

Trader Education Tutorial

Practical Application of Price, Time and Pattern – Part 2

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Over the last few months I have been detailing the Price, Time and Pattern characteristics of all the individual Elliott Waves. I have also detailed several trend reversal and trend continuation trade entry strategies. These tutorials are all available for download from the Traders Education Archives.

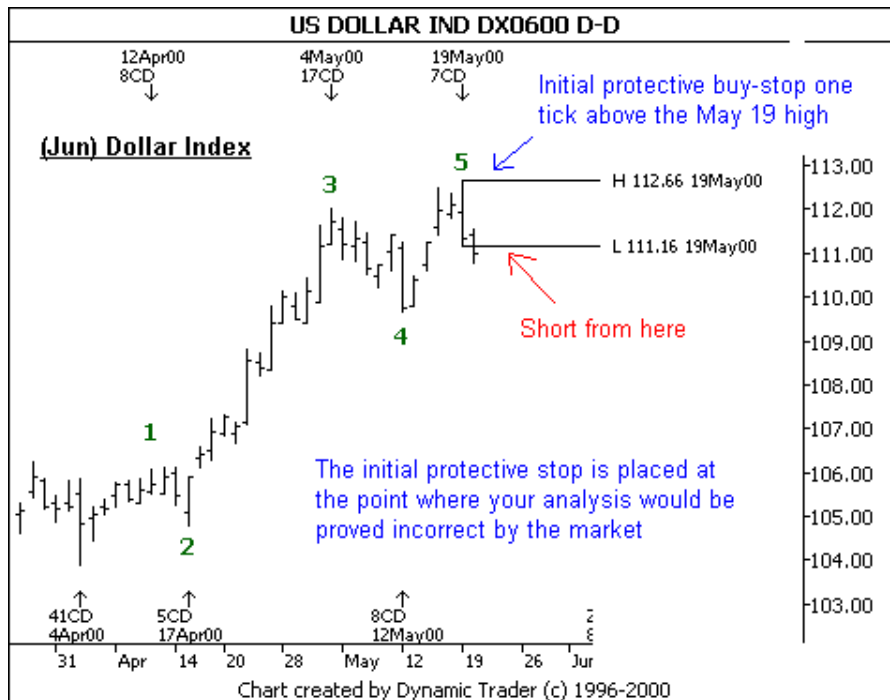
This week I would like to continue last week's tutorial which showed the analysis we used to initiate a short trade on the dollar index with a look at trade management. In other words, once we have successfully entered a position and the market trends favourably, how do we manage the trade?

To recap from last week: A new short position was entered in the (Jun) dollar index contract on the peak of the low of the outside reversal day of May 19 at 111.16. May 19 was assumed to be a Wave 5 high and therefore the completion of the entire advance off the Apr 4 low. The short strategy was recommended in the Dynamic Trader Report in advance.

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Step 1 – Initial protective stop placement.

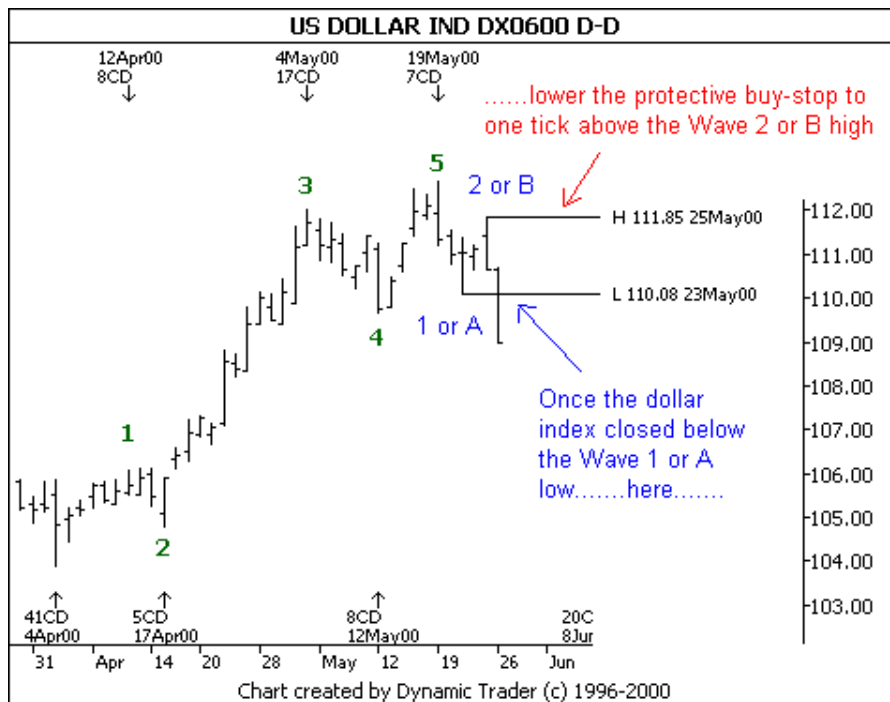
The job of the initial protective stop is to minimize the loss if a trade moves against the trader immediately, and as such is always placed at the point where the market proves the original analysis to be incorrect. In this example, a trade above the reversal day high of May 19 would void the trend-reversal trade set-up and the idea that May 19 was a Wave-5 high.



