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An Elliott and Gann Efficient Time / Price Tool, Part 2 of 2

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Most experienced traders have, in their trading arsenal, tools that use the time / price relationship. Less known and less assimilated by the public, the time factor should be understood, first as a stand-alone concept, and then as it integrates with, not only price, but volume as well.

As we have seen in Part 1 of this article, the price / time relationship plays a vital role in determining the exact reversal threshold. Few traders are aware that time is a variable containing a definite quantity of energy that vibrates at a specific frequency, from a thermodynamic point of view.

When time and price reach the resonance frequency – under the strict control of volume – this signals a harmonized market state that ends up in a reversal, thus preparing an entry procedure.

The use of ellipses, especially the horizontal type, will enhance the visibility of these harmonized market states on a chart, thus aiding market flow analysis and preparing the trader for the trade decision process, in a reversal zone environment, created by the intersection of the time and price coordinates.

The profitable side of ellipses is not only the way they mark the out-bursting level of an entry but also how the use of multiple inner ellipses can signal the "Add" level of additional contracts.

One should be aware that a sort of connivance may occur, not only inside multiple ellipses, but also between them and an eventual pitchfork. **The ultimate purpose of using ellipses and pitchforks is to reveal the occurrence of clusters and confluences that can constitute very strong reversal levels**. Moreover, both tools are dynamically related to market flow, being in constant sync with the price movements.

Ellipses and Pitchforks: Unveiling the Profitable Trades

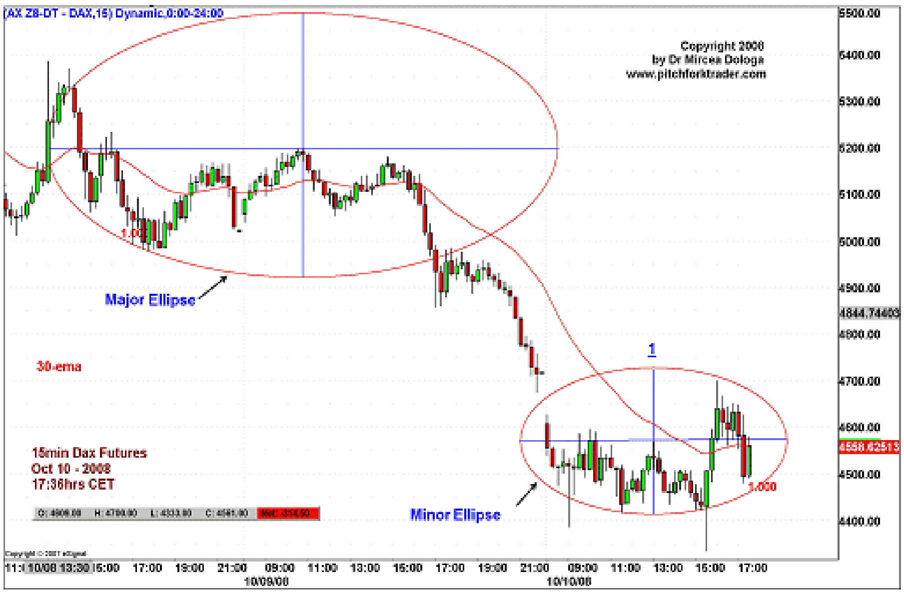

Figure 1. A Chart That Shows 2 Elipses, a Major and a Minor

In Figure 1, the chart's two ellipses were drawn to illustrate the synergy that can occur between pitchforks and ellipses.

There can occur a sort of enhanced analytic effect, not only between the two ellipses, (as seen in Figure 1), but also between them and an eventual pitchfork (refer to Figure 2). The main purpose of this set-up is to reveal the occurrence of clusters and confluences, which can constitute very strong reversal levels. This association of tools will help you to better visualize contextual and current market flows.

Figure 2. A Chart Identical to the One in Figure 1, but a Few Hours Later and into the Day's Close

On the chart in Figure 2, we have drawn a descending pitchfork and added a partially super-imposed ellipse (n° 2) on the minor n° 1 ellipse.

This set-up immediately revealed several charting elements indispensable for making a trade decision: the median line was tested numerous times, the horizontal axis of the minor ellipses served as a symmetry axis for the trading range and the UML bluntly halted the market.

