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Lesson 19: Elliott Wave Principle I

The Fundamental Split

Are market movements in a “random walk”

...or can we find a “pattern”...?

Elliott Wave Theory

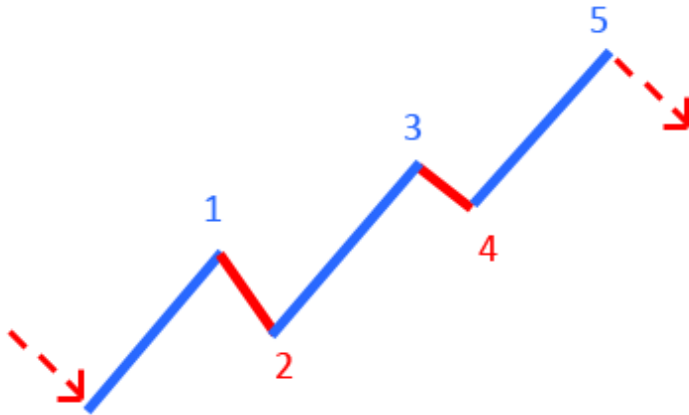
- Market movements reflect underlying psychology
- Ralph Nelson **Elliott** discovered recurring cycles, reflecting the connection between human emotions/actions and mass psychology
- Stems from the Dow Theory

2 of Dow's Principles

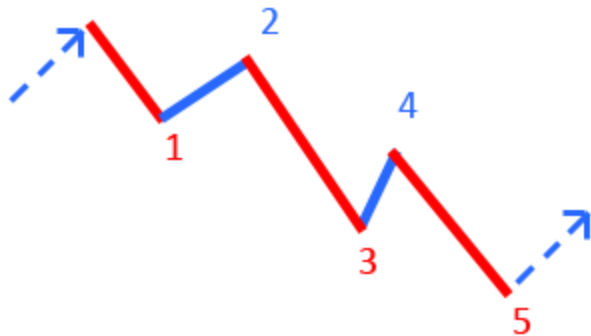
- 2 Types of Market Movements
 - Primary
 - Secondary (retracement or correction)
- A trend has 3 swings
 - 1. “Smart money” (from previous downtrend) – accumulation
 - 2. Based on the fundamental - participation
 - 3. profit taking – distribution

Elliott takes these principles further and tries to quantify them

The Basic Elliott Wave



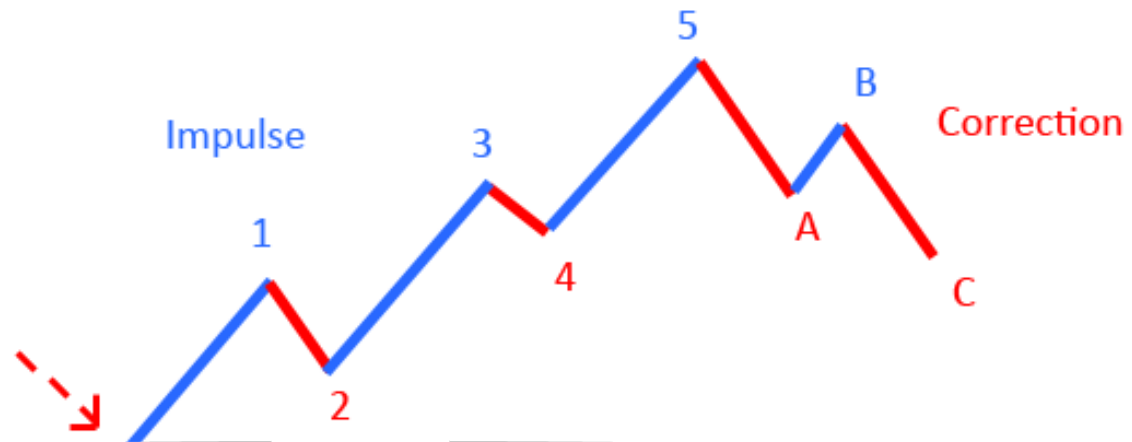
- Impulse Wave vs. Correction
 - Impulse (or Motive) wave is the direction of the primary trend
 - Correction is secondary and against the primary trend



