

VOLUME ONE - EDITION ONE

TRADING WITH THE TIME FACTOR

THE BEST OF THE TRADING TECHNIQUES
BY W.D. GANN - EXPLAINED, SIMPLY.



BY FRANK BARILLARO

THE BEGINNING

It is possible to do what many will tell you is the impossible.

PREFACE

It is possible to do what many will tell you is the impossible.

I am convinced there is a calculable geometric symmetry present in all financial markets. The secret is knowing how to find it. Once you know how to find it, you can apply it to predict the exact time and date of future market tops and bottoms, sometimes years in advance.

I am certain of this geometry because I have seen it. I have also been able to predict it occurring in the markets time and time again. In 2001, I am on the record for outlining in writing that my timing calculations were indicating that 'September 11, 2001 is a date to be wary of.' I also nominated the date which proved to be the yearly low for the Australian stock market in 2001 to the exact day. All of this before the event.

I saw the geometry that unfolded in the precious metals Gold market which coincided with the end of the 20 plus year bear campaign in gold prices. It enabled me to make a number of long term investment decisions, including a first purchase of gold bullion when it was trading just above US\$300 an ounce. Interestingly, the same geometry which ended the 20 year bear market was also present to within a week of calling the current all-time top in gold prices. In this course, I will share with you how all that unfolded.

I have calculated, and have shared with colleagues (including my stock broker), future dates to watch in the Australian stock market which have been accurate at predicting major turning points in the market, more than two years in advance. More recently in 2011, I wrote to friends and colleagues outlining that the US equities markets will continue on to higher prices in 2012 and 2013 – advancing the bull market in US equities that has since reached all-time record prices.

My friends and colleagues often ask me to explain how I can do it. However I have always felt that it would need a book to provide them with an adequate answer. So, after much convincing, I guess this is that book. This book draws upon the input and experience of my good friend and long term confidante, Frank "Bob" Nigro.

Together, we will be sharing with you over 30 years of collective experience in the financial markets and thousands upon thousands of hours of study and research into the trading techniques which we have seen consistently working for us to predict future market tops and bottoms. We have seen which techniques work. We have also figured out which ones don't.

The course summarises that 30 years of experience into simple to follow descriptions and illustrations. It does much of the hard work for you so that you can better understand the financial markets. It filters out the best of the best – and allows you to apply these techniques to your own stock, commodity or currency market analysis. Importantly, I will show you how to apply these Trading Tools in a manner that is simple to calculate and easy to understand. A few of these techniques are what Bob and I consider to be the best of those used by many of the professional traders and hedge fund managers currently out there. The majority however have been adapted off the works of W.D. Gann – who was legendary for his contribution to trading by technical analysis.

The Trading Tools I am about to share with you have proven the test of time. They worked over one hundred years ago and I am confident they will continue working for the next one hundred years.

This course will change the way you look at financial markets. By the end of it, I am confident that you will have learnt the geometric secret that is present in all markets – and that you too can achieve what others will tell you is the impossible.

Frank Barillaro

Before you begin, please read this really important stuff first...

Firstly, thank-you and congratulations for purchasing Trading with the Time Factor. I have absolutely no doubt that this trading course will change the way you look at financial markets.

I also want to welcome you to the start of a journey together. My goal is that by the end of it, I will have helped you to make better decisions about your investments and trading. The lessons I am about to share with you will stay with you for a life time. To fully appreciate them, you may need to read this course more than once. In fact, I strongly encourage you to do so.

This course has been separated into two parts. Volume One is about PRICE. In it, you will find the best lessons I could find to help you determine the likely prices of future market tops and bottoms. It is all about teaching you “where” to buy or sell.

If you find Volume One of interest, then I assure you that Volume Two will absolutely blow your mind. Volume Two describes how to TIME a market and your investments by using techniques to forecast the exact date of major market tops and bottoms. It is all about “when” to buy or sell.

Imagine knowing when the stock market or the price of gold is going to make its next major bottom. What could that do for your investment portfolio? If you think it is impossible, then I encourage you to keep reading. You will soon change your mind.

Before we begin, there are some important housekeeping matters which we need to cover off first. There is some fine print below that you should take the time to read and understand before you proceed. But just in case your time is short, let me summarise the key points for you below.

This course is not personal advice

I am not a licensed financial adviser, nor do I know your individual circumstances. If you are looking for personal advice, please consult someone who is appropriately licensed to do so.

This course is not general advice

This course is about educational material on how to analyse the markets only. It aims to teach you how to make your own investment decisions. That’s right, so that you can make your own decisions. This course teaches you the theory on how to fish. Unfortunately, I cannot catch the fish for you. But I can at least show you where to look. Trust me, by the end of it I am sure you will be able to do it.

The contents of this course are confidential

Please respect that I have spent hours upon hours in researching, drafting, writing and publishing this trading course. Not to mention the thousands of dollars spent. If you spent countless hours researching what the winning lotto numbers for next week’s jackpot were going to be and you told me, how would you feel if I shared those with the rest of the world on the internet?

Now, I’m not saying that reading this course is going to be like winning the lotto, but I hope you take my point. After all, if you are reading this, you have agreed to terms of confidentiality with me anyway. You wouldn’t go against your word now, would you?

Accuracy of contents

The contents in this course have been prepared in good faith and may be based on information obtained from sources believed to be reliable but no independent verification has been made, nor is its accuracy or completeness guaranteed. Each of the charts contained in this book have been hand designed by my good friend Joe Caminiti. Whilst we have attempted to re-create every line, angle, axis and label as accurately as possible we are only human and humans can make mistakes.

