Lesson 3: Market Structure Shifts (intro)

When referring to market structure (MS), Higher Time Frame (HTF) charts will give you a better representation and understanding of the trend.

A market structure shift (mss) occurs when price changes sentiment and breaks through previous price structures, to invalidate the current trend and start a new one. In order to understand when this occurs, lets review some basic ideas of market structure.

Swing High and Low Points

These are areas where liquidity is created. Retail traders will use these as ‘support’ and ‘resistance’ points. Seasoned traders will use them to enter or exit positions based on the trend. These points will (on any timeframe) have a minimum of 3 candles, with the middle candle creating the point. Trends usually create a pattern that are easy spot. Uptrends create higher highs and higher lows, whereas downtrends create lower highs and lower lows.

Imbalances

An imbalance occurs when there is an energetic move in a a particular direction that signals the start of an expansion - this is known as **displacement**. You usually see these types of explosive moves at expansions out consolidation, reversal expansions, or during trends. For our model, it is technically defined as the change of state in delivery of price, and is usually coupled with OB’s. These imbalances can create **Fair Value Gaps (FVG’s)*.** These are the imbalances where we want to start or add to a position to join the trend.

Market Structure Shifts (mss)

An mss tells us price has changed its state of delivery. This happens when displacement creates an imbalance and takes out a previous market structure that supported the trend. For example, here is an uptrend where a swing low gets taken out with an imbalance:

All this tells you is that the current trend has terminated, it doesn't necessarily mean we will reverse immediately. It all depends on the context of the market and what the narrative is for price. Recall price goes from expansion → target liquidity → consolidation/expansion OR reversal. We would want to have a reason to believe the current break in market structure is valid (more on this later in future lessons).

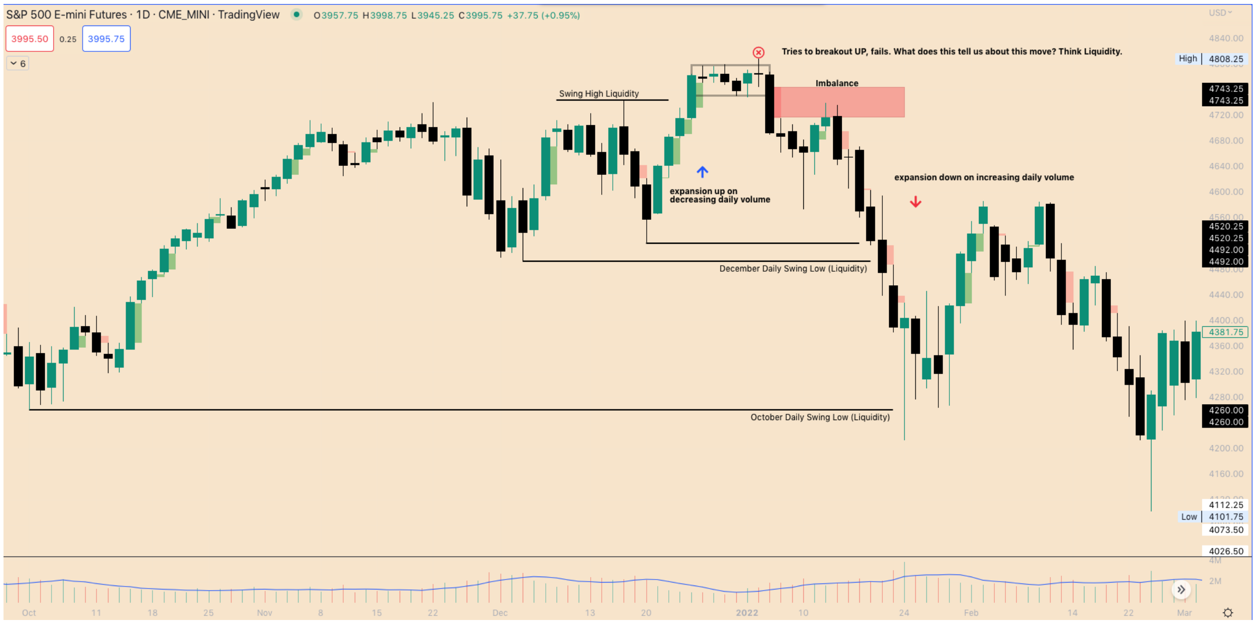
Here's what a break in market structure for a downtrend looks like:

This downtrend has been broken by displacement UP, creating an imbalance and signalling the current trend has been terminated. Now you would use the market structure created by price action to determine what price will do next (consolidate → then continue OR reverse)

MSS With Charts

Lets start to combine the things we have learned so far. Here's a list of what you'll need to know to follow along: liquidity, swing high and swing low points, displacements, imbalances, market structure and market structure shifts.