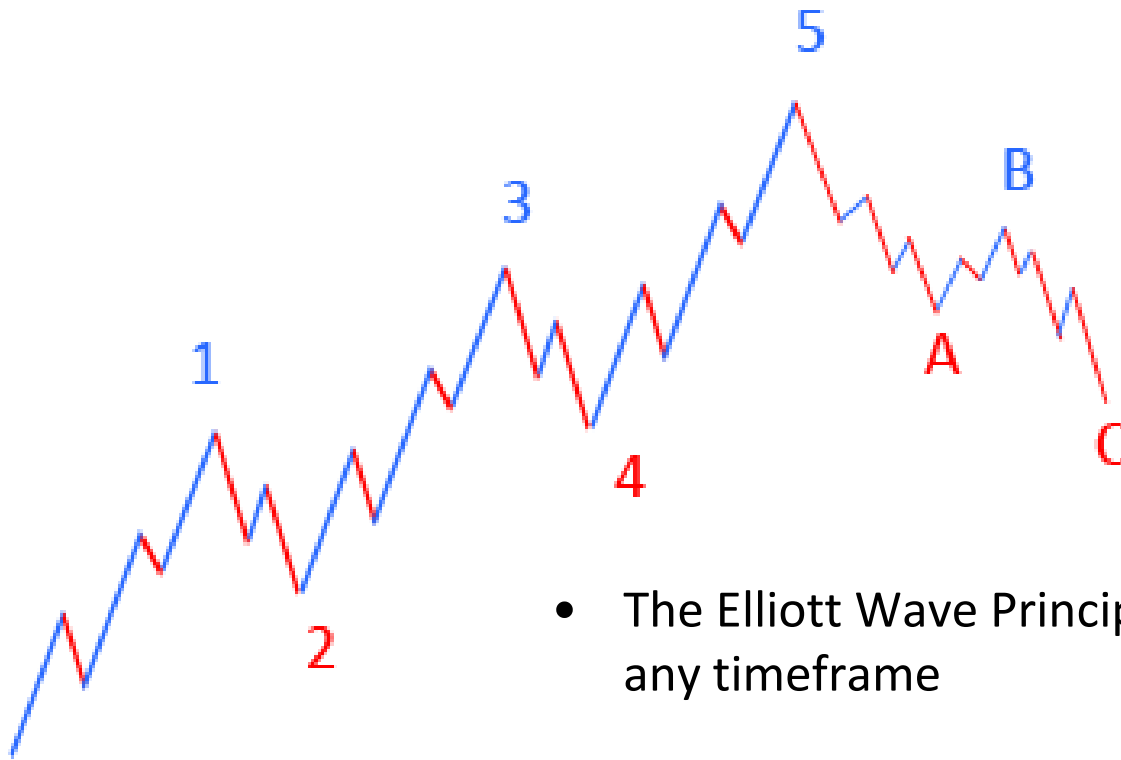
- One impulse wave consist of 5 smaller waves
 - 3 impulse
 - 2 correction

Basic 5-3 Wave I+C

- One complete wave includes...
- Primary trend has 5 impulse or motive wave followed by 3 corrective wave *Dow Principle of retracement
- Wave A is corrective wave's motive...

