following a sharp morning rally, the ES stalled at a distinct 1.618 extension at 992.75 and an overbought RSI reading above 70. The ES reversed at 993.

It is interesting to note in this example that the RSI provided a double-overbought reading above 70 within 20 minutes of the first, providing further confirmation of the Harmonic resistance of the 1.618 intra-day extension. These situations must be respected, as the measurements of the Harmonic price action and RSI clearly signaled an overbought situation.



Conclusion

Combining Harmonic Trading techniques and standard indicators is an effective means of gauging price action and identifying potential trading opportunities. ESignal's Advanced Chart Settings Layout provides the tools necessary to utilize these measures. The click and point Fibonacci retracement tool is an easy means of measuring such price movements. Furthermore, I find the highlight feature of extreme RSI readings as a clear means to distinguish price action. The combination of these tools works is effective with such other technical indicators like Stochastics and MACD, as well. ESignal's charting tools enable thorough analysis of price action like the 1.618/RSI technique and can substantially help to define profitable opportunities in the markets.

RSI

related to overall trend and other technical measures.

The importance of bias

The concept of bias can be measured in a variety of technical means. Indicators, oscillators and overall trend analysis are critical to analyze the relevant position of harmonic patterns.

Gartley on pattern used in conjunction with other technical working tools

He states, "the study of tops and bottoms, to be of greatest value, must be combined, and used in conjunction with the study of other working tools such as trendlines, moving averages, gaps, and particularly volume, as well as the Dow theory and the general market phenomena which we call "breadth of the market" studies frequently, before a copper bottom pattern may be considered as completed, these other working tools come into play, and provide confirmation of the probability the reversals taking place. In making the most of the study of reversal patterns, the market student or traitor should try to relate the development of the cardinal patterns to the fundamental picture at the time." bpg. 221

Chapter 9: BAMM Theory

BAMM - Bat Action Magnet Move

BAMM stands for ***Bat Action Magnet Move***. The essence of this theory lies in the primary tenet of Harmonic Trading that not all patterns are the same. As I outlined in *Harmonic Trading of Financial Markets: Volume One*, I wrote about "The Great Gartley Controversy." To quickly review, this controversy describes the importance of exact alignments of Fibonacci ratios with respect to price structures. My differentiation of similar pattern structures led me to discover the importance of respecting exact alignments. Specifically, the Bat pattern, which requires a different alignment of Fibonacci ratios than the general Gartley pattern, consistently guided my trade executions at different price levels. In doing so, I was able to differentiate price structures and define the best trading opportunities. The essence of this argument focuses upon primarily the location of the B point within the pattern structure. In my interpretation of the Gartley pattern, it is essential to identify the B point or midpoint at a 618 retracement of the XA leg. After identifying the structure, I realized in that any B point with a retracement less than a 618, specifically a 50 percent or less retracement resulted in a completion point that was closer to the initial starting point at X. With this understanding, I was able to differentiate price structures and have a good idea of where the price action was headed. In the Bat pattern, if the CD leg exceeded the B point, I was confident that the price action would test the 886 retracement of the XA leg. There were many times where I would watch this phenomenon develop, the price action would reach this target. It dawned on me to begin playing these moves, capturing a segment of the CD leg instead of waiting for the ultimate completion of the larger pattern. Like a magnet, the Potential Reversal Zone (PPRZ) of the Bat pattern frequently provided clear direction of where the price action was headed.

The following illustration of the bearish bat pattern shows the point where the BAMM is triggered. Utilizing the Bat pattern illustration, when a B point of a pattern is at a 50 percent or less, the CD leg typically experiences a greater retracement of the XA move. In the case of the Bearish Bat pattern, when the price action exceeds the B point in a breakout move, the segment of the CD leg typically will extend towards the 886 retracement usually complemented by other harmonic measurements. As we will see in the Alternate Bat pattern, if the B point is a 382 retracement of the XA leg or less, the corresponding move usually extends to a full retest of the initial X point, testing the 886 retracement at a minimum.

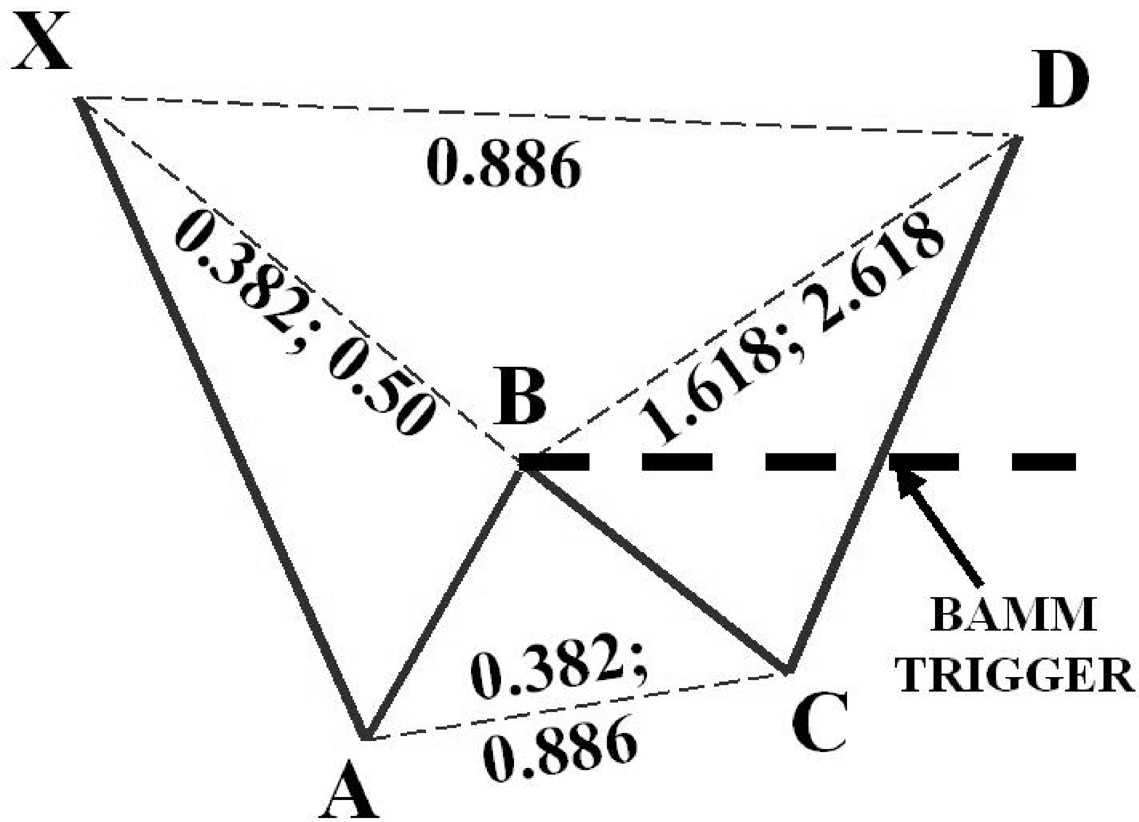
H. M. Gartley in his book, "Profits in the stock market," emphasized the importance of EXACT patterns. On page 208, he states:

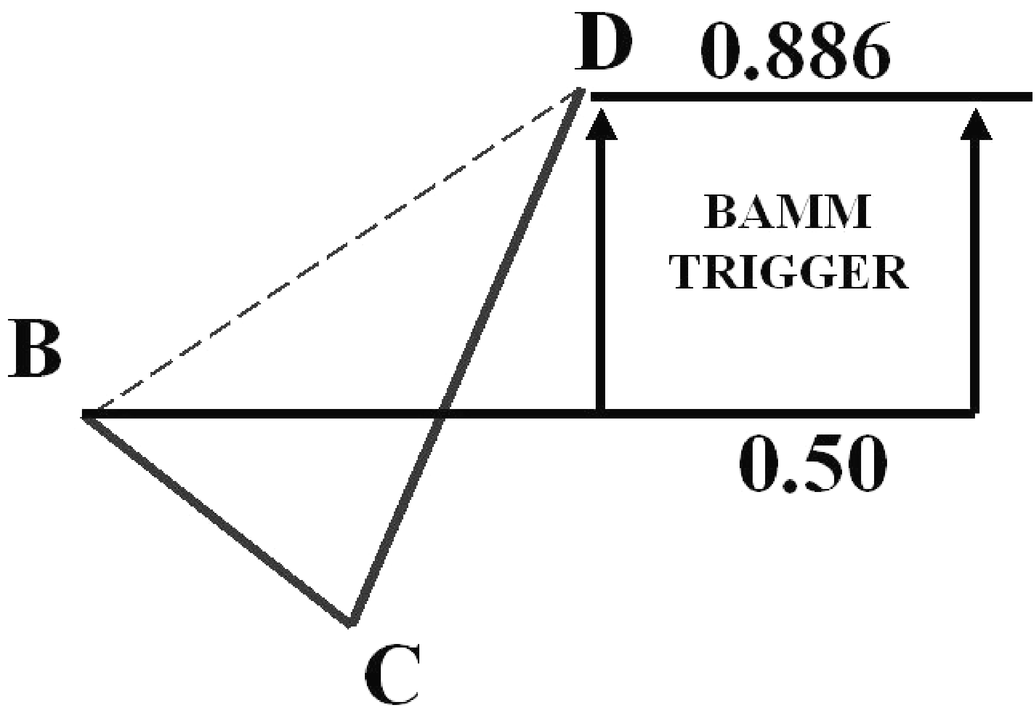
> ***"In the beginning, the study of the chart patterns, which are designated as the cardinal types of reversals, it must be clearly understood that their forecasting value largely depends on how perfect is the pattern, according to its type. A pattern which, in nearly every respect, closely resembles the accepted formation of a given type, is more likely to indicate the reversal of the trend accurately, and one with the observer much stretches imagination to make it conform to model pattern. One of the chief problems using patterns to determine reversals, is that so few perfect samples develop."***

The

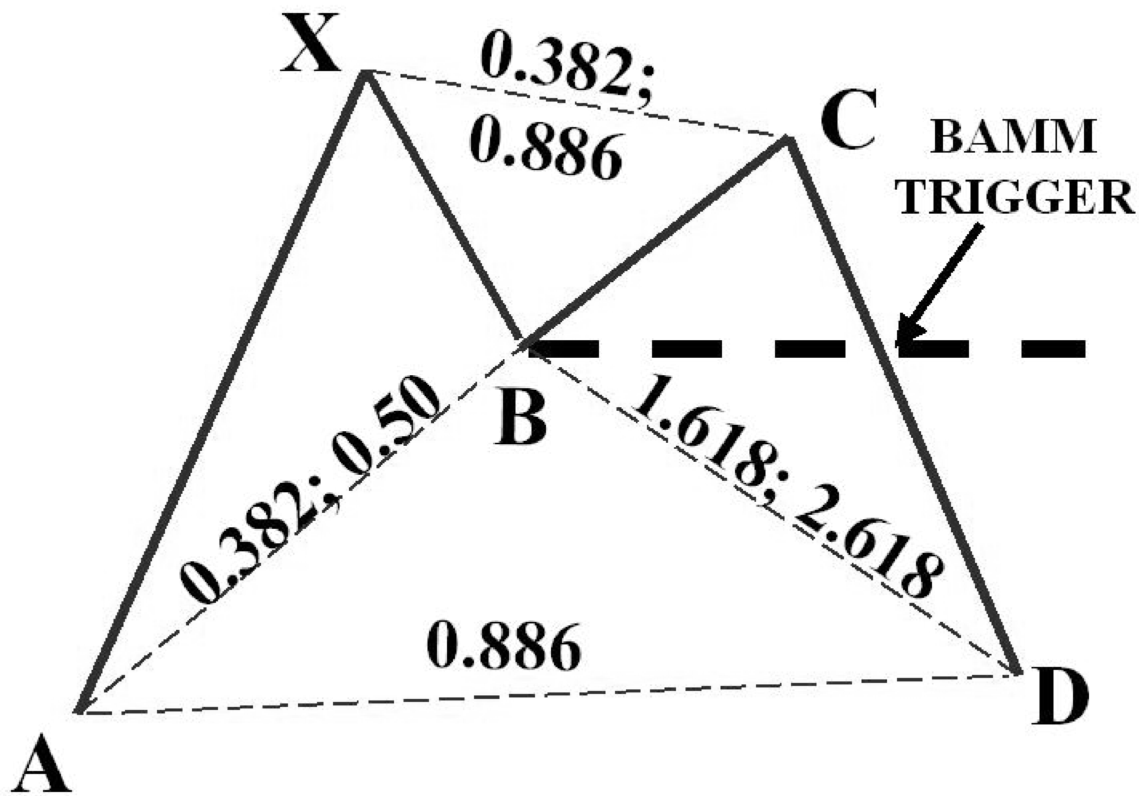
The understanding of these alignments can provide significant information on the direction of the price move and the ultimate target for its completion.

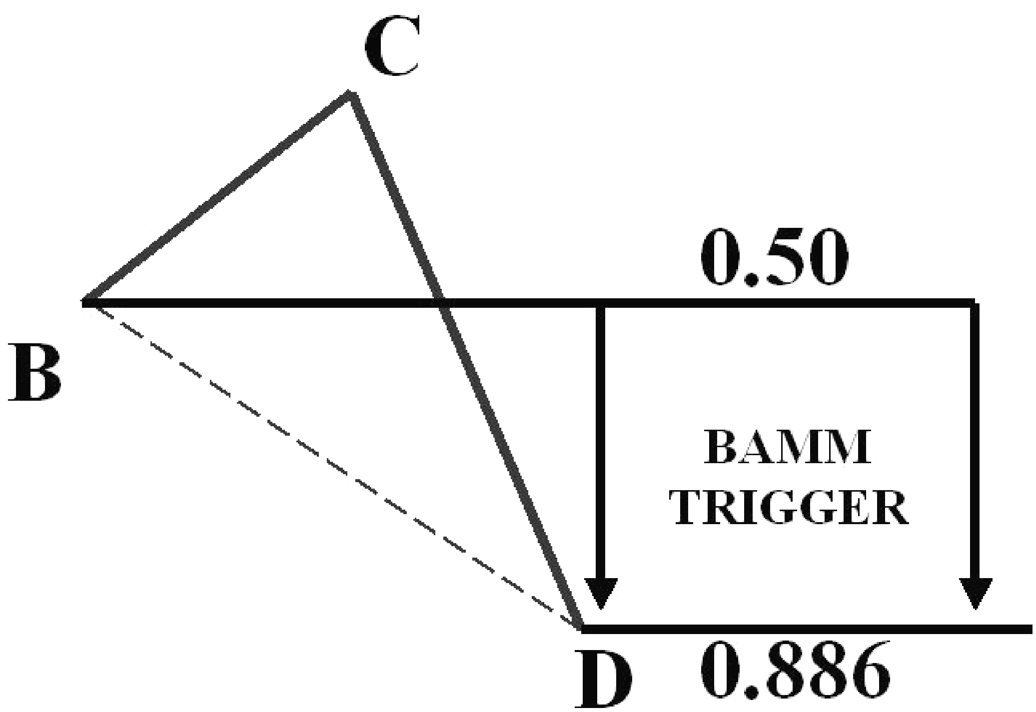
Bullish BAMM Breakout




D
0.886
BAMM
TRIGGER
B
0.50
C

Bearish BAMM Breakout




C
0.50
B
BAMM
TRIGGER
D
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CHP 10: RSI BAMM

The BAMM conqcept applied to indicators provided a perspective regarding a larger measure of bias and hence a potentiaelly bigger signal for the change in trend.
began to investigate the effectiveness of indicators as they relate to pattern completions, I realized that many of these technical tools formed similar structures as did the price action.

The RSI BAMM is a method that examines the structure of the indicator itself first without regard to the price action. There are many instances where the predominant trend will seem to go on forever. For example, a strong stock that enjoys a rally for many years may seem to never stop. Frequently such stocks trade quite nicely within an upward sloping trendlines range and seem to be invincible. These situations can lull a trader into a complacent mindset, believing that the rally will last forever. It is in an example like this that the importance of quantifying bias can be manifested. Therefore, all price action must be measured through pricing mechanisms and bias indicators.

Is a common misconception my many people the indicators are supposed to be utilized as a stand-alone technique but anyone that really understands technical analysis knows this is not the case. All methods must be compared, contrasted and analyzed with other approaches to determine the aggregate information provided from the price action. Whether to use trendlines, stochastics, Candlestick reversal patterns or any method, is imperative to have confirmation of multiple approaches to yield the most pertinent information for the best technical decision regarding any trade.

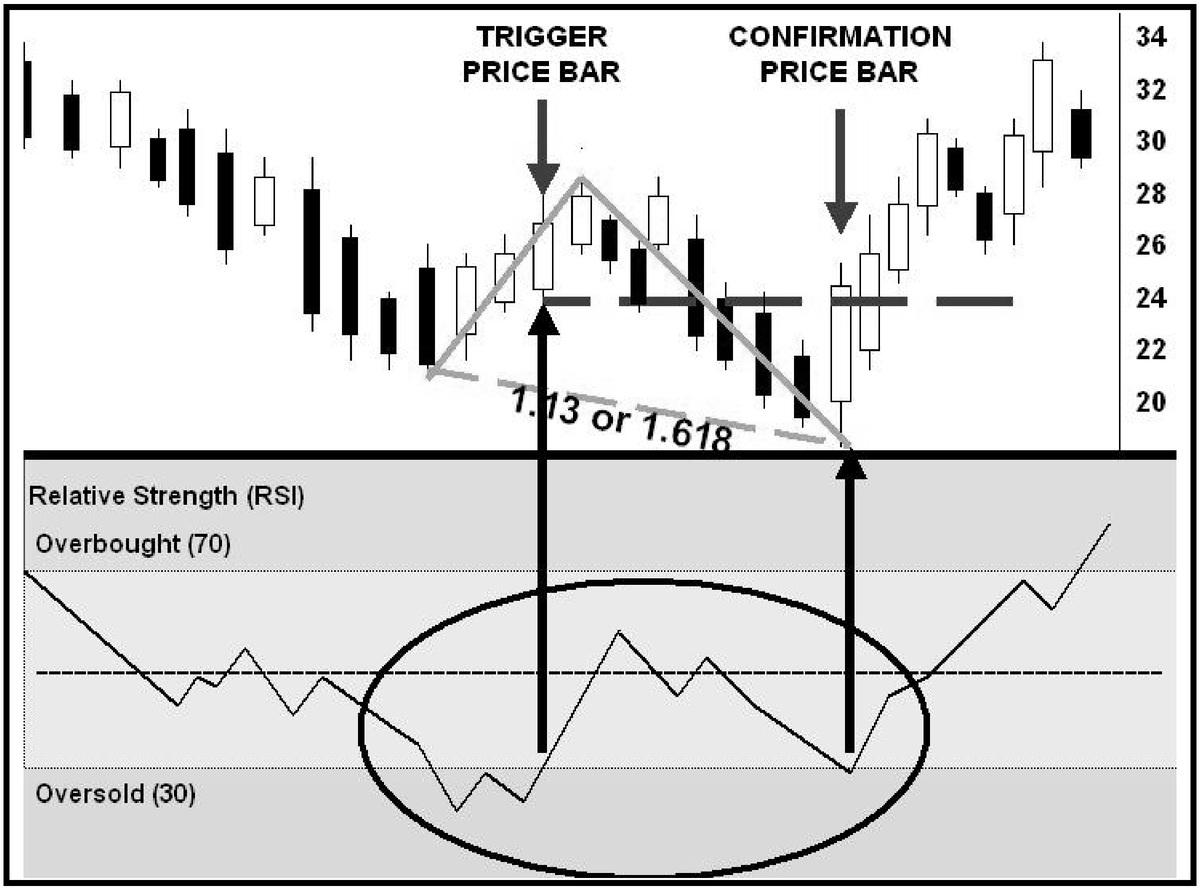
Although the RSI BAMM involves many steps to validate this technical phenomenon and it might seem somewhat complex first, is important understand we're identifying a unique technical situation. It is an advanced application of the basic tool that Wells Wilder developed decades ago. I have done a great deal of research on the various applications of the relative strength indicator. Starting with Wilder's original work and examining a variety of other material that discuss the indicator, I believe that the RSI BAMM is unprecedented application of this technical tool. Although many of the concepts do include a some of the simple theories involved with its application such as a divergence, confirmation and measurement, the advanced application of the method includes new concepts such as Fibonacci measurement techniques to confirm the indicator readings.

Let's first look at the development of the RSI BAMM and how it forms. For this example let's look at a stock that has sold off tremendously on a daily or weekly time frame. The first thing to look for is price action that possesses a relative strength reading that is below 30 for a bullish scenario and above 70 for a bearish scenario. But for now let's look at the bullish side. One of the reasons why the RSI BAMM is so effective is because it requires that the entire structure of the indicator perform below 30 reading. Therefore the initial structure of the RSI indicator will typically be well below the 30 reading and the RSI BAMM is typically a very early signal. This is an advantage because the structure itself can be distinguished while still allowing for enough time for the price action to set up correctly to validate the entire technique. Essentially, the RSI BAMM is a W-type structure in the bullish scenario that forms entirely below the 30 reading.

This is a mandatory aspect of the RSI BAMM, where all points of the W. formation must take place below the 30 reading. Is important to remember that this is an early signal and the price action quite frequently will continue in the predominant trend will after the W-type structure has formed. But, this is the divergence set up where the price action continues lower in the bullish situation, as the RSI stabilizes it moves higher. Depending upon the established trigger bar, the projected reversal level and the desired execution point for the trade it is quantified by the corresponding low of the RSI trigger bar and the extension of either a 113 or a 1.618 projection to define the estimated reversal zone. Is important take a minute and review exactly the process of how the relative strength sets up and the price action exhibits a divergent behavior. Again, this being the bullish example, the relative strength will for the W bottom to indicate the internal stabilization of the price action is measured by the relative strength formula. After the price action briefly stabilizes, it typically retest the trigger point where the the relative strength confirmed and prior support point with a specific W. type structure that forms and reversed in an oversold extreme man range of below a 30 reading.

Bullish RSI BAMM

The Bullish RSI BAMM begins with a complex reading in oversold area under the 30-limit. Referring to the RSI BAMM illustration below, the entire process requires several elements to validate this specific scenario. Although the entire illustration might seem a bit overwhelming upon first examination, this represents the ideal RSI BAMM model. I recommend that you thoroughly study this material before employing these strategies in your live trading.



Each step will be broken down to illustrate the ideal RSI BAMM model. Obviously, the ideal situation does not occur every time. It is important to remember that the real application of the RSI BAMM principles will require a degree of flexibility. However, the ideal model does present all of the critical elements that explain clearly the effectiveness of this strategy. It will take a period of study to fully comprehend all aspects of the RSI BAMM approach. In much the same manner that the initial rules of harmonic pattern identification and differentiation may have seemed overwhelming, the RSI BAMM rules – albeit a bit complex upon first study – provide a coherent and comprehensive method for accurately measuring potential areas of divergence. It is essential to maintain the patience to execute only those trades that possess all required elements that validate a trade signal based upon the rules of the Bullish RSI BAMM set up. Despite its initial complexity, the RSI BAMM strategy in combination with harmonic patterns effectively validates Potential Reversal Zones and improves the overall accuracy of the entire Harmonic Trading approach.

Step 1: Initial RSI Test of Extreme Bullish Limit

In the bullish RSI BAMM scenario, the first step is to identify price action that possesses a Relative Strength (RSI) reading in the extreme oversold zone below 30. It is important to note that the 30-level for the oversold limit, as well as the 70-level to define the overbought area, were first outlined by Wells Wilder in his book, *New Concepts and Trading Systems*. In addition, a 14-period average is calculated from his approach. Although this system utilizes the standard RSI measures, the indicator can be refined to utilize other levels and time periods to define the extreme relative strength levels. But, I leave that to you to research. I have experimented with other periods and these results have yielded excellent confirmation signals. In general, the standard parameters above a 70-reading as overbought and below the 30-limit as oversold with a 14-period average serves as the best guidelines for the entire RSI BAMM approach. Besides, who am I to disagree with Wells Wilder?

Step 2: Complete a Bullish M-Type Complex RSI Structure

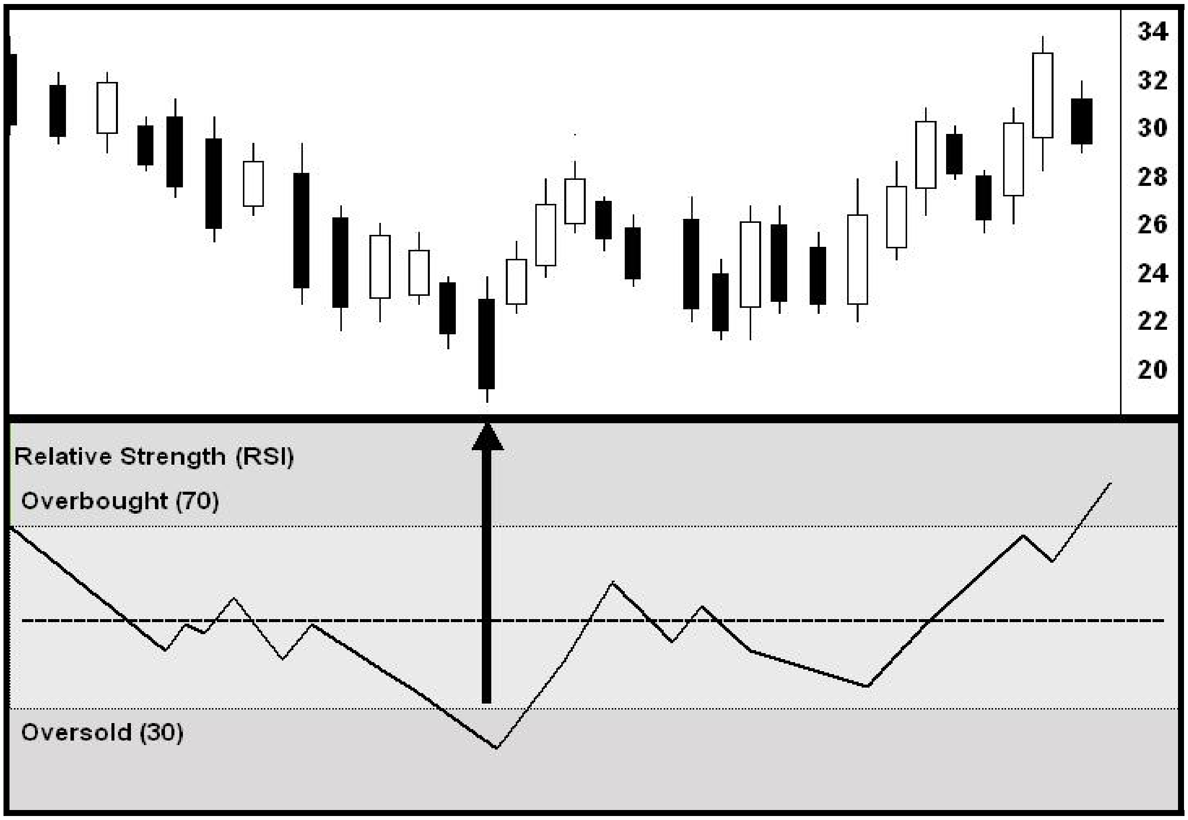
The initial focus should be on the formation of the indicator readings in the entire extreme range rather than looking for a specific numeric level. As I outlined earlier in this chapter for the bullish scenario, it is important to differentiate the two types of indicator structures that form at RSI extremes.

Two Types of Bullish Indicator Structures

There are two general classes of W-type indicator structures that test the extreme overbought level – impulsive and complex. Most bullish indicator readings that are below 30 will be impulsive in nature and will not yield the required structure to be considered as a valid RSI BAMM set up. However, valid complex structures that are correctly identified offer a tremendous technical advantage because they are particularly unique and represent a vital potential reversal area within the overall trend of the price action. The primary focus of the initial step is to identify a complex RSI BAMM M-type structure in the extreme oversold area under the 30-limit.

Bullish Impulsive Indicator Structures

A bullish impulsive indicator structure reflects price action that is experiencing a quick test of the extreme oversold support area that typically reverses quickly without any consolidating price action. Since the price action commonly reverses sharply in these cases, the indicator reading rallies above the extreme limit above 30 typically within 1 or 2 price bars of the initial test.



