

The Basics of the Wave Principle

The e-learning Series for Traders

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The Basics of the Wave Principle

- 1.00 Introduction — Ralph Nelson Elliott's Discovery**
- 2.00 Motive Waves**
- 3.00 Corrective Waves**
- 4.00 Rules**
- 5.00 Guidelines**
- 6.00 Wave Personalities**
- 7.00 Fibonacci Relationships**
- 8.00 Summary**

Financial Market Behavior Characteristics

Emotional (Unconscious)

Subjective

Impulsive

Ignorance and Uncertainty

Herding

Values Cannot Revert To Anything

The Wave Principle

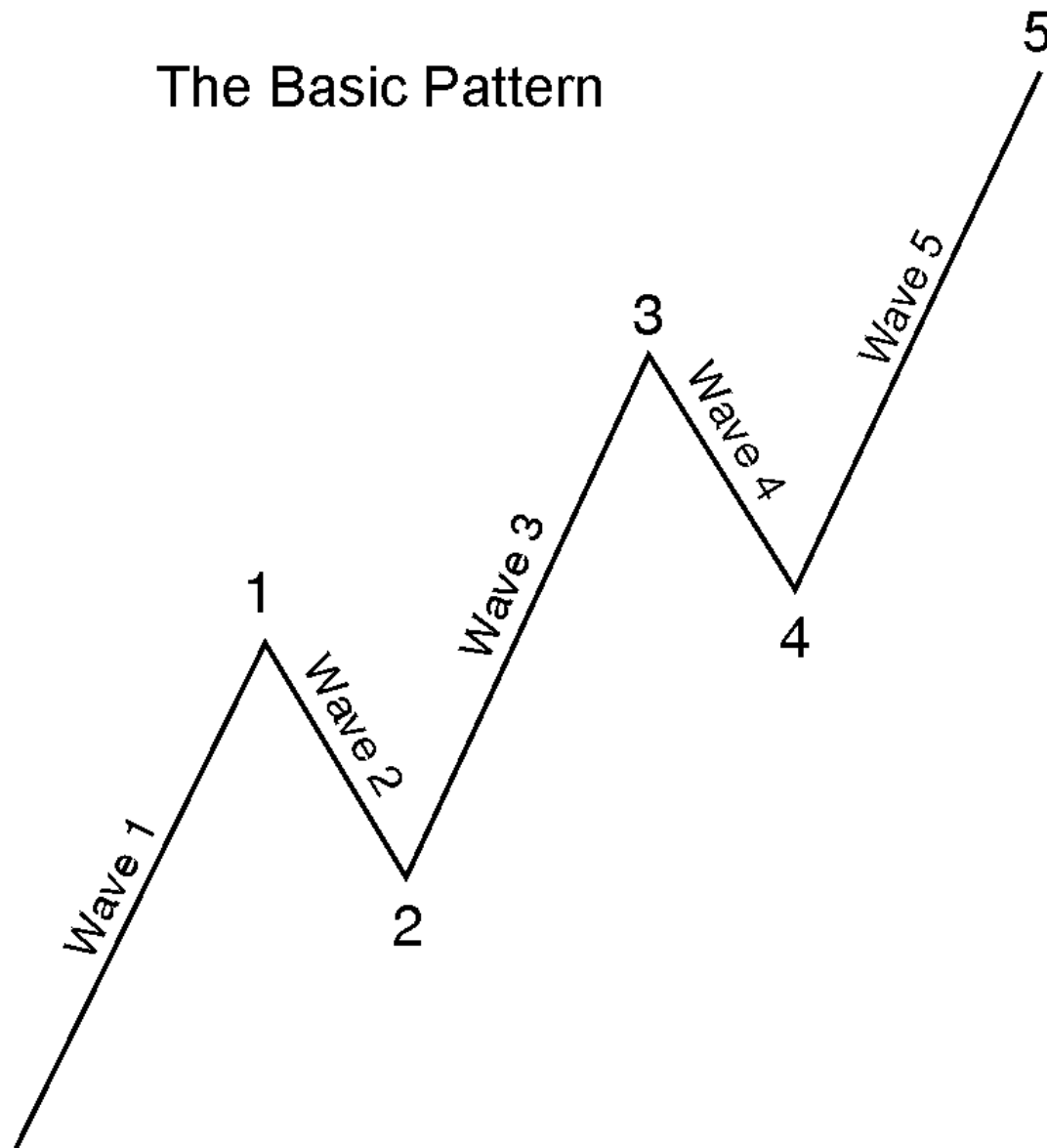
Financial Markets are Patterned

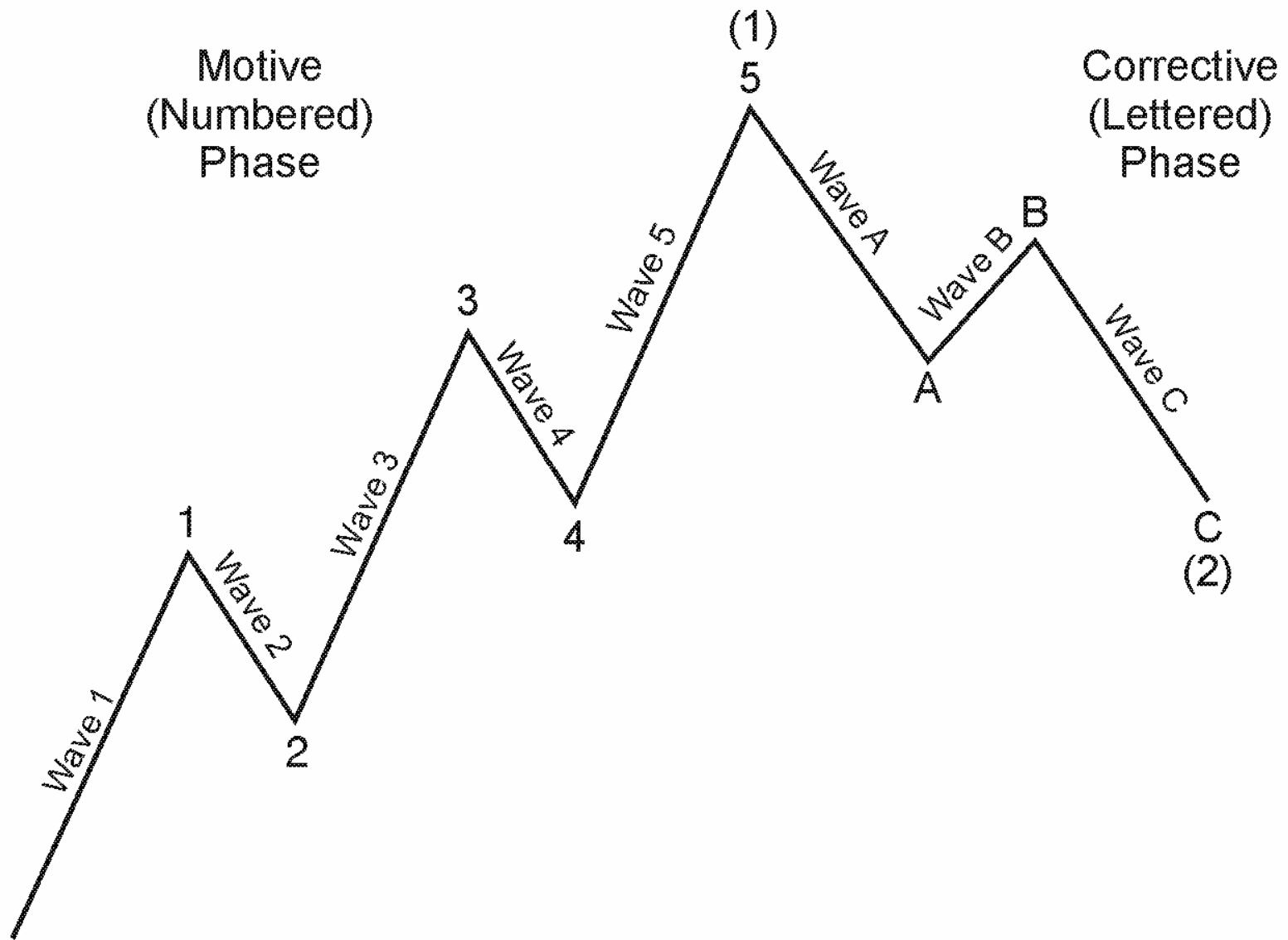


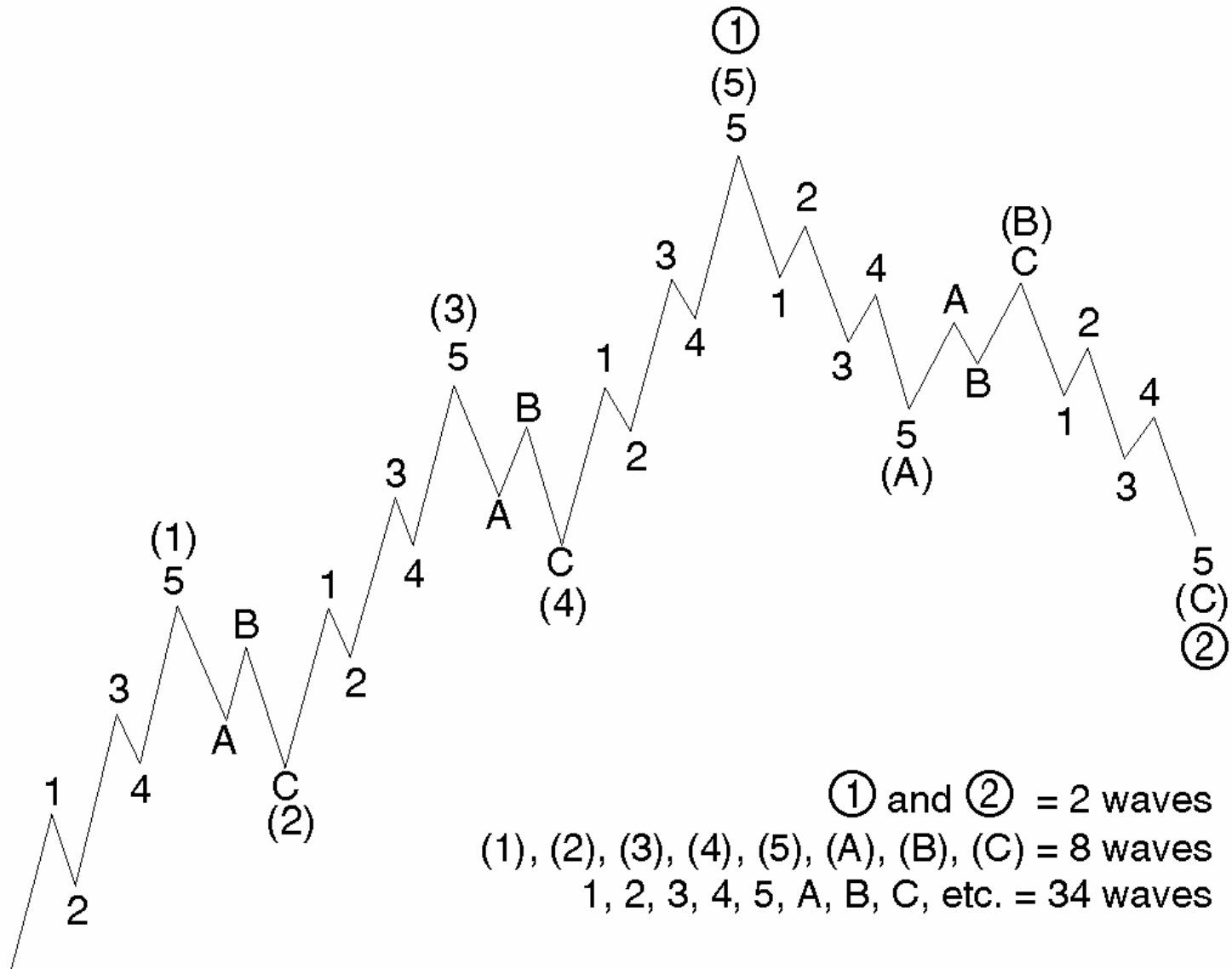
**Ralph Nelson Elliott
(1871 – 1948)**

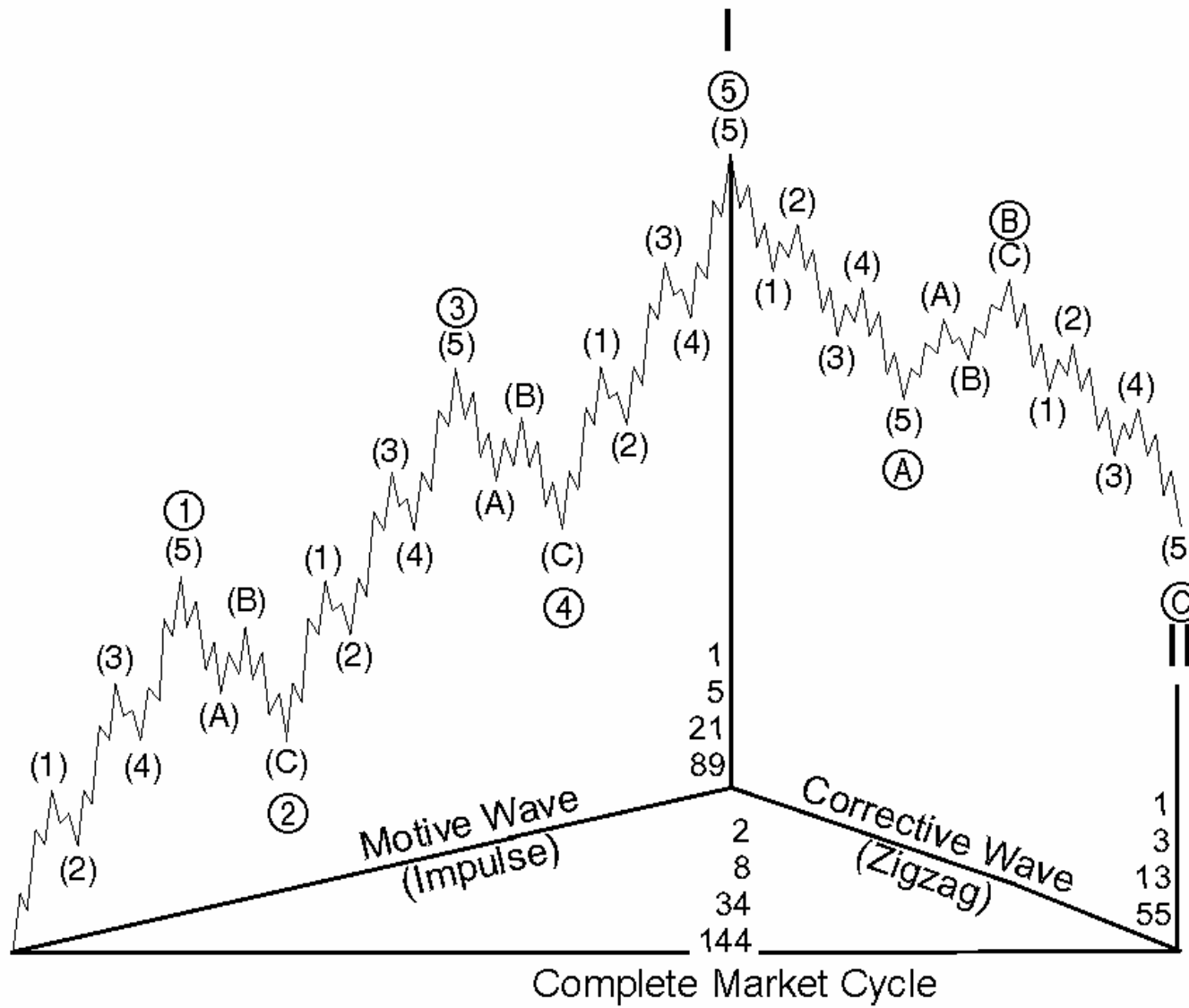
- **Crowd behavior trends and reverses in recognizable patterns, that he called waves.**
- **These structures link together to form larger versions of the same patterns and how those, in turn, become the building blocks for patterns of the next larger size and so on.**
- **In 1938, he coined this phenomenon The Wave Principle.**
- ***Nature's Law — The Secret of the Universe***

The Basic Pattern



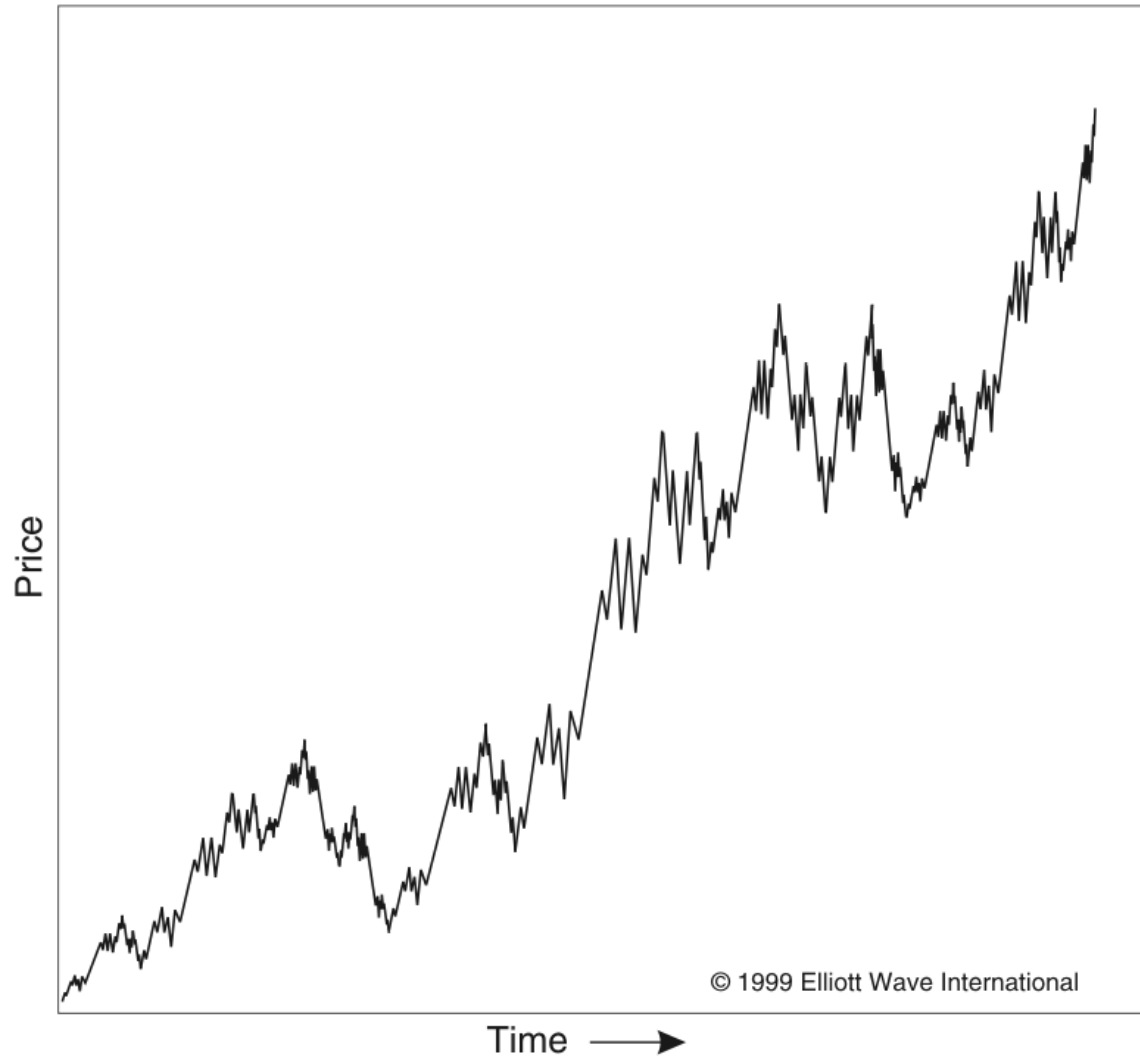


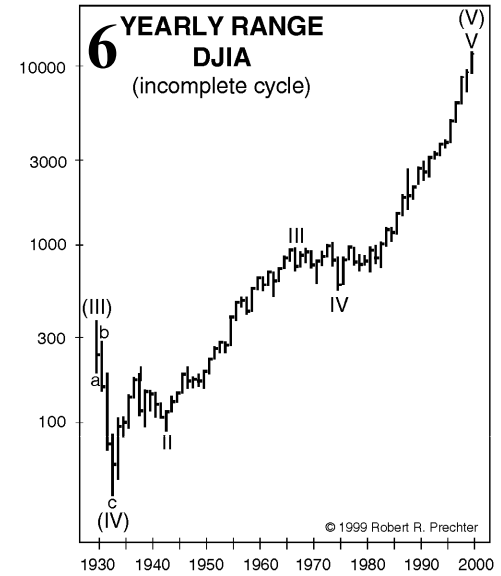
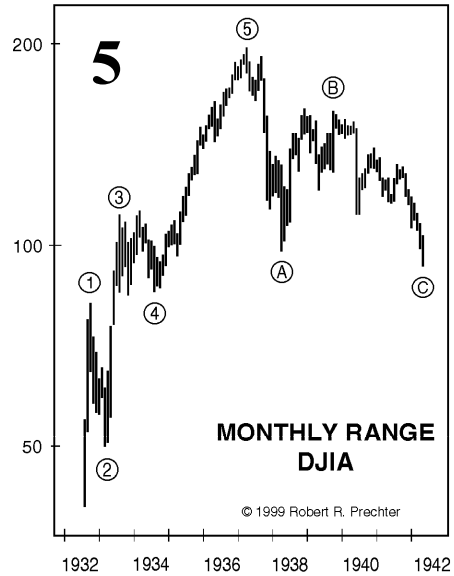
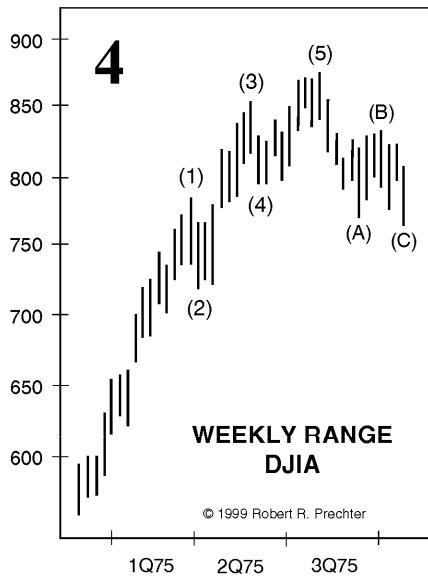
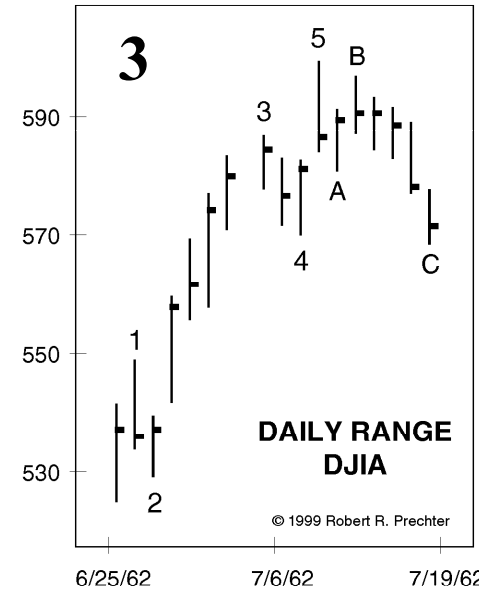
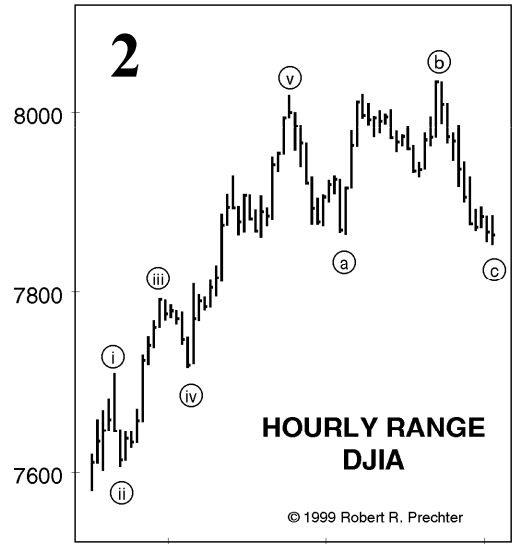
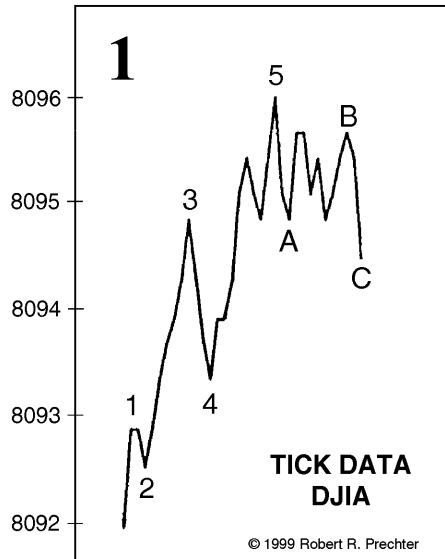


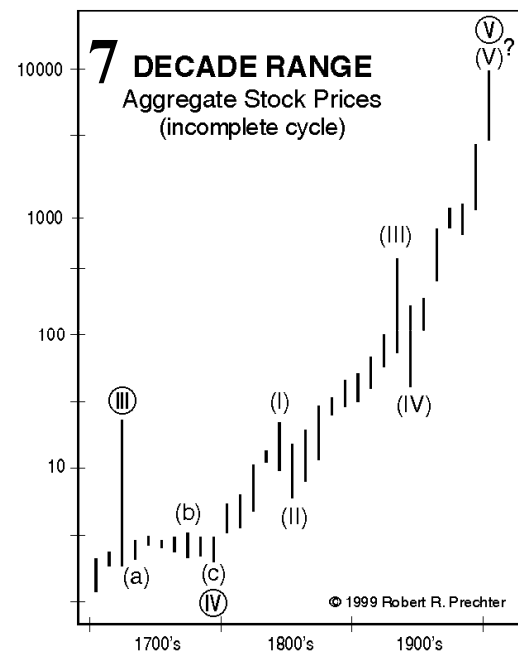
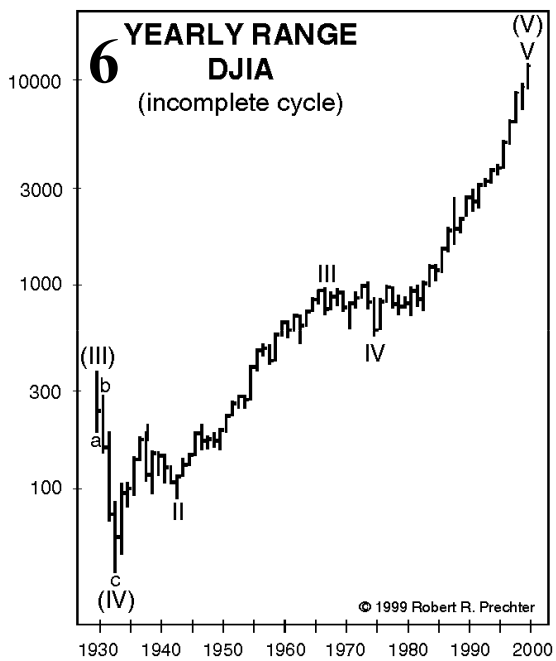
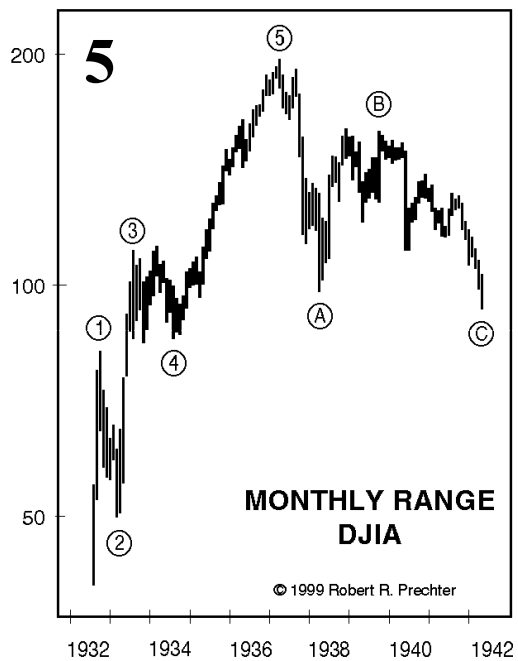


Wave Degree	5's With the Trend					3's Against the Trend		
1 Supermillennium	①	②	③	④	⑤	Ⓐ	Ⓑ	Ⓒ
2 Millennium	(1)	(2)	(3)	(4)	(5)	(A)	(B)	(C)
3 Submillennium	1	2	3	4	5	A	B	C
4 Grand Supercycle	Ⓘ	Ⓜ	Ⓝ	Ⓞ	Ⓟ	ⓐ	ⓑ	ⓒ
5 Supercycle	(I)	(II)	(III)	(IV)	(V)	(a)	(b)	(c)
6 Cycle	I	II	III	IV	V	a	b	c
7 Primary	①	②	③	④	⑤	Ⓐ	Ⓑ	Ⓒ
8 Intermediate	(1)	(2)	(3)	(4)	(5)	(A)	(B)	(C)
9 Minor	1	2	3	4	5	A	B	C
10 Minute	⓪	⓫	⓬	⓭	⓮	ⓐ	ⓑ	ⓒ
11 Minuette	(i)	(ii)	(iii)	(iv)	(v)	(a)	(b)	(c)
12 Subminuette	i	ii	iii	iv	v	a	b	c
13 Micro	①	②	③	④	⑤	Ⓐ	Ⓑ	Ⓒ
14 Submicro	(1)	(2)	(3)	(4)	(5)	(A)	(B)	(C)
15 Miniscule	1	2	3	4	5	A	B	C

A More Realistic Wave Depiction







The Wave Principle

Mankind's progress (popularly measured by stock market valuation) is not a straight line, random or cyclical.

Growth and thereby social systems are moving in a pattern consisting of five waves up and three waves down.

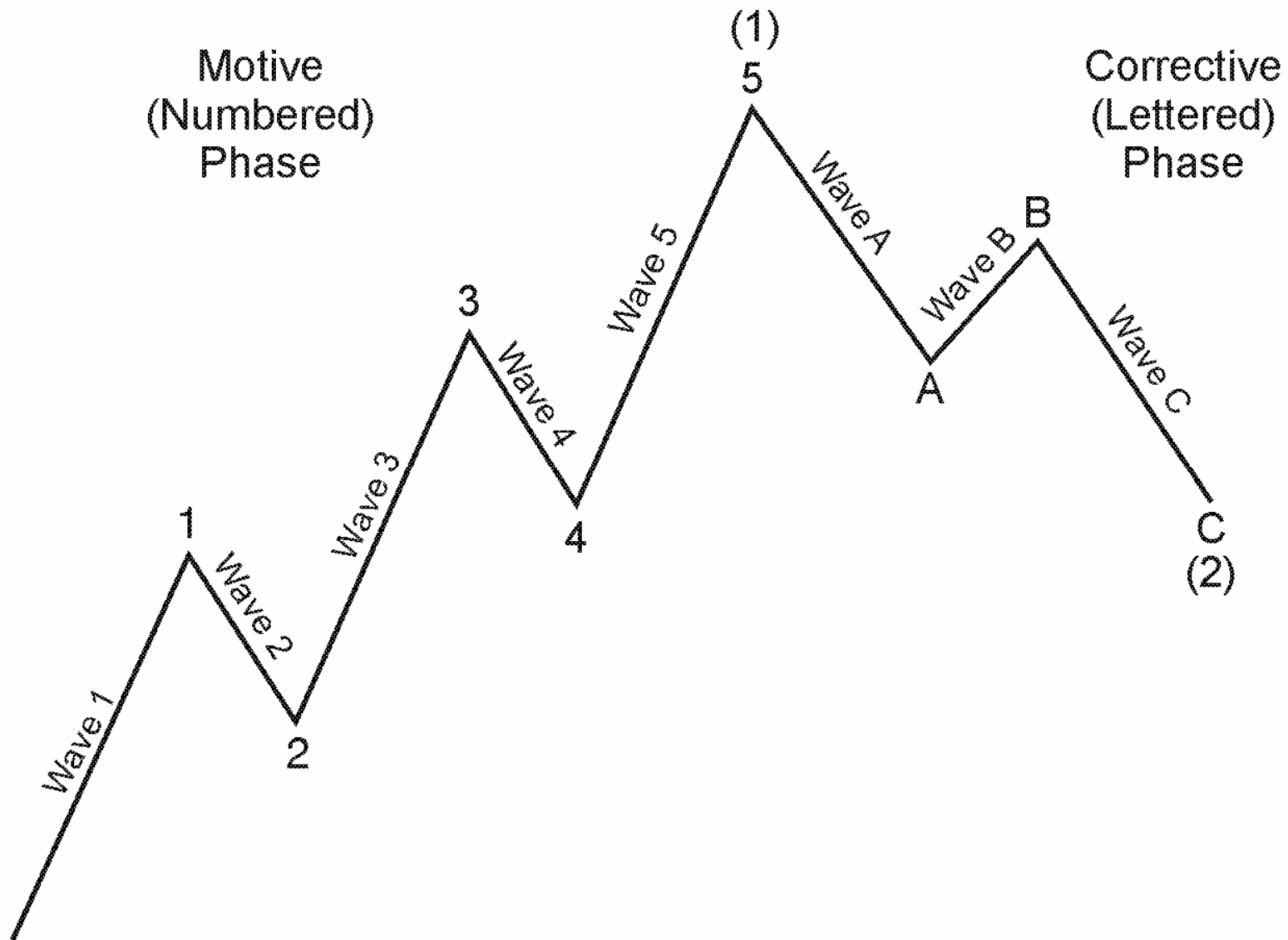
This pattern reflects the alternation of growth and non-growth or decline.

The Wave Principle

Predict Market Direction

Identify turning Points

Provide Guidance for Entering and Exiting Positions



MOTIVE WAVES

Key Characteristics

- Five-wave structures, numbered 1-5
- In the direction of the main trend of one larger degree
- Wave 2 cannot retrace more than 100% of wave 1
- Wave 3 can never be the shortest and is often the longest

MOTIVE WAVES

Five-Wave Structures

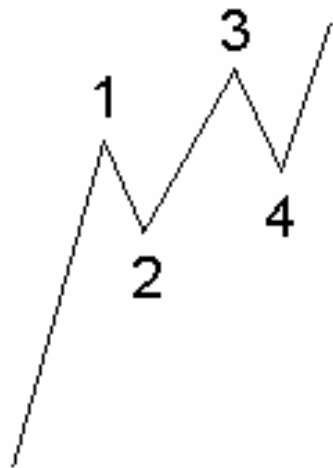
- Impulse
 1. Extensions
 2. Truncations
- Diagonal Triangles

IMPULSE WAVES

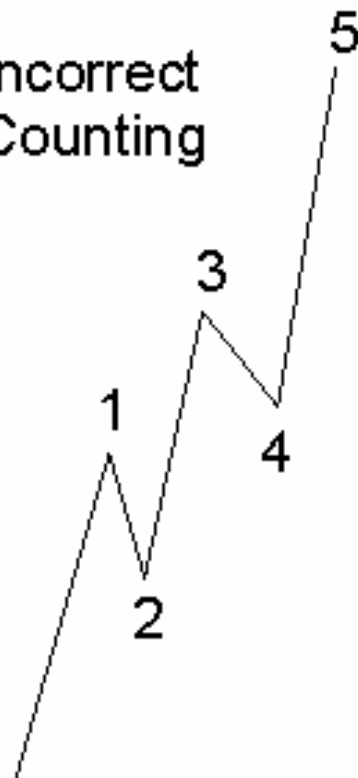
Key Characteristics

- Wave 4 never enters the price territory of wave 1.
- Actionary waves 1, 3 and 5 are motive waves.
- Wave 3 is always an impulse wave.

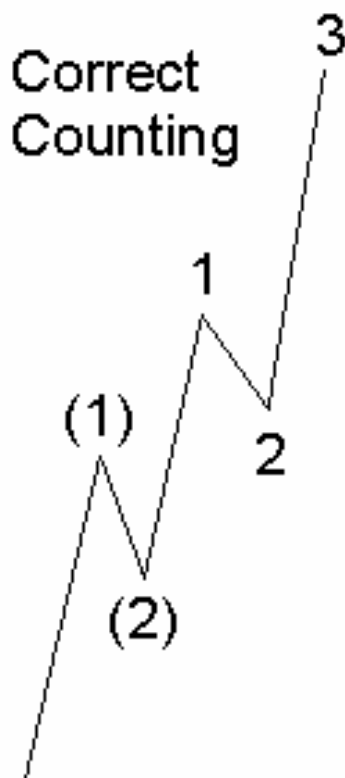
Incorrect
Counting



Incorrect
Counting



Correct
Counting



© 1978-1998 *Elliott Wave Principle*

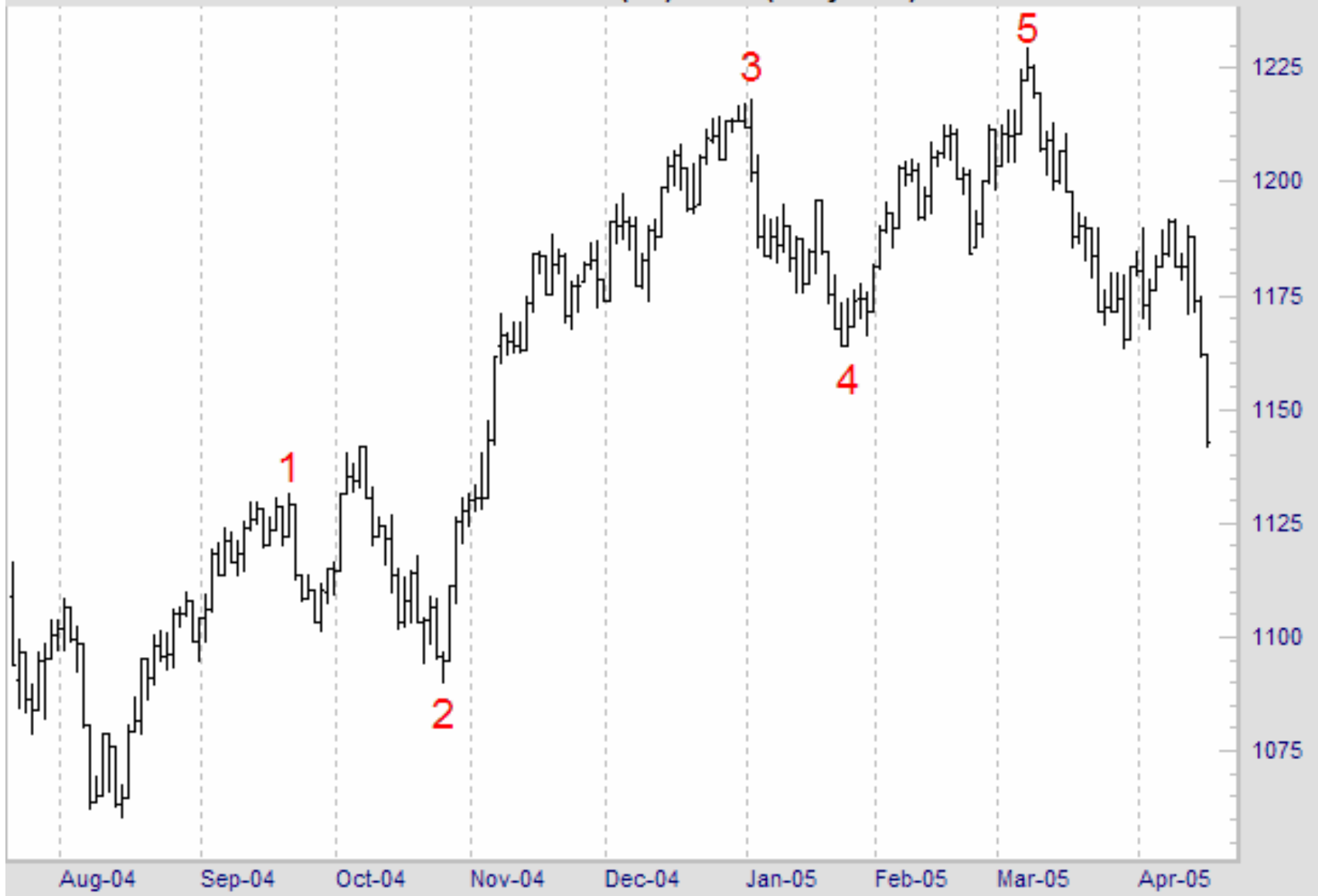
SP-099: S&P 500 Index (Pit) Cash (Daily bars)

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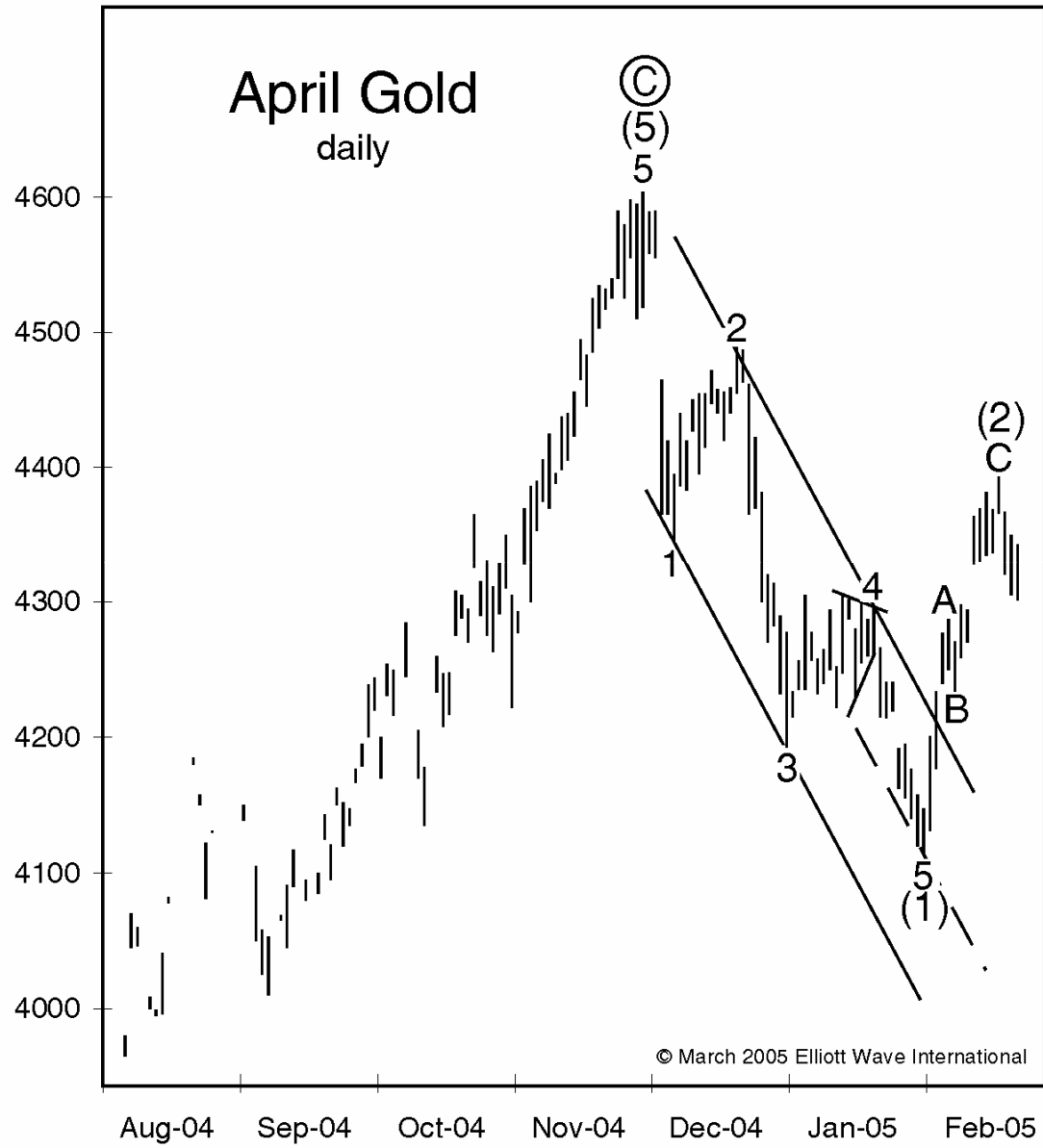


