

VOLUME

2

HARMONIC TRADING

ADVANCED STRATEGIES FOR PROFITING FROM
THE NATURAL ORDER OF THE FINANCIAL MARKETS



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Harmonic Trading: Volume Two

**Advanced Strategies for Profiting from the
Natural Order of the Financial Markets**

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Basic 5-0 Requirements

Although the pattern incorporates 5 points within the structure (X, A, B, C, D), the initial price leg (0) can start from 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 Extreme Harmonic Impulse move. The XA projection that defines the B point ideally must not exceed a 2.24. Any extension greater than a 2.24 will negate the structure, as smaller impulse moves are preferred. Again, this is the failed wave 3 or wave 5—in Elliott Wave terms—that establishes the rest of the structure.

- ***Look for initial impulsive reversal at X, A, B points that possesses a 1.13-1.618 extension.***
- ***The AB projection must possess a minimum 1.618 extension at the C point but not exceed 2.24.***
- ***The D point is defined by the 50% BC retracement and the Reciprocal AB=CD pattern completion.***

The BC leg is the longest price length of the structure that 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 AB minimum extension 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 complement the PRZ.

Although the 5-0 pattern is not a typical M- or W-type price structure, the same principles within the Harmonic Trading approach are applied to these situations. The Reciprocal AB=CD helps define the general area, while the 50% retracement pinpoints the precise range of the harmonic zone. The following illustrations and examples will clearly explain these concepts.

The Bullish 5-0 Pattern

The Bullish 5-0, illustrated in Figure 3.5, 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 Elliott Wave terms—that establishes the rest of the structure.

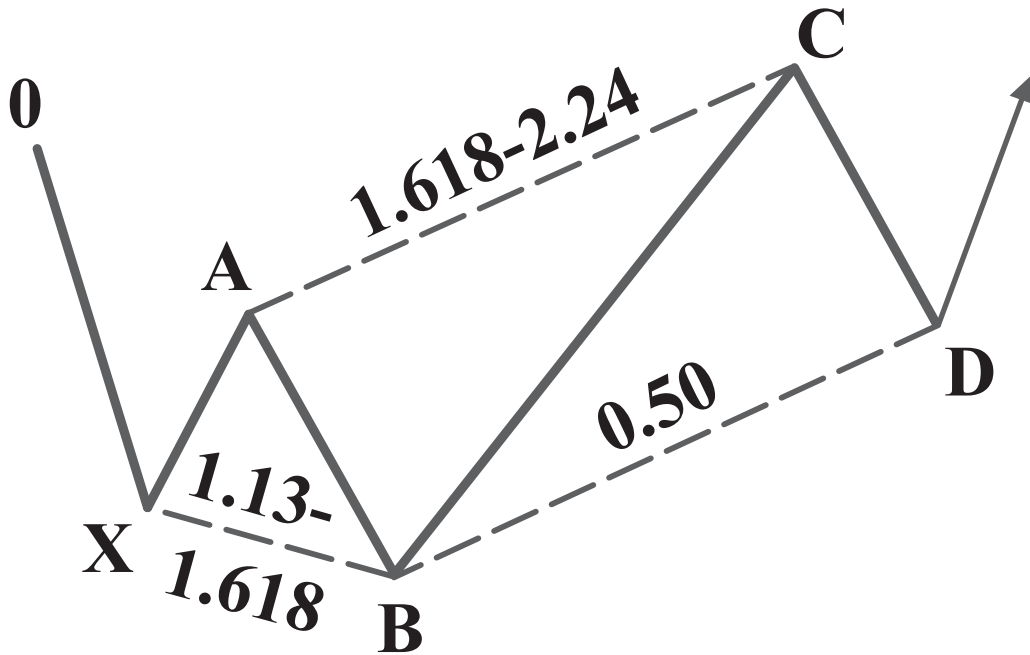


Figure 3.5

The important limits from a Harmonic Trading perspective require 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 complement the PRZ. It will take some time 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.

Eurodollar (EUR_A0-FX): 5-Minute Bullish 5-0 Pattern

This chart of the Euro demonstrates the effectiveness of the pattern in shorter-term situations (see Figure 3.6). After declining steadily throughout the previous day, the price action completed a failed down wave that nominally took out the prior session's low before rallying sharply to the 1.618 projection of the AB leg.



Figure 3.6

The Euro rolled over to retest the 50% level before resuming the uptrend. The Reciprocal $AB=CD$ complemented the 50% retracement at the 1.3910 level, defining a precise area to get long.

Standard & Poor's 500 Trust (SPY): Daily Bullish 5-0 Pattern

This chart of the S&P 500 Spider is another example of an ideal Bullish 5-0 pattern (see Figure 3.7). On this daily chart example, the SPY ETF possessed a distinct Bullish 5-0 pattern that exemplifies the ideal nature of the pattern.



Figure 3.7

Starting with an impulsive AB leg with a 1.13 extension, the ETF formed an ideal extended BC leg that reversed at the 2.0 projection of AB. The price action reversed sharply after testing the PRZ of the pattern.

NASDAQ 100 March 2010 Mini-Contract (NQ_H0): 60-Minute Bullish 5-0 Pattern

Figure 3.8 shows a distinct 5-0 pattern on the 60-minute chart that reversed sharply after testing the entire PRZ.



Figure 3.8

This chart is remarkable due to the pattern pinpointed the intraday support. The price action formed the proper alignment of ratios for the structure, stabilized in the PRZ, and reversed immediately after testing the completion point of the pattern. These characteristics are the ideal signs of a valid reversal for any timeframe. The key is to focus on the price action following the completion of the pattern.

Standard & Poor's 500 June 2009 Mini-Contract (ES_M9): 15-Minute Bullish 5-0 Pattern

This chart of the ES was illustrated in advance (see Figure 3.9). The structure was distinct, and the 50% retracement was calculated at 936. In addition, the Reciprocal Bullish AB=CD was projected to complete in the same area.



Figure 3.9

This 60-minute chart exemplifies the ideal structure for the 5-0, especially with the distinct 2.0 impulse projection. Like a magnet, the price action steadily declined to the 50% level of that extreme extension to complete the pattern. The chart in Figure 3.10 shows the price action, as the ES approached the PRZ at 1113.