These however should not detract from the message we are sharing with you. To the extent permitted by law, ThirtyTen Investments Pty Ltd does not give any warranty of reliability, accuracy or completeness of the information contained in this document and does not accept any responsibility in any way (including negligence) for errors in, or omissions from, the information in this document. The author or ThirtyTen Investments Pty Ltd is under no obligation to update or correct the information in this course.

One view isn't necessarily the right view

If there are any views or opinions expressed in this course, these may be the views of the author or other parties. Whilst everyone is entitled to a view or an opinion, it doesn't necessarily mean those views or opinions are right... Just ask my wife.

Future Returns

This is not a course telling you to implement a particular investment strategy or to invest into a particular market. That is a decision for you to make. Please bear in mind that when you are investing. The value of any investment and the income derived from it can go down as well as up. Never invest more than you can afford to lose and keep in mind the ultimate risk is that you can lose whatever you've invested. Please seek independent financial advice regarding your particular situation. Investments in foreign companies or foreign markets involve risk and may not be suitable for all investors. Specifically, changes in the rates of exchange between currencies may cause a divergence between your nominal gain and your currency-converted gain, making it possible to lose money once your total return is adjusted for currency.

Okay. Now that all of that is out of the way, let's begin,

Imagine knowing when the stock market or the price of gold is going to make its next major bottom. What could that do for your investment portfolio?

Before we get started

For a long time now, I have been mesmerised by the workings on Wall Street and the tales of fame and fortune by some of the great market legends such as Jesse Livermore, JP Morgan and the story of how the Hunt brothers cornered the silver market, making and losing billions in the 1980's.

In order to get the record straight right from the start however, I am not a full-time trader. As reluctant as I am to admit it, I am an investment banker by profession (but please don't hold that against me!).

A couple of years after my banking career started, I was fortunate enough to be given the opportunity of a traineeship on the foreign exchange trading desk at a major Australian bank – and I am still very grateful to the person who gave me that opportunity to this day. For me, it was a dream job.

Although brief, I learnt many things about professional traders and the different ways they approached the market. I had already been a student of the markets and Gann theory for a number of years beforehand, but the experience on the desk certainly added a new dimension to the way I looked at financial markets and the way professional traders approached them.

Unfortunately, the dream was short lived. My father, who was an inspiration to me for many things, sadly passed away unexpectedly on New Year's Day in 2006.

It prompted me to give up the traineeship so I could move back home from interstate to be closer to my family who needed me more at the time.

Eventually, I assumed a role working in structured finance – it allowed me to remove my law degree from being just a paper weight at home and actually put it to some use. The rigours and demands of a job in investment banking however don't afford me the luxury of being able to actively trade the markets day in and day out (not to mention the restrictive compliance rules on trading that come with such a profession).

And becoming a proud father of two young children recently now consumes most of my spare free time. Nonetheless, I have still found a way to keep an active interest in the markets... and to calculate an accurate forecast or two along the way.

I thought it is important for me to outline this to you from the start for a couple of reasons. Firstly, I am sure that there will be a few critics out there dismissing the idea that a book can be written about trading and the techniques pioneered by some of the market's greats by someone who doesn't trade the markets full time.

I am happy to cop such criticism – particularly if that person has read some of my forecasts and has a track record of being able to consistently produce them in writing as accurately as I have.

Secondly, but more importantly, I hope to demonstrate to you in this book that you don't have to be a full time trader to apply the techniques I am about to show you. By the end of this, it is my goal to have shown you how anyone can observe the symmetry which repeats itself in financial markets with only a modest level of analysis and by keeping it simple...

In writing this book, I have to recognise the contribution by my mate Frank "Bob" Nigro who has been a key driver in identifying what is the best of the best of the trading techniques I am about to share with you. Bob does earn his living from trading the financial markets. He has lived and breathed the markets day after day for more than fifteen years, and has always been his own boss. He answers to no-one, except the market, and sometimes, as Bob often tells me, his lovely wife and young daughter.

He provides a wealth of knowledge which has made its way into this course and a perspective from a full time trader, just in case you believe this course needed any.

How the mathematical and geometric relationships work in the market

One of the things which I agonised over when writing this book was how to choose which market (or markets) I was going to refer to as working examples of how market geometry works.

I have seen these techniques I am about to share with you work in all types of markets – be it, stocks, stock indices, currencies or commodities. To demonstrate this, I was tempted to find an example of a particular technique working in each of those markets and to write each chapter based on that. In doing so, however, I felt that it may not present the full picture which I believe is required in order to produce a successful forecast.

For that reason, I have chosen to present the examples in this book using the United States S&P 500 stock index as the primary basis. In my view, this index represents the global benchmark of equity indices, so it is a pretty reasonable place to start.

Rather than go back too far in time and pick out the best examples over the last one hundred years, I have chosen to use the most recent price action available (as of January 2014) – as I think this is probably more relevant to most of you. By the end of it, I hope to have shown you how all of the Trading Tools presented are still relevant in the market today dominated by an age of computerised trading, just as they were one hundred years ago before computers existed.

Although I have chosen the S&P500 as the basis for this book, it is important to recognise that the forecasting techniques I am about to show you can be applied to all markets. For that reason, where appropriate, I will be using some additional examples from the gold and silver markets as well as some examples of the Australian equity market, as they are basically the markets where I first cut my teeth and began to apply my learnings and making forecasts.

I will show you how to construct a road map for the next 12 to 24 months ahead so you may determine the likely position of the market. In addition, Bob has been kind enough to share the trade entry techniques that he has refined over the years in order to successfully trade off a forecast top or bottom and the tips that he uses to minimise losses and maximise profit.