SP-099: S&P 500 Index (Pit) Cash (Daily bars)

www.GenesisFT.com







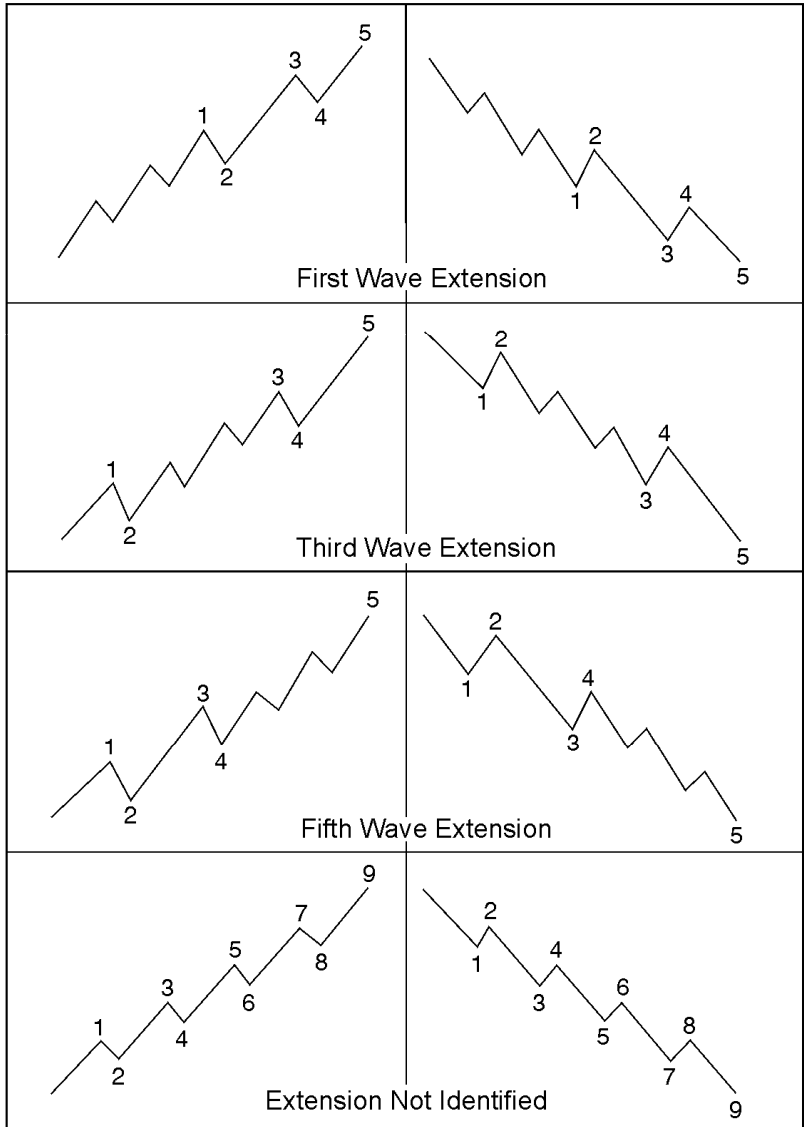
EXTENSIONS

Key Characteristics

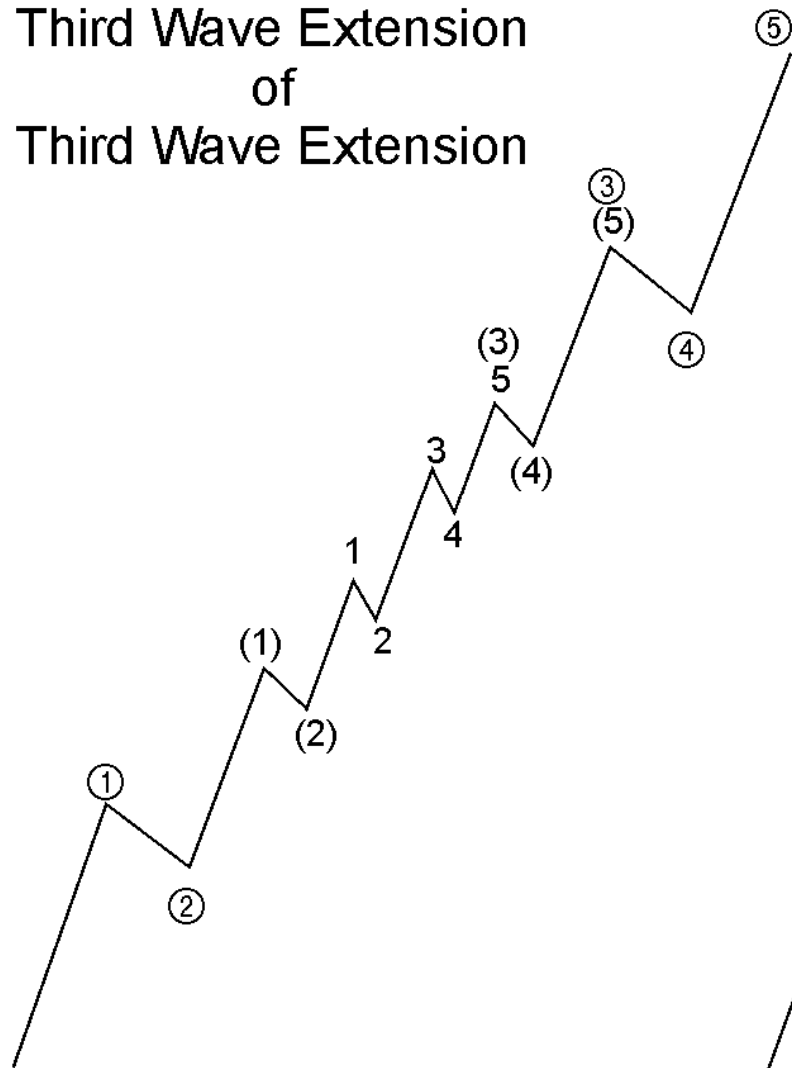
- Elongated impulse wave
- Appears in either wave 1, 3 or 5
- Often seen in wave 3 for the stock market
- Often seen in wave 5 in commodities

Bull Market

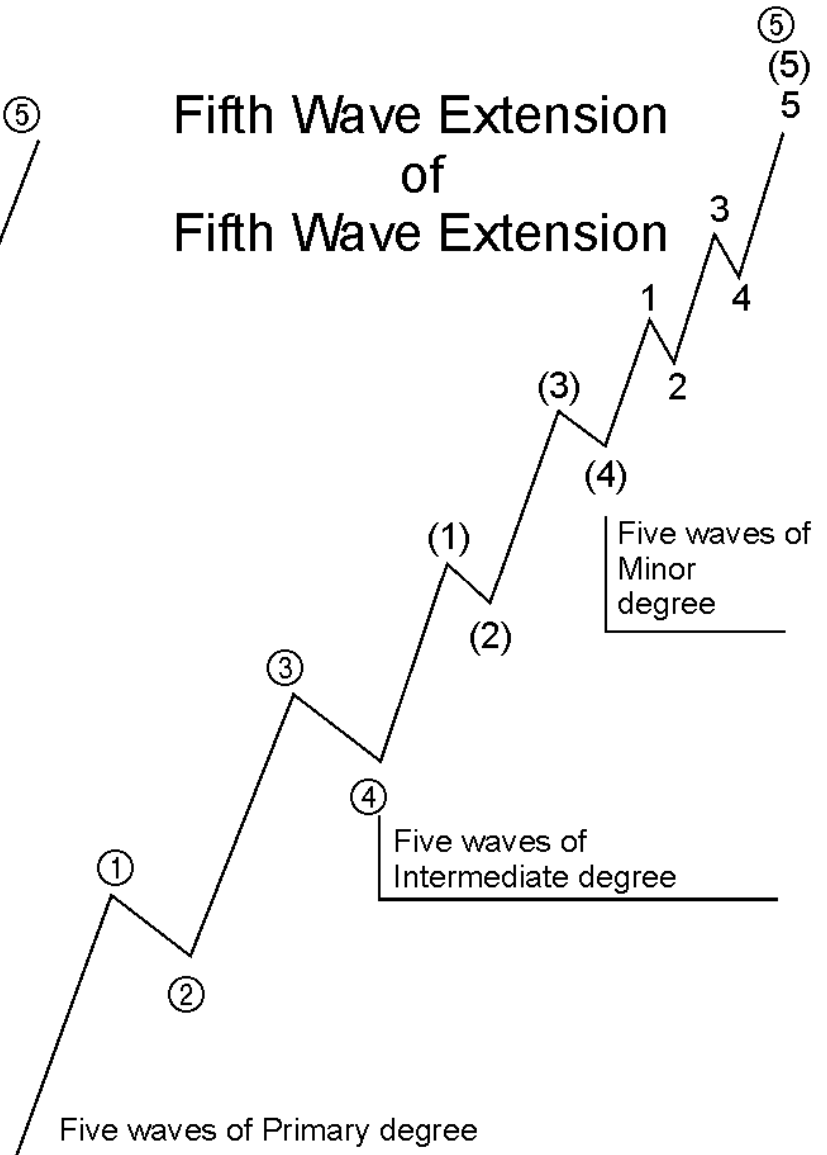
Bear Market

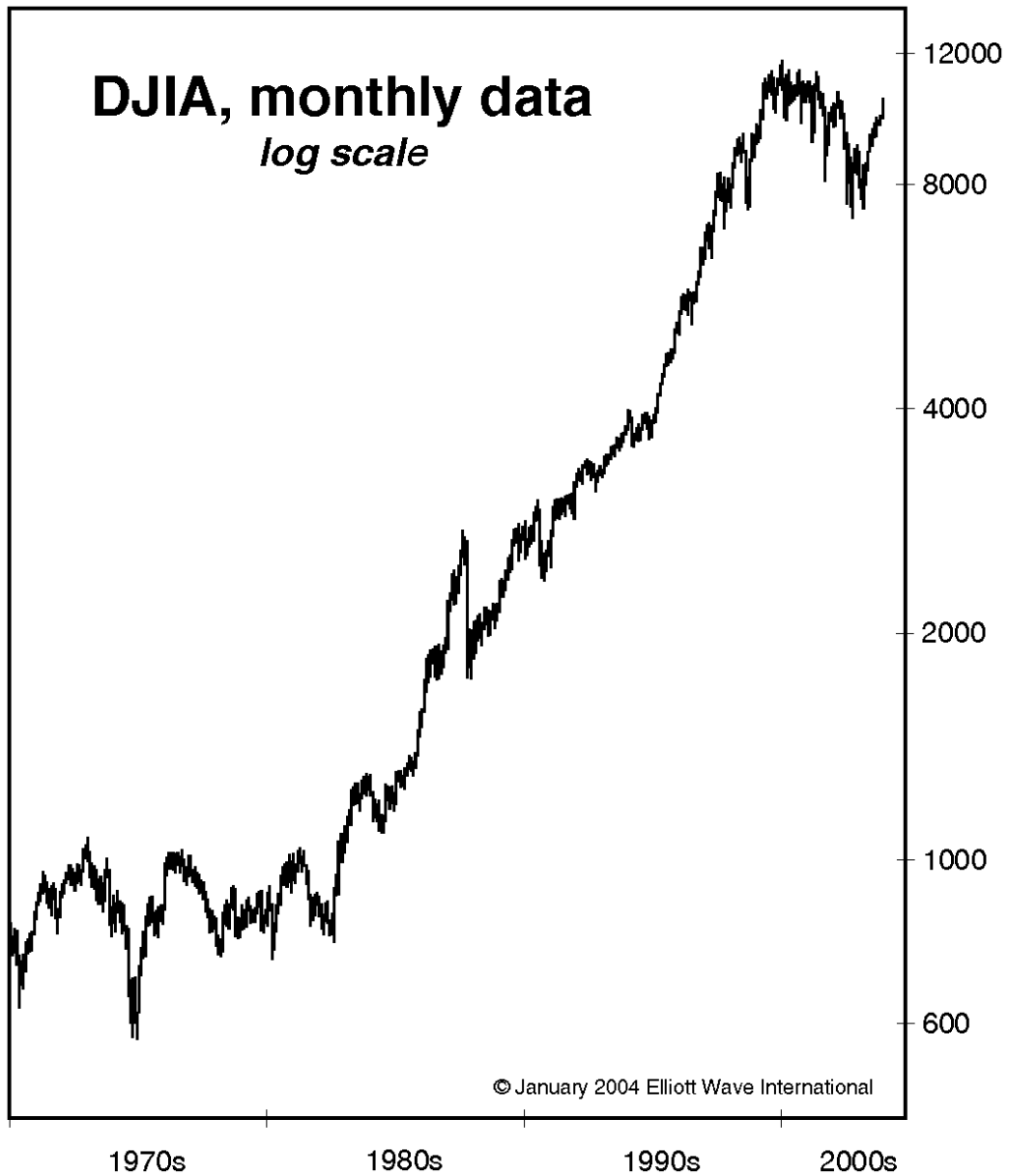


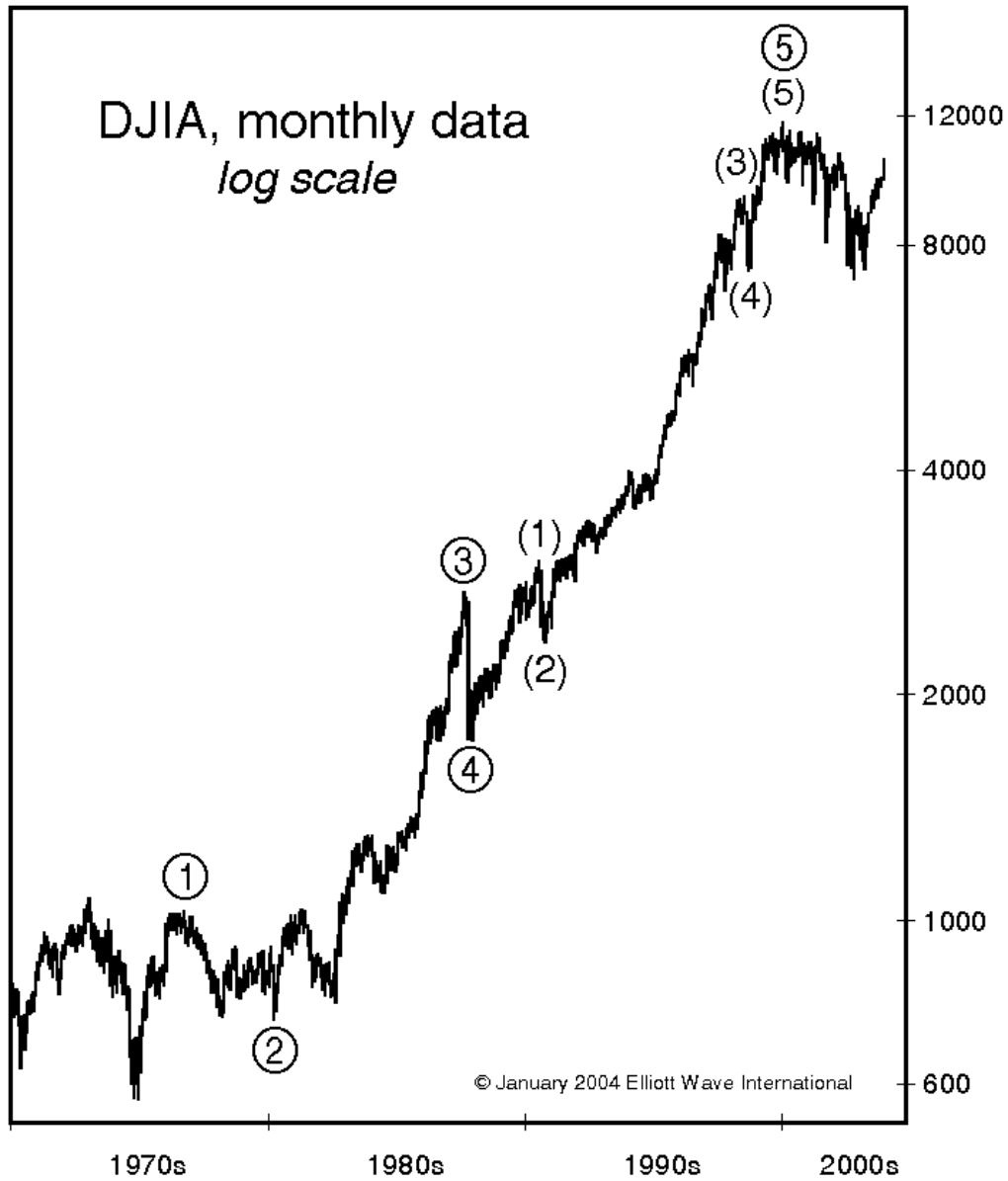
Third Wave Extension of Third Wave Extension

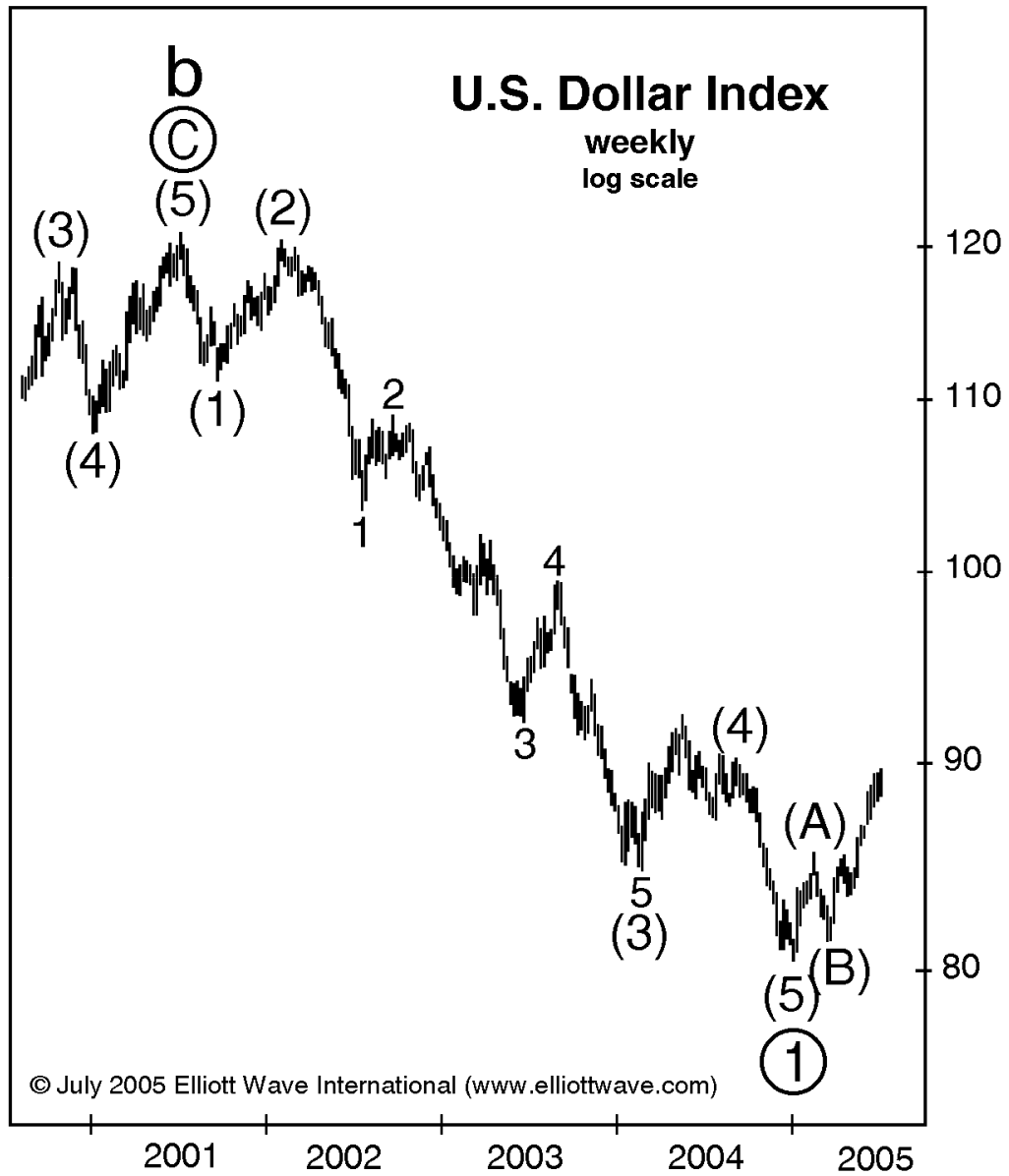


Fifth Wave Extension of Fifth Wave Extension





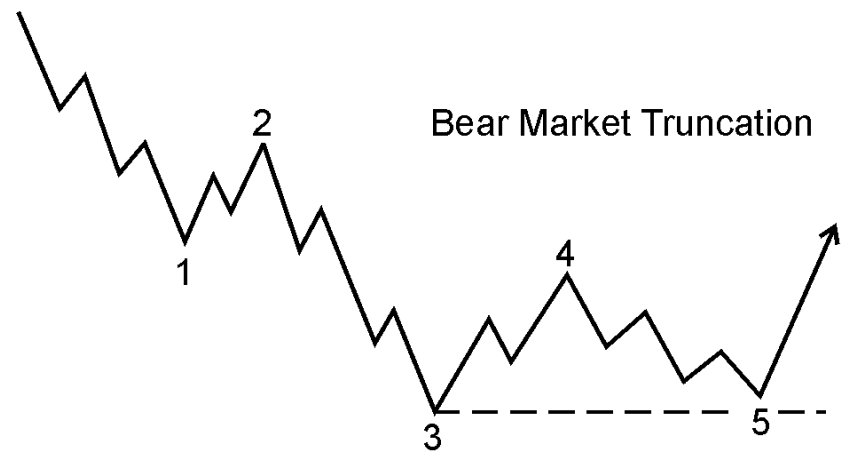
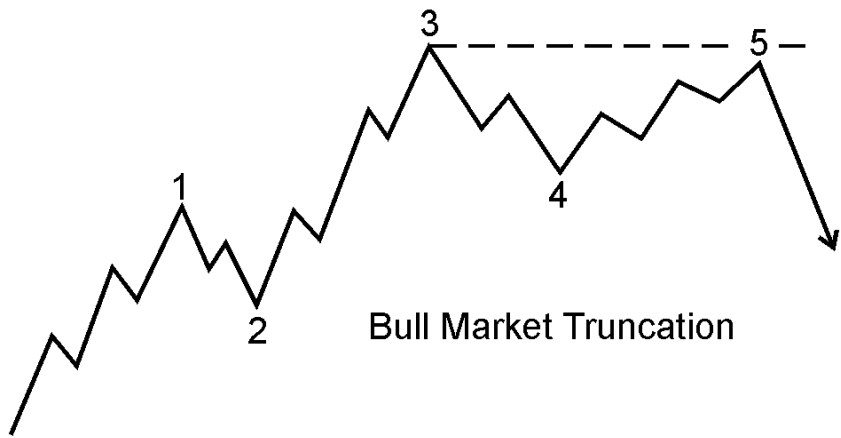


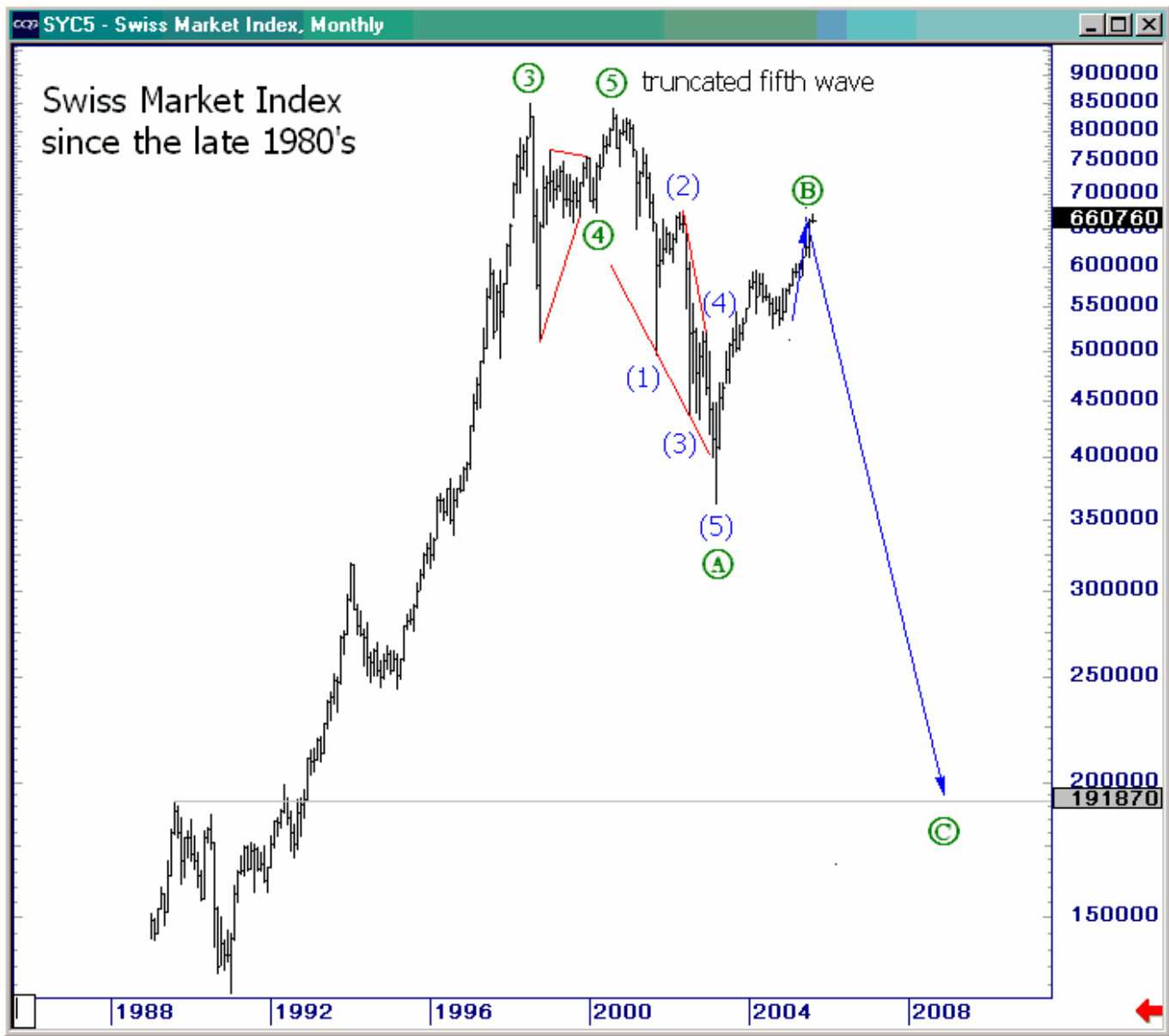


TRUNCATIONS

Key Characteristics

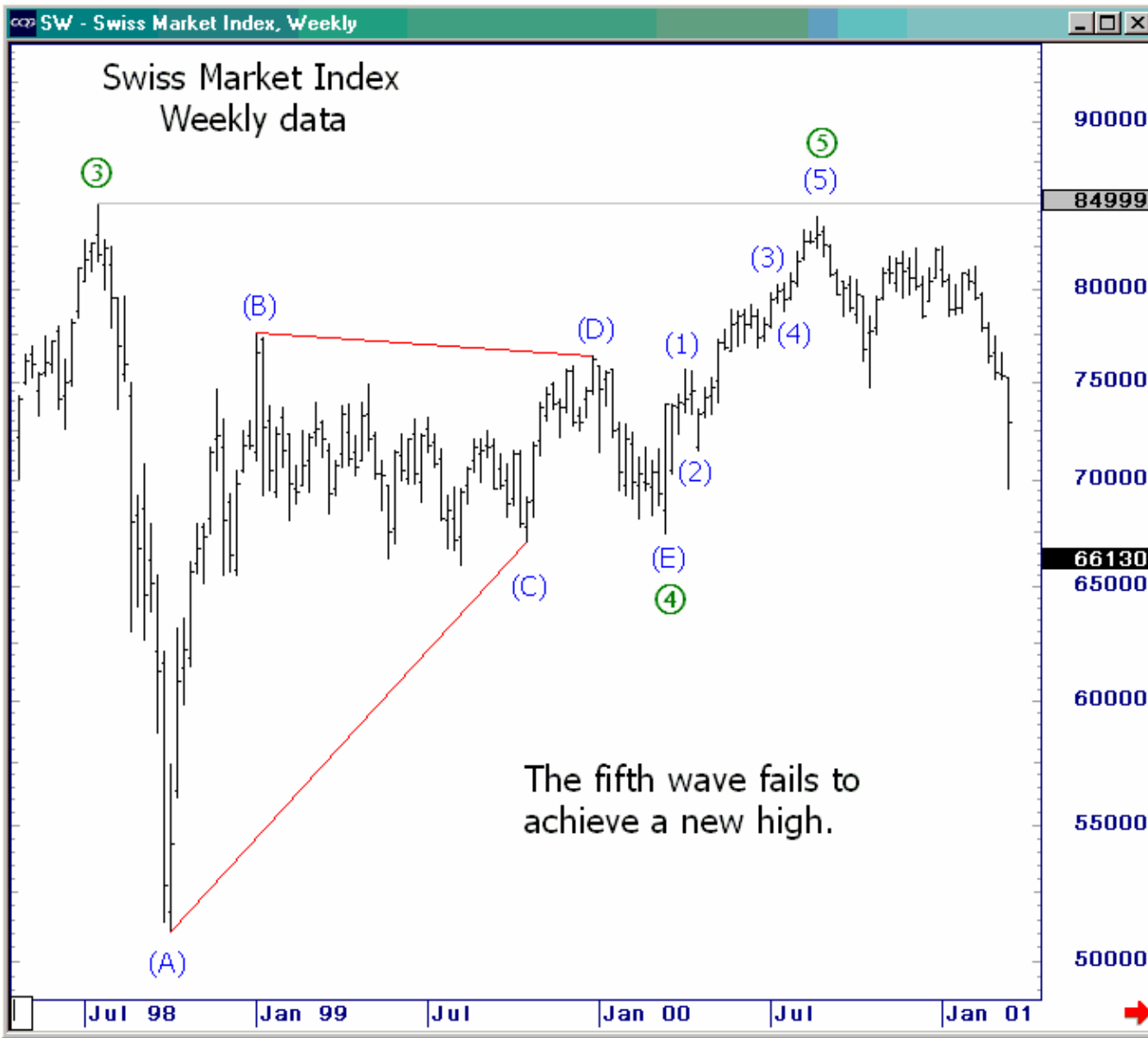
- Wave 5 does not exceed the end of wave 3
- Contains necessary five subwaves
- Often occurs after a strong third wave





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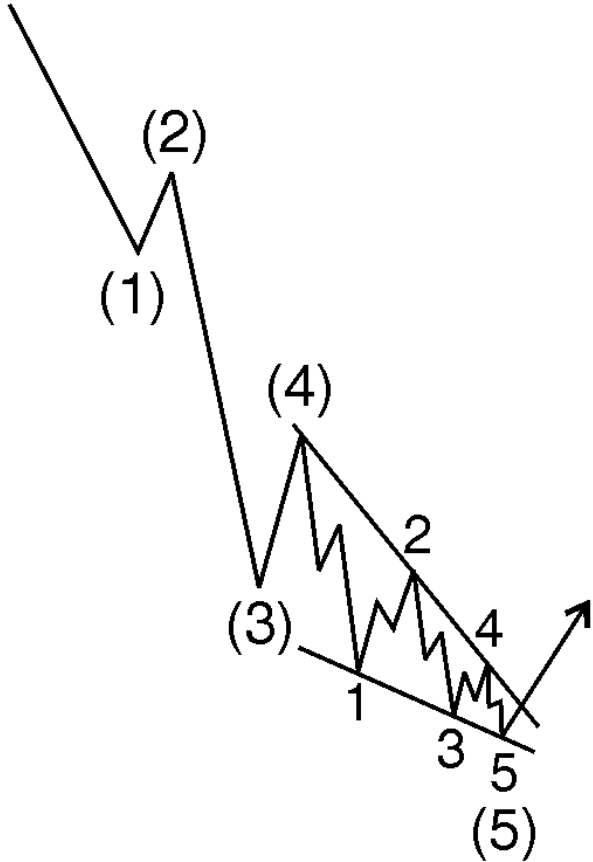
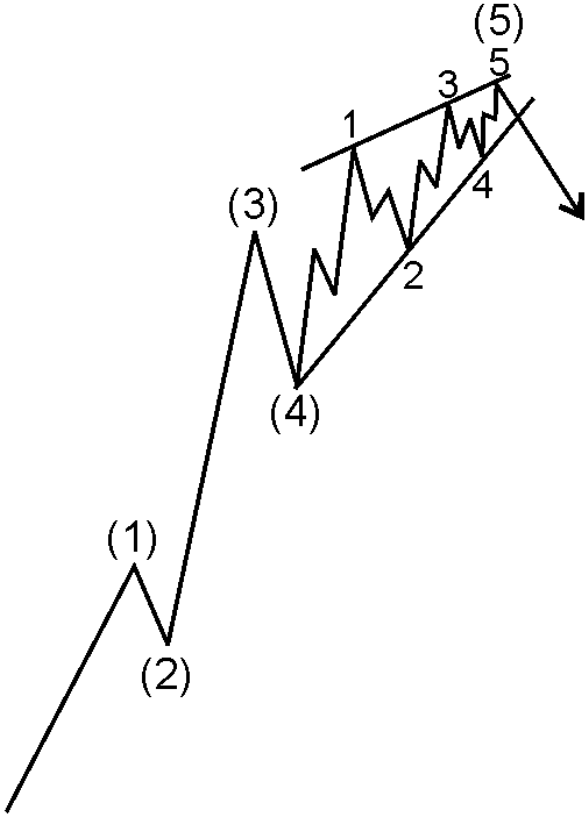
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DIAGONAL TRIANGLES

Key Characteristics

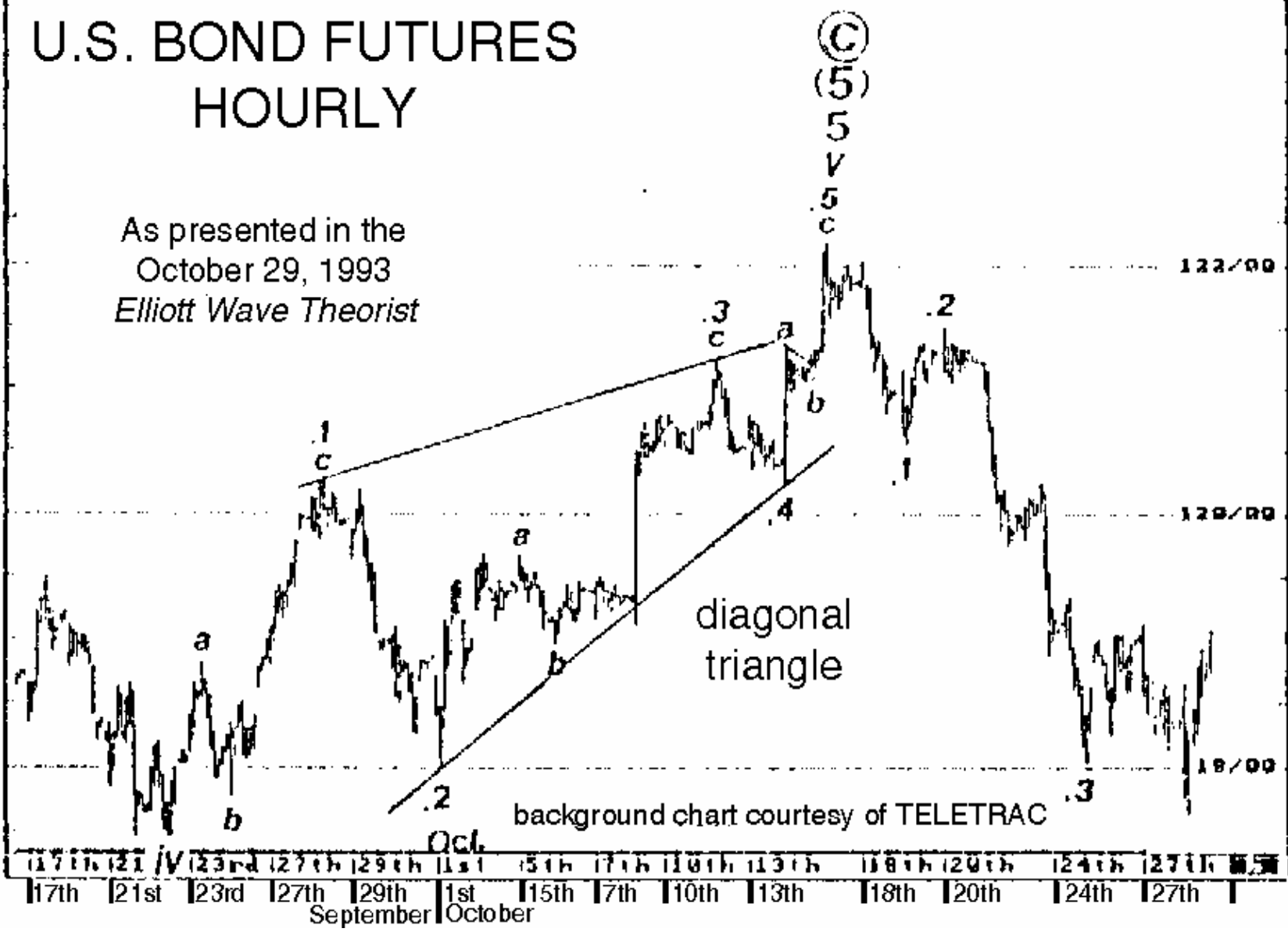
- Wave 4 almost always moves into the price territory of wave 1
- Waves 1, 3 and 5 are composed of three subwaves, not five
- Found at termination points of larger pattern, indicating exhaustion of larger pattern
- Normally has wedge shape within two converging lines

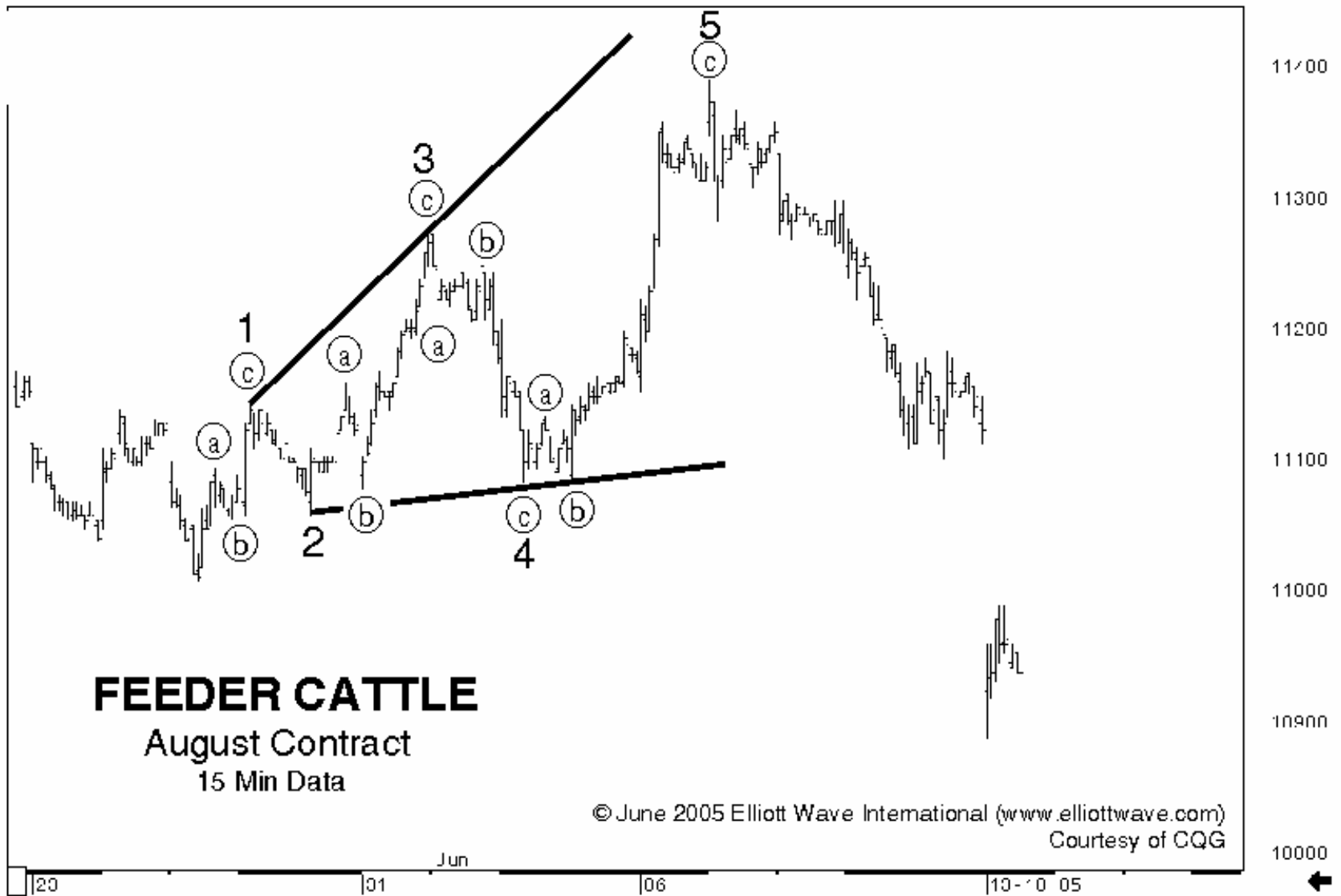
Diagonal Triangles

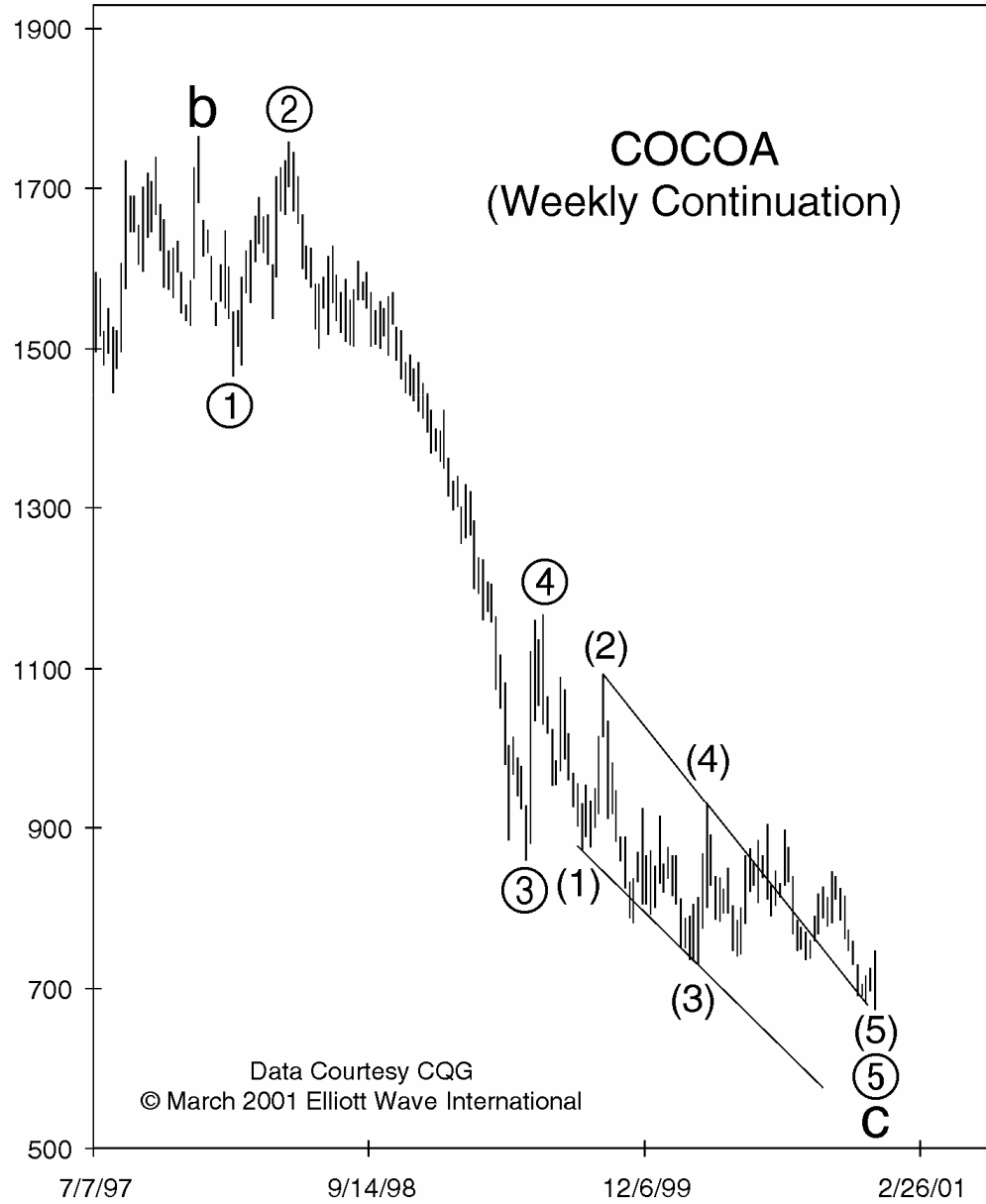


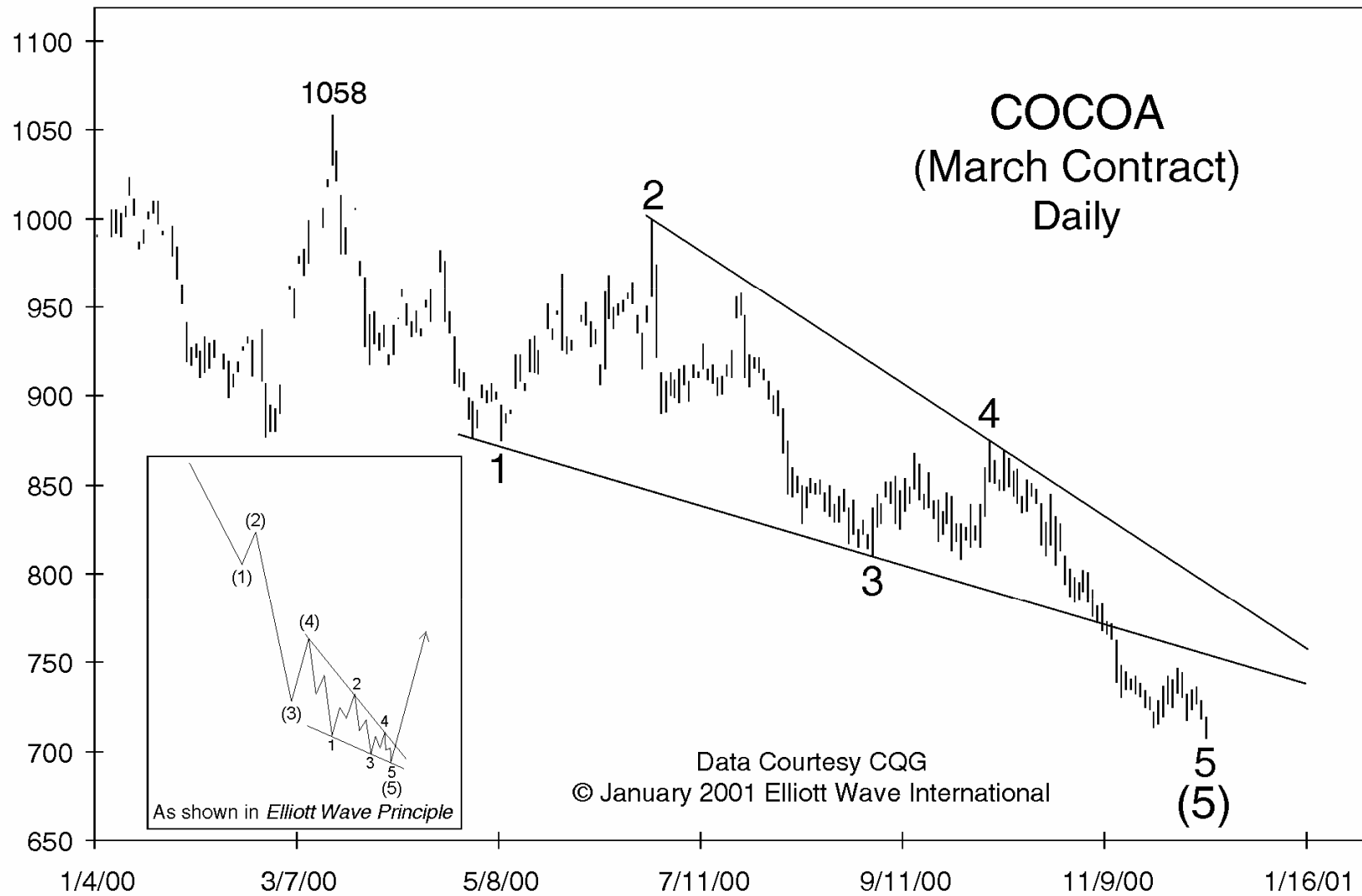
U.S. BOND FUTURES HOURLY

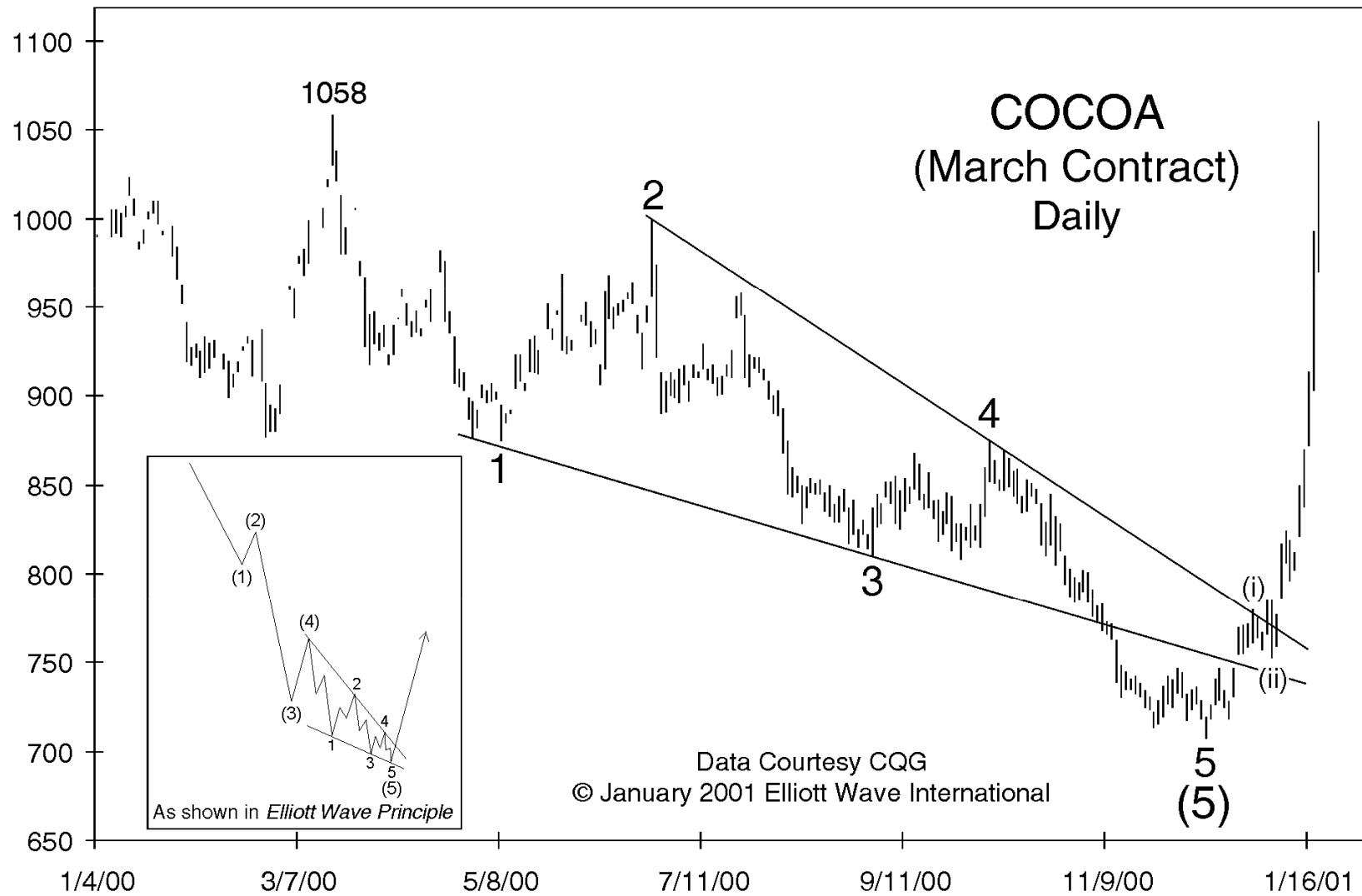
As presented in the
October 29, 1993
Elliott Wave Theorist