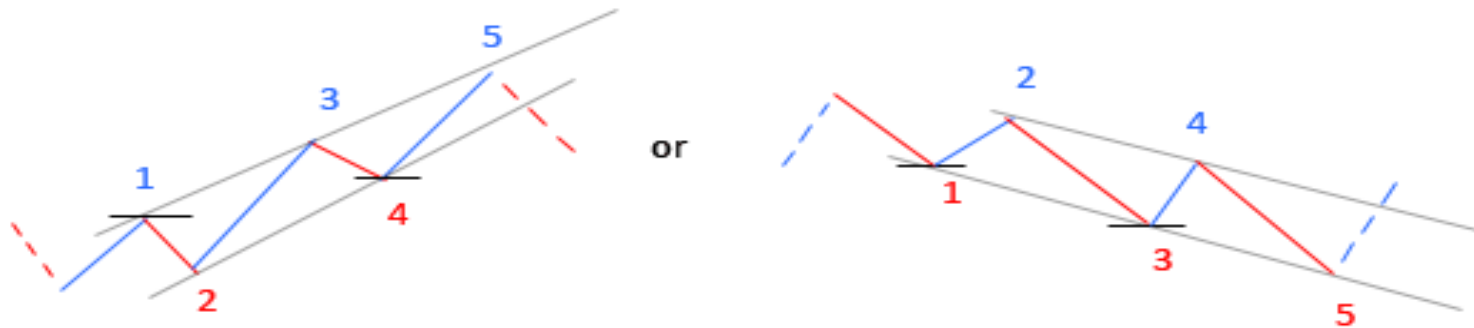


Scalable Structure



- The Elliott Wave Principle can be applied to any timeframe
- A wave has sub-waves, and is a sub-wave of another...

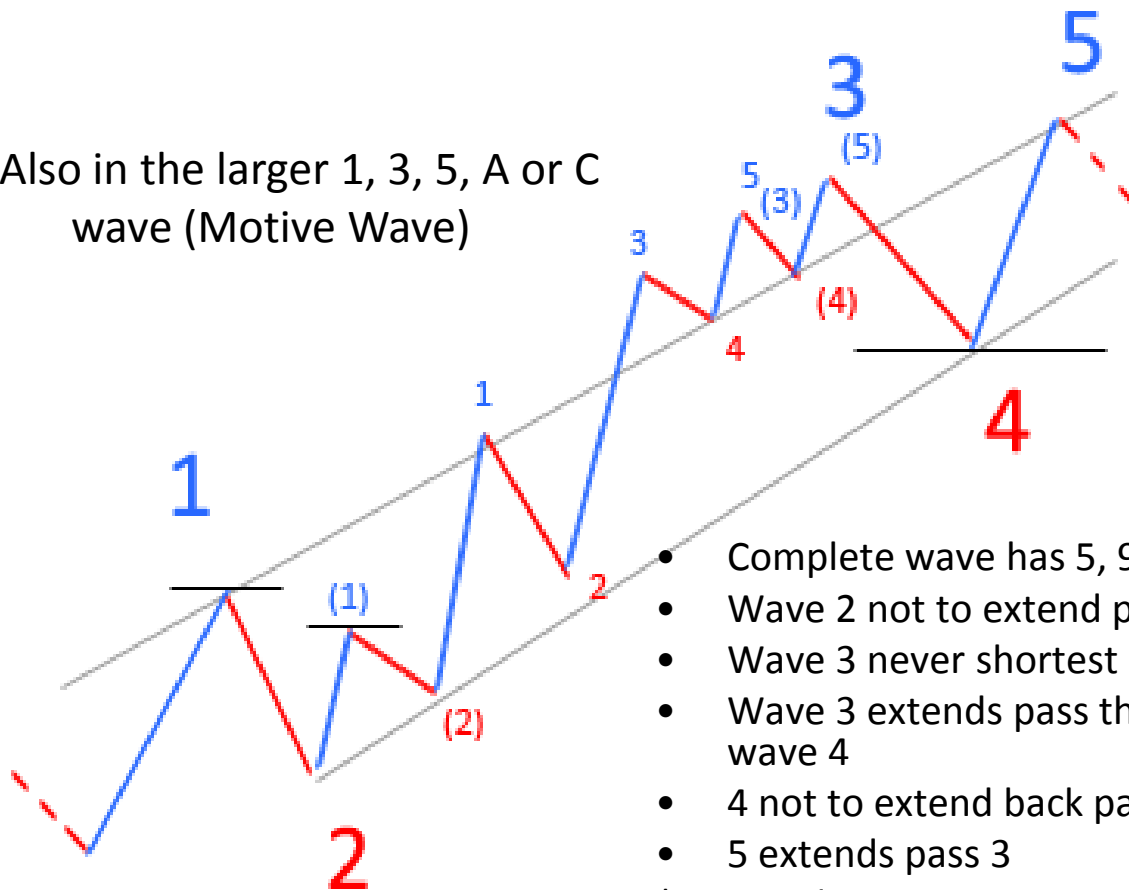
Impulse (Elliott Wave Guide)