Calculating a successful market forecast is a bit like a jig saw puzzle that requires you to put all of the pieces (or techniques) I am about to show you together. This course tries to simplify the jigsaw into fewer pieces.

I trust that you will find these examples as illuminating and useful as I do.

Each technique I am about to show you is an indicator which works in harmony with the others. The most successful forecasts therefore work when these techniques are all working together.

Discovering the geometry in markets

Bob and I began our journey studying the financial markets both as university students in the late 1990's. Our study was heavily influenced by the work of W.D. Gann in the early days, but we soon came to realise that there were many other tricks which worked just as well, if not better, and more consistently in the markets.

Having been Gann students for a number of years, the realisation that his techniques are not the be-all and end-all to trading helped simplify our thinking and improve our analysis greatly.

- This book therefore isn't all about Gann.

It is about the best of the techniques which we have found to consistently work out there – and a number of them are used in practice by the professional traders in the current day!

I had been trying to convince Bob for a number of years to help me with writing a book on the subject. Consistently, he has been able to find a good reason not to do it. Bob prefers to have his privacy and to focus his time on trading, and I respect that.

Likewise, he has been trying to convince me for years to give up the banking game and join him full time in the pursuit of the markets.

Whilst I have been very tempted at times, I have been enjoying the challenges and rigours of the banking world too much, particularly while I am still young and energetic. I know that the markets will always be there tomorrow and that once you have mastered the techniques I am about to show you, that they will stay with you for a lifetime. Both of us had therefore agreed to leave the book for another day. Becoming parents recently however certainly has changed our perspective.

This book therefore has much to do with making sure we have a record of our experiences in writing for our children to follow should they one day choose to explore the markets like we have. The product of this book is exactly how Bob and I would attempt to teach our 30 years of collective experience to our own. I say that with the upmost sincerity.

This book represents thousands of hours of our research in state and university libraries, hours upon hours of market analysis, and actual trading experiences along the way. What you are receiving are the Trading Tools which we feel represent succinctly, and simply, what is the best of the best for analysing the markets.

If you thought the price tag of this book was expensive, it might be worthwhile to point out that it has probably cost you a lot less than a trip to the dentist. My sincere hope is that in reading it, it is nowhere near as painful!

And just in case I have left you wondering how Bob got his nickname, it is a pretty simple story really. Bob used to spend quite a considerable amount of time at our family home as we started out, trawling through all sorts of books and historical charts of stocks and commodities as we tried to figure out how this stuff all worked.

He was like an adopted brother to me and my two younger siblings. Having the same first name as your best mate however can have its disadvantages.

Eventually it became a bit confusing for my two younger brothers each time one of them tried to attract our attention – they would often yell out “Frank”, and naturally, both Bob and I would turn around. Eventually, they decided to call myself “Bill” and Bob, “Bob” so the two of us could distinguish one from the other. The name Bob stuck. Fortunately, Bill didn't – so I have always been just Frank.

Who was W.D. Gann and why is he relevant?

William Delbert Gann is legendary when it comes to Wall Street and the impact he has had on trading the markets. Arguably, he has contributed more to the study of technical analysis than any other trader past or present.

Gann developed the theory that there is a discernible relationship in all financial markets between time and price. He believed that the geometric representation of price through time would reveal important cyclical patterns within markets that had predictive values. In other words, future projections in the stock market can not only be made to calculate price, but also to forecast the dates of future market tops and bottoms.

Gann is reputed to have taken more than \$50 million from the stock markets over his career in the first half of the 20th century – which is worth over a quarter of a billion in today's money. In his published annual forecast for 1929 he figured that 'a top must come no later than the end of August and that a "Black Friday" would come in September.'

He also nominated 3 September, 1929 as a key date. History will show that the high in the Dow Jones Industrials index which preceded the Great Depression was reached on 3 September 1929.

What followed was the greatest ever fall in stock prices to this day. In my opinion, that makes his work relevant!

Many have explained in different variations the premise for why Gann's theories work. One simple explanation which I think resonates is that as human nature will never change, history is destined to repeat itself.

As a result, future generations will repeat the behaviour (or cycles) of previous generations, thereby causing all financial markets to work in cycles which will repeat over and over.

At the start of his book *How to Trade Profits in Commodities*, Gann outlined that:

'Observations and comparison of past market movements, will reveal what [markets] are going to do in the future, because the future is but a repetition of the past...

The average man's memory is too short. He only remembers what he wants to remember or what suits his hopes or fears. He depends too much on others and does not think for himself.

Therefore, he should keep a record, graph or picture of past market movements to remind him that what has happened in the past can and will happen in the future.'

Gann believed that price charts which revealed the past performance of stocks or commodities held the key in order to predict the future performance of a stock or commodity.

By looking at a historical chart of prices, one should be able to identify the past cycles which have occurred, and which will inevitably repeat in the future.

Of course, over the years, I have learnt that there is a little bit more to it behind the theory of Gann than what I have simplified from the quotes above. For our current purposes however, it is important for you to recognise that in order to discover the predictable geometry that is present in all financial markets, you must accept that market cycles have, and will, repeat. This is the foundation for being able to successfully forecast future market tops and bottoms.

The Ticker and Investment Digest – Volume 5, number 2 (December 1909)

If you are still not convinced by the relevance of Gann and the trading methods he pioneered, the following excerpts might help. In December 1909, a publication called “The Ticker and Investment Digest” interviewed Gann after he provided them with a number of accurate predictions on commodity prices using the trading methods which he had developed.