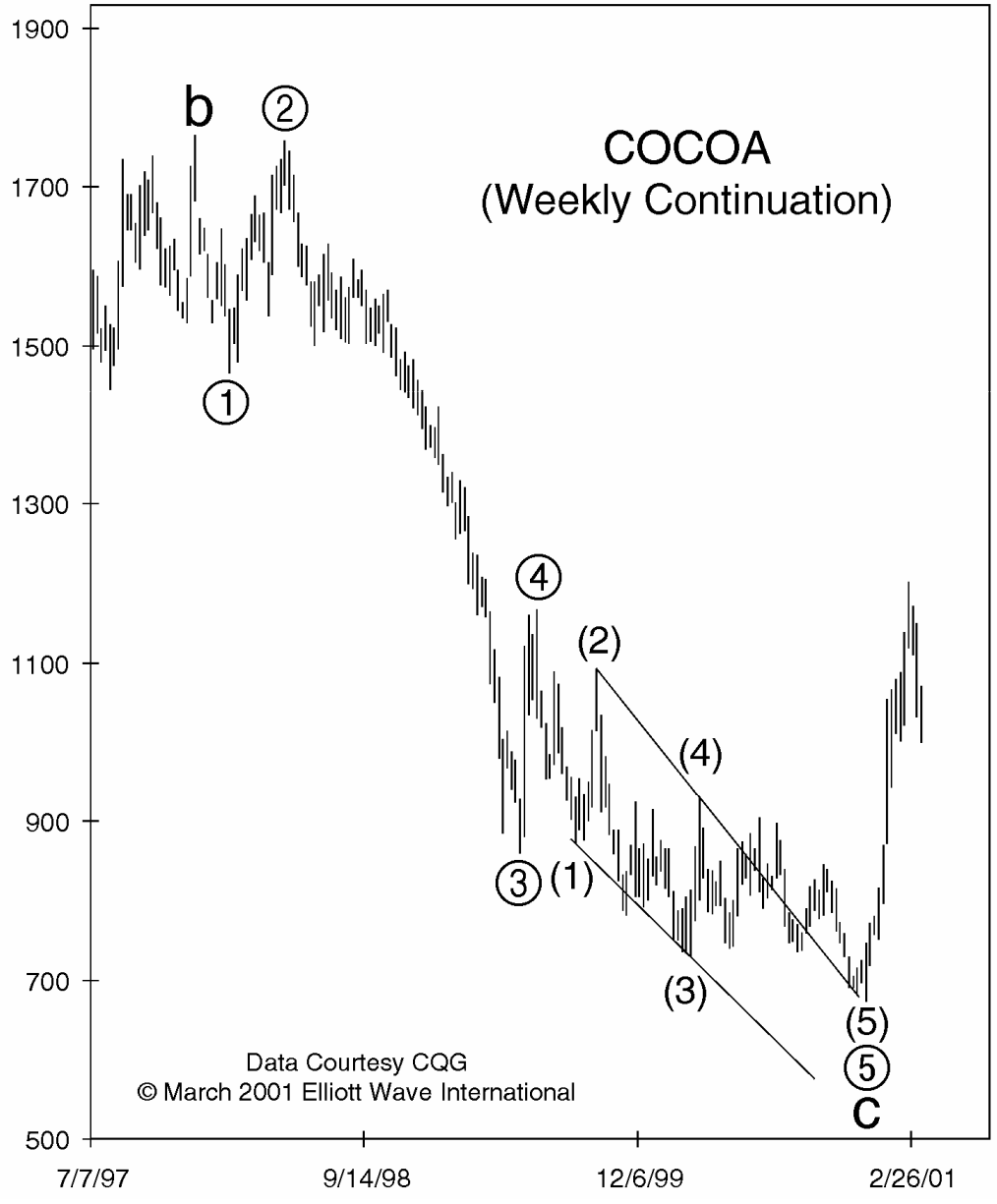












SUMMARY

The Wave Principle = Graphic of Mass Psychology

Motive Waves = 5 Wave Structures, Main Trend of One Larger Degree

Types of Motive Waves = Impulse, Diagonal Triangle

Impulse: Waves 1, 3, 5 = 5 Impulse Subwaves

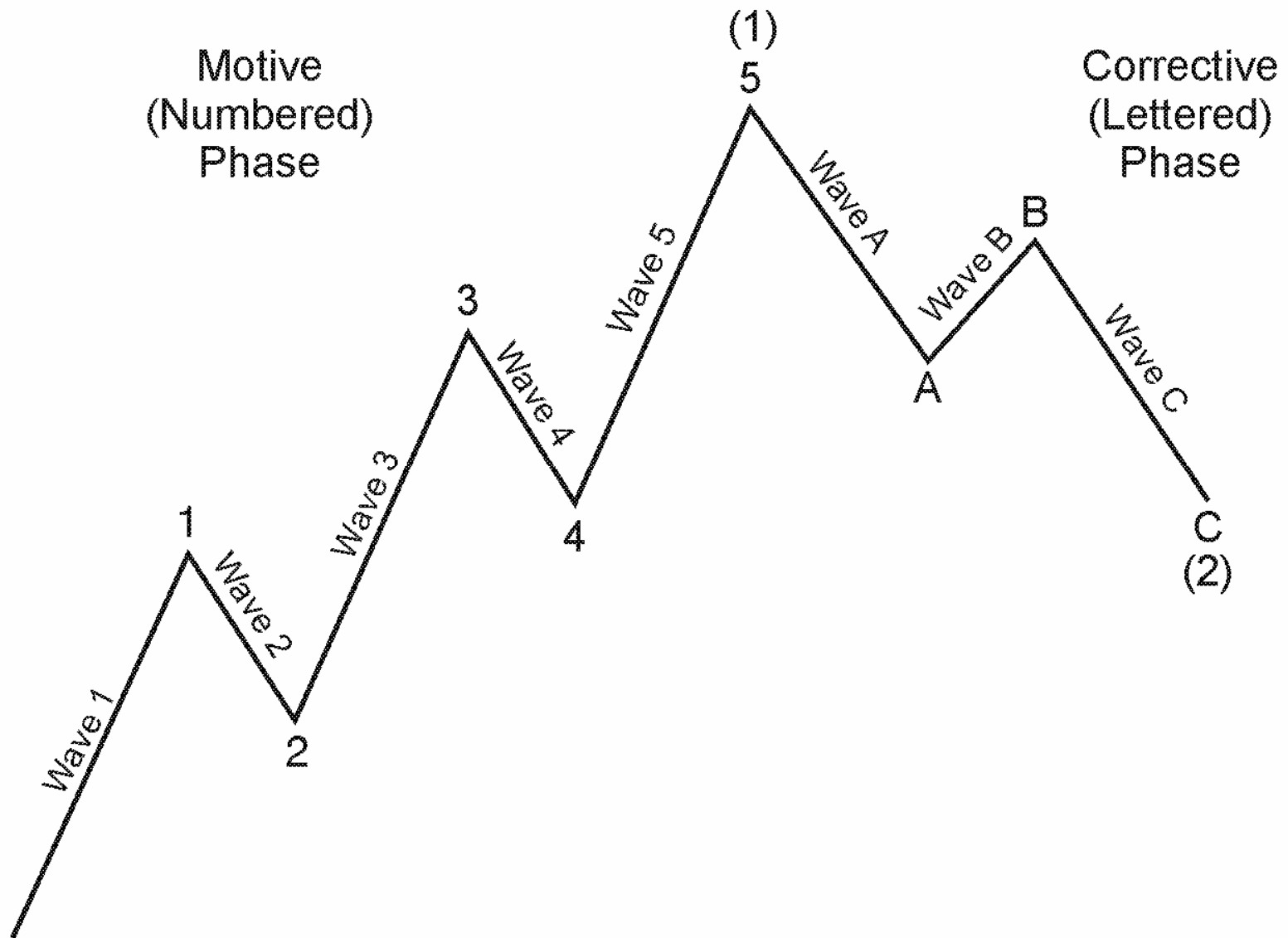
(Extensions, Truncations)

Wave 4 ≠ Price Territory of Wave 1

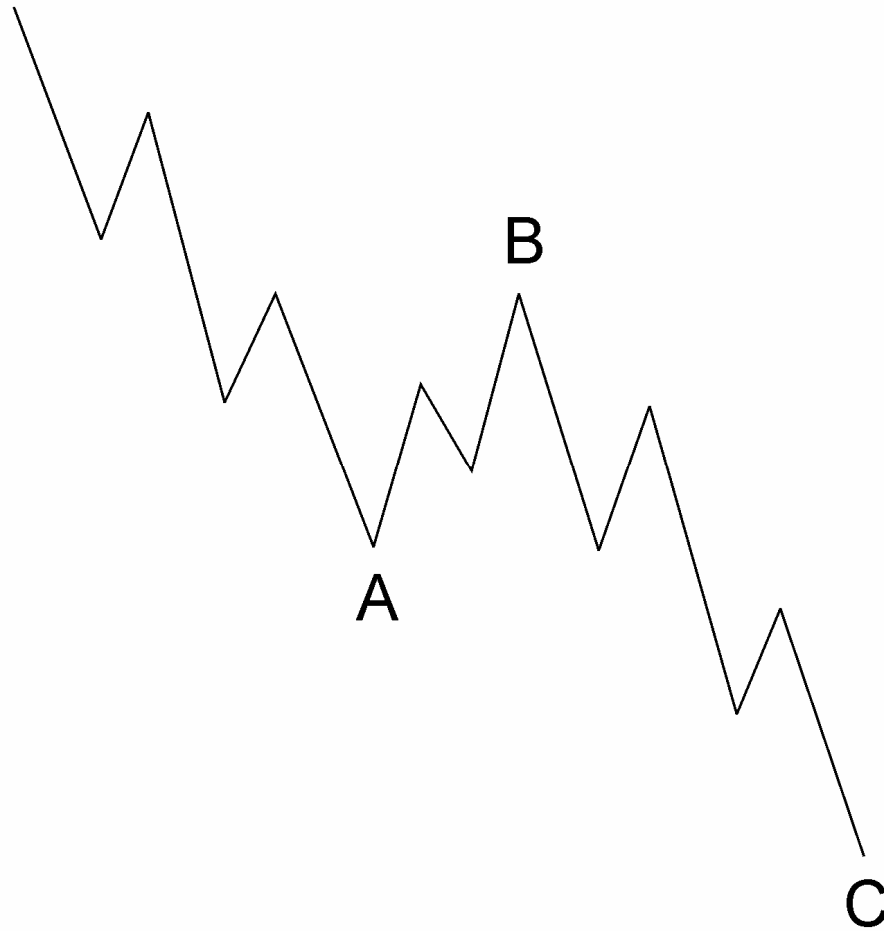
Diagonal Triangle: Waves 1, 3, 5 = 3 Subwaves

Wave 4 = Price Territory of Wave 1

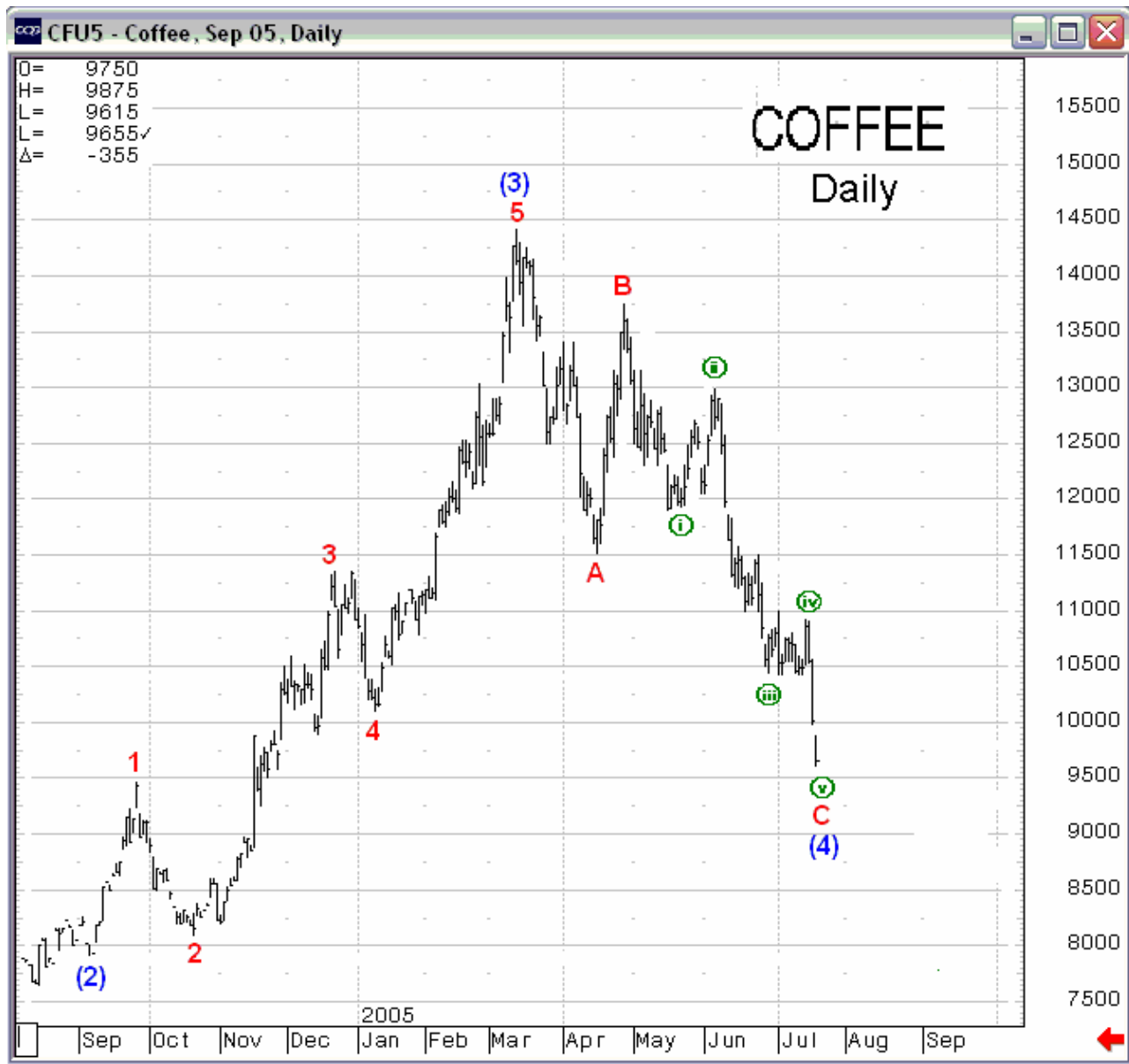
Signal = Imminent Major Trend Reversal



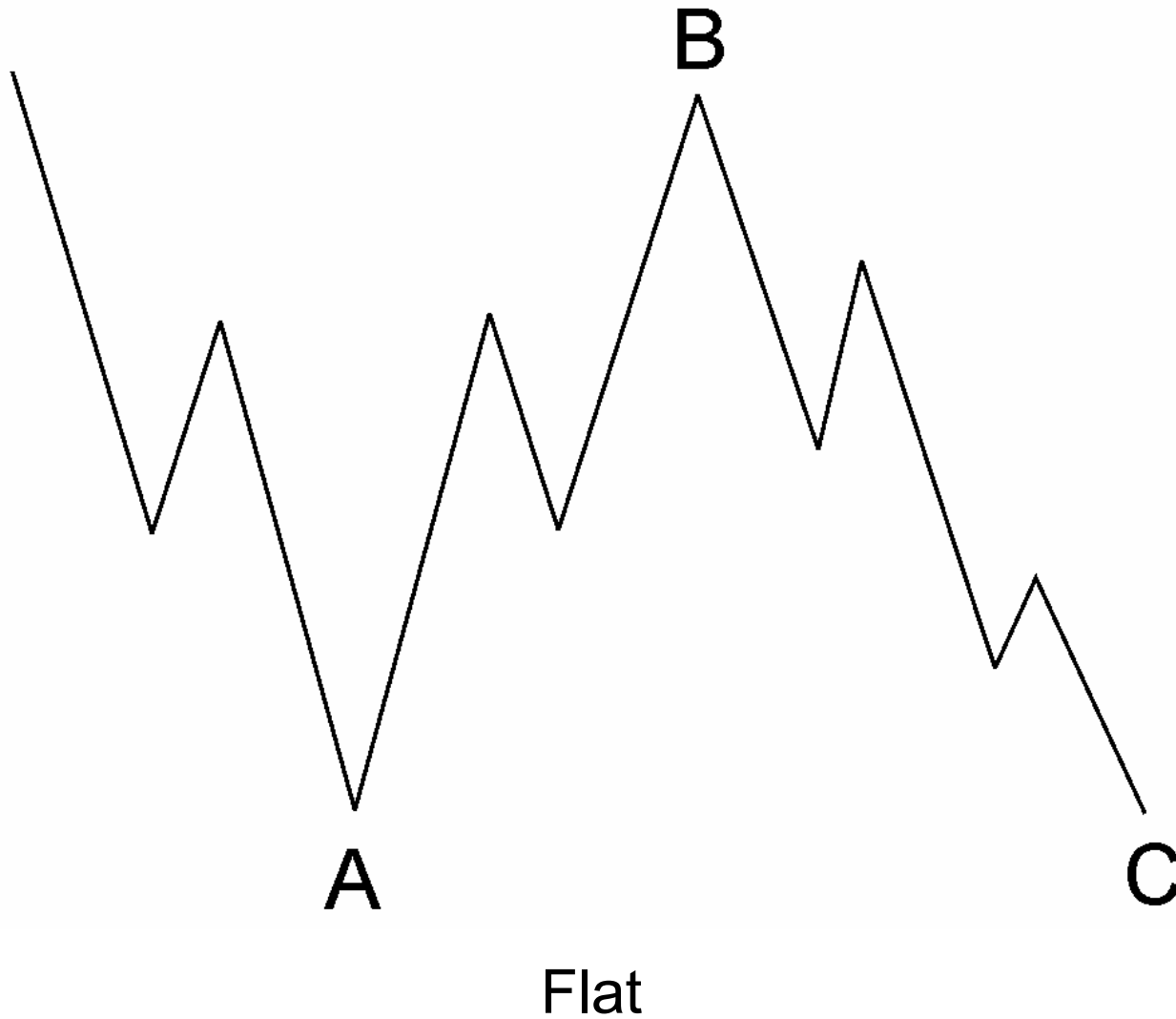
Characteristics of Corrective Waves



Zigzag

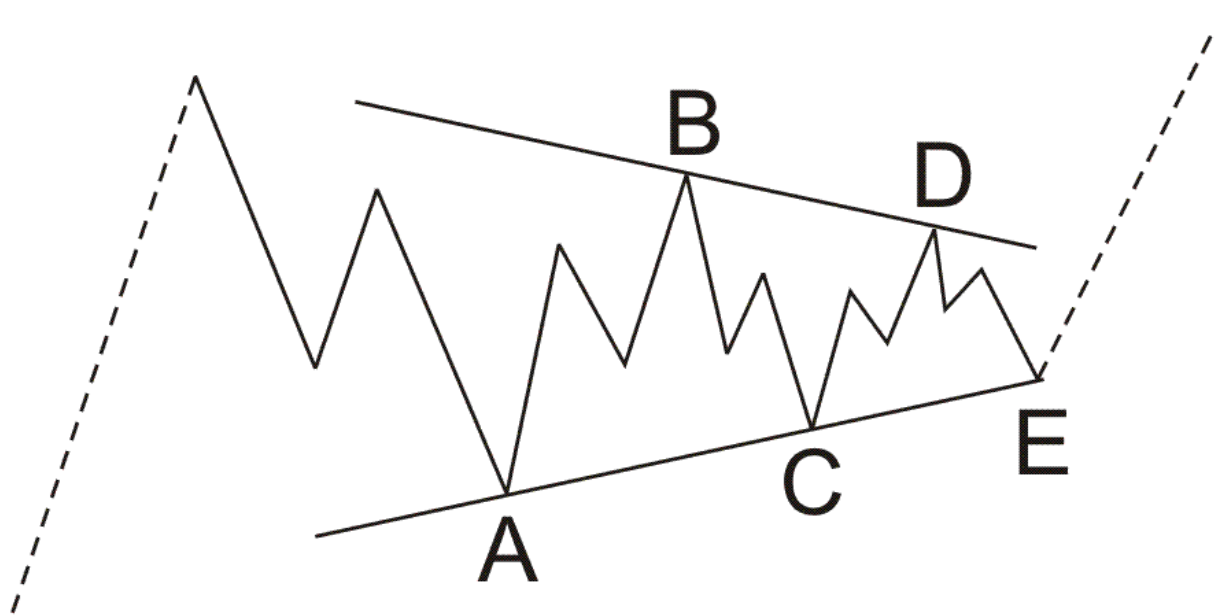


Characteristics of Corrective Waves



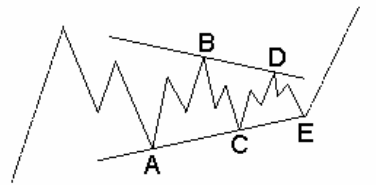
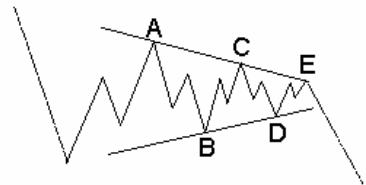
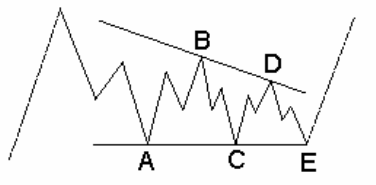
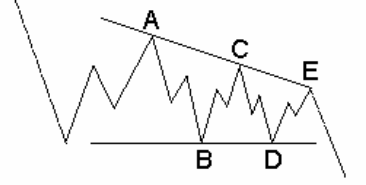
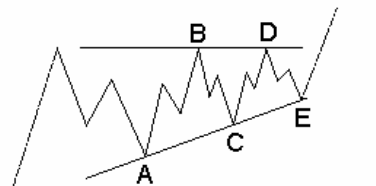
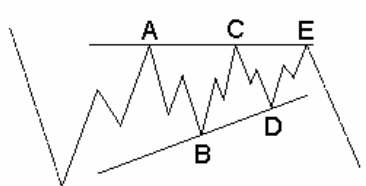
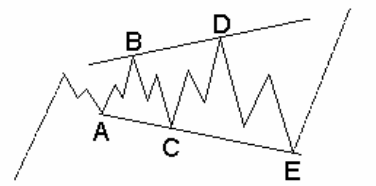
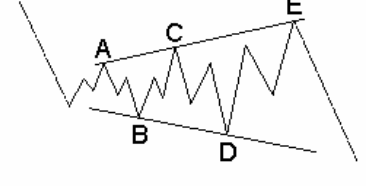


Characteristics of Corrective Waves



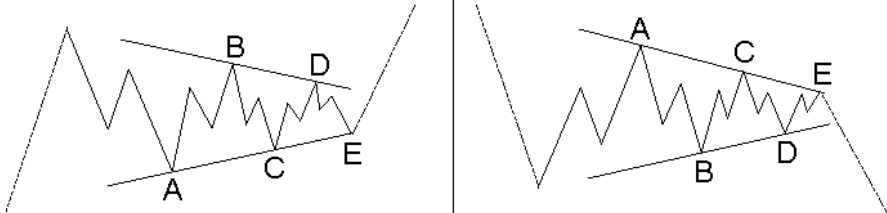
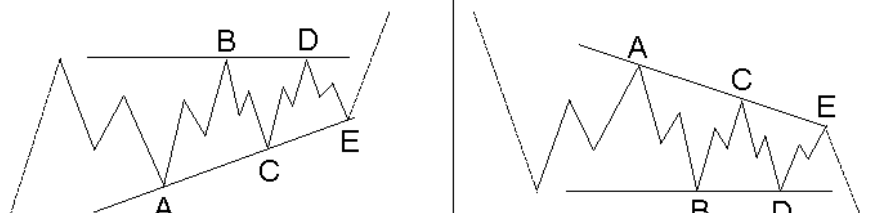
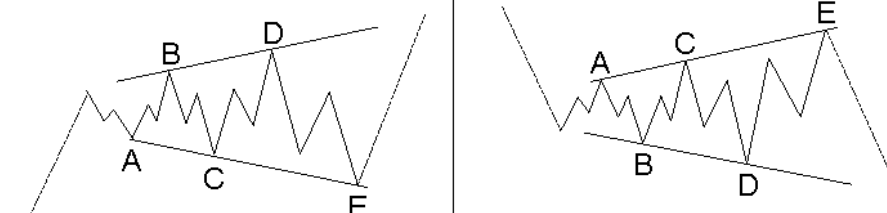
Triangle

Horizontal Triangles

	Bull Market	Bear Market
Contracting Triangles	SYMMETRICAL (Top declining, bottom rising)	
		
	DESCENDING (Top declining, bottom flat)	
		
Expanding	ASCENDING (Top flat, bottom rising)	
		
	REVERSE SYMMETRICAL (Top rising, bottom declining)	
		

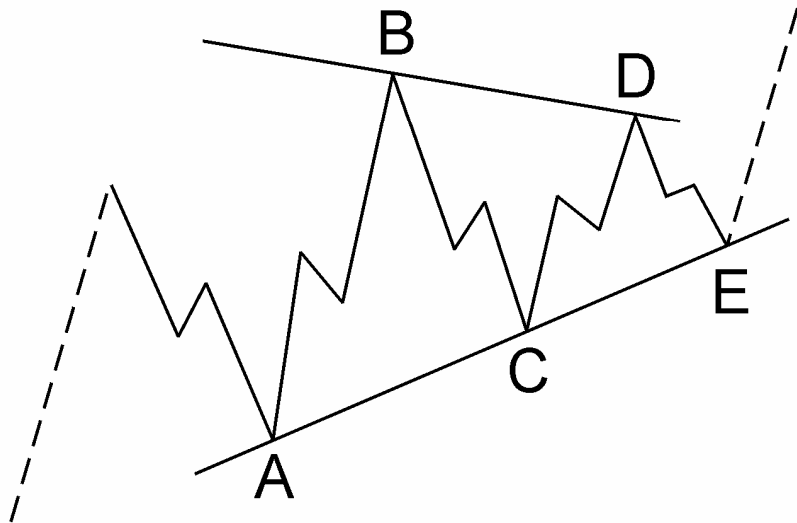
Barrier Triangles

Proper List of Elliott Wave Triangles

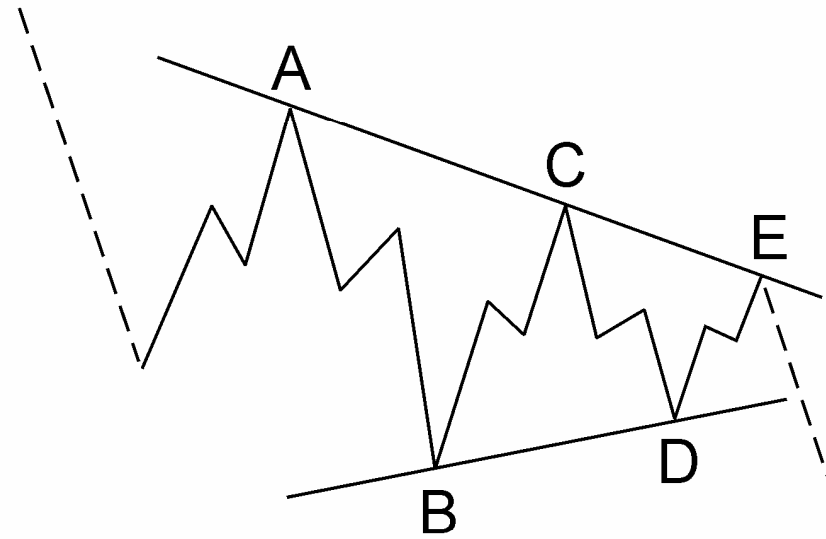
Bull Market	Bear Market
<p>CONTRACTING (upper line declining, lower line rising)</p> 	
<p>BARRIER (inner line contracting, outer line flat)</p> 	
<p>EXPANDING (upper line rising, lower line declining)</p> 	

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Running Triangles



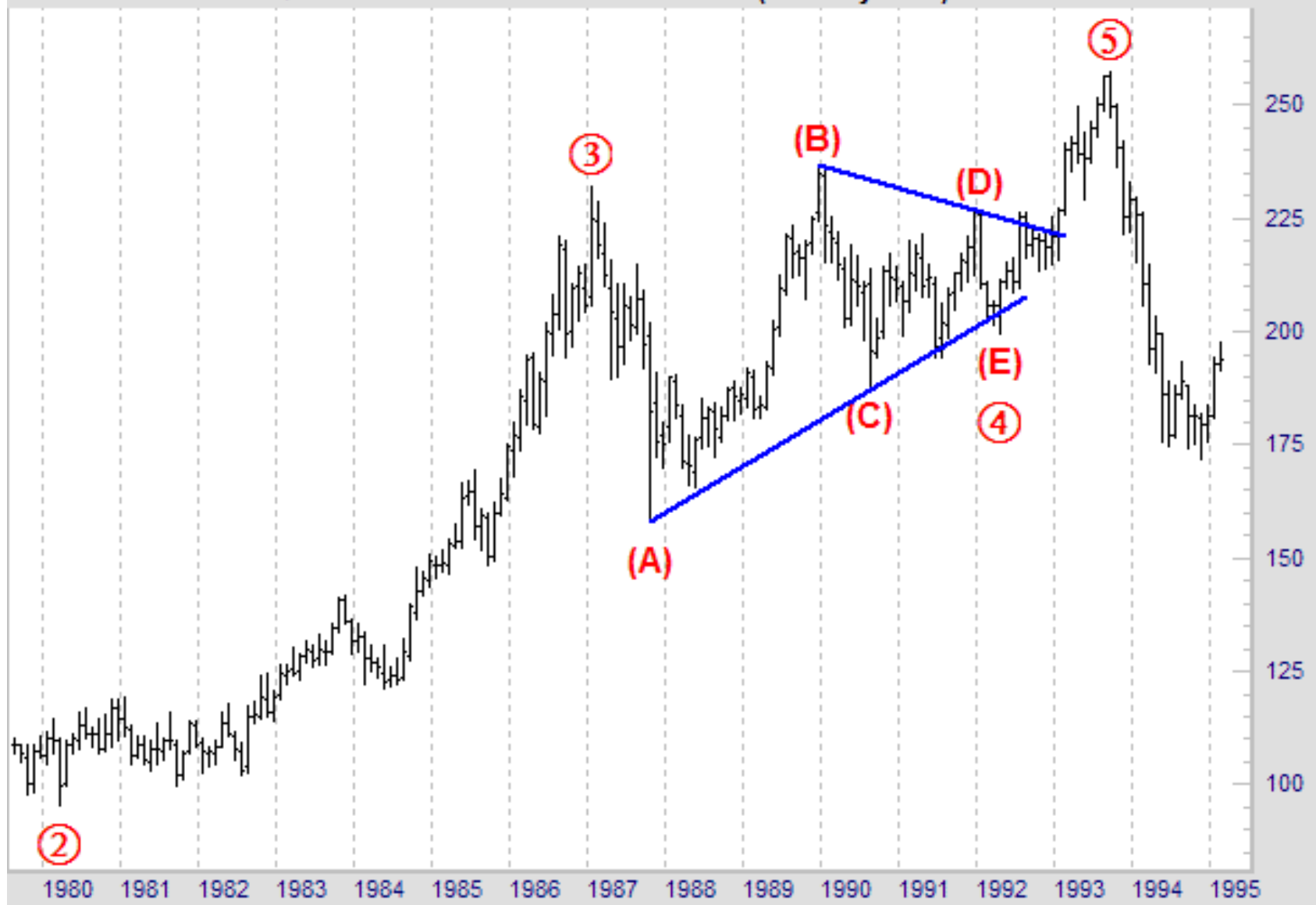
Bull Market

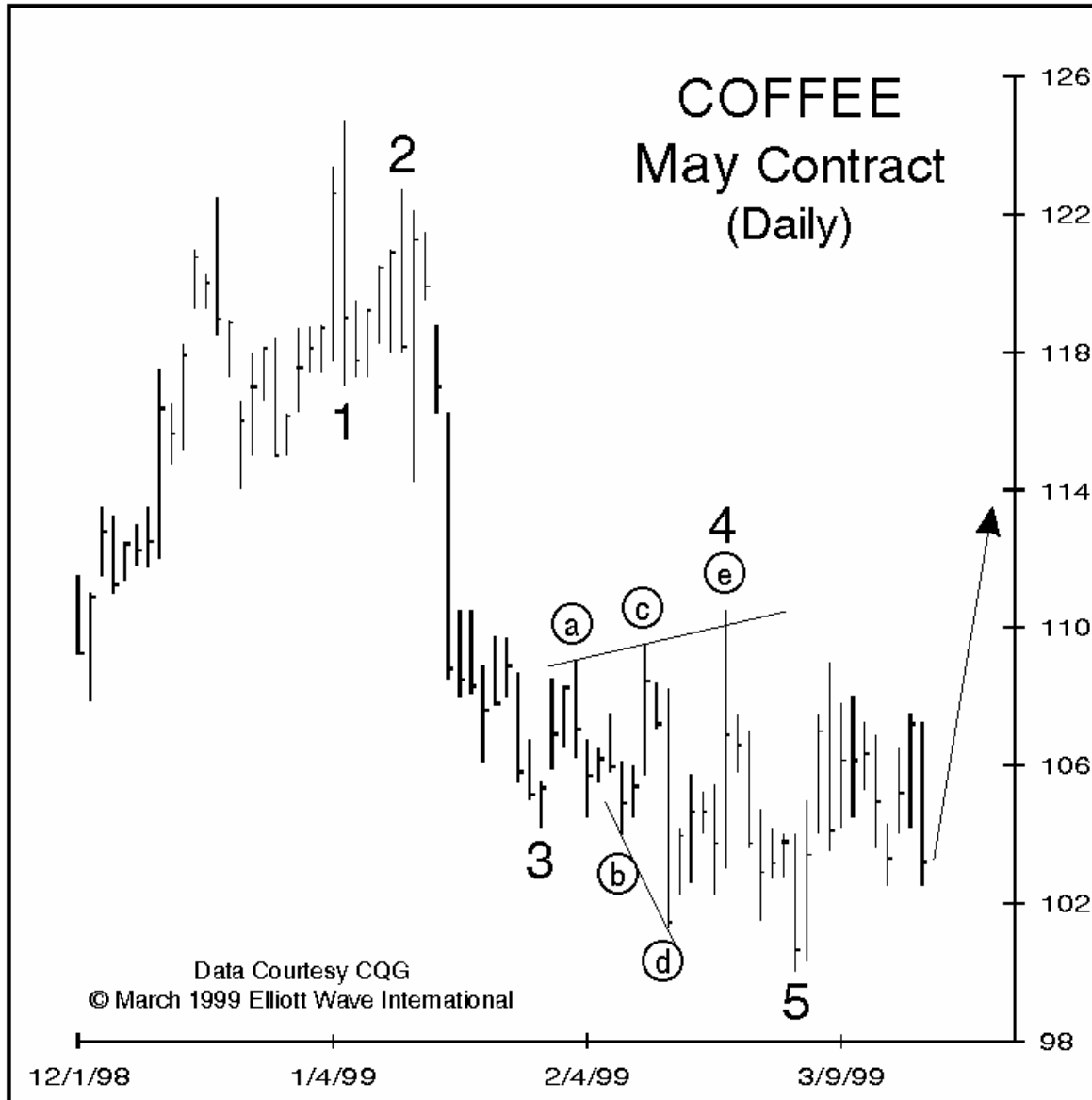


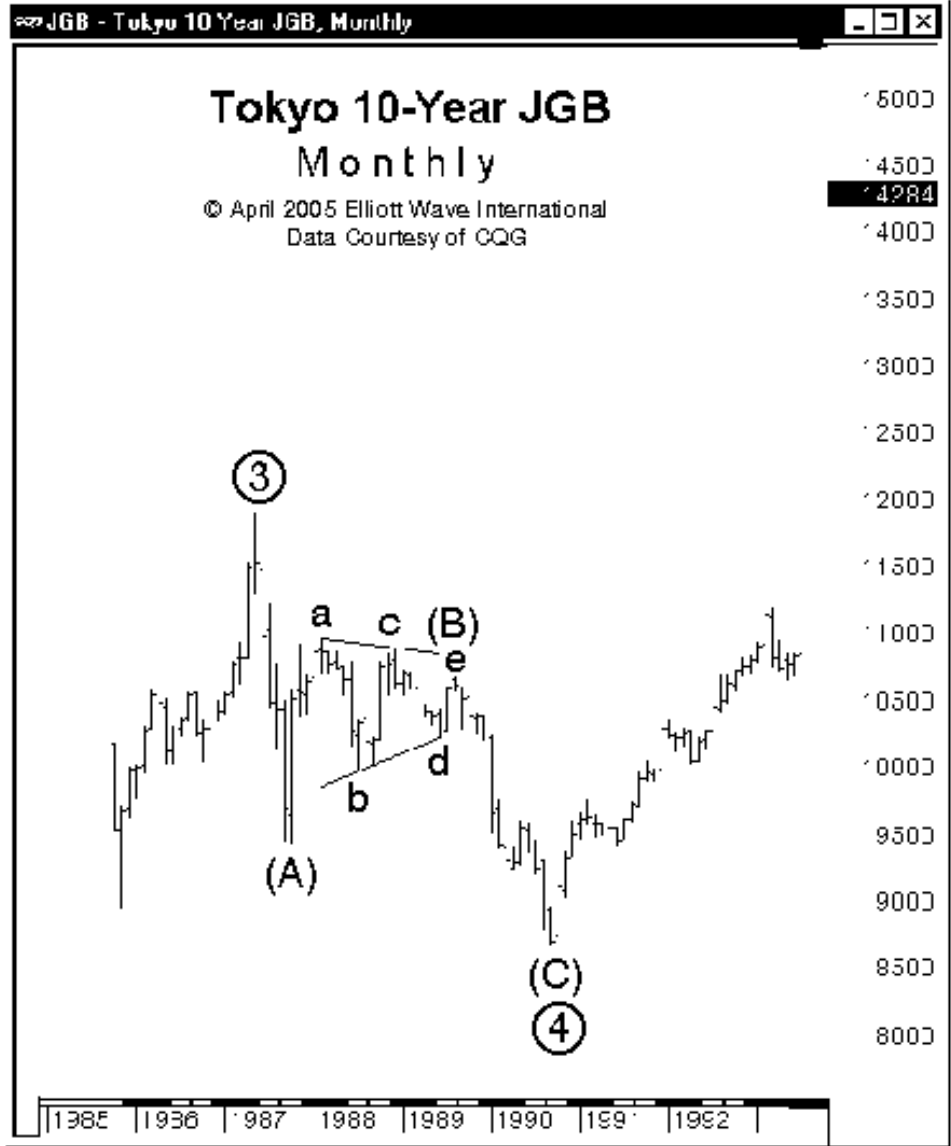
Bear Market

\$DJUA: Dow Jones Utilities Index (Monthly bars)

