

The Danton ShockWave
Principle®

The Dynamics of Price Revealed

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Introduction

The purpose of this booklet is to introduce a trading principle, namely the **Danton ShockWave Principle**, which identifies favorable trading opportunities in the market. It is simple, easy to learn, and can be extremely profitable if correctly implemented. **Danton ShockWave** analysis provides you with the information needed to make informed trading decisions in a quantitative and systematic manner, and teaches you how to identify high probability turning points (price objectives) on monthly, weekly, daily and intra-day time frames. Over the course of this booklet, you will be shown how to construct **Danton ShockWave** targets. How to implement this technique into your current trading plan, and how the to enter low risk trading opportunities. It cannot however; promise that you'll amass a fortune or that it will turn you into a successful trader. Because in reality, success depends on more than just market knowledge, it is a test of your physiological limitations (i.e., strengths, attitude, weaknesses, aggressiveness, discipline, and so on).

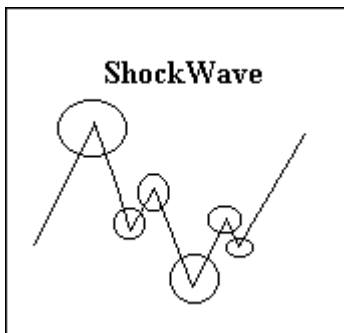
Danton ShockWave Concept

Sometime between 1813 and 1855 the Danish philosopher Kirkegaard manifested his genius and taught that "in life, sudden decisions, leaps or jerks can lead to progress." Progress it was!

In the broadest sense, Kirkegaard's statement has universal implications, though it has one simple conclusion. It suggests that the outcome of an event is a reaction to psychological input. A revolutionary hypothesis considering it implies our inner thoughts are a form of energy. As a matter of fact, it would be interesting research to get at the root of such thought, unfortunately for the scope of this book, it's impractical. For practical purposes, we will just assume that energy exists in everything we know and that price fluctuations are a statistical representation of energy flow in the markets. A rational assumption if we believe market movement is a reflection of human behavior. Consider how far we've come in the theory of price dynamics before you disregard this assumption as irrational. If you can accept that as fact, then it's possible to assume that energy can be measured, and that this measured energy can be used to predict possible distribution patterns in the future. We will prove throughout **Danton ShockWave** analysis that energy is in fact predictable and its structure unfolds in a geometric fashion.

Traders will always be divided into two camps. There are those who say, "If you don't use fundamentals, you'll never understand the markets." They look at the world as supply and demand, and what lies beyond that is terrifying - it's outside their realm. Technical analyst on the other hand, despises fundamentals, viewing it as an assault on their sacred modeling techniques. Well, I have witnessed a decade of market behavior - from bull markets to bear markets, from congestion to expansion, and from options to spreads, and throughout it all I have only witnessed one methodology that works consistently, technical analysis. It exists in a thousand different forms, from a thousand different calculations, almost all are fascinating, but ultimately they are one in the same. They all rely on past price information or pattern recognition to forecast future events.

Luckily, I realized the importance of technical analysis some time ago. My research took me to academic libraries, to bookstores, and to private libraries. I read journals, novels, biographies, textbooks,



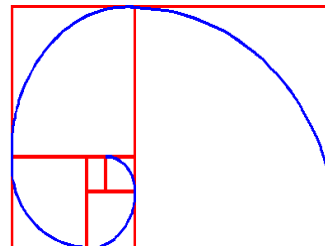
magazines, and studied trading plans for years without success. Yet, somewhere along the way, by chance, I began to visualize and conceptualize what is now the **Danton ShockWave Principle**. I have to admit, when I first told friends and fellow traders I couldn't wait to see their reaction. It's been four years since then and I'm still glowing with the novelty of sharing the idea, once again. In spite of potential skepticism!

In theory, a **Danton ShockWave** is a manifestation of the fear-greed mechanism found in sociological behavior. However, it goes one step further in its basic assumption of price behavior, in that, it measures initial price distribution at reversal points to project subsequent wave movement. In essence, measuring the dynamic input (energy) of all market participants at a particular moment in time to forecast future price movement within a given time period.