The article started by stating:

Sometime ago the attention of this magazine was attracted by certain long pull Stock Market predictions which were being made by William D Gann.

In a large number of cases Mr Gann gave us, in advance, the exact points at which certain stocks and commodities would sell, together with the prices close to the then prevailing figures which would not be touched...

The publication sent one of its staff to observe Gann real-time trading and the results he produced.

So much for what W D Gann has said and done as evidenced by himself & others. Now as to what demonstrations have taken place before our representative.

During the month of October, 1909, in twenty-five market days, W D Gann made, in the presence of our representative, two hundred and eighty-six transactions in various stocks, on both the long and short side of the market. Two hundred and sixty-four of these transactions resulted in profits; twenty-two in losses.

In other words, in a period which covered less than a month, Gann made 286 trades with an extraordinary win to loss ratio of over 92%. That trading resulted in a return of over 1000% of his original capital.

And just in case you thought that was a typo, it was 1000%. In my view, this is a trading record that I have never seen repeated by anyone... ever! If somebody has, then they certainly aren't telling anyone about it.

But what stood out to me the most from that article in 1909, and which continues to stand out to me each time I read it, is the following paragraph:

One of the most astonishing calculations made by Mr. Gann was during last summer [1909] when he predicted that September Wheat would sell at \$1.20. This meant that it must touch that figure before the end of the month of September. At twelve o'clock, Chicago time, on September 30th (the last day) the option was selling below \$1.08, and it looked as though his prediction would not be fulfilled.

Mr. Gann said, 'If it does not touch \$1.20 by the close of the market it will prove that there is something wrong with my whole method of calculation. I do not care what the price is now, it must go there.' It is common history that September Wheat surprised the whole country by selling at \$1.20 and no higher in the very last hour of trading, closing at that figure.

So there you have it. Not only do I believe Gann is relevant, he was at times, truly astonishing.

The philosophy behind price and time

Gann observed that price cannot exist outside of time. He was able to quantify that whilst the price of any stock, bond, commodity or currency stops trading as the market closes, time continues forward and is indifferent to price.

Most of you would be familiar with how a stock chart plots the price of a stock or commodity displaying its historical price action as a function of time.

Price is depicted on the vertical y-axis of a chart, whilst time is recorded on the horizontal x-axis. Gann identified that there is a total regularity to time. Each of the hours, minutes and seconds of a day can be scientifically measured with precision and measured against a predictable time line on a chart. At the time, this was a revolutionary concept.



Price vs Time Graph

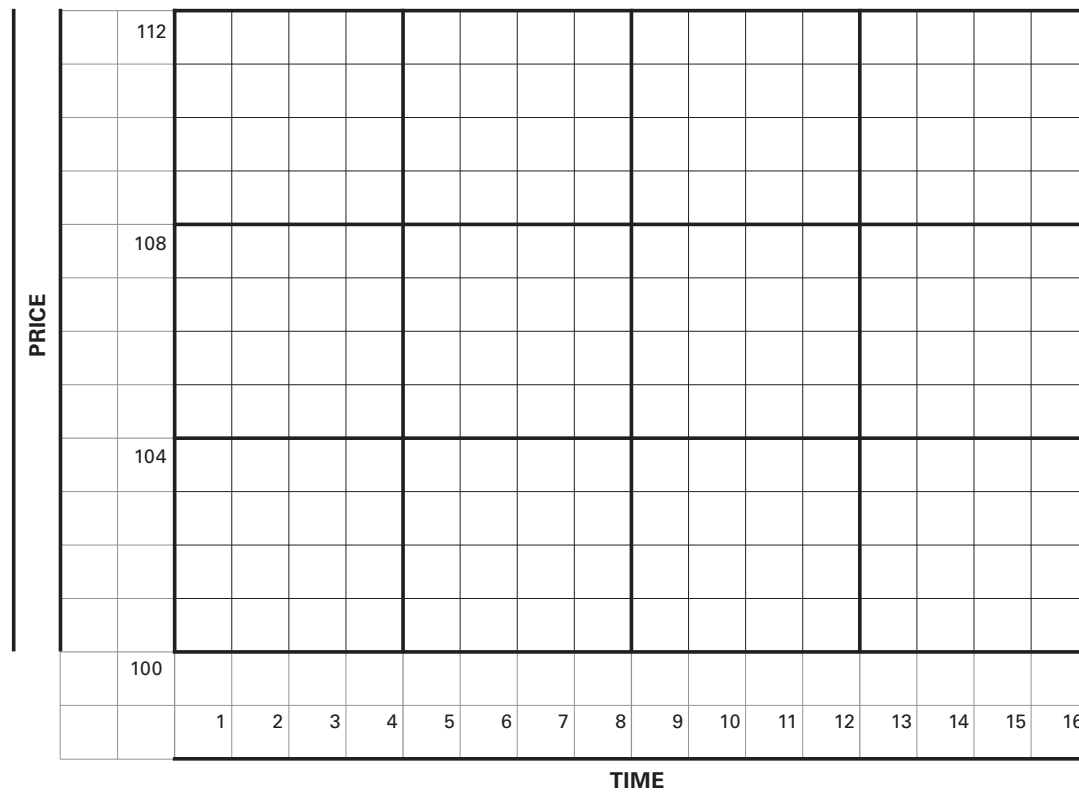
Intro .01

One thing which is important to realise is that Gann operated in an age where computer technology did not exist.