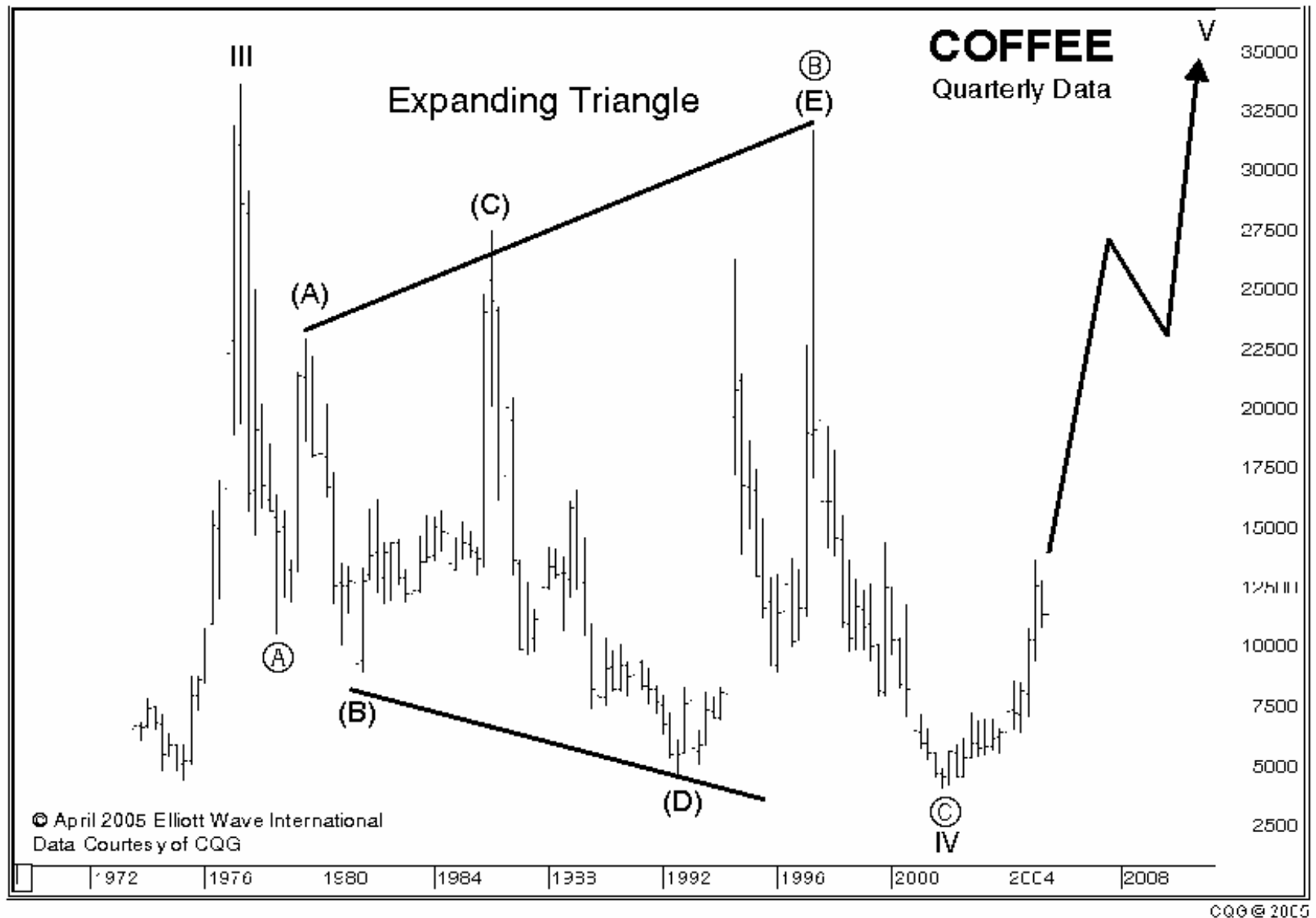
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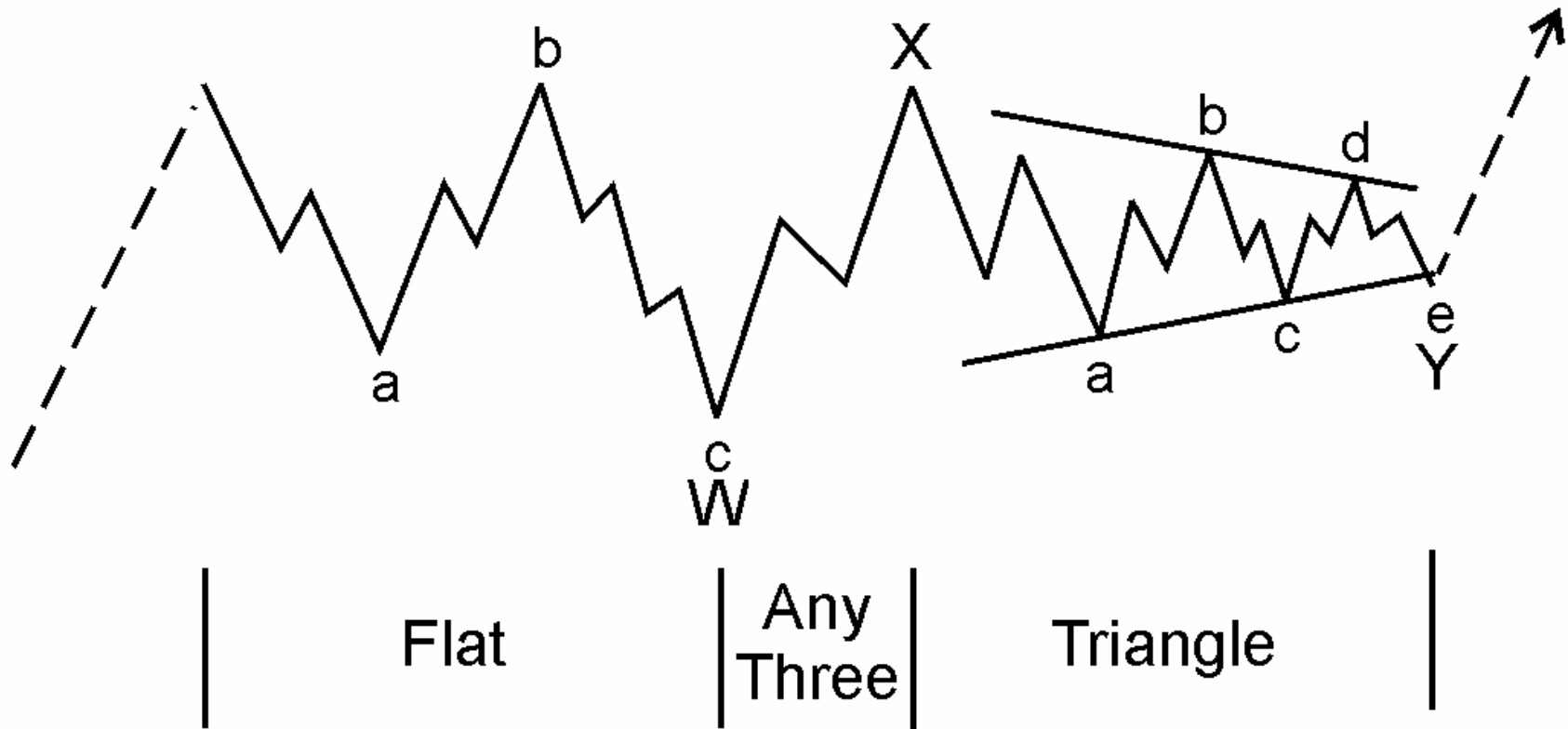




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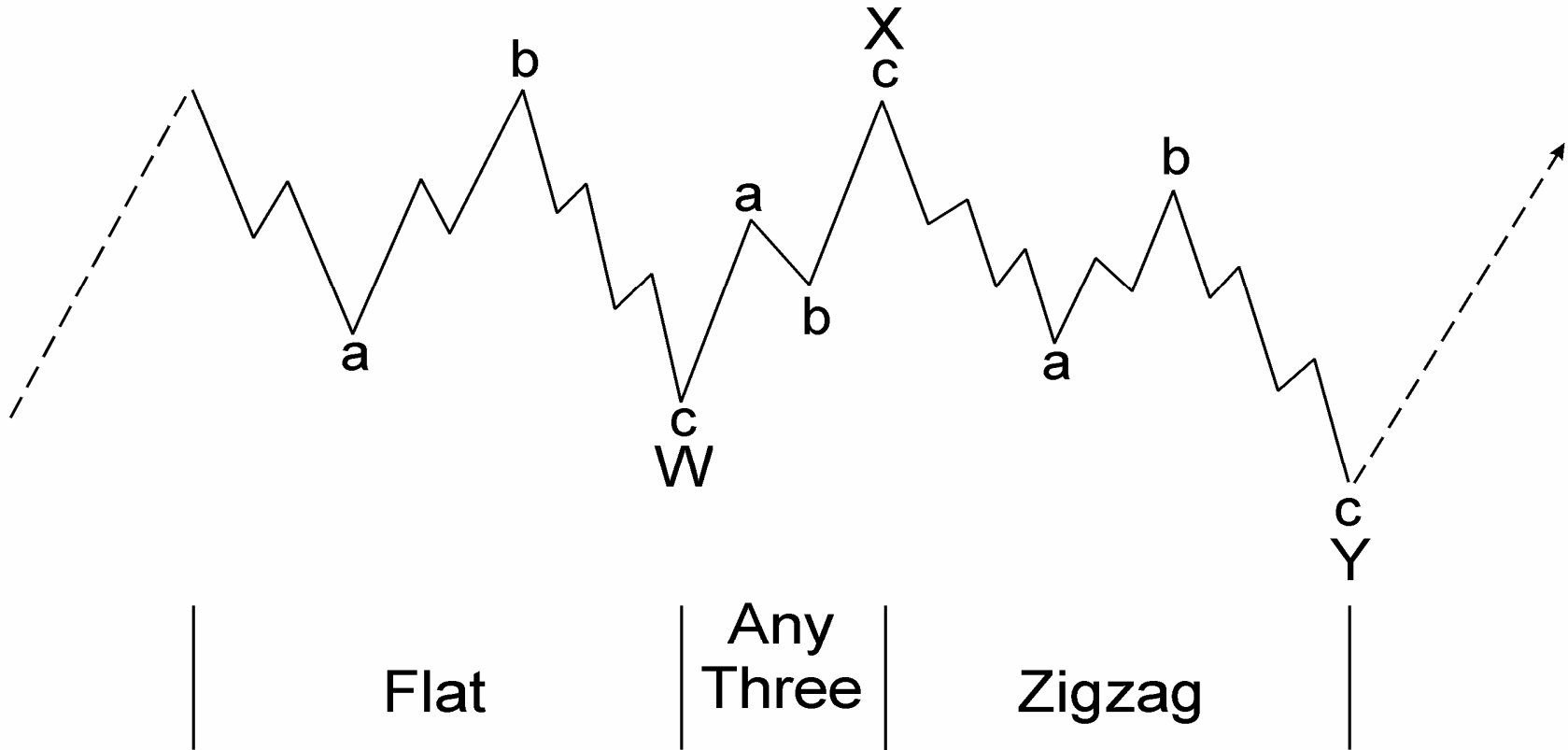


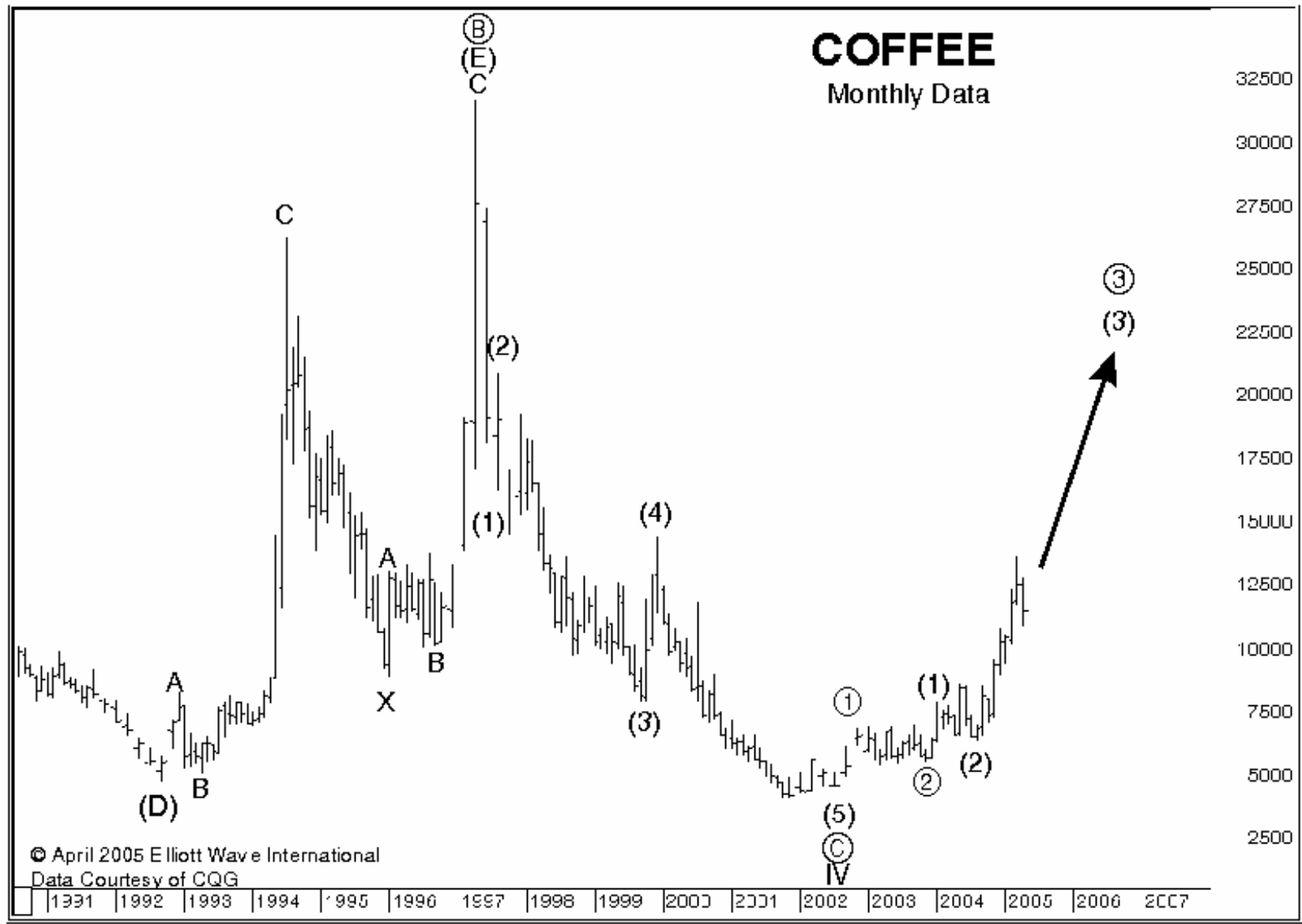
Characteristics of Corrective Waves



Combination

Combination



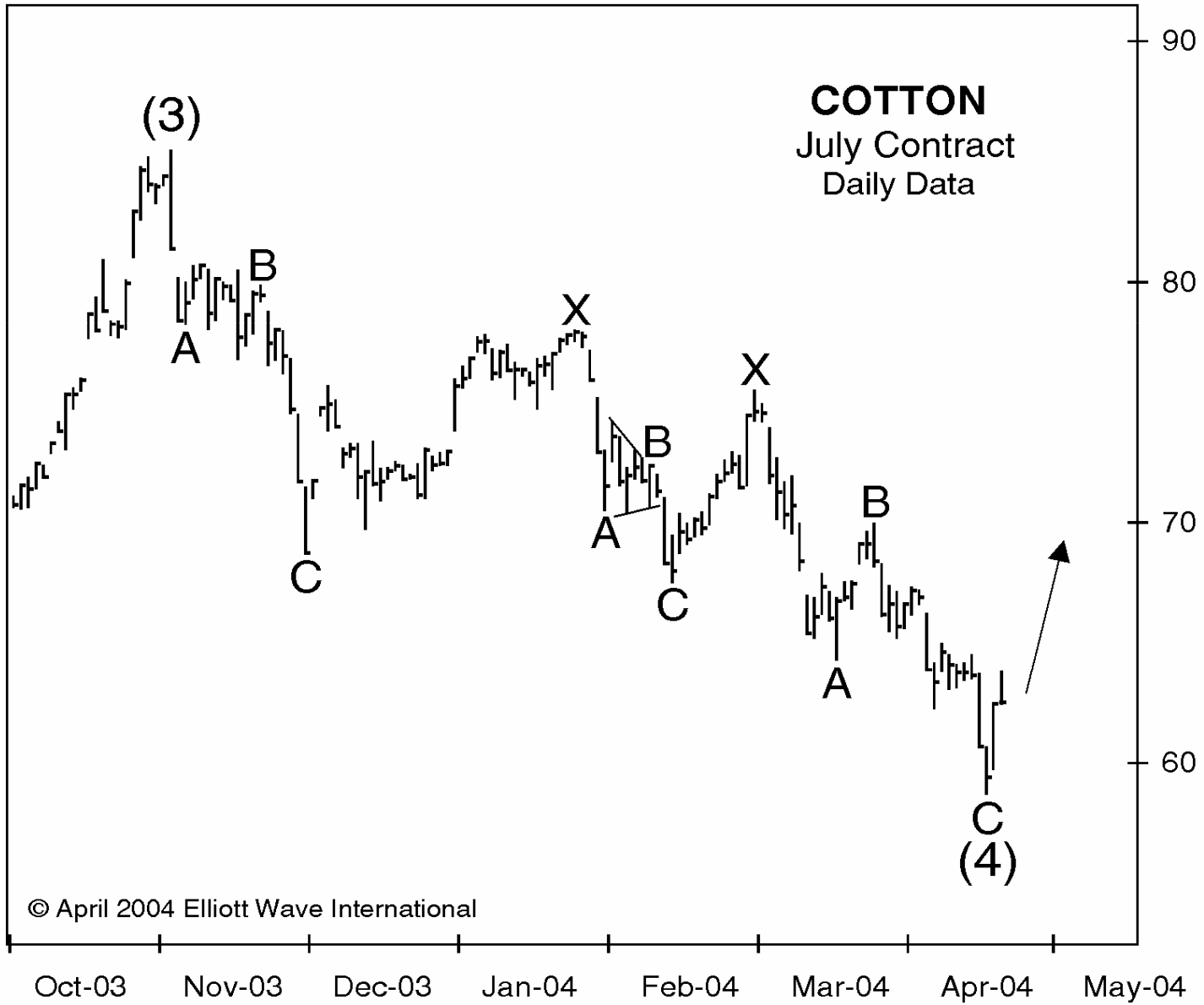


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Corrective Waves Summary

	A	B	C	D	E	Shape	Position
Zigzag	5	3	5			Sharp	Wave 2
Flat	3	3	5			Sideways	Wave 4
Triangle	3	3	3	3	3	Sideways	Wave 4
Combination		X wave				Sideways	Wave 4

Rules

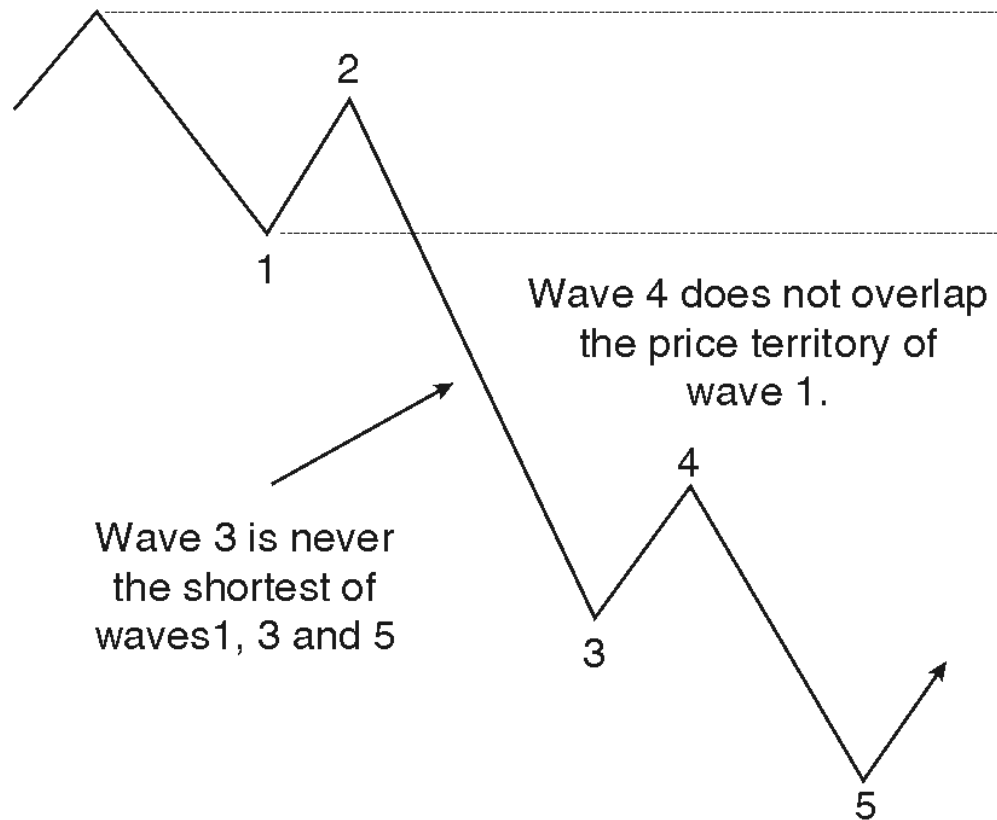
- Of waves 1, 3 and 5, wave 3 can never be the shortest wave.
- Wave 2 can never retrace more than 100% of wave 1.
- The end of wave 4 can never overlap the orthodox end of wave 1.

Strong Guideline

- No portion of wave 4 can enter the price territory of wave 1 or wave 2.

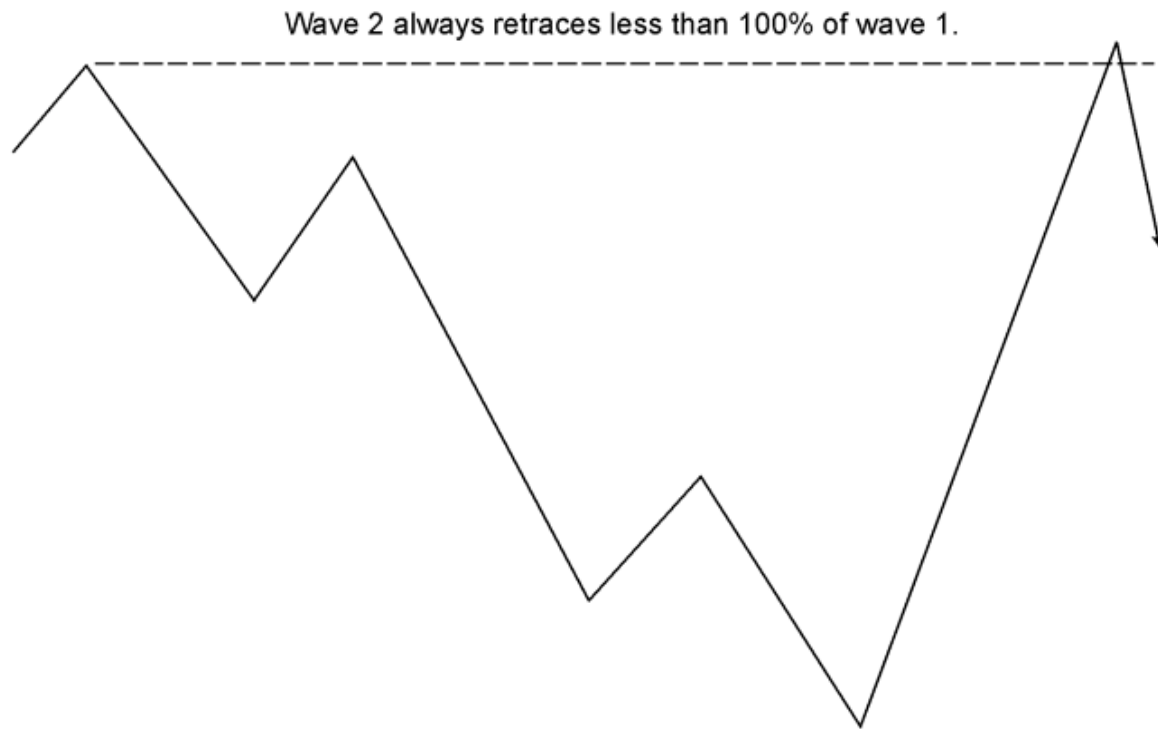
Rules

Wave 2 always retraces less than 100% of wave 1.



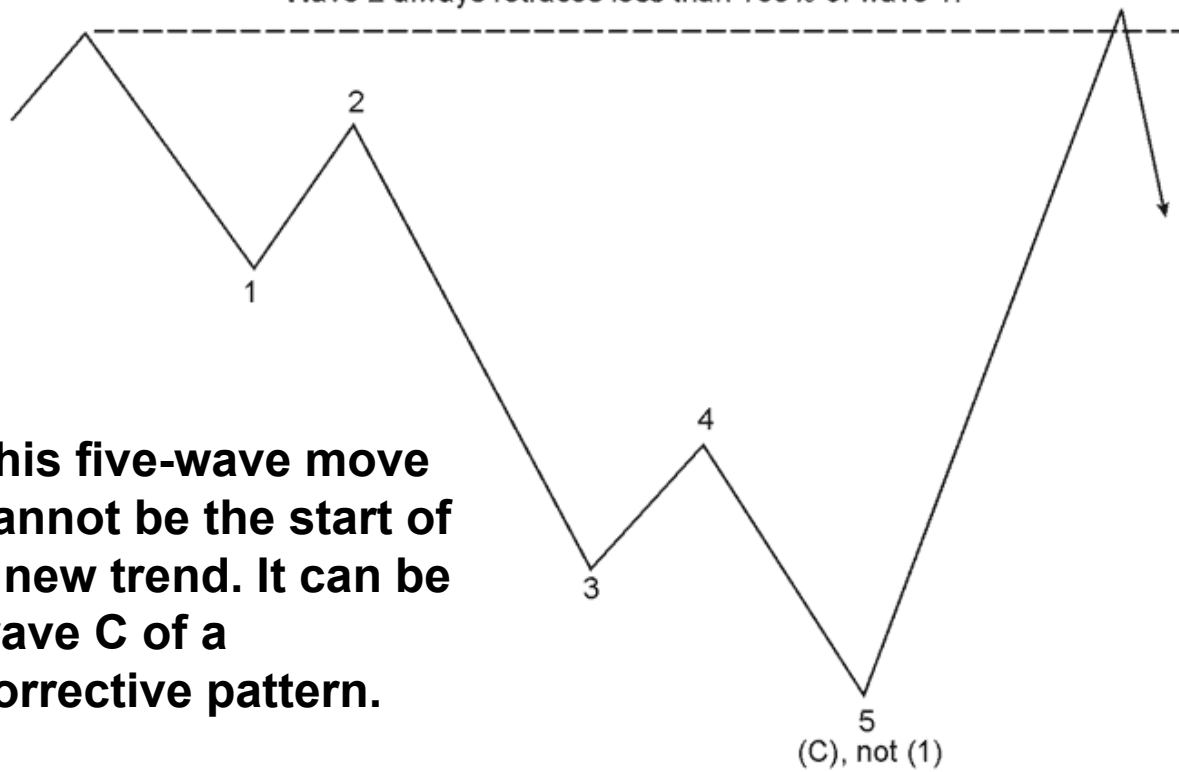
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Rules



Rules

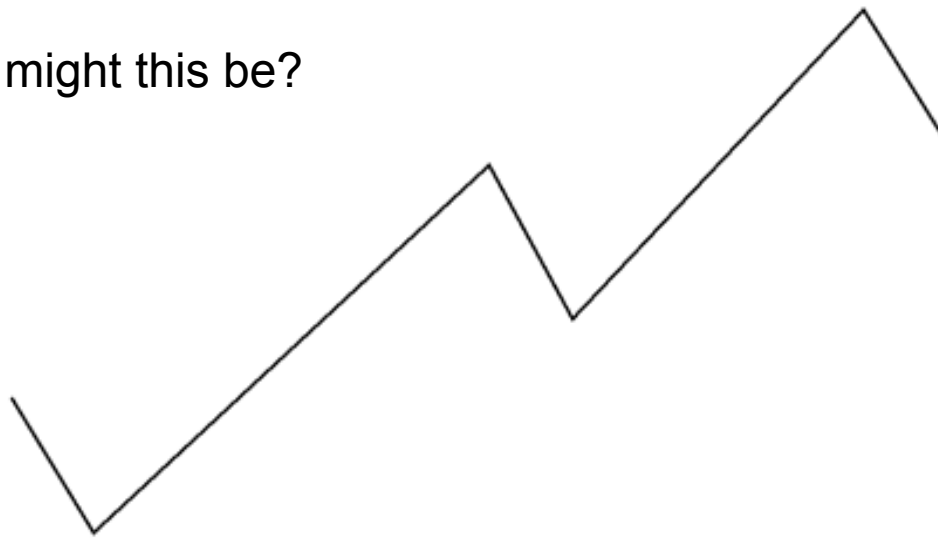
Wave 2 always retraces less than 100% of wave 1.



This five-wave move cannot be the start of a new trend. It can be wave C of a corrective pattern.

Rules

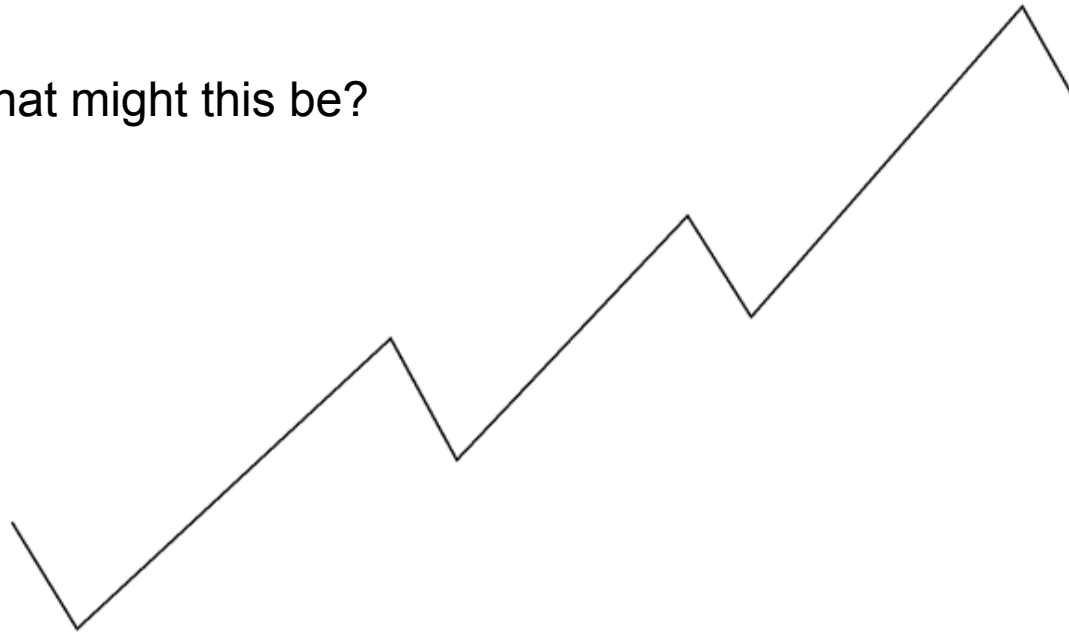
What might this be?



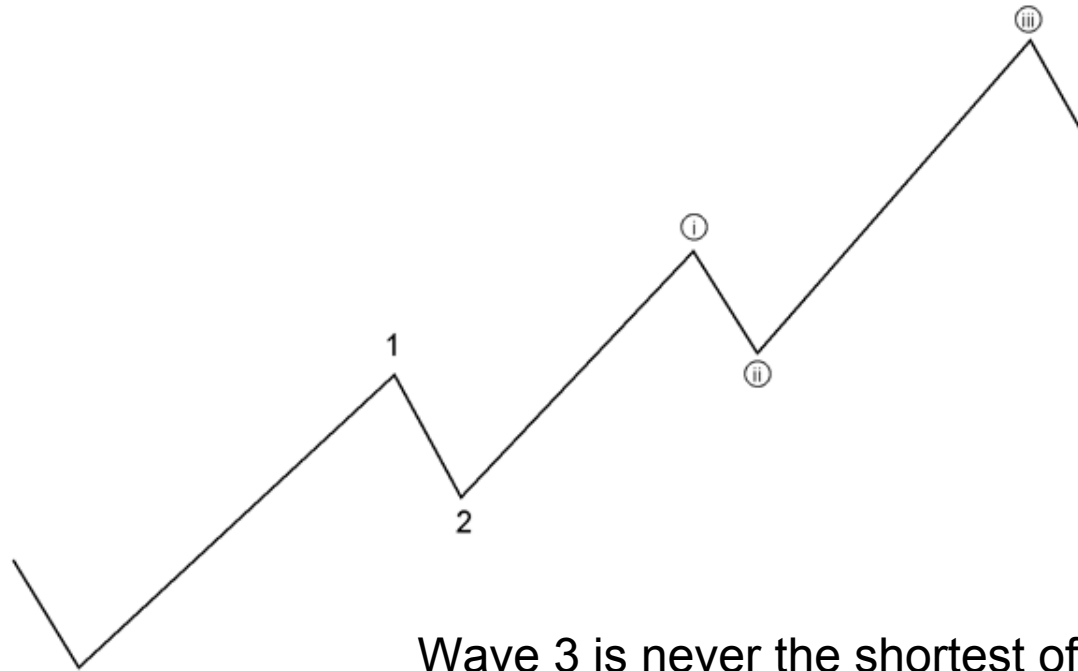
Significant Bottom

Rules

What might this be?

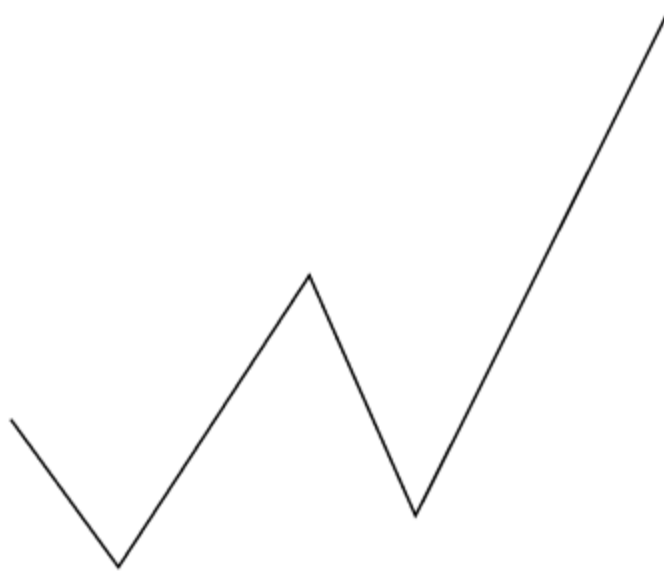


Rules



Wave 3 is never the shortest of waves 1, 3 and 5. This could be part of a wave 3 extension.

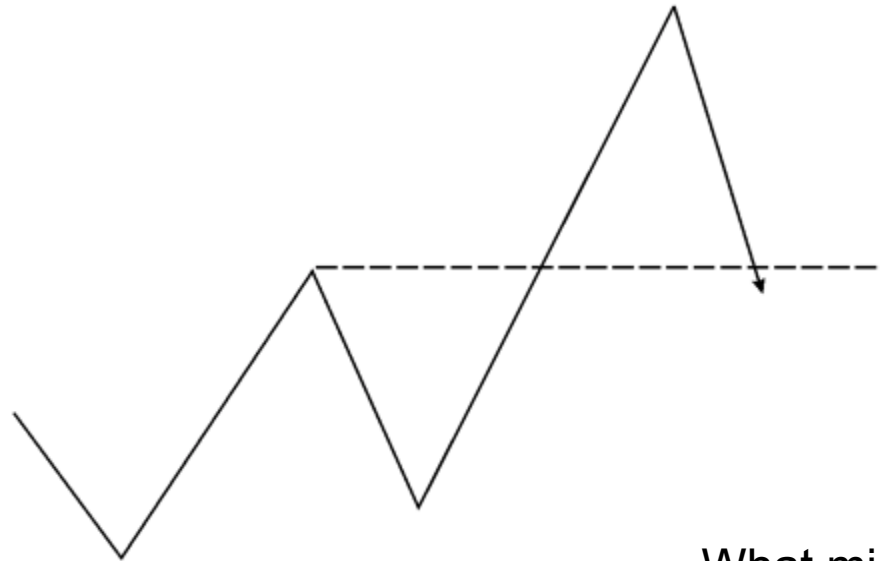
Rules



Significant Bottom

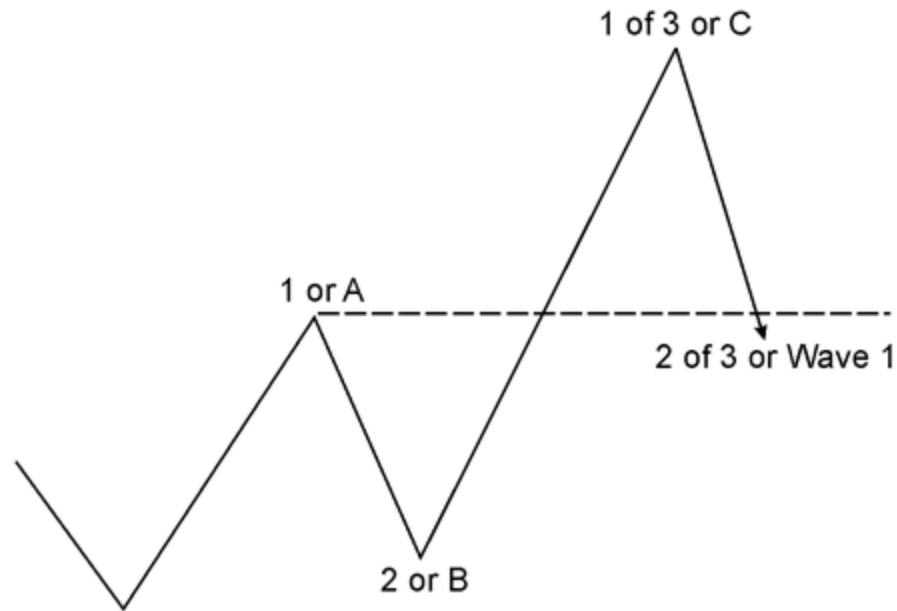
What might this be?

Rules



What might this be?

Rules



Wave 4 does not overlap the price territory of wave 1. This could be the start of a 3rd wave extension or an A-B-C correction.

Guidelines

- Equality
- Alternation
- Depth
- Channeling
- Throw-Over
- Volume
- Post-Triangle Thrust Measurement

Guidelines

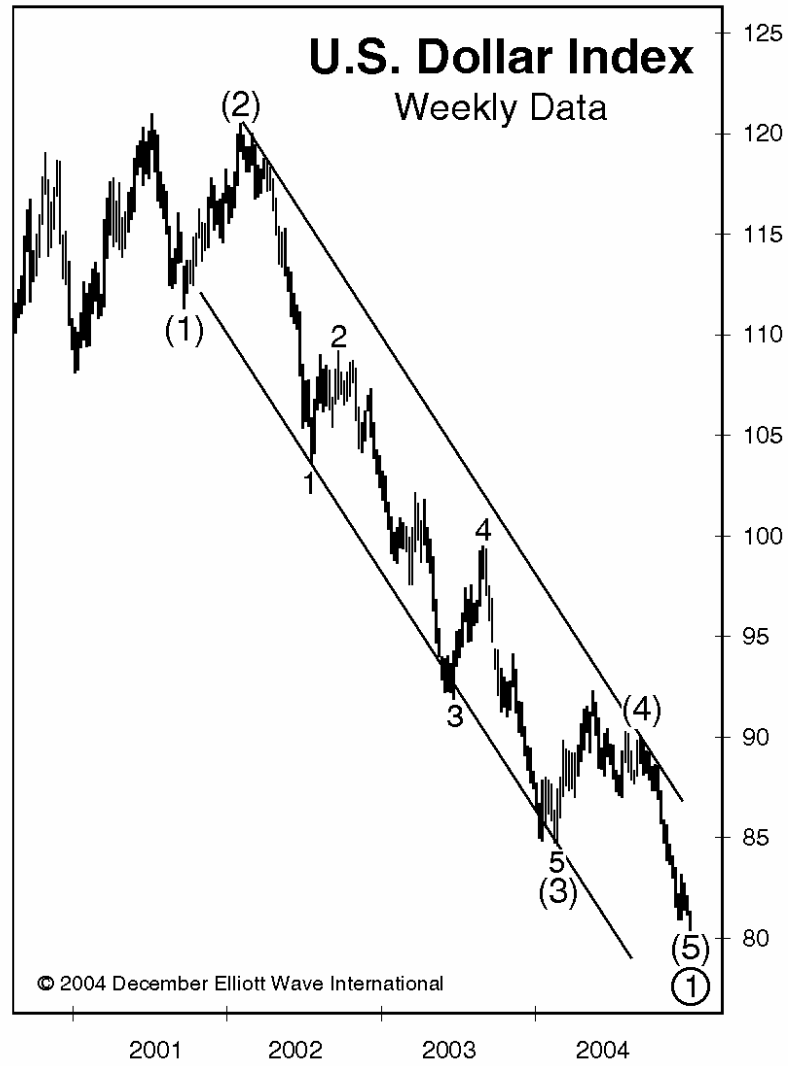
Wave Equality

- Two of the motive waves in a five-wave sequence will tend toward equality in time and magnitude.
- This is generally true of the two non-extended waves.
- For example, if wave 3 is extended then waves 1 and 5 will tend toward equality.

Equality



Equality



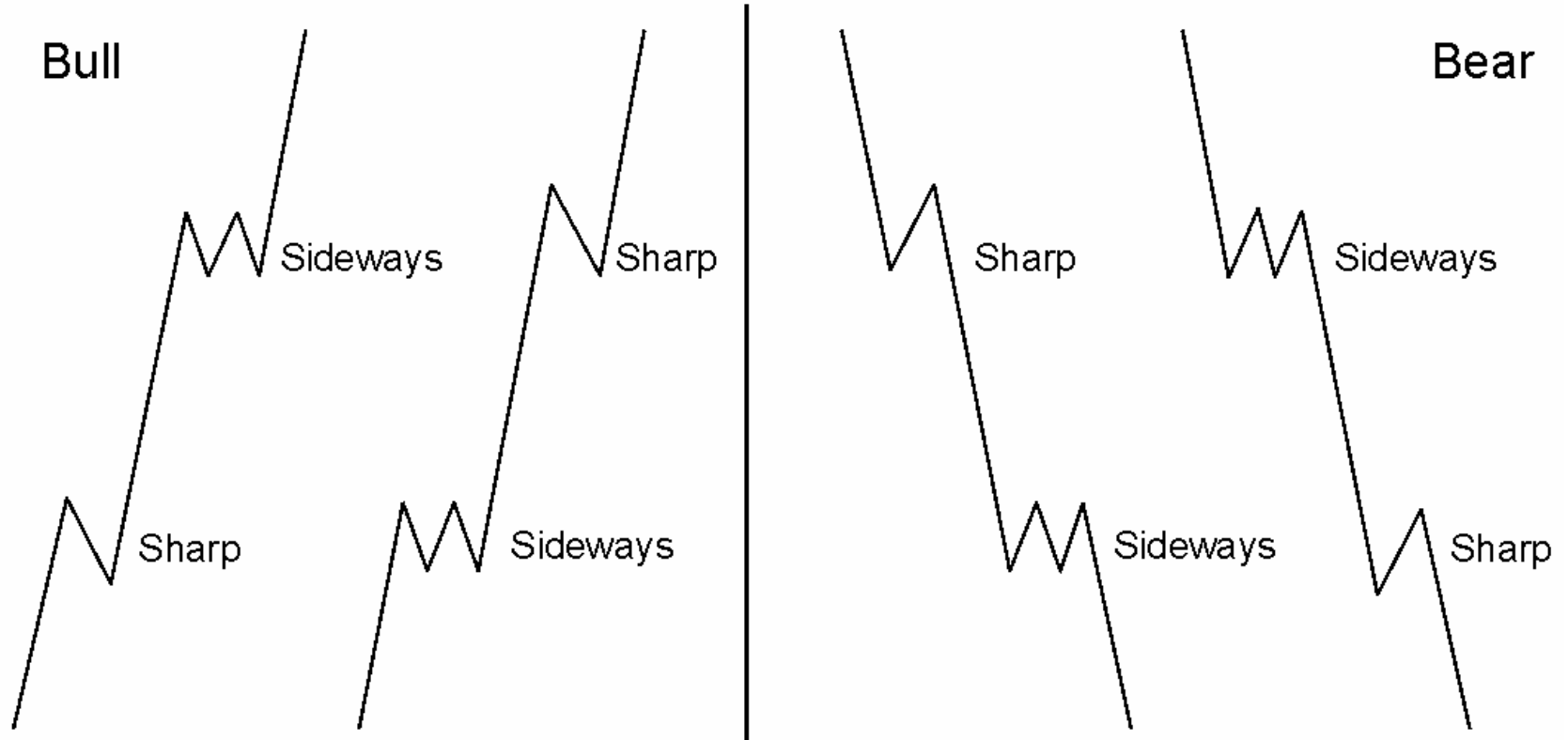
Guidelines

Alternation

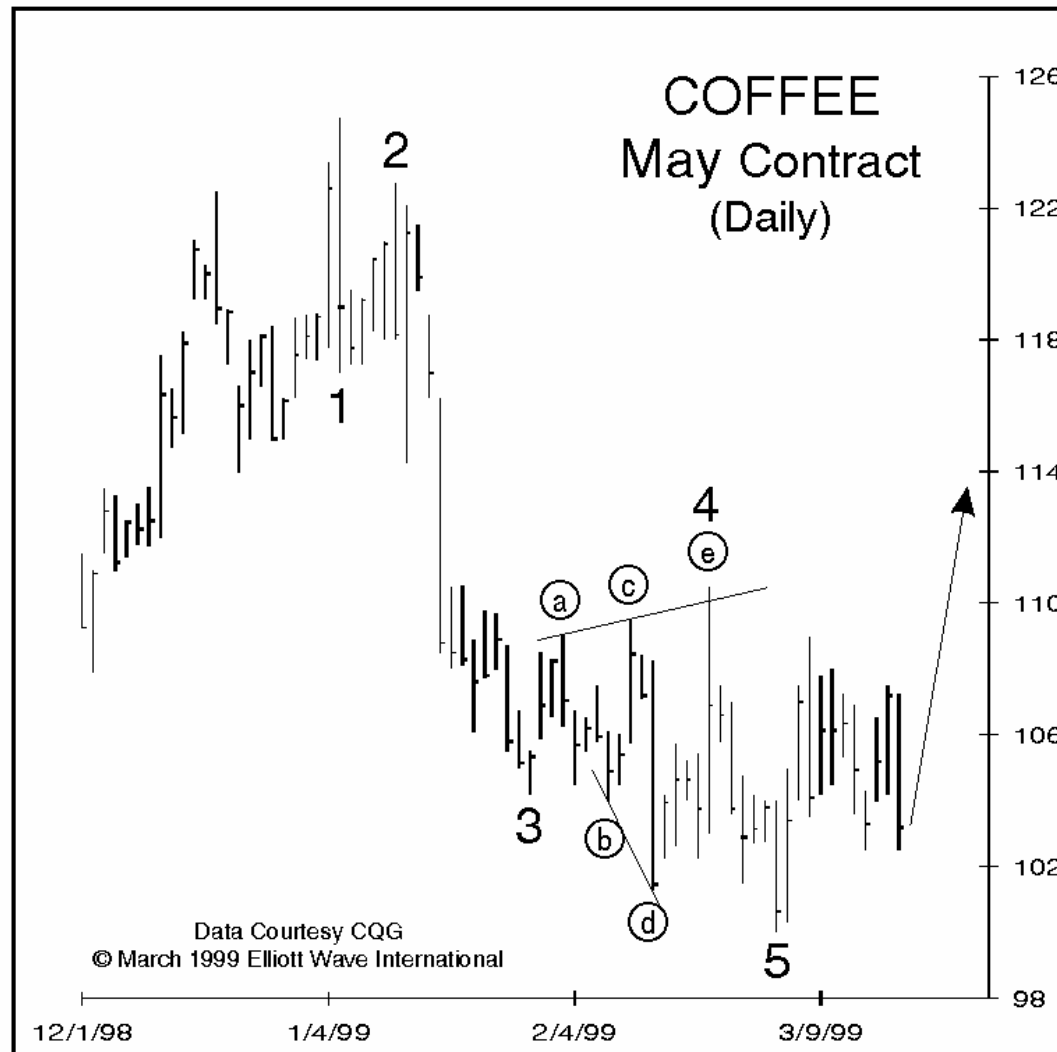
Within Impulse Waves

- If wave 2 is a sharp correction, expect wave 4 to be a sideways correction, and vice versa.
- Sharp corrections never include a new price extreme. Example: Zigzags
- Sideways corrections usually include a new price extreme. Examples: Flats, Triangles, and Combinations
- Diagonal triangles do not display alternation in subwaves 2 and 4.

