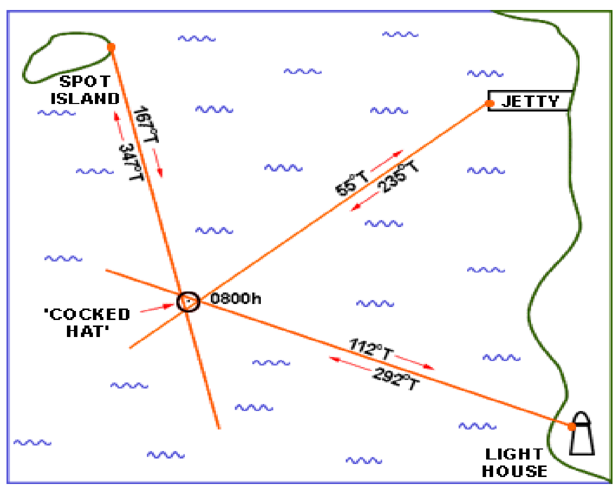
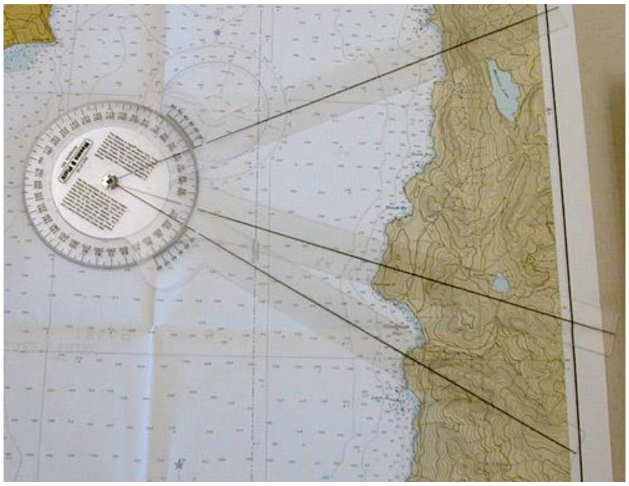
S&P in a Cocked Hat

Very occasionally I am forced to read a newspaper. Usually it is something as mundane as the weather which is of interest to me as I have many hundreds of new plants ranging from 150 meters of Murraya hedging, 40 or so assorted palms, giant Strelitzia, Gardenias, Citrus and a horde of exotics whose names escape me, all of which require that most precious commodity water. And if you want to know how precious water is, I invite you to have a spell at Queensland's Gold Coast where water is charged by the cup, quite a change from the glories of rural New Zealand where such action would be heresy. On these literary wanderings where the world of the great unwashed is forcibly imposed on one's eyeballs it seems to me that the world is concentrated on a) what someone else is doing and b) what the future holds. I am blissfully unconcerned by the former and generally unconcerned by the latter, but it is always important to know where we are in the greater scheme of life, and what are the emerging possibilities. For yachties and other offshore navigators, this is a de rigueur life form as your yacht's current position and proximity to hazards is an essential part of staying alive, and with markets churning and turning every trader like our nautical friends is obliged to have a more than proximate knowledge of where their boat is and the nearest hazard.

For those venturing on coastal jaunts within sight of land, there are some really simple techniques taught in basic navigation skills. Sight any two known landmarks and measure their angle to your boat with a basic hand bearing compass and plot those bearings on your chart. Where they intersect is where you are. A slightly more advanced technique is to plot three visible bearings and draw those lines on your chart which usually leads to a rough intersection as shown at right, and by the simple nature of having three lines, a wavering compass as the seas roll you about and the normal distortion of hand held sightings, the result will be the containment of a hopefully small area known to sailors as the "Cocked Hat". The added felicity of this technique is the smaller the cocked hat, the more accurate your positional sighting will be. Close to shore and floating calmly in protected waters will generally give you a quite small margin of error, but expand that distance to a few miles offshore and the vagaries of rudimentary tools assert themselves as the cocked hat grows exponentially.