Step 2 – First protective stop adjustment.

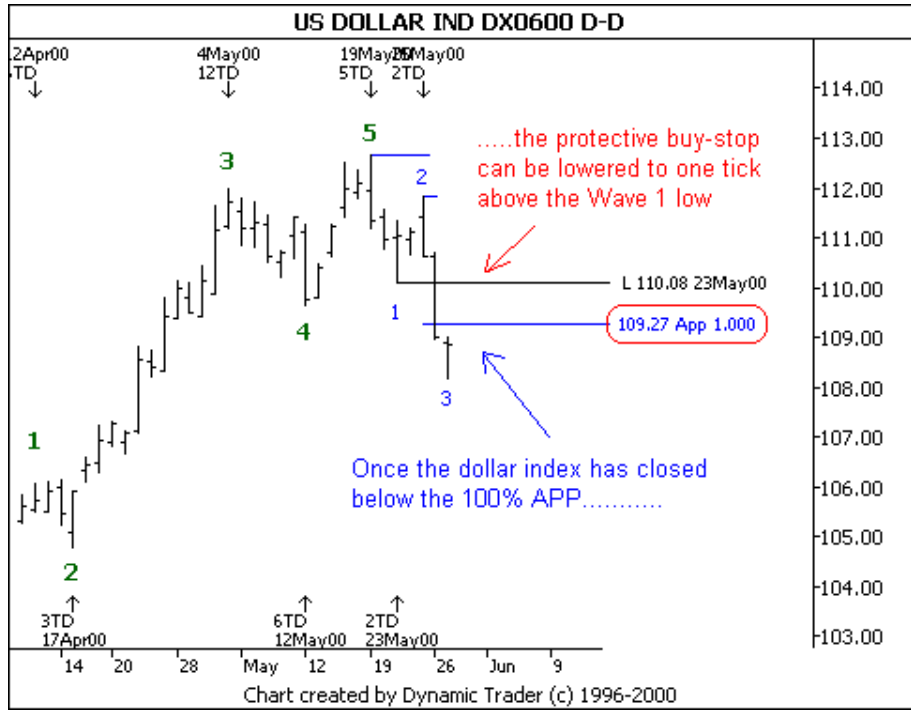
As a trade progresses in your favour, the protective stop is adjusted to protect profits as long as the trade continues to move as anticipated. The protective stop should be adjusted in a logical manner considering the technical analysis approach you use.

After a completed five-wave sequence a market is anticipated to make at least a simple ABC correction. We normally label this as a 1 or A, then 2 or B, then 3 or C, because *at this stage*, this move could be either a corrective ABC or impulsive 123 sequence. From the perspective of stop loss adjustment, the Elliott pattern is irrelevant at this stage. Once the Wave 2 or B correction is complete, lower the initial protective buy-stop to one tick above the Wave 2 or B high. Confirmation that the Wave 2 or B is complete is a close beyond the Wave 1 or A extreme.



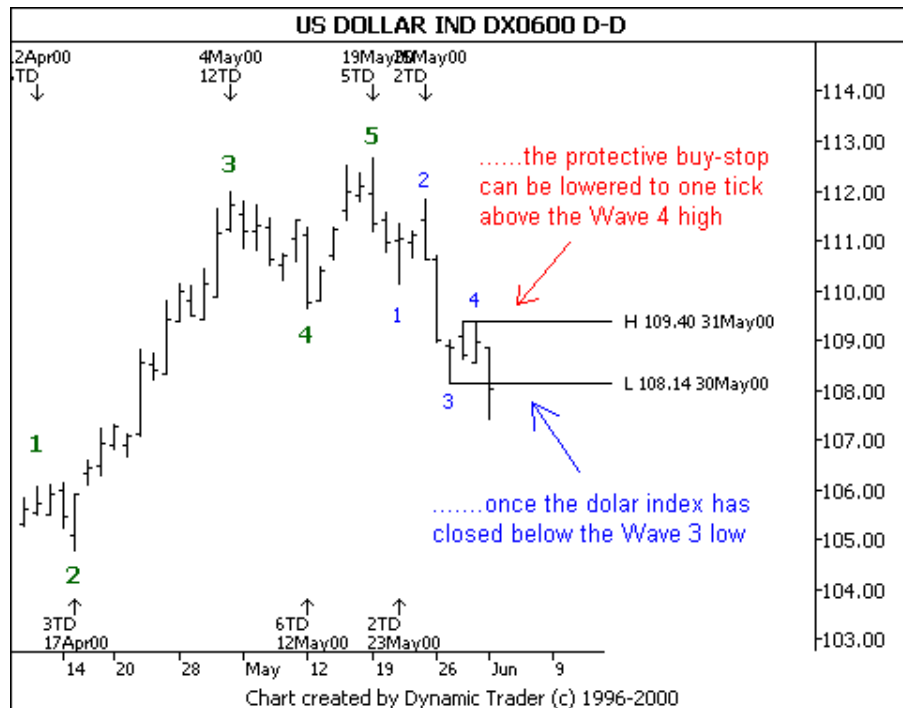
Step 3 – Second protective stop adjustment.

