

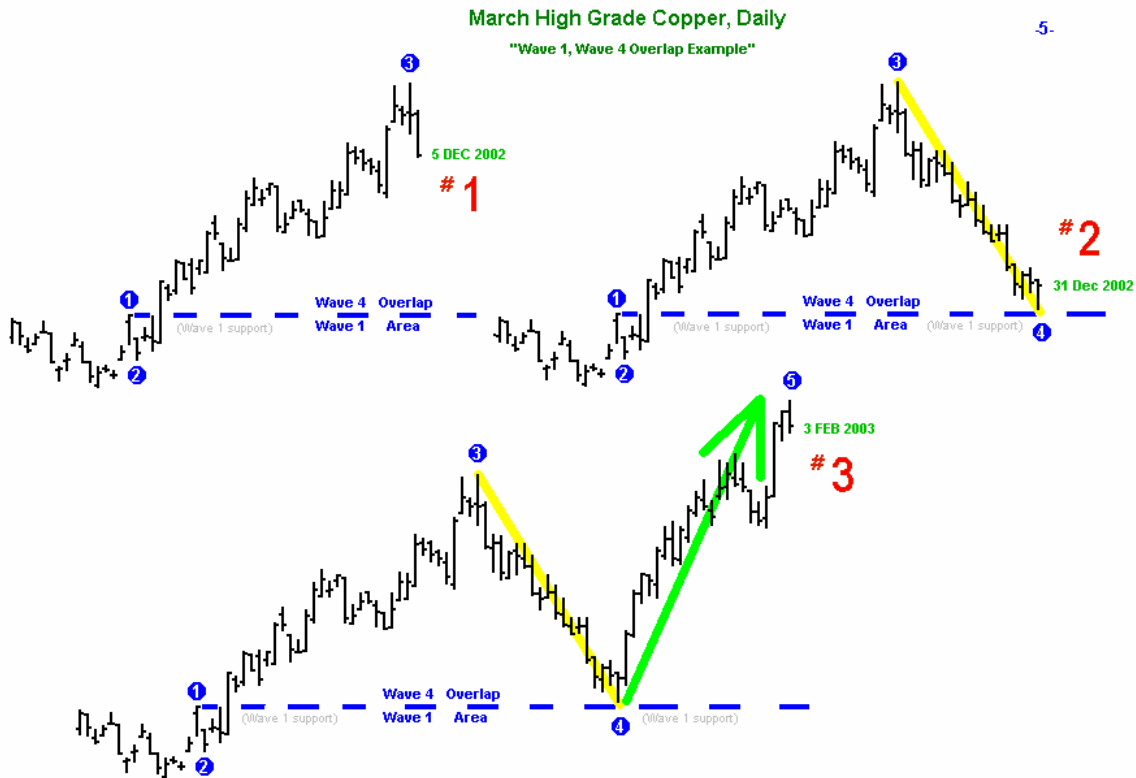
Elliott Wave Rules and Guidelines

WAVE 4 SHOULD NOT OVERLAP WAVE 1

(By Marc Rinehart)

Elliott Wave Theory in its simplest form defines a series of impulse and corrective price patterns as a *wave sequence* consisting of five general waves trending in either an up or down direction.