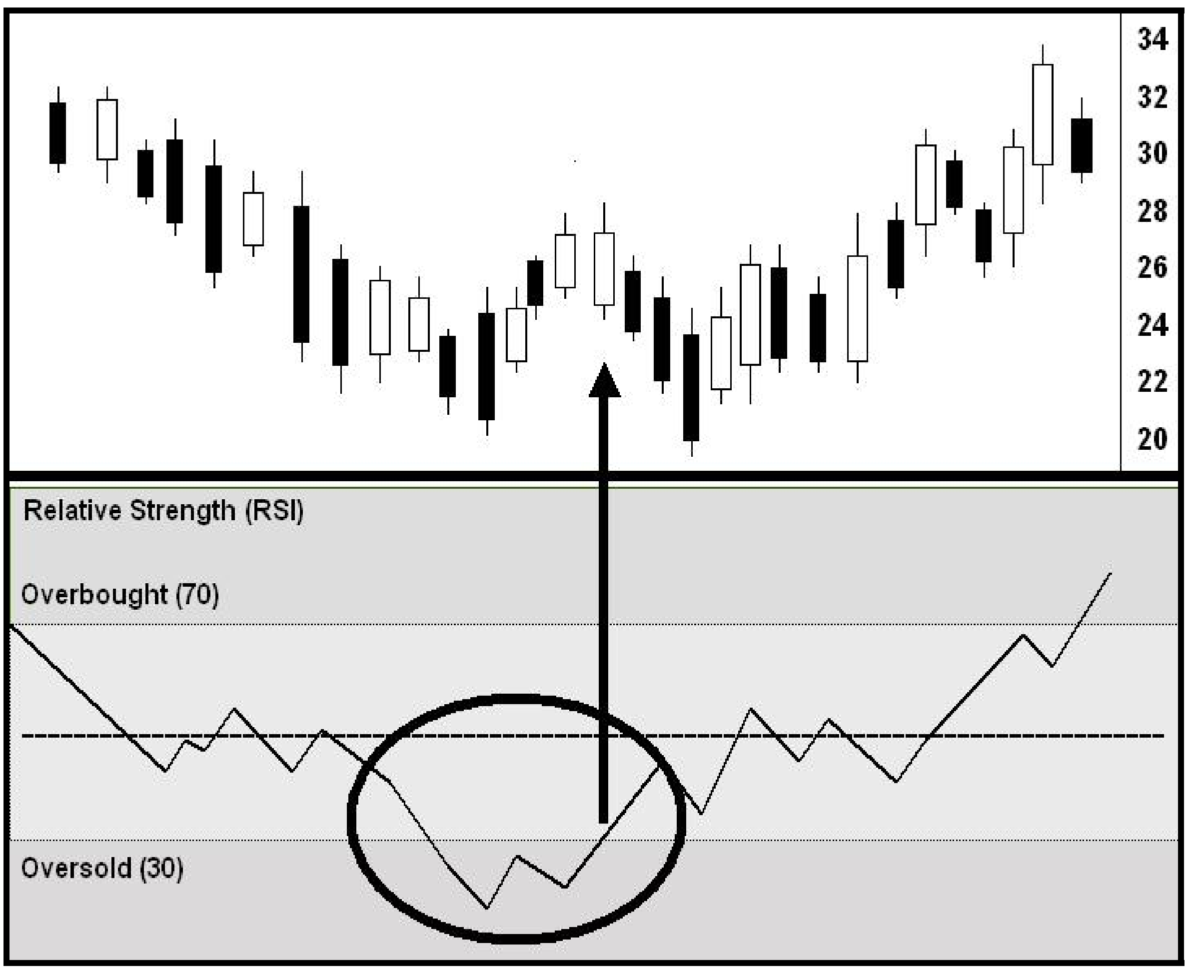
Although such impulsive formations may test the extreme bullish RSI level, it is important to focus on the nature of the indicator structure and not necessarily the exact numeric reading (as long as it is above the 70-limit). The exact indicator level is critical in quantifying the extreme state of RSI but the general indicator formation is the critical factor, as it serves as the essential trigger to validate a potential trade opportunity.

Impulsive structures can be effective technical measures as they can serve to confirm bullish patterns and other trading signals. But, it is important to note that the signals generated from extreme RSI readings do not constitute a comprehensive approach to trading the market. In fact, I believe that this is a common misconception for Relative Strength and most other technical indicators and oscillators.

In my opinion, such technical measures must be utilized as a complimentary methodology rather than as an exclusive approach. A Relative Strength reading above 70 does not automatically signify a trade opportunity. In fact, certain extreme impulse structures can signal significant continuations of the predominant trend. These strategies will be covered later in the book. For now, it is important to keep in mind that the general types of structures. Furthermore, as is the case with all technical indicators, other methods must be employed to validate any potential trade opportunity on a multiple confirmation basis.

Bullish Complex Indicator Structure

A complex structure represents an indicator formation that initially exceeds the 30-level and forms a W-type structure entirely in the extreme area. The complex structure typically remains below the oversold 30-limit longer than an impulsive formation. Also, it should be distinct from an impulsive indicator structure, possessing a clear “W” pattern.



Despite representing a more significant technical condition than an impulsive formation, the bullish complex structure is usually an early trading signal. In fact, it is common for price action to continue to decline sharply in price while the complex RSI structure is developing in the oversold range under the 30-limit. Although the advanced concepts will be clearly presented later in this chapter, it is important to keep in mind that a complex indicator reading is merely the starting point for the entire approach not the defining event of the methodology. Furthermore, the complex formation establishes the beginning of the most critical aspect of the entire RSI BAMM methodology – divergence.

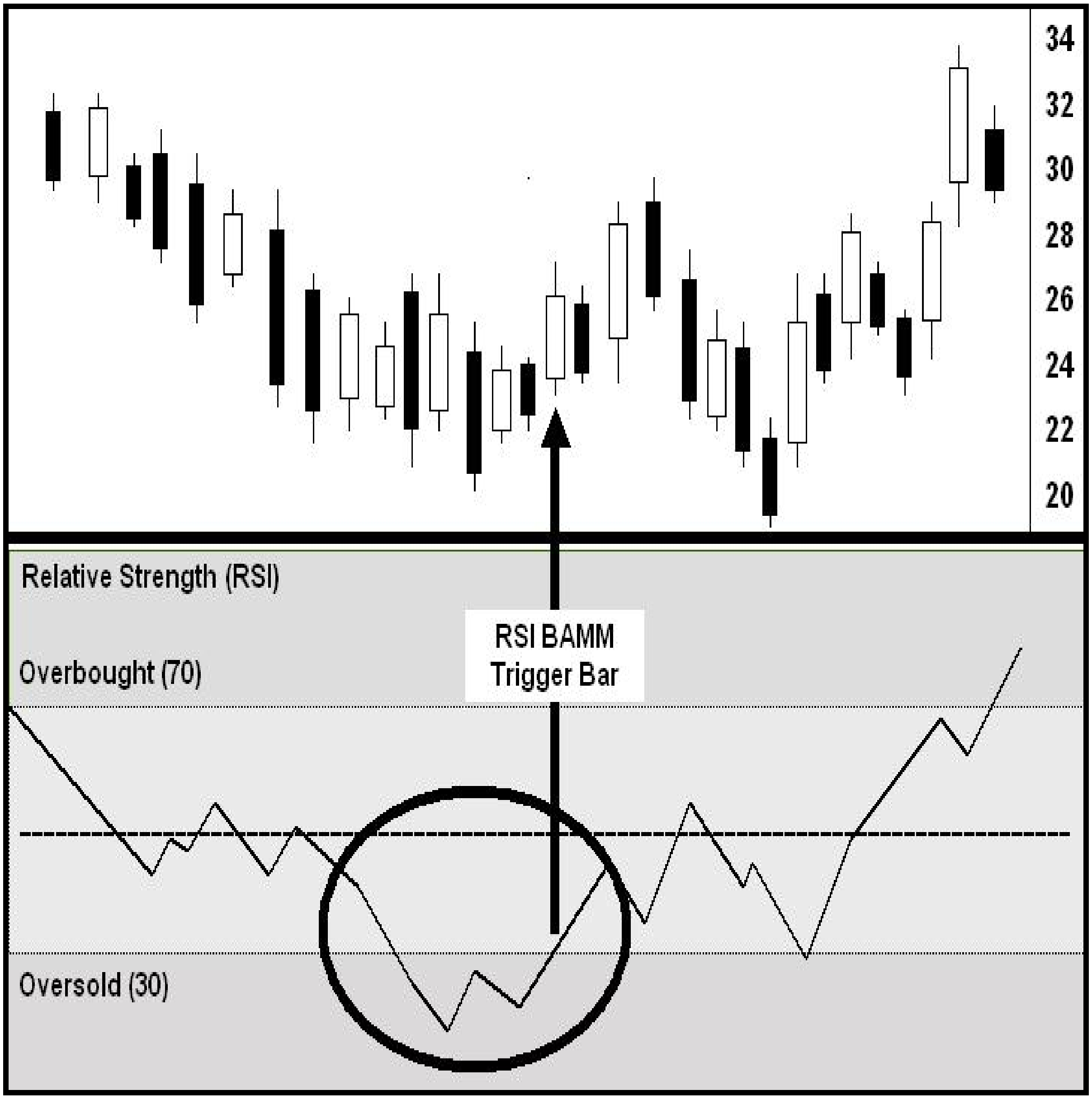
The bullish divergence occurs when the Relative Strength Indicator reading strengthens while the price action continues to decline. Although the price action may seem to be maintaining its current downtrend, valid complex bullish RSI structures usually trigger a reversal sooner rather later, and they can mark critical support levels for a potential change in the overall direction. Although a few other elements must fall into place for the bullish RSI BAMM to be validated, the formation of a complex RSI structure triggers the starting point for entire process. Again, this is an early signal and it is critical to wait for the W-type structure to break above the 30-line to confirm its completion. After the complex RSI structure has been established, the other considerations of potential pattern completions and specific RSI BAMM harmonic measurements can be projected to determine the optimal reversal area. This leads us to our next step, which is the defining and the measuring of the price level for that triggers this breakdown.

Step 3: Define the RSI Trigger Bar

After defining the complex RSI formation, the next step requires a measurement of the price area where the W-type indicator structure has completed. The price bar that causes the bullish complex RSI indicator reading to complete and to rally above the oversold 30-limit is known as the ***RSI BAMM Trigger Bar***.

After identifying the RSI BAMM Trigger Bar, it is critical to mark the bottom of this price bar by drawing an extended line from the low, projecting the minimum RSI BAMM support level to the right of the chart (as is illustrated in the diagram). This RSI BAMM Trigger Bar support line serves as a minimum technical level for the corresponding retest and the anticipated execution area of the completion of the final phase of the RSI BAMM.

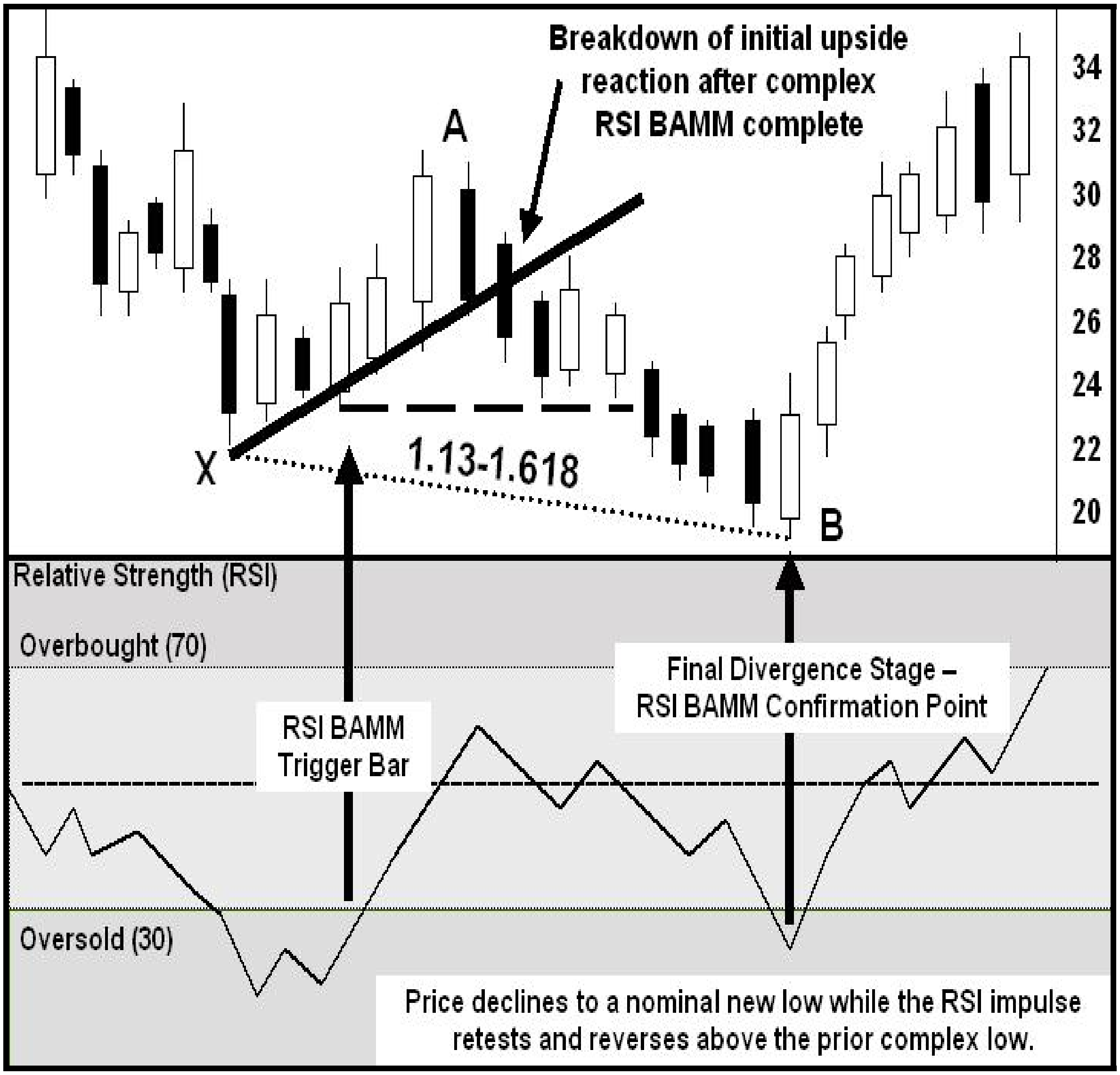
From a general perspective, the RSI BAMM Trigger Bar denotes the starting point for the critical divergence phase that the entire methodology is attempting to define and to quantify. Although there are strategies that I will present later in this chapter to capitalize on the initial indicator reaction, from a broader perspective the RSI Trigger Bar can reveal a great deal about the validity of the set up and the state of the potential price action. For now, the most critical element of the RSI BAMM approach begins after the indicator has reversed from the oversold area by completing a complex W-type structure.



The position of the Bullish RSI BAMM Trigger Bar in relation to the prior extreme high point is critical. Although its significance will be further explained later in this section, it is important to remember that the bullish RSI BAMM Trigger Bar typically will be the price bar that is the exact prior low of the current move or within a few intervals of the extreme low. The Trigger Bar is critical because it marks the completion point of the complex RSI structure. In essence, it is the price bar that completed the W-type structure and rallied the indicator reading above the oversold 30-level.

Step 4: Reaction of RSI and Price

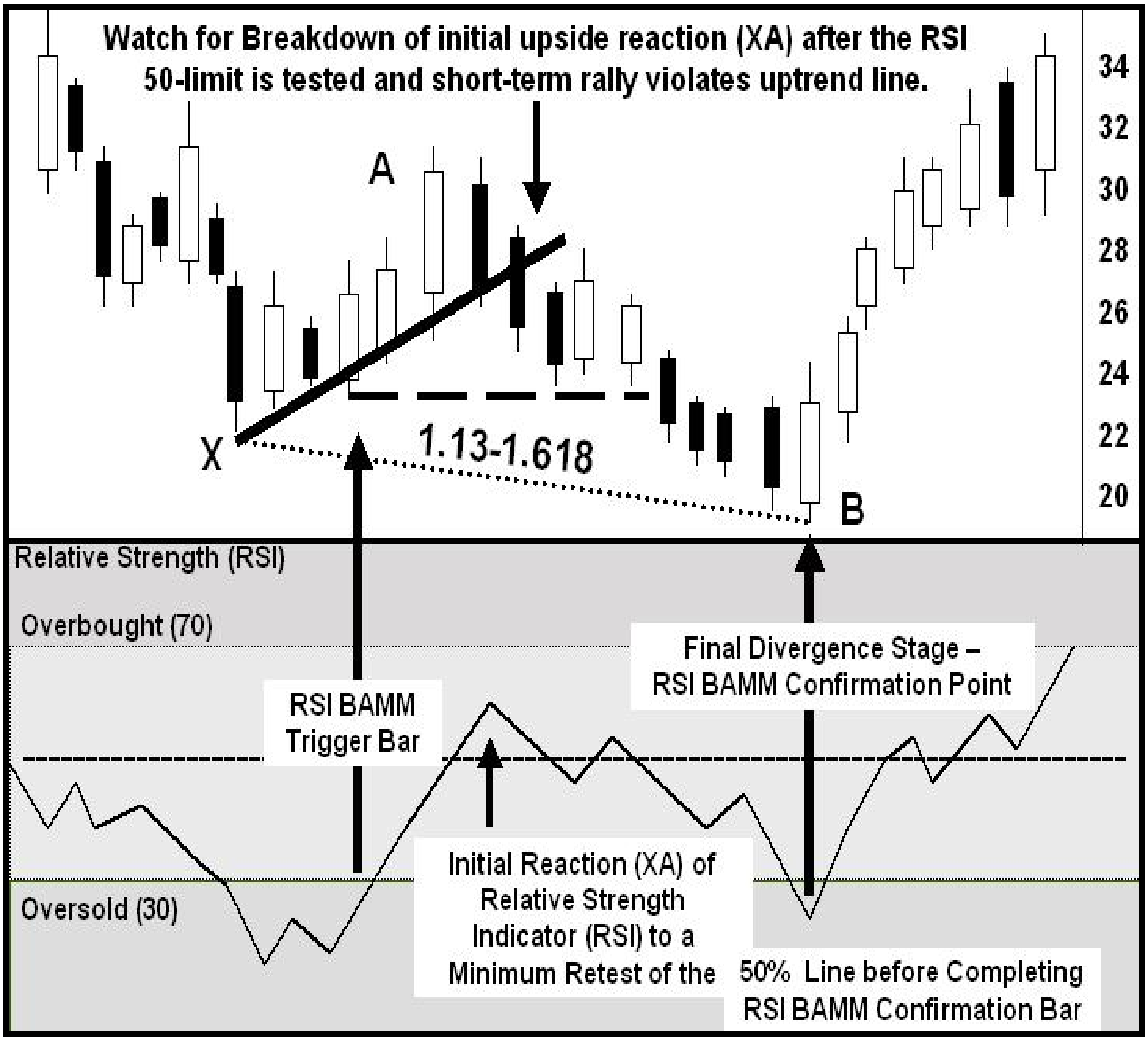
The initial breakdown of the RSI and price following the completion of the complex indicator formation represents the first phase of the approach. In an ideal RSI BAMM scenario, the price and indicator decline in tandem.



Frequently, the initial breakdown offers a distinct trading opportunity but these strategies will be covered a bit later in this chapter. For now, the initial breakdown requires a few elements to set up the completion of the RSI BAMM.

Specific Type of Retest

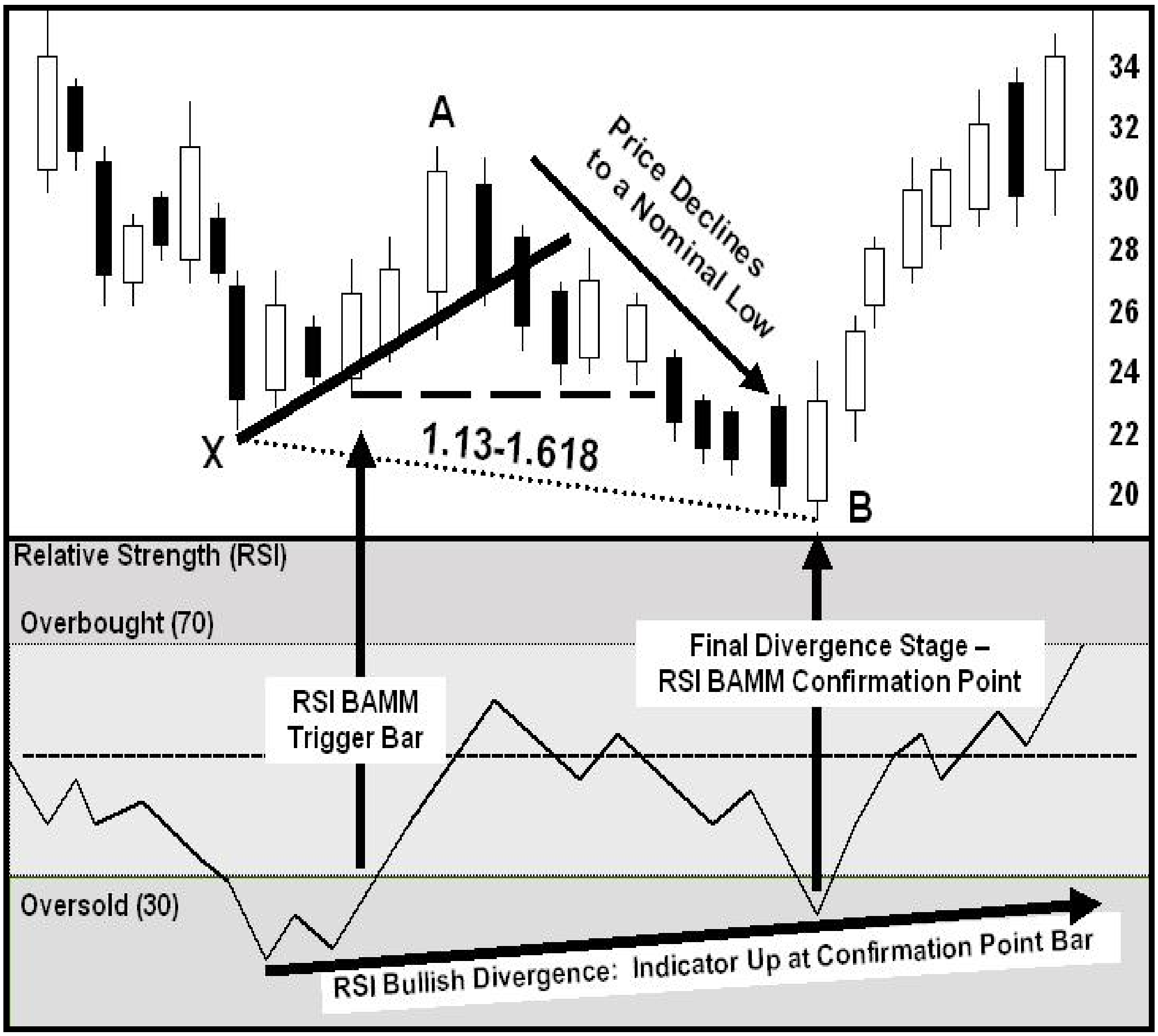
There are a few technical events that must occur on this initial Trigger Bar reaction. Namely, the RSI reading MUST decline to at least the 50-level as the price nominally reacts. Although there is room for interpretation as the RSI reading may exceed the 50-level on this initial reaction, it serves as a minimum requirement that precedes the corresponding retest of the resistance area established by the RSI BAMM.



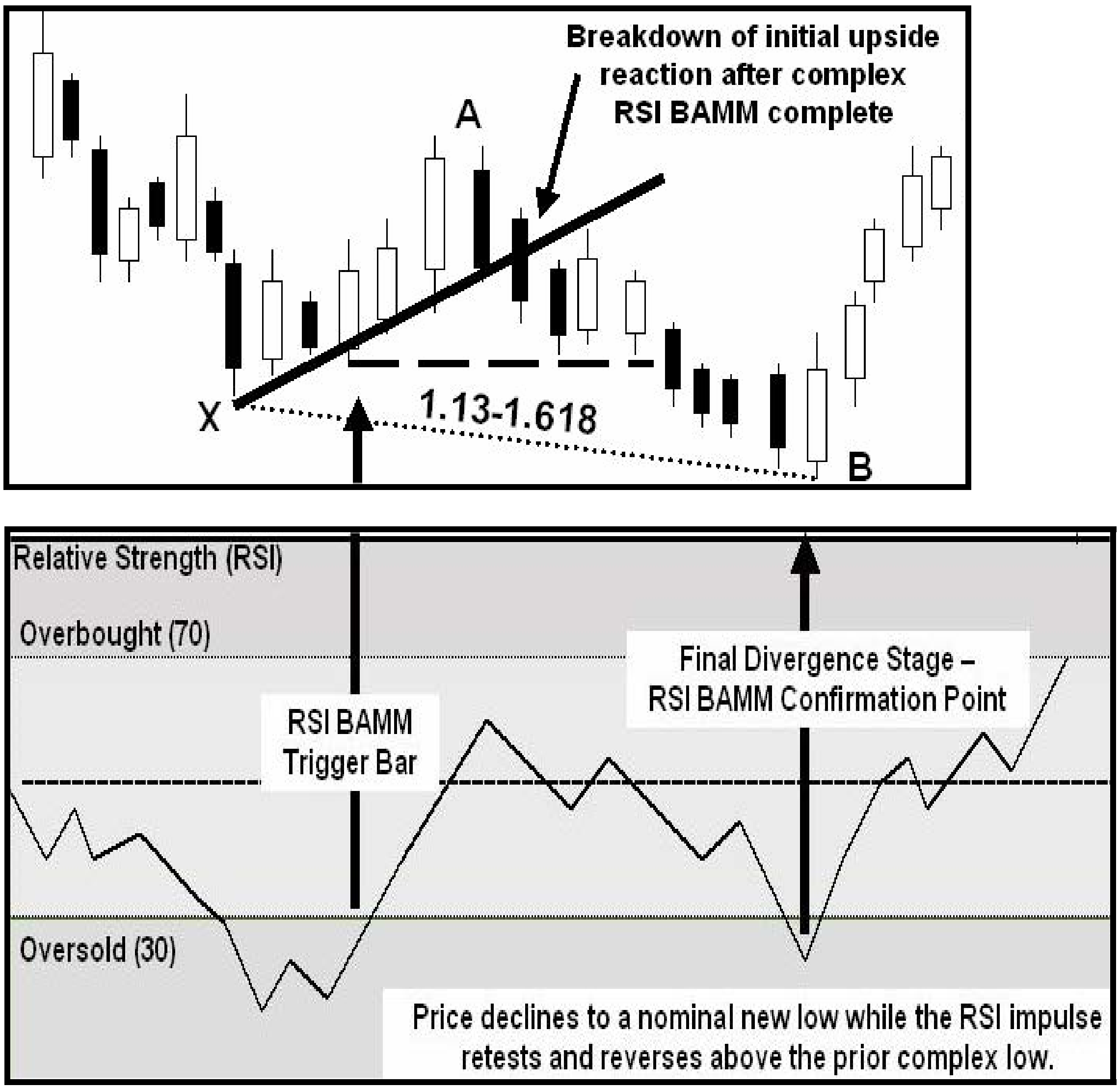
Again, this specific type of retest offers other short-term trading opportunities that I will explain a bit later in this chapter. But, the important aspect of this element of the process establishes the final divergence phase of the entire approach.

Step 5: The Final Phase - Divergence of RSI vs. Price

The final divergence stage begins after the RSI reading pulls back to at least the 50-line and the short-term price breaks out from the downtrend line of the initial reaction. It is important to remember that the horizontal line drawn from the peak of the RSI Trigger Bar to the right of the chart defines the minimum resistance level for the completion of the RSI BAMM and the eventual entry of the trade.



This is a situation where the Relative Strength Indicator reading is providing an early signal to the end the predominant trend. Although this signal may be the end of the trend technically, the price action typically experiences one last decline to retest the support area established by the complex Bullish RSI structure. This final stage of the retest reveals a great deal about the strength of the predominant trend and the validity of the signals generated by the complex RSI structure. In essence, the price action diverges in a “last gasp” from the indicator reading. The price action will nominally exceed the prior low of the area marked by the complex RSI structure, while the indicator reverses after an impulsive retest of the oversold 30-limit. The critical point of the divergence can be seen in this snapshot of the illustration where the trend of the price action continues nominally lower while the trend of the RSI reading moves higher, typically completing an impulsive structure at the confirmation point.



This final stage of the entire setup reveals the extent of divergence, where the Relative Strength reading of the trend indicates a reversal hand while the price continues to decline in a final dip. If the RSI structure is a valid support signal, typically the price action will reverse quickly after exceeding the initial prior low point. Although I will outline the advantages of utilizing Harmonic Trading techniques of pattern recognition and Fibonacci measurement strategies with the RSI BAMM, it is important to examine this general technical phenomenon on its own before trying to understand other complementary methods. From a basic RSI approach, the RSI BAMM defines a specific type of divergence while employing price pattern recognition techniques to define the price level - Potential Reversal Zone (PRZ) – where a change in trend is likely to occur. Most important, this divergence - where the price and the Relative Strength Indicator readings move in opposite directions - frequently defines high probability areas for significant harmonic patterns completions. The combination of these techniques creates a comprehensive approach that requires many conditions to be met before a trade signal is triggered. Hence, the RSI BAMM filters out more invalid patterns than the standard approach and requires a stricter application of the technical rules to generate a valid trade opportunity.