From a fundamental standpoint, each shock represents a change in sentiment regarding future price direction. A tactical coup in a sense, as a power struggle evolves between buyers and sellers buying what they perceive to be cheap and selling what they believe to be expensive. It is here, the moment a reversal occurs, that we discover what the market participants' beliefs are regarding future price direction. A large shock (energy reaction) indicates strength in the subsequent move, as participants liquidate old positions and enter new positions in the direction of the reversal forcing a trend change. Likewise, a small shock indicates weakness in the subsequent move, as market participants take profits or add positions with the original trend, implying that the primary trend is still intact and a minor correction has occurred. Picture a shock as producing successive waves in a pool of water following the impact of a rock. A small rock dissipates little energy therefore; the subsequent waves (price movement) are smaller and somewhat transitory in their progression. A large rock on the other hand, disperses a lot of energy, as such; the waves will be larger and more noticeable as they progress outward. In short, the larger the rock (crowd consensus) the bigger the reaction. Hence the further energy (wave) will travel.

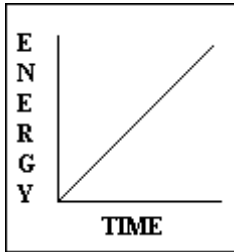
This single aspect of price behavior forms the basis of the *Danton ShockWave Principle*. The energy manifested during a price reversal is the underlying key to the subsequent price action, and ultimately is the determining factor as to where price will correct or consolidate in the future. As a matter of fact, the characteristics of price behavior following a shock statistically support the dynamic input of all market participants, considering it is a direct reflection of the fear/greed mechanism inherent in each and every of us. Because of this physiological impact, it is highly unlikely that price will ever move unimpeded over any distance, since short-term traders would be buying into corrections and selling into rallies. This analytical framework ultimately gives you three advantages: the ability to identify overextended markets, the ability to anticipate where a reversal/congestion area will occur, and greater trading confidence by eliminating some doubt.

The idea of growth following a shock is best illustrated by a pattern that has fascinated mathematicians and artists for centuries, and more recently technical analyst -- the logarithmic spiral. The growth patterns associated with the logarithmic spiral are unique for many reasons. It resembles an infinite expanding universe with no boundaries inward or outward. And it fundamentally mimics those patterns found in natural phenomena such as snail shells, galaxies, art, flower petals, elephant tusks, pine cones, tree leaves, and our own physical makeup and feelings. In essence, it represents the dynamic nature of all things we know to exist. Why then, shouldn't it pervade into the world of man (and the market's) considering man's existence an integral part of the puzzle. We cannot reject the notion that a correlation exists, but to what extent?



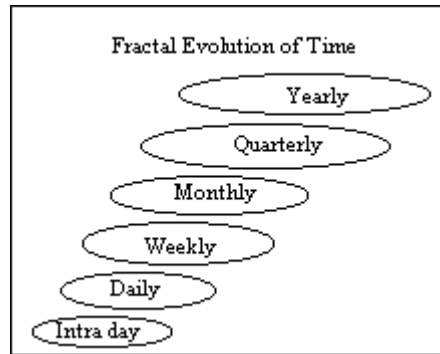
Lets assume the universe is a dynamic enigma for all practical purposes and its energy will eventually permeate into all living things at some point in time (generating the energy that forms the basis for growth patterns to ensue). Let further assume that this "energy" is a derivative of gravitational effects caused by certain planetary relationships. Couldn't one surmise that this energy will have an effect on the static makeup of the atmosphere. More importantly, couldn't one speculate that this energy would have an effect our philosophical makeup at a particular moment in time or at a future date? Certainly, you've heard police across the nation citing the "Full Moon" phenomenon as the culprit for an increase in violent crime statistics. Is this just a denial of poor performance on their part or a true planetary coincidence? Well the evidence suggests the later. There are numerous examples throughout history to support the "planetary effect on mankind" hypothesis. Some of the better-known incidences known to effect our philosophical makeup and biological clocks are Sunspots, Moon phases, and planetary aliments. Admitting the relationship is hypothetical at best but rational nonetheless. If life has form, then we must not reject the notion that human behavior, which is apart of that existence, be exempt. Nor should we discount the residual impact on our emotions. If a relationship does exist, we must assume this energy is the catalyst for future growth patterns as nothing else in nature suggests that life should be exempt or unsymmetrical. By extension, we must accept the possibility that a rippling effect would extend into the markets.