Figure 3. A Chart Identical to the Prior One, but with the Third Minor Ellipse (n° 3) Being the Only Difference

We have tried to illustrate that the minor ellipses – which closely follow the current market – should always be ahead of market flow, oriented toward the most probable future move.

The addition of the n° 3 ellipse prepares the market mapping, in case of an up trend bursting out of the bottom trading range. In spite of this ergonomic trading set-up, there is another missing minor ellipse, in case of a rectangle's continuation.

Figure 4. A Chart Identical to the Prior One, but Having an Additional Small Ellipse

On the chart in Figure 4, we have drawn the n° 4 ellipse, which will efficiently assist the trader in the case of the rectangle's continuation downward.

We closely observed the last two closing bars: an up bar having a huge up tail, well balanced by the second bar (and last), which has a down tail. We would say that they try to compensate, neutralizing reciprocally. On an upper time frame (such as the 30-minute), they will appear as a doji bar (an indecision) having two big tails.

Figure 5. A Chart Identical to the Prior One, but with Some Decisive Improvements

On the chart in Figure 5, we have added a fifth minor ellipse (n° 5), just in case market flow will continue horizontally. The drawing of the pitchfork's trigger line is very important, in case of a sudden breakout.

Even if market flow has to trespass the upwardly situated n° 3 ellipse first, the presence of the trigger line may trigger a test and retest, just on it; in which case, the trader will be glad to perform an "add-on" re-entry. At any rate, the set-up is not only efficient but also aesthetic!

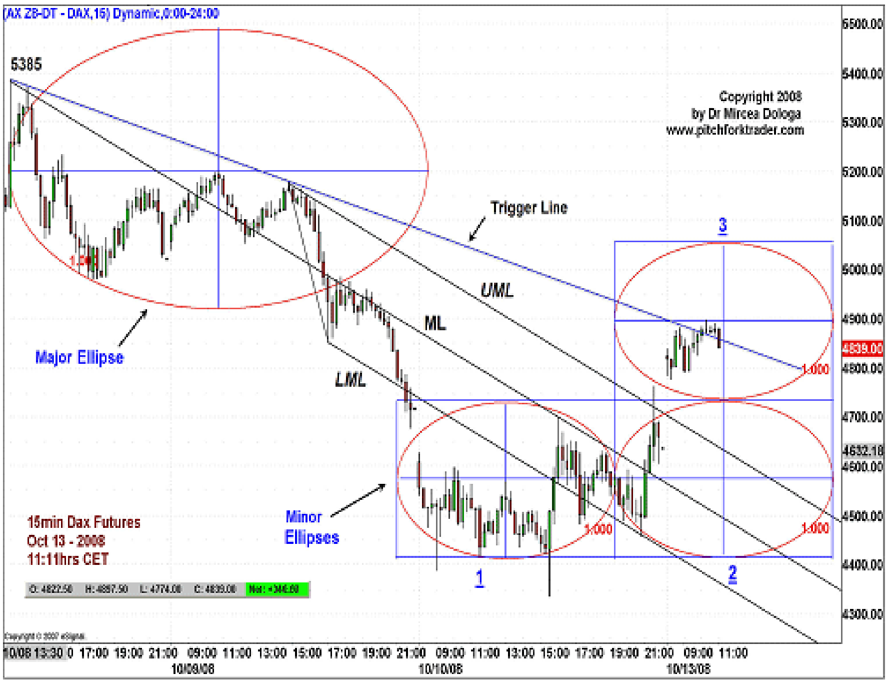

Figure 6. A Chart Identical to the Prior One, One Day Later, and into the Morning's Market Activity

The huge up gap on the chart in Figure 6 incited us to change the ellipses' set-up. Thus, we deleted the overlapped minor ellipses but drew a new set of three adjacent ones.

As we had anticipated, the trigger line played an important role here – as a reversal causal factor. The same is true of the left and lower side half axis of the n° 3 ellipse. There is a perfect symbiosis between the former and latter elements.