Bullish RSI BAMM Confirmation Point: 1.13 vs. 1.618

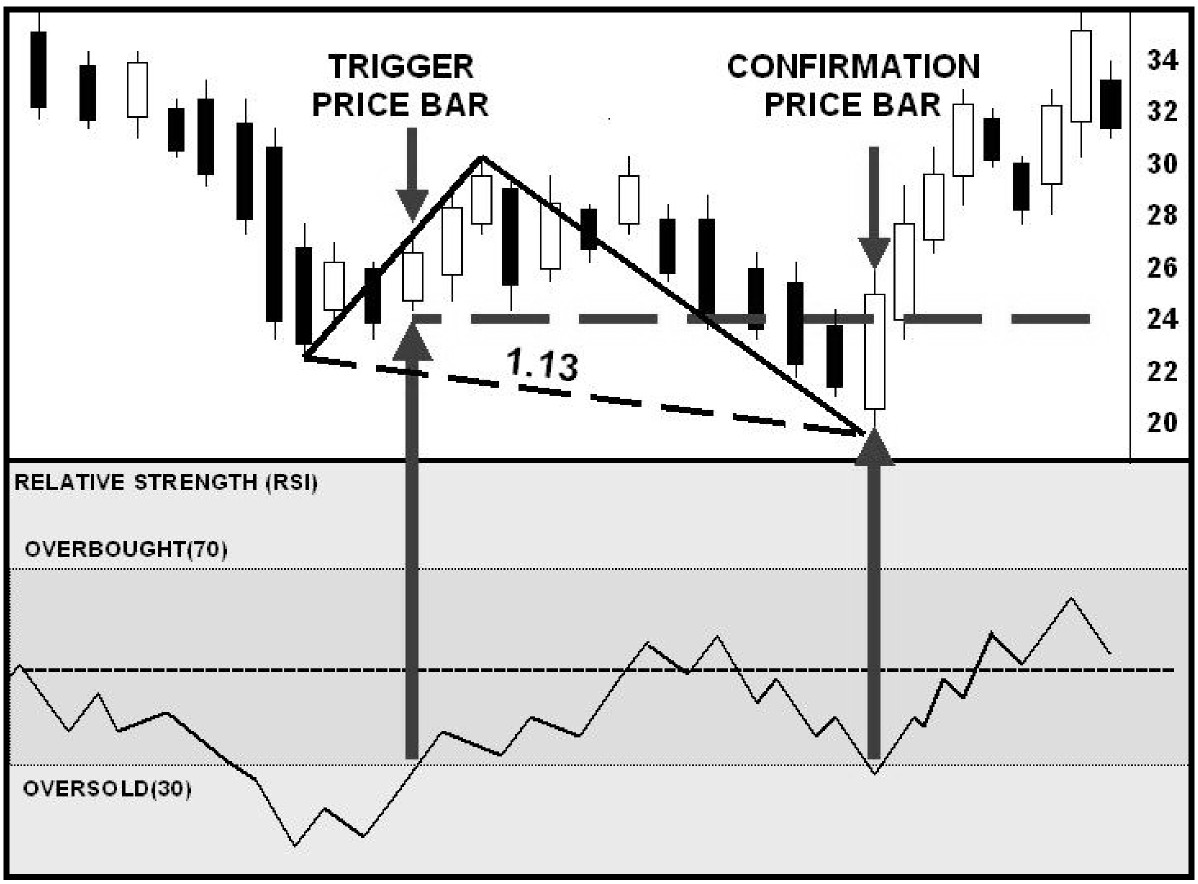
In the development of the RSI BAMM, I was challenged for quite some time to discern the correct extension for the confirmation point. Although the difference between 1.13 and 1.618 may appear small, in real trading situations this gap frequently can be quite expensive. With respect to the primary tenets of Harmonic Trading and pattern identification, exact specification of technical measurement techniques is required to yield the most accurate information regarding the validity of any trading opportunity. Although these are general rules, I noticed a unique variation in the ultimate extension of the final divergence phase of the Bullish RSI BAMM.

The key factor depended upon the position of the Trigger Bar relative to the prior low. If the RSI BAMM Trigger Bar is a few price bars (typically 2-4) from the prior low, the execution of the trade will occur at the corresponding 1.13 extension. However, a RSI BAMM Trigger Bar develops at the extreme high for the move will result in a 1.618 extension at the confirmation point.

The technical divergence that occurs in this step is the most important part of the entire approach because it gauges the price action at a critical "internal" point within the trend. Although the RSI BAMM structure may form in the indicator and indicate internal strength, the retest where the RSI has stabilized and the price action has diverged offers an enormous amount of information regarding the technical state of the overall trend. Specifically, when the price declines below the initial low established by the RSI BAMM Trigger Bar yet the indicator reverses from an impulsive test of the overbought 30-limit, the confirmation point serves as a critical measure that validates the existence of any bullish patterns that converge with either a 1.13 or a 1.618 extension. The prescribed RSI BAMM projection points define a precise technical window for a potential reversal. In combination with harmonic pattern recognition techniques, these methods complement each other immensely when all evidence analyzed yields similar technical results. Simply stated, the key is to look for a harmonic pattern that completes in the same area and at the same time as the RSI BAMM Confirmation Bar. For now, it is important to review the basic rules for the measurement of the projected divergence – either 1.13 or 1.618.

1.13 Extension @ Bullish RSI BAMM Confirmation Point

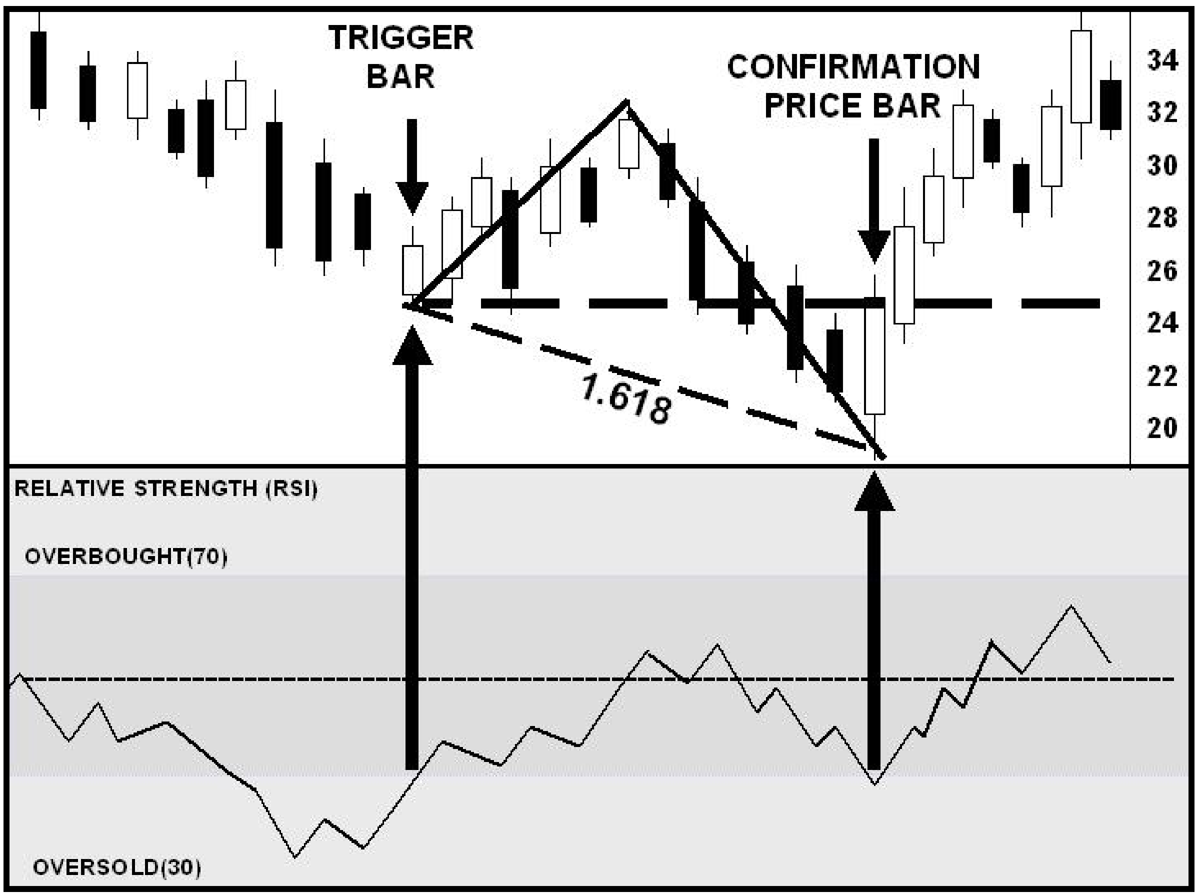
Although the general rule regarding the confirmation point extension differentiates the 1.13 and 1.618 ratios, the focus of the Trigger Bar should be on the extreme prior low. Essentially, if the Bullish RSI BAMM Trigger bar is NOT the low price bar, the 1.13 extension is utilized to quantify the execution area for the trade.



Again, the typical position of the Bullish RSI BAMM Trigger Bar is the 3rd or 4th price from the prior extreme low of the measured move. Without question, an extreme low price bar that produces the RSI BAMM Trigger bar will utilize a 1.618 extension. However, the 1.13 extension is less clear because it serves as a critical minimum price level at the RSI BAMM confirmation point.

The completion of harmonic patterns may influence the ultimate execution point of the trade beyond the minimum target of the confirmation point in the case of a 1.13 extension. For example a Bullish Butterfly may form in the final divergence leg and complete at a 1.27 projection slightly past the 1.13 of the RSI BAMM Confirmation Point. In this situation, the completion of the harmonic pattern would be more significant and serve as the entry level for the trade. Although a test of the 1.13 extension should always be a minimum requirement for a trade to be triggered at the RSI BAMM Confirmation Point, the completion of a harmonic pattern in this area possesses greater significance and more distinct technical price levels to determine the validity of a potential trade.

1.618 Extension @ RSI BAMM Confirmation Point

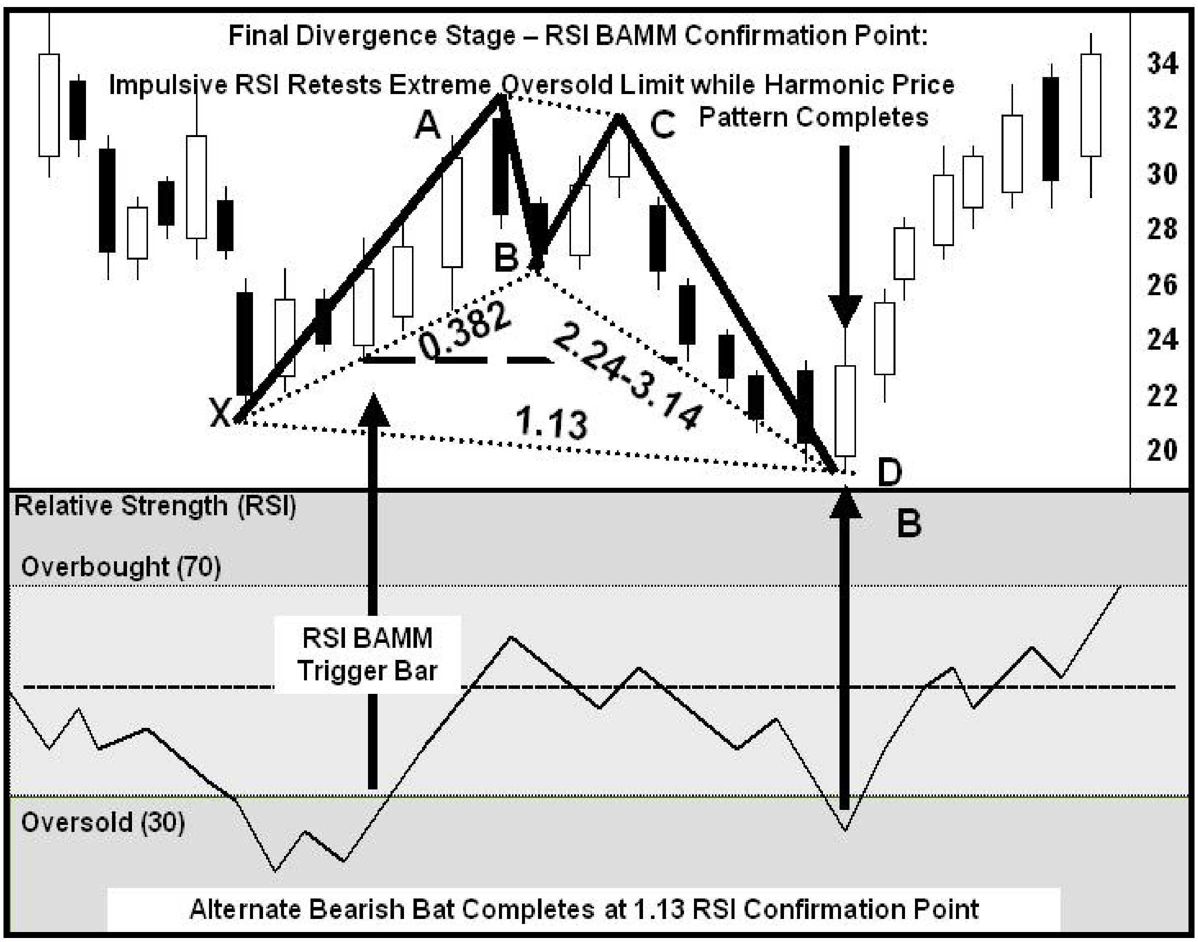


In either situation**,** the general rule for the confirmation point extension must focus on the location of the Trigger Bar, as it relates to the extreme prior peak. ***If the RSI BAMM Trigger bar IS the extreme low price bar, the 1.618 extension is utilized to quantify the confirmation point and the execution area for the trade.***

Step 7: Trade Execution at the Bullish Pattern Completion and the Bullish RSI BAMM Confirmation Point

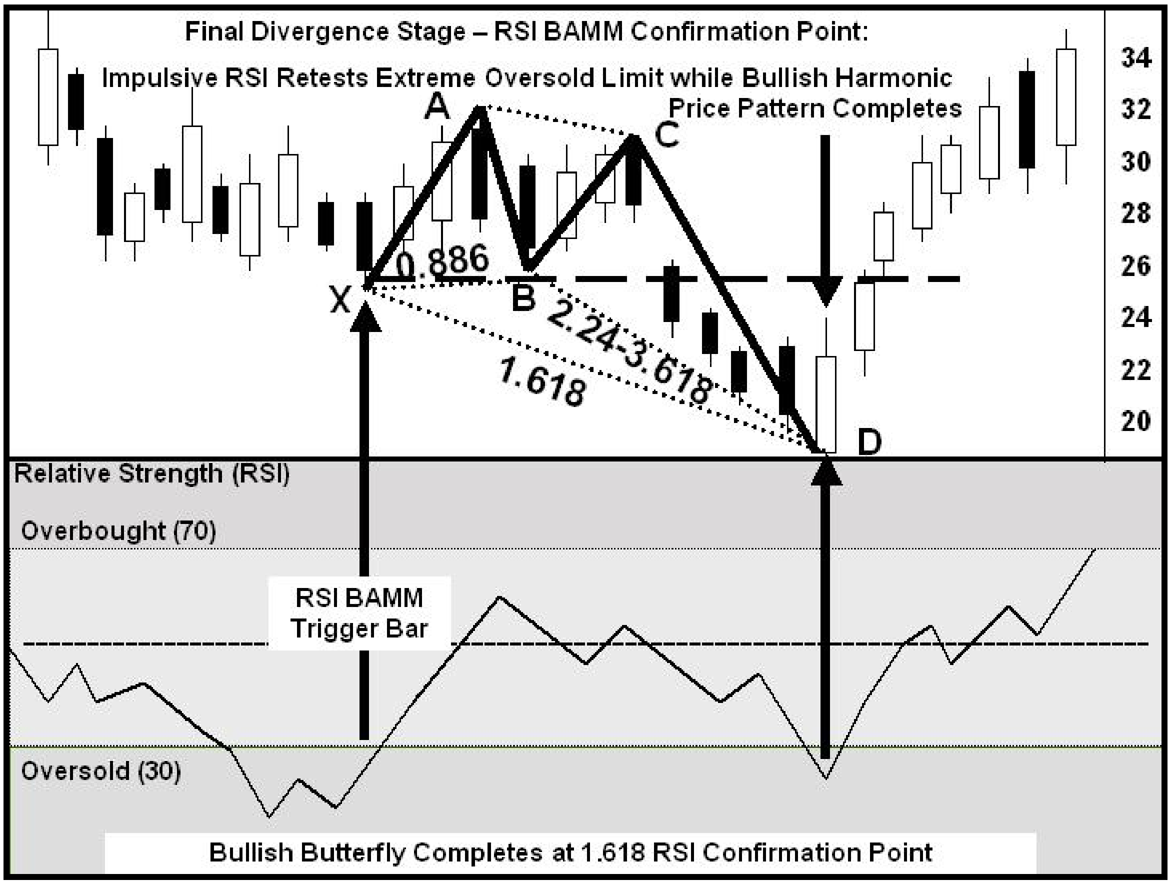
After establishing the necessary steps to define the final divergence phase of the Bullish RSI BAMM, the integration of harmonic patterns at the confirmation point represents the ultimate advancement of the entire Harmonic Trading methodology. Although the RSI BAMM confirmation point is generally differentiated by location of the Trigger Bar as it relates to the prior low, the price area of execution the trade is defined by the completion of a distinct harmonic pattern in its Potential Reversal Zone (PRZ). The combination of these two methods in this manner yields precise levels of harmonic support and accurate entry levels for potential trades. However, there are a few important scenarios that must be regarded, as to know which patterns are to be applied to the appropriate RSI BAMM scenario. The primary focus should determine whether the RSI BAMM Confirmation Point will end at a 1.13 or 1.618 extension.

Intermediate RSI BAMM Trigger Bar Signals 1.13 Extension



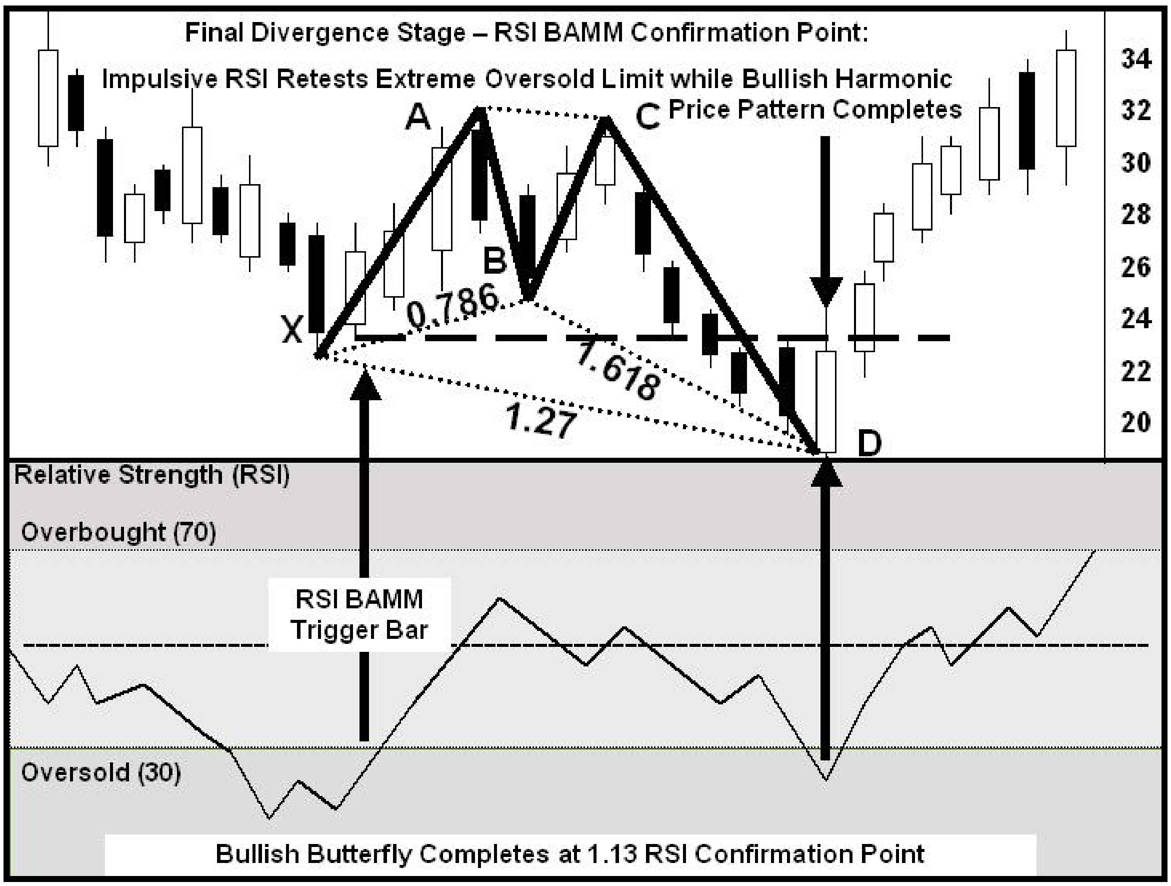
The following illustration shows the entire Bullish RSI BAMM methodology while incorporating a Bullish Alternate Bat at the confirmation point.

Extreme RSI BAMM Trigger Bar Signals a 1.618 Extension



Pattern Completion in 1.13-1.618 RSI BAMM Area

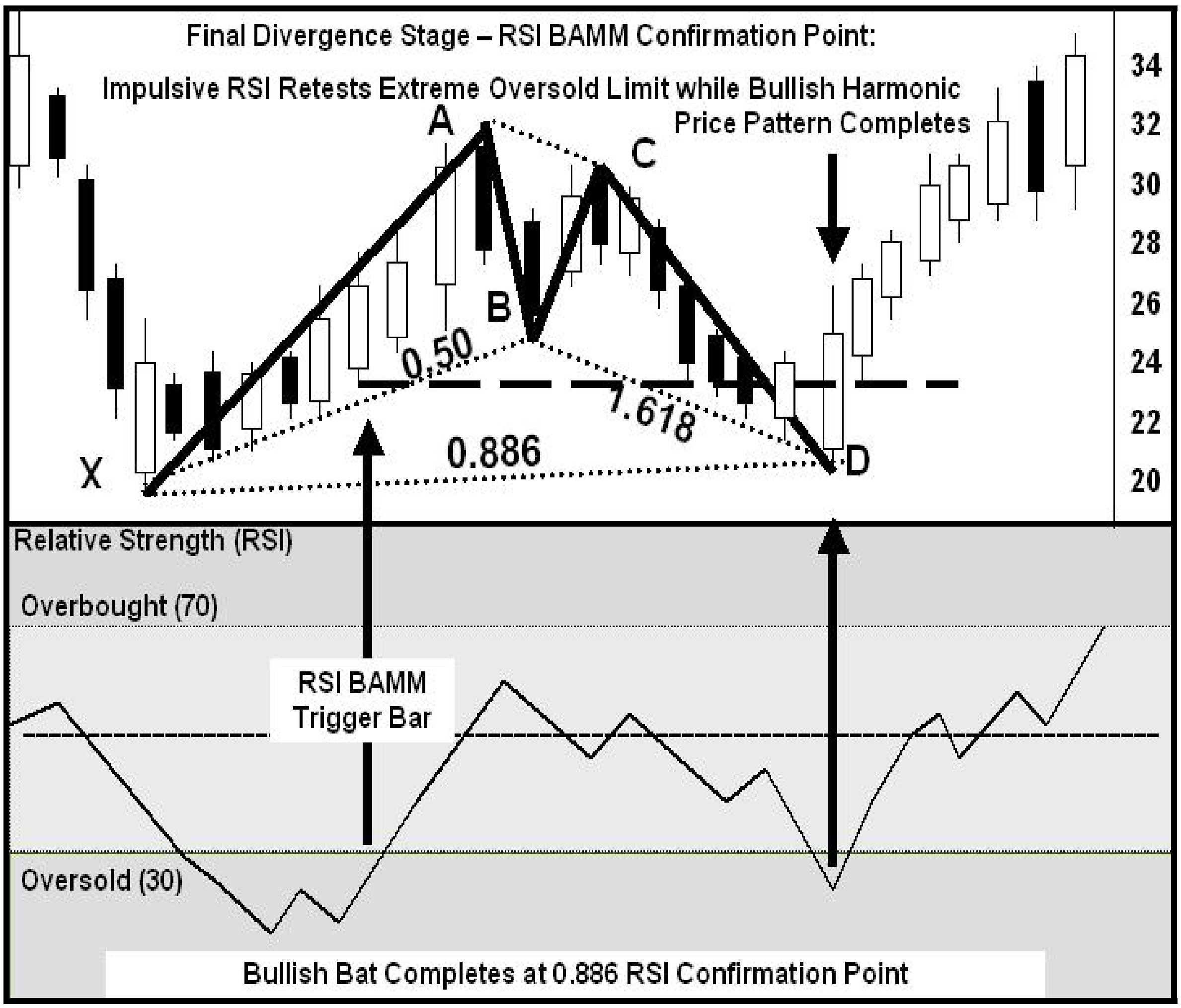
It is important to remember that the line drawn across the chart from low point of the RSI BAMM trigger bar acts as a minimum support line for the entire set up. The corresponding harmonic projections of the Bullish Butterfly completion act as the most critical price range for a valid trade execution. Although the two price levels of the 1.13 and the 1.618 define the entire area for the RSI BAMM, the pattern that is completing within these act as the limits are the .



Essentially this is defining the area where the bias has changed and the price trend will not changed to reflect be new bias. It is important in note that the final move that takes the price action below the prior low for a brief time to either the 113 or 1618 extension is called the divergence. Although others have used the concepts of divergence as it relates to indicator readings and price action, in this situation the divergence behavior is a little different. The RSI indicator formation is unique and the overall approach includeS specific harmonic measurements to define the entire technical phenomenon.

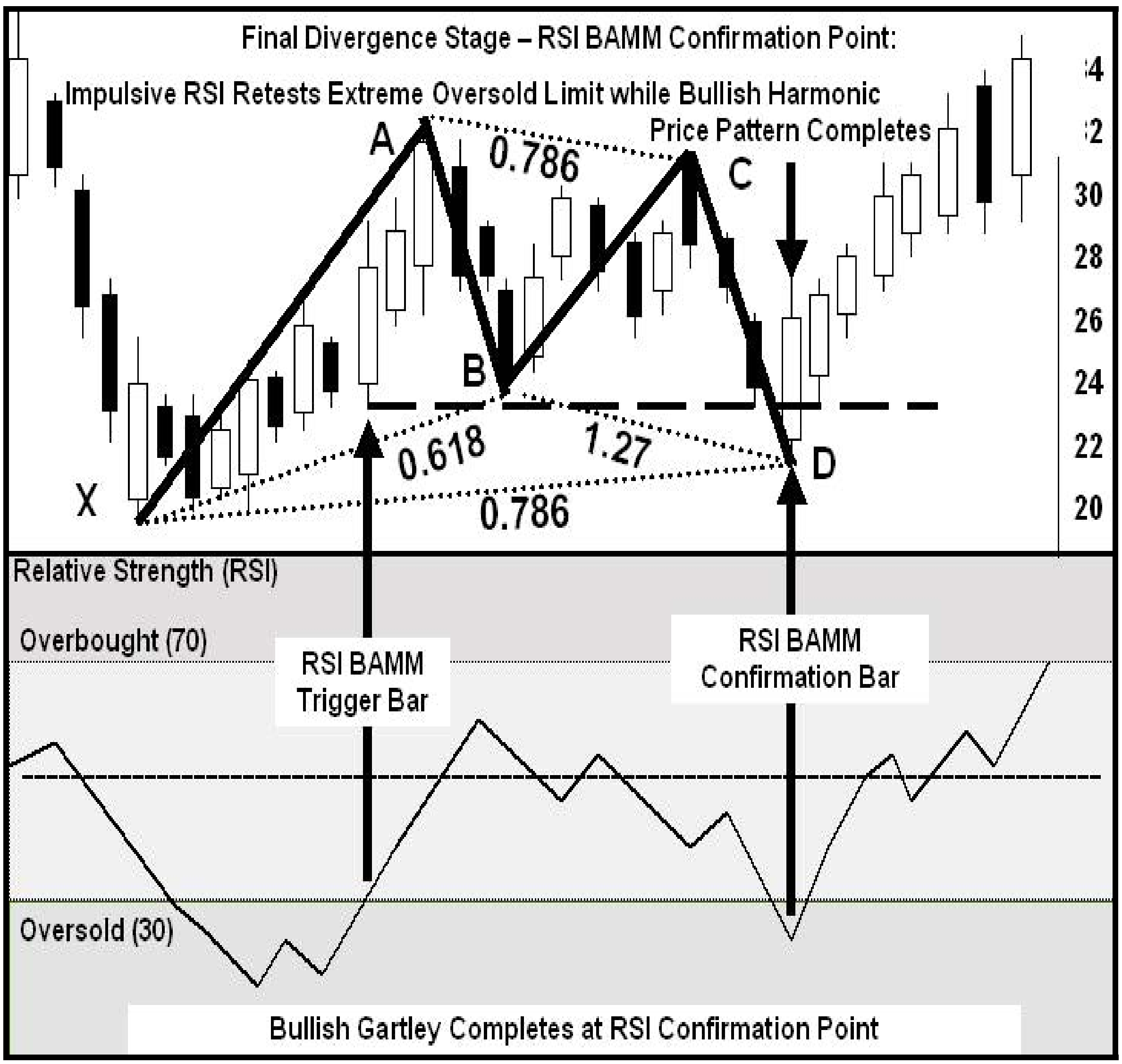
Pattern Completion Before 1.13-1.618 RSI BAMM Area: Bullish Bat

look to execute trade in potential reversal zone combined with RSI BAMM zone the execution line for the entire RSI BAMM is at the 113 or 1618 extension but this is not the only consideration for executing a trade. Remember, this is one technique that complements other approaches Neve be Harmonic Trading Price pattern recognition or whatever.