The question then, is to what degree this effect pervades man's world. If you believe (like I do) that time limits (energy) growth, then each segment of time will be effected with a different degree of severity.



The rationale, when man reacts, he reacts in a manner he feels appropriate to a perceived threat. Of course, this reaction time will be different for each of us, due to innate differences such as physiological makeup and physical limitations. Therefore, if physiological and physical input limits growth then surely time itself is the real limiting factor. Theoretically, without artificial constraints energy would expand into infinity, in the real world however, time is created; therefore, we must work within its environment. As such, each time segment within the hierarchy of time will produce its own distinct vibration (shock) within its measured environment; and the growth patterns (energy dissipation)

following this vibration will be limited by the same environment. The result is self-evident; an intra-day shock will produce less energy than one on a higher time segment. Hypothetically implying an intra day shock will never encompass the day's entire trading range. A rather convoluted thought in today's markets. If the market's were truly a free and open place of exchange the events (news, report, etc) impact would be factored into the market in an extremely violent move, inevitably finding equilibrium. Unfortunately, in today's market's, the exchanges governing body's have imposed trading limits to limit the inherent risk of trading. A curb that ultimately constricts the market's ability to evolve unencumbered. With trading limits, we are forced to expand our time horizons accordingly should a limit move occur.



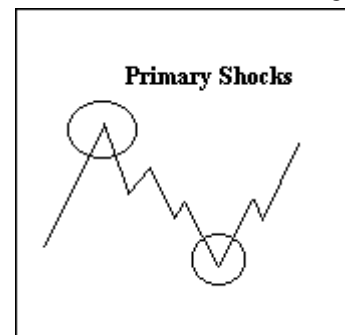
If we explore this relationship using fractal geometry, which is one of the disciplines of nonlinear dynamics, we can see an interesting similarity of principles. Which by definition simply states, "a shape will maintain the same jagged form no matter how much it is magnified." Fittingly implying that the process of evolution occurs at all levels from the universe as a whole to the quantum level. Supporting our assumption that market vibrations and pattern growth on lower time segments should mirror those of higher time segments apart from their scale. Theoretically indicating there is no preferred time segment to trade. They all contain the same basic patterns and look the same apart from risk. Time is just a measure of change, as such each segment is labeled according to segment under study: intra-day, daily, weekly, monthly, quarterly, yearly, etc. This is the framework in which *Danton ShockWave* analysis has evolved.

Danton ShockWave Classification

The most important consideration in *Danton ShockWave* analysis is deciding where to start each projection since projected targets will be used to take profit, initiate new positions, close open positions, scalp around, spread against and enter options positions. In truth, the process couldn't be any simpler considering each projection begins at some reversal point on a chart. From this adaptation, a primary and secondary shock is determined by where it develops on a chart. To illustrate I have gotten a little ahead of myself, but it's necessary you understand, however, that from these two distinct shocks a Level 1 target zone and Level 2 target zone will be created.

Primary Shock

Primary shocks form the cornerstone of *Danton ShockWave* analysis. In fact, it is the primary pattern used to identify the overall structure of the market, and to project support/resistance levels in the subsequent price move (wave). Hence the reference primary. They are simple to locate because they always occur at an extreme reversal point on a chart. To illustrate, examine the process of *Danton ShockWave* construction.



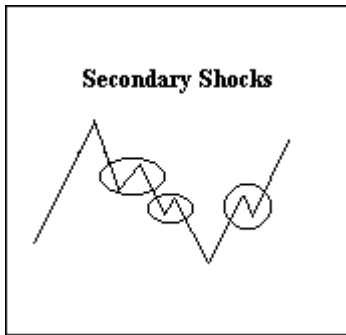
Step 1: Identify a major reversal area in which to project a primary *Danton ShockWave*. In the example to the right, it is the KRB high (see the red arrow on the high pointing down).

