Lesson 1: Price and Liquidity

Word Bank

Price
Price Action (PA)
Algorithms (Algo's)
Time
Market Structure (MS)
Buyside Liquidity (BSL)
Sellside Liquidity (SSL)
Swing High (SH)
Swing Low (SL)
Adjacent SH/SL
Higher Time Frame (HTF)

Price

Price is the $ amount that a buyer or seller are willing to transact at. When you record price through a range, and record each transaction over time, you create **Price Action** (**PA). PA** is what we watch for when we anticipate the price being delivered to liquidity.

Algorithms (Algo's)

Algo's are responsible for more than 75% of the volume in developed markets. Their role is to deliver price from one point to another over a period of time based on some preset factors. Our job is to simply understand what the Algo's are trying to do and follow suit.

Time

Once you begin to understand **PA**, you will now need to couple it with time to give it meaning. **PA** without time is useless. You won't understand why price is moving the way it is, nor have a grasp of the **Market Structure MS**. For example, waking up without knowing what time it is means nothing. You need to know what time it is for you to understand what to expect next.

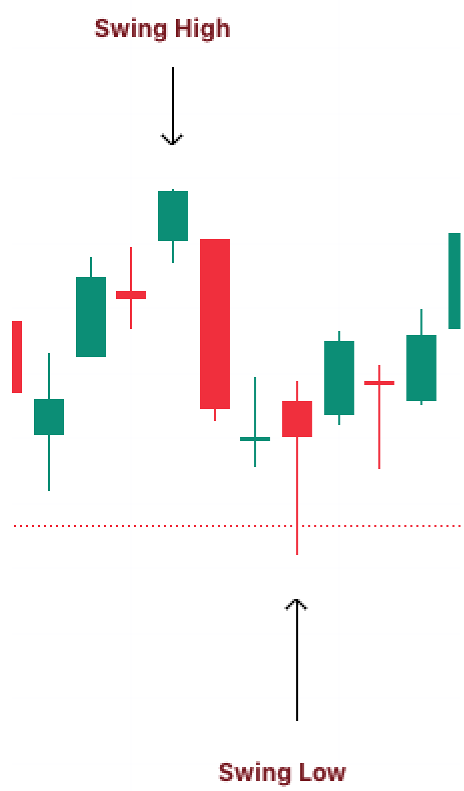
Liquidity: Buyside and Sellside

When you hear these terms, people like to make them synonymous with support and resistance. Don't make this mistake. Although they may align at times, these are two distinct concepts. Liquidity refers to the area on a chart where price has made a **SH** or **SL**. These are points are where traders are positioned either long or short, with stop losses just below or above.

[Liquidity can be found under any candle but for our purposes, we're targeting swing highs or swing lows]

A SH is formed when you have 3 candles creating a point, with the middle candle being the highest.

A SL is formed when you have 3 candles creating a point, with the middle candle being the lowest.



Now where on this chart does liquidity reside? For the SH, it resides above the high of the middle candle. For the SL, it resides below the low of the middle candle. These are known as **Buyside Liquidity (BSL)** and **Sellside Liquidity (SSL).**

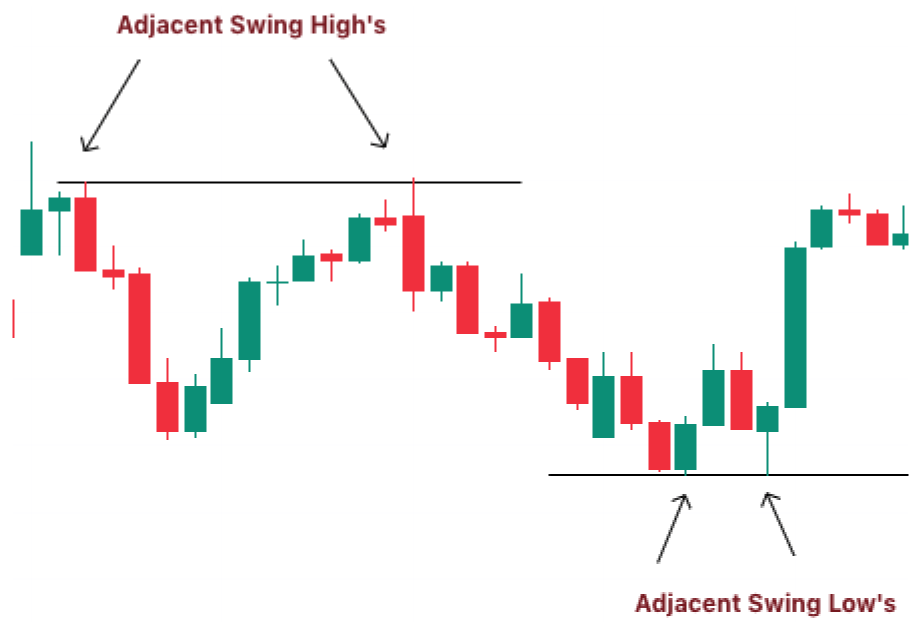
- **BSL** refers to the area where stop losses are placed for traders who are positioned short. When these areas are broken, short traders are forced to cover their positions, forcing them to BUY back the shares they sold short. Thus, anyone who is looking to sell their shares to someone will find buyers here → hence the name **BSL.**