Of course, we're looking to harmonic patterns and other considerations such as pattern completions must be considered before executing a trade. But this is where the power of confirmation of mobile technical methods gives us a much greater for probability of a valid reversal and profitable move. As I will show in future examples, when the RSI BAMM lines up with distinct harmonic pattern completions, the accuracy of these methods are greatly increased.

Pattern Completion Before 1.13-1.618 RSI BAMM Area: Bullish Gartley




VZ 5-MAY-06
Weekly
EMA13 38.60
EMA20 38.89
EMA50 38.40
SMA50 38.29
SMA200 40.57
Bollinger(20,2.0)
0.886AB
0.618XA
1.270BC @ $28.084
0.786XA @ $29.926
AB=CD @ $29.060
1.270BC @ $28.084
Settings
Vol(10) 42,089,000
HVR(100-6) 1.00
RSI(14) 40.70
Stoch(5-3) 17.3
MACD(6-12-6) -1.02 Hist: -0.40
ADX(14) 22.71 14.00 -29.21
CMF(21) -0.092
Accum/Diss(20)
Overbought
Oversold
The Harmonic Analyzer (TM) : VZ
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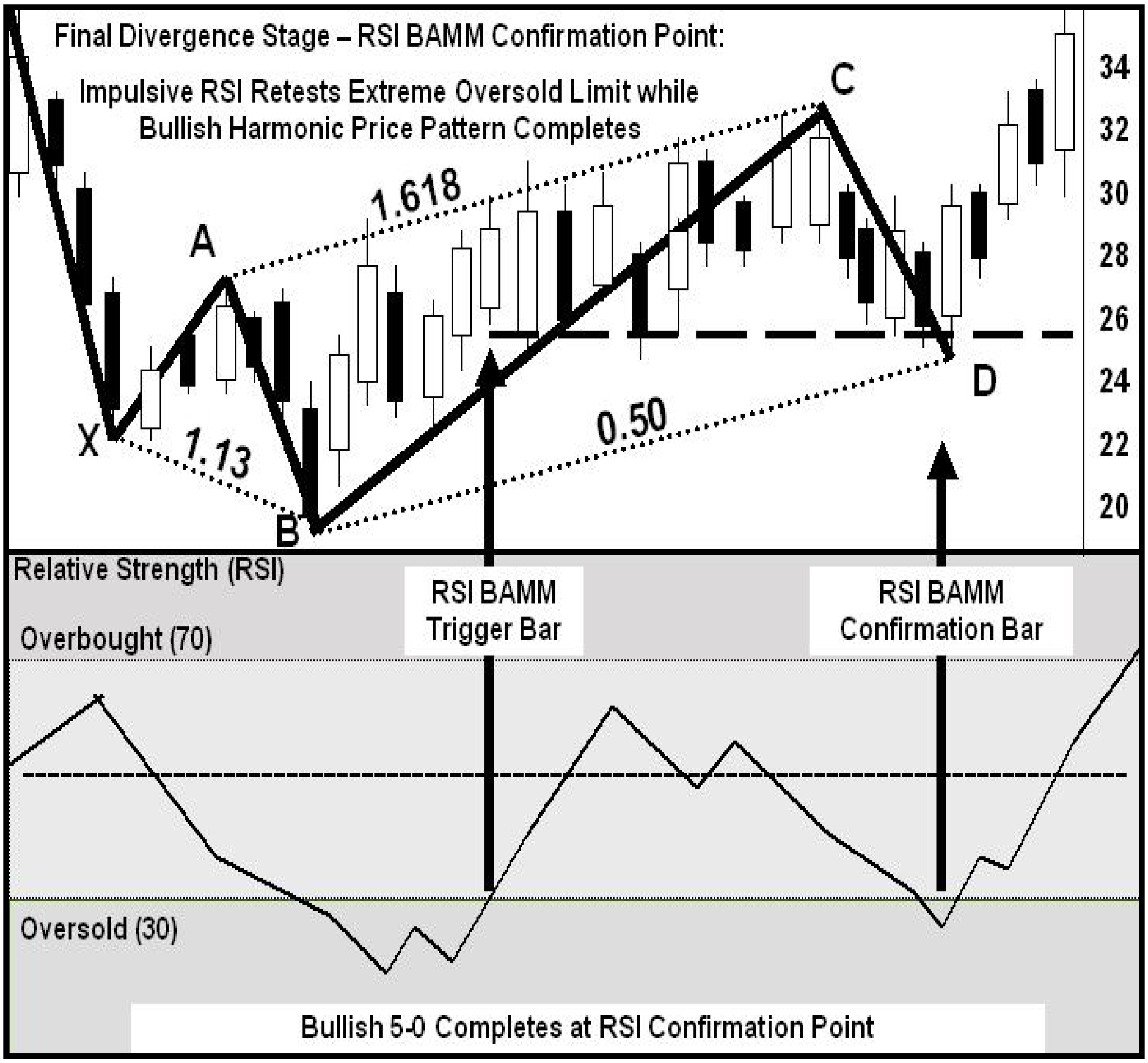
Pattern Completion Before 1.13-1.618 RSI BAMM Divergence Area: Bullish 5-0



RSI BAMM Violations and Stop Loss Considerations

is a combination of extreme price limit the RSI BAMM - typically beyond the 1618 - and the price limit of the pattern that corresponds with the setup. After defining the entire range of RSI BAMM and harmonic pattern completion points, the only consideration beyond the execution is the stop loss limit. Again, this will also include the price levels that by the larger harmonic patterns that are included in the trading setup from a pure RSI BAMM perspective the key validation only truly occurs beyond the 1618 extension of the final divergent move. Although it is important to differentiate between whether the RSI BAMM uses a 113 or a 1618 extension, the validation of the technical phenomenon becomes questionable beyond the 2.00 extension of the final move. As is the case for harmonic pattern failures, price action that violates these price levels especially on the first test should raise a red flag that the primary trend is quite strong. The area defined by the RSI BAMM is truly a do or die price level that is not leave much room for discretion.

Let's first look at the RSI BAMM on its own where we identify a situation label each step of the process and follow of the price action all the way through the reversal points.

This is an advantage because the structure itself can be distinguished while still allowing for enough time for the price action to set up correctly to validate the entire technique. Essentially, the RSI BAMM is a W-type structure in the bullish scenario that forms entirely below the 30 reading. This is a mandatory aspect of the RSI BAMM, where all points of the W. formation must take place below the 30 reading. Is important to remember that this is an early signal and the price action quite frequently will continue in the predominant trend will after the W-type structure has formed.

Bullish RSI BAMM without Impulse Confirmation Bar

It is important to note that the confirmation bar retest of the oversold 30-limit during the final step does not always occur in all RSI BAMM situations. But when it does, it represents the ideal complex RSI BAMM setup, including the last impulse test of the extreme oversold area.
Pattern completion most important

Reversal should truly get moving after impulse RSI test is complete

Move RSI limit to 40 for the minimum requirement of the confirmation point

Employ other studies to confirem the directional bias – is it changing or is it contiuing

Playing the Bullish Complex RSI Breakout up to the 50 limit

After the W. structure is formed in the RSI indicator and the price action balances rallying out of of the extreme area it is common for that initial move to be quite strong. In fact, a reflex balance after a long downtrend and prolonged selling trend will usually yield a one-sided rally where the buyers have all but disappeared and there's nothing but sellers. Although this can generate what many call and dead cat bounce, it is frequently short-lived. The teasing to note in this situation is a RSI reading that balances out of of the extreme -30 level and rally is to than 50 mark for higher sometimes even as high as a 70 reading before beginning the final divergent price move to complete the entire RSI BAMM. This is the best situation the goddess the corresponding move the to retest the prior W. structure in the RSI over home reading will have more momentum and greater significance to confirming the internal reversal at hand.

Know the zone

Compare RSI vs Price progress

RSI first, then price

To take an example woke through it step-by-step
remember this is just one technique that may seem complex but it's quite simple. The combination of the Fibonacci measurement and pattern formations are the primary basis for any trade. When patterns complete in the same area as other techniques confirm, the probability for a reversal and the increase significance of the price area for the overall trend can be discerned more readily, as the price action to frequently adheres to such complex opportunities to confirm my multiple methods.

v


NQ_M3 20-JUN-03_14:2...
5min
EMA13 1,210.70
EMA20 1,211.19
EMA50 1,211.70
SMA50 1,212.58
SMA200 1,206.78
Bollinger(20,2.0)
1,225.0
1,220.0
1,215.0
1,210.0
1,205.0
1,200.0
1,195.0
08
10
12
14
16
18
20
Settings
Vol(60) 39
HVR(100-6) 0.98
RSI(14) 33.39
Stoch(14-3) 25.0
MACD(12-26-9) -0.86 Hist: -0.16
ADX(14) 33.24 16.64 -53.05
CMF(21)
Overbought
Oversold
The Harmonic Analyzer (TM) : NQ_M3-5MIN
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Edit ... $INDU $INDU-15min $COMPQ $COMPQ-15min XLNX SPY-60min QQQ-15min ORBZ ES_Z4 NQ_Z4 $NDX BMY GE SIRI SUNW EP DYN $XOI EUR_A0-FX
CPB 05-NOV-04 Weekly EMA13 24.25 EMA20 25.05 EMA50 26.72 SMA50 27.31 SMA200 33.63 Bollinger(20,2.0)
26.00 25.00 24.00 23.00 22.00 21.00 20.00 19.00 18.00
A M J J A S O N D J F M A M J J A S O N D J F M A M J
2003
Settings Vol(10) 10,474,900 HVR(100-6) 1.39 RSI(14) 37.99 Stoch(5-3) 44.9 MACD(6-12-6) -1.02 Hist: 0.01 ADX(14) 33.36 11.53 -26.65 CMF(21) -0.002 Accum/Dis
Overbought
Oversold
The Harmonic Analyzer (TM) : CPB
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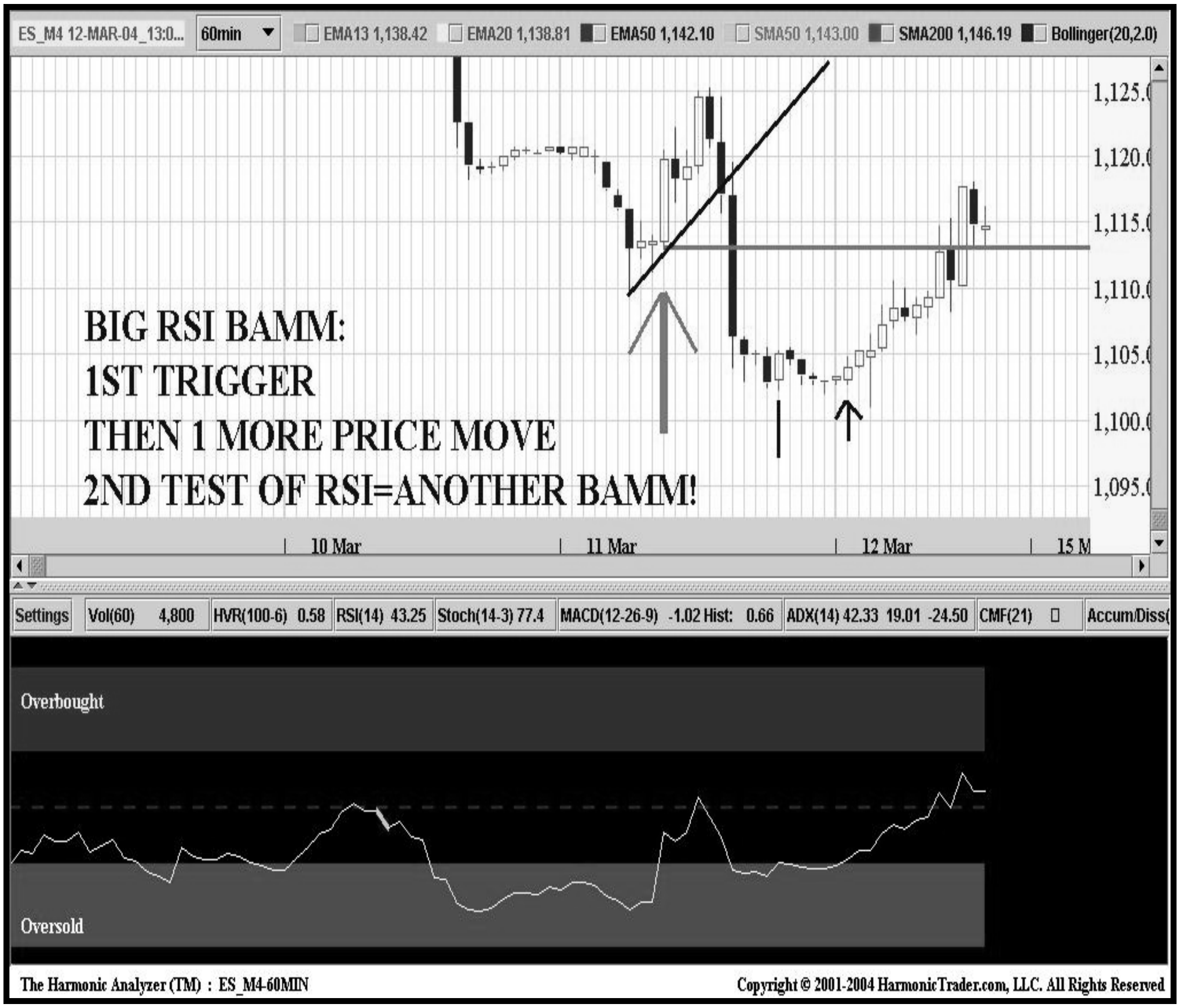
The Harmonic Analyzer (TM) : NQ_Z4-15MIN si bamm

SETTING UP TRIGGER BAR



Establish Deivergence

Execution Bar =

If trigger bar extreme high or low or next bar, then look for minimum 113-1618 divergence set up

If trigger bar 3-4 bars from extreme high or low, look for 886-113 divergence set up.

Ideally, the divergence set up should combine with RSI secondary test where index tests min 50 line then briewfly retests –30 (bull)/+70 (bear to form RSI Confirmation bar.

The Harmonic Analyzer (TM) : ES_Z3-60MIN


NQ_H4 05-MAR-04_11:0...
60min
EMA13 1,468.43
EMA20 1,470.44
EMA50 1,475.19
SMA50 1,479.81
SMA200 1,475.82
Bollinger(20,2.0)
3 Mar
4 Mar
5 Mar
Settings
Vol(60) 39,973
HVR(100-6) 1.26
RSI(14) 47.01
Stoch(14-3) 49.5
MACD(12-26-9) -3.78 Hist: -0.06
ADX(14) 32.23 16.74 -23.22
CMF(21) -0.006
Overbought
Oversold
The Harmonic Analyzer (TM) : NQ_H4-60MIN
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EUR_A0-FX 23-APR-04_12:00
60min
EMA13 1.19
EMA20 1.19
EMA50 1.19
SMA50 1.20
SMA200 1.20
Bollinger(20,2.0)
1.1950
1.1925
1.1900
1.1875
1.1850
1.1825
1.1800
1.1775
1.1750
21 Apr
22 Apr
23 Apr
24 Apr
Settings
Vol(60) 3,000
HVR(100-6) 0.75
RSI(14) 30.92
Stoch(14-3) 12.1
MACD(12-26-9) -0.00 Hist: -0.00
ADX(14) 41.73 8.67 -25.68
CMF(21) 0.076
Accum/Diss(
Overbought
Oversold
The Harmonic Analyzer (TM) : EUR_A0-FX-60MIN
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RSI BAMM WITH PATTERNS


ES_M4 12-MAR-04_13:0...
60min
EMA13 1,118.36
EMA20 1,120.69
EMA50 1,128.85
SMA50 1,130.61
SMA200 1,144.13
Bollinger(20,2.0)
BIG RSI BAMM:
1ST TRIGGER
THEN 1 MORE PRICE MOVE
2ND TEST OF RSI=ANOTHER BAMM!
10 Mar
11 Mar
12 Mar
15 Mar
Settings
Vol(60) 114,290
HVR(100-6) 1.59
RSI(14) 41.79
Stoch(14-3) 54.1
MACD(12-26-9) -4.58 Hist: 0.26
ADX(14) 62.13 21.19 -41.02
CMF(21) 0.631
Overbought
Oversold
The Harmonic Analyzer (TM) : ES_M4-60MIN
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ES_M4 12-MAR-04_13:0...
60min
EMA13 1,138.42
EMA20 1,138.81
EMA50 1,142.10
SMA50 1,143.00
SMA200 1,146.19
Bollinger(20,2.0)
BIG RSI BAMM:
1ST TRIGGER
THEN 1 MORE PRICE MOVE
2ND TEST OF RSI=ANOTHER BAMM!
10 Mar
11 Mar
12 Mar
Settings
Vol(60) 4,800
HVR(100-6) 0.58
RSI(14) 43.25
Stoch(14-3) 77.4
MACD(12-26-9) -1.02 Hist: 0.66
ADX(14) 42.33 19.01 -24.50
CMF(21)
Overbought
Oversold
The Harmonic Analyzer (TM) : ES_M4-60MIN
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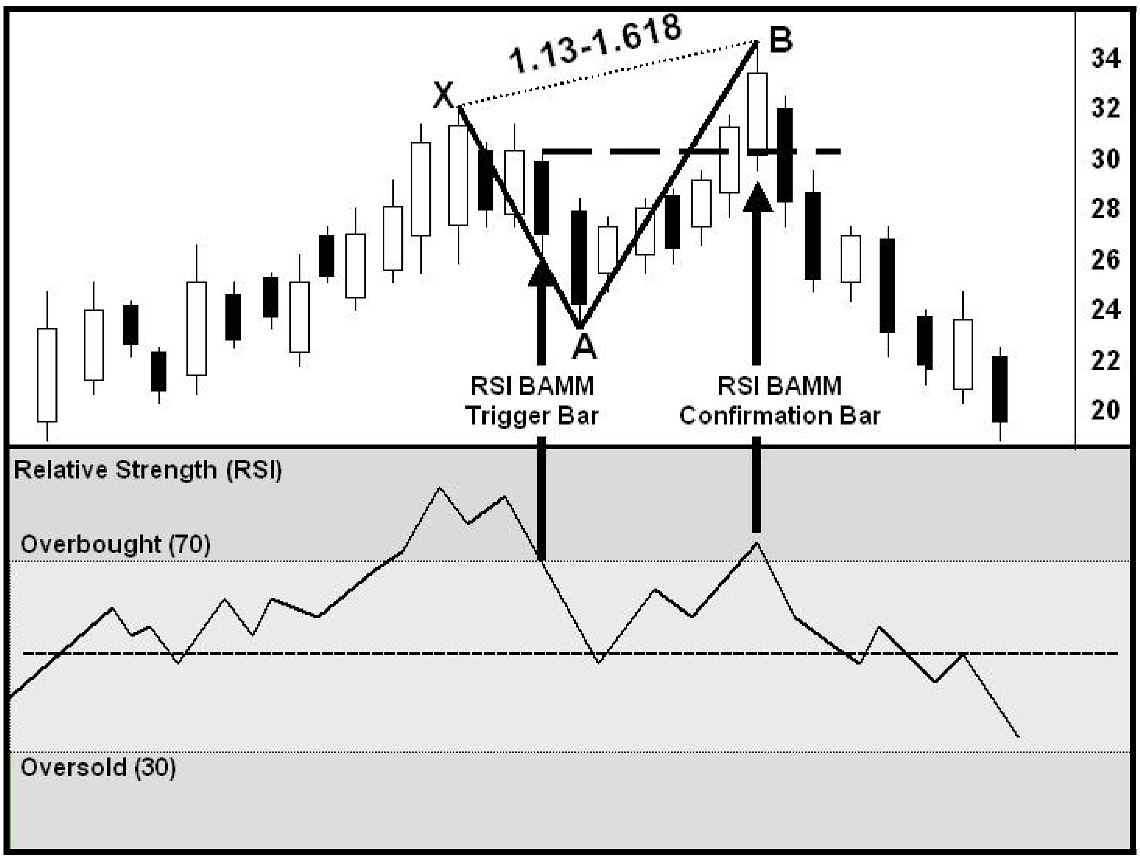
Bearish RSI BAMM

The Bearish RSI BAMM begins with a complex reading above 70. Referring to the RSI BAMM illustration below, the entire process requires several elements to validate this specific scenario. Although the entire illustration might seem a bit overwhelming upon first examination, this represents the ideal RSI BAMM model. I recommend that you thoroughly study this material before employing these strategies in your live trading.



Each step will be broken down to illustrate the ideal RSI BAMM model. Obviously, the ideal situation does not occur every time. It is important to remember that the real application of the RSI BAMM principles will require a degree of flexibility. The ideal model does present all of the critical elements that explain clearly the effectiveness of this strategy.

It will take a period of study to fully comprehend all aspects of the RSI BAMM approach. In much the same manner that the initial rules of harmonic pattern identification and differentiation may have seemed overwhelming, the RSI BAMM rules – albeit a bit complex upon first study – provide a coherent and comprehensive method for accurately measuring potential areas of divergence. It is essential to maintain the patience to execute only those trades that possess all required elements that validate a trade signal based upon the rules of the RSI BAMM set up. Again, it is important to remember that this illustration represents an *ideal model* and a technical framework to provide a set of guidelines that attempts to quantify precise technical events and to optimize overall trading decisions. However, the RSI BAMM strategy in combination with harmonic patterns effectively validates Potential Reversal Zones and improves the overall accuracy of the entire Harmonic Trading approach.

Step 1: Initial RSI Test of Extreme Bearish Limit

In the bearish RSI BAMM scenario, the first step is to identify price action that possesses a Relative Strength (RSI) reading in the extreme zone above 70. It is important to note that the 70-level for the overbought limit, as well as the 30-level to define the oversold area, were first outlined by Wells Wilder in his book, *New Concepts and Trading Systems*. In addition, a 14-period average is calculated from his approach.

Step 2: Complete a Bearish M-Type Complex RSI Structure

The initial focus should be on the formation of the indicator readings in the entire extreme range rather than looking for a specific numeric level. As I outlined earlier in this chapter for the bullish scenario, it is important to differentiate the two types of indicator structures that form at RSI extremes.

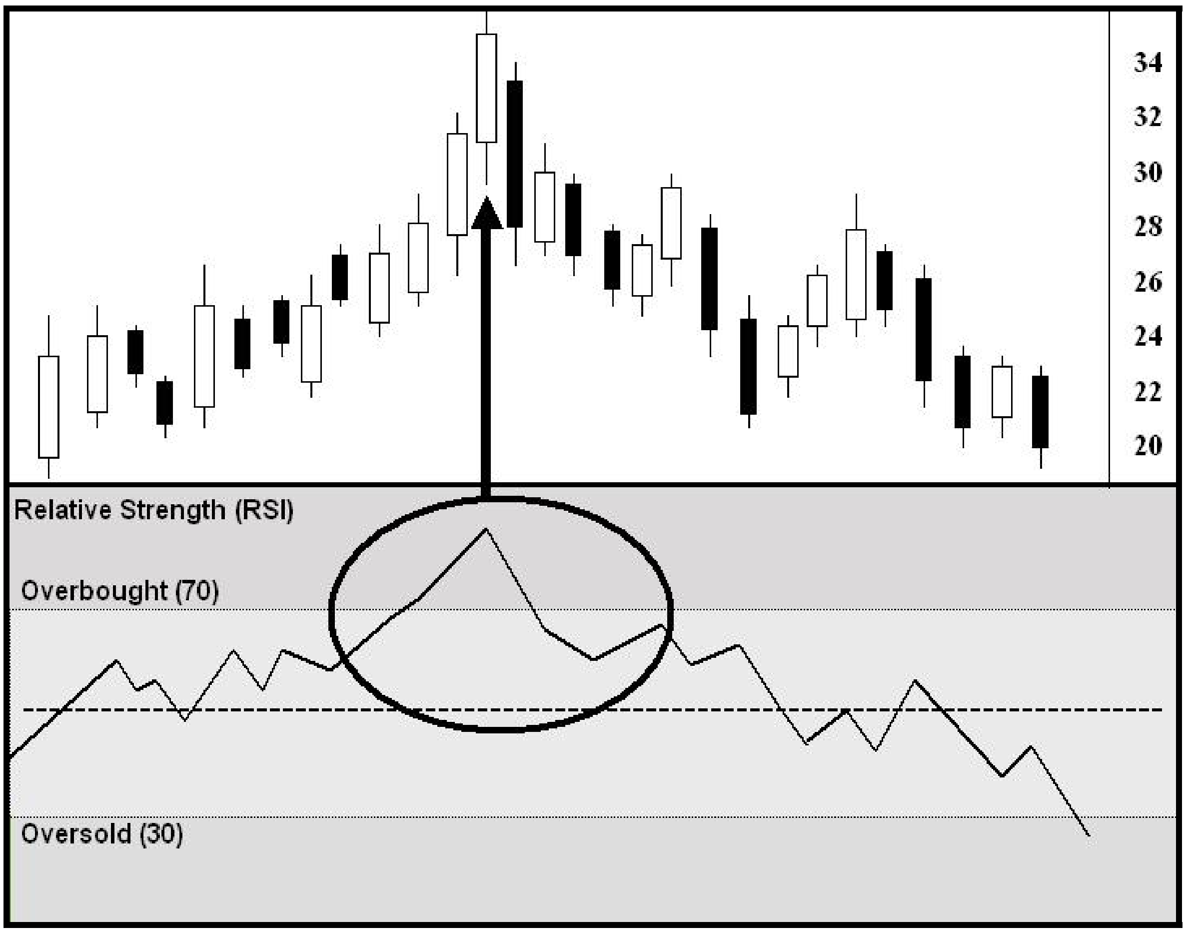
Two Types of Bearish Indicator Structures

In much the same vein as harmonic patterns, it is important to classify the general types of indicator structures that form in overbought RSI area. Although each type could be assigned more specific classifications, indicator readings form either an impulsive or a complex structure. Typically, most bearish RSI readings that are above 70 will be impulsive in nature and do not yield the required structure to be considered as a valid set up. However, valid complex structures that are correctly identified offer a tremendous technical advantage because this situation is especially unique and represents a vital potential reversal area within the overall trend of the price action.

Sometimes, a complex RSI BAMM formation can be frustrating because the setup may not ideally unfold following the initial trigger. This can be particularly frustrating when a potential set up is followed for quite some time and fails to adhere to the RSI BAMM model. In the same manner that not all patterns form ideally, it is important to wait for only those situations that clearly provide all the required elements to validate the set up. Regardless, the primary focus of the initial step is to identify a complex the RSI BAMM M-type structure in the extreme area.

Bearish Impulsive Indicator Structures

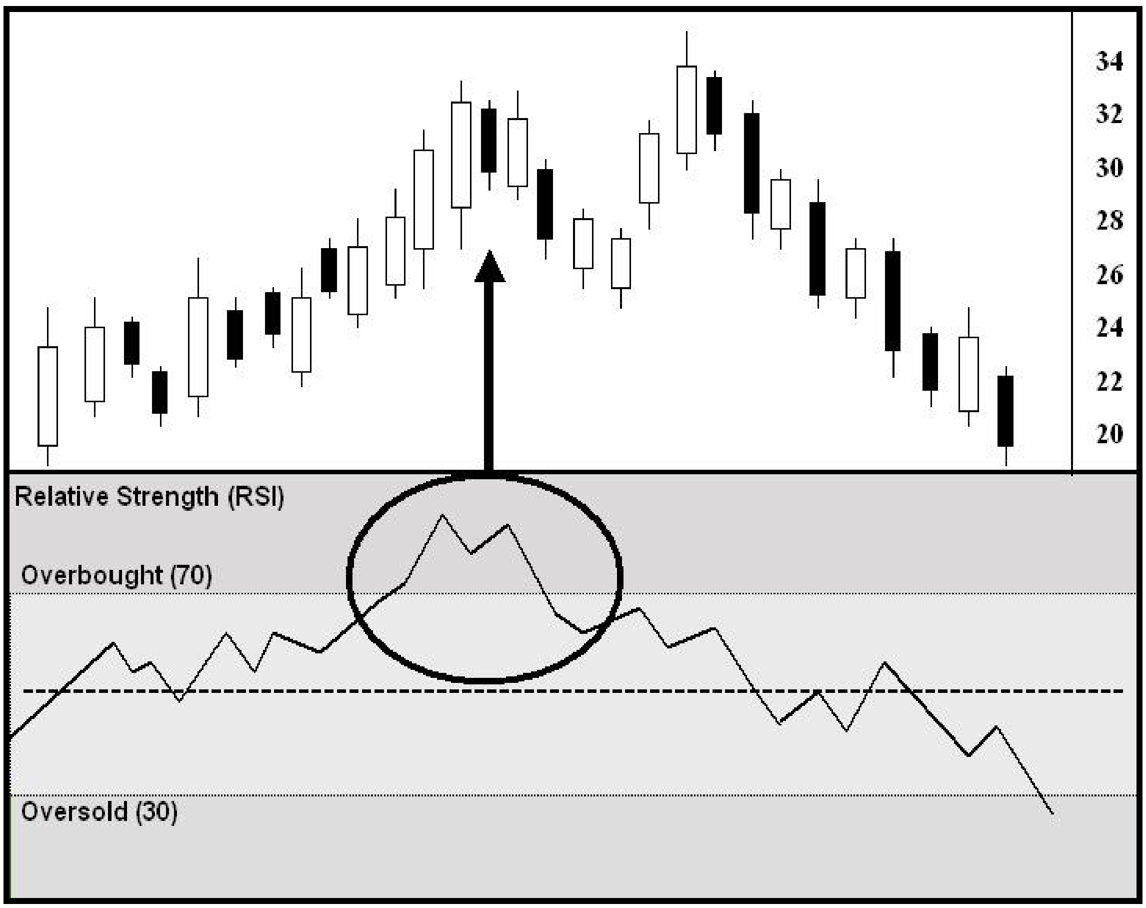
A bearish impulsive indicator structure reflects price action that is experiencing a quick test of the extreme overbought resistance area that typically reverses quickly without any consolidating price action. Since the price action commonly reverses sharply in these cases, the indicator reading rolls over and sinks below the extreme limit under 70 typically within 1 or 2 price bars of the first overbought reading.