So ideally we have an actual single intersecting point for these angles (called "bearings" by yachties mainly to confuse the uninitiated) but a practical impossibility for real life situations or alternately a very tight cocked hat, implying a degree of precision. As you see from the above picture a bearing to an object is the reciprocal of the bearing from an object so an almost fool proof refinement is to use a station pointer, a simple plastic device that will help you get that cocked hat in the right place. Set the bearings from the compass rose in the tool and then move



the station pointer until the bearings preset by you are intersecting the known landmarks and stick your charting pencil through the small hole in the center of this hand tool and voila, you have established your yacht's position with a degree of accuracy. So some simple tools to create bearings and plot their relationship one to another has satisfactorily shown where we are from which a scan of the subject chart reveals whatever else we wish to know. None of this tells us about the future. A tsunami could send us helplessly onto those nasty rocks that constantly lurk at ocean fringes; a rogue wave can cause vital gear failure and strong enough winds can wreck the sails of the unwary or worse, dismast our yacht leaving us at the mercy of the elements. Nothing in our positional search speaks to impending perils or sunny skies and fair winds. The future is still to be observed as it unfolds but knowing where we are and our position relative to knowable hazards is at the very least an essential survival skill. The chart above clearly shows not to steer North West!

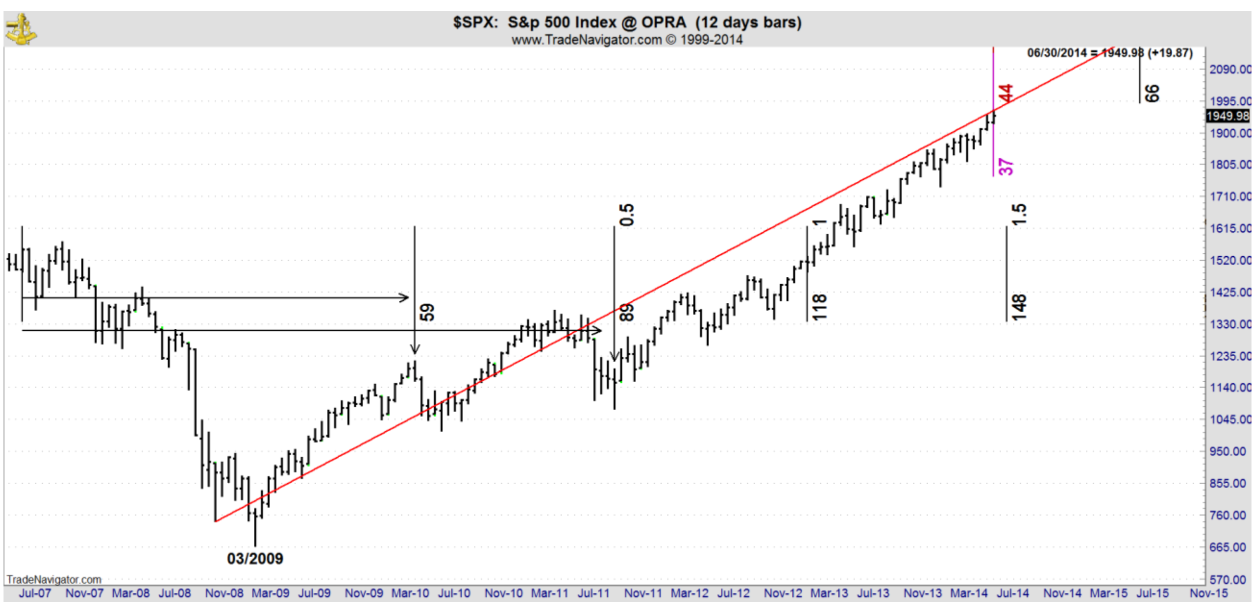
And so it is for traders. We are all (or the winning ones at least) vitally invested in this life of adventure, excitement, failure and reward. So long as markets exist we will never lack for intellectual stimulation and challenges every day and for some of us many times a day. We are indeed sailing along a fair coast with breezes that range from sublime to ferocious but we know these changes in wind speed and ocean conditions akin to volatility surges for traders are the makeup of our chosen journey and knowledge, preparedness and vigilance are the tools to keep our ship on a more or less even keel. And a key part of these qualities is a regular position check.

At my bi-monthly webinars I often take you to the long term charts to keep a perspective on our present position. Since the 2009 low we have had a relatively straightforward trip as we sail towards our Christmas date with 2000+ in the S&P index. Like most markets this broad index has stayed largely within its Danielcode trading channel and I have shown you the following chart on many occasions. Remember that the DC trading channels are dynamic, that is they grow with the market, subject to those concrete rules which make these channels impressive guides rather than an unrestrained regression channel that is all encompassing and therefore of no empiric value to our steadfast seafarer. Thus the time of the end is a moving target now located near 2200 and many months away. But more of that another time. At present it is enough to know that our 6 day timing chart runs within its long term trading channel (Blue lines) and within its more recent Black line channel which starts at 10/07/2011. In the whole five plus years of this mighty bull market (where are those folks who continued to insist that this historic rally was a secular bear market correction?) you can see that the index dropped to its 2 standard deviation support just once in its entire trip and has never before breached its 1 SD upper Blue boundary. Until now. And that extreme price action is a signal to take stock of where we are and to quantify the immediate hazards.