Step 2: From the *Danton ShockWave* primary projection a target zone is created as horizontal lines across the chart in various formats and colors. Notice the support zone at the bottom of the chart.

Step 3: Use the predefined entry rules to take a trade against the trend. For now, familiarize yourself with the simplicity of the process.



Chart 1: Primary Shock



Secondary Shocks

Although primary and secondary shocks consist of the same pattern formations they are markedly different patterns distinguished by their whereabouts on a chart. Primary shocks form at significant price reversal points, whilst secondary shocks occur as minor reversals in trending markets. Therefore, they play a gratuitous role in *Danton ShockWave* analysis. Hence, the name secondary shocks. While they react and develop from the same fundamental influences effecting primary shocks, their projections are used primarily to support primary target levels by further defining the target zone.

However, they are still used to identify the wave target immediately following their formation. To illustrate, refer to Chart 2.

Step 1: Identify the starting point for the *Danton ShockWave* secondary projection. In this example to the right, we are using a retracement level just off the lows (green arrow pointing up).

Step 2: From the *Danton ShockWave* secondary projection a target zone is created as horizontal lines across the chart in various formats and colors. In this example two a Level 1 and Level 2 target zone appear. We will discuss their differences later.

Step 3: Entering a trade is relatively simple by using one of the pre-defined patterns listed in the section - Entry Signals.

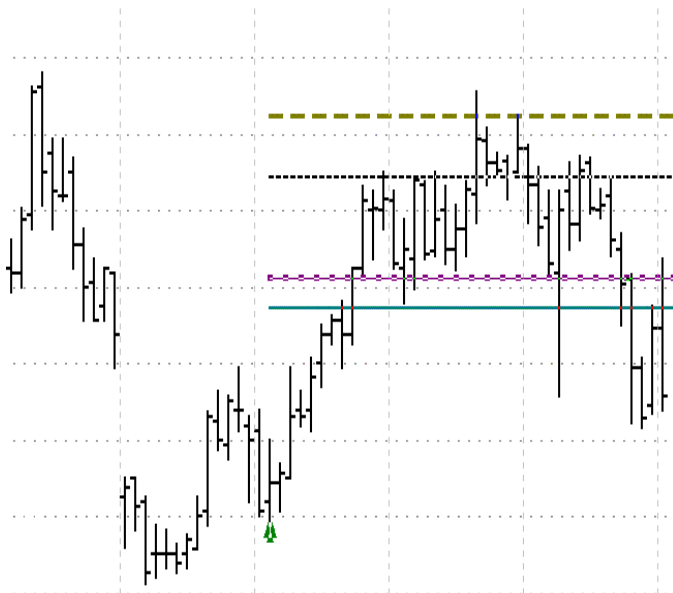


Chart 2: Secondary Shock

Combining Shocks

One of the easiest and most effective ways to reduce exposure is to combine the target zones of a primary and secondary shock. The process creates a price "cluster" that can be used to narrow our entry point. The intent is to reduce exposure. See Chart 3.

Step 1: Combine primary and secondary shocks to create a price cluster.

Step 2: Use the predefined entry patterns shown below to enter a position.