Although such impulsive formations may test the extreme bearish RSI level, it is important to focus on the nature of the indicator structure and not necessarily the exact numeric reading (as long as it is above the 70-limit). The exact indicator level is critical in quantifying the extreme state of RSI but the general indicator formation is the critical factor, as it serves as the essential trigger to validate a potential trade opportunity.

Impulsive structures can be effective technical measures as they can serve to confirm bearish patterns and other trading signals. But, it is important to note that the signals generated from extreme RSI readings do not constitute a comprehensive approach to trading the market. In fact, I believe that this is a common misconception for Relative Strength and most other technical indicators and oscillators. In my opinion, such technical measures must be utilized as a complimentary methodology rather than as an exclusive approach. A Relative Strength reading above 70 does not automatically signify a trade opportunity. In fact, certain extreme impulse structures can signal significant continuations of the predominant trend. These strategies will be covered later in the book. For now, it is important to keep in mind that the general types of structures. Furthermore, as is the case with all technical indicators, other methods must be employed to validate any potential trade opportunity on a multiple confirmation basis.

Bearish Complex Indicator Structure



A complex structure represents an indicator formation that initially exceeds the 70-level and forms an M-type structure entirely in the extreme area. The complex structure remains above the extreme 70-limit longer than an impulsive formation and it should be distinct from other types of indicator readings. Despite representing a more significant technical condition than an impulsive formation, the bearish complex structure is typically an early trading signal. In fact, it is common for price action to accelerate to the upside while the complex formation of the RSI reading completes. Furthermore, the initial reaction to the complex RSI structure may not seem to indicate a change in trend due to such strong price action. Despite this perceived strength, the validity of the entire RSI BAMM technique is not determined until the M-type structures has entirely formed in the overbought area above 70. Although the advanced concepts will be clearly presented later in this chapter, it is important to keep in mind that a complex indicator reading is merely the starting point for the entire approach not the defining event of the methodology.

As the illustration shows, the initial test of the complex indicator formation typically experiences an acceleration of the predominant trend. Despite the perceived strength of the rally, the complex formation establishes the beginning of the most critical aspect of the entire RSI BAMM methodology – divergence.

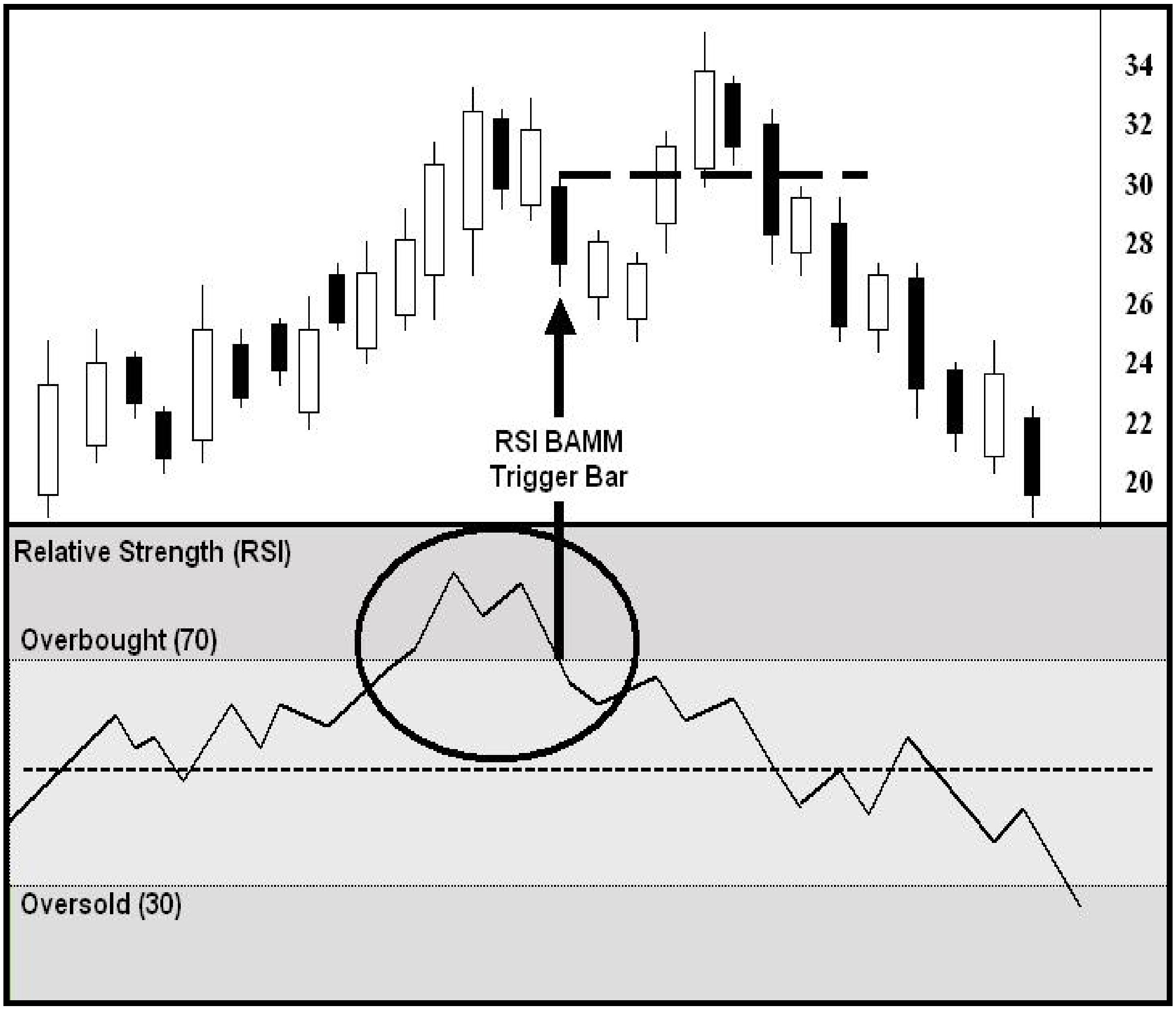
The bearish divergence occurs when the Relative Strength Indicator reading weakens while the price action continues to rally. Although the price action may seem to be maintaining its current uptrend, valid complex RSI structures usually trigger a reversal sooner rather later and mark a critical area for a potential change in the overall direction. Although a few other elements must fall into place for the RSI BAMM to be validated, the complex RSI structure is the starting point for entire process. Most important, this is an early signal and it is critical to wait for the M-type structure to break under the 70-line. After the RSI formation has been completed, the other considerations of potential pattern completions and specific RSI BAMM harmonic measurements can be projected to determine the optimal reversal area. This leads us to our next step, which is the defining and the measuring of the price level for that triggers this breakdown.

Step 3: Define the RSI Trigger Bar

After defining the complex RSI formation, the next step requires a measurement of the price area where the M-type indicator structure has completed. The price bar that causes the complex RSI indicator reading to complete and to decline below the extreme 70-limit is known as the ***RSI BAMM Trigger Bar***.

After identifying the RSI BAMM Trigger Bar, it is critical to mark the top of this price bar by drawing an extended line from the peak, projecting the resistance from the peak to the right of the chart, as is illustrated in the diagram. This RSI BAMM Trigger Bar resistance level serves as a minimum technical area for the corresponding retest and the anticipated execution area of the completion of the final phase of the RSI BAMM.

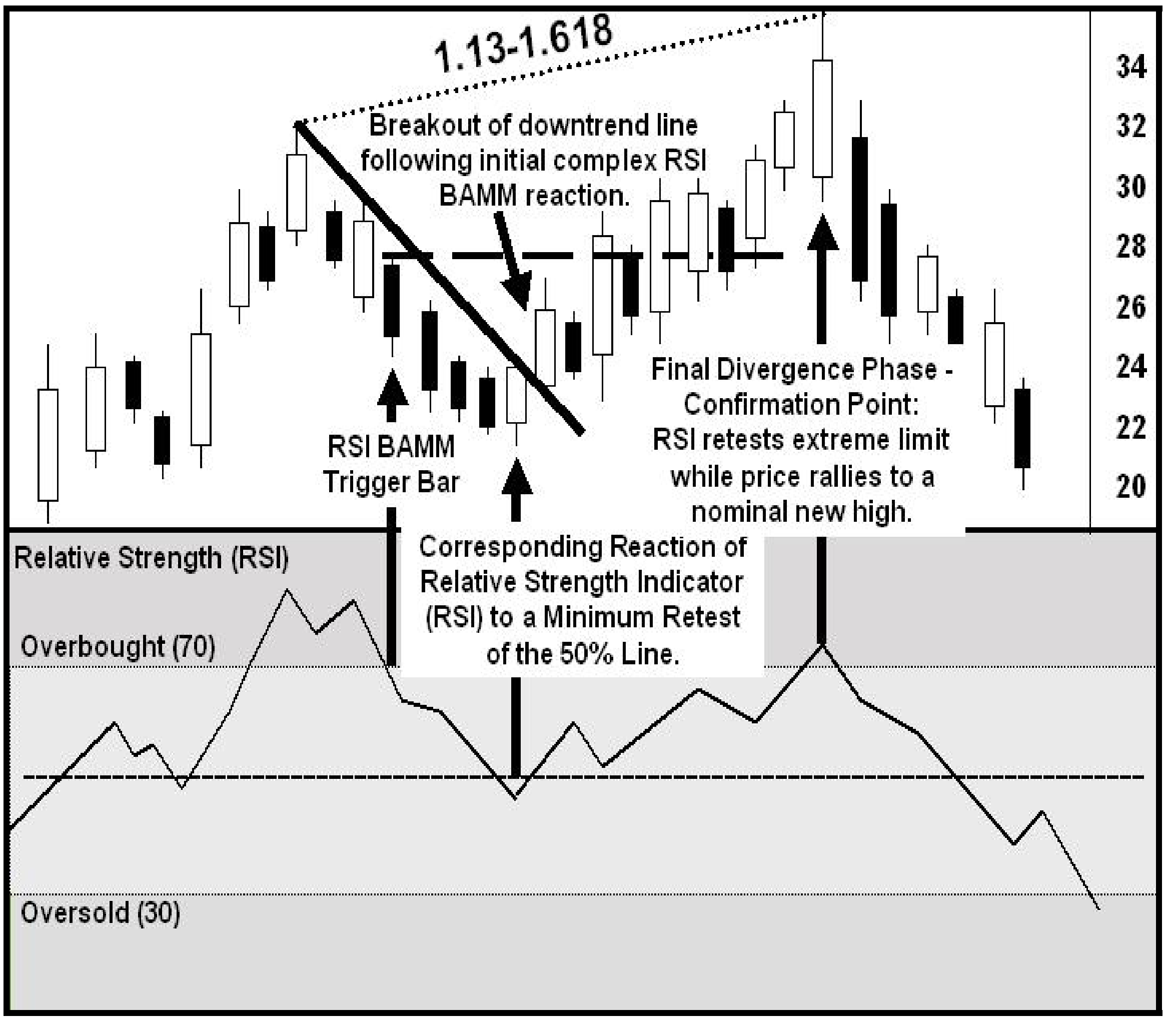
From a general perspective, the RSI BAMM Trigger Bar denotes the starting point for the critical divergence phase that the entire methodology is attempting to define and to quantify. Again, the completion of the complex RSI indicator structure is only the starting point of the process. Although there are strategies that I will present later in this chapter to capitalize on the initial indicator breakdown, from a broader perspective the RSI Trigger Bar can reveal a great deal about the validity of the set up and the state of the potential price action. For now, the most critical element of the RSI BAMM approach begins after the indicator has reversed from the overbought reading by completing the complex M-type structure.



The position of the Bearish RSI BAMM Trigger Bar in relation to the prior extreme high point is critical. Although its significance will be further explained later in this section, it is important to remember that the RSI BAMM Trigger Bar typically will be the price bar that is the prior peak of the current move or within a few intervals of the extreme high. This is critical and the Trigger Bar's position will determine the execution area for the corresponding retest and completion of the RSI BAMM.

Step 5: Reaction of RSI and Price

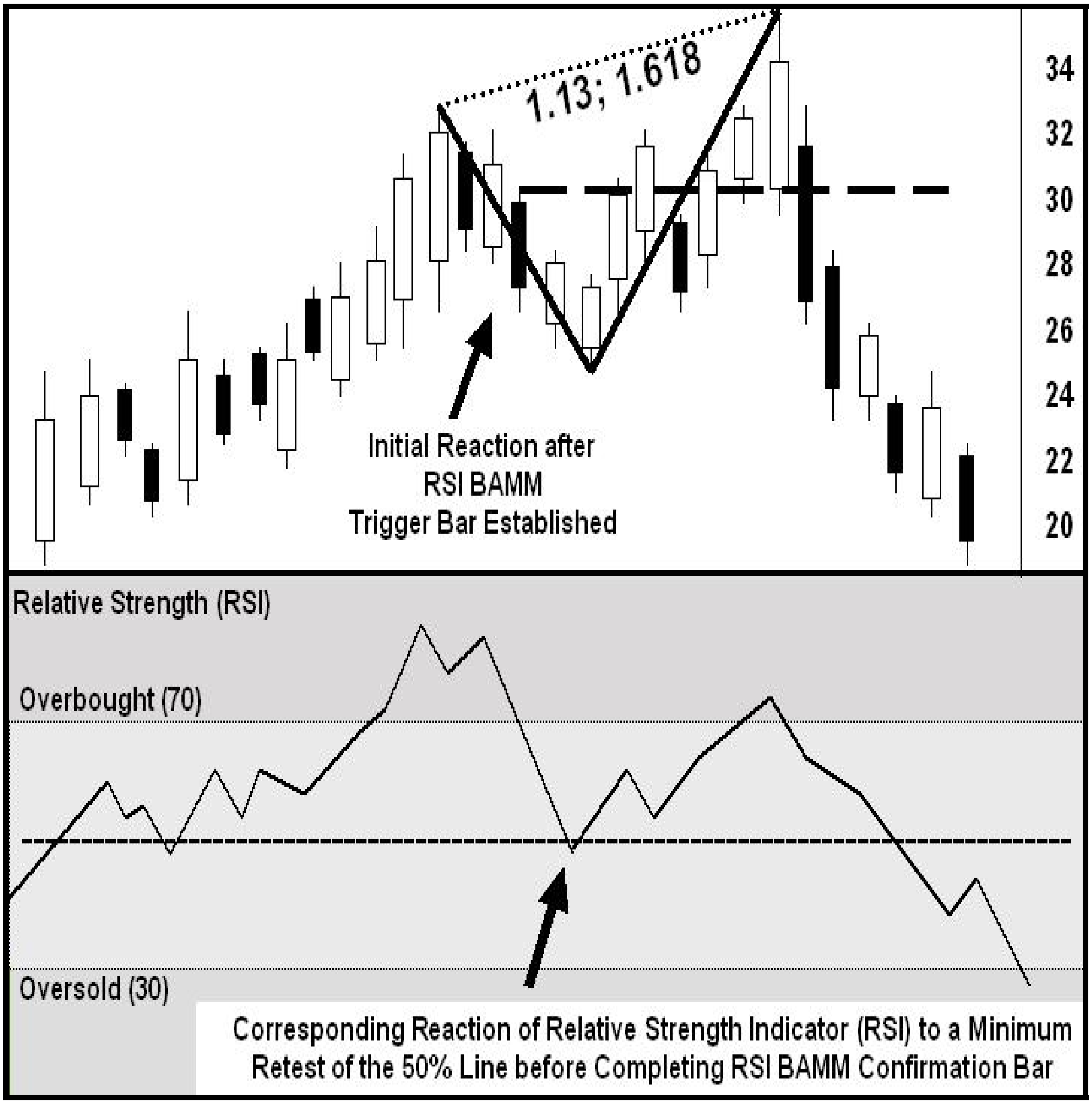
The initial breakdown of the RSI and price following the completion of the complex indicator formation represents the first phase of the approach. In an ideal RSI BAMM scenario, the price and indicator decline in tandem.



Frequently, the initial breakdown offers a distinct trading opportunity but these strategies will be covered a bit later in this chapter. For now, the initial breakdown requires a few elements to set up the completion of the RSI BAMM.

Specific Type of Retest

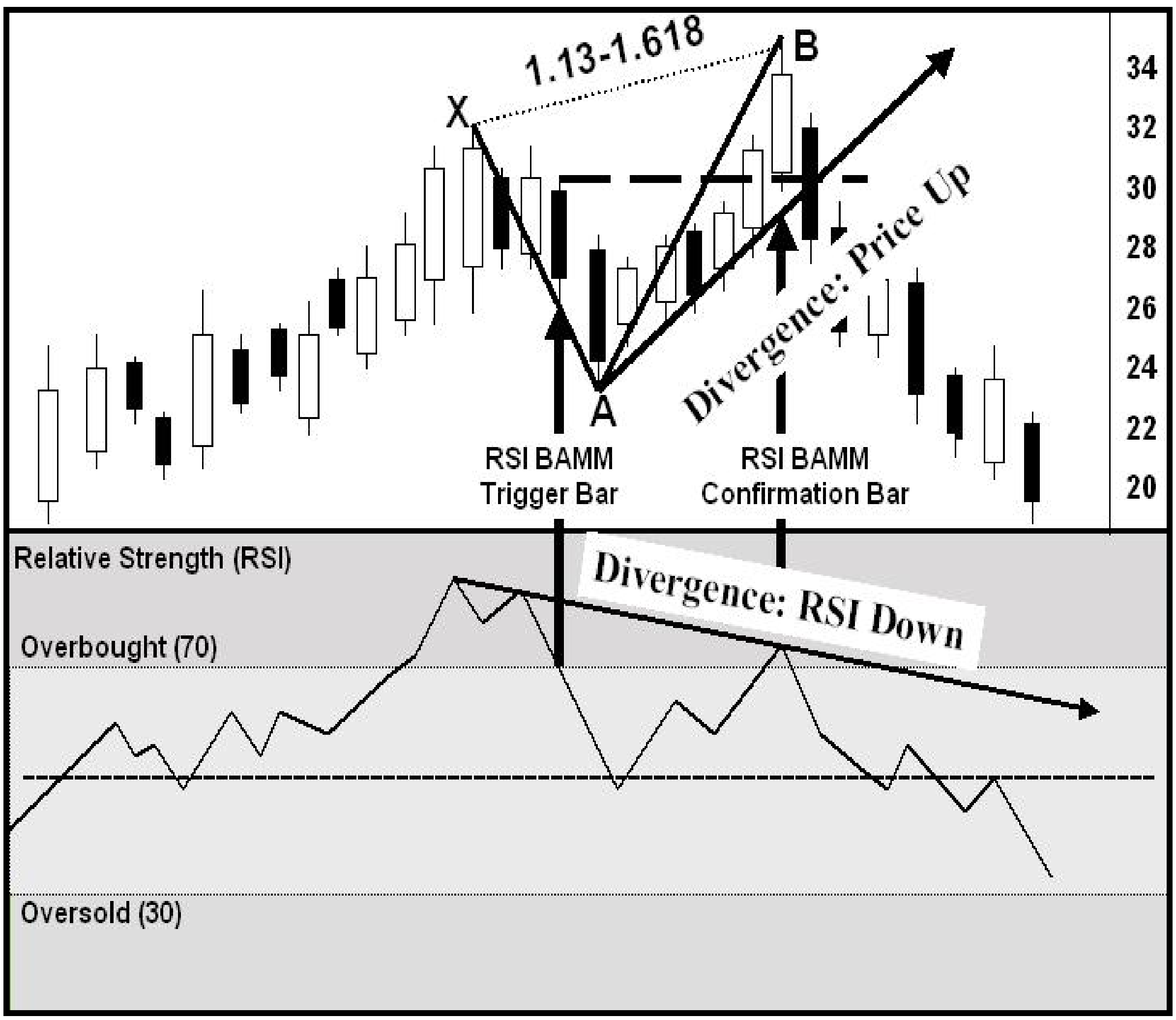
There are a few technical events that must occur on this initial Trigger Bar reaction. Namely, the RSI reading MUST decline to at least the 50-level as the price nominally reacts. Although there is room for interpretation as the RSI reading may exceed the 50-level on this initial reaction, it serves as a minimum requirement that precedes the corresponding retest of the resistance area established by the RSI BAMM.



Again, this specific type of retest offers other short-term trading opportunities that I will explain a bit later in this chapter. But, the important aspect of this element of the process establishes the final divergence phase of the entire approach.

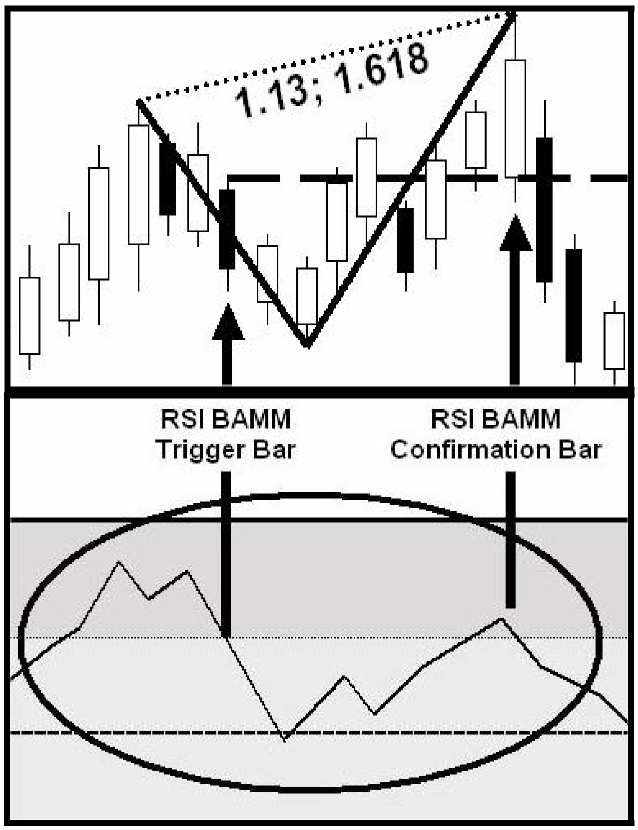
Step 5: The Final Phase - Divergence of RSI vs. Price

The final divergence stage begins after the RSI reading pulls back to at least the 50-line and the short-term price breaks out from the downtrend line of the initial reaction. It is important to remember that the horizontal line drawn from the peak of the RSI Trigger Bar to the right of the chart defines the minimum resistance level for the completion of the RSI BAMM and the eventual entry of the trade. This is a situation where the Relative Strength Indicator reading is providing an early signal to the end the predominant trend. Although this signal may be the end of the trend technically, the price action typically experiences one last rally to retest the resistance area established by the complex RSI structure.



This final stage of the retest reveals a great deal about the strength of the predominant trend and the validity of the signals generated by the complex RSI structure. In essence, the price action diverges in a “last gasp” from the indicator reading. The price action will nominally exceed the prior high of the area marked by the complex RSI structure. This final stage of the entire setup reveals the extent of divergence, where the internal reading of the trend indicates a reversal hand while the price continues to rally.

The critical point of the divergence can be seen in this snapshot of the illustration where the trend of the price action continues up (notice uptrend arrow) while the trend of the RSI reading fails to continue higher, typically completing an impulsive structure.

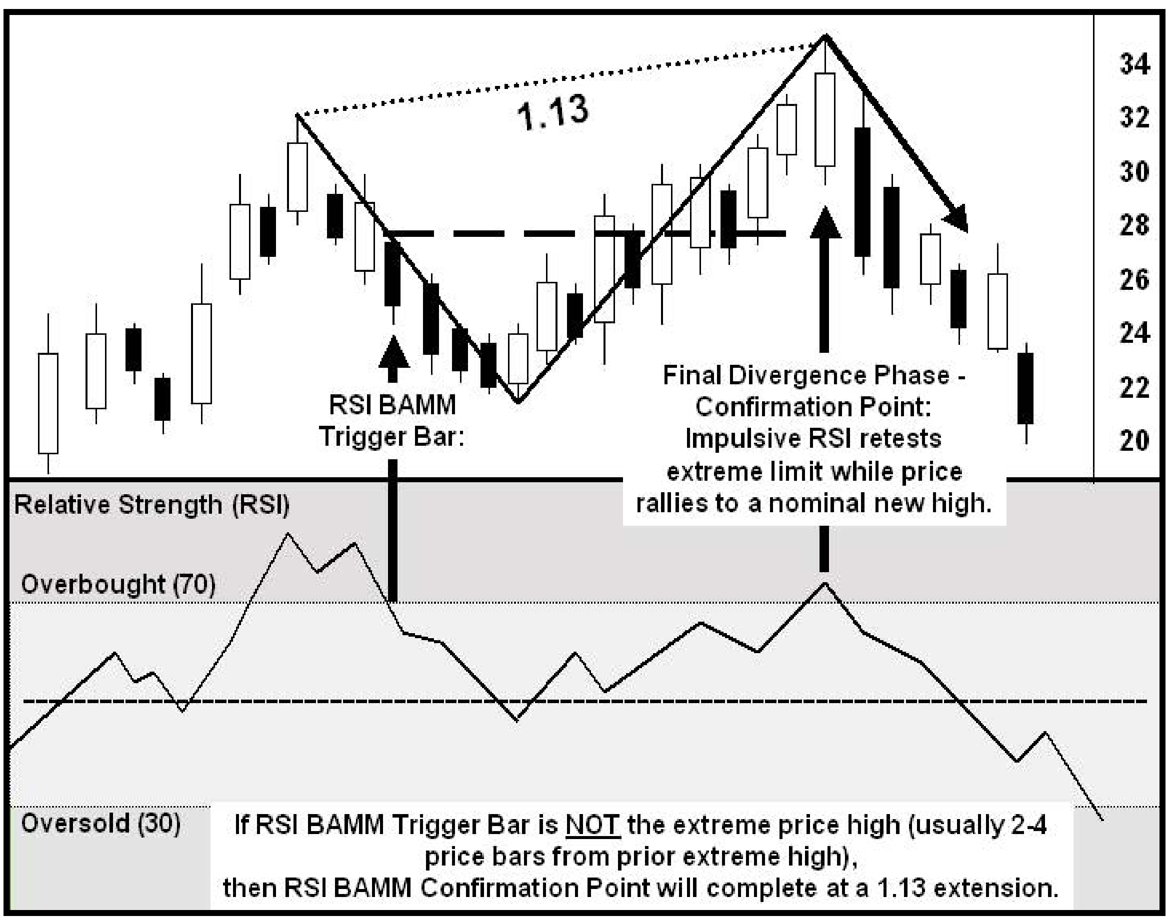


If the RSI structure is a valid resistance signal indicating a reversal at hand, typically the price action will reverse quickly after exceeding the initial prior high level. Although I will outline the advantages of utilizing Harmonic Trading techniques of pattern recognition and Fibonacci measurement strategies with the RSI BAMM, it is important to examine this technical phenomenon on its own before trying to understand other complementary methods. Most important, this area of divergence where the price and the relative strength readings move in opposite directions serves to quantify the critical reversal levels.