[if you find this confusing, think where are the shorts and their stops]

- **SSL** refers to the area where stop losses are placed for traders who are positioned long. When these areas are broken, long traders are forced to cover their positions, forcing them to **SELL** the shares they had bought. Thus, anyone who is looking to buy shares from someone will find sellers here → hence the name **SSL.**

[if you find this confusing, think were are the longs and their stops]

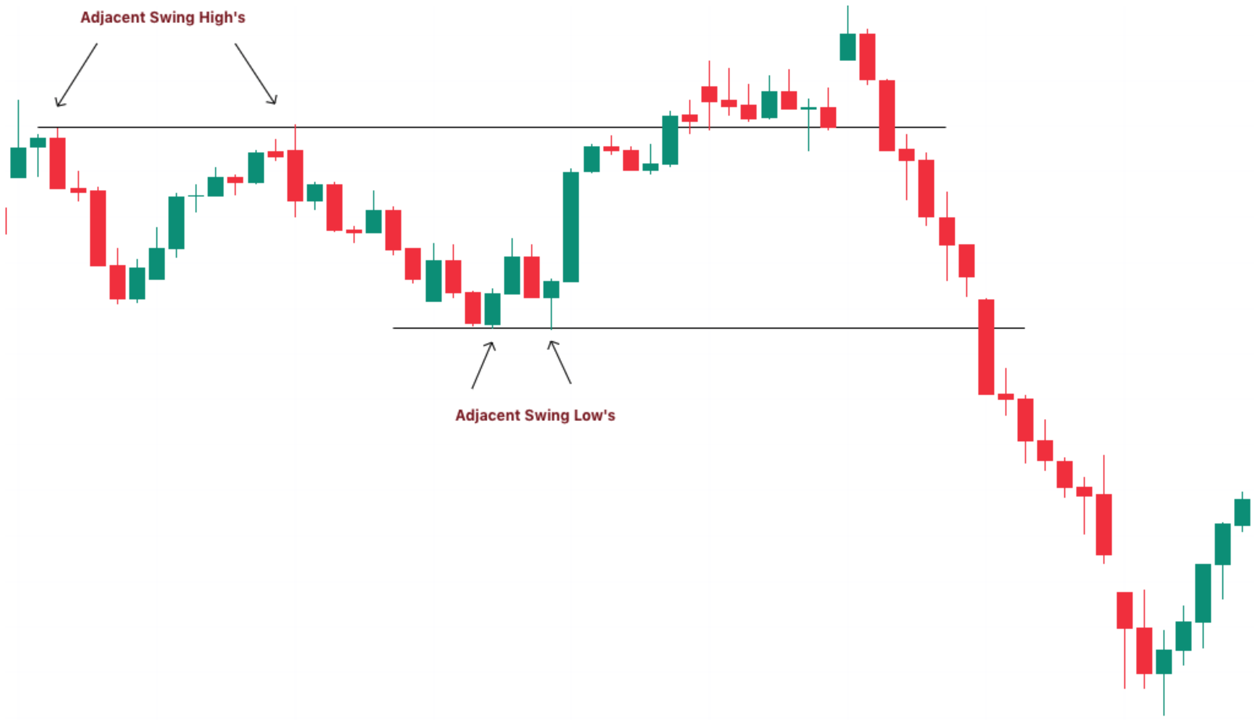
- When you have **adjacent** SH or SL formations, we refer to these as equal highs or equal lows. These create the illusion of ‘support and resistance’ when in fact, these are areas of BS and SS liquidity!