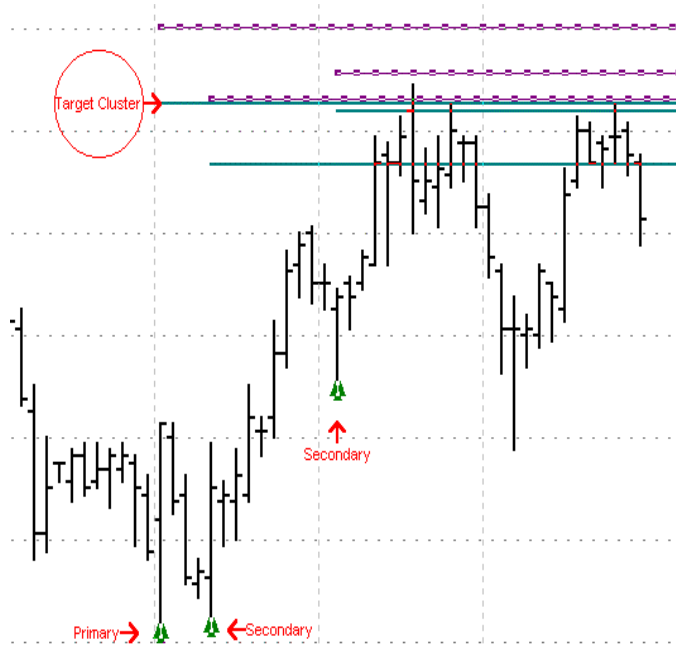
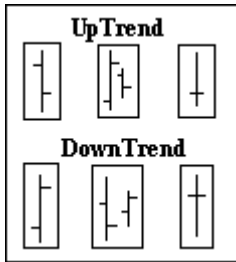


Chart 3: Creating Target Clusters

The Entry Signals

As a rule, we use the market's natural symmetry to identify weakness. By watching the emergence of momentum patterns we have the ability to predict when the market is going to turn. In turn, we use this weakness as an opportunity to enter a position in the early stages of a trend reversal. The patterns used are by definition key-reversal patterns (KRB). A pattern best described as single price bar whose peak (high/low) is not surpassed in price by either the bar preceding or following its formation and a close that's against the trend. Technically a close that is equal in value with the open still qualifies as a valid KRB pattern formation. The diagram above depicts some of the more common patterns we use. The patterns on the left are obviously textbook reversal patterns. The patterns in the middle occur after a strong move, and the second bar is used as a signal bar. The patterns to the right indicate direction of the impending move. The Chart to the right (Chart 5) demonstrates the frequency at which this pattern occurs in the markets. Note: not all KRB patterns are marked on the chart. Please, take a moment and familiarize yourself with the KRB pattern formations.

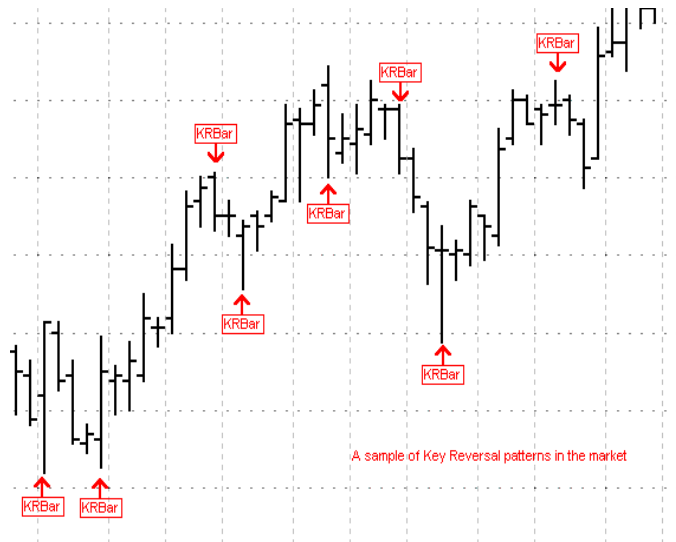


Chart 4: Key Reversal Patterns

Level 1 Target Zone

When the market is trending, and I mean that loosely, expect price to reverse or at least congest at Level 1 target zone. As noted earlier, price will never move infinitely over any distance, unless something significant is suddenly factored into the market. A good example, usually around seven o'clock or nine o'clock in the Bond market as Government numbers are released, expect the first level to fail and the second to hold. This occurs in part, because the floor is buying and selling into the number to take advantage of the aberration.

Chart 6: Illustrates the entry process with two examples.