Establishing the RSI BAMM Confirmation Point: 1.13 vs. 1.618

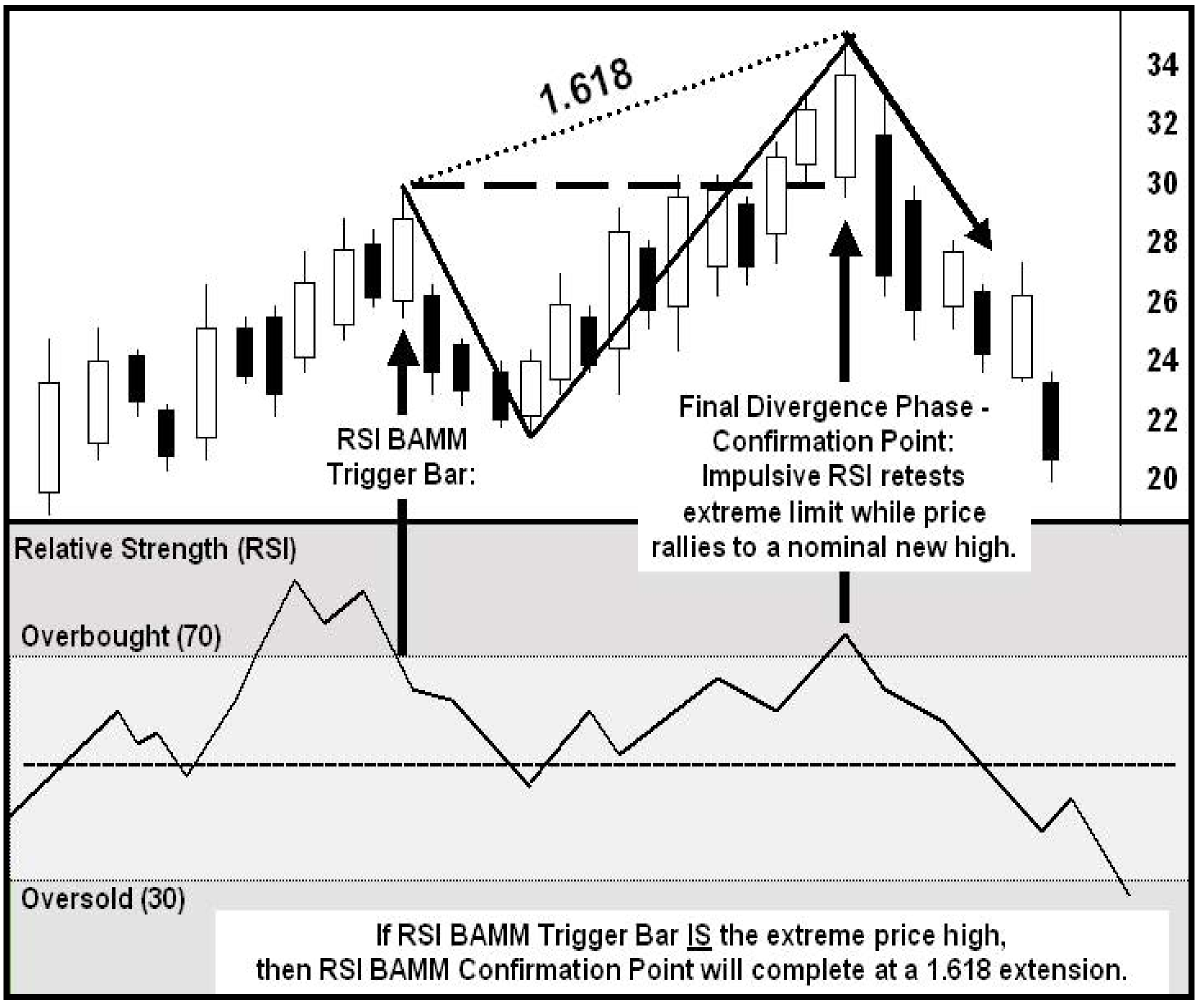
In the development of the RSI BAMM, I was challenged for quite some time to discern the correct extension to employ for the confirmation point. Although the difference between 1.13 and 1.618 may appear small, in real trading situations this gap frequently can be quite expensive. With respect to the primary tenets of Harmonic Trading and pattern identification, exact specification of technical measurement techniques is required to yield the most accurate information regarding the validity of any trading opportunity. Although these are general rules, I noticed a difference in the ultimate extension of the final divergence phase of the RSI BAMM depending upon the position of the Trigger Bar relative to the prior high. If the RSI BAMM Trigger Bar is a few price bars (typically 2-4) from the prior high, the execution of the trade will occur at the corresponding 1.13 extension. However, a RSI BAMM Trigger Bar develops at the extreme high for the move will result in a 1.618 extension at the confirmation point.

1.13 Extension @ RSI BAMM Confirmation Point



Although the general rule regarding the confirmation point extension differentiates the 1.13 and 1.618 ratios, the focus of the Trigger Bar should be on the extreme prior peak. Essentially, if the RSI BAMM Trigger bar is NOT the high price bar, the 1.13 extension is utilized to quantify the execution area for the trade.

1.618 Extension @ RSI BAMM Confirmation Point

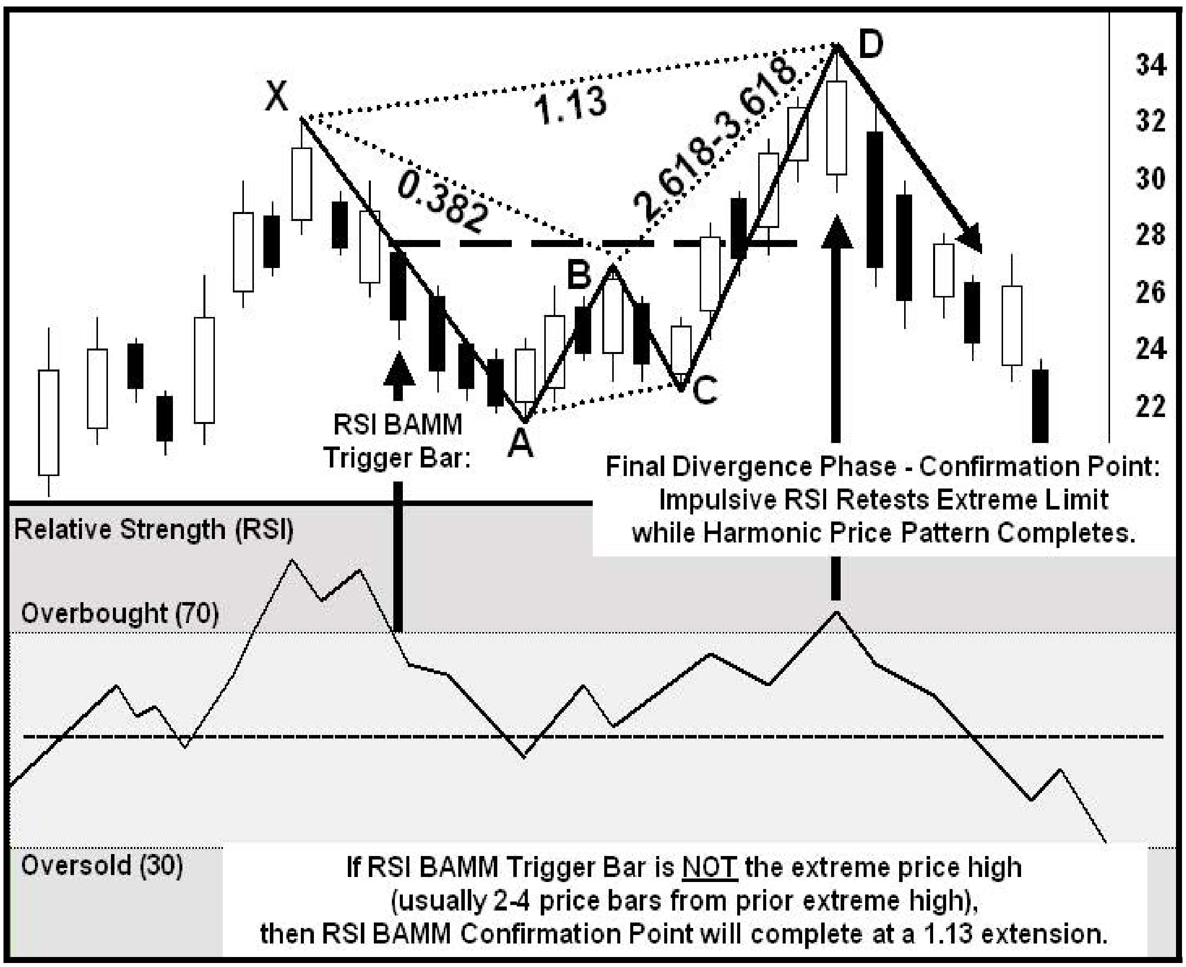


In either situation**,** the general rule for the confirmation point extension must focus of the location of the Trigger Bar as it relates to the extreme prior peak. If the RSI BAMM Trigger bar IS the high price bar, the 1.618 extension is utilized to quantify the execution area for the trade.

Step 7: Pattern Completion at the RSI BAMM Confirmation Point

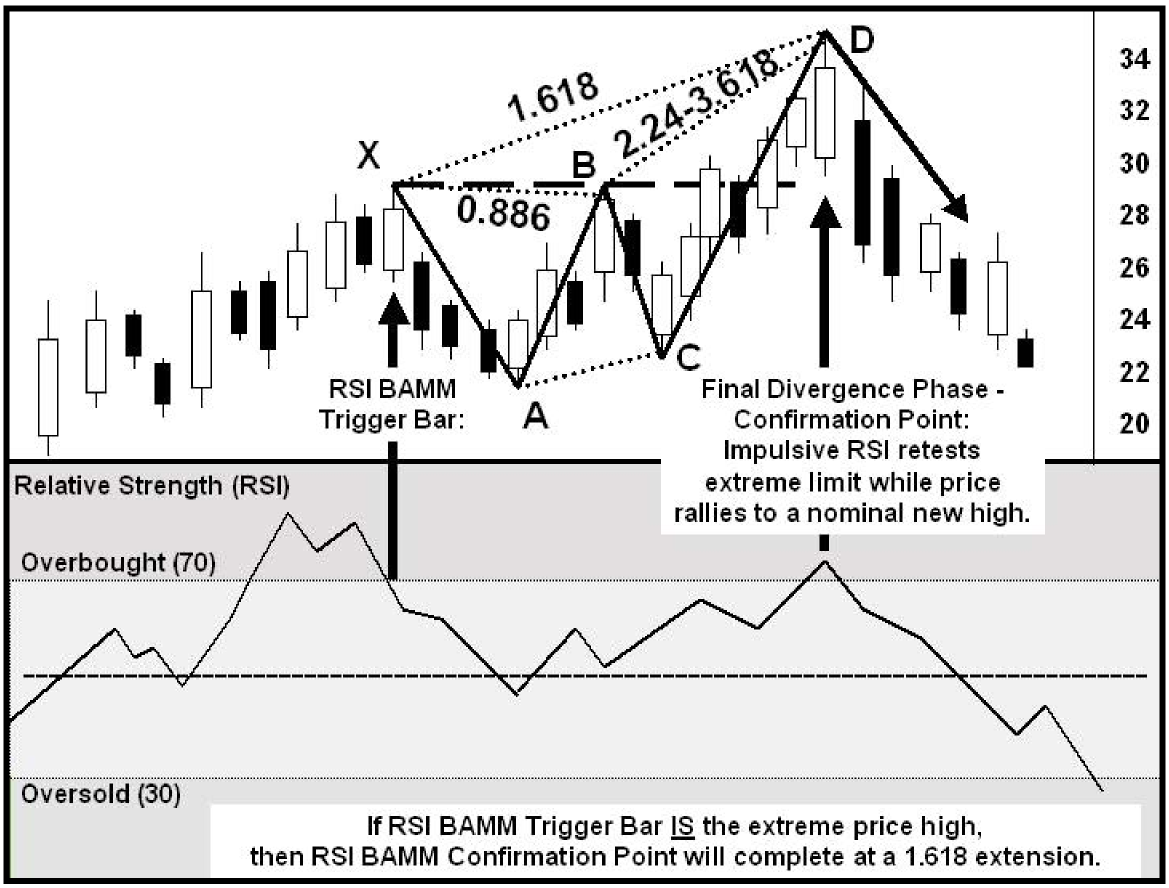
After establishing the necessary steps to define the final divergence phase of the RSI BAMM, the integration of harmonic patterns at the confirmation point represents the ultimate advancement of the entire Harmonic Trading methodology. Although the RSI BAMM confirmation point is generally differentiated by location of the Trigger Bar as it relate to the prior high, the price area of execution the trade is defined by the completion of a distinct harmonic pattern in its Potential Reversal Zone (PRZ). The following illustrations show the entire RSI BAMM methodology with various harmonic patterns at the confirmation point.

Intermediate RSI BAMM Trigger Bar Signals 1.13 Extension



Although the position of the RSI BAMM Trigger Bar in relation to the prior high defines the execution area of the completion of the RSI BAMM, the formation of distinct harmonic patterns during this final divergence stage is the penultimate confirmation signal for the execution of the trade. The pattern's Potential Reversal Zone (PRZ) combined with the RSI BAMM extension provides significantly more accurate technical evidence of a probable reversal at hand. In the case of the 1.13 extension, the Alternate Bat is typically the most likely harmonic pattern to complete in this situation. Although other retracement patterns like the Gartley or the Bat may form in conjunction with a 1.13, the position of the RSI BAMM Trigger Bar will typically be 5 or more price bars from the prior high, as I will show a bit later in this chapter.

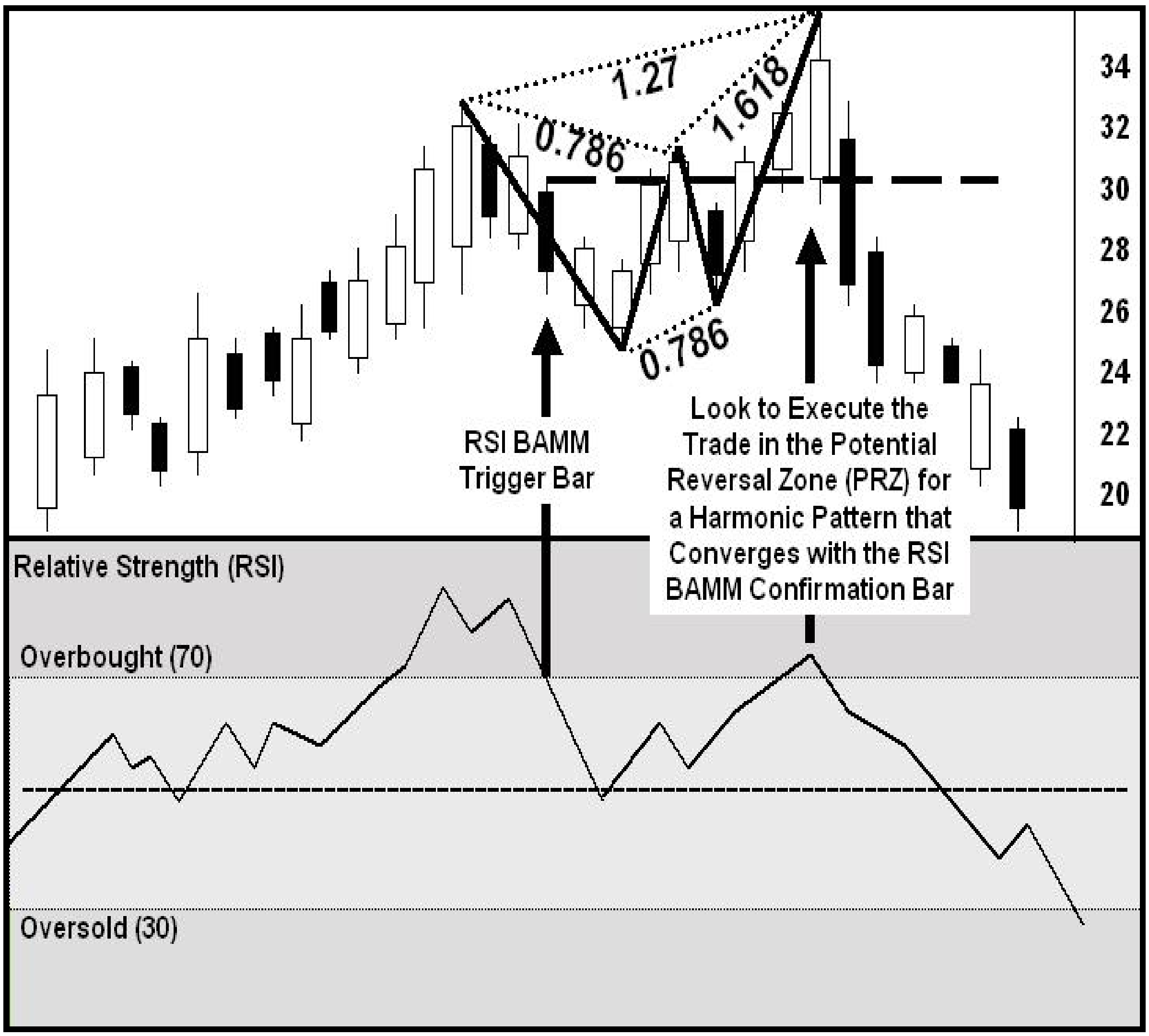
Extreme RSI BAMM Trigger Bar Signals a 1.618 Extension



Similar to the 1.13 RSI BAMM extension, the 1.618 limit is defined by the position of the Trigger Bar. In this case, a Trigger Bar that is the extreme prior high will result in a corresponding pattern that utilizes a 1.618 projection. Within the Harmonic Trading arsenal of patterns, this will usually manifest Crab or Deep Crab patterns.

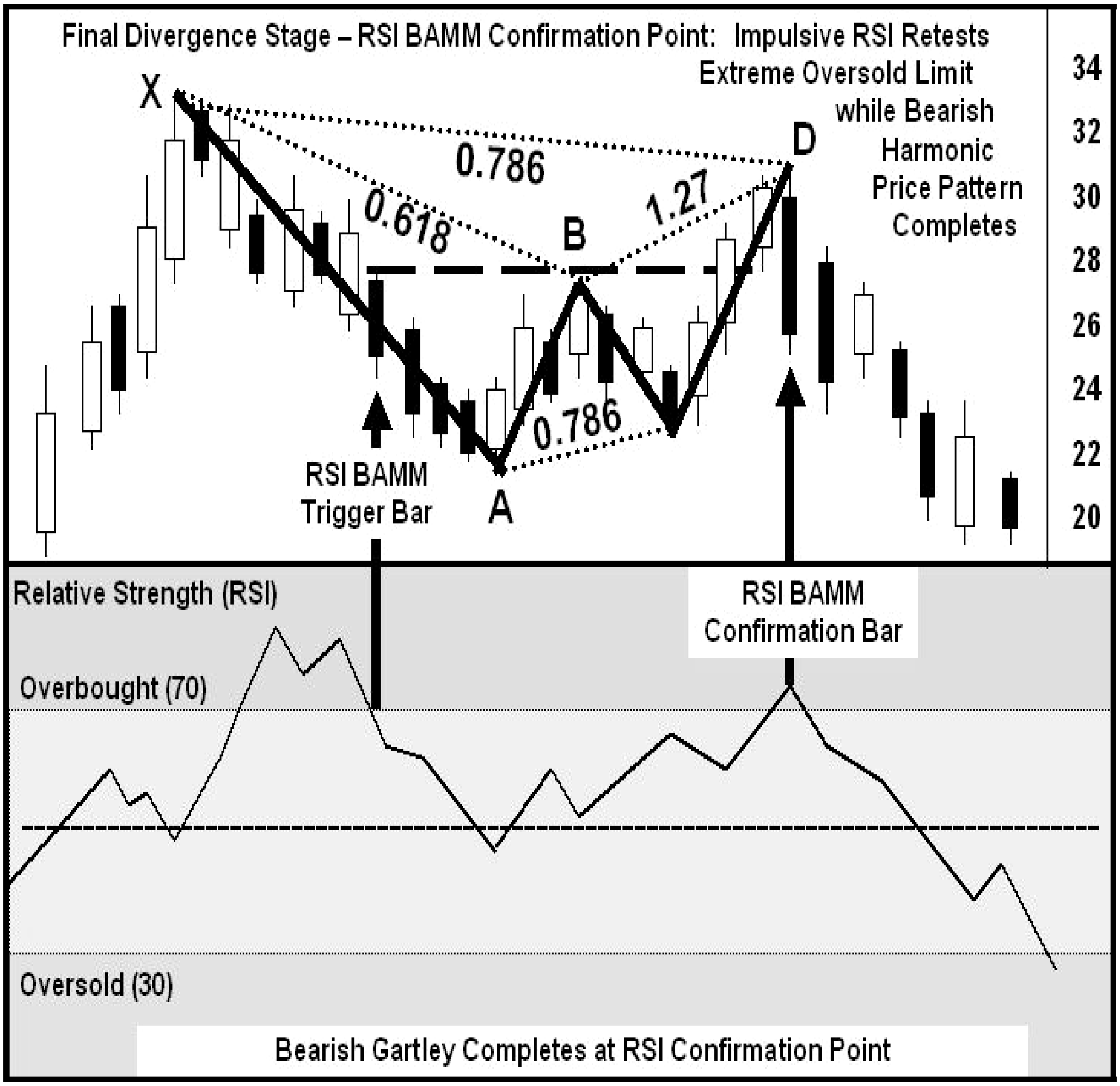
Pattern Completion in 1.13-1.618 RSI BAMM Area

Sometimes the RSI BAMM extensions (1.13/1.618) create a zone, where a pattern like a Bearish Butterfly completes – typically at the 1.27 XA projection – in the middle of the range. Although this may create some confusion, it is important to remember that the pattern completion point represents the most critical price level in this area.



This underscores the importance of the Potential Reversal Zone (PRZ) within the RSI BAMM limits (1.13-1.618) as the most critical price area for the ultimate execution of the trade.

Pattern Completion Before RSI BAMM Confirmation Area: Bullish Gartley



Cephalon (CEPH)

Wait for RSI +70
LOOK for M-type structure

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CEPH 29-JUN-06 Daily EMA13 70.50 EMA20 68.79 EMA50 61.80 SMA50 59.65 SMA200 47.12 Bollinger(20,2.0)
zz 9.0E-4 zz 0.0145 zz 0.11 zz 1.0 zz 10.0
1.618 @ $82.873 (+16.423 +24.71%)
90.00
85.00
80.00
75.00
70.00
65.00
60.00
55.00
27 3 9 17 23 30 6 13 21 27 6 13 20 27 3 10 17
2006 Feb Mar
Settings Vol(60) 7,019,115 HVR(100-6) 1.45 RSI(14) 49.74 Stoch(14-3) 49.1 MACD(12-26-9) 3.50 Hist: -0.84 ADX(14) 59.85 29.75 -20.54 CMF(21) 0.139
Overbought
Oversold
The Harmonic Analyzer (TM) : CEPH
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CEPH 29-JUN-06
Daily
EMA13 73.82
EMA20 72.99
EMA50 68.12
SMA50 68.64
SMA200 49.90
Bollinger(20,2.0)
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zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618 @ $82.873 (+16.423 +24.71%)
1.618XA @ $82.873
2.000BC @ $82.830
1.270AB
0.886XA
0.618AB
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B
C
D
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80.00
77.50
75.00
72.50
70.00
67.50
65.00
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27
3
10
Feb
Mar
Settings
Vol(60) 2,074,275
HVR(100-6) 0.60
RSI(14) 63.28
Stoch(14-3) 80.4
MACD(12-26-9) 1.78 Hist: -0.01
ADX(14) 25.59 28.23 -13.84
CMF(21) 0.234
Accum/Diss
Overbought
Oversold
The Harmonic Analyzer (TM) : CEPH
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CEPH 29-JUN-06
Daily
EMA13 52.66
EMA20 51.60
EMA50 48.79
SMA50 47.92
SMA200 44.48
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618 @ $82.873 (+16.423 +24.71%)
1.618XA @ $82.873
2.000BC @ $82.830
1.270AB=CD
1.618XA @ $82.873
2.000BC @ $82.830
0.886XA
0.618AB
X
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80.00
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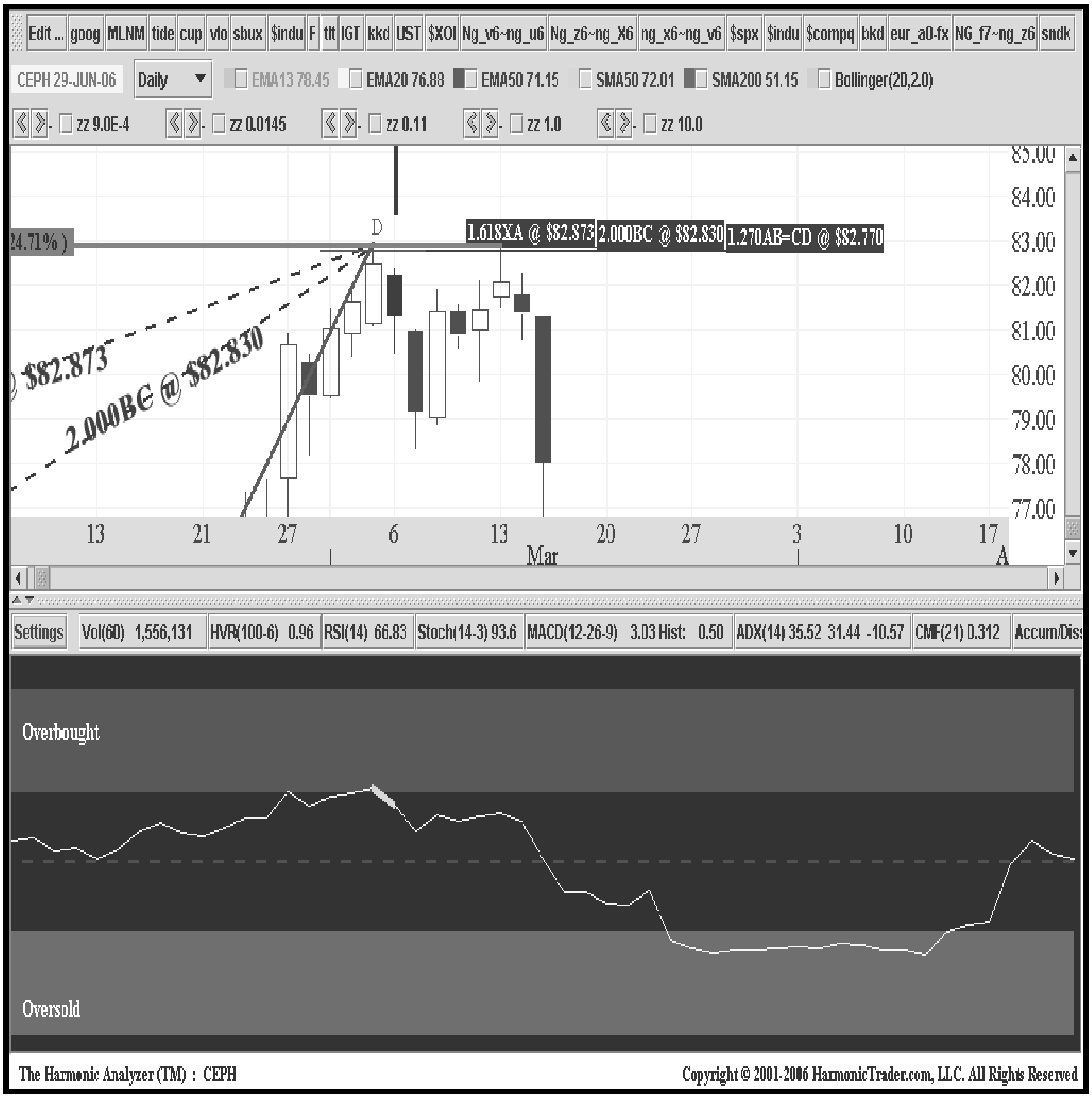