#1 Adjacent Swing High's and Adjacent Swing Low's. These areas are building up BS and SS Liquidity.

You will find BSL and SSL on all time-frames of a chart. The larger time-frame, the more significant that level becomes. So when looking for ares of liquidity, start with a **Higher Time Frame (HTF)** and work your way down into the hourly, 15min, 5min, 3 to 1min time-frames. Then couple this framework with adjacent SH and SL areas to really find significant areas of liquidity!

So lets break the notion of 'Support and Resistance' while were at it. When price is moving along with a trend, these areas of liquidity become important as they allow traders to scale in and out of positions. For example, the picture above shows adjacent high's and low's. If the trend is down, you would want to short by selling at a higher price and cover by buying at a lower price. The picture above is that of a downtrend. In typical support and resistance fashion, we would expect 'resistance' to hold and 'support' to break. Lets take a look at what happens.



#2 Continued from above: Price breaks 'resistance' and moves into BS Liquidity as smart money will accumulate shorts above where retail recognizes as resistance. Their target will be SS Liquidity where retail recognizes as support.

What we see happen is resistance breaks to the upside. Therefore, we are probably reversing the downtrend. WRONG! This is a classic move to trap retail traders into believing the trend is reversing by breaking what we see as retail resistance. What is actually happening, is price is moving into something called a premium (more on this later), where smart money will look to position themselves short. How? When the 'resistance' breaks, it triggers the stop losses of weak retail and eager traders trying to short the price move up. These stop losses will force these traders to buy back their shares at higher prices from smart money, who will be selling these shares short!

What happens next? Once this BSL is purged, there will be a lack of buyers interested at higher prices. Algo's will begin to deliver price back down towards SSL, or what we see as retail 'support'. Once this level breaks, stop losses will force weak and eager traders (who were long) to sell their shares at lower prices. Smart money that shorted above, will be able to buy back and cover their short position from the shares of traders who were long!

Now that is just one example of how liquidity works. Once you begin to see these areas of liquidity, your understanding of price and how it delivers changes drastically. One final note, significant areas of liquidity will allow larger volume transactions to occur without changing the price all too much. If price begins to change quickly, chances are, the area of liquidity isn't significant.

How Does Price Move?

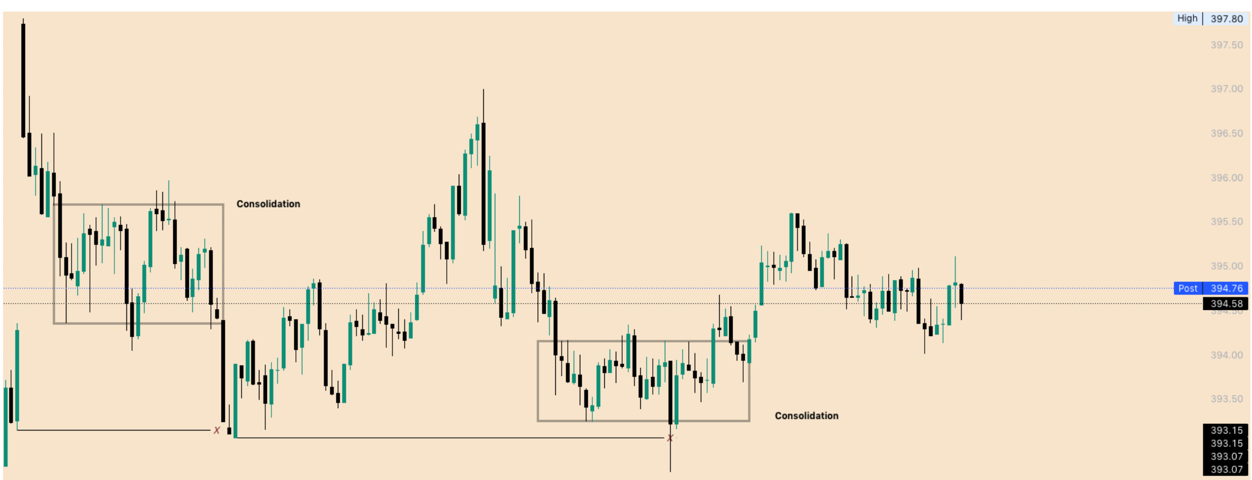
Price action (on any time frame) will repeat the same process over and over again. Trading should be boring and predictable, not exciting and unknown. By being predictable, you should be able to recognize a setup that allows you to execute a trade with the probability of the reward being significantly higher than the risk (more on this later).

