

Reading the Market

readthemarket.com

Here's what we look for on the charts:

General: HTF. Know where price is coming from and going to, and the PA past and present in all the TFs, from the Monthly down.

Specific: At the zones you want to trade, look to

Past. study the zone in all TFs, down to M1 ask yourself

Where were the decisions made? Clean S/D? Mark these lines. No clean S/D? – compressed zone.

Did price really shoot away from the zone, or did it cp away?

Did the zone itself react at the right place? Look beyond the zone further into the past. See what it reacted to. Was there a better S/D nearby that price wants to visit? This explains many fakeouts.

Present.

Approach.

How is price returning to the zone?

Where's the nearest flag in the TF you want to trade? This is your tg1 in this TF. Flags in the LTFs? What does PA tell you?

Has price tested the last flag on approach? (good sign)

Has price compressed into the zone in this TF or LTFs? (good sign)

Is there big news on the way? Has there just been big news?

Reaction

In LTF, does price react violently to the first decision point? Does it quickly engulf the nearest S/D? (good sign)

Does price simply CP away? Maybe it wants to go to the next decision point

If the first decision point breaks, watch the signs on approach to the next, and, of course, reaction.

Chew this over for now. Apply it to your chart history. Apply it to as many failed setups as successful ones. Millions of them if possible! Capture and file them all. This will help make it instinctive.

Order Flow

When we look at the market watch window in our trading platform we'll see each instrument's symbols and next to it two different prices, one is bid and another is ask or offer. These prices are offered to us through an online broker who is not just a broker but also a dealer.

"Dealers and brokers help people trade. Dealers trade with their clients when their clients want to trade. The prices at which a dealer will buy and sell are the dealer's bid and ask prices. After they trade with their clients, dealers then try to trade out at a profit by selling what they have bought or by buying back what they have sold. In effect, clients pay dealers to take their trading problems. The dealers then try to solve them at a profit. Dealers profit by buying low and selling high. Successful dealers must be excellent traders.

Brokers are agents who arrange trades for their clients. They help their clients find traders who are willing to trade with them. They profit by charging commissions."

Dealers are market makers and also known as market specialists, so they play a big role as a market participant beside other pro money, understand how they play and you'll play with them. Now we understand that online brokers act as brokers and dealers.

Back to the market watch window, the ask/offer shows the lowest offer price which the market is willing to sell at and for you to buy, the bid shows the highest bid price which the market is willing to buy at and for you to sell.

As you know there are two types of orders "market orders" and "limit orders", in the image below is an example of an order book, aka; DOM, Price Ladder, Level II. Bear in mind this is only for explanation purposes; in the currency and metals market there is no depth of market, it only applies to centralized markets such as futures, equities and commodities. Of course banks and dealers have their own order books but it only show their clients' orders. Back to the image, the offers column for sell limit orders, bids column for buy limit orders and in middle is the price. I've taken eur/usd prices as an example, the orders are standard lots/contracts (i.e. 200K = 2 lots and 1M = 10 lots), the two prices highlighted in yellow represent the Bid/Ask prices which we see on our market watch (spread in this example is unrealistic and only to make it easier).

Bids	Price	Offers
	1.3050	1M
	1.3040	100K
	1.3030	
	1.3020	500K
	1.3010	200K
400K	1.3000	
	1.2990	
200K	1.2980	
300K	1.2970	
	1.2960	
500K	1.2950	

Anyone entering the market with market orders will be buying at 1.3010 and selling at 1.300. Now let's say you place a buy market orders of 500K (5 lots) what will happen?! Your orders will be executed at the lowest offer consuming the 200K at 1.3010 and a 300K out of 500K at 1.3020 and this price will be the new lowest offer with 200K limit orders, so as offers were consumed price moved up to 1.3020

Another scenario; you are placing a sell market orders of 1 million (10 lots) what is the outcome?! Your orders will be executed at the highest bid consuming the 400K at 1.3000, the 200K at 1.2980, the 300K at 1.2970 and a 100K out of 500K at 1.2950 and this will be the new highest bid with 400K limit orders, so as bids were consumed price moved down to 1.2950

This is how price moves up or down by consuming orders, and bigger orders generate buying/selling pressure (momentum) pushing price in its direction consuming smaller orders until it stops (slows down /stalls) at a new price where there are opposite bigger orders placed.