Chart 1: The Short Setup



Here's a daily chart of $ES we've used before in the previous lesson. We know that there is an attempt to break up out of the consolidation that fails. By default, price should seek sellside liquidity. This is found under daily candle lows or at swing lows! So now we have targets for algos to deliver price to.

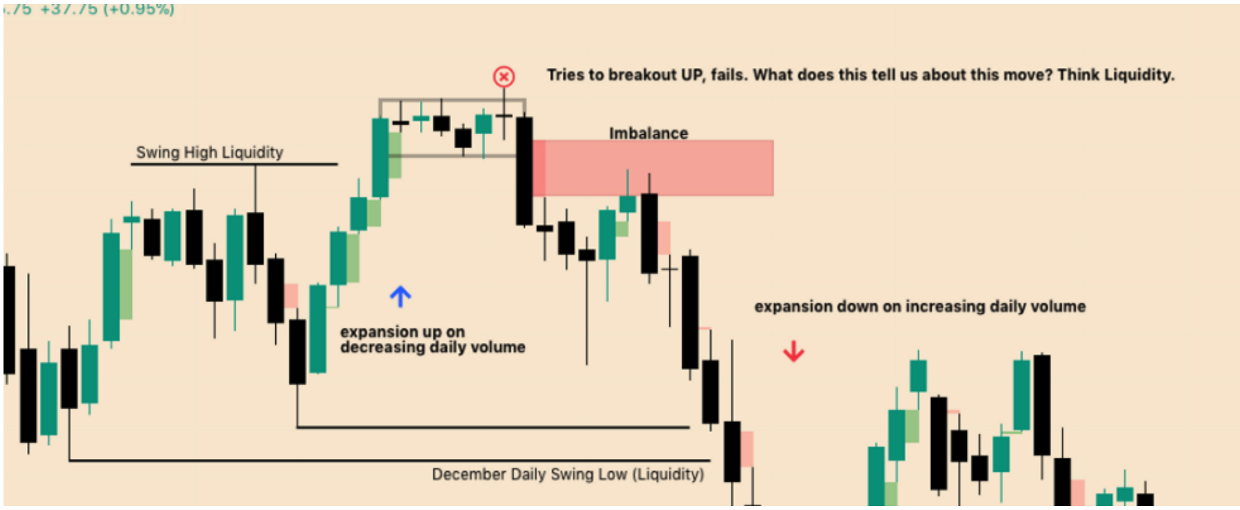
Recap of this move from the last lesson…

So where does the algo attack first? Buyside liquidity! But notice how price fails to push up and we end up with a candle where the close and open are basically the same → aka doji. This is signalling that not much interest for buyers was found above the recent swing high, our buyside liquidity area.

So what happens next?

The subsequent day ends up being a big down day. If you look to the left of the picture, all of the up-closed candles in green have sellside liquidity at their lows! So if you are short from the previous day (doji in consolidation) where do you want to cover your position? Where sellside liquidity exists (→ ask yourself, where do longs have their stop losses?). So each of these daily lows are now targets to the downside. With what we just learnt above, the daily candle displaces to the downside with energy, from the consolidation, taking out the recent swing low and creating an imbalance AND forming our mss!

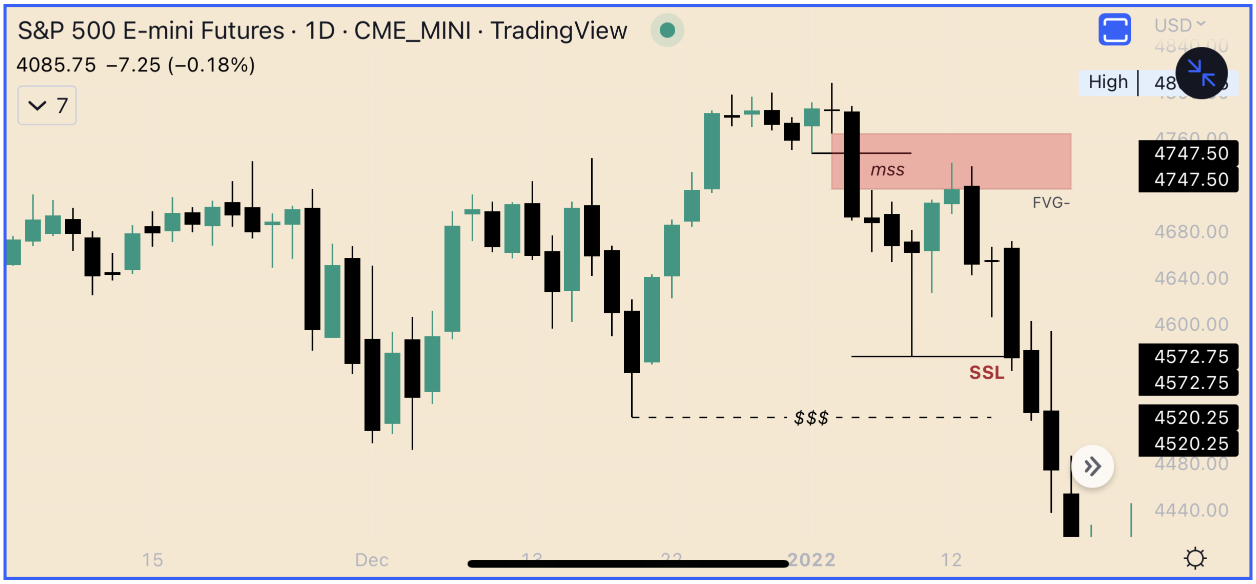
(Realized I didn't label the mss, it's the bottom of the consolidation box where the swing low is!)



