

## Adding PTI (Profit Taking Index) ~ Theory

Using Elliott Wave analysis, any major rally or decline can be classified as a Wave 3 (see Figure 8-1). Once a Wave 3 is in place, Elliott Wave theory continues to look for a Wave 4 Retracement followed by second attempt in the same direction. This last phase is called Wave 5.

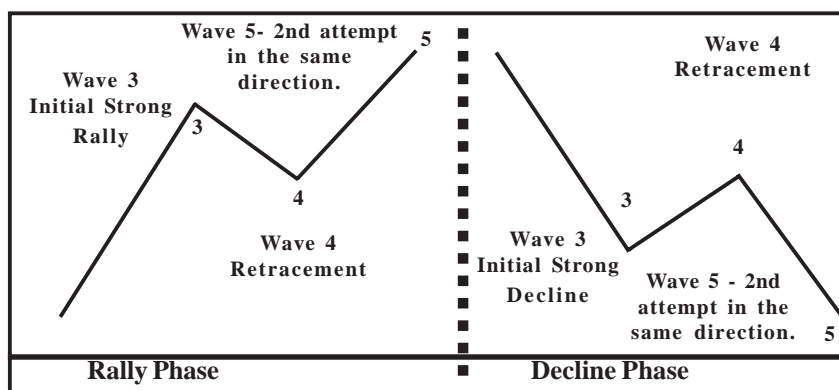


Figure 8-1: Completed Five Wave Sequences

The patterns in Figure 8-1 are completed 5-Wave sequences and are great after the fact. However, while the pattern is in progress, the trader is left with a major dilemma at the end of the Wave 4 Retracement. *This dilemma occurs because many times the second attempt fails to materialize.*

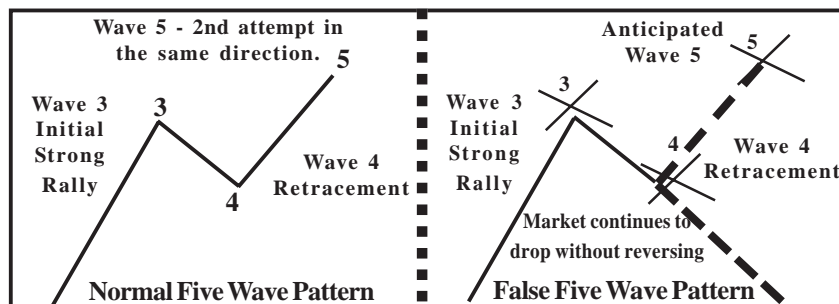
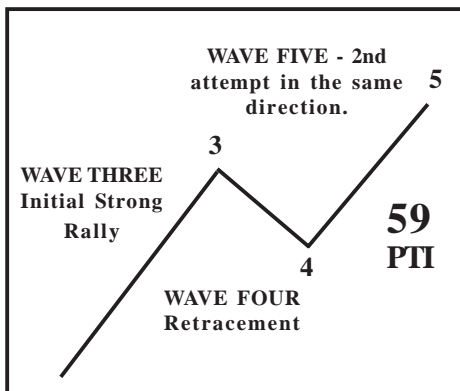


Figure 8-2: False/Normal Five Wave Patterns

## Profit Taking Index

From our years of research and development, we designed the **Profit Taking Index (PTI)**. The Profit Taking Index compares the Buying/Selling momentum in Wave Three with the Buying/Selling momentum in Wave 4. This comparison is then passed to an algorithm that calculates the Profit Taking Index Value.

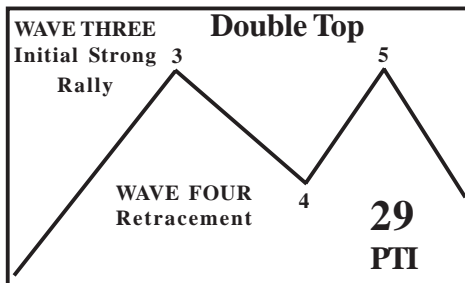
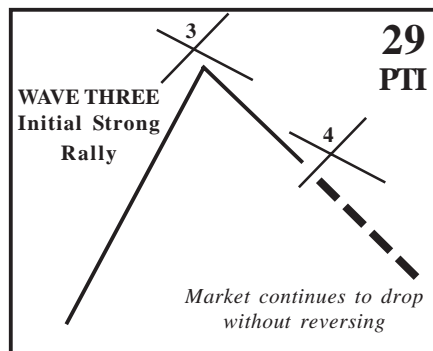


### Normal Five Wave Pattern

Statistically, if the Profit Taking Index is **greater than 35**, the market exhibits a greater tendency to initiate a Fifth Wave or a Second Attempt Phase.