One last thing, the stop loss pending orders are considered as limit orders and when it's executed it adds pressure in the opposite direction.

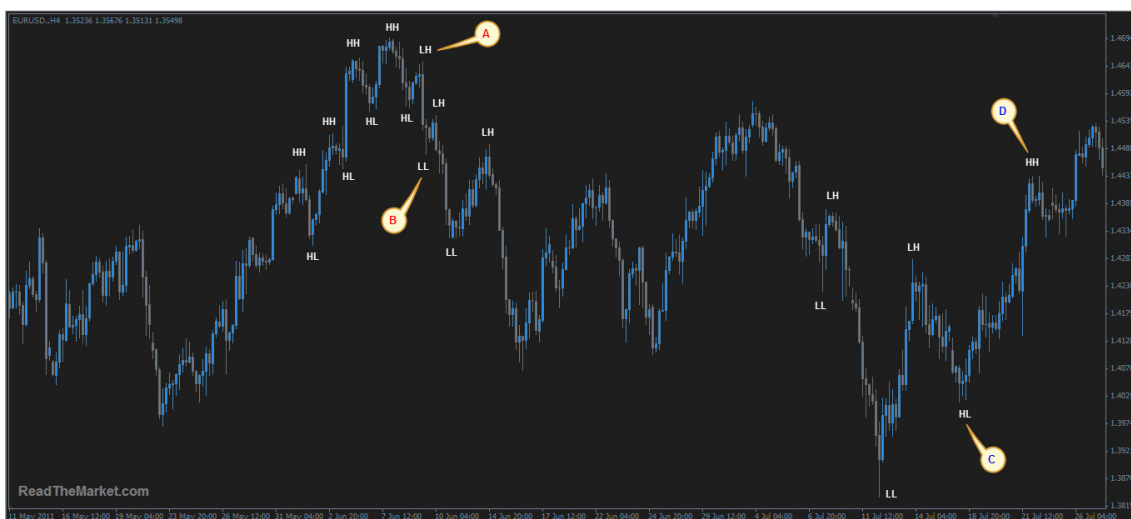
Trend Direction / Highs and Lows

The Highs and Lows or Peaks and Valleys are the core of technical analysis. To draw an uptrend line you'll need to locate rising valleys or higher lows to draw the trend line below, and to draw a down trend line you'll need to locate falling peaks or lower highs to draw the trend line above (please refer to [Technical Analysis](#) and [Trendlines](#) in Confluence for more). However, there is a big difference between the Trend Direction and a Trend Line, a confusion that most of new traders suffer from.

So long as price keeps creating Higher Highs (HH) and Higher Lows (HL) then it's trending up, and when it keeps creating Lower Lows (LL) and Lower Highs (LH) then it's trending down. So when does the price change direction from uptrend to down trend and vice versa?

In the image below, on the left side we can see price has changed direction from an upward movement to down ward movement and this could be identified in four stages, starting with the last created HH, followed by a HL then creation of a new LH and this is a key stage [A] and finally a LL [B] and this confirms a change in direction. Notice the new LH has formed the right shoulder of a Head & Shoulders pattern.

On the right side of the chart price has changed direction from a down ward movement to upward movement and it happened in four stages as well, starting with last created LL, followed by a LH then a creation of a new HL and this is a key stage [C] and finally a HH [D] and this confirms a change in direction.