To get our first "fix", a nautical expression referring to "fixing" our yacht's position on the chart and not what most of you assumed, we use exactly the same technique outlined earlier and used every day by the inshore flotilla of a famous cocked hat man Admiral Horatio Nelson, hero of the battles of Cape St Vincent, the Nile and finally Trafalgar close against the reefs of Cape Trafalgar, North of the Straits of Gibraltar where he died for his country.

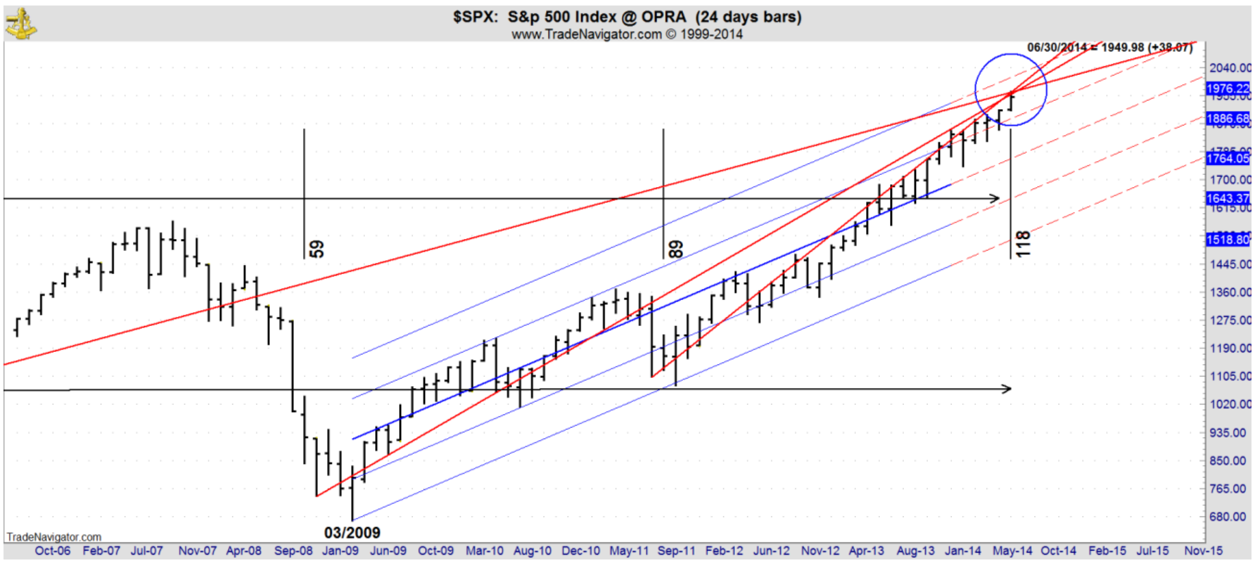
Like Nelson's ship masters navigating through perilous seas, we too have our headlands and features from which to take our bearings. These are the key features of trading charts where the high before the high and its inverse cousin the low before the low are vital landmarks for traders, as are the high after the high and the low after the low which are prime targets to start the Danielcode time cycles that control all markets. To plot the course of markets yourselves you can see all in my two "Master Class" articles published by Financial Sense and archived there and under the Articles tab at www.thedanielcode.com . These are a treatise of the war we constantly wage to read the clues that advanced charting affords though we never face the perils that Nelson and his men perforce attended every day. For true yachties divorced from the mendacity of electronic chart plotters and their like, dead reckoning is a combination of time on distance plus course. For us traders, the DC channels define course but time is most often the harbinger of change, and thus whilst we always watch the compass, it behooves us mightily to watch the clock. We can plot time on the "Y" axis of charts just as price is plotted on the "X" axis. That is linear time and the simplest and most common method of marking market time.