- 1) From the low of A, we project our *Danton ShockWave* target up to create a resistance Level 1 target zone. As price penetrates **the outer line of the Level 1 target zone** we look to take a short position when price closes below **the inner line of the Level 1 target zone**. This occurs on the following bar (see **Sell Signal**). Evidence of weakening upside momentum is given with an inside KRB pattern formation.
- 2) From the high of B, we project our Danton ShockWave target down to create a support Level 1. As price penetrates **the outer line of the Level 1 target zone** we look to take a long position when price closes above **the inner line of the Level 1 target zone**. This occurs on the fourth bar of penetration (see **Buy Signal**). Evidence of weakening downside momentum is given with a classic KRB pattern formation.

Level 2 Target Zone

To get good idea of what a Level 2 target zone represents picture a rubber band on the verge of breaking and you have it. This level represents the maximum distance any wave should travel without reversing or at the very least, going into congestion. In fact, if price hasn't had any significant corrections while trading up to this point there's a 75% chance that it will once it reaches this point. Because the market is said to be "overextended from it mean." Knowing this, we are in the position to maximize our profits. For aggressive traders increase your position size accordingly.

Chart 7: On this chart, we will examine a sell signal at a Level 2 target zone. Note: the two black horizontal lines represent a Level 1 target zone projected from the primary shock at the lows. Notice how the target of the secondary shock offers a better entry price. Therefore, we base our decisions accordingly. The first sign of an extended market is when price blows through the Level 1 target zone projected from the Secondary shock. As such, we are on alert for a reversal at the Level 2 target zone. When price penetrates **the outer line of Level 2 target zone**, we look to take action. Our entry signal is given five bars after the penetration (see **Sell signal**) with a KRB pattern formation and a close below the inner line of the Level 2 target zone.

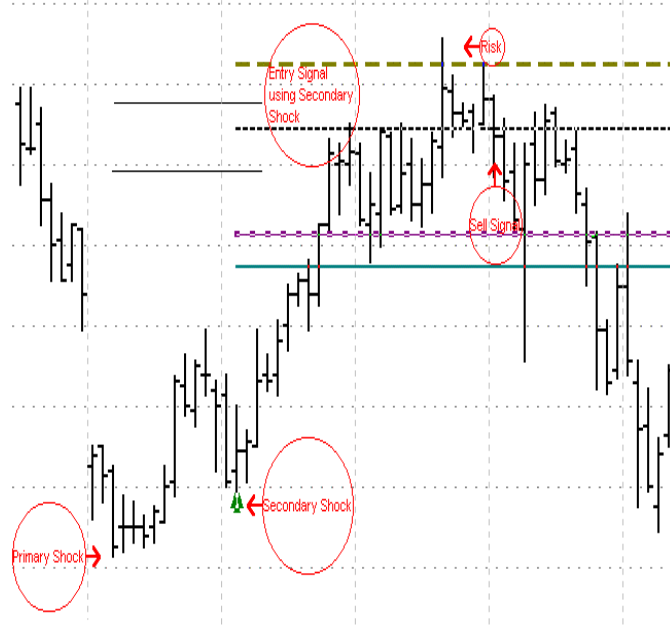


Chart 7: Level 2 Target Zones

Danton ShockWave and the hierarchy of time

One of the biggest oversights in technical analysis is not realizing that an interaction between time segments exist. Like it or not, each shock induced fluctuation is dependent or reliant on the period surrounding it, considering the lower time segment shocks provide the foundation needed for higher time period growth, and the higher time segments dictate direction. Consequently, your expectations of price movement should reflect the segment under study. At any rate, our analysis thus far has been limited to shock developments on one time segment. By doing so, we have ignored many low risk trading opportunities that exist by using a lower time segment for entry.

The primary reason we use multiple time segments in trading is to reduce risk and entering a position at a better price than we could have on the higher time segment. Of course, once the higher time segments confirms the lower we have an opportunity to add to our position. The following chart demonstrates the significance of multiple period interactions.