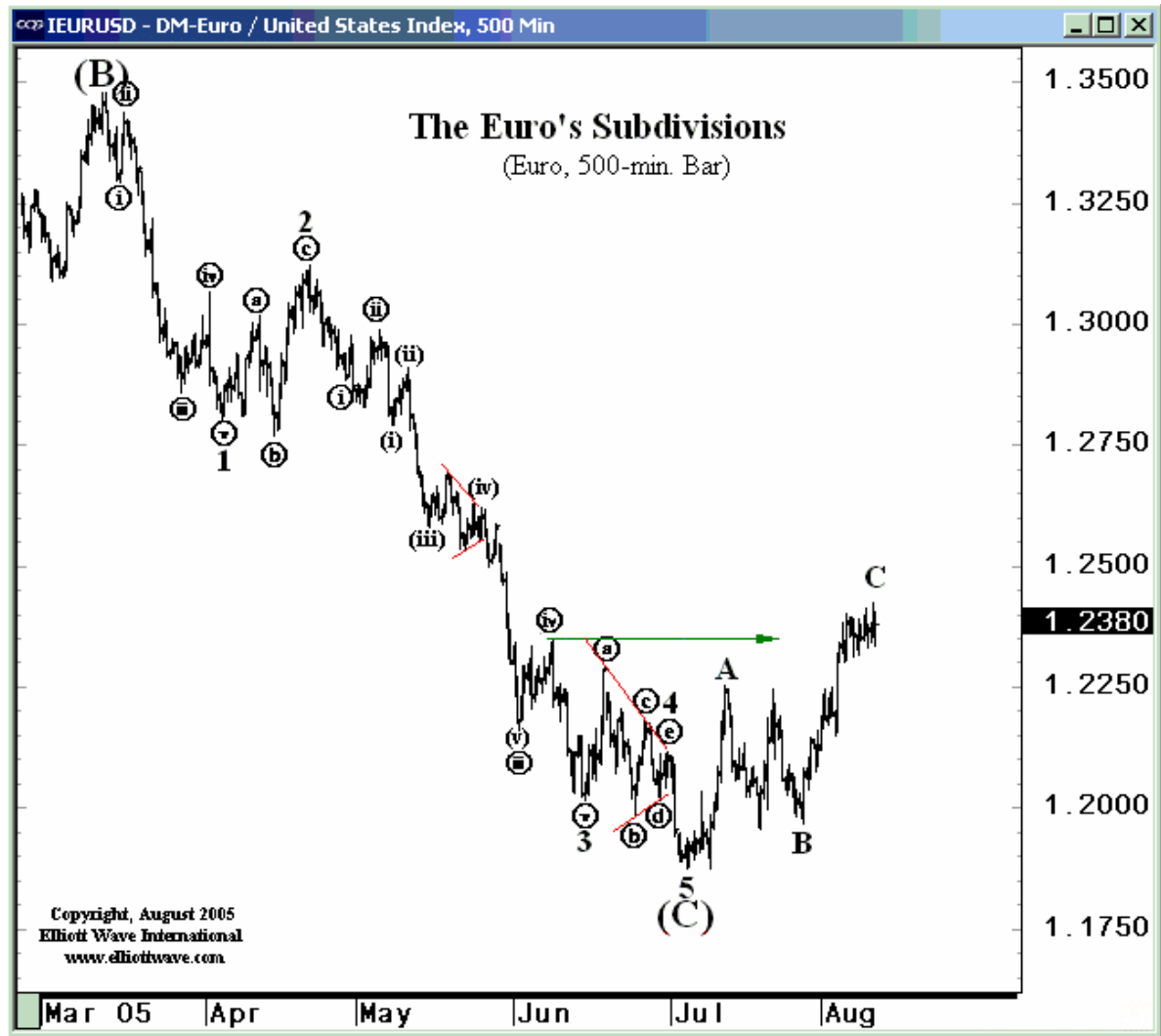
Alternation within Impulse Waves



Alternation within Impulse Waves



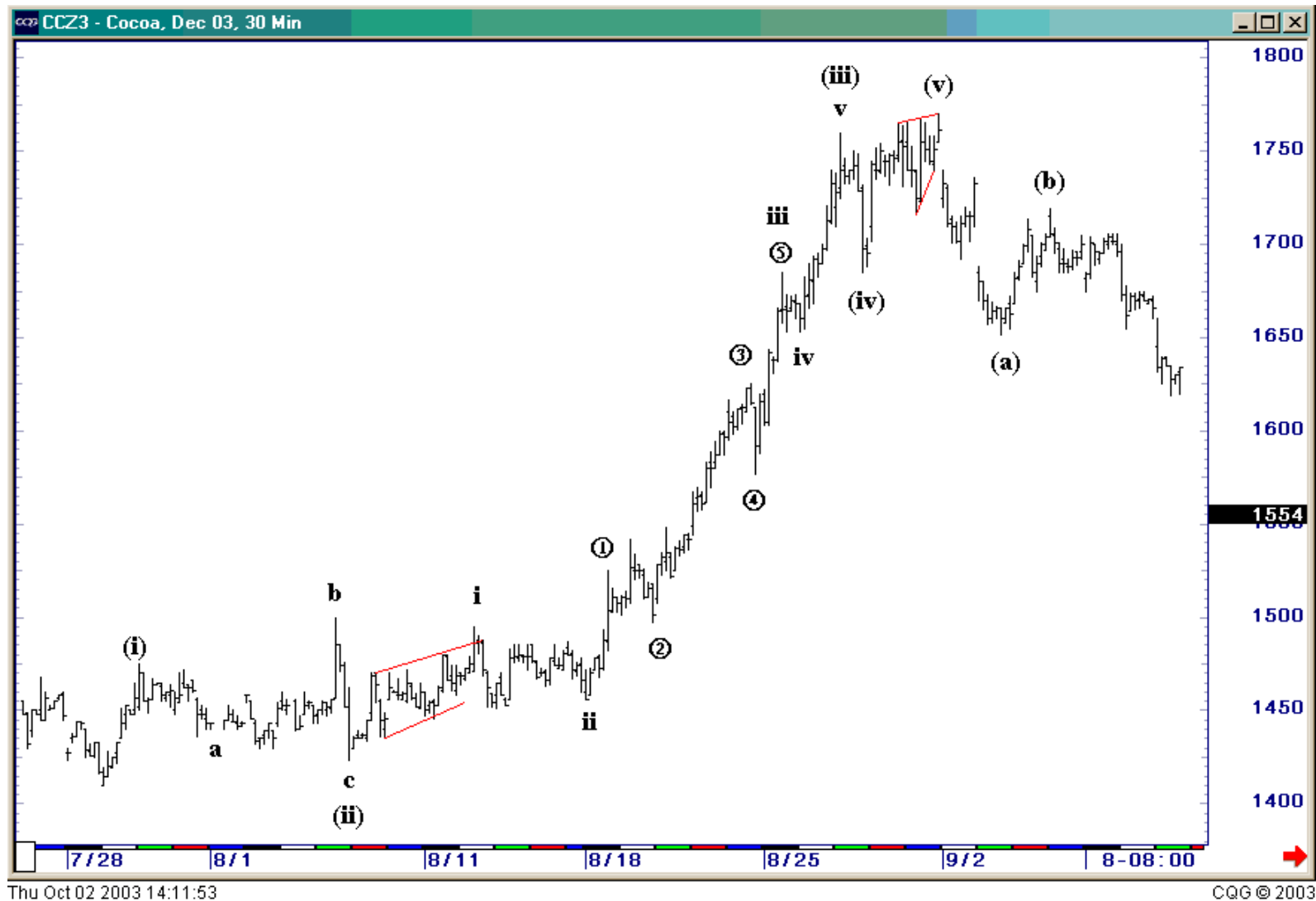
Alternation within Impulse Waves



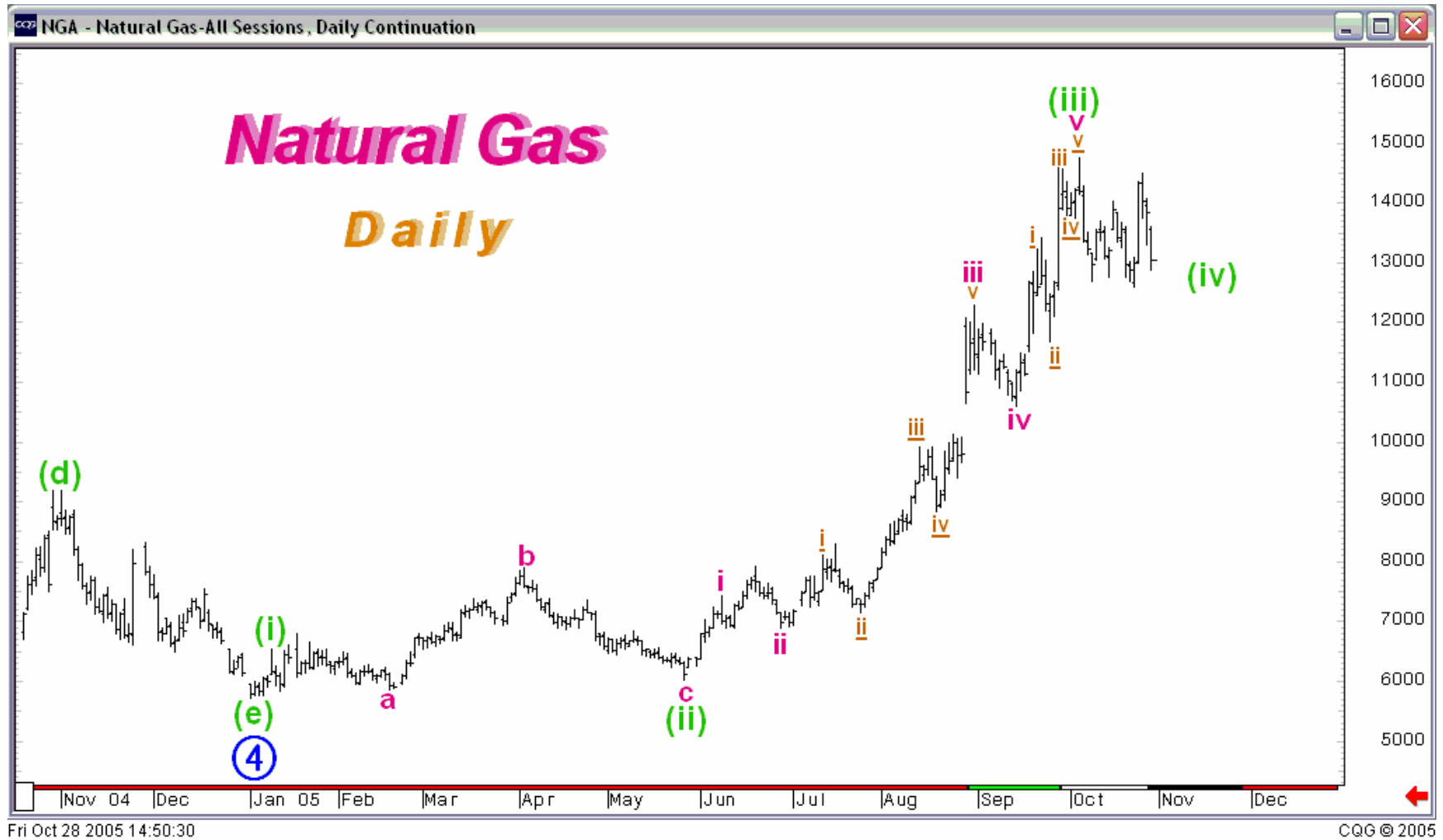
Wed Aug 10 2005 15:21:42

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Alternation within Impulse Waves



Alternation within Impulse Waves



Guidelines

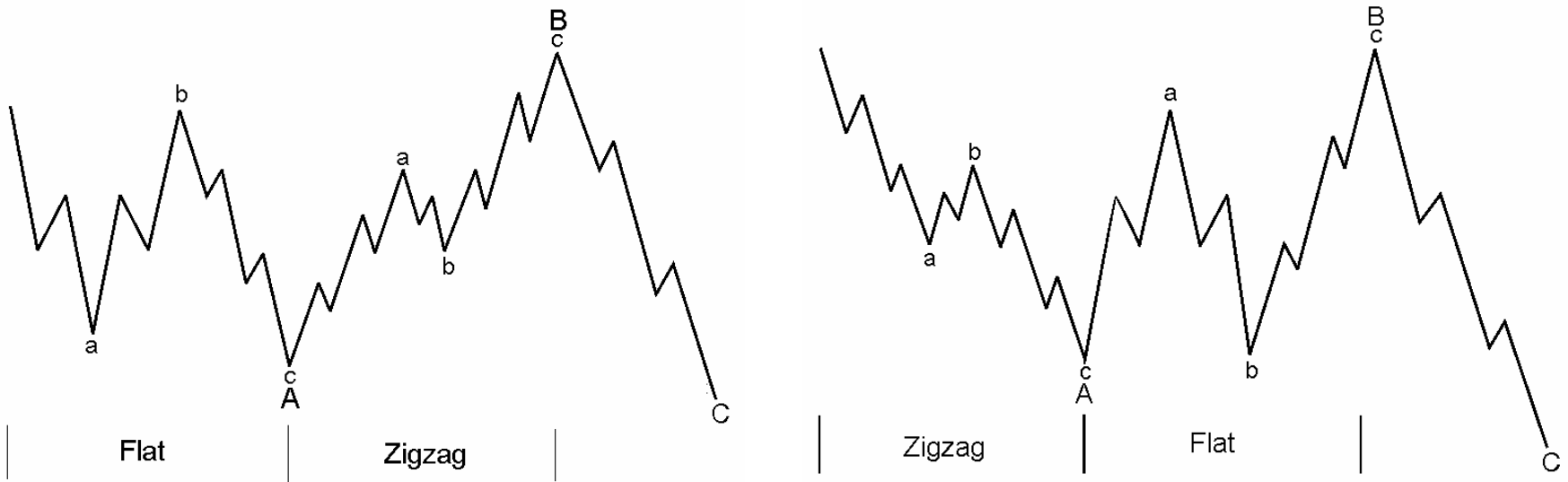
Alternation

Within Corrective Waves

- If a correction begins with a flat a-b-c structure for wave A, then expect a zigzag a-b-c structure for wave B, and vice versa.
- If a large correction begins with a simple a-b-c zigzag for wave A, wave B will stretch out into a more complex a-b-c zigzag.

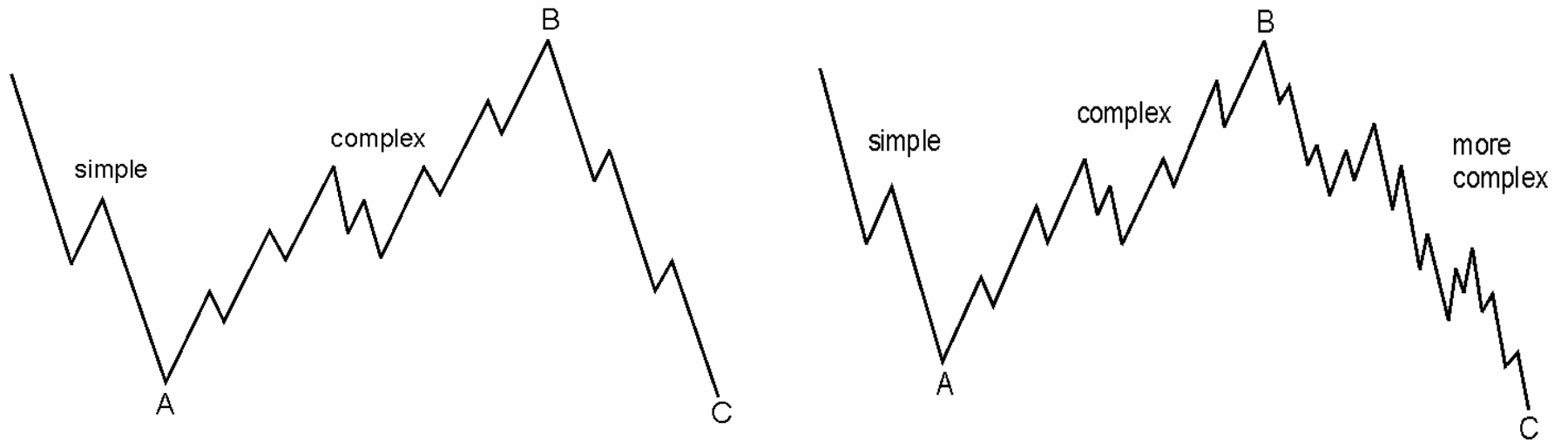
Guidelines

Alternation within Corrective Waves

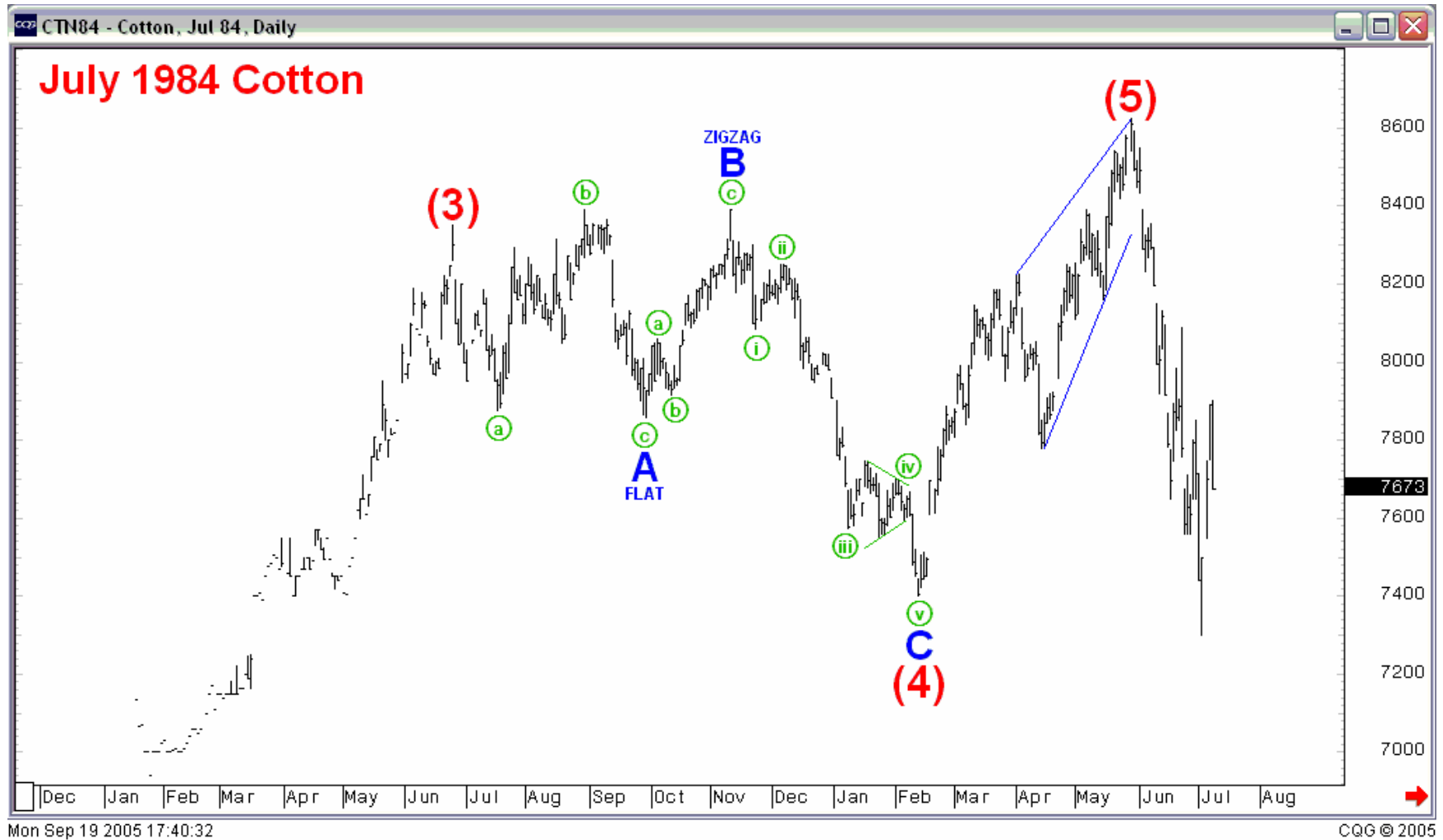


Guidelines

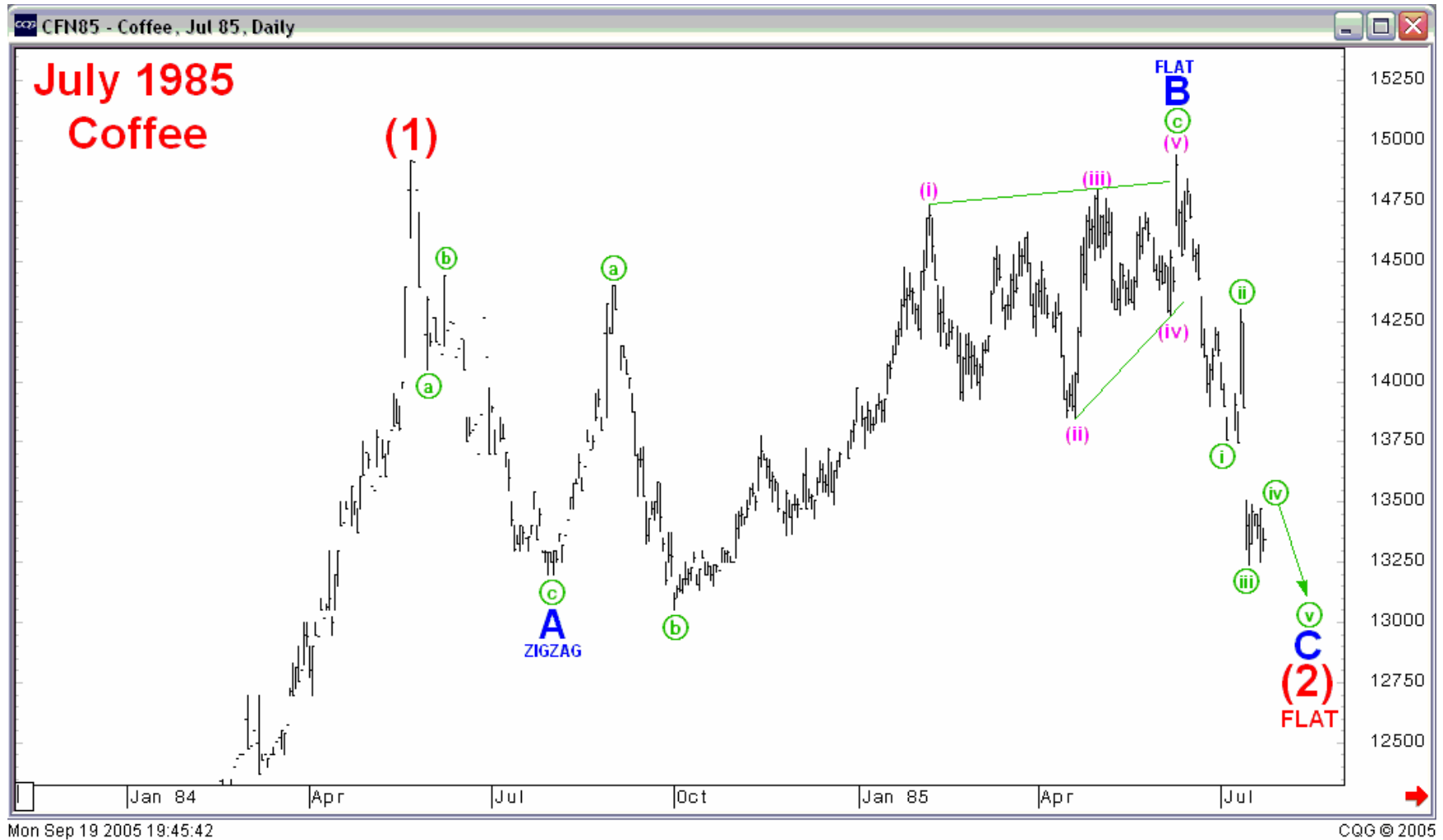
Alternation within Corrective Waves



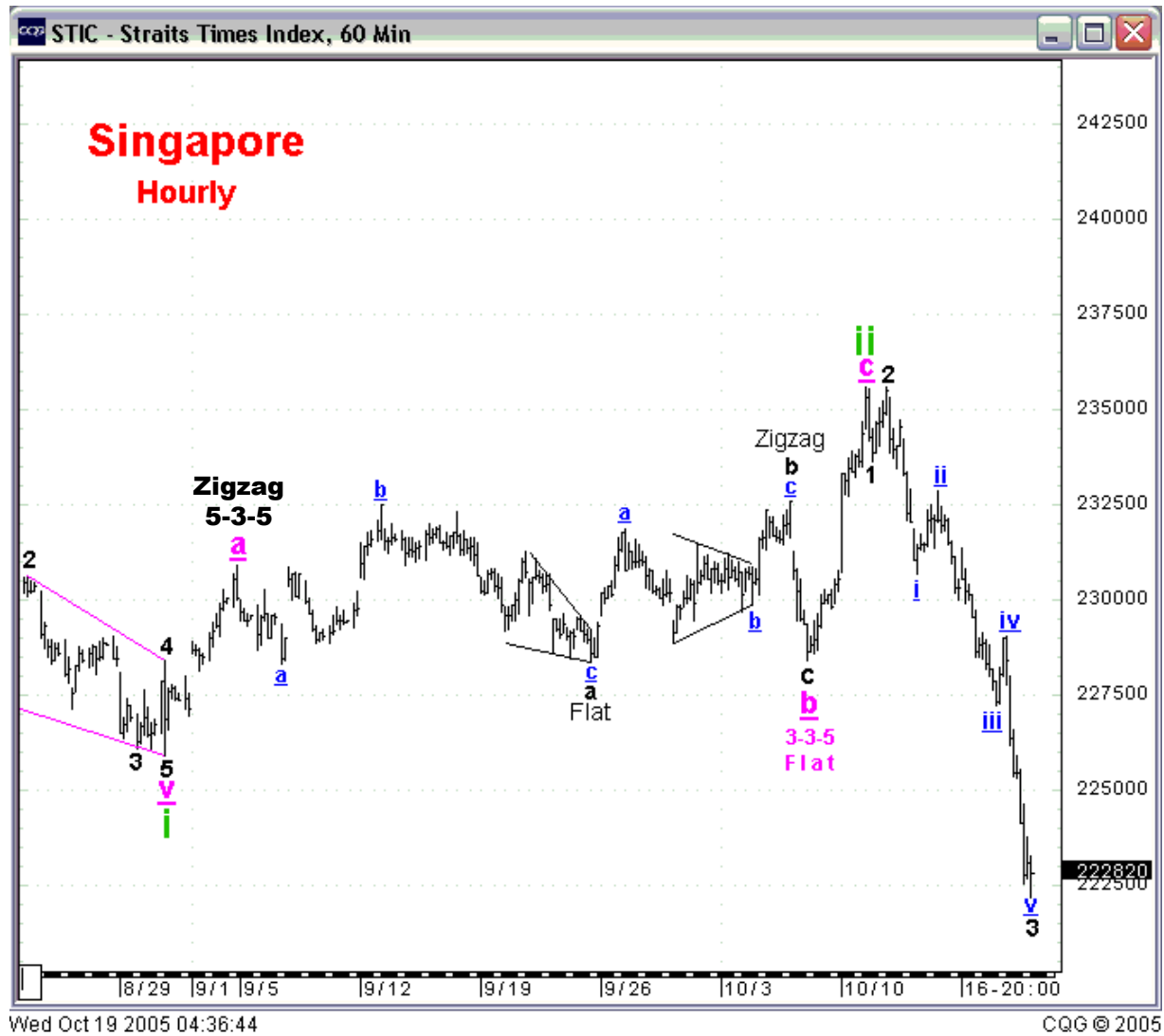
Alternation within Corrective Waves



Alternation within Corrective Waves



Alternation within Corrective Waves



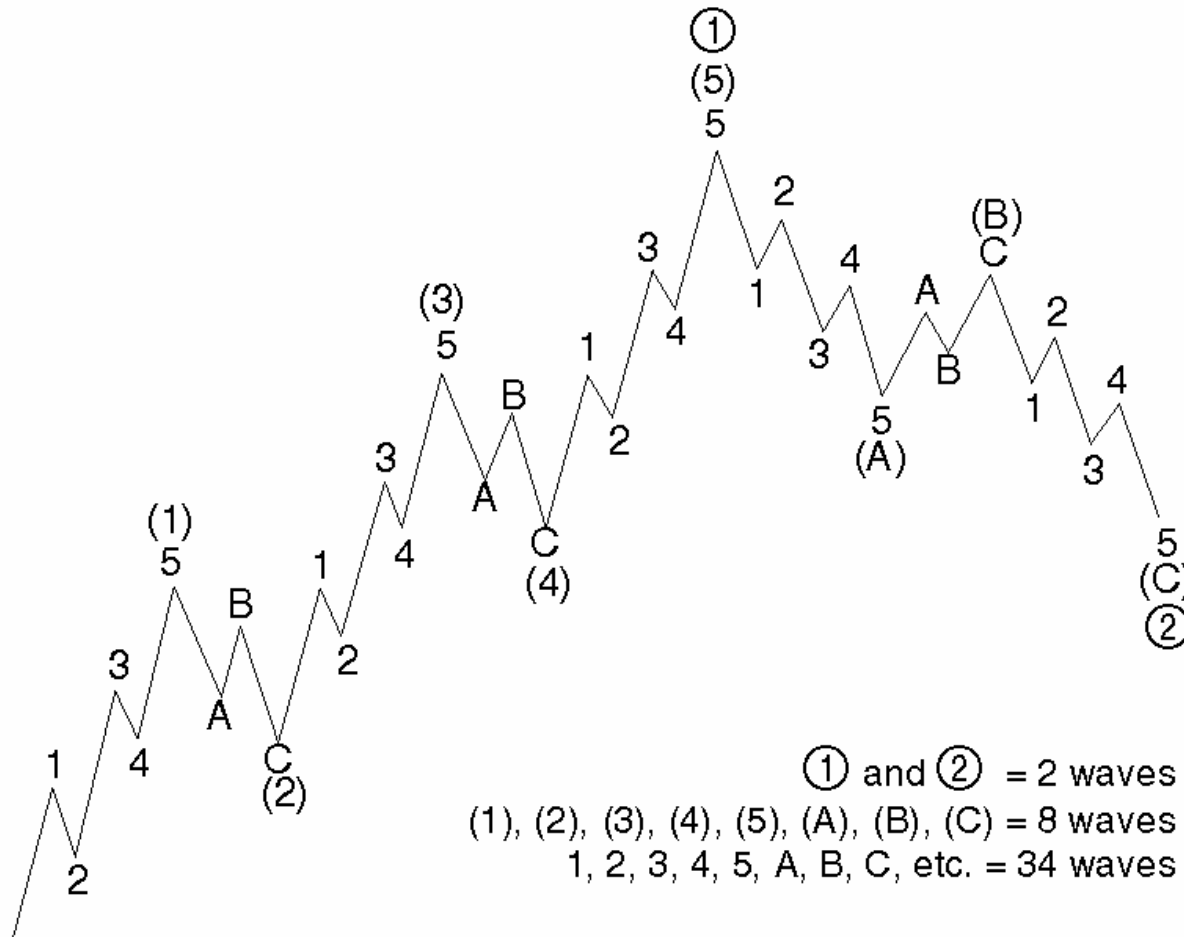
Guidelines

Depth of Corrective Waves

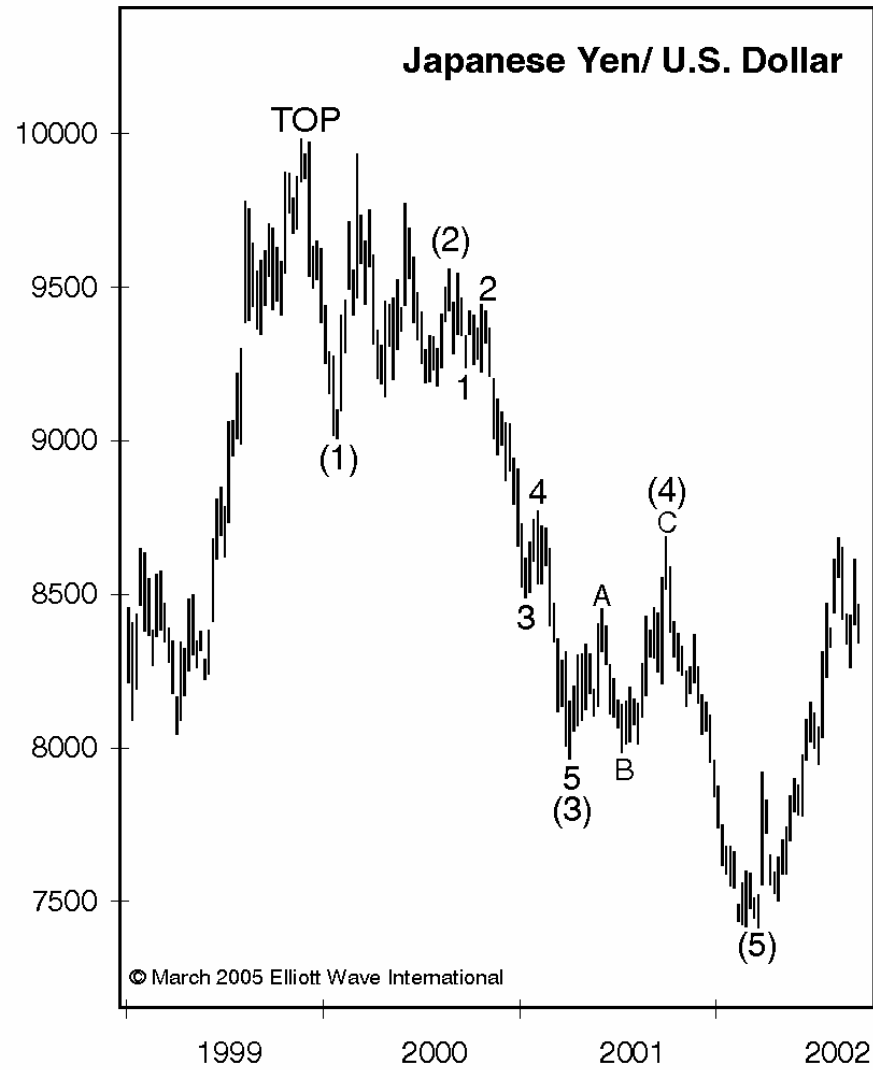
Corrections, especially when they are fourth waves, tend to register their maximum retracement within the span of travel of the previous fourth wave of one lesser degree and most commonly near its terminus.

Guidelines

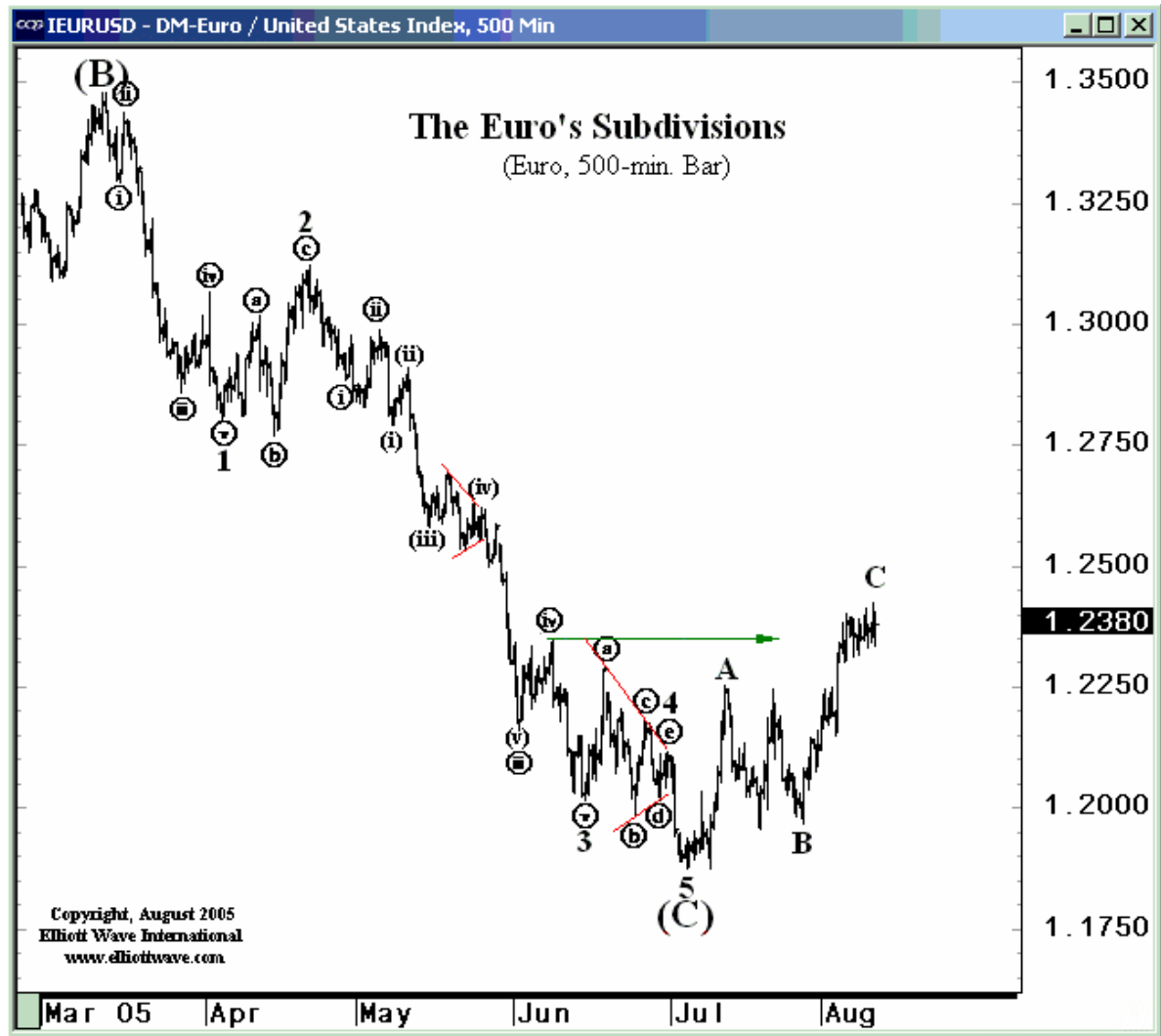
Depth of Corrective Waves



Depth of Corrective Waves



Depth of Corrective Waves



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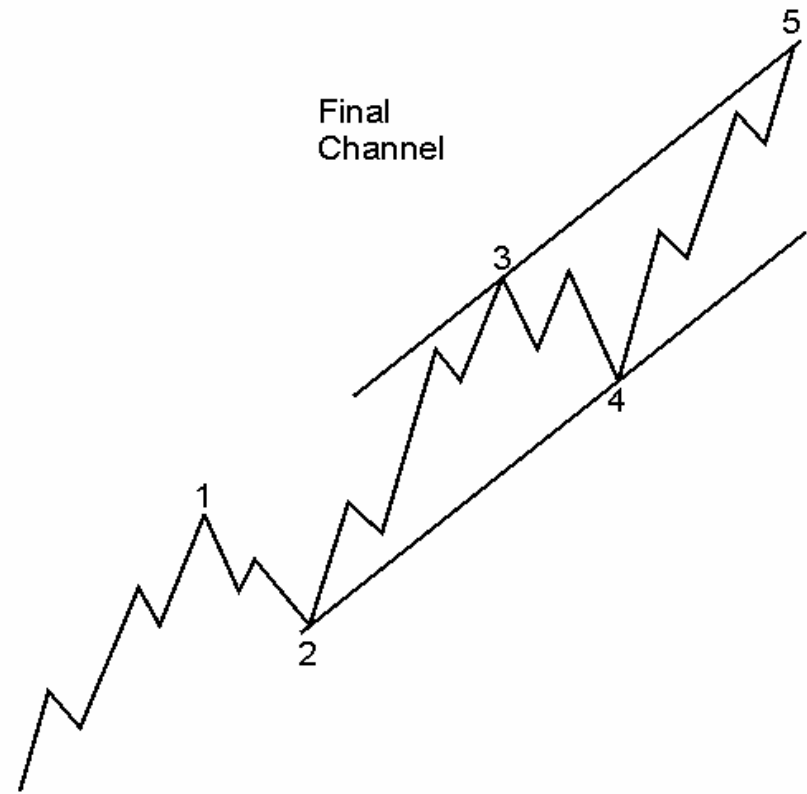
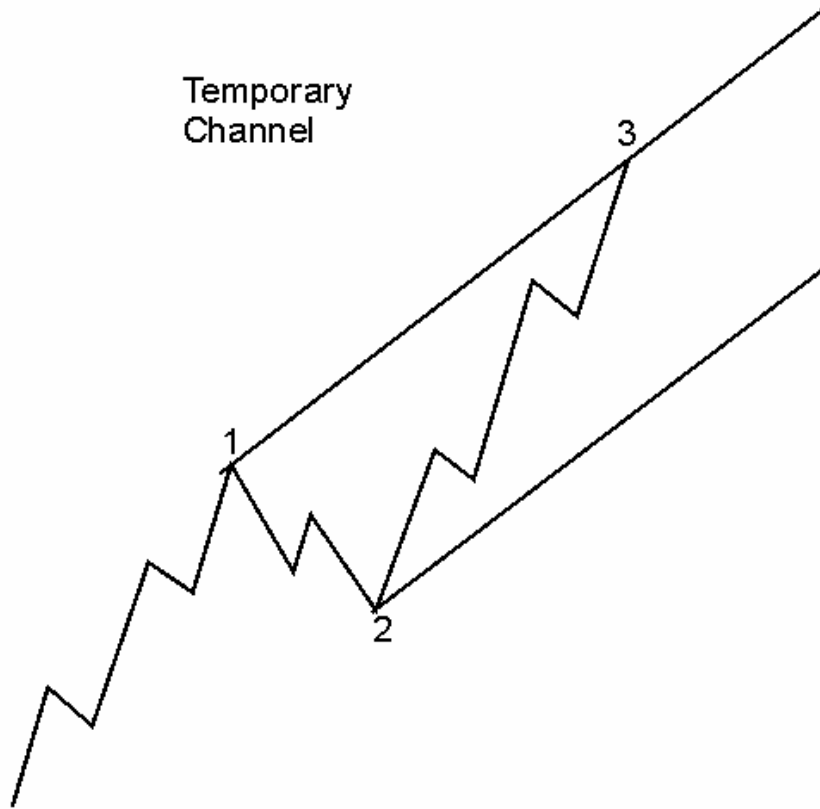
Guidelines

Channeling

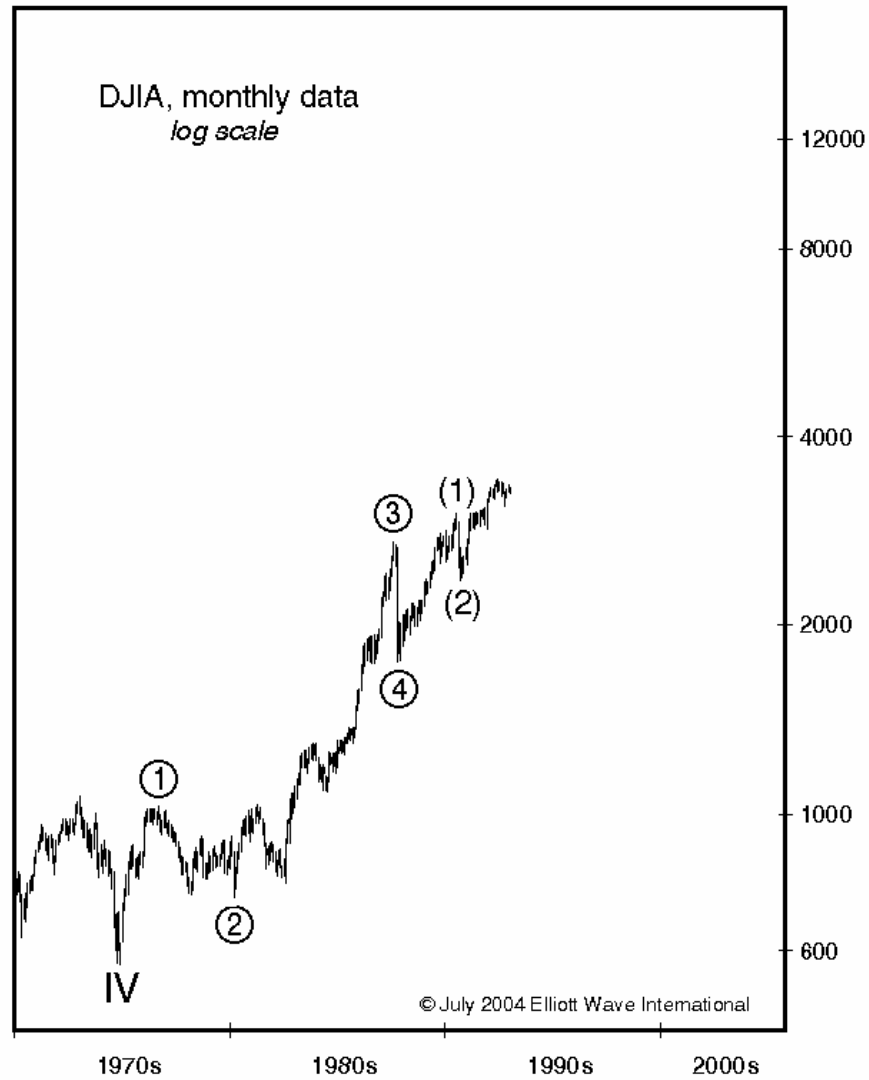
A parallel trend channel typically marks the upper and lower boundaries of impulse waves and zigzag corrective waves.