Accordingly, he kept a meticulous collection of hand drawn charts. He did, for the most part, go to painstaking effort to ensure he recorded his data on charts which were created with equal intervals in both time (as measured on the horizontal axis) and price (as measured by the vertical axis). Gann employed the use of chart paper with eight squares to the inch, with every fourth line highlighted.

This allowed him to create a chart that was scaled where one unit of price (for example, one cent or one point on a stock index) was exactly in proportion to one unit of time (for example, one day, week or month).

Personally, I think the need to keep track of your charts on grid like paper is no longer required given there are so many effective trading software programs out there today to do it for you. If however, you do intend to maintain hand drawn charts like Gann did then I would highly recommend doing so by using the same 8 x 8 chart paper that Gann used, and keeping your charts in the same price to time relationship.



Price vs Time Graph

Intro .02

This method will help you immensely in seeing the geometry unfold with your very own eyes, and will be of considerable assistance if you do go about attempting to re-create some of Gann's charts or work through many of the examples he left behind in his writings, by hand.

Fibonacci

There is no doubt that WD Gann has heavily influenced my thinking and the way I approach my analysis of the markets. But it was the discovery of a broader, underlying geometry present in the markets which made me realise that my analysis had to extend far greater than his work alone.

I was aware of the Fibonacci sequence and its application to the financial markets when I began my traineeship as a foreign exchange trader in a leading Australian bank. One of the up and coming traders on the floor, who I figured had about 5 to 10 years of experience, quizzed me whether I had heard of Fibonacci on my first day on the role – he was expecting me to have no idea who Fibonacci was, and to send me off on a research journey so that I would stay out of his way for a little while.

Much to his surprise, I told him what I knew about the mathematician, so he sent me off to fetch him a coffee and a sandwich instead! To be perfectly honest, at the time, I was more surprised that he knew who Fibonacci was – and surprised even further when I learnt that he adopted the Fibonacci sequence in his trading. I quickly learned that Fibonacci was used by a number of the other seasoned traders on the floor.

The Fibonacci sequence was named after Leonard Fibonacci, the author of the book *Liber Abaci* written way back in 1202.

Whilst Fibonacci is acknowledged for introducing the sequence to Western European mathematics, its origins are dated back much earlier into Indian mathematics. The Fibonacci sequence of numbers follows a distinctive pattern which can be found throughout a number of biological structures such as the branching in trees, the growth pattern of a flower and the arrangement of a pine cone, amongst others.

The sequence is depicted by a set of numbers as follows: 0, 1, 1, 2, 3, 5, 8, 13, 21, 34, 55, 89, 144... and so on.

Each number in the sequence is simply the sum of the two preceding numbers, allowing the sequence to continue indefinitely. In the example above, I have deliberately left the sequence to end at 144 – it is a number you will become familiar with a little later.

What is remarkable about the Fibonacci sequence, and why it is so relevant to the geometry of markets, is that the numerical sequence is such that each number is approximately 1.618 times greater than the number preceding it.

At this point in time, I think it is important for you to pause and reflect on that number 1.618, as you will see it (or a derivation of it) appear time and time again in the markets.

The relevance of 1.618 to geometry is that it closely reflects the mathematical “Golden Ratio.” The Golden Ratio has fascinated Western mathematics for close to 2,500 years. Mathematicians from Ancient Greece first studied the Golden Ratio because of its frequent appearance in geometry.

Since then, some of the greatest mathematical minds of all time, including Pythagoras, Leonardo of Pisa and the astronomer Johannes Kepler have spent hours analysing the Golden Ratio and its properties. Some have said that it has inspired thinkers of all disciplines like no other number in the history of mathematics.

The Fibonacci Retracement

In trading, I believe the Fibonacci sequence (in particular, Fibonacci Retracements) is used more frequently by technical traders than any other price forecasting tool in the industry. It is very rare for you to switch on the financial channel on TV and not hear one technical analyst or another discuss it. Perhaps it is the mere fact that nearly every technical analyst is aware of the Fibonacci Retracement is what makes it relevant. I will show you later on, just how powerful and predictive these retracements can be.

A Fibonacci retracement is created by selecting two points on a chart, represented by a market top and bottom, and by dividing the vertical distance by the selected Fibonacci ratios. The percentages are then used to draw horizontal lines across the chart and identify possible support and resistance levels.

The key Fibonacci level used the most is a retracement of 61.8%. Again, I point you back to the Golden Ratio number I referred to early. It can be found by dividing one number in the Fibonacci sequence by the number that follows it – for example, $55/89 = 0.6179$. Whilst the mathematical result of the numbers in each of the sequences does not exactly equal 0.618, they are very closely approximate. The number to use in your analysis however is 61.8%.

I also like to use the ratio of 38.2% in my analysis. This is found by dividing one number in the Fibonacci series by the number that is found two places to its right – for example, $55/144 = 0.3819$.

Many traders will often use the ratio of 23.6%, which is found by dividing one number in the series by a number that is three places to its right – for example, $34/144 = 0.2361$.

In my analysis, I stick simply to 61.8% and 38.2%. For now, these are the only two numbers we need to worry about.

The example in the next chart uses the market top identified as point A as the starting point and the following market low at point B as the end. (The price action in the chart actually reflects the movement of the Australian stock market from its all-time high in 2007 to the end of 2013).

For the purposes of our illustration however, we will assume a nominal price for our starting and ending points. Each Fibonacci retracement level is calculated using the percentages between these two points). For example, if the top at point A occurred at a price of \$11.00 and the low at point B at a price of \$1.00, we have a range of \$10.00 which we use to calculate the Fibonacci retracements.