### False Five Wave Pattern

Statistically, if the Profit Taking Index is **less than 35**, the market generally **fails** to initiate a Fifth Wave or 2nd Attempt Phase.



### Failed Five Wave Pattern

#### Double Top

If the Profit Taking Index is less than 35, and the market still initiates a Fifth Wave Phase, the potential for a Double Top becomes very high.

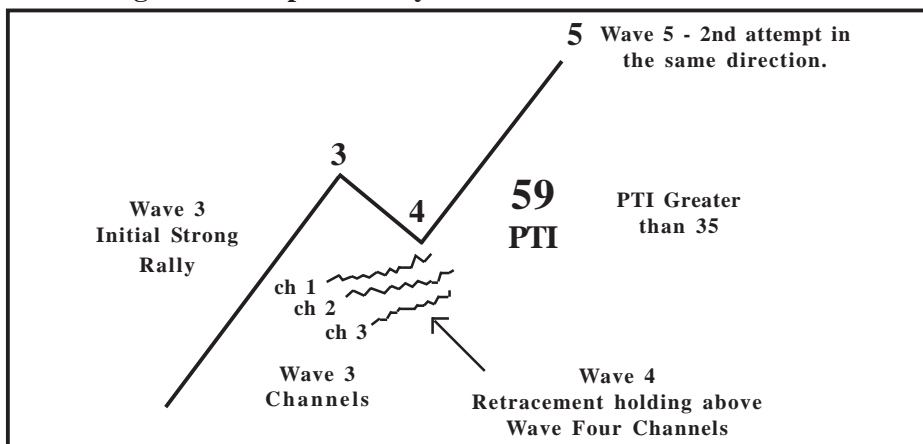
## Adding Wave 4 Channels

Wave 4 Channels are another proprietary study developed along with the Profit Taking Index. The Profit Taking Index mainly deals with Buying/Selling momentum at different stages. The Wave 4 Channels deal with time. After a strong rally, the retracement phase is allowed a certain amount of time prior to initiating the second attempt (Wave 5) Phase.

Statistical studies show that if the retracement phase consumes too much time, the 2nd attempt phase diminishes its full effect. The Wave 4 Channels are three time/price lines.

If the Wave 4 Retracement holds above the Wave 4 channels, the odds for a strong second attempt are greater.

**If the Wave 4 Retracement breaks below the Wave 4 channels, the odds for a strong 2nd attempt are very low.**



## The Significance of Wave Four Channels

- 1) If the Wave 4 retracement holds above the first channel (displayed in blue), the statistical odds are better than 80% for a strong Wave 5 rally.
- 2) If the Wave 4 retracement holds above the second channel (displayed in green), the odds for a strong Wave 5 rally is only 60%.
- 3) The third channel (displayed in red) is a final stop, because once this channel is broken the odds for a new high in Wave 5 are very low. The very few times a Fifth Wave is generated after breaking the red channel, the rally becomes a tedious, slow and drawn-out process, which literally eats away your patience and option premiums.

- When the Elliott Oscillator pulls back to zero, the Profit Taking Index (PTI) should be greater than 35. In Figure 8-3, the PTI is at 69, which indicates normal profit taking in the Wave 4 Decline.
- In addition, the prices should hold above the Wave 4 Channels, which indicate the ideal length of time for normal profit taking.
- In this chart, the prices are holding above the second Wave 4 Channel. Everything here looks good for a buy.