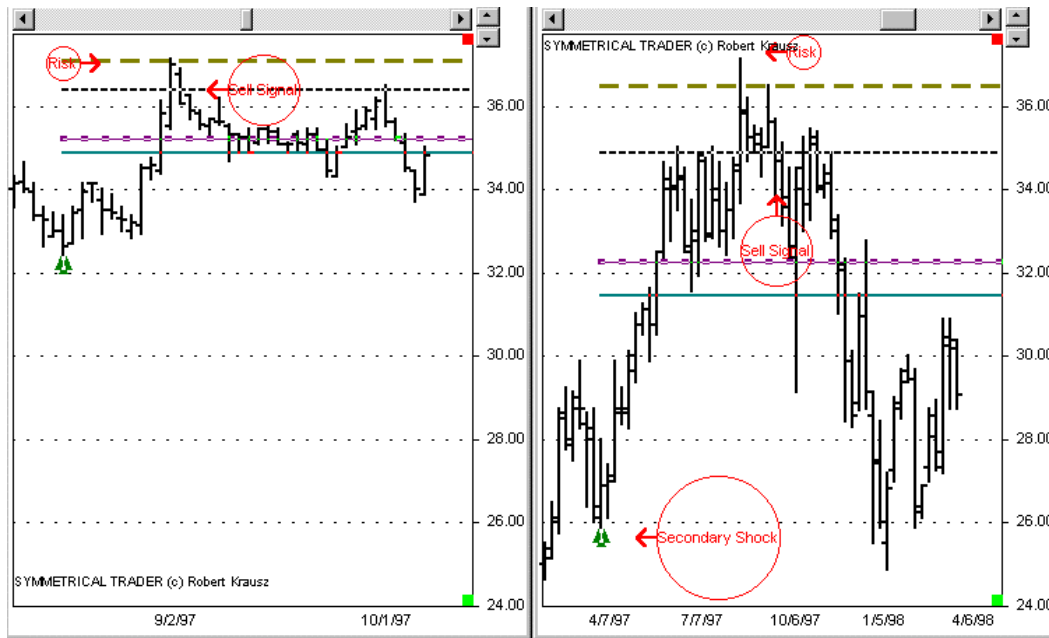


Chart 8: Interaction in the Hierarchy of Time (lower time segment is on the left)

Chart 8: The above chart illustrates the interaction between time segments. The window on the left represents the lower time segment and the one on the right the higher. To better illustrate the principle the price scales have been "linked" together.

- 1) Notice that price has penetrated the **outer line of the Level 2 target zone** on the higher time segment chart to the right. At this point, we want to use a lower time segment to maximize our entry point.
- 2) Using a primary shock on the lower time segment we project a **Level 2 target zone** that is in close proximity to **the Level 2 target zone** on the higher time segment. In fact, it is slightly higher offering a better entry price. As price penetrates (barely) the **outer line of the Level 2 target zone** on the lower time segment we wait for a sign of weakness and then take action. This occurs on the following bar when price closes below the inner line of the Level 2 target zone with a classic KRB pattern formation (see **Sell Signal**). Risk a new high (see **Risk**).
- 3) To maximize profits I would add contracts when the higher time segment confirms weakness. See **Sell Signal** on chart to the right.

There are many combinations that you can use between time segments to maximize profits. Personally, when I roll a lower time segment trade into a higher time segment I manage my risk accordingly. Hence, I use the higher time segments vibrations to take action.

Conclusion

Successful trading requires commitment, discipline, money management and of course, a system or methodology. Although this last point is debatable as many traders make a good living in the markets without using any form of technical analysis at all. Commitment and discipline are essential, and given their importance deserve to be listed separately. Discipline is the ability to “get back in the saddle” after experiencing a series of losses. Our inherent weakness’ and the roller coaster nature of the markets make this extremely difficult to at times. The ability to “step up to the plate and swing the bat day in and day out indifferent to the outcome,” reinforces your subconscious and ultimately builds the confidence needed for success; provided your trading plan is valid. To a certain degree, determination and commitment are similar, and realized by thoroughly back-testing a methodology over a significant time segment that encompasses all market conditions. This seemingly mundane task is often the difference between success and failure in trading. Those unwilling to put forth the effort will face many obstacles in the future.

Think of the market as a pool of endless opportunity!