The 61.8% point for example would be represented by the price \$7.18 – which equals $61.8\% \times \$10.00 + \text{the low of } \1.00 . We will discuss Fibonacci in more detail a little later.

23.6%

38.2%

61.8%



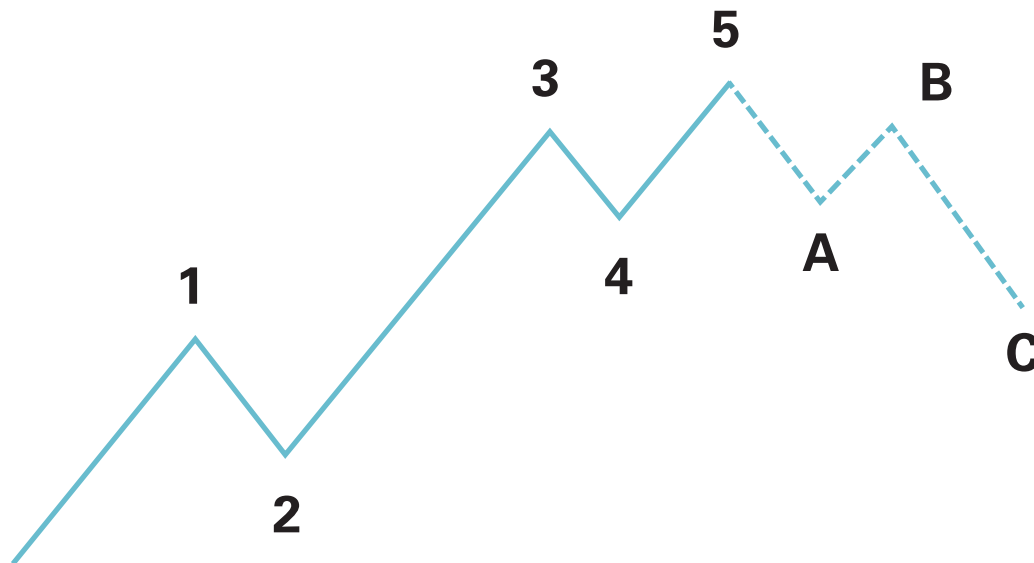
Ralph Nelson Elliott

If you have spent any time studying technical analysis of the markets, you will probably notice the name R.N. Elliott come up – a lot. Elliot is credited with discovering his Elliott Wave Principle, which he used to describe market price movements occurring as a result of natural human behaviour.

The underlying premise to Elliott theory is that markets represent a mass of people – the crowd – and their behaviour. Changes in the mass of psychology of the crowd will therefore cause fluctuations in markets based on the underlying pessimism or optimism of the crowd prevailing at the time.

According to Elliott, this creates specific patterns which can be measured in the markets and will often repeat themselves due to the underlying basis that human nature over time never changes.

At the heart of Elliott Wave Theory is that each major market movement (or dominant trend) will unfold in a five way sequence (represented below as 1 to 5), and each minor movement (or corrective trend) will unfold in a three way sequence (represented below as A to C).



Elliott Wave Principle

Intro .04

I acknowledge that this is just an over simplification of Elliott's work, and I apologise if I have offended any of the Elliott Wave practitioners out there.

However, what I have found, particularly with the increase of computerised trading over recent years, is attempting to identify a more detailed application of Elliott Wave sequence and applying it over the markets on the smaller moves (ie the moves that occur within the major long term trend) can produce confusing results.

In the interest of keeping it simple, I stick to the basic five wave and three wave sequences above. In the next chapter you will see that this is one thing that both Elliott and Gann had in common.

Making it simple

One of the pitfalls which I have faced when studying the various tools used in technical analysis is that there are so many indicators, it can make it difficult for the inexperienced to know which ones to use and when they should be used.

Over the years, Bob and I have discovered that there were some techniques which work better and more consistently than others. This is particularly the case when using Gann. For Bob in particular, this has caused him to redefine his analysis and simplify the way he looks at markets. My own ability to forecast market tops and bottom also relies on a selected number of indicators which I use as primary tools.

These are the tools we will share with you in this course – keeping it simple.

The basis of this book is all about simplifying your analysis.

For me, too much information can make it all a little bit unworkable. With that in mind, the Trading Tools I am about to share with you are what I truly feel represent the absolute best.

SECTION ONE

The simple objective should be to trade the trend – not a perspective.

Identifying the trend

The first objective for anyone looking to analyse the market is to be able to identify the trend and make sure you are invested with it!

This section is all about showing you how to review the historical price movements of your selected market and identify what the chart is telling you. It is my opinion that the greatest profits are made by making sure you are trading with the major trend and not against it. Not only can your profits be much greater, but trading with the trend is easier and requires much less work.

One of the things you will need to control once you have mastered the ability to predict a market top is the lure of the fast gains that can be made by successfully being able to nail a high which precedes a crash. It is often said that 'markets will go up by the stairs, but down by the elevator' – in other words, bear markets bring fast profits.

The problem is however, that markets in general (equity markets in particular) spend most of their time these days going up. If you are constantly being a perma-bear trying to call every market top, you will often see yourself sitting on the sidelines whilst the others are making the bull market gains.

A very good case in point is the bull market in Gold from the 2001 low to the September 2011 high. Whilst there were a number of significant corrections in between, the best money to be made was by holding a long position in gold over that period. Once you were able to identify that a bull market was underway, even a passive 'buy and hold' strategy would have rewarded you handsomely.

On the other hand however, attempting to trade each of the corrections in the bull market and always trying to predict the top would have left you licking your wounds from being short, or feeling cold while you were out on the sidelines whilst the gains were being made. Repeat that experience if you were a perma-bear constantly calling for a correction in US equities to occur throughout 2012 and 2013.