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CEPH 29-JUN-06
Daily
EMA13 78.45
EMA20 76.88
EMA50 71.15
SMA50 72.01
SMA200 51.15
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
D
1.618XA @ $82.873
2.000BC @ $82.830
1.270AB=CD @ $82.770
$82.873
2.000BC @ $82.830
Settings
Vol(60) 1,556,131
HVR(100-6) 0.96
RSI(14) 66.83
Stoch(14-3) 93.6
MACD(12-26-9) 3.03 Hist: 0.50
ADX(14) 35.52 31.44 -10.57
CMF(21) 0.312
Overbought
Oversold
The Harmonic Analyzer (TM) : CEPH
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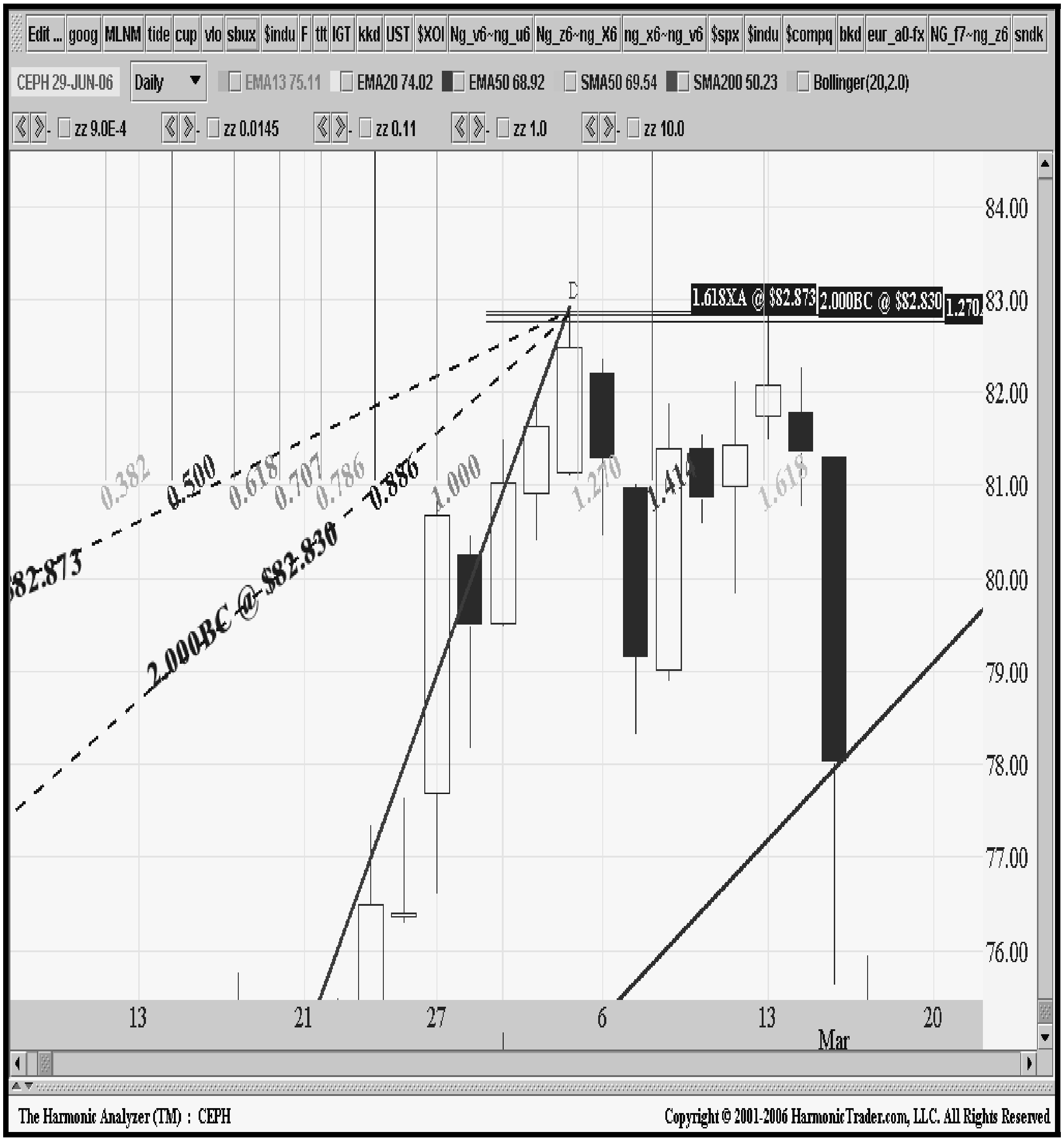
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CEPH 29-JUN-06
Daily
EMA13 75.11
EMA20 74.02
EMA50 68.92
SMA50 69.54
SMA200 50.23
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618XA @ $82.873
2.000BC @ $82.830
D
0.382
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0.618
0.707
0.786
0.886
1.000
1.270
1.414
1.618
$82.873
2.000BC @ $82.830
84.00
83.00
82.00
81.00
80.00
79.00
78.00
77.00
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The Harmonic Analyzer (TM) : CEPH
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CEPH 29-JUN-06
Daily
EMA13 46.82
EMA20 47.12
EMA50 47.96
SMA50 48.61
SMA200 48.31
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618XA @ $82.873
2.000BC @ $82.830
1.270AB=
0.886XA
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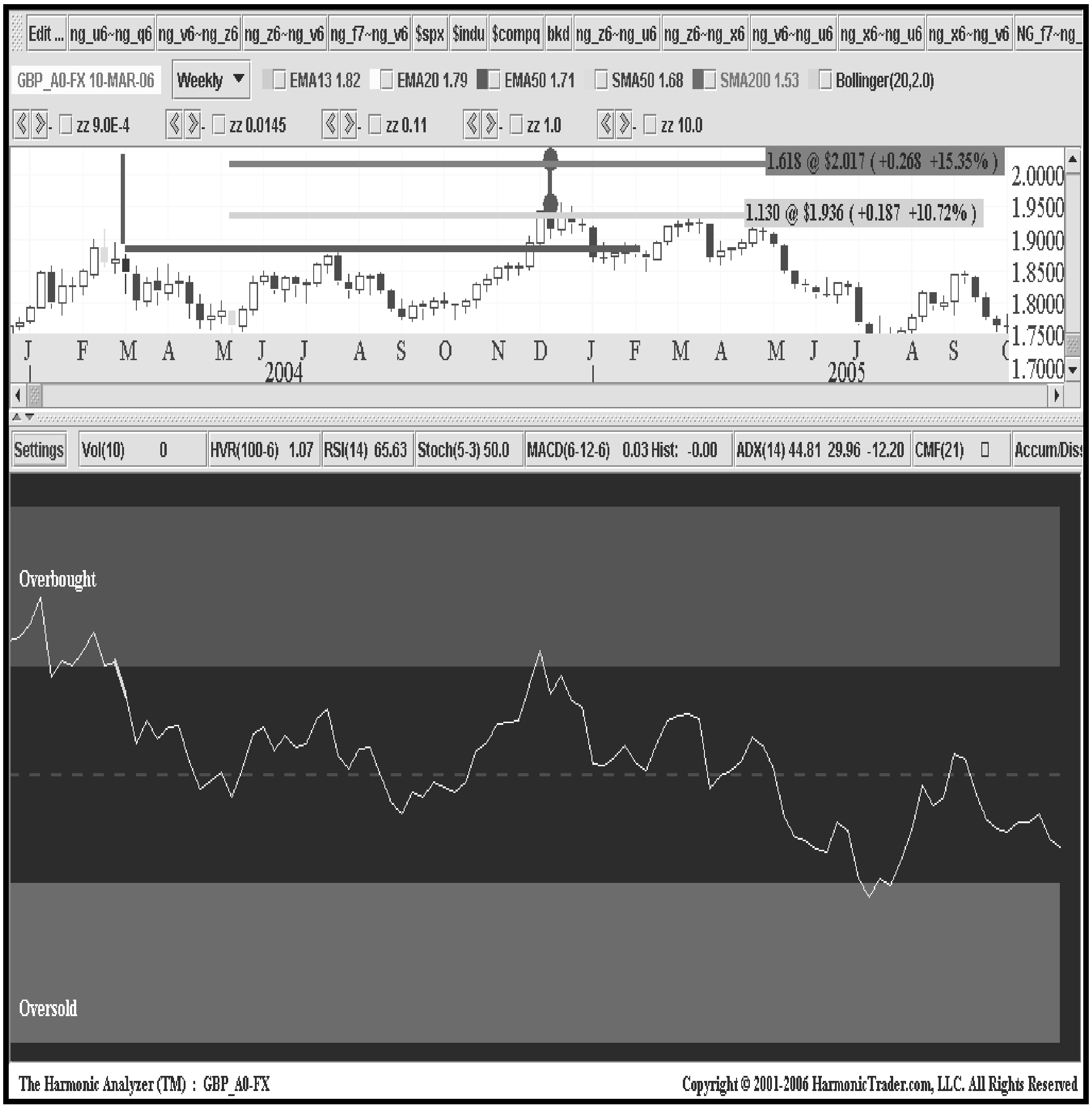
British Pound (GBP_A0-FX)

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GBP_A0-FX 10-MAR-06
Weekly
EMA13 1.81
EMA20 1.81
EMA50 1.78
SMA50 1.80
SMA200 1.59
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618 @ $2.017 (+0.268 +15.35%)
ipButterfly
i1.270AB=CD @ $1.935
1.27XA @ $1.959
1.618BC @ $1.943
1.130 @ $1.936 (+0.187 +10.72%)
1.27XA @ $1.959
0.786XA
1.618BC @ $1.94
0.786AB
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1.9000
1.8500
1.8000
1.7500
1.7000
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The Harmonic Analyzer (TM) : GBP_A0-FX
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GBP_A0-FX 10-MAR-06
Weekly
EMA13 1.82
EMA20 1.82
EMA50 1.79
SMA50 1.82
SMA200 1.59
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.27XA @ $1.959
1.618BC @ $1.943
1.130 @ $1.936 (+0.187 +10.72%)
$1.959
1.618BC @ $1.943
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1.9200
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1.8800
1.8700
1.8600
1.8500
A S O N D J F M A M J J A S
2005
The Harmonic Analyzer (TM) : GBP_A0-FX
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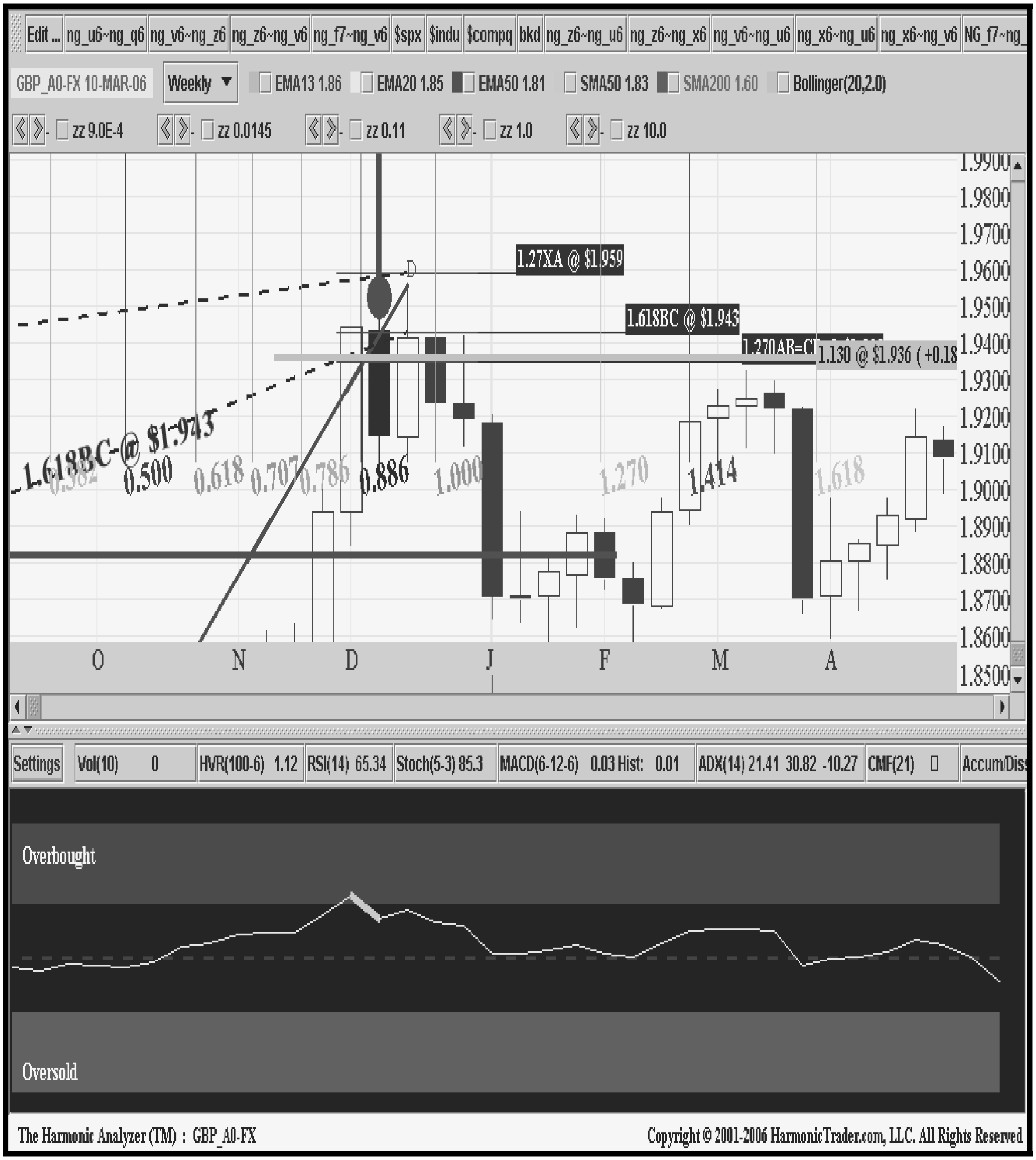
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GBP_A0-FX 10-MAR-06
Weekly
EMA13 1.86
EMA20 1.85
EMA50 1.81
SMA50 1.83
SMA200 1.60
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.27XA @ $1.959
1.618BC @ $1.943
1.130 @ $1.936 (+0.18
1.618BC @ $1.943
0.500
0.618
0.707
0.786
0.886
1.000
1.270
1.414
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1.9400
1.9300
1.9200
1.9100
1.9000
1.8900
1.8800
1.8700
1.8600
1.8500
Settings
Vol(10) 0
HVR(100-6) 1.12
RSI(14) 65.34
Stoch(5-3) 85.3
MACD(6-12-6) 0.03 Hist: 0.01
ADX(14) 21.41 30.82 -10.27
CMF(21)
Accum/Diss
Overbought
Oversold
The Harmonic Analyzer (TM) : GBP_A0-FX
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GBP_A0-FX 10-MAR-06
Weekly
EMA13 1.85
EMA20 1.84
EMA50 1.80
SMA50 1.83
SMA200 1.60
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.27XA @ $1.959
1.618BC @ $1.943
1.130 @ $1.936 (+0.187 +10.72%)
0.707
0.786
0.886
1.000
1.270
1.414
1.618
1.9800
1.9700
1.9600
1.9500
1.9400
1.9300
1.9200
1.9100
1.9000
1.8900
1.8800
1.8700
1.8600
1.8500
1.8400
1.8300
1.8200
D
J
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A
M
The Harmonic Analyzer (TM) : GBP_A0-FX
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Edit ... ng_u6~ng_q6 ng_v6~ng_z6 ng_z6~ng_v6 ng_f7~ng_v6 $spx $indu $compq bkd ng_z6~ng_u6 ng_z6~ng_x6 ng_v6~ng_u6 ng_x6~ng_u6 ng_x6~ng_v6 NG_f7~ng_
GBP_A0-FX 10-MAR-06
Weekly
EMA13 1.63
EMA20 1.62
EMA50 1.60
SMA50 1.61
SMA200 1.51
Bollinger(20,2.0)
zz 9.0E-4
zz 0.0145
zz 0.11
zz 1.0
zz 10.0
1.618 @ $2.017 (+0.268 +15.35%)
1.27XA @ $1.959
1.618BC @ $1.943
AB=CD @ $1.935
1.130 @ $1.936 (+0.187 +10.72%)
1.27XA @ $1.959
0.786XA
1.618BC @ $1.94
0.786AB
A
B
D
2.0000
1.9500
1.9000
1.8500
1.8000
1.7500
1.7000
A S O N D J F M A M J J A S O N D J F M A M J J A S O N D J F M A M J J
2004
2005
2006
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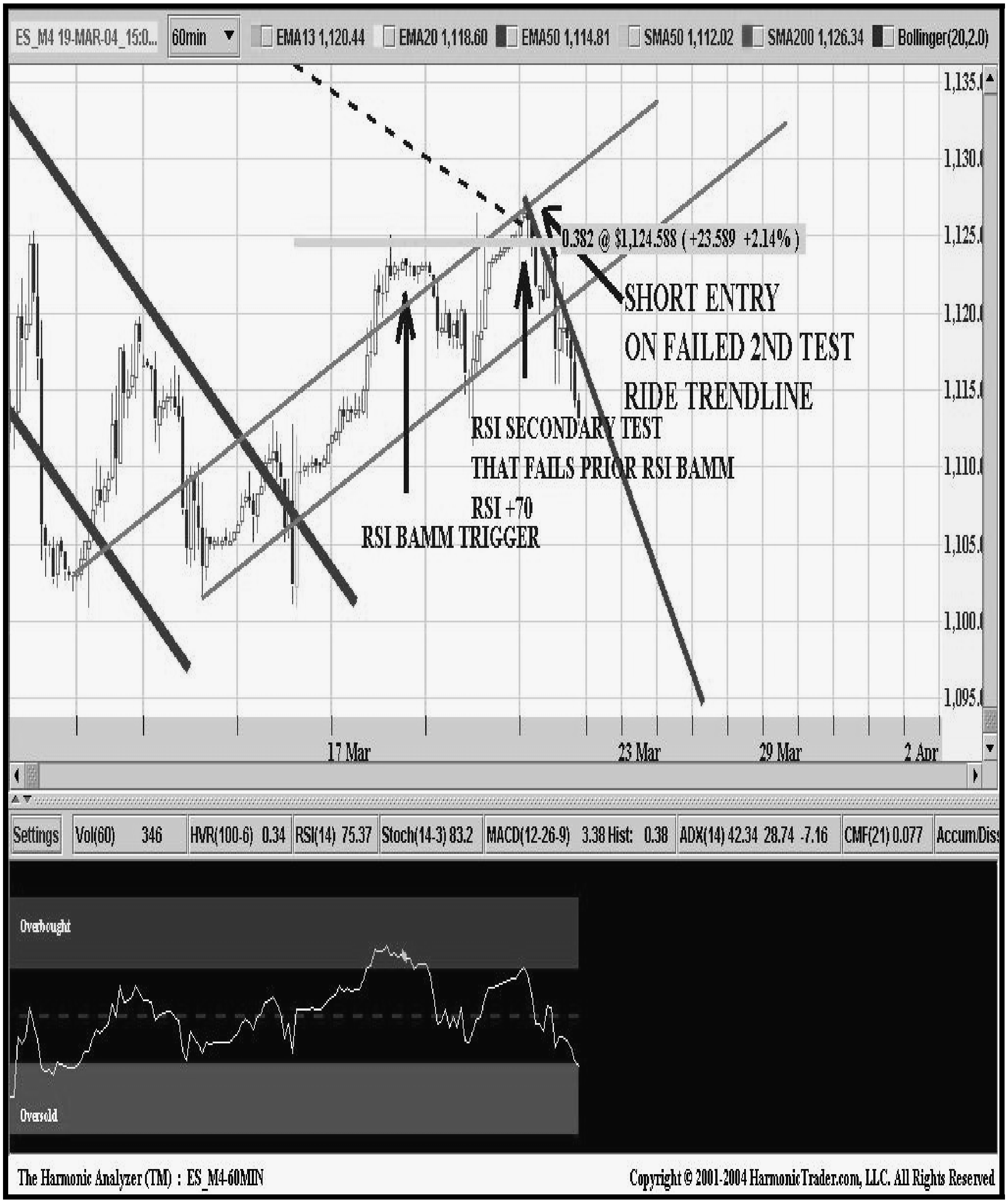
San Disk (SNDK)


ES_M4 19-MAR-04_15:0... 60min
EMA13 1,120.44 EMA20 1,118.60 EMA50 1,114.81 SMA50 1,112.02 SMA200 1,126.34 Bollinger(20,2.0)
0.382 @ $1,124.588 (+23.589 +2.14%)
SHORT ENTRY
ON FAILED 2ND TEST
RIDE TRENDLINE
RSI SECONDARY TEST
THAT FAILS PRIOR RSI BAMM
RSI +70
RSI BAMM TRIGGER
17 Mar
23 Mar
29 Mar
2 Apr
Settings Vol(60) 346 HVR(100-6) 0.34 RSI(14) 75.37 Stoch(14-3) 83.2 MACD(12-26-9) 3.38 Hist: 0.38 ADX(14) 42.34 28.74 -7.16 CMF(21) 0.077 Accum/Dis
Overbought
Oversold
The Harmonic Analyzer (TM) : ES_M4-60MIN
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Edit ... $INDU $SPX $COMPQ YM_m5 XLNX eur_A0-FX ES_m5 NQ_m5 EBAY JPM ADTN AXP CL_Z5 NG_H5 CSCO MDT biph icos ep bud
ES_M5 04-APR-05_11:...
15min
EMA13 1,187.45
EMA20 1,186.98
EMA50 1,185.84
SMA50 1,185.18
SMA200 1,182.96
Bollinger(20,2.0)
zz 0.0010
zz 0.0121
zz 0.11
zz 1.0
zz 10.0
Settings
Vol(60) 742
HVR(100-6) 0.70
RSI(14) 63.93
Stoch(14-3) 77.0
MACD(12-26-9) 0.87 Hist: 0.06
ADX(14) 33.29 31.01 -10.20
CMF(21) 0.327
Overbought
Oversold
The Harmonic Analyzer (TM) : ES_M5-15MIN
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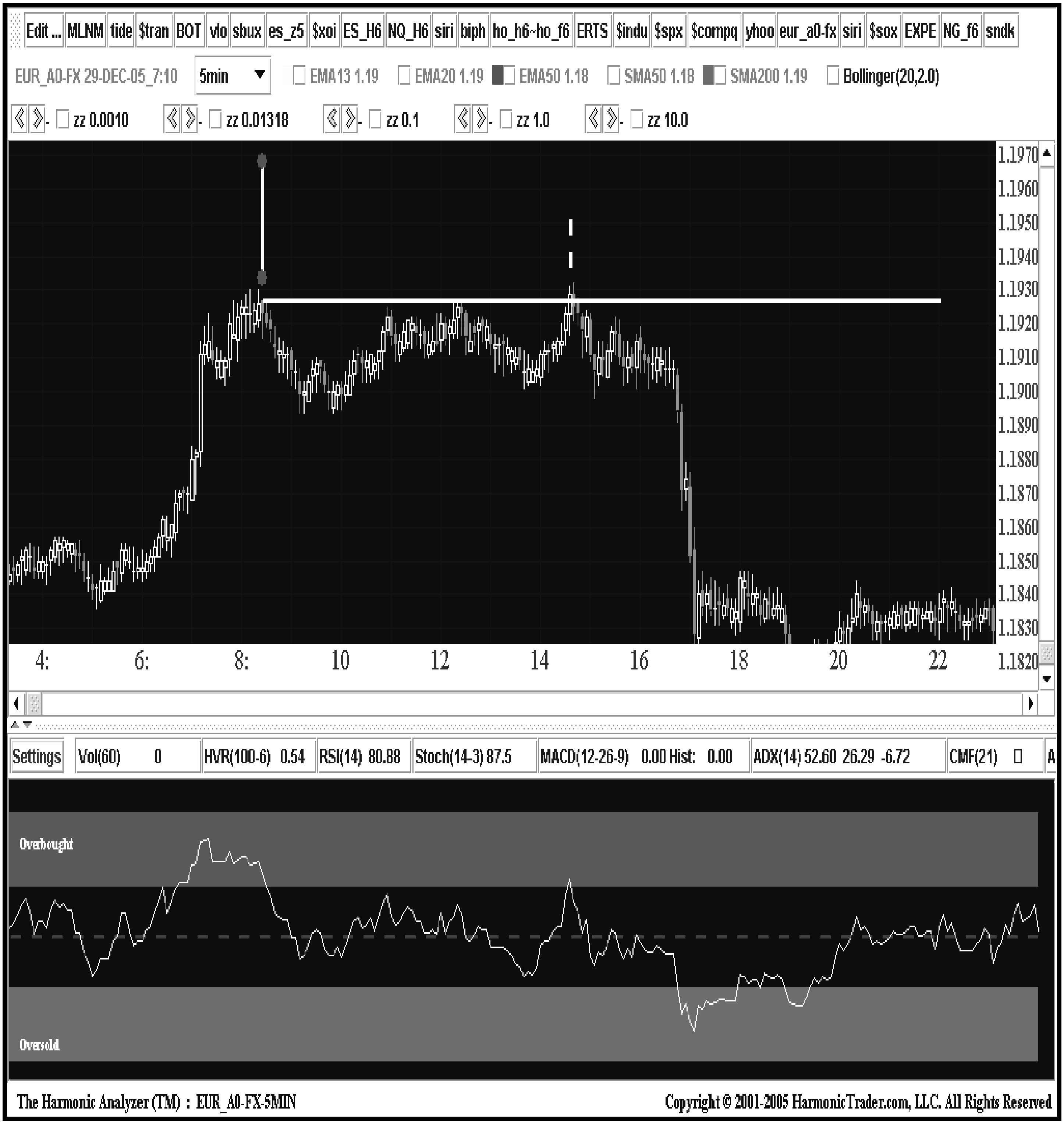

1987 Bearish RSI BAMM


Edit ... MLNM tide $tran BOT vlo sbux es_z5 $xoi $xau biph RIMM ERTS cl_z5 yhoo eur_a0-fx gbp_a0-fx $sox EXPE NG_f6 Nq_z5
^DJI 25-NOV-05
Daily
EMA13 2,631.39
EMA20 2,600.23
EMA50 2,509.72
SMA50 2,494.38
SMA200 2,232.84
Bollinger(20,2.0)
zz 0.0010
zz 0.01198
zz 0.1
zz 1.0
zz 10.0
Settings
Vol(60) 1,984,000
HVR(100-6) 1.03
RSI(14) 66.02
Stoch(14-3) 82.8
MACD(12-26-9) 58.69 Hist: 6.01
ADX(14) 47.34 23.02 -11.29
CMF(21) 0.209
Overbought
Oversold
The Harmonic Analyzer (TM) : ^DJI
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RSI BAMM FAILURE

Advanced RSI BAMM Tips

- **Look for pattern completion on larger time interval.**

- **Look for secondary BAMM on 50 RSI retest and immediately execute at that price level.**

- **pattern completion on larger time interval.**
- **Violate time frame = when initial RSI BAMM sinks below 80**

RSI BAMM Summary

1. Look for Extreme RSI Complex indicator reading.
2. Look for initial Reaction of M-type RSI indicator breakdown to 50-limit reading at a minimum with a nominal price reaction.
3. Wait for divergence of RSI and Price: Look for an impulsive RSI retest of extreme 70-limit that does not exceed high point reading of the prior complex structure.
4. Execute trade at completion of harmonic pattern within the range of the appropriate RSI BAMM extension levels.

Is this Really Harmonic Trading?

To answer this, we need to ask the proverbial question: "What is Harmonic Trading?" The answer is:

"Harmonic Trading is a methodology that utilizes the recognition of specific structures that possess distinct and consecutive Fibonacci ratio alignments that quantify and validate harmonic patterns. These patterns calculate the Fibonacci aspects of these price structures to identify highly probable reversal points in the financial markets… The identification of historically repetitive price patterns is the primary means that these techniques utilize to interpret the market's signals. It is in this effective price pattern identification ability that Harmonic Trading possesses its greatest advantages. The precision and accuracy of the specific pattern alignments define a consistent and effective approach that can be easily applied. Furthermore, each distinct pattern acts as a model for the basis of all trading decisions. Once a potential pattern is identified, the trading opportunity can be managed according to a defined set of rules that are particular for each situation. Although each pattern possesses different elements, Harmonic Trading does identify specific repetitive situations within the chaos of the financial markets."

Harmonic Trading of the Financial Markets: Volume One, pg. 7-8. Carney, Scott M., Nevada: HarmonicTrader.com, L.L.C. 2004.

the execution line for the entire RSI BAMM is at the 113 or 1618 extension but this is not the only consideration for executing a trade. Remember, this is one technique that complements other approaches Neve be Harmonic Trading Price pattern recognition or whatever. Of course, we're looking to harmonic patterns and other considerations such as pattern completions must be considered before executing a trade. But this is where the power of confirmation of mobile technical methods gives us a much greater for probability of a valid reversal and profitable move. As I will show in future examples, when the RSI BAMM lines up with distinct harmonic pattern completions, the accuracy of these methods are greatly increased.

xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx

STEP2 measure the trigger bar and troll a line to the right projecting from the LOW of the price bar
the trigger bar is defined in the bullish scenario has the price bar that confirms the W. pattern in the indicator and is the price action that resulted in yielding a move out of of the extreme -30 area. This trigger bar will typically be less than five price bars from the extreme low in the bullish scenario. Is important to make a difference between whether the trigger bar is the extreme low for is a few bars from the extreme low. Although I will get into this little later, it is important to note that the trigger bar is typically the third or fourth price bar from the extreme low. In these situations, the corresponding harmonic projection that is used in the RSI BAMM measurement will be a 113 extension. In the cases where the trigger bar is the actual extreme low, the harmonic projection that is used in the RSI BAMM measurement will be a 1.618 extension.
I will go in greater detail as I review examples of each type of RSI BAMM. Regardless of what the eventual harmonic projection is, the RSI BAMM trigger bar will always be the price bar that sets up the W. structure in the extreme -30 reading in the indicator.

step 3 wait for the divergence
Look for rsi/price divergence

After the trigger bar is established, the price action at this time is usually rebounding from an oversold technical situation. The extent of this rebound rally is typically short-lived, as it is more a reaction to the predominant downtrend and the initial stages oF a reversal. This is important concept because the RSI BAMM initial formation is an early signal that acts says a warning to watch the price action in this area. The RSI indicator reflects the relative price action of the current situation vs. the strength of the trend 14. Prior. Furthermore, the RSI indicator is only one part of the story. It reflects an overall reading a bias that measures the degree of the move more than the exact price level has measured by harmonic ratios. Since we're addressing a bullish scenario, the reflex rally after the W. type structure is formed within the RSI oversold -30 level typically will experience a retest of the initial low after a brief BOUNCE. The easiest way to determine this retest or roll over is to look for a clear trendline violation from the extreme low. Another technique that confirms the retest is forming is to see in sdeviolation of the 382 retracement of the short-term bounce. The trend line violation and 382 were retracement violation are clear signs that a full retest is in the works where the larger targets of the RSI BAMM extension move and more significant harmonic Price patterns complete.

step 4 if divergence occurs measure the prior price Leg that preceded the final move

The divergent price action that occurs in this step is the most important part of the entire approach because it gauges the price action at a critical "internal" point within the trend. Although the RSI BAMM structure is formed in the indicator - indicating internal strength - this retest where the RSI has stabilized and the price action has diverged - offers an enormous amount of information regarding the technical state of the overall trend. After the roll over has occurred to retest the initial low point is critical to measure the short-term bounce and project either a 113 or 1618 extension to defining the RSI BAMM reversal point. If the trigger bar is not the extreme bar, the corresponding harmonic projection will be a 113 extension. If the trigger bar is the extreme the though then the corresponding harmonic projection will be a 1618. The Remember, the line drawn across the chart Fromm low point of the RSI BAMM trigger bar acts as a support line for the entire set up. The corresponding harmonic projections act as the extreme price level for the RSI banded be valid. These two price levels defining entire area for the RSI BAMM. Essentially this is defining the area where the bias has changed and the price trend will not changed to reflect be new bias. It is important in note that the final move that takes the price action below the prior low for a brief time to either the 113 or 1618 extension is called the divergence. Although others have used the concepts of divergence as it relates to indicator readings and price action, in this situation the divergence behavior is a little different. The RSI indicator formation is unique and the overall approach includeS specific harmonic measurements to define the entire technical phenomenon.
xxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxxx

RSI BAMM Violations

Price limit vs RSI limit

SHOW WHEN RSI takes out prior RSI level

Stop Loss Considerations

the step 6 the stop loss is a combination of extreme price limit the RSI BAMM - typically beyond the 1618 - and the price limit of the pattern that corresponds with the setup. After defining the entire range of RSI BAMM and harmonic pattern completion points, the only consideration beyond the execution is the stop loss limit. Again, this will also include the price levels that by the larger harmonic patterns that are included in the trading setup from a pure RSI BAMM perspective the key validation only truly occurs beyond the 1618 extension of the final divergent move. Although it is important to differentiate between whether the RSI BAMM uses a 113 or a 1618 extension, the validation of the technical phenomenon becomes questionable beyond the 2.00 extension of the final move. As is the case for harmonic pattern failures, price action that violates these price levels especially on the first test should raise a red flag that the primary trend is quite strong. The area defined by the RSI BAMM is truly a do or die price level that is not leave much room for discretion

CHP 8: HISTORICAL STUDIES

WEEKLY RETRACEMENTS

Charles H. Dow Award 2003

Harmonic Trading:

Price Patterns that Identify Critical Reversals in the Financial Markets

By Scott M. Carney

HarmonicTrader.com

President

What is Harmonic Trading?