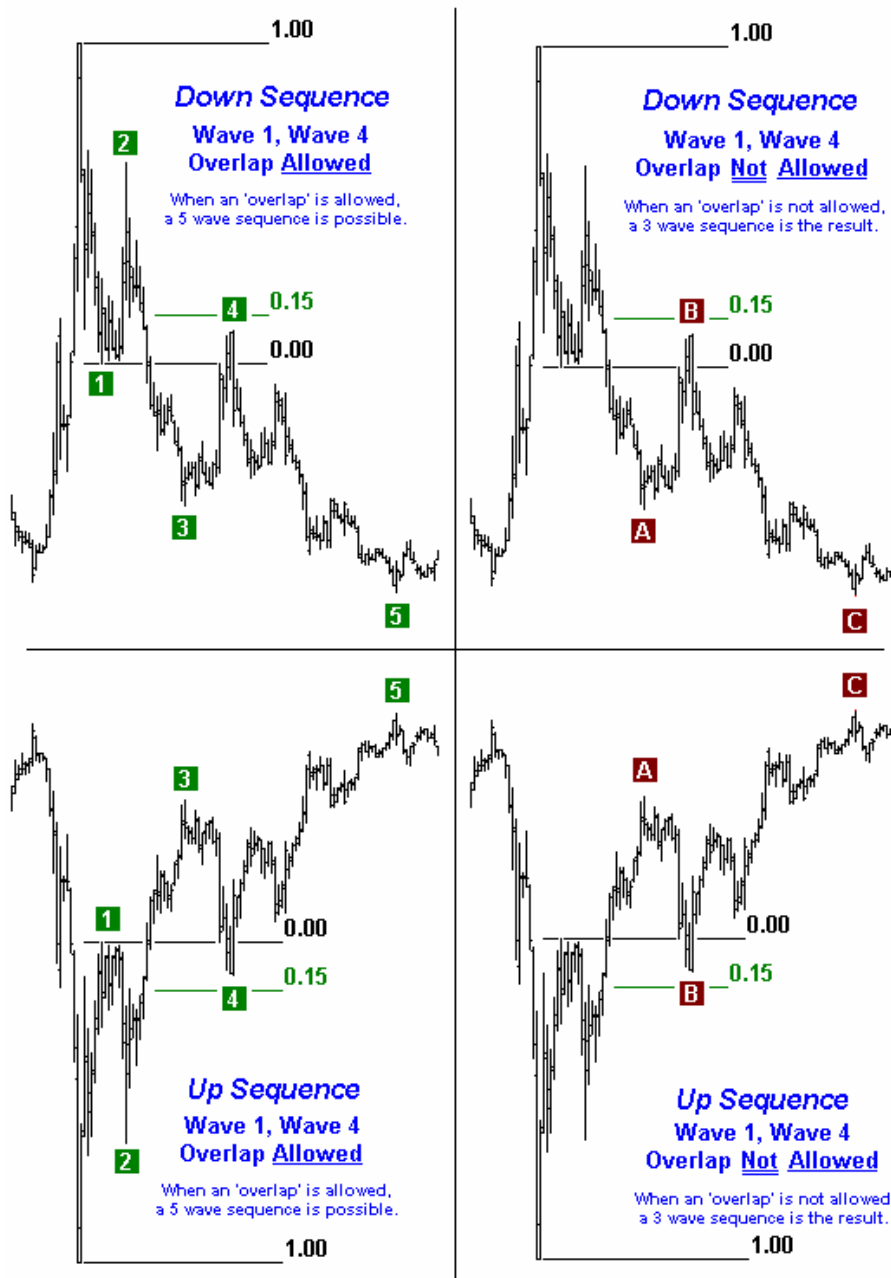
Within a general five-wave sequence there are guidelines designed to help you better *wave count*, calculate or predict wave relationships. One guideline is referred to as the "**Wave 4, Wave 1 Overlap Rule.**" This rule states for a valid five-wave sequence to occur Wave 1 cannot overlap any Wave 4 profit-taking pullback.



This means the end of Wave 4 should not trade through the peak or depression of the Wave 1 end. If an overlap occurs, the sequence becomes a three-wave (A-B-C) corrective pattern.



A more generous interpretation states a five-wave sequence still can be valid if you allow no more than 10 to 15% overlapping of Wave 1 and Wave 4 to occur. During the early stages of researching the Advanced GET Elliott Wave logic, it was concluded allowing for the 10-15% overlap exception statistically is a valid Elliott Wave approach for improving Wave 4 trading opportunity.