A more nuanced facilitation of the ever ticking clock is to rate time as a function of another indicator. Just as two bearings from known landmarks will give us an approximate position for our yacht, so known landmarks of time and price create high probability inflection points that are manna for close observers. To marry the disparate elements of time and price we use a special type of bearing called an Angle. But these are no ordinary angle. Like the Danielcode trading channels they have fixed rules that limit their availability of deployment but just as our offshore bearings impart precious information these special angles called the 4th Degree or for Danielcode afficionados the 4th Seal, impart similar nuances. A standard application of 4th Seal theory has a qualified angle showing important and likely vigorous support or resistance coinciding with a major DC time cycle. Of special import to 4th Seal forecasting is the attainment of both a known DC price level *and* a known DC time cycle. In these infrequent instances we say that Time and Price are Squared. This is not my original expression but was coined by the legendary WD Gann, beloved by past generations of brokers for his amazing expositions of how marketing was the unique money maker of the brokering business. Today we take it for granted that marketing is the driving force to perceptions of prowess, but it was not always so and Gann was the trailblazer for many of today's brokers. For Gann, Time and Price Squared occurred at intersections with his 1X1, 3X1 and other support and resistance points, drawn like the 4th Seal as angles on charts. Gann created these angles from fixed ratios ie one period of time and one allocation of price created a plotting point for the 1X1 line; then two periods of time and two allocations of price and so on. Although Gann's angles did nothing observable to markets other than an occasional happenstance allowing still more marketing and promotion of the great man, the concept was interesting enough for me to adopt the phrase for the 4th Seal, which unlike Gann's fixed points is a phenomenon created by the market itself. So without more ado, let me take you there with initially our 6 day timing chart:



The red line is a 4th Degree angle that complies with the construct rules for this superb forecaster of market turns. We have price abutting the angle with a degree of precision but we do not have the time cycles that would herald a major market turn. The Black time cycles are the remnants of the dominant DC 59 cycle that called the 2007 top and the 2009 low with precision, then continued to forecast the 05/2010 top and the 10/2011 low which tested the 2SD downside support from the major DC trading channel. Its next extension is the start of August and thankfully for bulls the dreaded 1st hop on the 59 cycle that signified the 2007 crash cycle is nowhere in evidence. But we do have the expiration of both the 44 cycle which is Gold's ruler and the 37 cycle. That is enough to say that S&P is at Time and Price Squared on this 12 day chart but odds favour a minor correction although I opine that when you see what a minor correction actually means, most of you will be yelling "abandon ship" as you leap over the side into the murky depths!

Turn now to the 24 day timing chart, and at last you see the cocked hat. And this one where 3 separate and valid 4th Seal lines intersect gives us a powerful "fix". The longest of the 4th Seal lines starts way back in 03/2003 and reaches through time to create this confluence of 4S angles.



And we have "Time" with the extension of our dominant 59 time cycle marking the current bar. Again, this is not the 1st hop crash cycle so you can remain sanguine of the immediate probabilities which on this evidence suggest a correction rather than a terminal course change. But a mere correction implies a withdrawal to the median of our long term trading channel, and that folks is near 1800 or about 12% below current price. For Futures traders pullbacks are a joy as the downside trade pays exactly the same as the long trade. And usually happens much faster. More like a tack than a gybe, or in layman's terms bow about rather than the slower stern about the favored method of changing course in Nelson's great behemoths which without significant

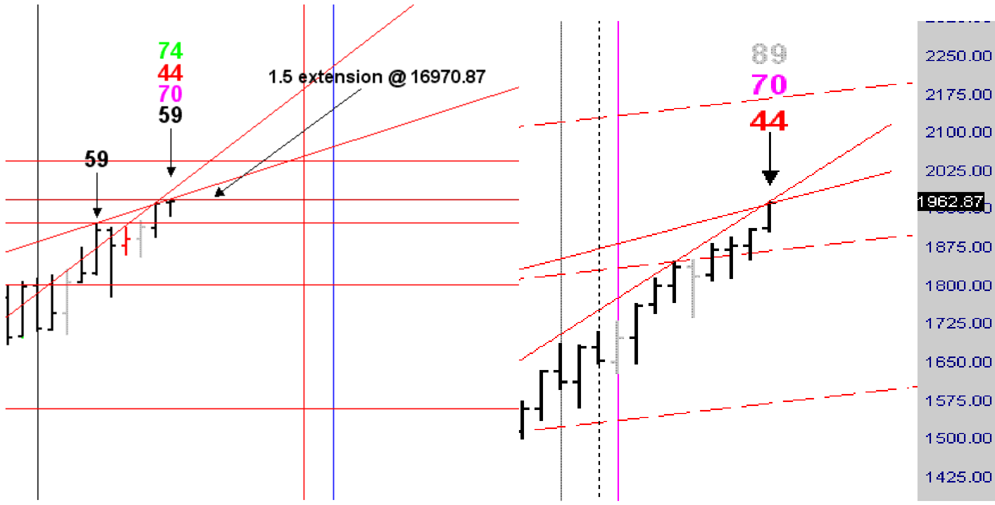
fore and aft sails were a cumbersome and dangerous vessel for tacking, particularly in the light airs which preceded the Battle of Trafalgar. Slow and risky is not a winning option for warriors or traders alike.