Guidelines

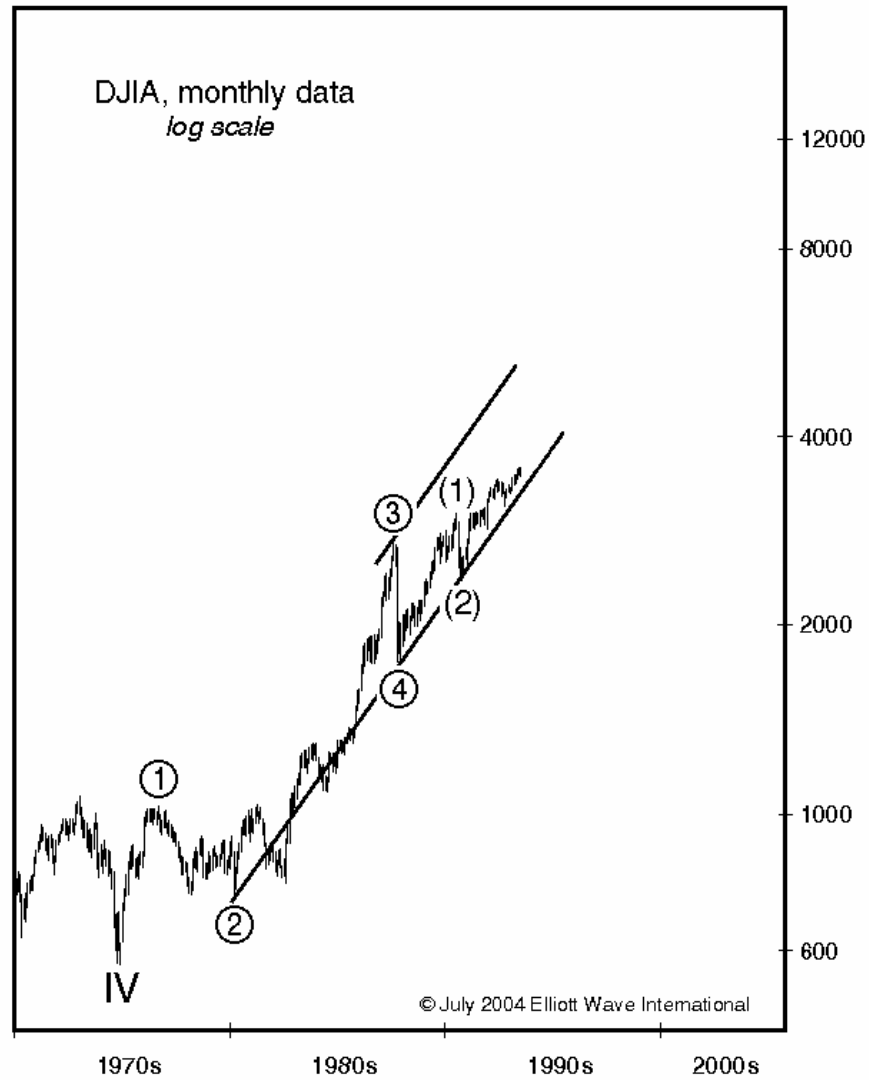
Channeling in Impulse Waves



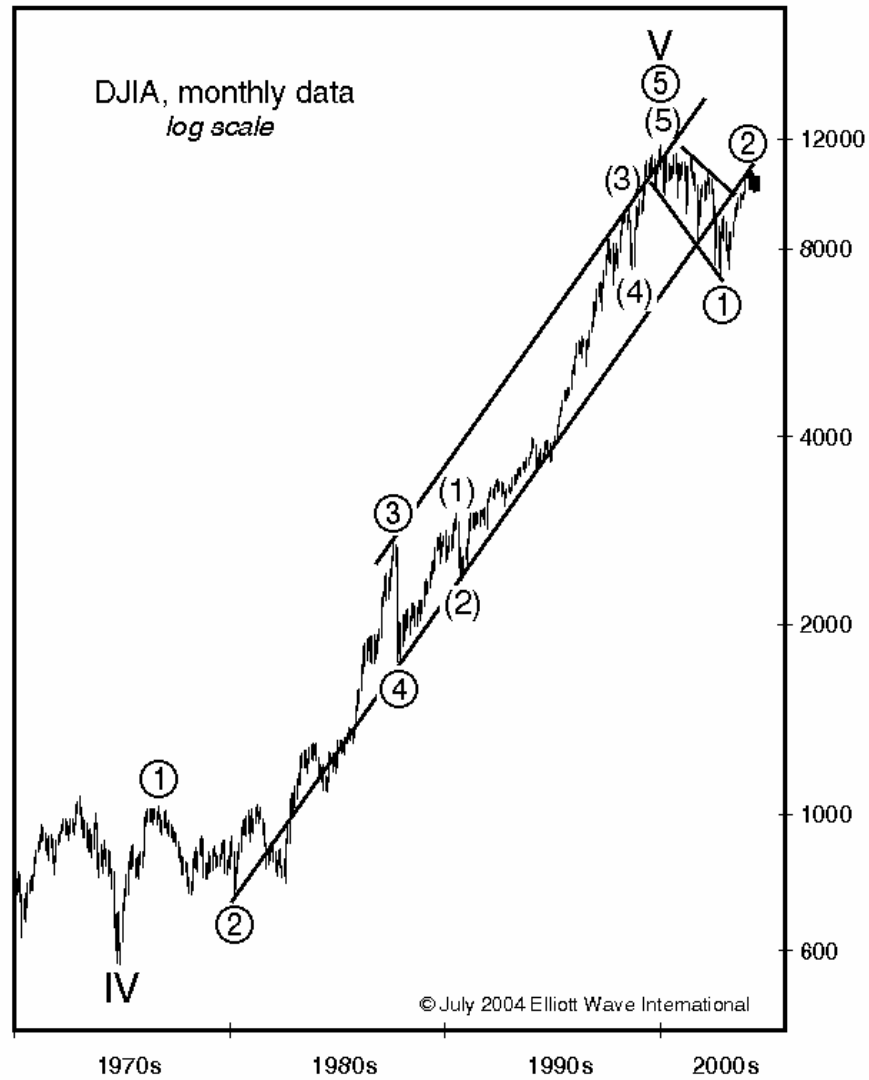
Channeling in Impulse Waves



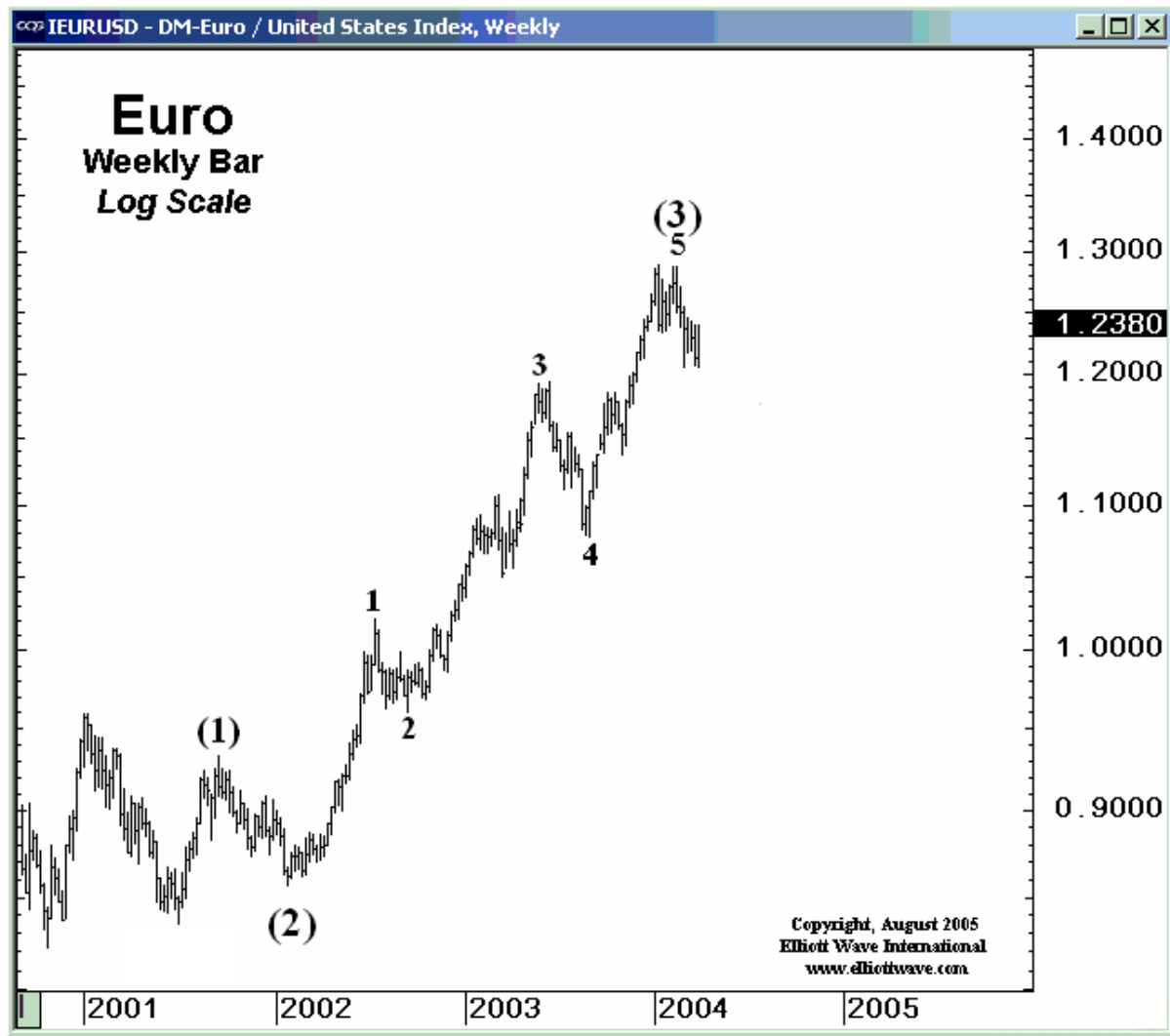
Channeling in Impulse Waves



Channeling in Impulse Waves



Channeling in Impulse Waves



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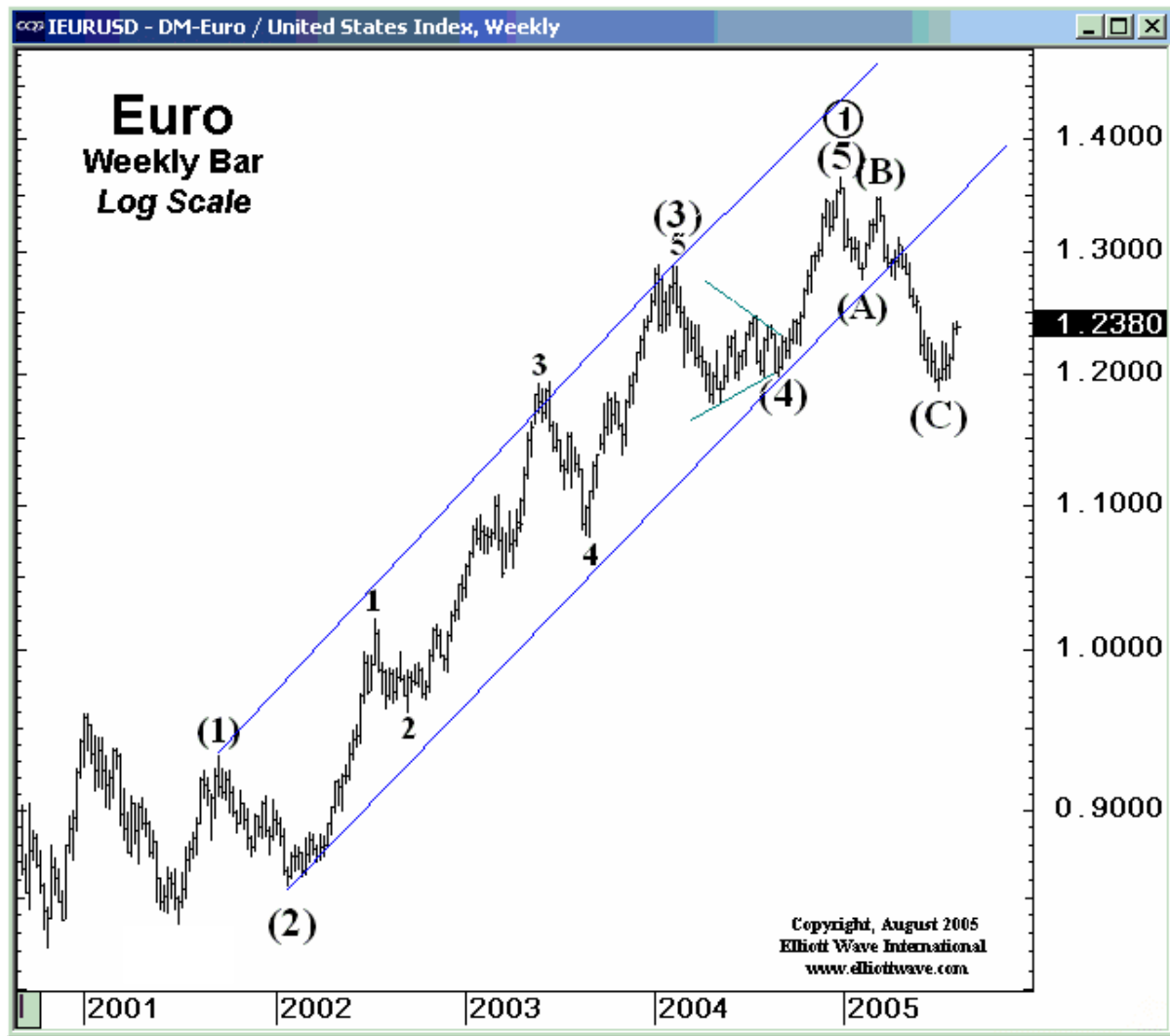
Channeling in Impulse Waves



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Channeling in Impulse Waves

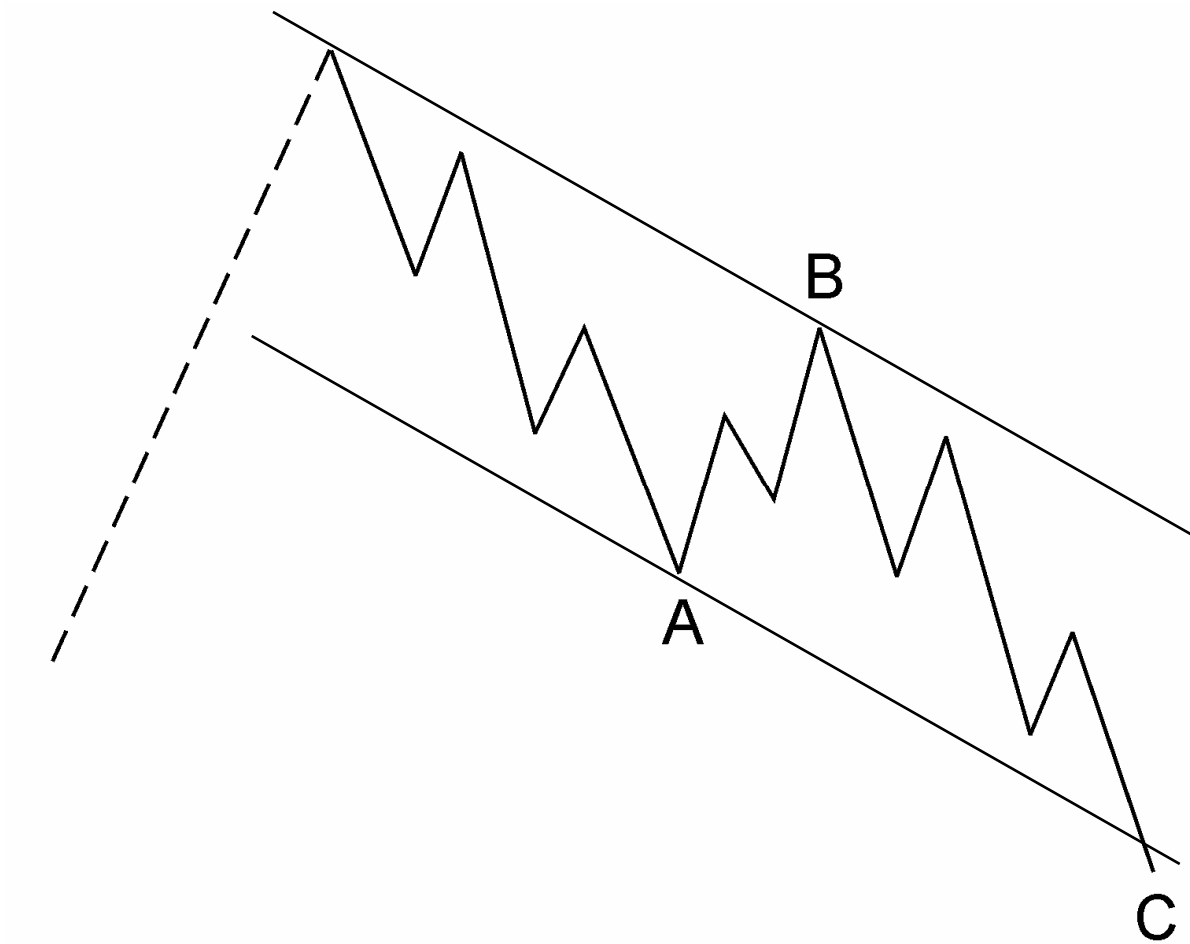


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Guidelines

Channeling in Zigzags



Channeling in Corrective Waves



Tue Aug 23 2005 13:08:20

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Channeling in Corrective Waves

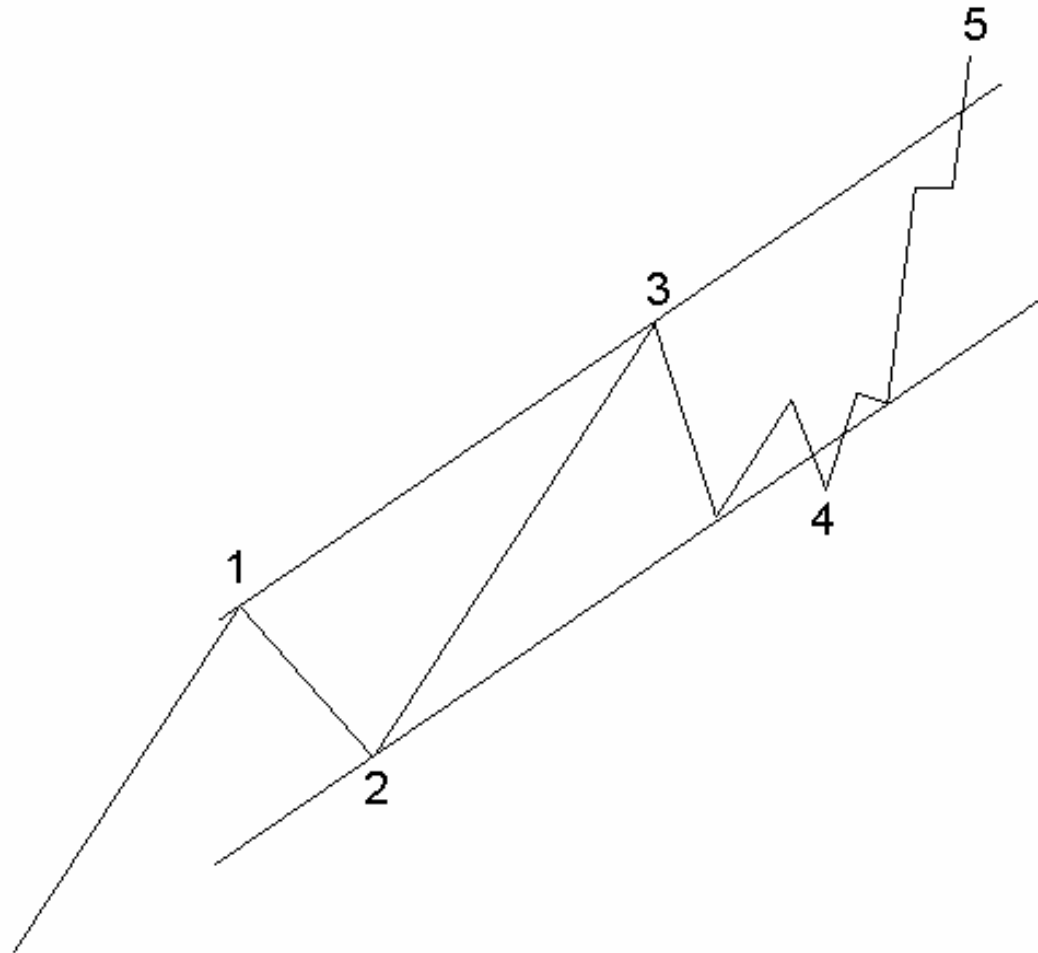


Channeling in Corrective Waves

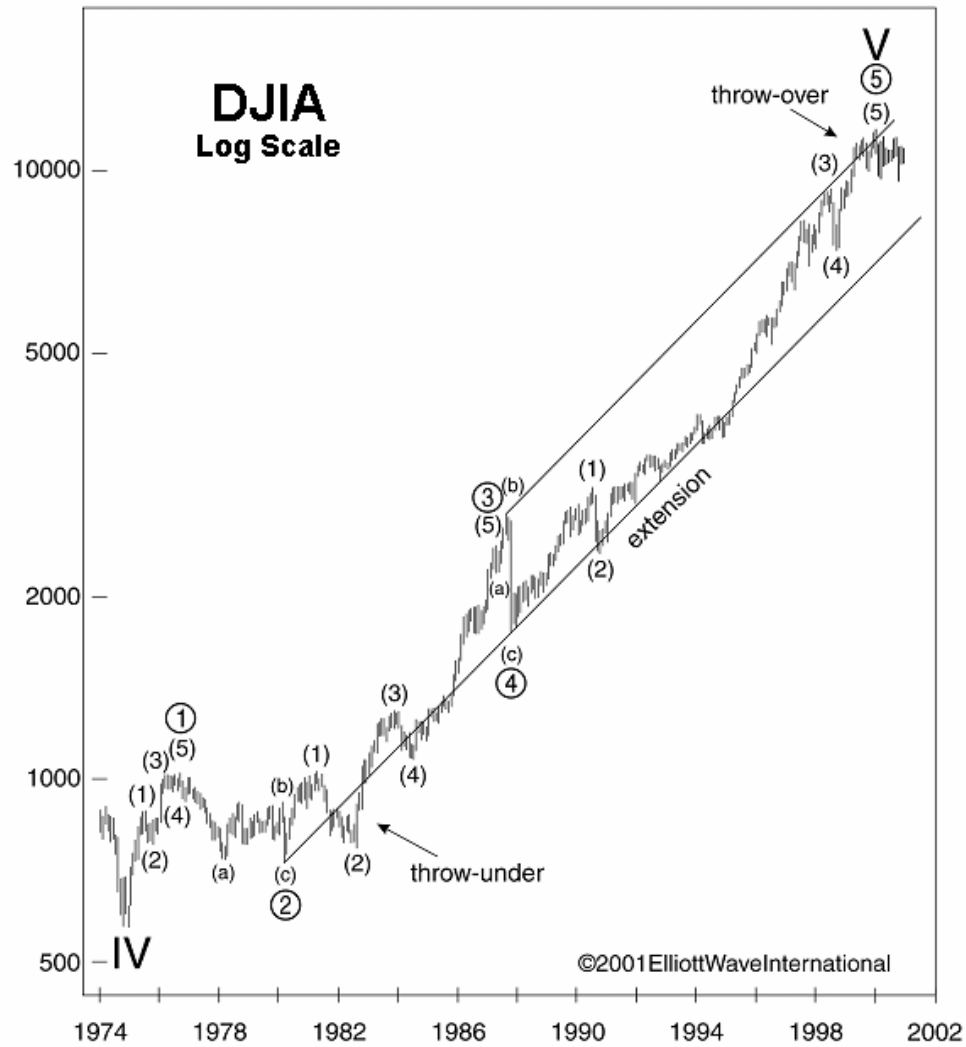


Guidelines

Throw-Over



Throw-Over



Guidelines — Volume

Waves < Primary Degree

Normally, 3rd wave volume > 5th wave volume

5th wave volume \geq 3rd wave volume = 5th wave extension

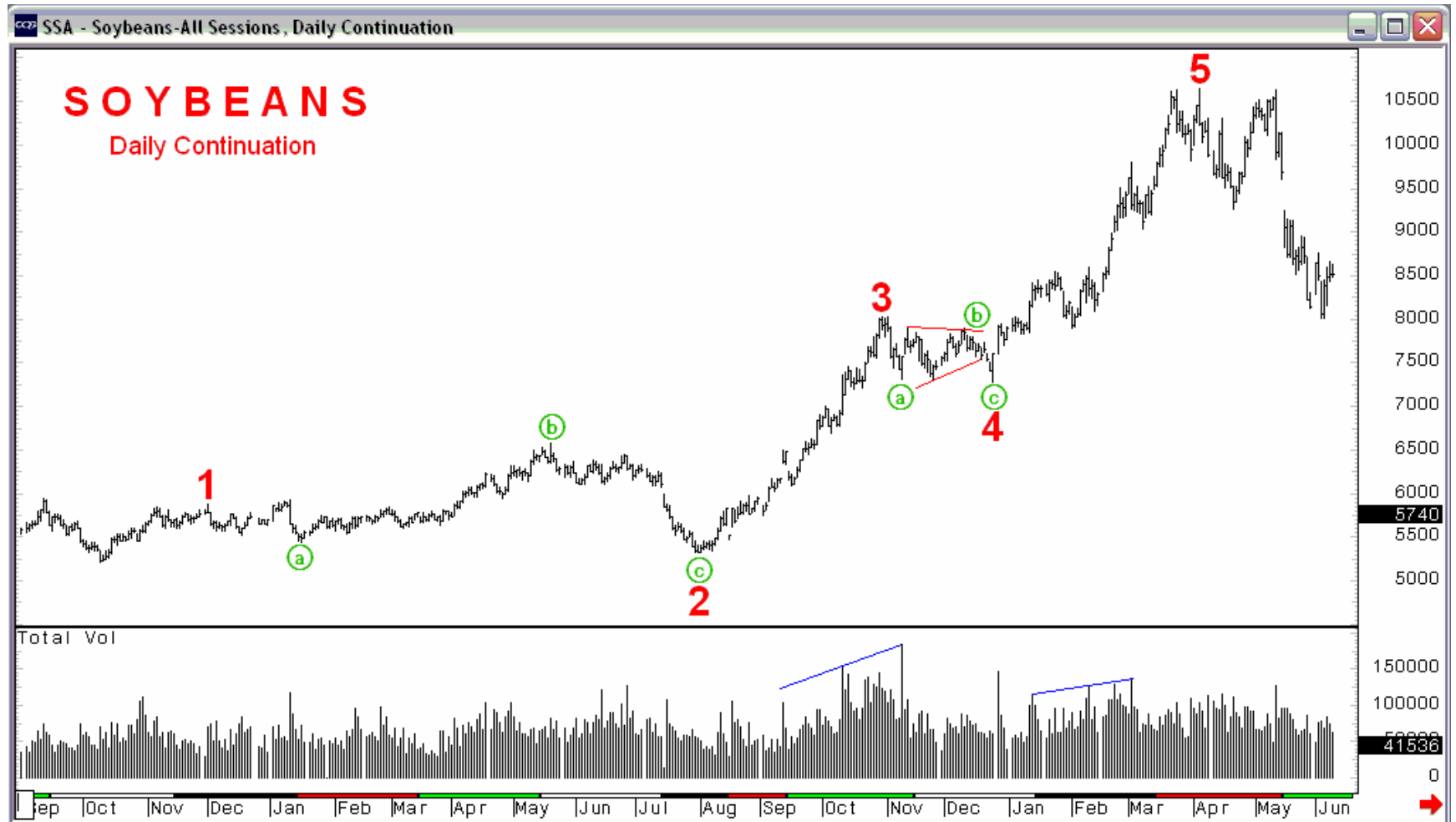
Waves \geq Primary Degree

Higher volume in 5th waves

All-time high volume at terminal points in bull markets

- Volume often spikes briefly at the throw-over point of a parallel trend channel line or a diagonal triangle resistance line.
- Volume contracts in corrective waves.

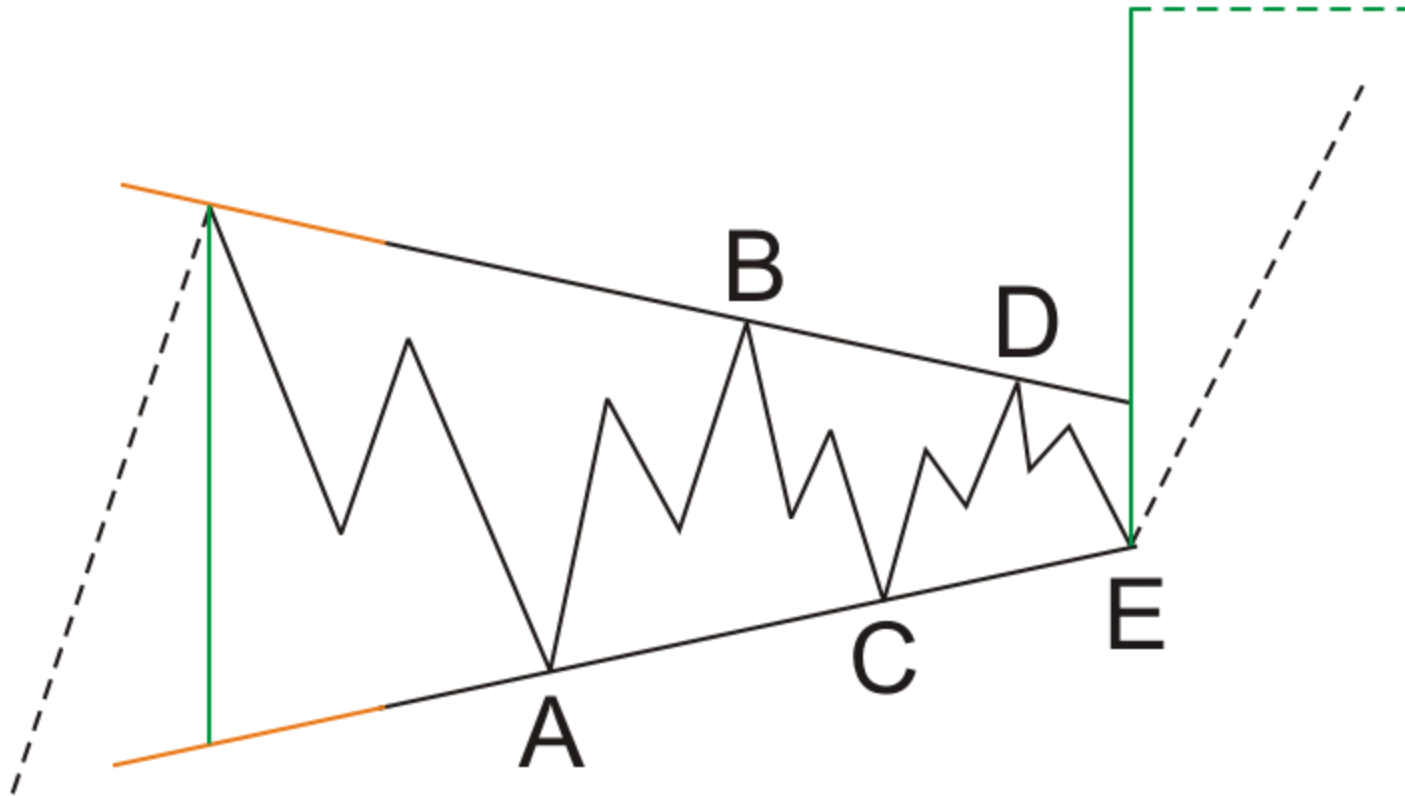
Volume

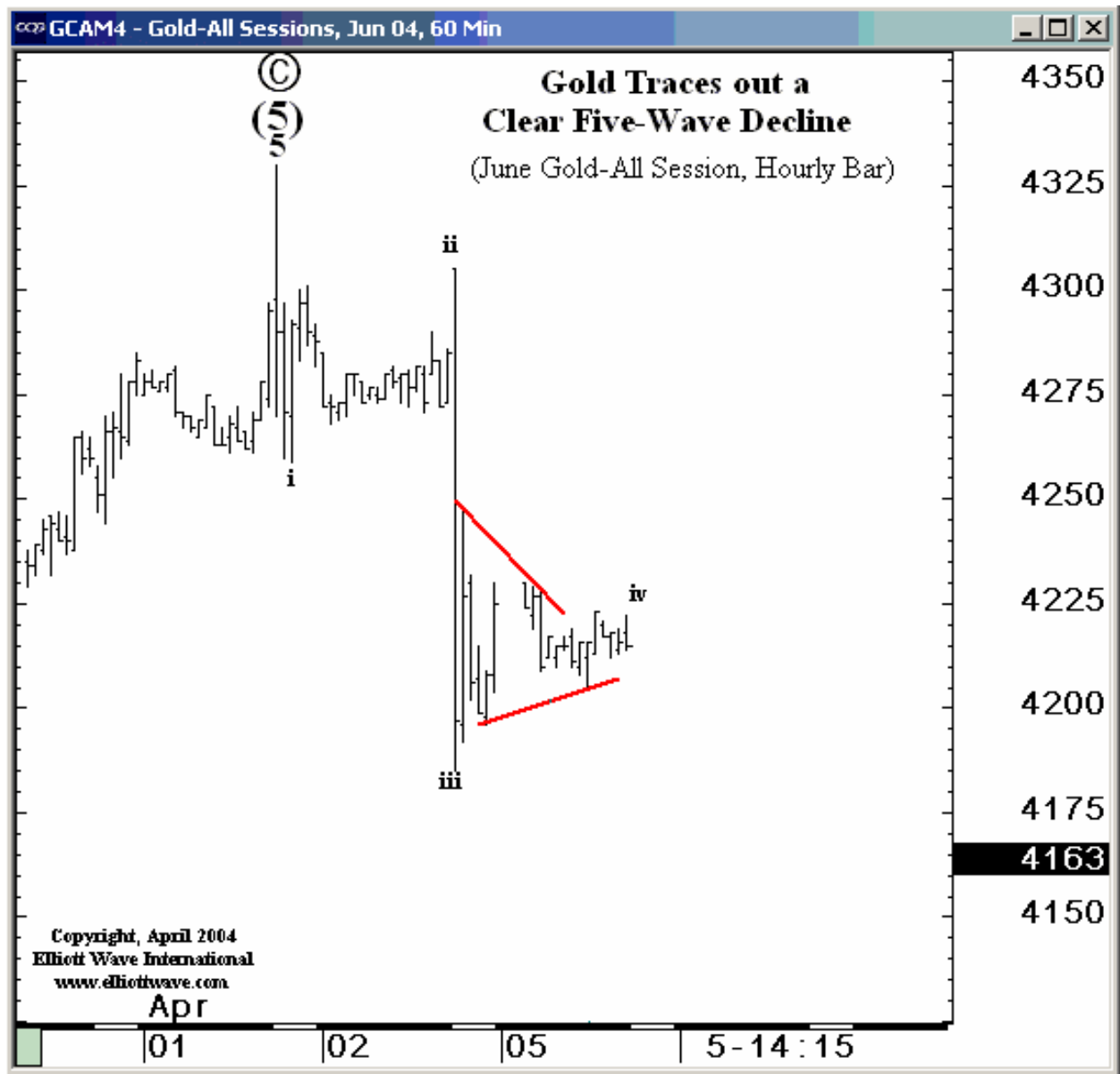


Tue Sep 20 2005 10:48:48

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Post-Triangle Thrust Measurement





Mon Apr 05 2004 13:48:41

CQG © 2004



Mon Apr 05 2004 13:48:41

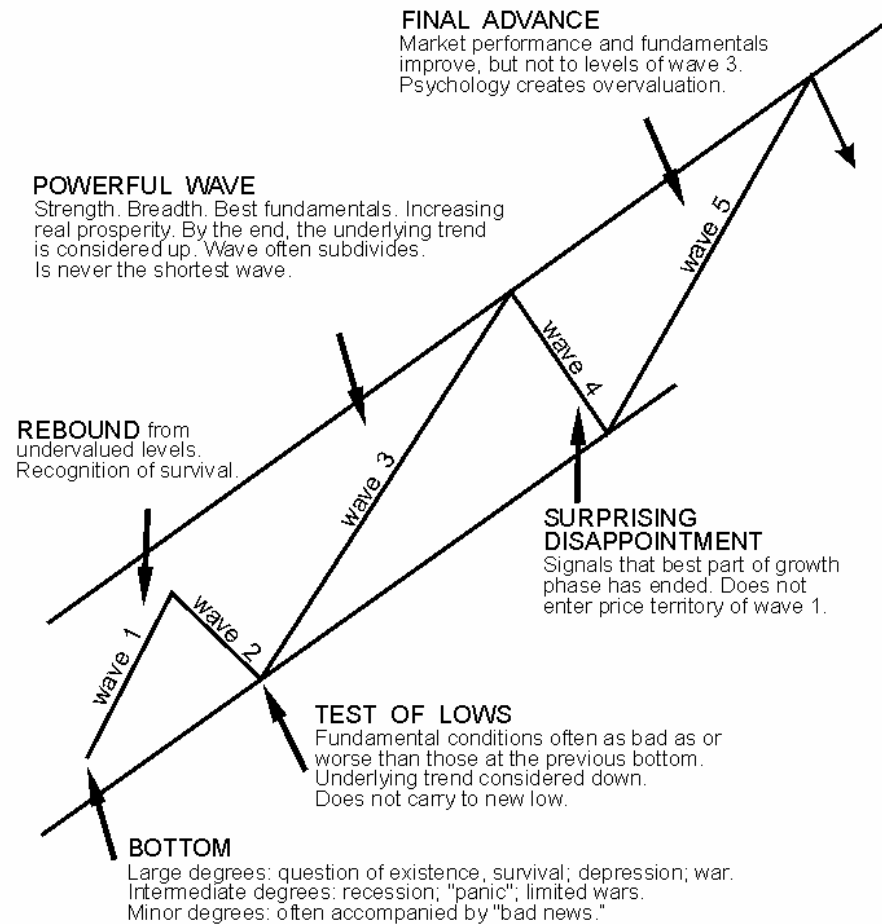
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Summary

- Two motive waves in a five wave sequence will tend toward equality.
- If the second wave is sharp, then the fourth wave is usually sideways, and vice versa.
- Corrective waves usually end in the span of the previous fourth wave of one lesser degree.
- Impulse waves tend to be bounded by a channel composed of two parallel lines.
- A throw-over/throw-under occurs when wave 5 terminates beyond the trend channel.
- The post-triangle thrust measurement estimates price target for the next wave in the pattern of one larger degree.

Wave Personality

Idealized Elliott Wave Progression



Wave Personality

Idealized Corrective Wave

TOP

Large degrees: prosperity and peace appear guaranteed forever. Arrogant complacency reigns.
Intermediate degrees: economic improvement, good feeling.
Minor degrees: often accompanied by "good news."

NARROW, EMOTIONAL ADVANCE

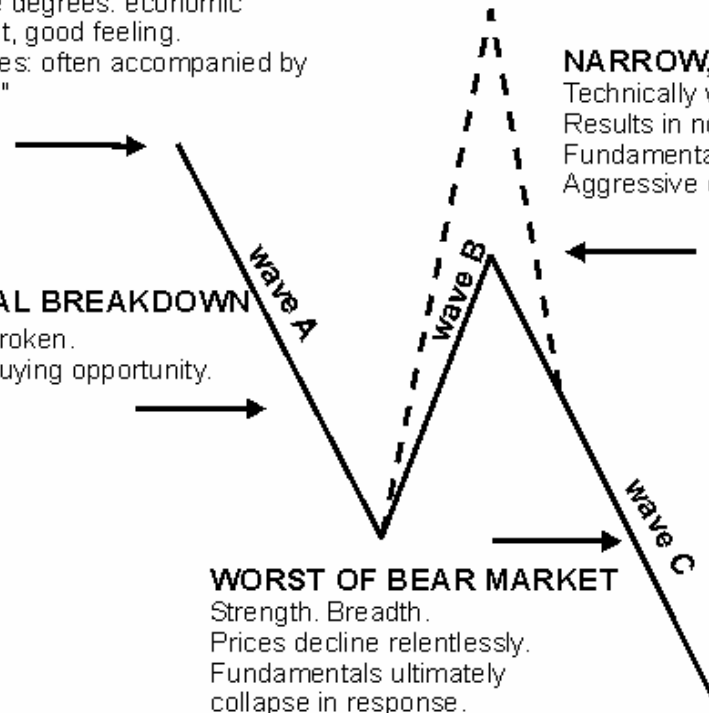
Technically weak, selective.
Results in non-confirmations.
Fundamentals weaken subtly.
Aggressive euphoria and denial.

TECHNICAL BREAKDOWN

Trendlines broken.
Viewed as buying opportunity.

WORST OF BEAR MARKET

Strength. Breadth.
Prices decline relentlessly.
Fundamentals ultimately collapse in response.