What does predictable look like?

We need to look for how price behaves at any given moment. So lets define price using these 4 ideas:

Consolidation	Expansion
Retracement	Reversal

Consolidation: occurs before price makes a move in any direction and after price has made an expansion towards a target(s) OR once it has hit the target(s) → BSL or SSL

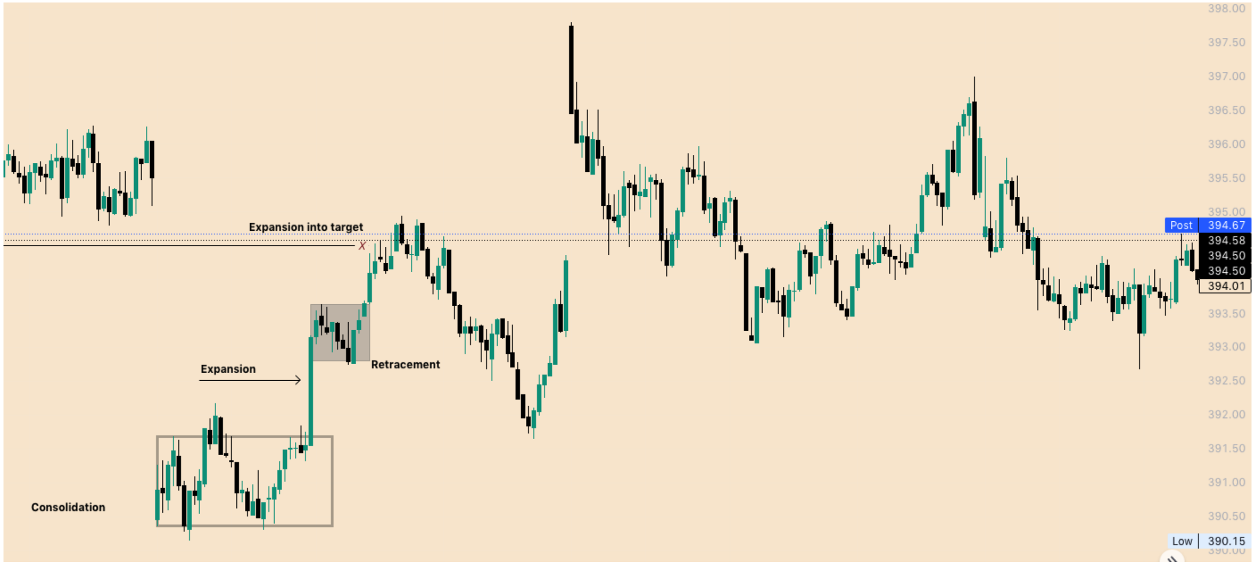


1. Expansion move down → consolidate → expansion move down into target
2. Expansion move down → consolidate → target hits → reversal attempt (fails to expand down)

Expansion: Occurs after consolidation. Price will fake a move in one direction and then expand in the desired direction towards the target(s).

1. Consolidation → **Expansion** → Retracement → **Expansion**

Retracement: This is known as the pullback. It occurs once price has made a directional move and needs to pullback before continuing the trend. It is much different from a reversal.



1. Price retraces back into the expansion phase before moving up again towards the target. If you notice, while it does this, it is taking out SSL from eager longs trying to get into the move.

Reversal: Once price has reached it's target(s), it will either look to continue in the direction of the trend, or aggressively break the trend and start a new one. The start of the new trend with confirmation is called a reversal.

Price will move in one of these 4 ways → and this will repeat over and over again on ALL time frames. They key is to be able to read price action and be on the right side of the move, which leads us into the next lesson.

Combining Price and Liquidity

Lets say that you want to go long on a trade. Where and when do you buy? On a breakout? A retest of a breakout? When resistance turns into support? What if you could buy into the trend before it starts or when it is pulling back to go even higher? No patterns needed, no indicators needed. Don’t believe me? You’ll have to move onto the next lesson so you don’t miss out!