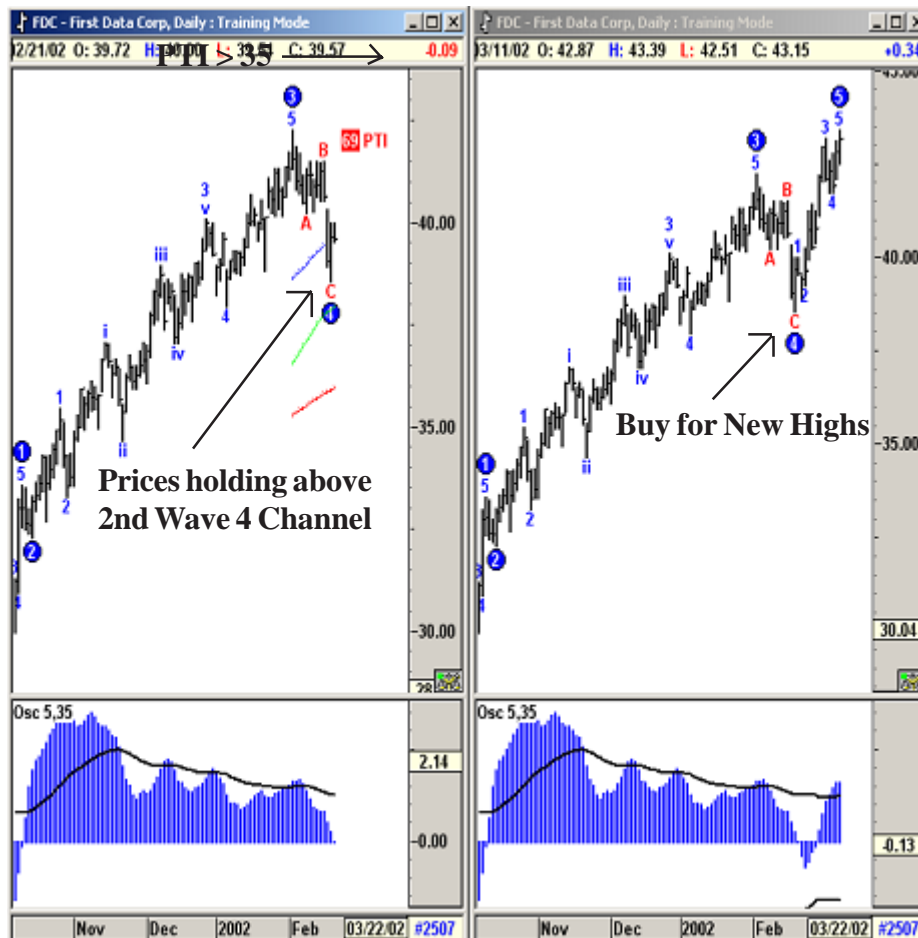


Figure 8-3: Profit Taking Index and Wave 4 Channels

Figure 8-4: New Highs

## Regression Trend Channels

We developed a tool called the Regression Trend Channels. The idea is to find the best-fit linear regression of data between any two points. The standard deviation of the data from the regression line is used to display the upper and lower channels.

While the trend continues, the market trades in the channels. Once the price breaks the Regression Trend Channels, a change of trend (bias) is indicated.

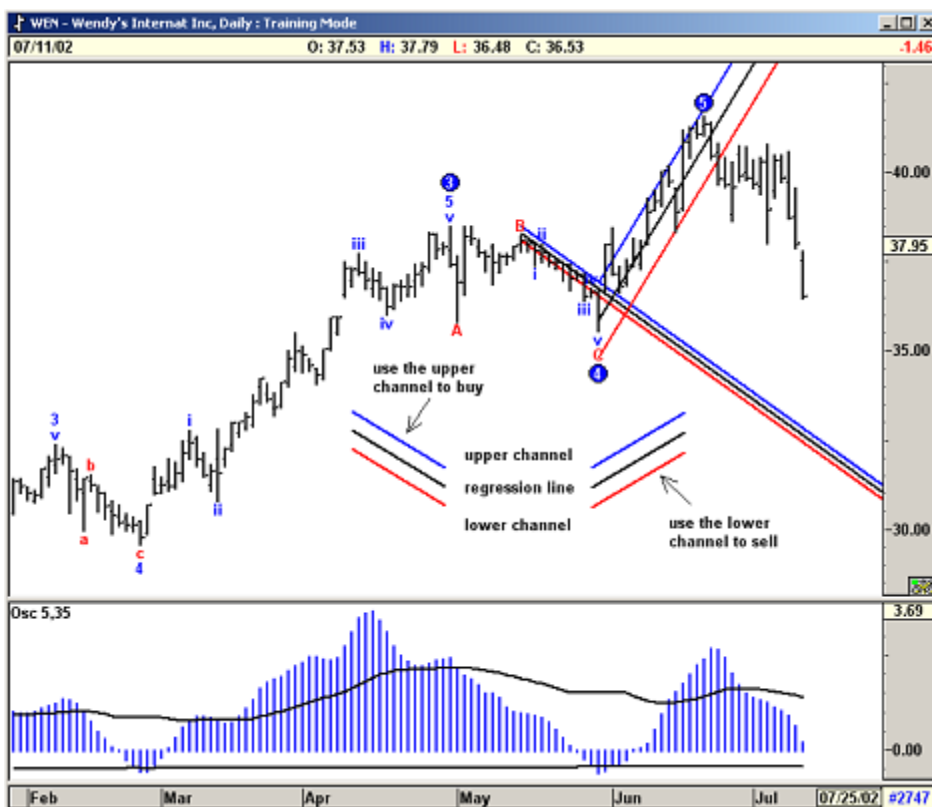


Figure 8-5: Regression Trend Channels

Both at the end of Wave 4 and Wave 5, the Regression Trend Channels can be used to provide entries in the direction of the trade.

# ***Notes***