Painting The Picture

Now lets piece together what has happened with price, and where it wants to go.

mss = market structure shift
OB- = order block
SSL = sellside liquidity
$$$ = our target



Price displaces to the downside, creating both a mss and an imbalance. Note, the mss line is also our bearish order block line (OB-). The day after our displacement down, another doji candle forms. These three candles create an imbalance which is referred to as a **Fair Value Gap (FVG).** This area is outlined with the red box -FVG (- indicates down). Recall, this area is an incomplete auction, where orders are waiting to be filled inside this -FVG. This is where we would want to add with the new downtrend that is forming.

Combining what we learnt from the last lesson and this one, an imbalance becomes important when it takes out a previous market structure! For our case, we're looking at imbalances to take out swing highs or swing lows! This move works even better when we come out of consolidation just after a taking out liquidity!

Chart 2: The Long Setup

Here is an example of a downtrend being broken to the upside.

$$$ = SSL and new yearly lows

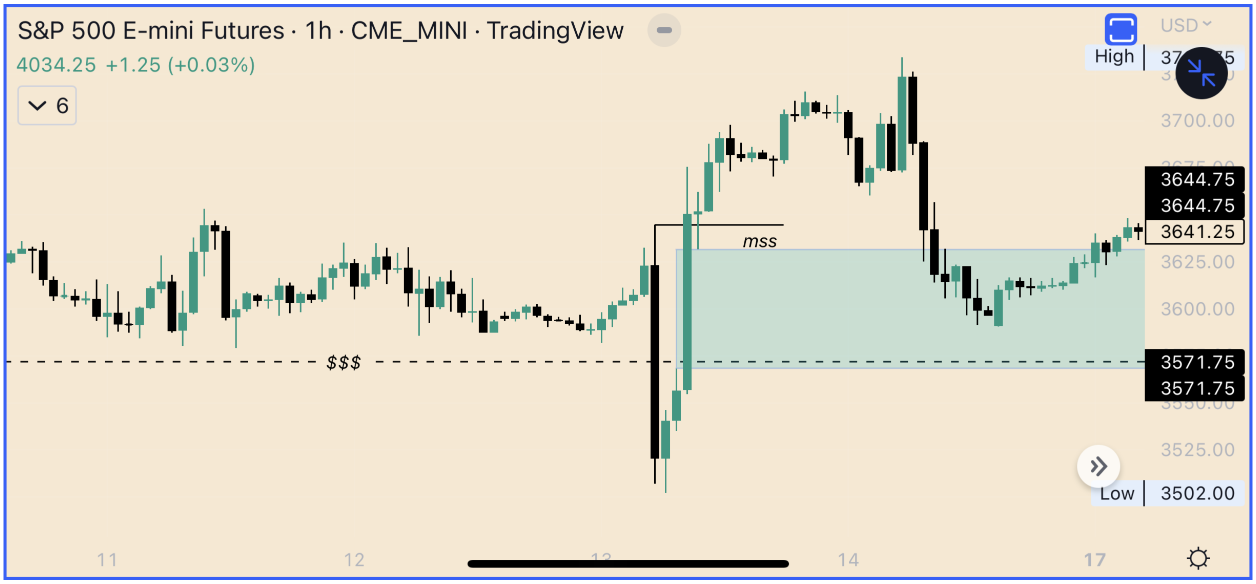
mss = market structure shift UP

FVG = our imbalance to add long

The Narrative

Price takes our our major sellside liquidity level and aggressively reverses back UP!