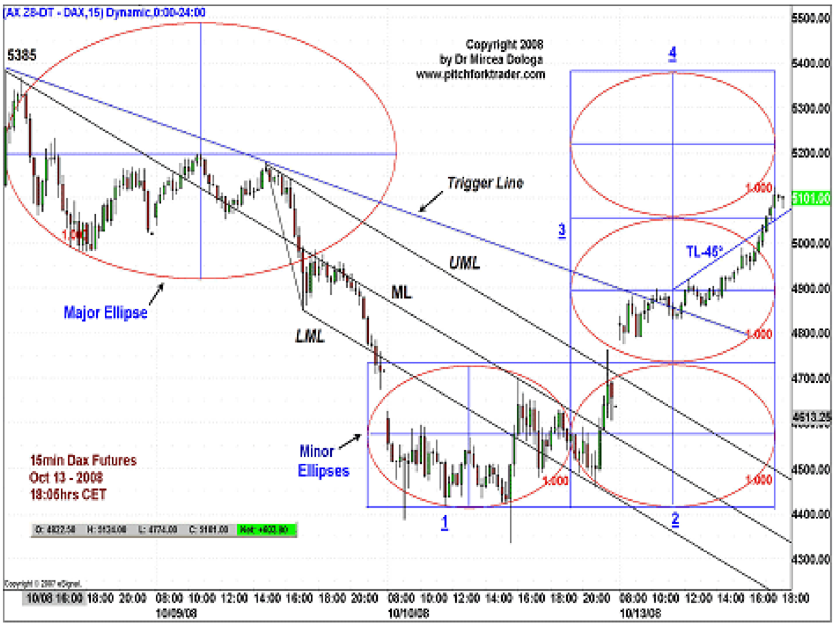

Figure 7. A Chart Identical to the Prior One, but Later into the Afternoon's Market Activity (18:05 Hrs. CET)

On the chart in Figure 7, the trigger line again played an important role as a balancing axis. It assisted market flow to test and retest its line, then test the right-half axis of the n° 3 ellipse 4 times, before starting to climb to just under the 45° angle line.

The market's high-steam momentum catapulted the price above this steep line angle, just outside the n°4 ellipse. The immediate trespassing (or not) will be the test for a further up-sloping continuation.

The Real-Time Ellipse Trade

Figure 8. An Illustration of an Ellipse Short Trade Example of a Daily Gold (Comex) Futures Chart

The chart in Figure 8 is based on several initiating factors: the top location of the ellipse, the down-sloping failure signaled by the descending TL-1 trend line and the eight-times-tested arc of the lower right portion of the PHI ellipse (L / H ratio is 0.618).

We applied the Three-Pawn Technique in automatic mode (refer further to Table n° 1). The test and retest of the lower right arc will initiate the short trade.

Figure 9. A Chart That Continues the Market Activity of the Prior Chart, but Two Days Later

As we expected, market flow tested and then retested the ellipse's arc, and, thus, the trade was initiated with the Three-Pawn Technique used in automatic mode: short entry at 918 level, initial stop loss at 933 level and two pre-arranged targets at the 850 and 776 key levels, respectively.

Their selection criteria are based on the fact that they are both old-lows levels, very susceptible to interaction with market flow. For risk and money management techniques, please refer further to Table n° 1.

Figure 10. A Chart That Continues the Market Activity of the Prior One, but 16 Days Later

The above chart continues the market activity of the prior, but 16 days later. We can observe that the trade developed as we have anticipated. As we planned, we have exited with two contracts at the first target level (850) and then with the remaining contract, at the second target level (776).

Again, for the P&L statement, refer to Table n° 1. In spite of the excellent results, there is always room for improvement; we should have performed at least one add-on re-entry, at the low of the penultimate bar. In addition, we should have let loose another trading unit (or several), in case of a 776 key level (the second old low) breakdown.

Before we close this article, let's briefly revisit our Three-Pawn Technique.

The Three Pawn Technique – a Money and Risk Management Technique

The Three-Pawn Technique is a Triple Order Preparation and Trade Execution technique detailed in this author's three-trading-manual trilogy (refer to the end of this article for details about the trilogy).

We have reached the stage of evaluating any trade in a precise manner with the help of the Three-Pawn Technique. It is a "to be or not to be" situation or a "to make or not to make" entry decision. This progressive-order technique consists of three steps:

Step 1: Find the most optimal entry and place the **first order**.

Step 2: Look for the best stop-loss location – and then enter a stop order immediately after the entry order is executed. This will be the **second order**.