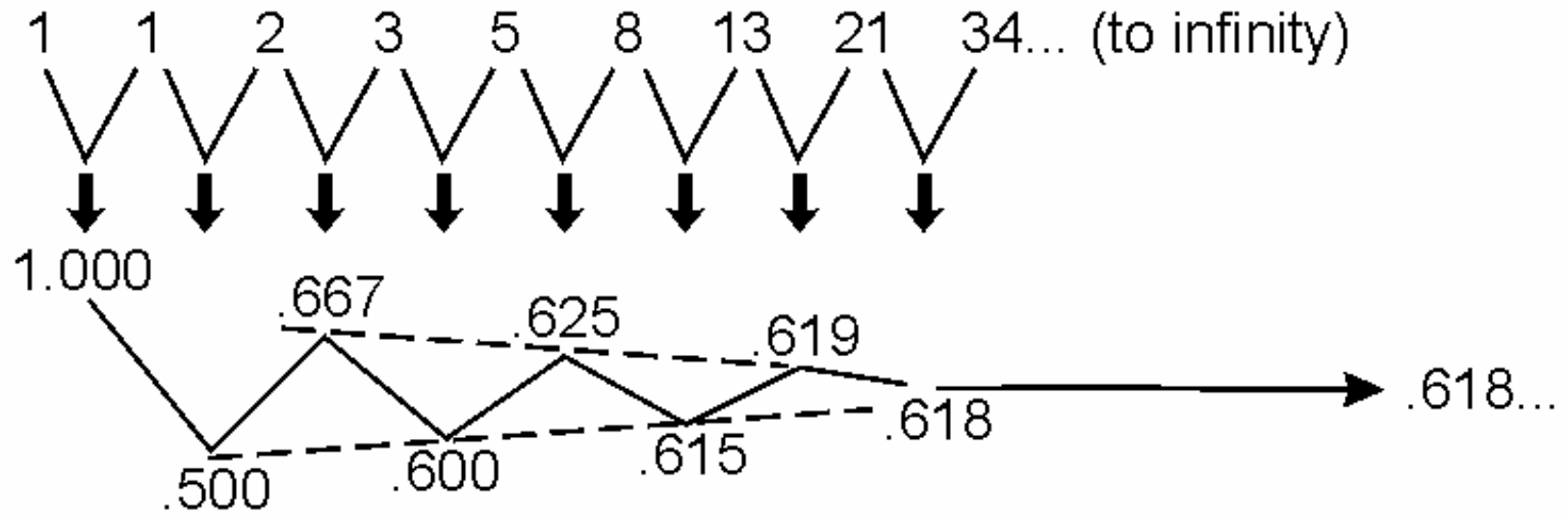
Fibonacci Relationships In Financial Markets

The Golden Ratio

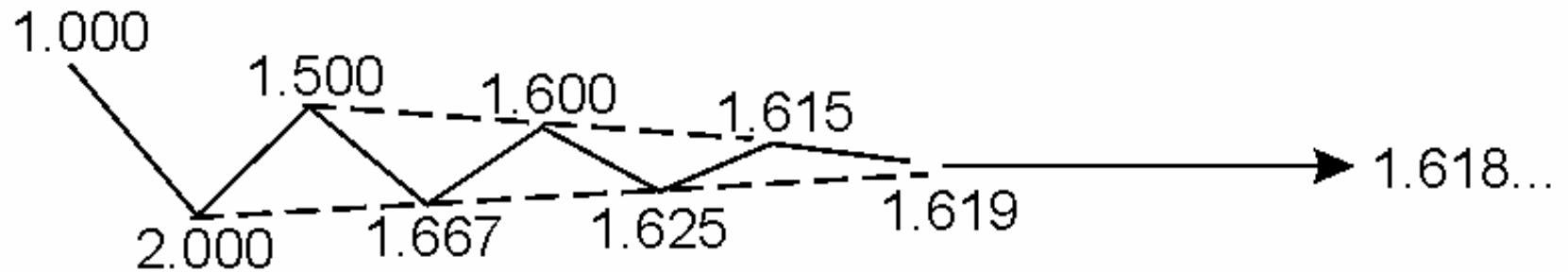
PHI Φ

.618 or 1.618

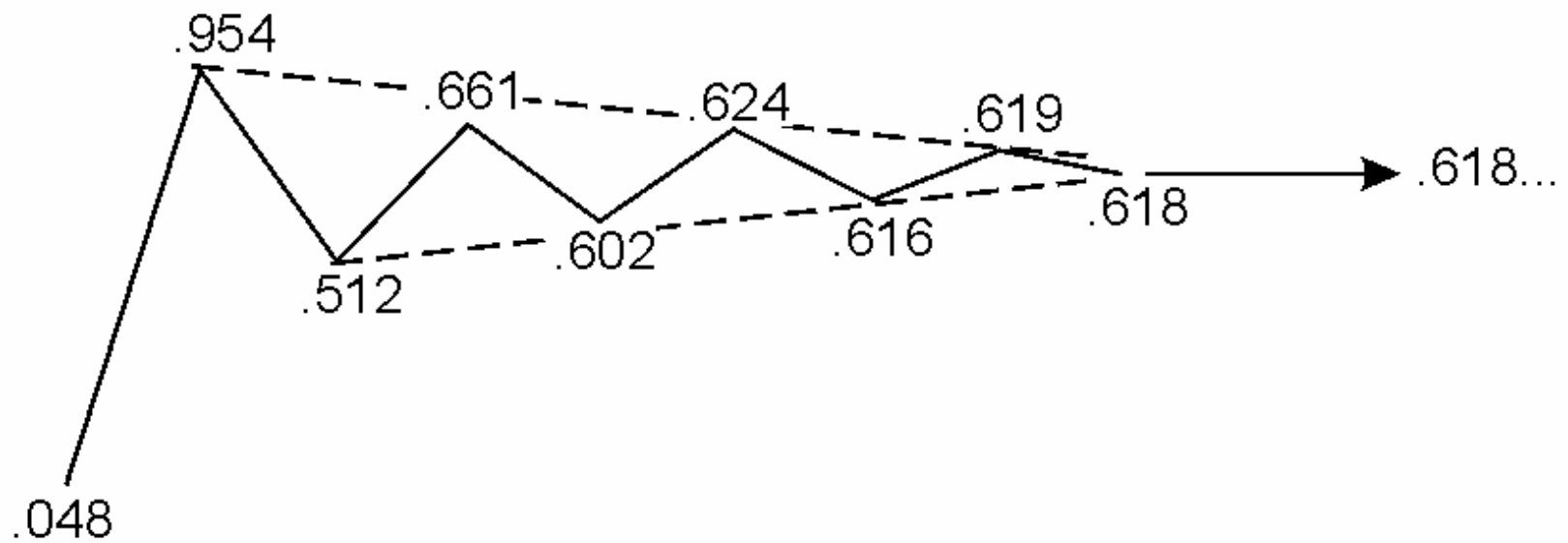
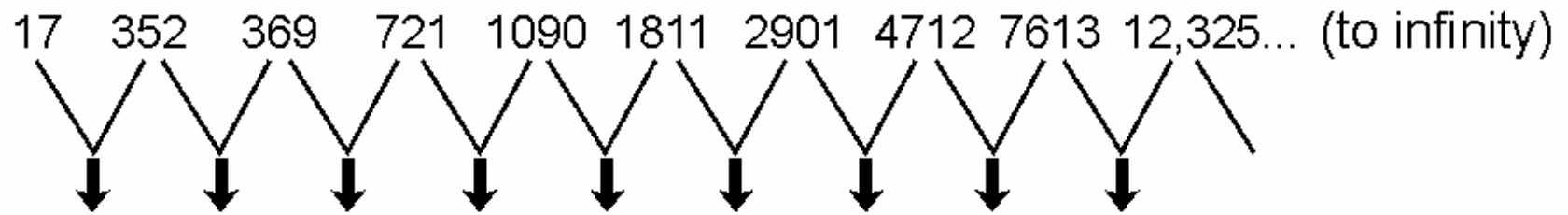
Golden Ratio, PHI, Φ



Inverses:



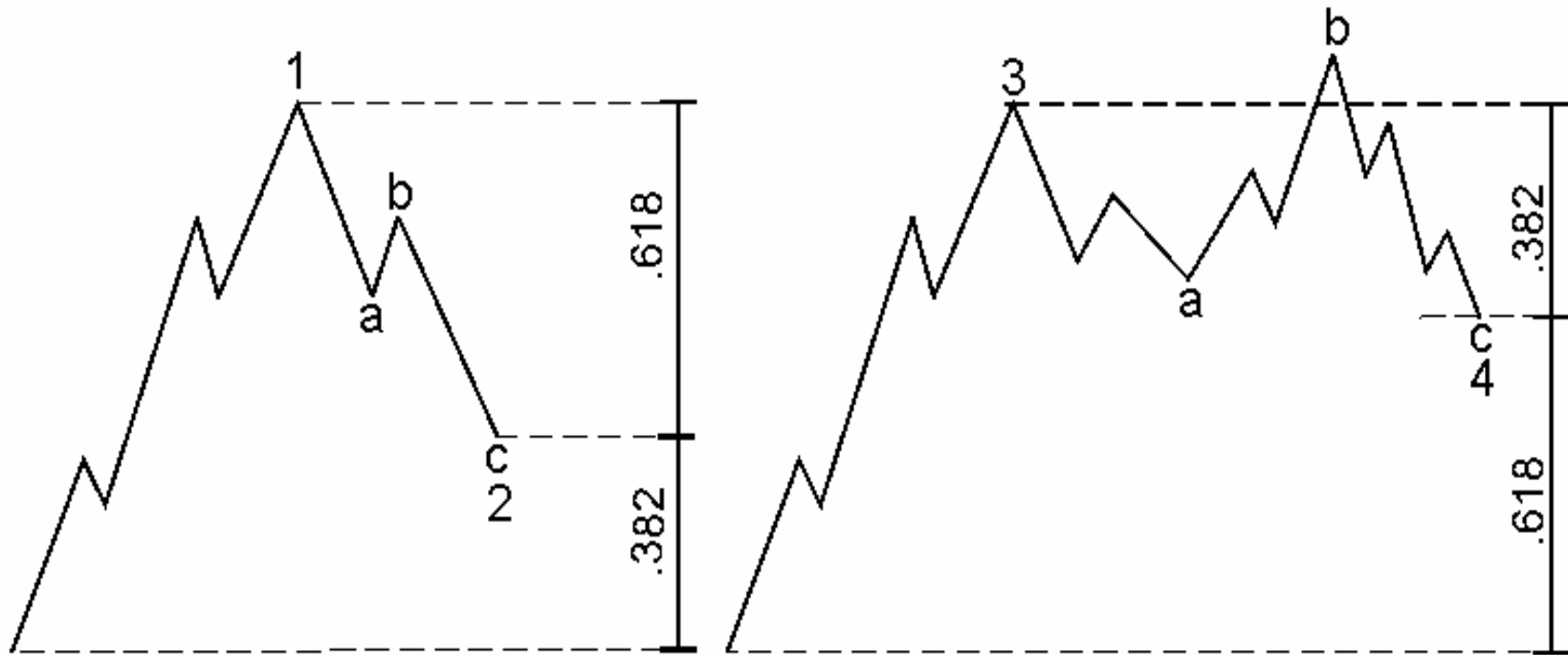
Golden Ratio, PHI, Φ



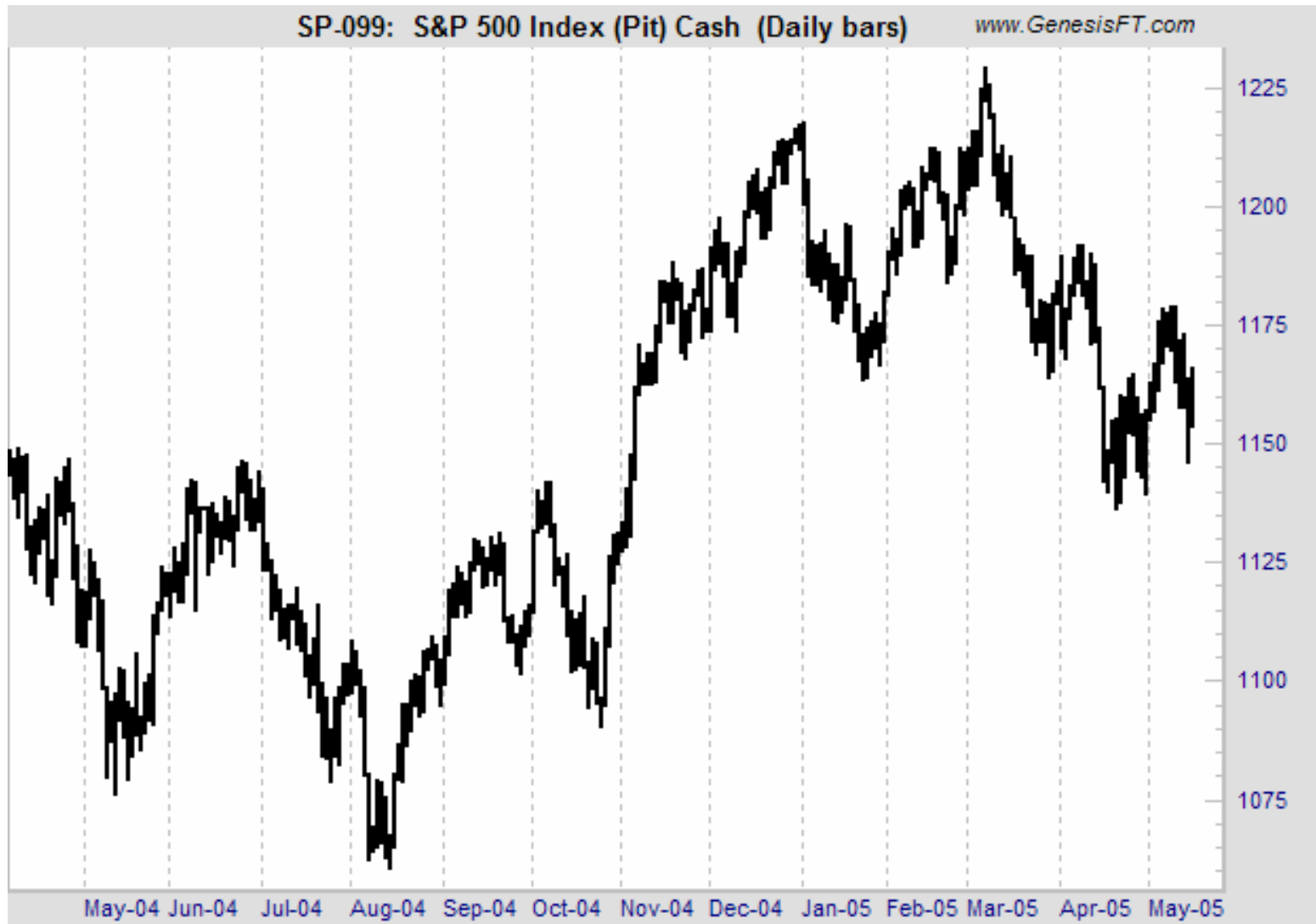
Fibonacci Relationships are Seen in Time and Amplitude

- Retracements
- Multiples

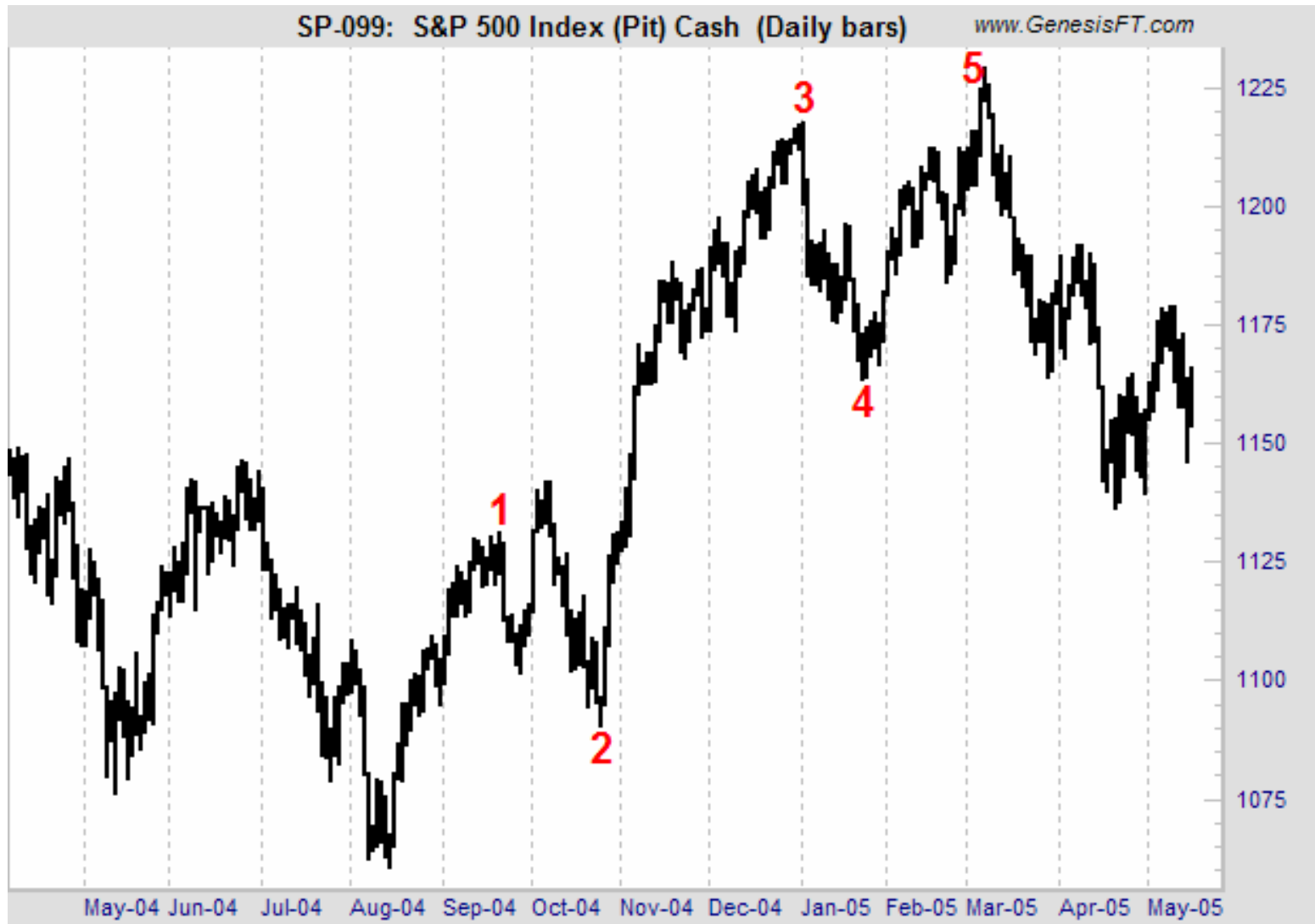
Retracements



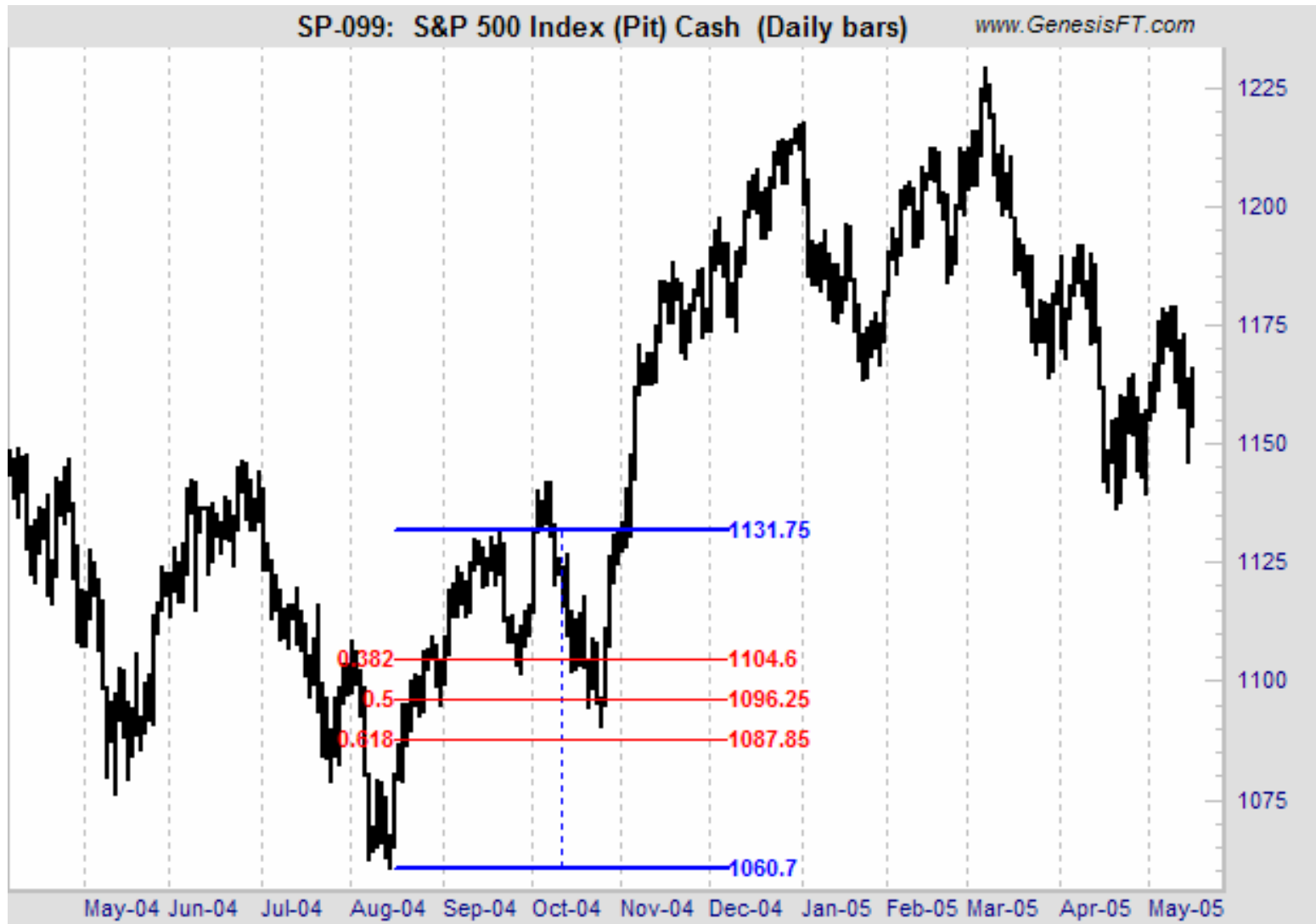
Retracements



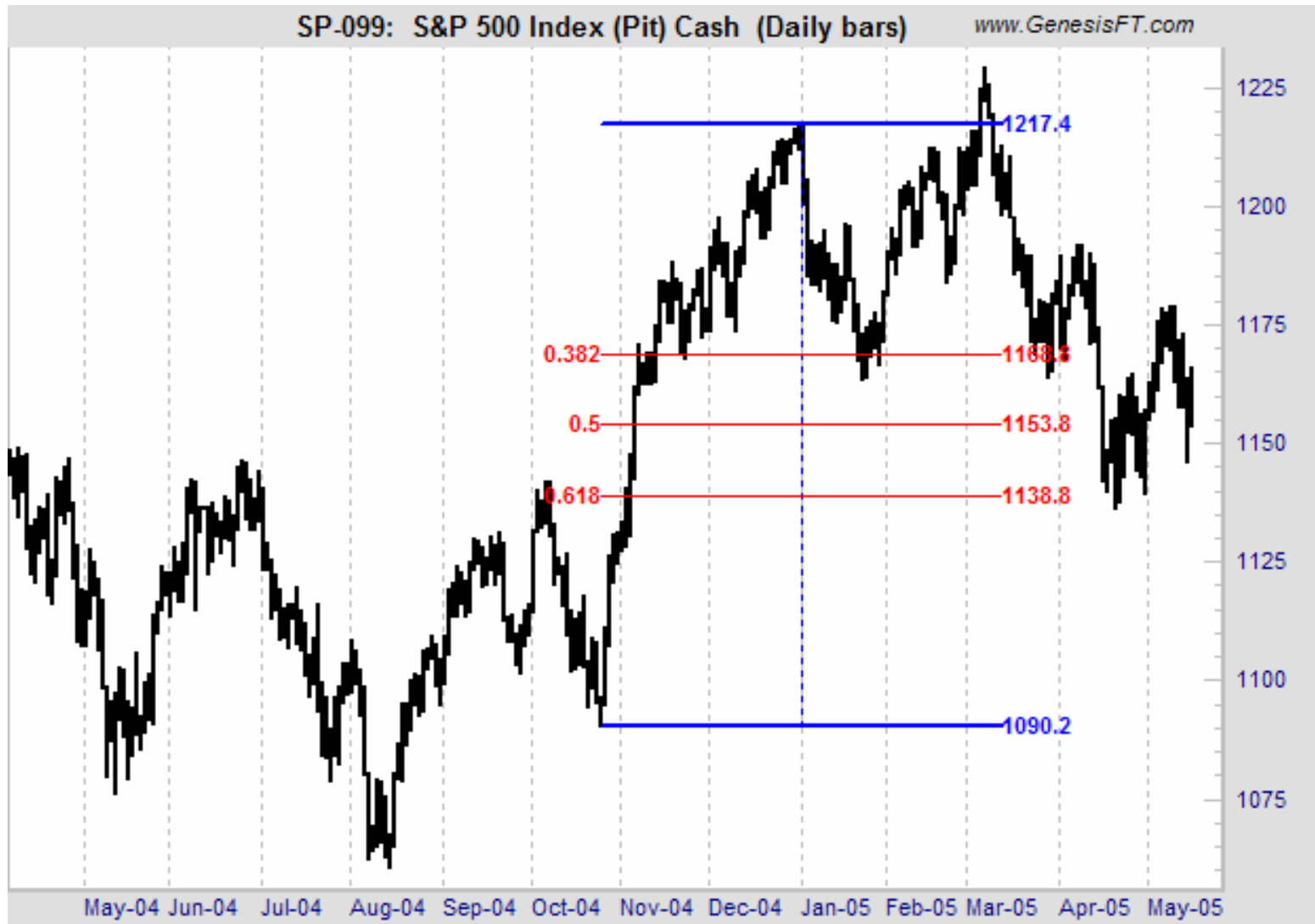
Retracements



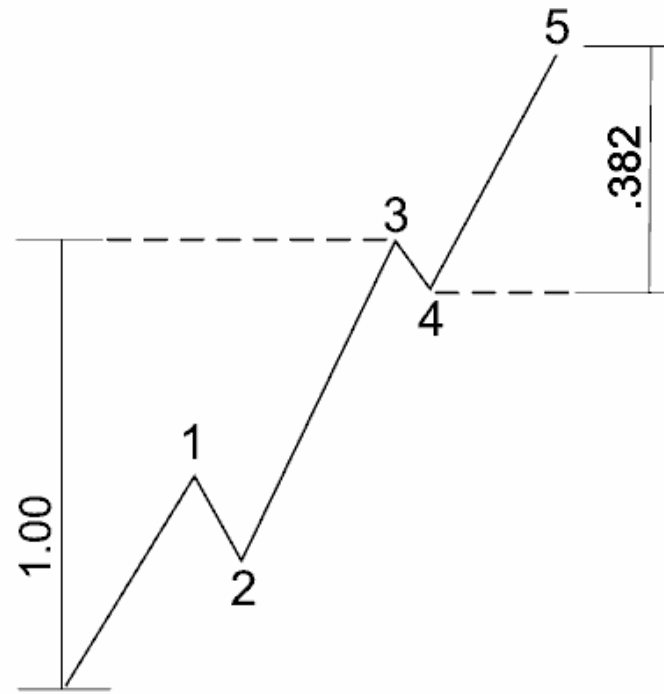
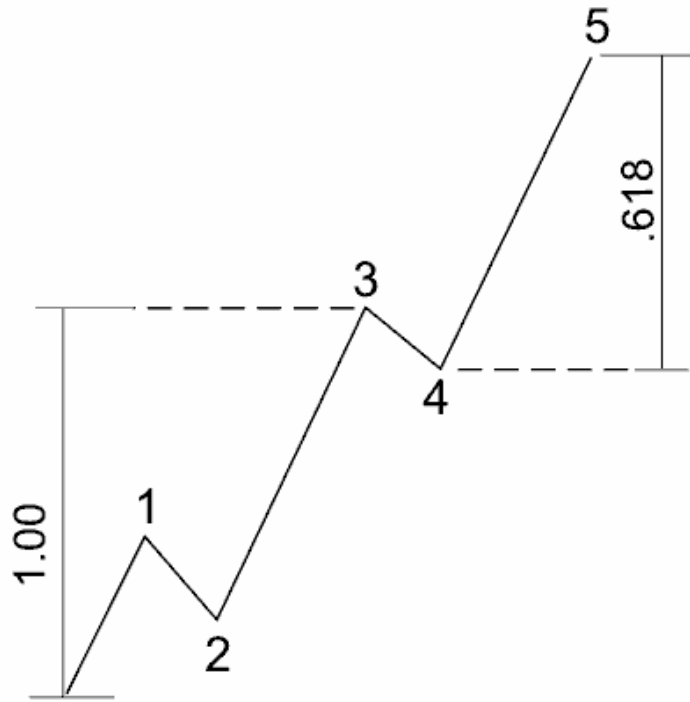
Retracements



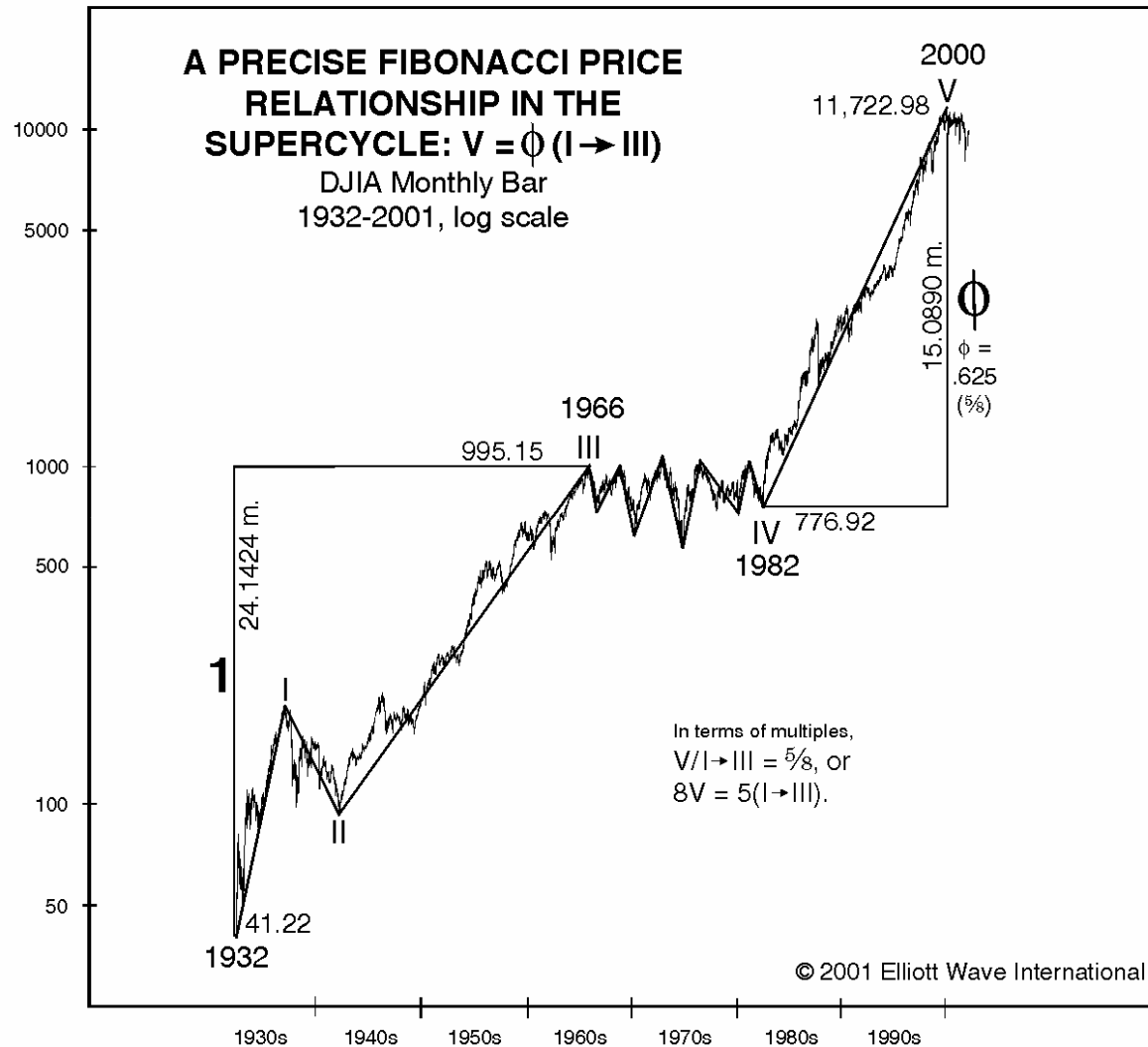
Retracements



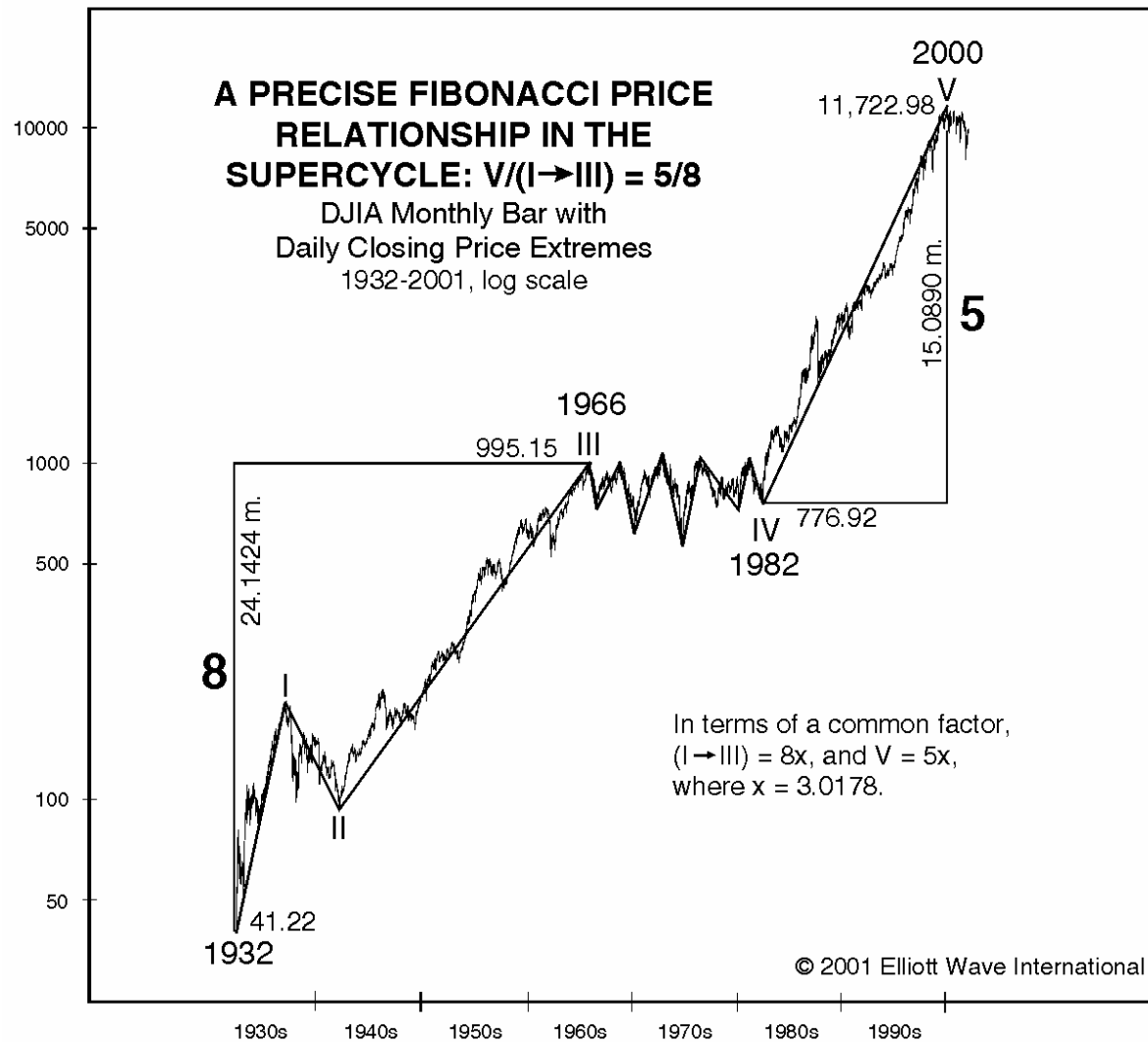
Multiples in Impulse Waves



Multiples in Impulse Waves

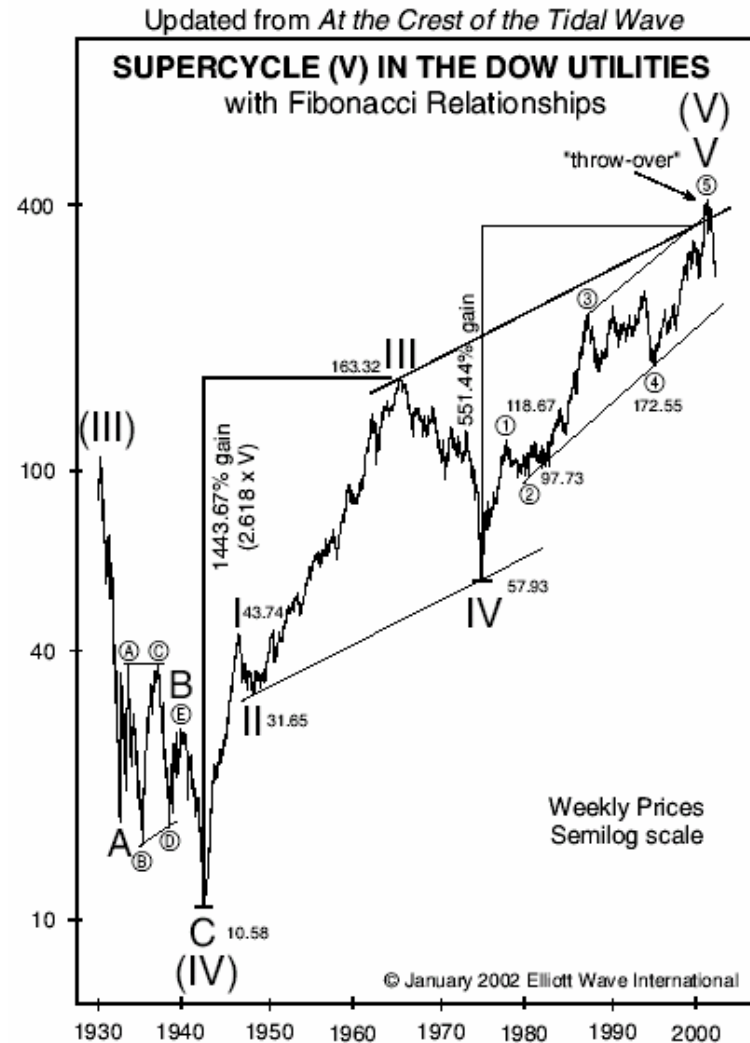


Multiples in Impulse Waves

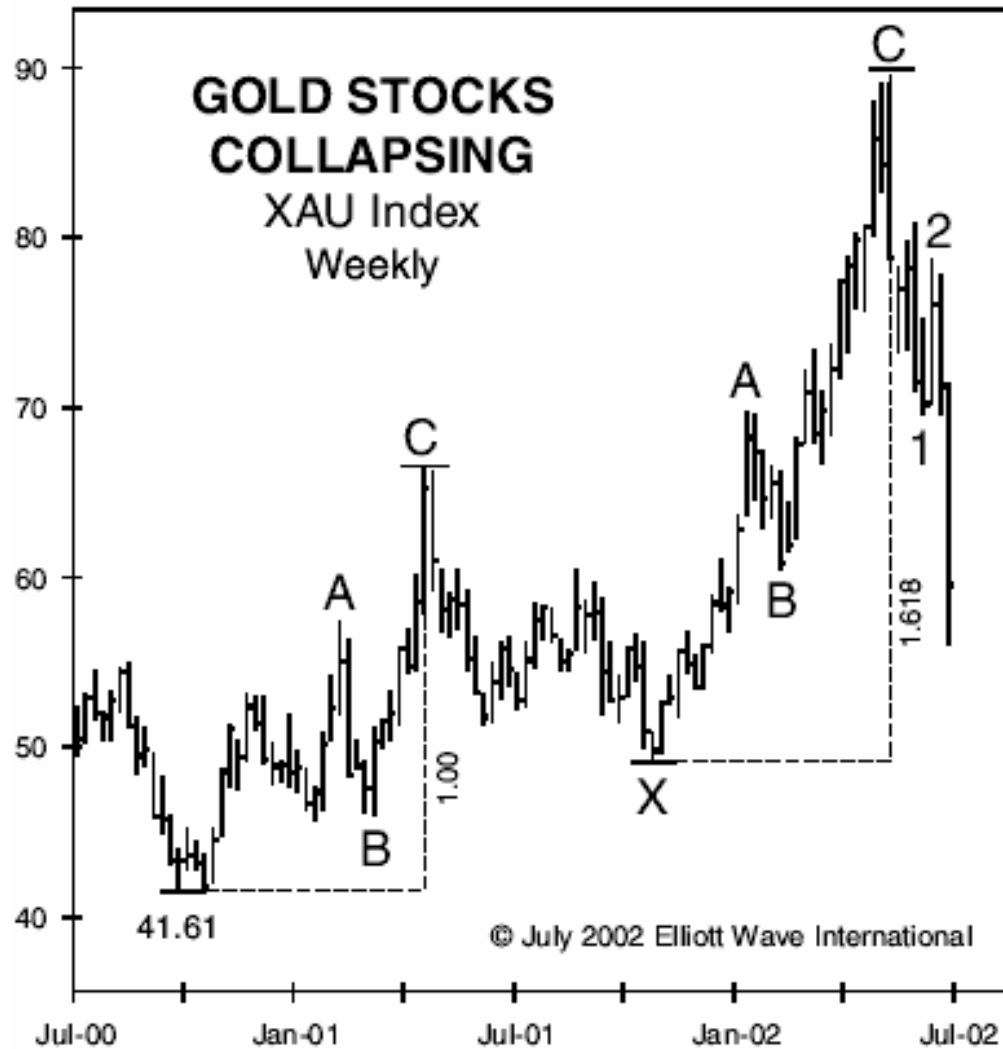


Multiples in Impulse Waves

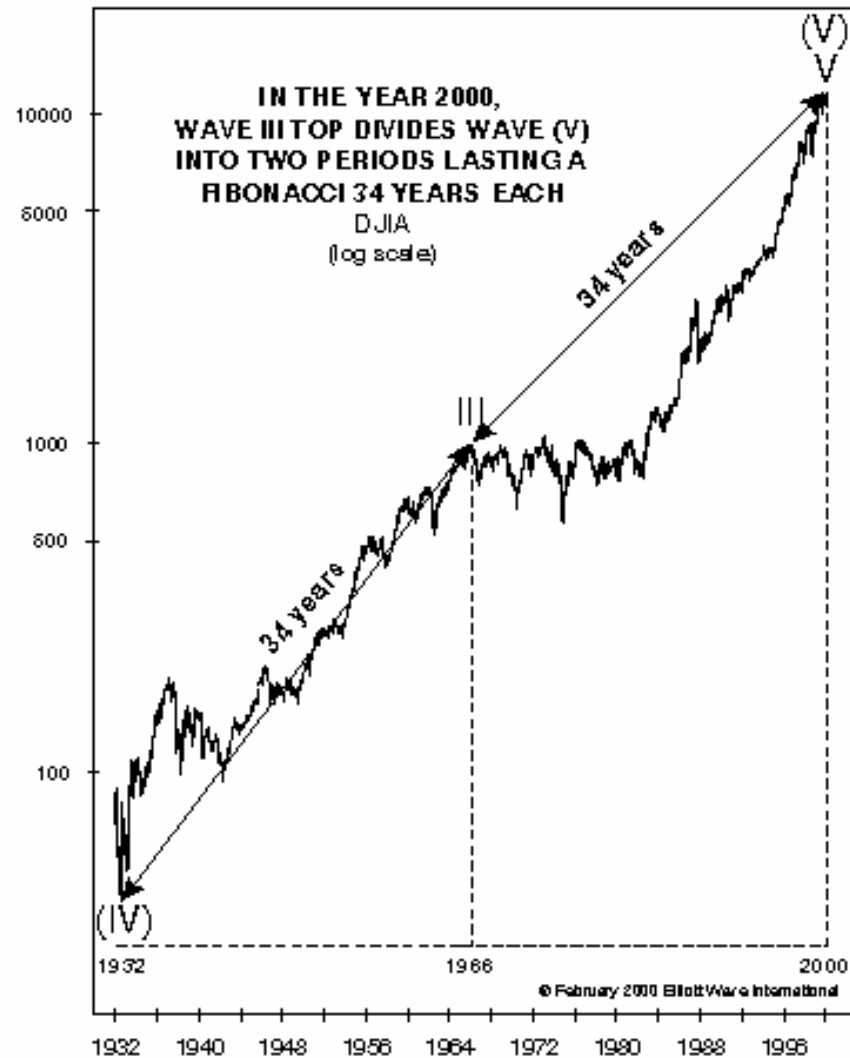
Net of waves 1 through 3 times .382 = percent movement of wave 5



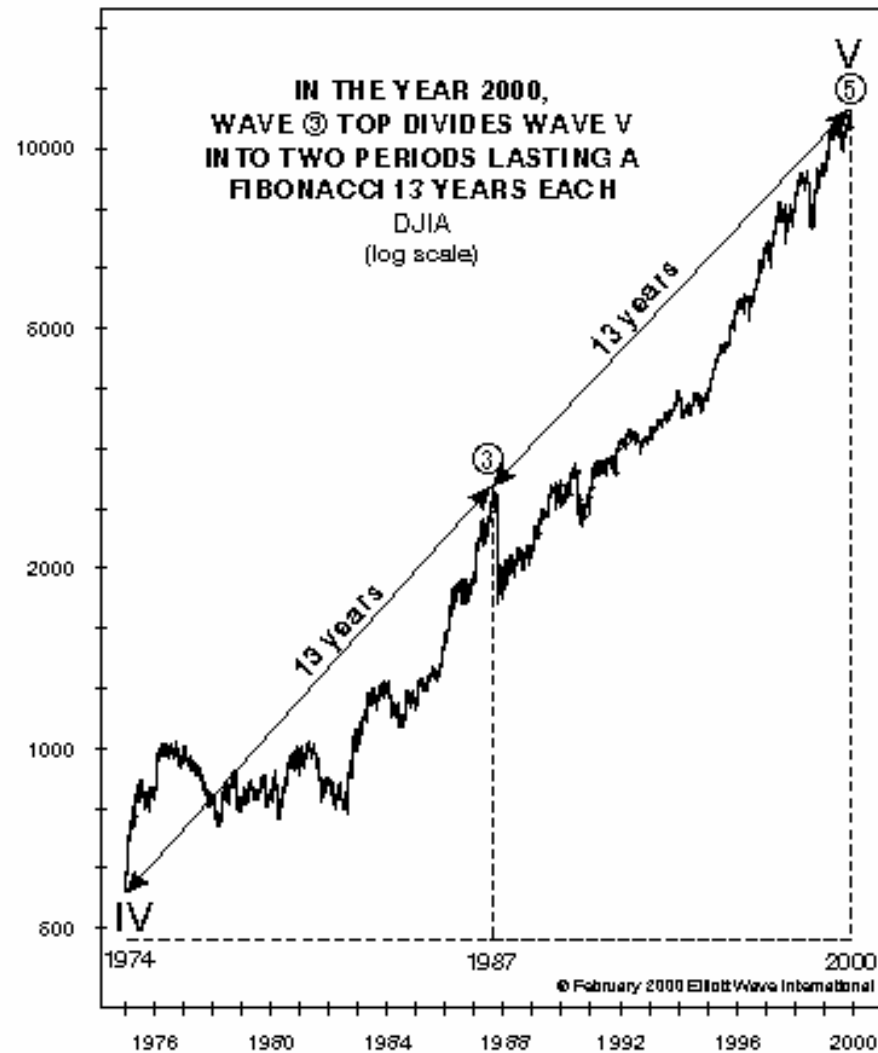
Multiples within Corrective Waves — Zigzags



Fibonacci Time Relationships



Fibonacci Time Relationships



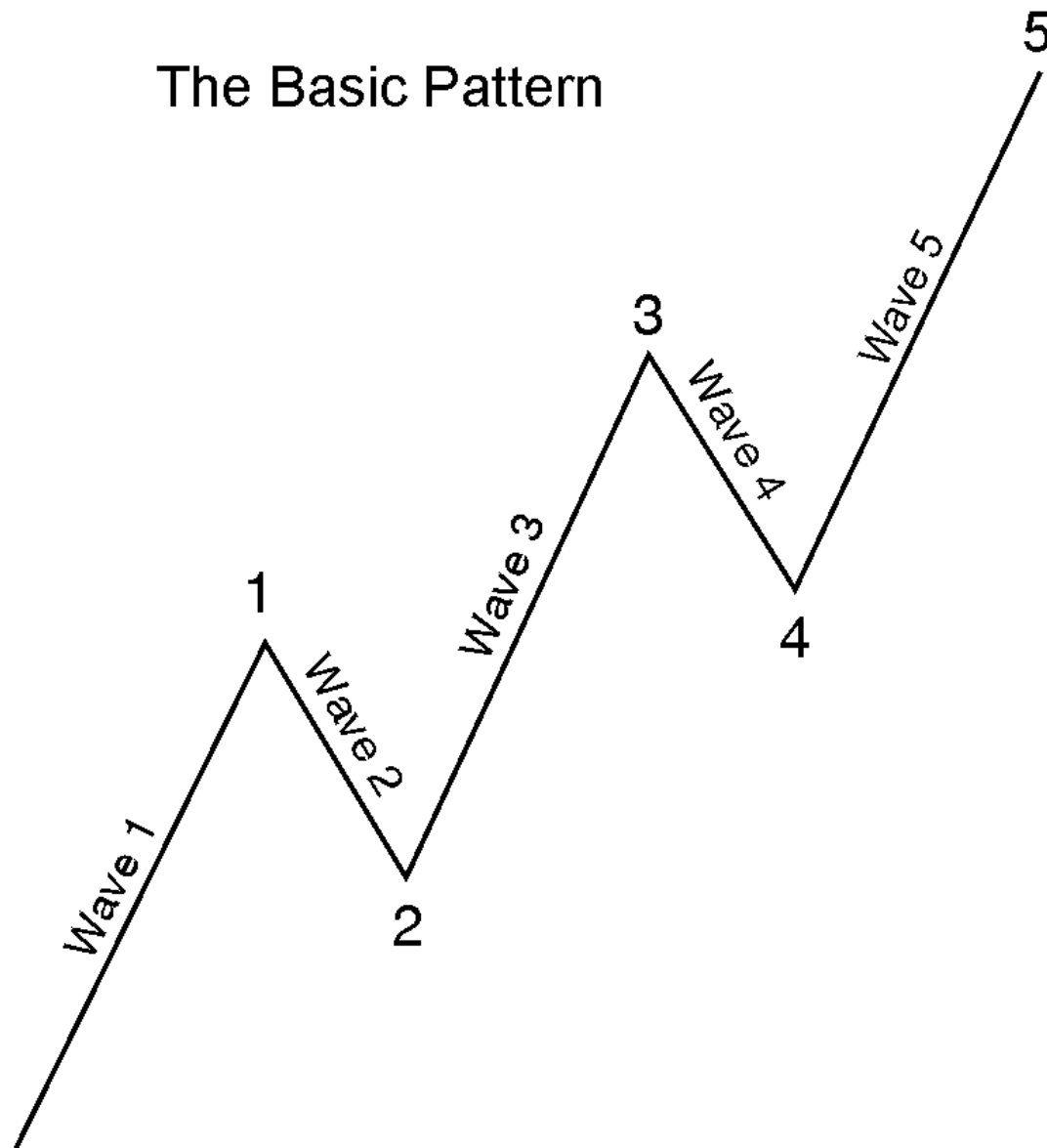
Summary

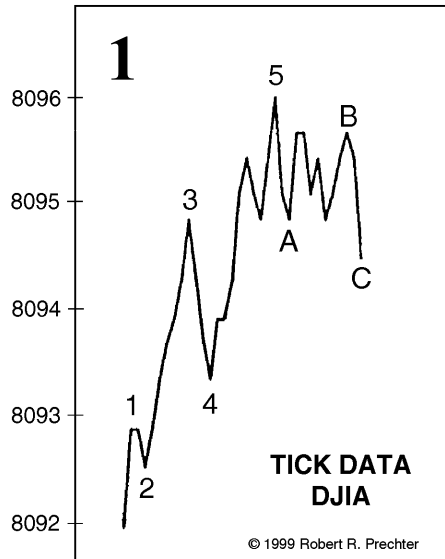
- The Fibonacci Ratio (Φ), an irrational number approximating .618, known as the Golden Ratio, is found in nature, human biology, human thought, and aggregate human behavior such as the stock market.
- The Wave Principle is a robust fractal governed by Fibonacci mathematics.
- Sharp wave corrections tend to retrace 61.8% or 50% of the previous wave.
- Sideways corrections tend to retrace 38.2% of the previous wave.
- Subdivisions of impulse waves tend to be related by Fibonacci numbers .618, 1.0, 1.618 and 2.618.
- Subdivisions of corrective waves tend to be related by Fibonacci numbers .382, .618, 1.0 and 1.618.