Once the current market move is confirmed to be a Wave 3 and not a Wave C, the protective buy stop can be lowered to one tick above the Wave 1 low. Initial confirmation that the current move is more likely to be a Wave 3 is a close beyond a 100% alternate price projection of Wave 1. In other words, where the price range of the current move off the Wave 2 or B swing is greater in price than the initial Wave 1 or A swing.



Step 4 – Third protective stop adjustment.

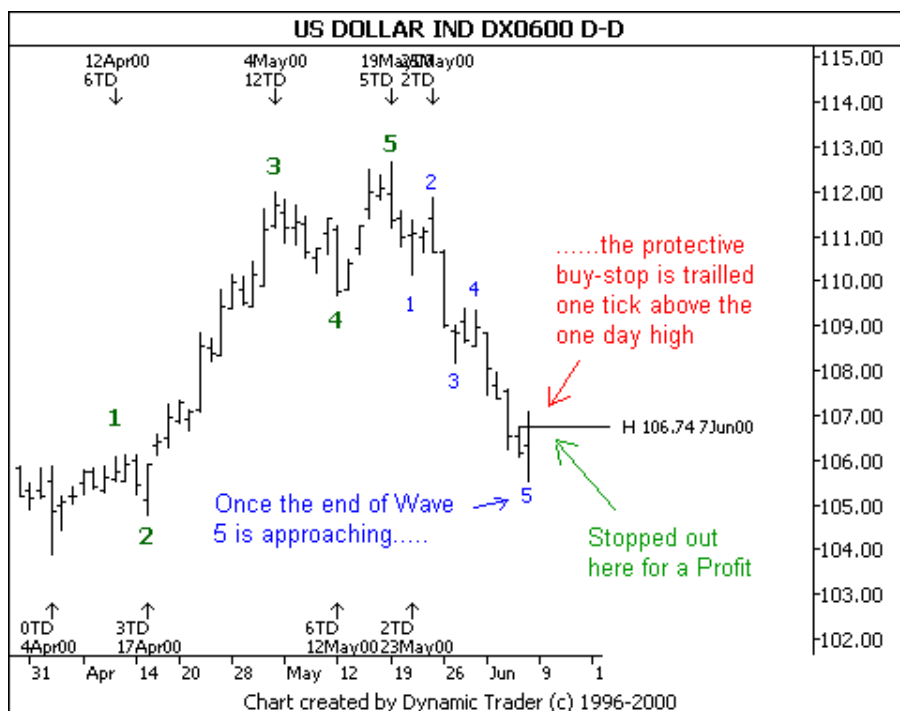
A Wave 4 correction follows a Wave 3; once this Wave 4 correction is complete, the protective stop can be lowered (in this example) to one tick above the Wave 4 high. Confirmation that the Wave 4 is complete is a close beyond the Wave 3 extreme.



Step 5 – The final protective stop adjustment.

The dollar index now appears to be in the fifth wave off the May 19th high. Wave 5 is the last swing in a completed Elliott wave sequence, therefore the current decline off the May 19th high is anticipated to be nearing an end. We now project the highest probability price targets for the termination of the wave 5. Once the market trades into this Wave 5 price target, the protective stop must be brought closer to the market to protect open profits. I have not shown the end-of-wave 5 price targets in this tutorial, as I wish to concentrate on protective stop loss adjustment.

If a market reaches the Wave-5 target zone, trail the stop one tick above the one-day-high or exit on a daily reversal signal.



The chart above shows the final result. The short trade was entered one day after the Wave-5 high on May 19 and was not stopped out until June 8 for a profit of \$4,420. This is *Dynamic Trading!*

While this analysis may seem an idealized after the fact example, chosen very carefully to show a good result, it was in fact detailing a specific trade recommendation published at the time in the Dynamic Trader report. I hope you can see how valuable the Dynamic Trading approach to technical analysis and trading strategies can be for you!

Lesson Learned

The protective stop is adjusted as a market moves in your favour just beyond a level which would prove your analysis incorrect. In this way, the trader should remain in a trade as long as the market continues to move as anticipated.

Finally, when the market enters the final stages of the entire trend, the stop is moved closer to the market to protect as much open profit as possible.

All five steps are logical, consistent and the same for any market and on any time frame.

Learn The Complete Dynamic Trading Approach

The “Putting It All Together” chapter of the Dynamic Trading book teaches the trader the trader how to integrate the specific time, price and pattern analysis techniques with the most logical trading strategies from trade-entry to trade management.

Every week in the Dynamic Trader Report, we include a specific trade tutorial. We completely explain all trade recommendations so the subscriber will know exactly how and why we arrive at trading decisions.

There is no “secret” to trading. Traders must learn a comprehensive, logical and step-by-step approach to trade analysis and management.