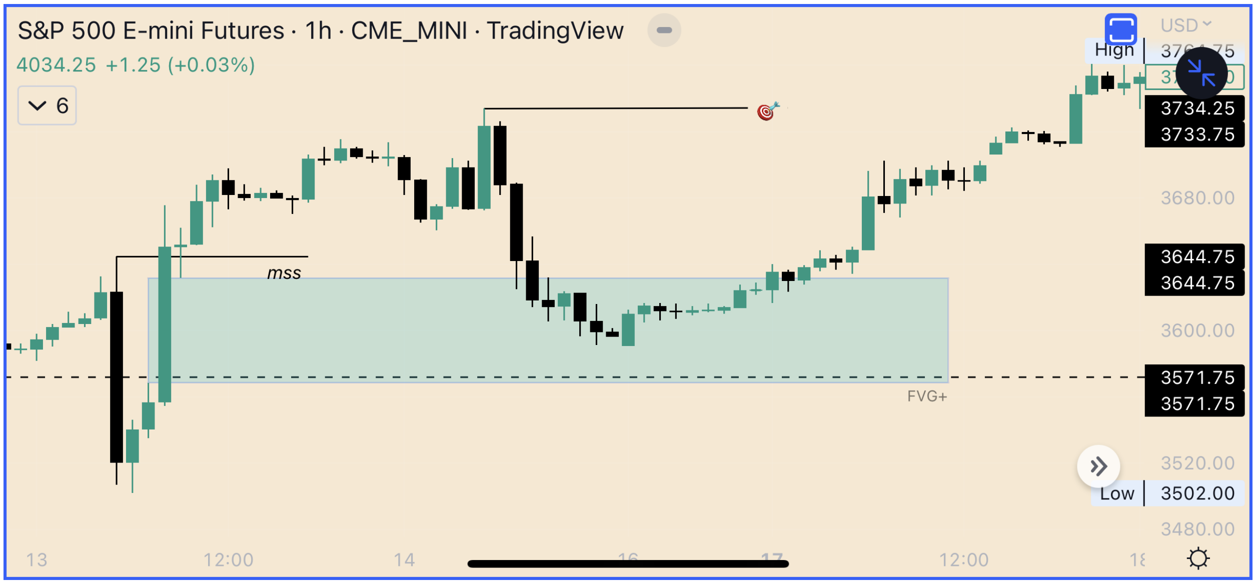
The aggressive move back up takes out a recent swing high. This is our setup for mss long! The trend down has terminated for now. We are at key yearly levels, indicating this is an area where price can switch direction (after taking out major sellside liquidity). Our future targets then would be swing highs. So what are we looking for?



We are looking for a shift in market structure (labelled with mss). The aggressive move back up takes out the swing high and continues up before falling back down. This is our mss. Now we want to look for our FVG to add in.

The blue box denotes the FVG of interest. Why? The giant downcandle before our move up is called what again? An order block! This candle represents buyers loading up before the big move up. We expect this candle to hold for our bullish bias. The fact that our FVG and order block overlap gives this setup even more confluence to add long.

This happens because there was an attempt to displace down, but ended up with a bigger displacement back up! Don't get greedy shorting at all time lows unless there are major sellside liquidity targets near by!



We want price to enter this FVG and begin to move out of it. The more aggressive the move back out, the stronger the push up will be towards the target.

After running our major sellside liquidity target, and having a mss UP, our eyes should revert to recent swing highs as targets for long adds. Why? This is where we have liquidity of recent shorts. Smart money who are positioned long will be looking to take profits where there is obvious liquidity!

Recall stops go under the order block swing low and we can begin to move them up as price displaces away from our adds (more on this in future lessons).

Review

A mss occurs when a recent swing high or swing low gets taken out AFTER taking out key liquidity! We look for an obvious break of these points with displacement. This displacement creates an imbalance which is called a FVG. This is the area where we want to look to add and join the trend of the mss!

As the new trend hits targets, we want our market structure to keep supporting the trend and forming even more market structure shifts!

Consolidate → expansion → consolidate → expansion → and so on…

Each expansion should create a mss!

**Fair Value Gaps: A brief intro into our next discussion*

A FVG is an important element of market structure. When it is involved in creating a mss, this signals the possible start of a new trend for the delivery of price. Using the long example above, when price re-enters into the FVG (the imbalance responsible for the mss), our bias would be to find the entry to go long. Why? The mss was to the upside after taking out yearly sellside liquidity and thus, price retracement into the FVG should be treated as an opportunity to go long!