The safest money in that market (and the easiest) was made by the bulls – not by the bears. It was afterall, a bull market.

Chapter One – How to know you are trading with the trend

Markets will either operate in one of three stages of activity which can be described to categorise the direction of stock or commodity prices:

1. Bull market

Where prices are going up, defined by higher tops and higher bottoms

2. Bear market

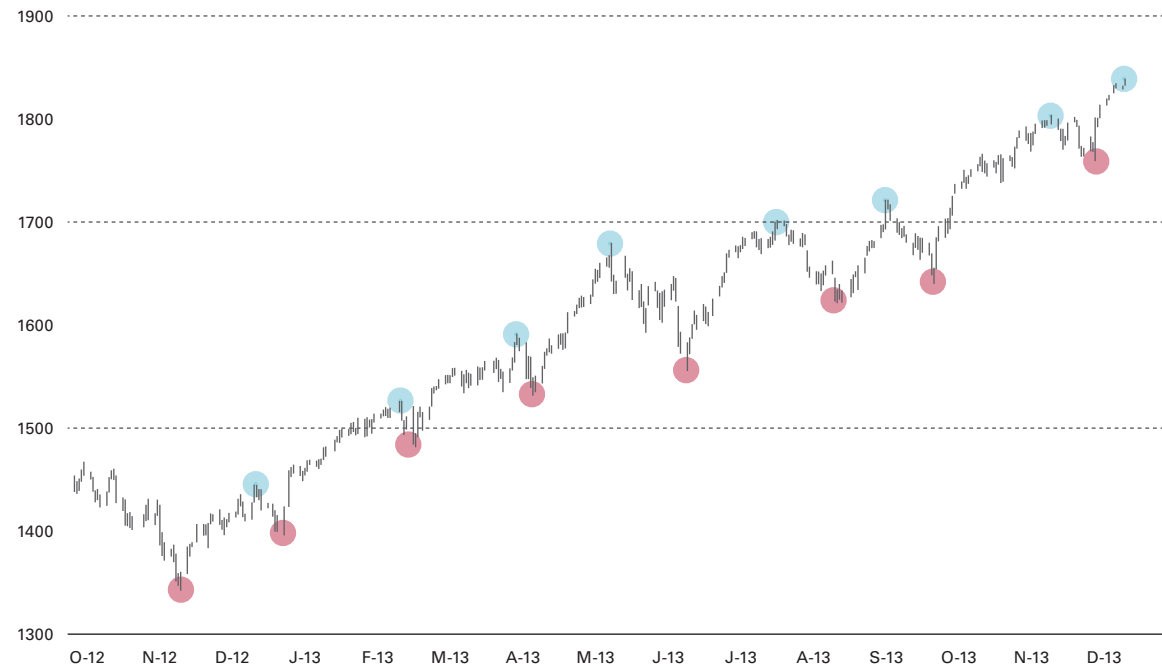
Where prices are going down, defined by lower tops and lower bottoms

3. Sideways market

Where prices appear to be 'range bound' and are not consistently displaying the characteristics of either a bull or bear market

Illustration of a Bull Market

The following chart depicts the performance of the S&P500 market throughout the 2013 calendar year. Notice how the market was consistently making higher tops (in green) and higher lows (in red).



The Bull Market

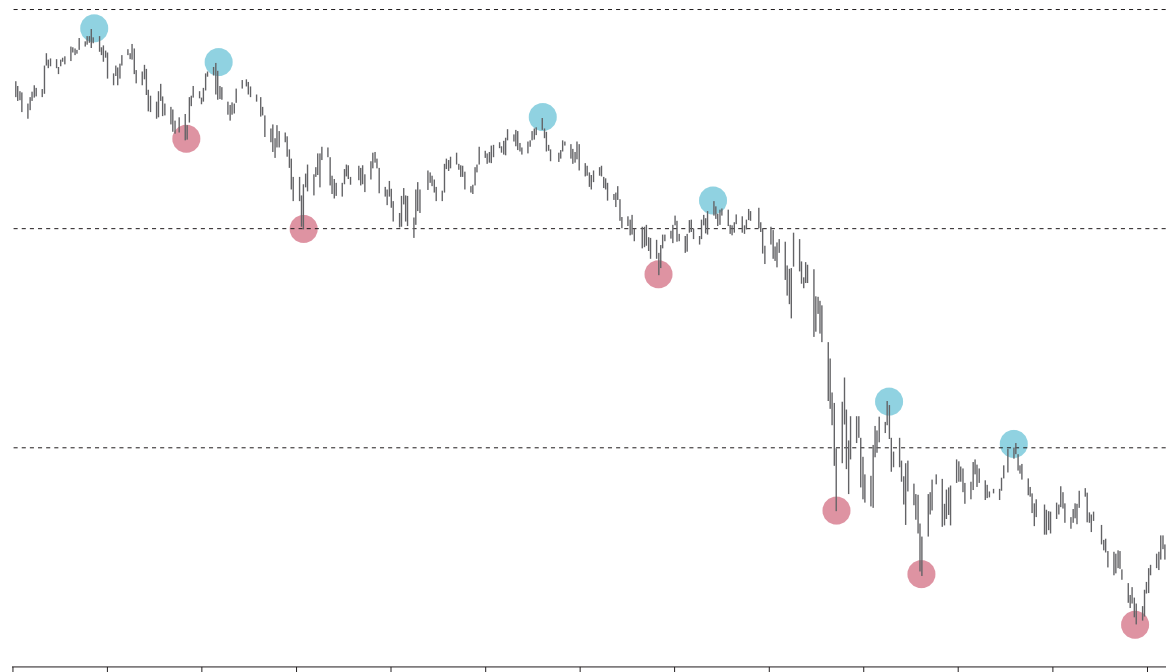
Illustration 1.01

In a bull market such as this, the safest money is made trading the long side of the market by trading with the trend. The 'buy and hold' theory works beautifully in these types of markets.