Step 3: Find the most appropriate logical profit objective and then calculate the optimal reward / risk ratio (R / R ratio), which should not be under the 2.5 value. If that is the case, place the **third order** right after the stop loss order is working on the broker's waiting list.

We seldom take 2 to 2.5 R / R ratio trades and only if they have a high probability. Do not forget that our main purpose is capital preservation. **There is always another opportunity, but only if you are still in possession of your capital**. Our purpose is not to make any home runs, but rather, **we are looking for low-risk, high-probability trades**.

Most of the time, these three progressive trade orders, labeled the Three-Pawn Technique, are pre-arranged at the moment when the trade decision is made. It is vital for capital preservation's sake, that once they are established, they never be changed.

Because of the reliability and automation of this technique, we named it the automatic trading mode. It is one of the best remedies for the "trigger-shy" syndrome.

If only two orders are pre-arranged, we are in a semi-automatic mode. If all three orders are not pre-arranged, we are simply in manual mode.

The Three-Pawn Technique must be understood, learned and practiced everyday, with no exceptions. This requires discipline and patience:

Discipline: Requires respecting 100% of the three rules
Patience: In waiting for the entry order to be executed

Once this is accomplished, the second and third rule will automatically follow, almost flawlessly. The trader must reach a high level of routine, continuously checking and double checking his / her well meditated decisions and actions in such a way that the main task is preserved from everyday noise.

We have to insist that a precise following of the Three-Pawn Technique dominate the trading life of a novice trader. Without such a close following of this technique (the main objective of which is capital preservation), a novice trader's account usually does not exceed three months.

Fortunately, for those traders who have completely assimilated this technique, it will represent something of a warranty of consistent profits.

Trade Execution	
Date IN	07/30/08
SHORT Entry	918,0
Value - 1 Point ($1.0)	$100
Traded Vehicle	Gold Comex
N° of Contracts	3
Stop Loss	933,0

Total PROFIT/ LOSS	
Date OUT	08/15/08
Points	278,0
PROFIT	$27 800
Trade Time Length (days)	16

Risk & Money Management	
Risk per Contract - pts	15,0
	$1 500,0
Total Risk- pts	45
TOTAL RISK	$4 500
Reward / Risk RATIO > 2,5	9
Target n° 1	850,0
n° Contracts	2
Profit- pts	136,0
Profit- value	13 600 €
Target n° 2	776,0
n° Contracts	1
Profit- pts	142,0
Profit- value	$14 200
Target n° 3	0,0
n° Contracts	0
Profit- pts	0
Profit- value	$0

Trade's Grades= Poor *, Average **, Good *** & Excellent ****

Risk Degree= Aggressive or Conservative

Fill in below (only italic letters), after the trade !

Trade's Grade: *Excellent****

Risk Degree: *Aggressive*

Trade's Main Reasons: *Ellipse top location, Down-sloping failure & Multiple arc tests*

Trade's Journal: *Better profitability if multiple Add-On(s) used + A third target missing & Better use of ellipse's inner angles (entry, re-entry & targets)!*

Table n° 1. The Three-Pawn Technique Table: SHORT Gold (Comex) Trade – 2 Targets, Risk and Money Management

Be aware that the Three-Pawn Technique will relieve the trader, not only of the stress of managing a trade, but also of the peculiar exercise of risk and money management. Don't hesitate to **implement it every time – before you enter a trade**.

As we can observe, so far, the trading techniques performed using time / price tools closely associated with a strict and efficient money and risk management technique, largely open the gates to continuous profits.

We would like to express here our gratitude and admiration for two titans of technical analysis.

Ms. Dawn Bolton-Smith, the matriarch of technical analysis, a life member of the Australian Technical Analysts Association (ATAA), is, in spite of being into her eighth decade, still doing market analysis everyday, using Gann charts by hand, on millimeter paper – and also teaching the younger generations.

We had the pleasure of hosting her in our Paris offices, and we were delighted by a reciprocal experience. What better example of a dedicated lifetime student of the markets?

Mr. Michael S. Jenkins is one of the founding fathers of modern technical analysis and remains one of the most creative masters of it. He was, and still is (even after more than several decades of experience), capable of continuing Mr. W. D. Gann's work. To us, he represents an illuminated mind. When we trade, we always keep his advice in mind: "**Trades have an 80% chance of success when our entries and exits are guided by confluence between time and price.**"

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