This famous painting is titled The Battle of Trafalgar: Nelson's Victory and H.M.S. Téméraire hotly engaging the French Rédoubtable, the huge Spanish four-decker Santisima Trinidad ahead of them off Victory's port bow by DGM Gardner. This wonderfully dramatic portrayal elicits a real feel for the ferocity of Lord Nelson's final engagement. At the time Napoleon ever a landsman other than when escaping captivity by the British, deemed the loss of his and the Spanish fleets a mere setback, but with all of the panache for which the French are famous (and tight control of the Paris media) he announced the outcome of the battle as a glorious victory!! Some things never change.

To wrap up the probabilities that the tight cocked hat implies, let me add this week's summary on the S&P and on the Dow Jones Industrial Average from the 4th Seal tab at my website:

> "Update alert 6/10 10.37 GMT: The DJIA is now at its next major extension on the 24 day chart with a bunch of major cycles all expiring in one big cluster. This is a perfect setup for a major turn in this market. Look how the DJIA recognized the 1.445 extension. This is a message that this market is tracking this DC sequence. The next one is the 1.5 extension and we just touched it. You are warned. (added 24 day DJIA chart to this update)
>
> From last week : We have topped on schedule so far and the turn down is now evident. We now had a decline of more than 3 days which increases the odds of this being a higher degree top with more downside to come. The DC 4th seal resistance recognition right on a significant DC time cycle cluster and the DC price mathematics all affirm the view of a higher degree top in place. Be aware that because of the absence of any correction on the last three 4th seal inflections equities are now at risk of a sudden and swift decline. Up days are considered corrective and from now on we make sure we are short in the elected sell signals. On the chart side you see the 6 and 24 day S&P and the 24 day DJIA. Get ready for some action folks.
>
> We issue another major alert on equities this week. The setup is now even more mature than last week. The S&P is now at precise 4th seal resistance and in the DC week where major time cycles expire on both the 6 day and 24 day chart. This market is very ripe for a turn so any DC sell signal should be taken with both hands. The DJIA recognized the 1.5 extension last week, had a 3 day correction and went back up, recognized the 1.5 extension at 16970.87 again and closed on the black line of the correcting swing. The DJIA is also at major 4th seal resistance on the 24 day chart with major time cycles expiring on the 6 and 24 day chart. All ingredients are in place for a higher degree top here. I'm still warning to prepare for some action. We had sell signals on Thursday and Friday of last week so if they get elected make sure you're in the market. I still believe we are on the verge of a larger correction in equities. The picture side contains 6 and 24 day charts for both the S&P and DOW."

DJIA on left below and S&P from our 4th Seal page:



I invite you to visit us at www.thedanielcode.com where there are numerous articles and webinars on markets and on trading. Whatever your level of expertise or interest in trading there is something new and exciting to learn.

And by all means feel free to wear your cocked hat. For new traders our T.03 signals are the place to start. Email me at jneedham@thedanielcode.com for more information or contact Terry at support@thedanielcode.com to secure your free trial of any of our products. From 4th Seal analysis in S&P, Gold and much else through our short term FractZen trading by signals-direct-to-your-cell, all things are possible.

"The folly of Interpreters has been, to foretell times and things, by this Prophecy, as if God designed to make them Prophets. The design of God was much otherwise. He gave this and the Prophecies of the Old Testaments, not to gratify men's curiosities by enabling them to foreknow things, but that after they were fulfilled they might be interpreted by the event; and his own Providence, not the Interpreters, be then manifested thereby to the world. For the event of things predicted many ages before, will then be a convincing argument that the world is governed by providence." Sir Isaac Newton, the Father of Modern Science. Observations upon the Prophecies of Daniel, published 1733.

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> The fox knows many things, but the hedgehog knows one big thing. A Hedgehog Concept is not a goal, intention or strategy to be the best. It is an understanding of what you can be best at. The distinction is absolutely crucial. ~ Isaiah Berlin, The Hedgehog and the Fox