Illustration of a Bear Market

The chart (right) depicts the performance of the S&P500 market throughout the bear market campaign which began off the high in October 2007 until it reached its final low in March 2009. Notice how the market was consistently making lower tops (in green) and lower lows (in red).

Bear markets will often move faster in terms of price over a shorter period of time than a bull market, and can easily get ugly if you are on the wrong side of the trend.



The Bear Market

Illustration 1.02

Illustration of a sideways market

The following chart depicts the performance of the precious metal market in Silver throughout 2011 and 2012. Notice how the market during that period was not distinctively making either higher tops or higher bottoms, but was rather trading within a range bound by the two horizontal blue lines. These types of trading conditions are a professional traders dream but can be a nightmare for the beginner who will often get caught buying from the professionals at the top of the range and selling back to them at the bottom.

As an aside: notice how that it was not until late 2012 where the Silver market made its first lower top and lower bottom (as represented by the green and red markers) – this was your indication that the trend had turned down and that a bear market had commenced.

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The Sideways Market

Illustration 1.03

'You will always make the most profit by following the main trend and playing the long swing...

It is much better to make 3 or 4 trades each year and make large profits, than it is to try and make 100 to 200 trades a year and be wrong half the time, and finally end up with a net loss.

Let your rule be to -

**GO WITH THE MAIN TREND,
AND NEVER BUCK IT.**

If you don't know what the trend is, don't get in the market.'

The clear lesson to be gained from that piece of advice is that identifying what the trend is, is fundamental before one should even think about entering the market. You will produce much better results attempting to identify and trade a market bottom in the middle of a bull run than attempting to forecast each corrective top against it.

This is the view I shared with friends and colleagues in late 2011 when I became convinced that the bull market in equities was set to continue. Had I been looking for the short side of the trade all of the time, it would have proven itself to be quite costly. Those who were have missed out on some of the fastest gains in recent memory.

Know what the trend is, and make sure you are on the right side of it!

Source. W.D. Gann – How to Make Profits in Commodities (Pg 55)

Swing charts

One of the simplest trend following methodologies used by Gann in his analysis was the construction of a swing chart. Gann used the swing chart not only as a trend indicator, but as the basis for a mechanical method of entering and exiting trades.

In order to construct a swing chart, you will need to know the daily high and low prices in each time period you are using. For this reason, swing charts can be drawn using the traditional open-high-low-close bar chart or from candlestick charts.

How to construct a swing chart

The construction of a swing chart results in what Gann called a Trend Line Indicator. It can be created using any period of time – daily, weekly, monthly, yearly or even intra-day periods.

When using a bar chart or candlestick chart, there are four classifications of 'day' types. Each is identified with respect to the previous day or period.

1. Up day = higher high and higher low
2. Down day = lower low and lower high
3. Outside day = higher high and lower low
4. Inside day = lower high and higher low

In each case above, you can substitute the word 'day' with your preferred period of time – for example, week, month, hour, or 15 minute period.

In a bull market, the Swing Chart moves to the high of on an up day and keeps moving higher until a reversal day or down day is recorded. If the market has made three up days in a row, that will convert into one vertical line moving all the way up to the high of that third day.

For the swing chart to move down, either a 'down day' or an 'outside day' would need to occur, causing the low of the previous bar (or 'day') in the upward move to be broken, therefore creating the swing down.

The swing chart would then continue lower until a new 'up day' or an 'outside day' breaks new highs on the bar charts. To make your life a little easier, inside days are simply ignored for the purposes of constructing a swing chart.

When an outside day occurs, my general rule of thumb is to follow what the intra-day price movements were when constructing your swing chart. For example, if we have had three consecutive up-days followed by an outside day that started the trading day lower, but then ended higher, I would swing the chart down to the low of that outside day, and then back up again – simply following the chronological movement of the market.

The swing chart provides you with a definable, mechanical method for identifying a trend and removes much of the 'noise' that is created when using just a daily bar or candlestick chart.

When the swing chart is making higher tops and higher bottoms, the trend is up.

Likewise, if the swings are making lower tops and lower bottoms, you should consider the trend down.



The Swing Chart

Illustration 1.04

Multi-period or multi-point swing charts

One useful adaption of the swing chart is to minimise the number of swing movements using time or price as a constraint. For example, rather than construct a swing chart using every bar (or day) as your time period to follow, you may increase the amount of time or price required to move your swing chart up or down. For example, Gann often worked with 3-day swing charts.

A 3-day swing chart requires there to be three 'up days' to occur before the swing line is moved up. If only 2 days up occur, the swing does not move. You can follow this same approach by filtering the swings through price – ie a 100 point swing chart means you need a price move of 100 points or more before the swing chart line will move. You should vary the price used depending on your market.

In my experience, I will most often use a one-day swing chart and a 2-day swing chart to confirm my forecasting. I have found that the 2-day swing chart in particular is useful to cut out some of the noise which can often result with the use of a daily swing chart alone. This is particularly so with the influence of computerised trading and many of the algorithm driven 'black boxes' out there which are programmed to trigger stops and therefore create false moves if using a one-day swing chart.