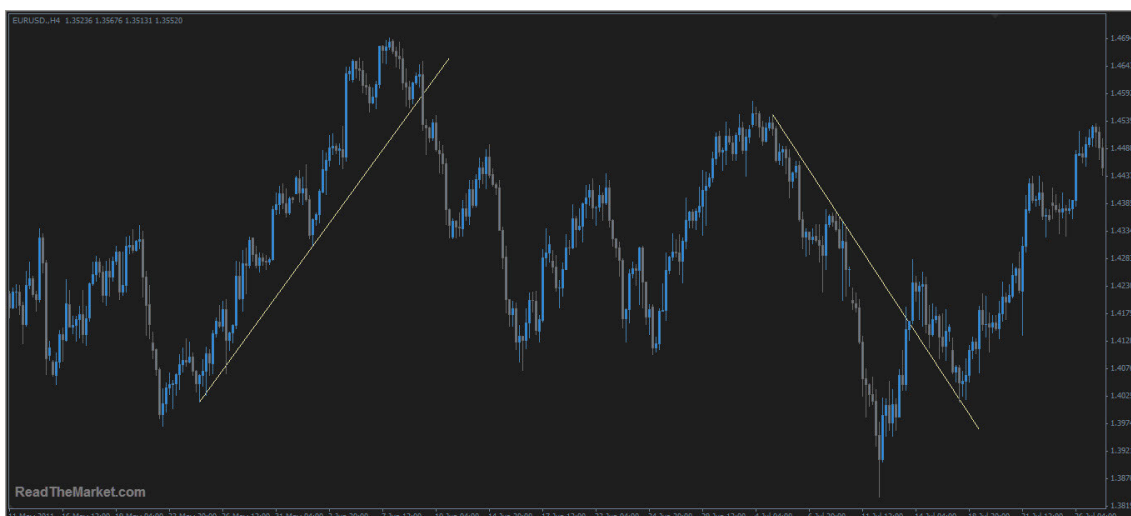


Conclusion:

- A change from an uptrend to down trend happens in 4 steps (HH > HL > LH > LL).
- A change from a down trend to an uptrend happens in 4 steps (LL > LH > HL > HH).

Now on the same chart we've drawn the trend lines (TL) to observe the breakouts. On the left side we have an up TL which price has broken right after the new LH then dropped for a long distance.

On the right side we have a down **TL** which price has broken after the last **LL**, failed to go higher and returned to retest it, creating the new **HL** then rallied up.



Conclusion:

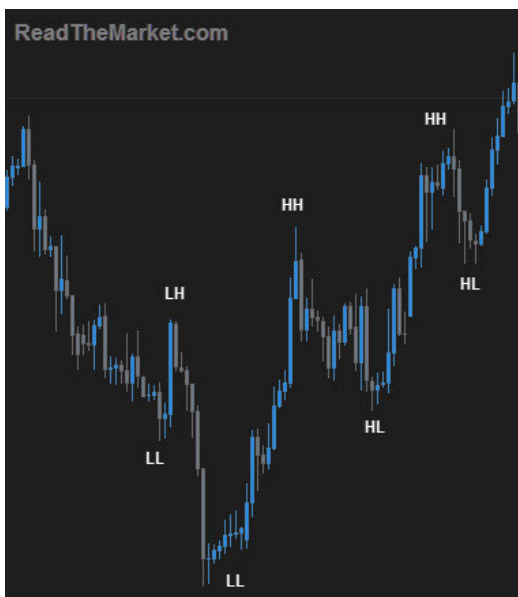
- In an uptrend a break of **TL** after a **LH** is most probably followed by a drop in price where a break of **TL** after a **HH** requires a retest of broken **TL** and creation of a **LH**.
- In a down trend a break of **TL** after a **HL** is most probably followed by a rally where a break of **TL** after a **LL** requires a retest of broken **TL** and creation of a **HL**.

There is a different order of stages for the change of direction with an earlier key stage, and the complete stages create a pattern that is known as Quasimodo (QM).

In this image price has changed direction from an upward movement to down ward movement in four stages, starting with the last created **HL** followed by a **HH**, then creation of a new **LL** and this is the key stage, followed by a new **LH** and this confirms a change in direction.



In this image price has changed direction from a down ward movement to an upward movement in four stages, starting with the last created **LH** followed by a **LL**, then creation of a new **HH** and this is the key stage, followed by a new **HL** and this confirms a change in direction.



Conclusion:

- A change from an uptrend to down trend in a QM happens in 4 steps (**HL** > **HH** > **LL** > **LH**).
- A change from a down trend to an uptrend in a QM happens in 4 steps (**LH** > **LL** > **HH** > **HL**).

One last note; please bear in mind that identifying peaks and valleys could vary from a trader to another but if you face any confusion then its recommended to change your candle or bar chart to line chart where you can easily identify the peaks and valleys.