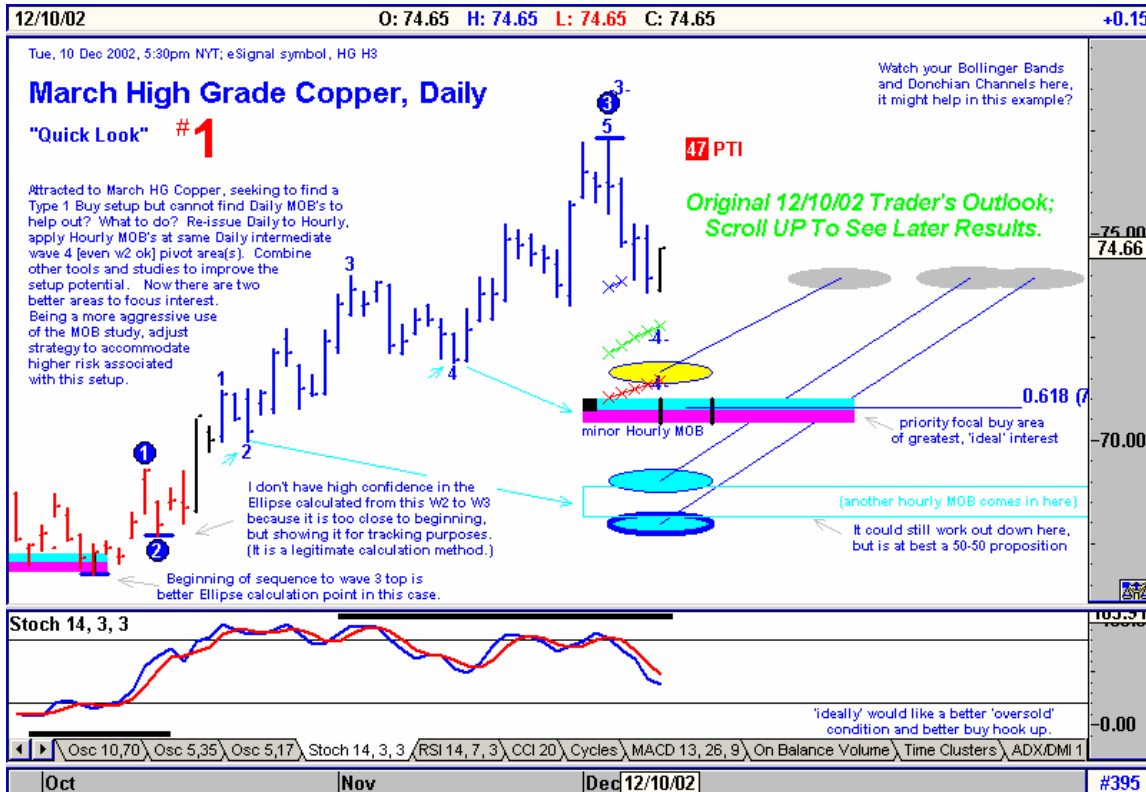


The significance of the *Wave 4, Wave 1 Overlap* rule, allowing for 10-15% overlap, is an important distinction when using Elliott Wave theory. Knowledge of this rule is useful in better defining and using *wave counts* to establish more realistic risk-verses-reward trading parameters.

Say you wish to establish a *Type 1 Buy* opportunity on a Wave 4 pullback. Why not include the overlap area in your positioning strategy if it is nearby and relevant to the trade setup. A slight adjustment in your stop loss placement, for example, could keep you from prematurely stopping out of what later turns into a winning position. The *Wave 4, Wave 1 Overlap* area can provide a respectable risk-reward ratio for aggressive traders in what is the 'last hope' wave count option.

To summarize AGET interpretation when using the *Wave 4, Wave 1 Overlap* rule: overlap violation cannot be allowed in cash markets; in futures and stock markets, research confirms a 10 to 15% *Wave 4 and Wave 1* overlapping is allowed. While rare, there are instances where a five-wave sequence still can evolve after a minor overlap. Again, remember the use of the overlap count in trading should be recognized only as a 'last resort' option on any buy or sell Type 1 setup.

An *Wave 4, Wave 1 Overlap* example is seen in the NY March '03 High Grade Copper Daily futures contract. This contract was posted 10 December, 2002, first in Advanced GET *Trader's Outlook*. A Wave 4 pullback was suggested, monitoring for a possible Type 1 Buy setup was advised at that time. (See HGH3 Chart #1)



Near the end of December a Type 1 Buy opportunity grew complicated. A quality Type 1 Buy trade setup was no longer possible using primary AGET Type 1 setup tools.

Specifically, in this example: the Wave 4 Channels didn't hold, suggesting a breakdown. The PTI became less than 35, suggesting 'normal' profit-taking was no longer evident. The 5/35 Elliott Oscillator did not hold 1.40, Ellipses minor MOB shown previous did not stop retracement.

Under this picture there really was no reason to buy HG Copper. However, what happens if you are a more aggressive risk-taker and you still want to really buy this copper contract? Knowing the *Wave 4, Wave 1 Overlap rule* provides aggressive traders an objective 'last chance' option. (See HGH3 Chart #2)

In the final analysis the overlap held. If a trade was taken, using the Regression Trend Channel or 6/4 DMA Channeling technique, combining with an aggressive Ellipse study application could have been utilized as a part of a trailing stop strategy to help protect profits. (See HGH3 Chart #3)