Harmonic Trading is a methodology that utilizes the recognition of specific price patterns and Fibonacci numbers to determine highly probable reversal points in the markets. This methodology assumes that trading patterns or cycles, like many patterns and cycles in life, repeat themselves. Harmonic Trading is an evolution of cyclical price and time analysis that incorporates Elliott Wave principles, Fibonacci measurement techniques and other technical considerations.

Harmonic Price Patterns are defined by specific structures that are quantified by Fibonacci calculations. Essentially, these patterns are price structures that contain combinations of <u>distinct and consecutive</u> Fibonacci retracements and projections. By calculating the various Fibonacci aspects of a specific price structure, Harmonic Patterns can indicate a specific area to examine for potential turning points in price action.

Harmonic Trading techniques respect the natural ebb and flow of buying and selling. When these alignments are identified correctly, valid Harmonic Patterns indicate critical support and resistance levels where the predominant cycle is changing.

Patterns within Chaos

Many have argued that the stock market is a random entity. According to the Random Walk Theory, popularized in the book, *The Random Character of Stock Market Prices*, by Paul H. Cootner (MIT Press, 1964), price action is "serially independent." This means that price history is not a reliable indicator of future price action. Although this theory does possess validity, since anything can happen in the stock market, history has proven that within this randomness there is a degree of repetition.

Specific Fibonacci Ratio Alignments

Harmonic Patterns are price structures that contain combinations of specific consecutive Fibonacci retracements and projections. These combinations are the very basic frameworks that offer significant information regarding the state of *potential* price action and help to identify the *potential* state of the market. Furthermore, specific Fibonacci alignments serve to differentiate similar price structures. This concept is the critical element of Harmonic Trading and provides significant insight into the state of price movements.

Principle of Harmonicity

J.M. Hurst presented one of the earliest and most comprehensive explanations of the basic tenets of Harmonic Trading in his cycles course from the early 1970s. His explanation of the *Principle of Harmonicity* states: “The periods of neighboring waves in price action tend to be related by a small whole number.” (*J.M. Hurst Cycles Course*, Traders Press, 1973.) The important concept to grasp is that price waves or distinct price moves are related to each other. Furthermore, Harmonic Trading utilizes Fibonacci numbers and price patterns to quantify these relationships.

Fibonacci Numbers

Fibonacci numbers are based upon the Fibonacci sequence discovered by Leonardo de Fibonacci de Pisa (b.1170-d.1240). His most famous work, the Liber Abaci (Book of the Abacus), was one of the earliest Latin accounts of the Hindu-Arabic number system. In this work, he developed the Fibonacci number sequence, which is historically the earliest recursive series known to date.

The series was devised as the solution to a problem about rabbits. The problem is: If a newborn pair of rabbits requires one month to mature and at the end of the second month and every month thereafter reproduce itself, how many pairs will one have at the end of n months? The answer is: un. This answer is based upon the equation: un+1 = un+un-1.

Although this equation might seem complex, it is actually quite simple. The sequence of the Fibonacci numbers is as follows:

0, 1, 1, 2, 3, 5, 8, 13, 21, 34, 55, 89,144, 233, 377 ...... up to infinity

Starting with zero and adding one begins the series. The calculation takes the sum of the two numbers and adds it to the second number in the addition. The sequence requires a minimum of eight calculations.

(0+1=1)...(1=1=2)...(1+2=3)...(2+3=5)...(3+5=8)...
(5+8=13)…(8+13=21)…(13+21=34)…(21+34=55)

After the eighth sequence of calculations, there are constant relationships that can be derived from the series. For example, if you divide the former number by the latter, it yields 0.618.

34/55 = 0.618181 ~ 0.618
55/89 = 0.618181 ~ 0.618

And, if you divide the latter number by the former, it yields 1.618.

144/89 = 1.617977 ~ 1.618
233/144 = 1.618055 ~ 1.618

The 0.618 and the 1.618 are the two primary Harmonic ratios that are directly derived from the Fibonacci sequence that are utilized to quantify Harmonic Price Patterns.

These two numbers exist in many natural and man-made phenomena. The 0.618 and the 1.618 ratio relationships have been found in the proportions of the Great Pyramids. Universal examples exhibit this phenomenon, as well. For example, Venus takes 225 days to complete a revolution around the sun. The Earth requires 365 days to complete one revolution. The result of 225 divided by 365 is approximately 0.618 of a year. (225/365 = 0.6164 ~ 0.618)

Fibonacci Number Derivations

The Fibonacci numbers utilized in Harmonic Trading are either directly or indirectly derived from the primary ratios of the 0.618 and the 1.618 from the Fibonacci sequence. Although market technicians utilize a variety of percentage ratios to measure price movements, the following list represent the most suitable ratios that determine precise Harmonic patterns.

Primary Ratios: 0.618 & 1.618

(From the Fibonacci Number Sequence)

Primary Derived Ratios:

- 0.786 = square root of the 0.618
- 0.886 = fourth root of the 0.618
- 1.13 = inverse of the 0.886 (1/0.886)
- 1.27 = inverse of the 0.786 (1/0.786)

Complimentary Derived Ratios:

0.382, 0.50, 0.707, 1.41, 2.0, 2.24, 2.618, 3.14, 3.618

Price Structures

The analysis of Harmonic price structures is based upon the elements of simple Geometry and Elliott Wave principles. However, unlike the general wave counts of Elliott Analysis, Harmonic Trading focuses on exact price structures. Specifically, Harmonic Trading examines 5-point reversal price structures, differentiating these movements with respect to their Fibonacci alignments.

Elliott Wave M and W Corrective Patterns

Most technicians are aware of the “M” and “W” corrective patterns explained within Elliott Wave Analysis. These corrective structures are vital in the validation of wave counts and Elliott theory. However, these “M”s and “W”s can be further refined by quantifying each point’s Fibonacci measurements.

Price Point Alignment

Specific price point alignment of Harmonic Patterns is mandatory. Each pattern must possess an exact alignment that must not be violated. The most significant point in these “M” and “W” Harmonic Patterns is the mid-point (B). Unlike Elliott Wave number counts, Harmonic Trading denotes each point with letters, marking each price move as XA, AB, BC, CD.

What is a Harmonic Price Pattern?

Harmonic Price Patterns are defined by specific price structures, quantified by Fibonacci calculations. Essentially, Harmonic Price Patterns are 5-point price structures that contain combinations of distinct consecutive Fibonacci retracements and projections. By calculating the various Fibonacci aspects of these 5-point price structures, Harmonic Patterns can indicate a specific area to examine for potential turning points in price action called a Potential Reversal Zone.

Potential Reversal Zones

The combination of distinct and consecutive Fibonacci ratio alignments creates these areas known as Potential Reversal Zones. Essentially, the Fibonacci aspects of a particular Harmonic Price Pattern offer specific measurements that can define critical areas of support and resistance. The concept of a Potential Reversal Zones is one of the most important considerations in Harmonic Trading. The key to utilizing these Harmonic measures when analyzing the markets is to determine the area where the greatest group of calculations converges. Furthermore, larger price structures on daily or weekly will define more significant areas of support and resistance than intra-day patterns.

Another important consideration is the amount of numbers within the Potential Reversal Zone. The number of discernable Fibonacci retracements and projections that exist within a specific area will indicate the importance of that price level. In addition, tight alignments of Fibonacci measurements within a price structure will enhance the importance of that price pattern. When a congregation of Harmonic numbers is within a close range, the area should be considered very significant. This is an important guideline because a very Harmonic area potential support or resistance will indicate a great deal about a stock's direction. For example, if a Potential Reversal Zone contains four or five Fibonacci calculations, the area should be considered very Harmonic. If a stock reverses from this area, the Potential Reversal Zone could be considered as an important turning point. However, if a stock does not reverse, it would indicate that the predominant trend is quite strong.

Three Harmonic Patterns: The AB=CD, The Gartley and The Bat

The AB=CD Pattern

Ideal Bullish AB=CD | **Ideal Bearish AB=CD**

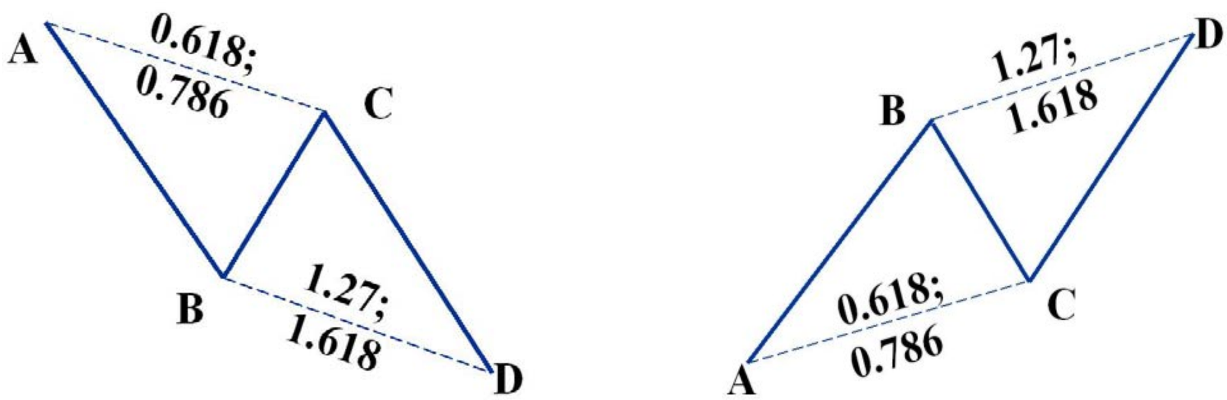


Figure 1.

The AB=CD pattern is a structure where each price leg is equivalent. The Fibonacci numbers in the pattern must occur at specific points. In an ideal AB=CD pattern, the AB price movement is followed by a smaller retracement. The C point in the price structure must retrace to either a 0.618 or 0.786 of the AB leg. After this pullback, the CD leg continues an equivalent distance in the predominant trend.

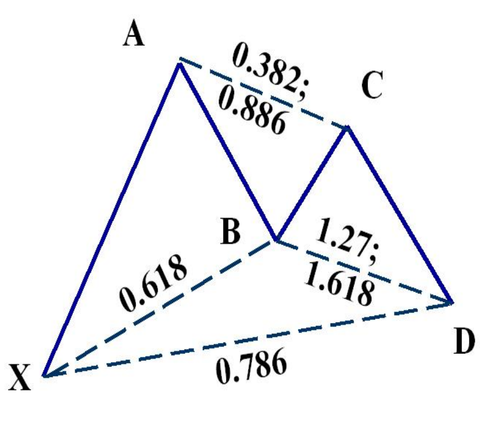
The C point retracement sets up the BC Fibonacci projection that should converge at the completion of the AB=CD. Ideally, the BC Fibonacci projection should be either a 1.27 or 1.618. It is important to note that a 0.618 retracement at the C point will result in a 1.618 BC projection. A 0.786 retracement at the C point will result in a 1.27projection. The most important consideration to remember is that the BC projection should converge closely with the completion of the AB=CD.

The Ideal Gartley Pattern vs. The Bat Pattern

Although similar in their respective "M" and "W" Elliott-type price structures, the Ideal Gartley Pattern and the Bat Pattern are two different entities that utilize different Fibonacci retracement and projection calculations. These patterns each have specific rules that define their structure and their respective Potential Reversal Zones.

The Ideal Gartley Pattern

Ideal Bullish Gartley



Ideal Bearish Gartley

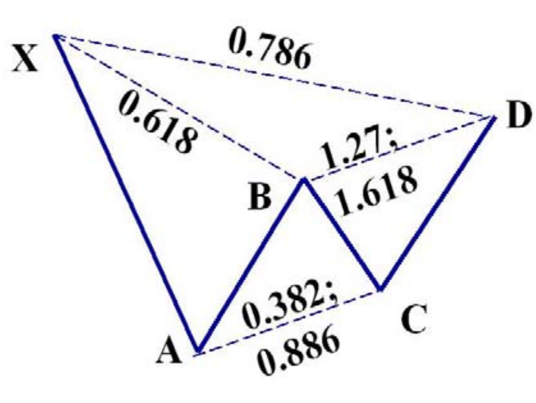


Figure 2.

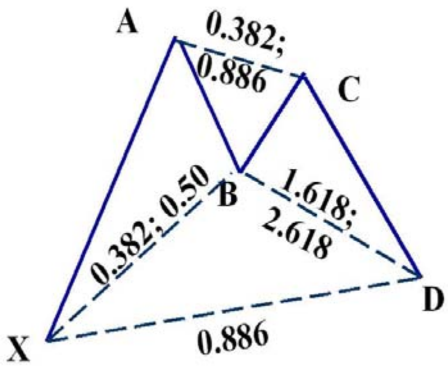
H.M. Gartley outlined the Gartley pattern in his book, *Profits in the Stock Market*, published in 1935. This is one of the best-known Harmonic patterns in the trading community today. In recent years, a multitude of articles in the financial media have mistakenly cited Mr. Gartley for assigning specific Fibonacci ratios to this structure. However, this is not the case. Mr. Gartley did not discuss Fibonacci ratios in his entire book.

Larry Pesavento in his book, *Fibonacci Ratios with Pattern Recognition* (Trader's Press, 1997) was the first to assign Fibonacci ratios to the price structure. In fact, Mr. Pesavento was the one responsible for naming this price structure. It is important to note that he assigned the Fibonacci ratios of either a 0.618 or a 0.786 to only the completion point (D). Although this was a revolutionary a and move slowly continue to students development in the field of Harmonic Trading, he did not differentiate each point within these "M" and "W" price structures.

In my first book, *The Harmonic Trader* (1999), I differentiated this structure by defining the exact alignment of consecutive Fibonacci retracements and projections required to define this framework, creating the *Ideal Gartley Pattern*. There are others who have assigned Fibonacci retracements to this price structure. However, they use a variety of Fibonacci numbers at each price point. Despite these variations, the Fibonacci alignments that define a precise five-point reversal pattern are the 0.618 at the B point and the 0.786 at the D point. Furthermore, the pattern must possess a distinct AB=CD pattern that converges in the same area as the 0.786 XA retracement and the BC projection (either 1.27or 1.618). The most critical aspect of the Gartley is the B point retracement, which must be at a 0.618 of the XA leg.

The Bat Pattern

Bullish Bat **Bearish Bat**


A
0.382;
0.886
C
0.382; 0.50
B
1.618;
2.618
D
X
0.886

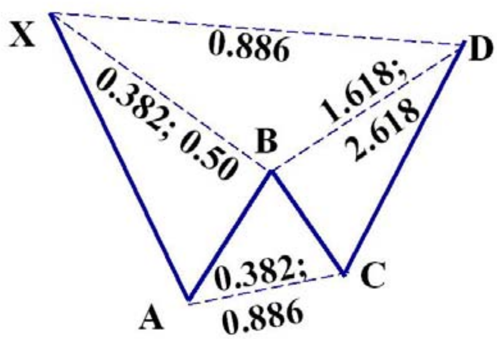

X
0.886
D
0.382; 0.50
B
1.618;
2.618
0.382;
C
A
0.886

Figure 3.

The Bat pattern is a precise Harmonic Pattern that I introduced on my website, HarmonicTrader.com in 2001. The pattern incorporates a 0.886XA retracement, as the defining element in the Potential Reversal Zone. Unlike the ideal Gartley pattern conditions, the mid-point (B) must be less than 0.618, preferably a 0.50 or 0.382 retracement of the XA leg. In addition, the AB=CD pattern within the Bat is usually extended and it frequently requires a 1.27 or 1.618AB=CD calculation. Furthermore, the BC projection must be at least 1.618 to validate the pattern.

The Mid-Point (B) in Corrective Waves

The mid-point (B) in corrective waves is the primary method to differentiate Harmonic Price Patterns. The completion of the Harmonic Patterns will vary, depending upon where the mid-point is located within these 5-point corrective structures. For example, the shallow B-point retracement within the Bat Pattern usually creates a situation whereby the CD leg is extended beyond the exact AB=CD completion point and the BC projected measurement is at least 1.618 or greater. This is quite different from the ideal Gartley Pattern alignment, where the AB=CD pattern is usually equivalent and the BC projection is 1.618 or less. Such differentiation helps to define similar price structures and offers a great deal of technical information regarding the state of future potential price action.

The Standard and Poor's 500: A 20-year Review

As a broad representation of the market, the Standard and Poor's 500 has formed these two patterns throughout its history, marking many historic market reversal points. Specifically, the corrective "M" and "W" patterns of the Gartley and the Bat have signaled important market tops and bottoms.

For this research, I utilized the Harmonic Analyzer, an unprecedented Harmonic Price Pattern recognition software program that automatically scans for these specific situations based upon preset algorithms. The software utilized the prescribed Fibonacci alignments of the aforementioned Gartley and Bat patterns. The settings are illustrated in this table.

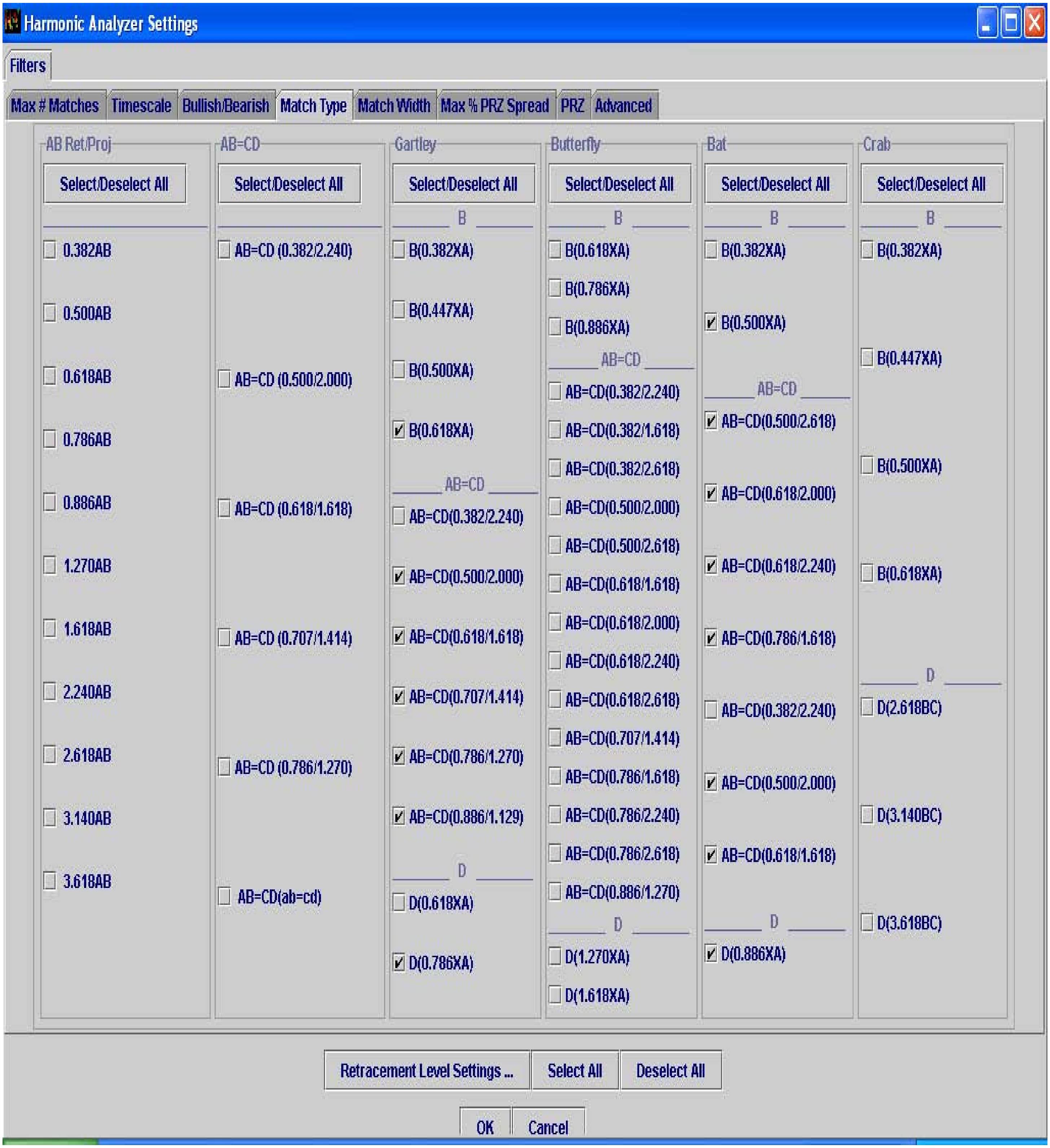

Harmonic Analyzer Settings
Filters
Max # Matches
Timescale
Bullish/Bearish
Match Type
Match Width
Max % PRZ Spread
PRZ
Advanced
AB Ret/Proj
Select/Deselect All
0.382AB
0.500AB
0.618AB
0.786AB
0.886AB
1.270AB
1.618AB
2.240AB
2.618AB
3.140AB
3.618AB
AB=CD
Select/Deselect All
AB=CD (0.382/2.240)
AB=CD (0.500/2.000)
AB=CD (0.618/1.618)
AB=CD (0.707/1.414)
AB=CD (0.786/1.270)
AB=CD(ab=cd)
Gartley
Select/Deselect All
B
B(0.382XA)
B(0.447XA)
B(0.500XA)
B(0.618XA)
AB=CD
AB=CD(0.382/2.240)
AB=CD(0.500/2.000)
AB=CD(0.618/1.618)
AB=CD(0.707/1.414)
AB=CD(0.786/1.270)
AB=CD(0.886/1.129)
D
D(0.618XA)
D(0.786XA)
Butterfly
Select/Deselect All
B
B(0.618XA)
B(0.786XA)
B(0.886XA)
AB=CD
AB=CD(0.382/2.240)
AB=CD(0.382/1.618)
AB=CD(0.382/2.618)
AB=CD(0.500/2.000)
AB=CD(0.500/2.618)
AB=CD(0.618/1.618)
AB=CD(0.618/2.000)
AB=CD(0.618/2.240)
AB=CD(0.618/2.618)
AB=CD(0.707/1.414)
AB=CD(0.786/1.618)
AB=CD(0.786/2.240)
AB=CD(0.786/2.618)
AB=CD(0.886/1.270)
D
D(1.270XA)
D(1.618XA)
Bat
Select/Deselect All
B
B(0.382XA)
B(0.500XA)
AB=CD
AB=CD(0.500/2.618)
AB=CD(0.618/2.000)
AB=CD(0.618/2.240)
AB=CD(0.786/1.618)
AB=CD(0.382/2.240)
AB=CD(0.500/2.000)
AB=CD(0.618/1.618)
D
D(0.886XA)
Crab
Select/Deselect All
B
B(0.382XA)
B(0.447XA)
B(0.500XA)
B(0.618XA)
D
D(2.618BC)
D(3.140BC)
D(3.618BC)
Retracement Level Settings ...
Select All
Deselect All
OK
Cancel

Figure 4.

The Harmonic Analyzer was programmed to search for weekly patterns exclusively. This was to minimize repetitive matches of daily patterns and to find valid results of significant long-term corrective formations.

The Harmonic Analyzer was preset to begin its scan starting from July 1st, 1982 to July 1st, 2003, representing 20 years of market action in the Standard and Poor's 500 index. The following table shows 5 valid matches of three Bat patterns and two Gartley patterns. Four of these matches were bullish and one was bearish.


Harmonic Pattern Matches (5) Min Match Width: 0 Days Max Match Width: 1000 Days Max PRZ Spread: 50% Min # Convergences: 1

Sorted By (Date, Match Width)

Matches Filters

1	^spx WEEKLY 14-MAR-03	Bullish	iBat	(500,786,886)	Width:	115	ABOVE	PRZ:	3/3	(0.886XA@789.794)(1.27AB=CD@827.316)(1.618B(
1	^spx WEEKLY 1-SEP-00	Bearish	Gartley	(618,786,786)	Width:	120	BELOW	PRZ:	3/3	(0.786XA@1,507.187)(AB=CD@1,504.630)(1.270B(
1	^spx WEEKLY 3-MAR-00	Bullish	iBat	(500,786,886)	Width:	100	BELOW	PRZ:	0/3	(0.886XA@1,261.550)(1.27AB=CD@1,282.168)(1.(
1	^spx WEEKLY 4-DEC-87	Bullish	iBat	(500,500,886)	Width:	35	ABOVE	PRZ:	2/3	(0.886XA@221.106)(AB=CD@226.580)(2.000BC@22
1	^spx WEEKLY 13-AUG-82	Bullish	Gartley	(618,618,786)	Width:	625	ABOVE	PRZ:	1/3	(0.786XA@104.444)(AB=CD@95.550)(1.618BC@99.(

Figure 5.

Pattern 1: Bullish Gartley (Completed August 13th, 1982)

This Bullish Gartley pattern possessed a Potential Reversal Zone with three Harmonic measurements that defined an area between 95.55 and 104.44. This was a considerable weekly pattern that marked the 1982 low. In addition, the sharp rally that followed after the reversal indicated that this Harmonic support was quite strong.

Chart 1.

Pattern 2: Bullish Bat (Completed December 4th, 1987)

Chart 2.

Following the Crash of 1987, the Standard and Poor's 500 completed this Bullish Bat. This pattern possessed a Potential Reversal Zone with three Harmonic measurements that defined an area between 226.50 and 221.10. Although not as large as the 1982 Bullish Gartley, this distinct pattern confirmed the 1987 Crash low as critical support in the 220 area. Again, it is important to note the persistent rally that followed after the pattern completed, indicating this Harmonic support was quite strong. This is especially significant due to the crash that preceded this pattern. In this situation, the Bat pattern acted as a signpost of future action, providing a clear signal the crash was indeed over.

Patten 3: Bullish Bat (Invalid Match)

Chart 3.

The Harmonic Analyzer generated this match that did not complete. The specific price point alignment of the pattern was violated before the Potential Reversal Zone was tested. This result was the only invalid match of the entire 20-year weekly scan for the Standard and Poor's 500.

Pattern 4: Bearish Gartley (Completed September 1st, 2000)

Chart 4.

This valid pattern match of the Bearish Gartley marked the top in 2000. This formation formed in the Standard and Poor's 500 after a critical failure of the previous all-time high at 1550. It is important to note the sharp reversal that transpired following the completion of the pattern. Such action is indicative of valid Harmonic patterns. In this case, the Bearish Gartley was signaling a critical turning point.

Pattern 5: Bullish Bat (Completed March 14th, 2003)

Chart 5.

This recent pattern marked the low for the index in March. This Bullish Bat pattern possessed a Potential Reversal Zone with three Harmonic measurements that defined an area between 789.80 to 828.90. Is this pattern indicating that the market is at a critical juncture and it is reversing the primary bearish trend of the past three years? Based upon the previous examples of the past 20 years, it seems quite likely. Again, the sharp reversal from this pattern over the past several months is similar to the 1982, 1987 and 2000 situations and it must be considered as substantial evidence that a larger trend reversal is developing.

Conclusion

The Market Technicians Association's slogan states: "In price there is knowledge!" This motto relates well to Harmonic Trading techniques, as these specific price structures can offer a great deal of information regarding the potential state of the markets. When significant valid Harmonic Price Patterns are identified, they can frequently act as signposts of future market direction. The research of valid weekly Harmonic Patterns in the Standard and Poor's 500 index of the past 20 years clearly substantiates this statement. It is important to note that Harmonic Trading techniques are not a "Black Box" methodology. Other technical considerations, such as overall trend, indicators and oscillators, should be utilized to confirm the information provided by the Harmonic Price Patterns. But, the historic evidence proves that these situations repeat within the chaos of the markets and they must be respected.

Appendix

Bibliography