- Impulse wave is a 1, 3, or 5, OR A or C
 - $1 \approx 3 \approx 5$ impulse waves (Ratio Analysis)
 - **3 never shortest compared to 1 and 5 (Dow?)**
 - **Wave 2 not to pass origin**
 - **4 not to extend pass 1 (except special cases)**
 - *5 to extend pass 3*
 - *2 and 4 (corrective) are different (alternation)*
 - *Retracement to wave 4 of smaller degree.*

Wave 3 Extension

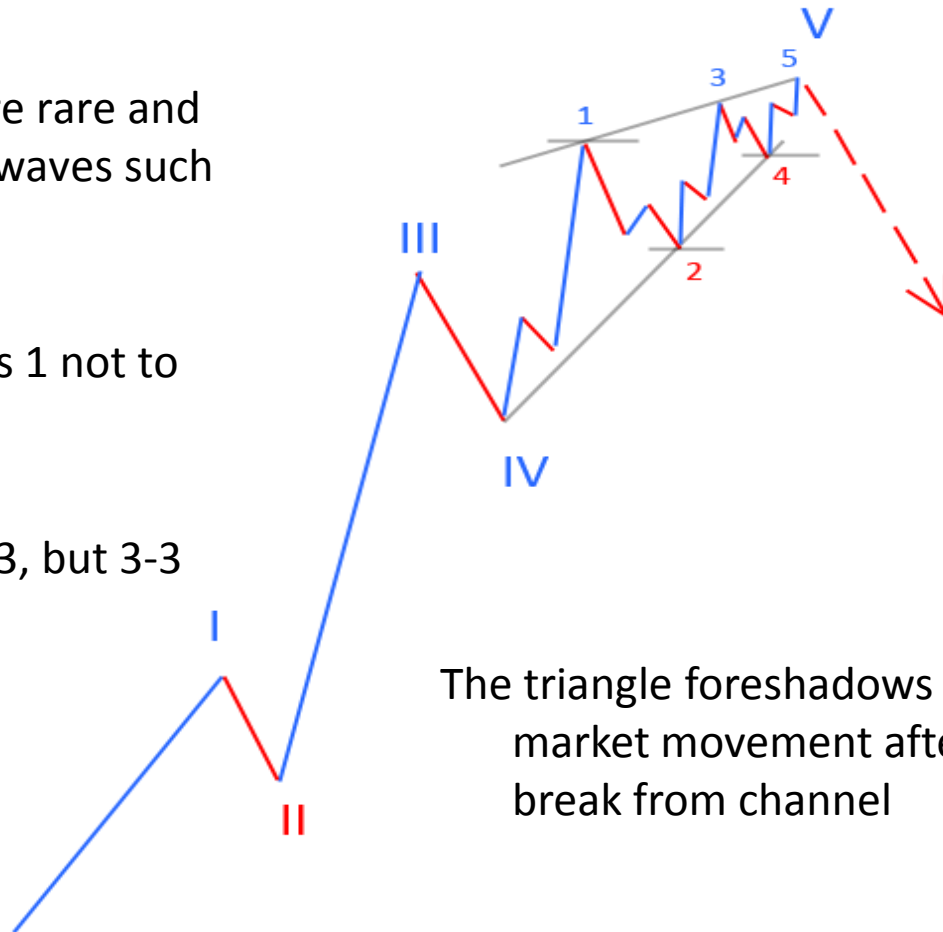
Also in the larger 1, 3, 5, A or C wave (Motive Wave)



- Complete wave has 5, 9, 13, or 17 waves
 - Wave 2 not to extend past 1
 - Wave 3 never shortest of 1,3,5
 - Wave 3 extends past the channel but returns in wave 4
 - 4 not to extend back past 1
 - 5 extends past 3
- * *Note: alternative interpretations of sub-waves in wave 3*

Diagonal Triangle

- True diagonal triangles are rare and should occur at terminal waves such as 5 (V), or C
- Wave 1 > 3 > 5
- Wave 4 extends back past 1 not to origin of 2
- Channel lines converge
- Internal structure NOT 5-3, but 3-3



The triangle foreshadows violent market movement after the break from channel