The Basics of the Wave Principle

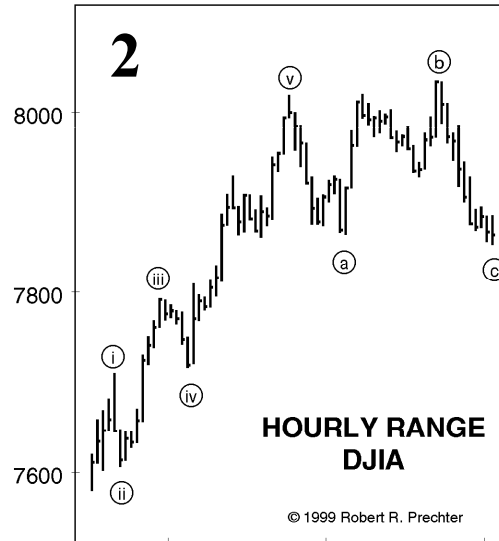
Summary

The Basic Pattern

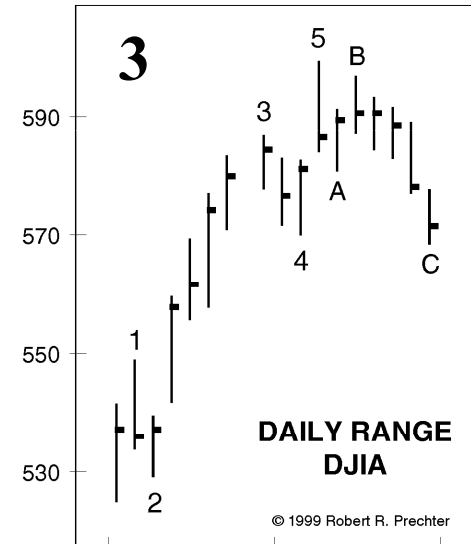




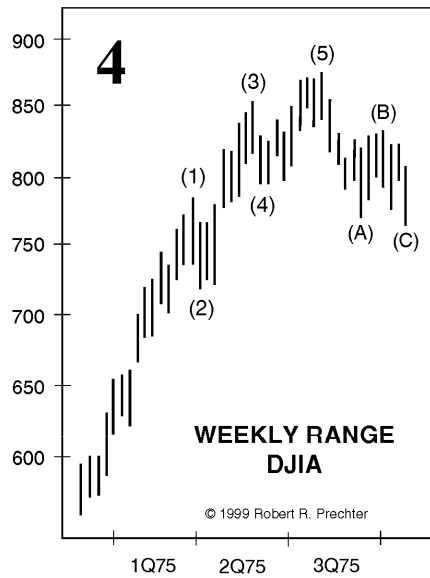
Oct. 6, 1997 3:56-3:59 E.S.T



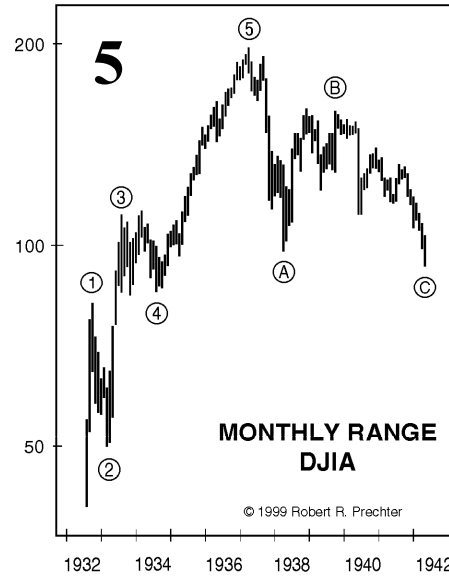
9/15/97 9/19/97 9/25/97



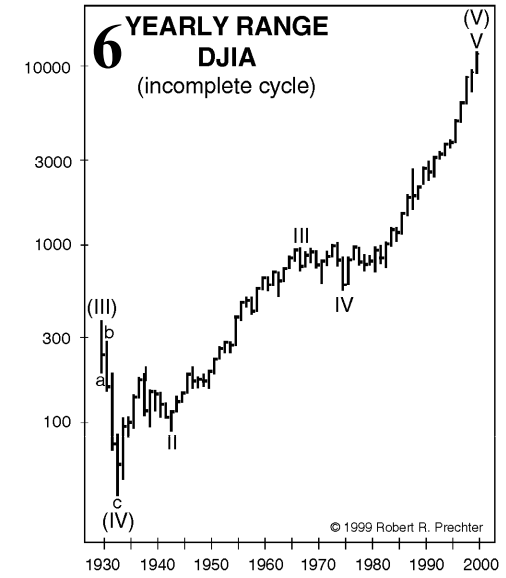
6/25/62 7/6/62 7/19/62



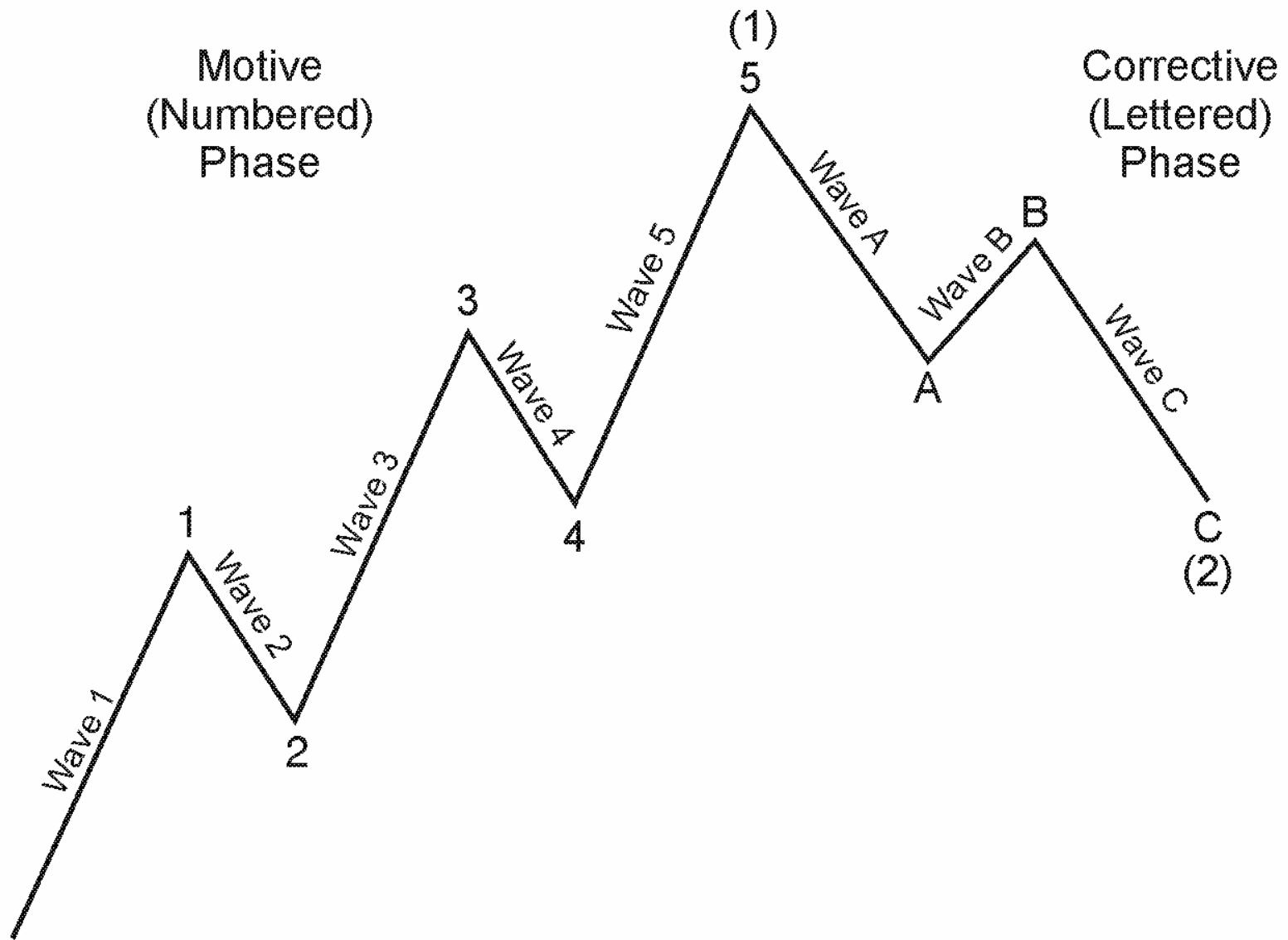
1Q75 2Q75 3Q75

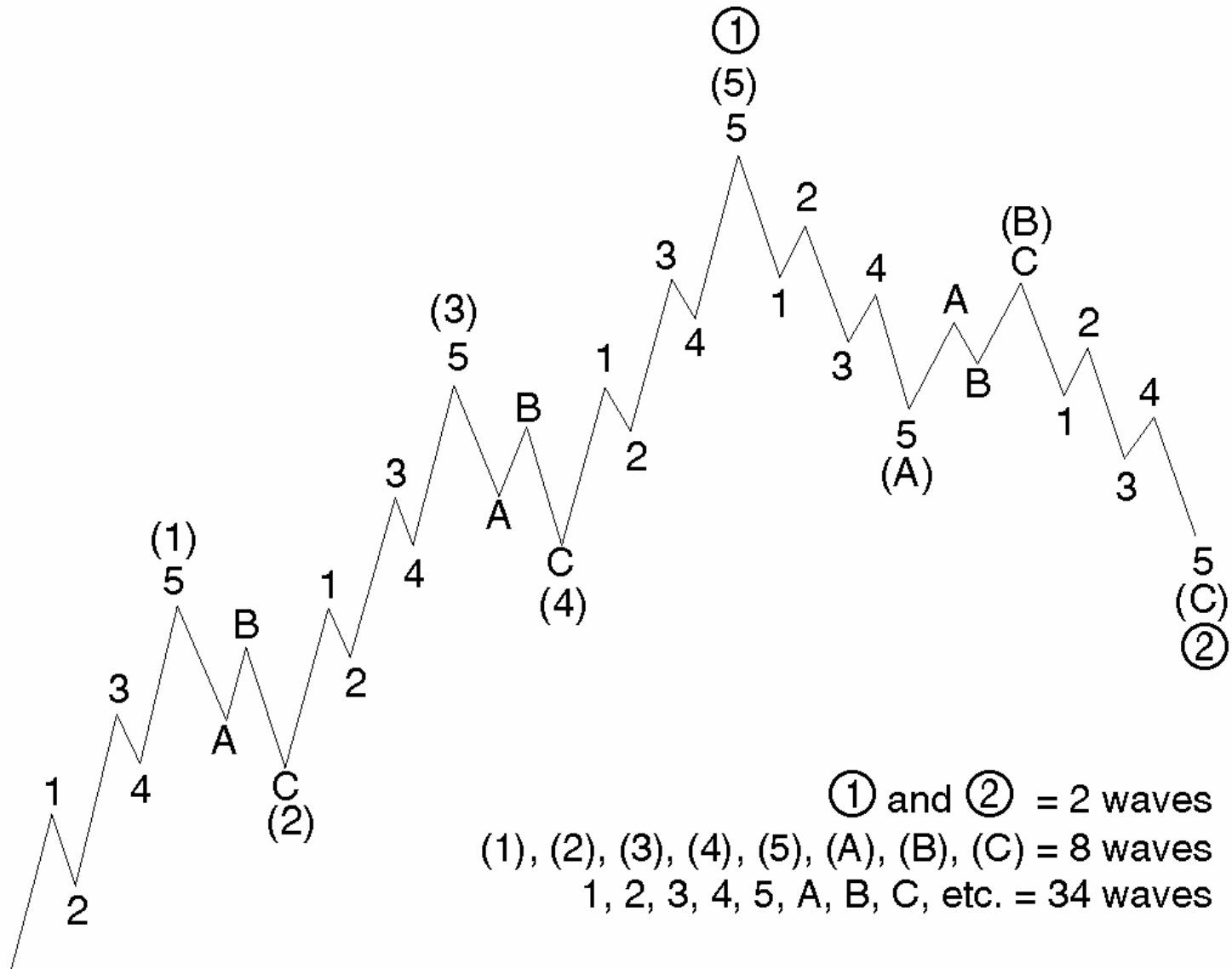


1932 1934 1936 1938 1940 1942



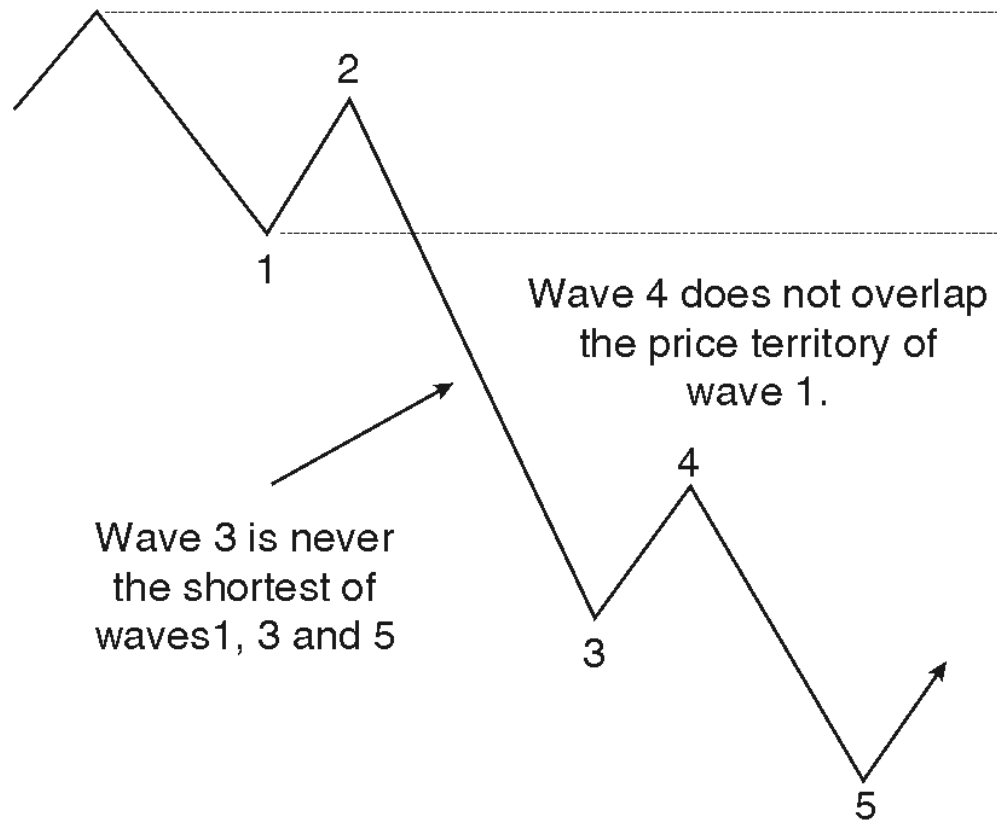
1930 1940 1950 1960 1970 1980 1990 2000





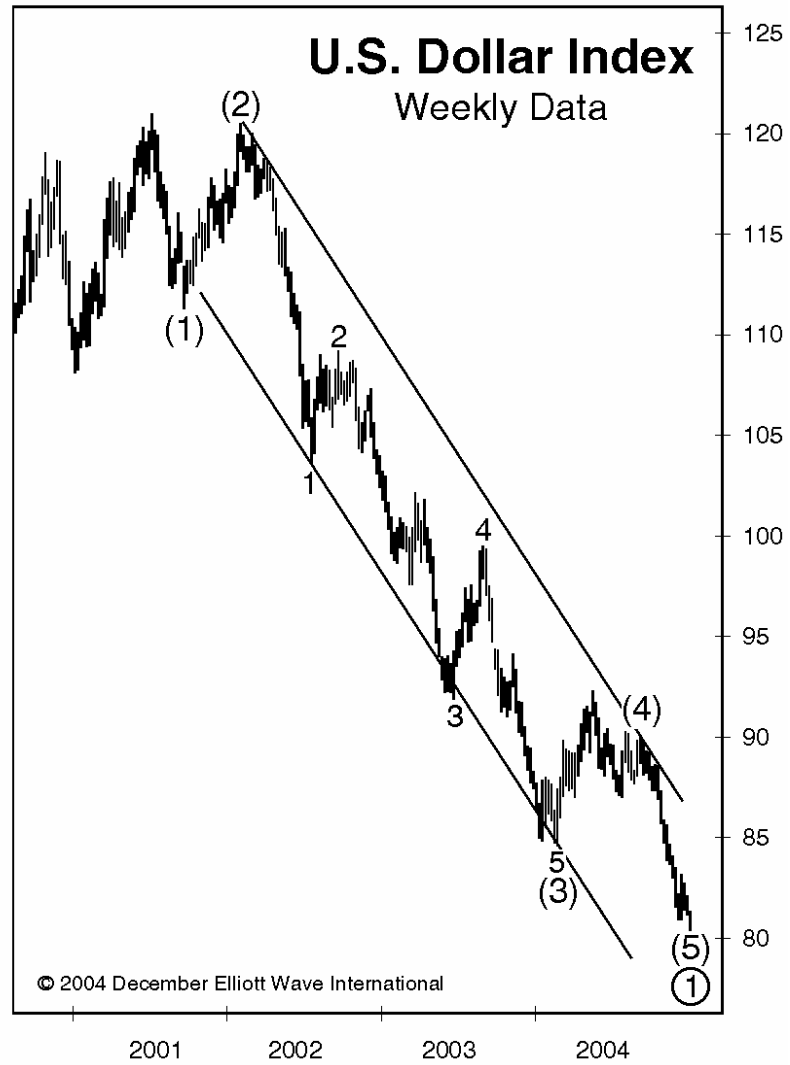
Rules

Wave 2 always retraces less than 100% of wave 1.

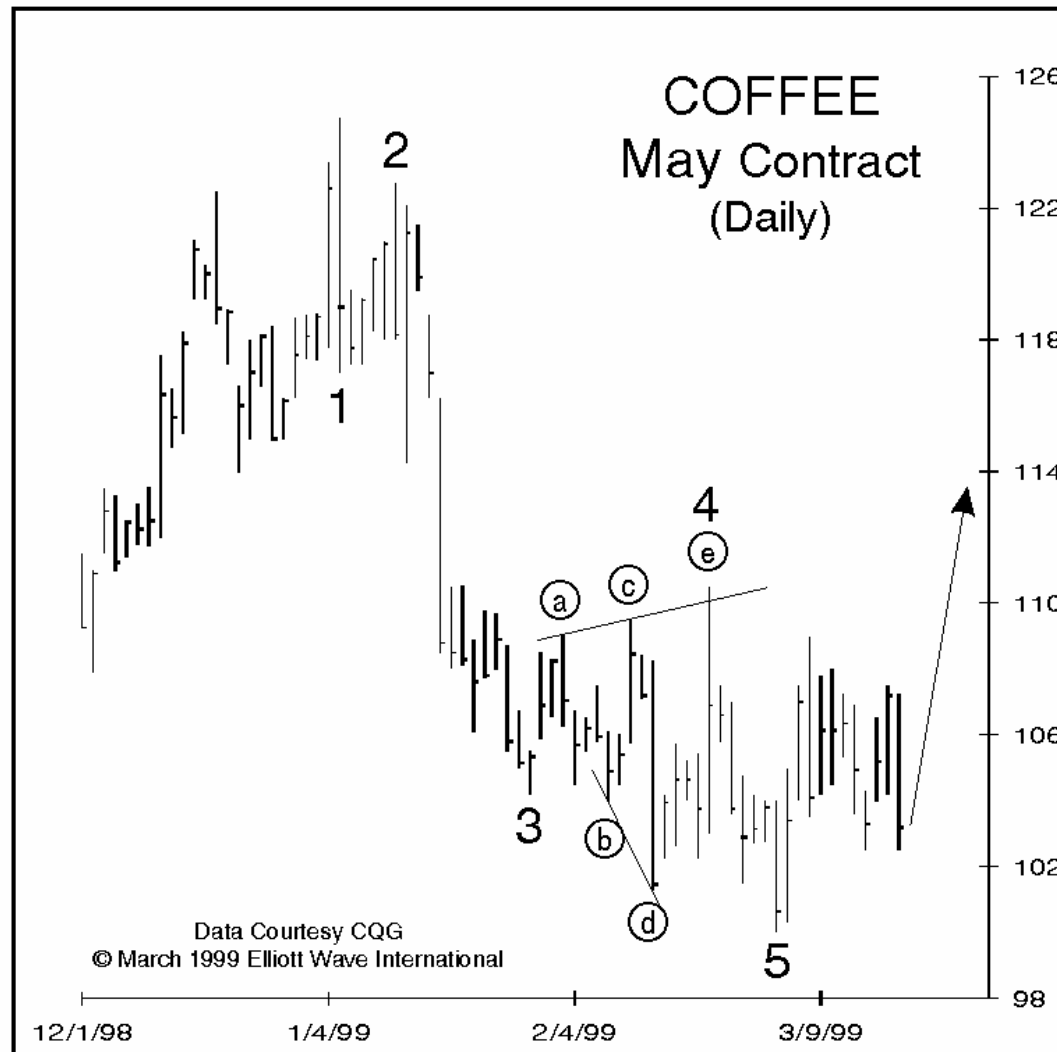


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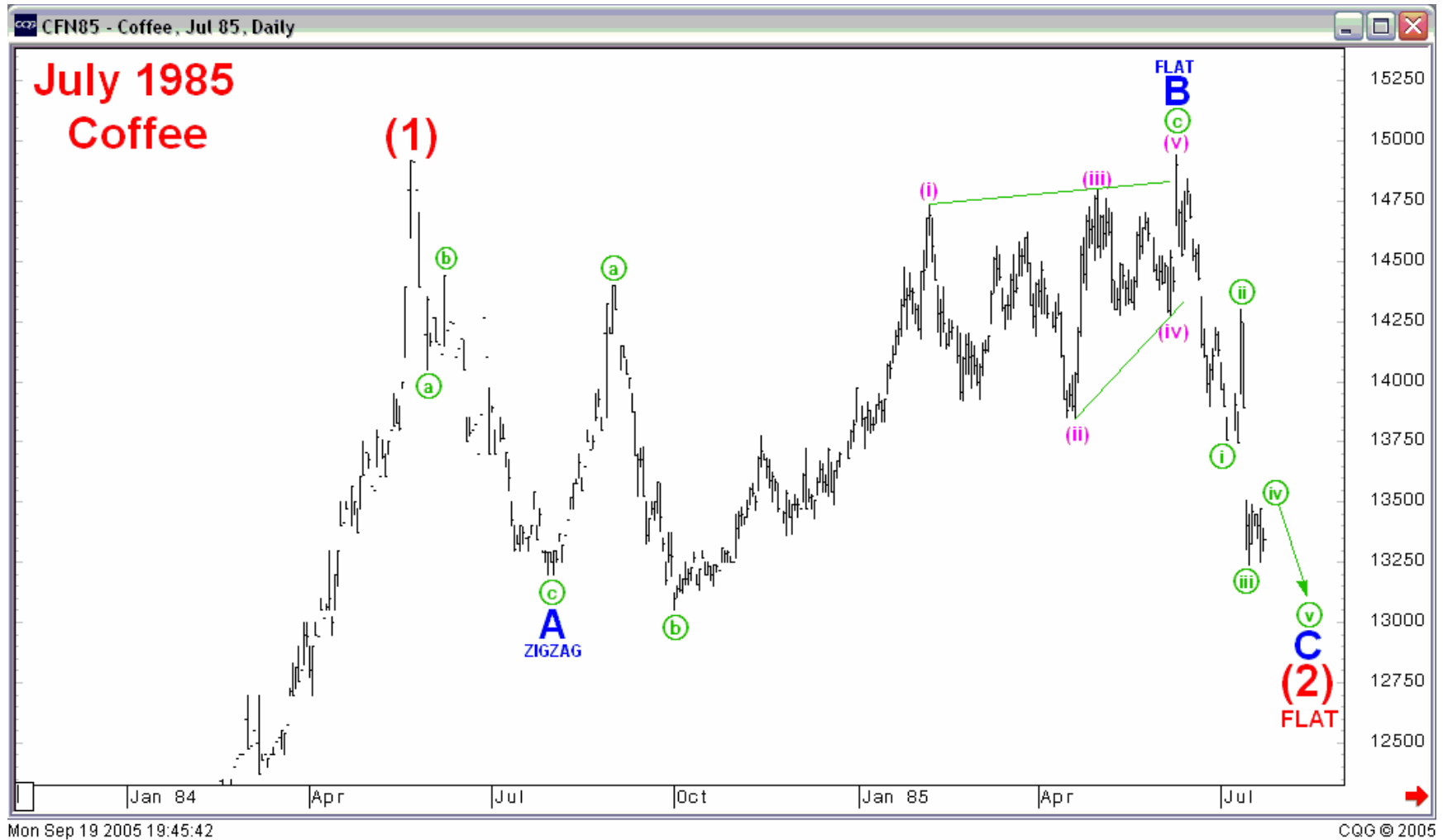
Equality



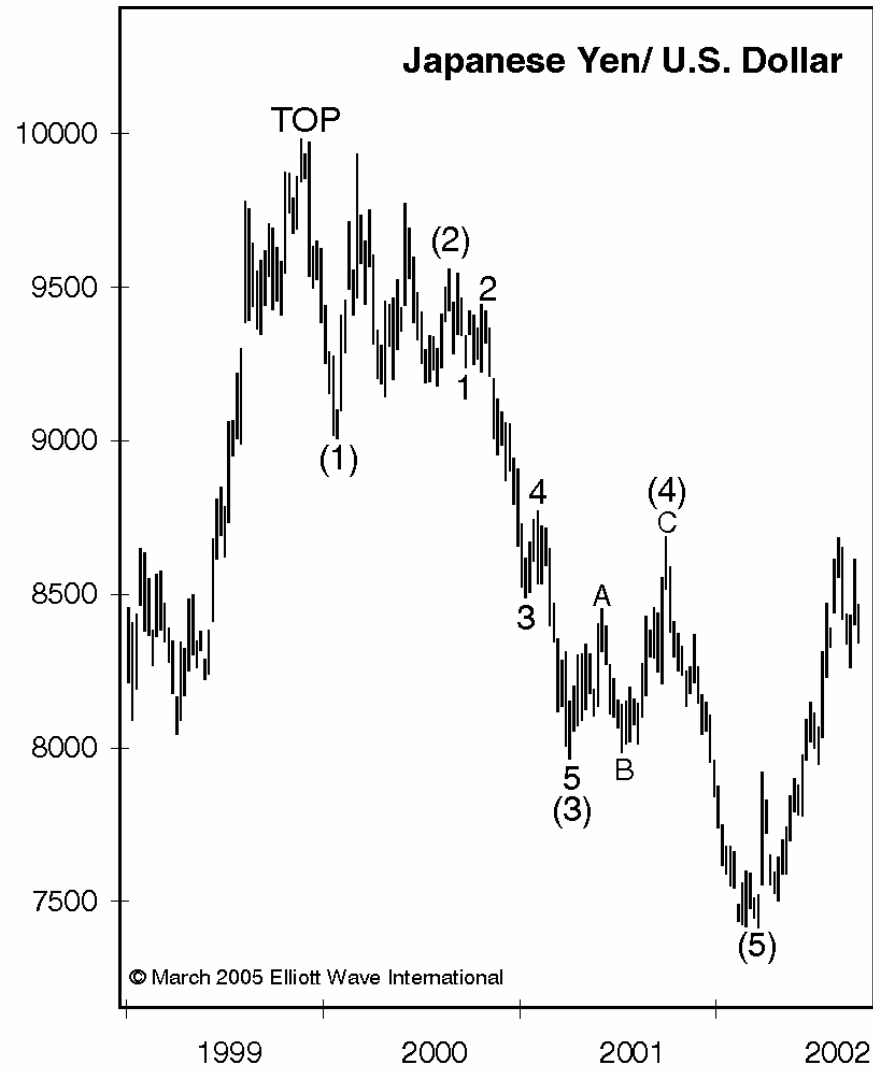
Alternation within Impulse Waves



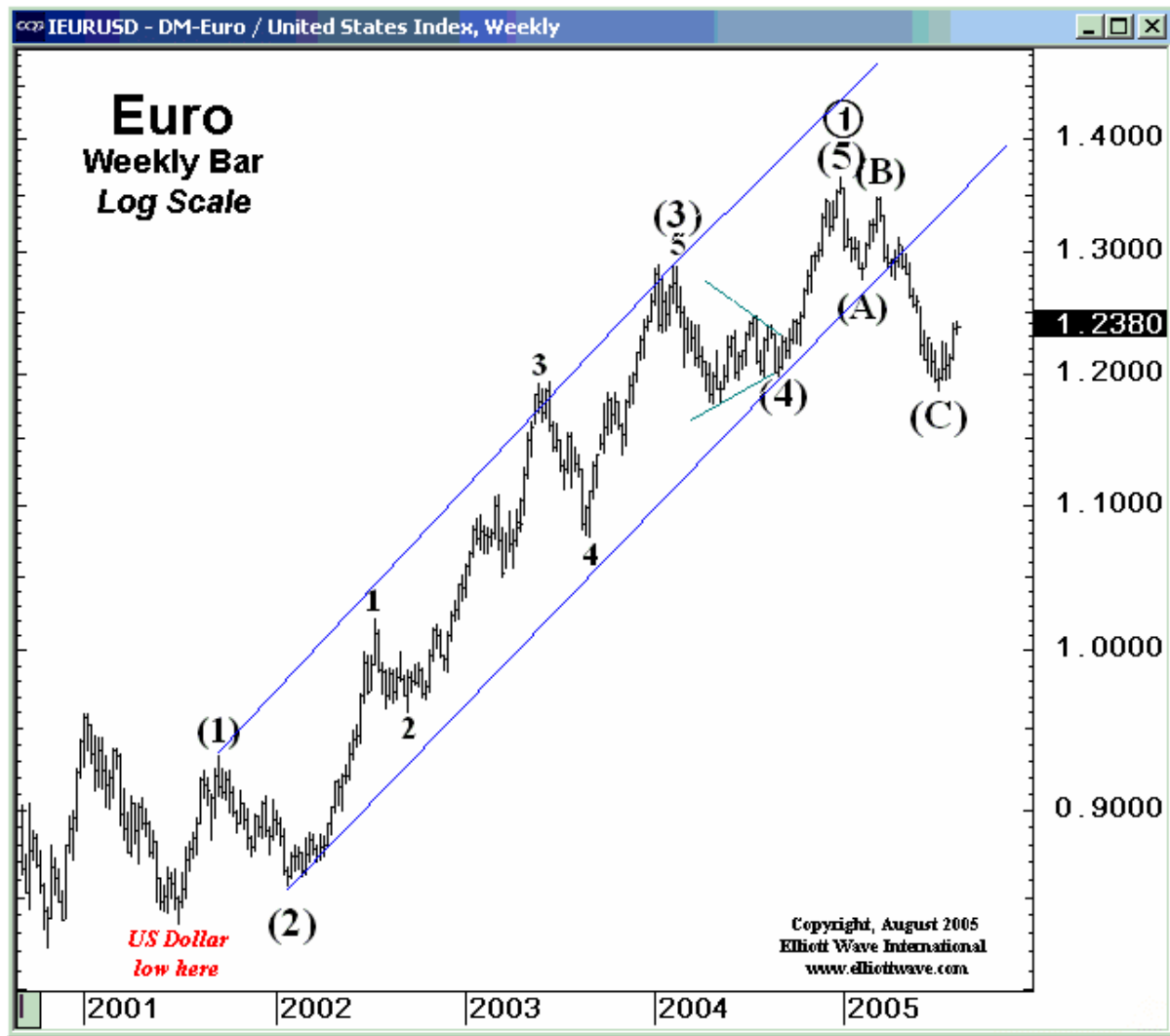
Alternation within Corrective Waves



Depth of Corrective Waves



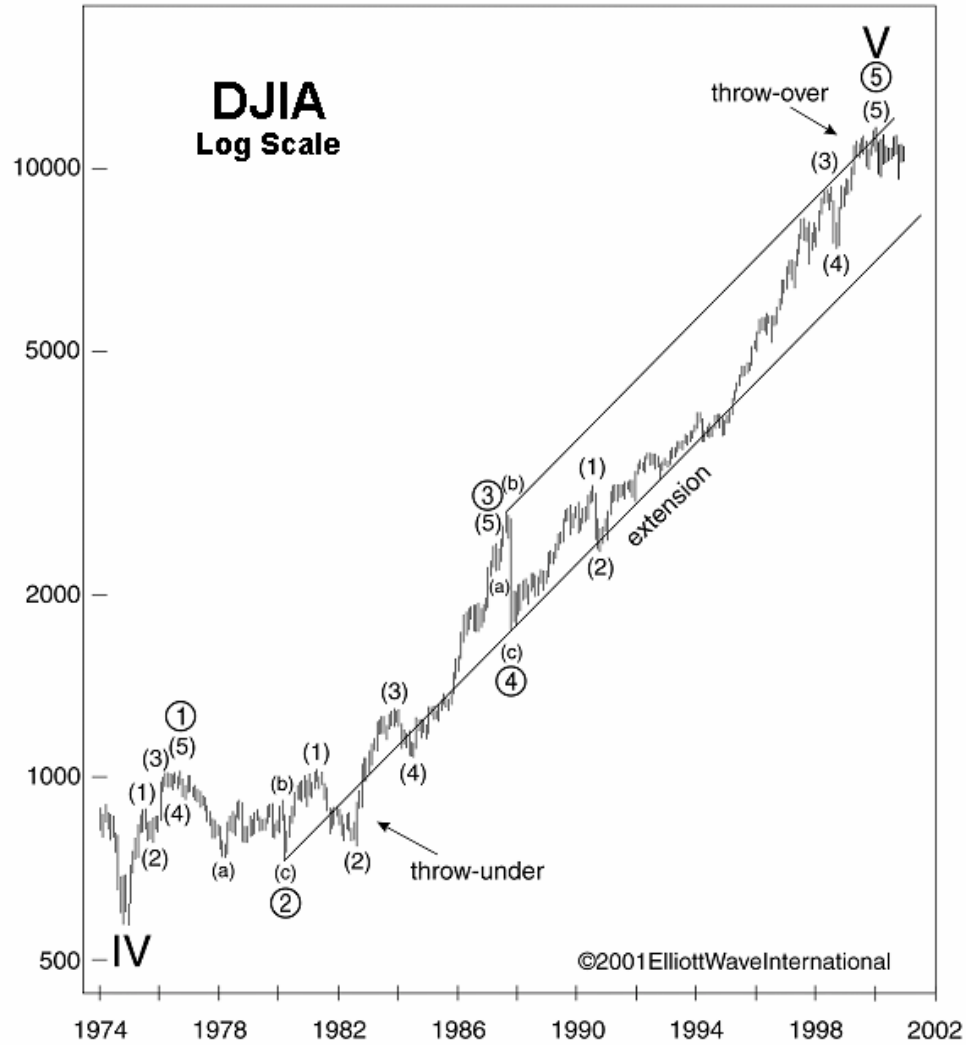
Channeling in Impulse Waves



Wed Aug 10 2005 15:21:10

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Throw-Over



Volume



Tue Sep 20 2005 10:48:48

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Post-Triangle Thrust Measurement

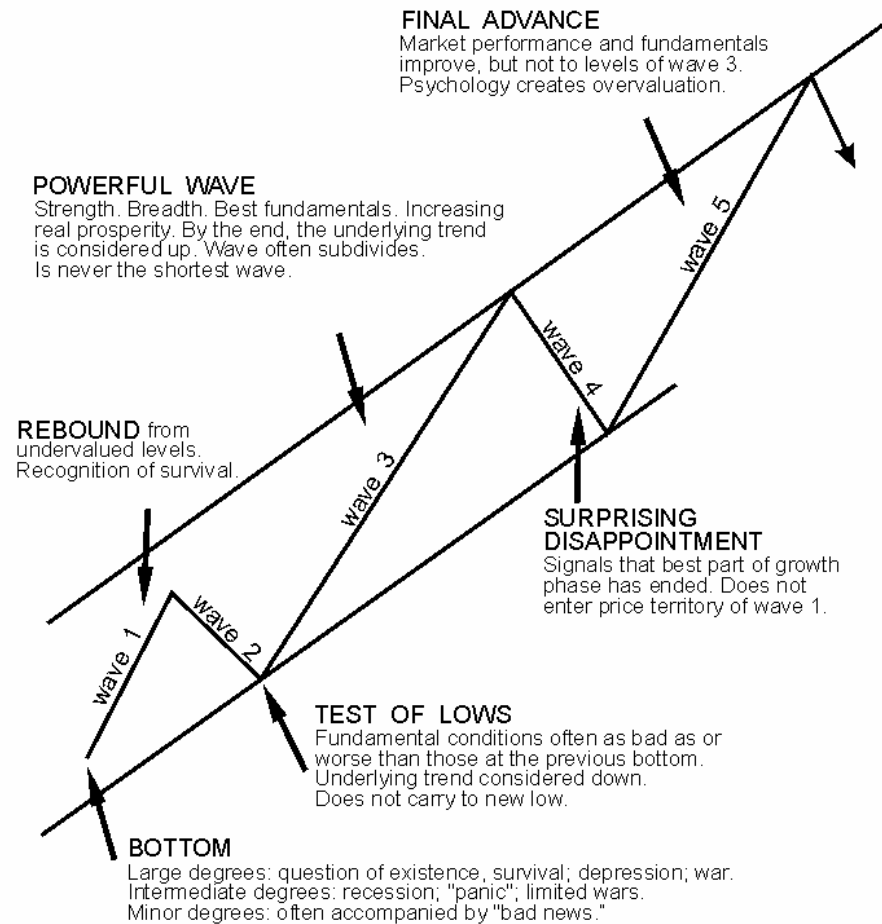


Mon Apr 05 2004 13:48:41

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Wave Personality

Idealized Elliott Wave Progression



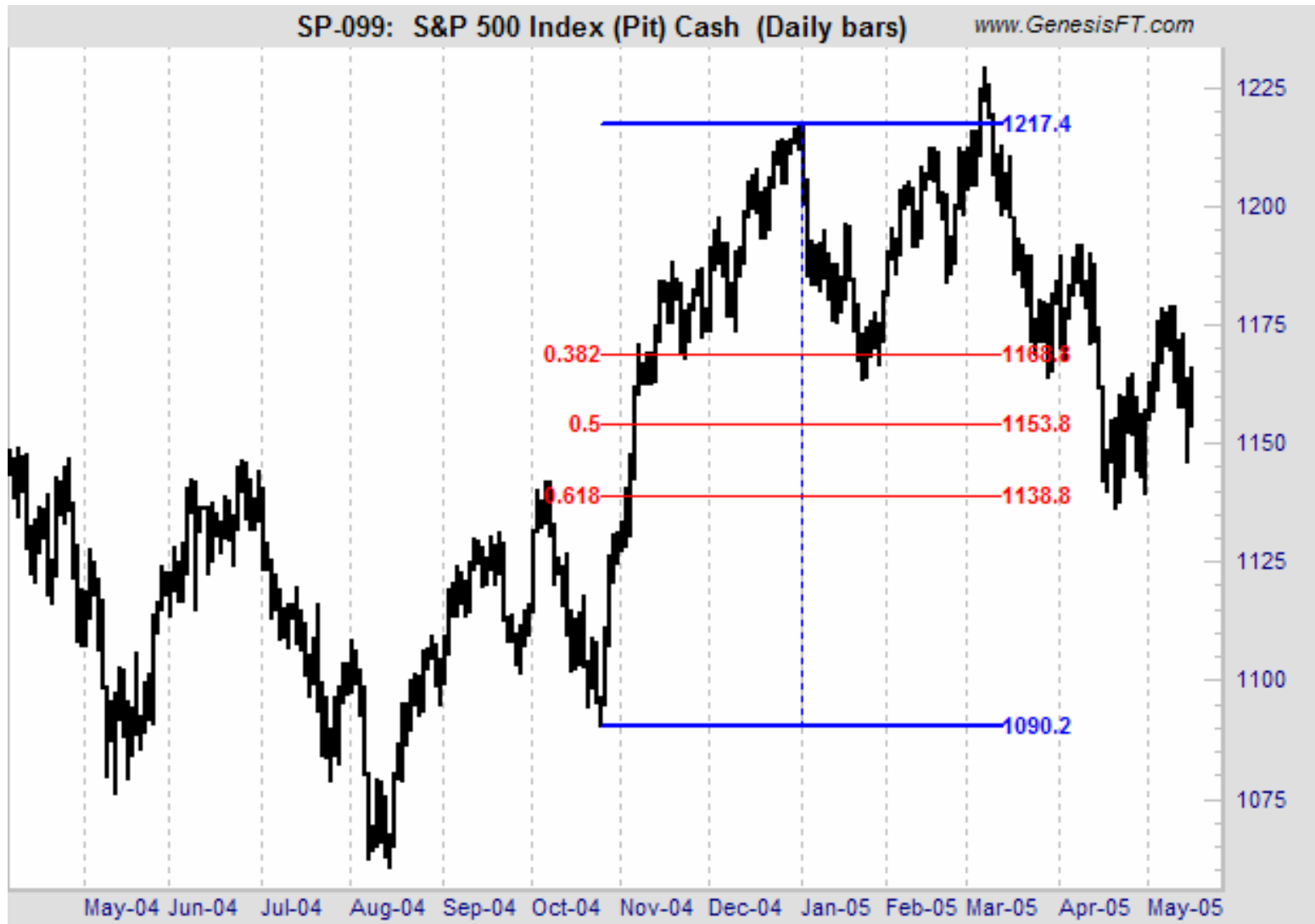
Fibonacci Relationships In Financial Markets

The Golden Ratio

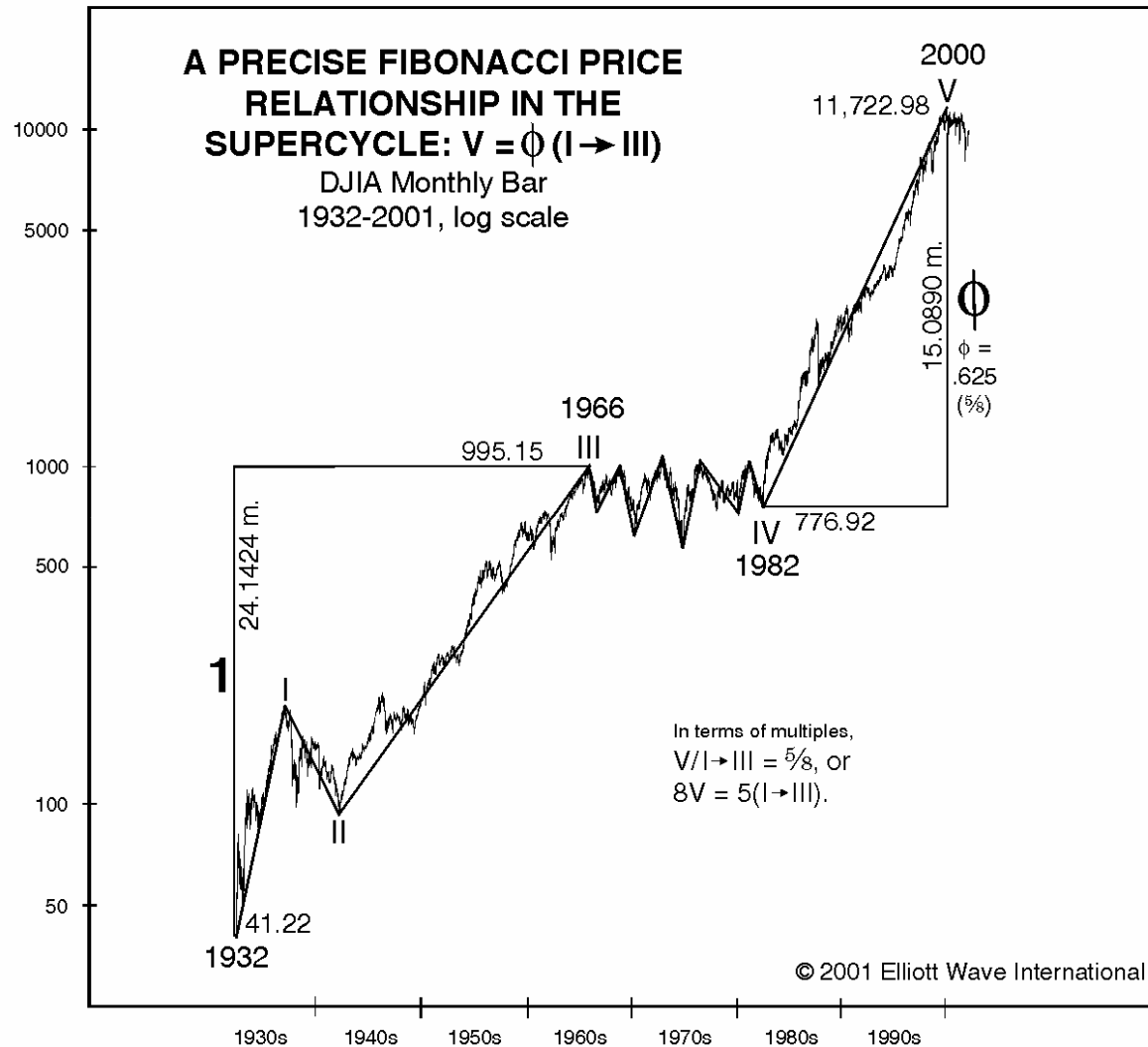
PHI Φ

.618 or 1.618

Retracements



Multiples in Impulse Waves



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