What is Supply/Demand trading?

K.I.S.S.

Every possible market, whether it is a financial market or not, is being moved by the ongoing supply and demand that is present in this particular market. Supply (sellers) represents the quantity of products that is available in the market and Demand (buyers) represents the quantity of products that is wanted in the market. When there is more demand than supply, the price of any product is going to rise (demand exceeds supply) and when there is more supply than demand (supply exceeds demand), the price of the product is going to drop.

Selling at Supply or Buying at Demand offers you the best price possible. So why would you want to pay more for a product, service or currency if you can get it at a better and cheaper price?

The Edge

In trading, knowing where a Supply/Demand level is, is knowing and understanding what type of trader or trading account is on the other side of your trade.

Knowing that there are two different types of market participant: The novice trader that belongs to the 95% and the Banks, institutions and Big Money that belongs to the 5%...

A small retail trader isn't able to move price in the market, only institutions and banks are able to do so. The good news is that it is possible to trade in the right direction and to follow the Big Money by simply buying at Demand and Selling at Supply. In other words it is up to you to choose which market participants you want to join!

How to recognize a novice trader?

Most of the retail traders aren't trading profitably, it is a fact. They are losing because they buy after a period of buying and they sell after a period of selling while institutions/banks are doing just the opposite!

Identifying a Supply and Demand Level/Zone

Finding a good Supply or Demand level on a price chart isn't that difficult. The first thing we want to do is:

1) Look for an area on your charts where you see that price shot up (for demand) from a certain point in a strong fashion or dropped (for supply) from a certain point in a strong fashion.

We look for a specific point where price had to leave, where it simply couldn't stay there. We can tell this because of the strong move up or down.

See chart below for an example:



2) Once we found an area on the charts where price shot up or dropped down in a strong fashion, we then want to see if we can find the base of the move.

The base is essentially a cluster of trading, where the candle's bodies are trading sideways, next to each other, creating a zone.

If you can find that kind of zone and then see price dropping or rising in a strong way from that zone, then you have a Supply or Demand area.

Let's look at the charts from point 1 to see if we can find a zone.

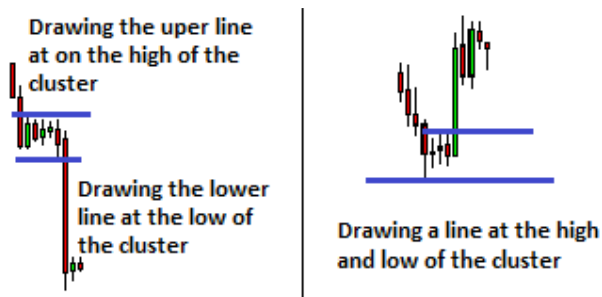


On both of the examples we clearly see the zones we were looking for, preceding the strong moves. This is a Demand level on the left and a Supply level on the right!

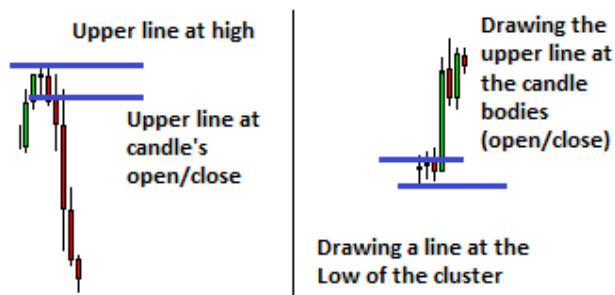
Concretely defining a Supply/Demand zone

Once we found a zone/area as explained above we want to define the base as well as possible by drawing a line on the upper and lower part of the trading cluster. There are two possible ways to define the base (depending on the traders' preference).

1) Draw the upper line at the high of the cluster, draw the lower line at the low of the cluster.



2) For Supply: Draw a line at the high of the cluster for the upper part and draw a line at the candles' bodies (open/close) for the lower part.



For Demand: Draw a line at the low of the cluster for the lower part and draw a line at the candles' bodies (open/close) for the upper part.

DBD-RBR-DBR-RBD

Another way to identify a zone is also to look at DBD-RBR-DBR-RBD

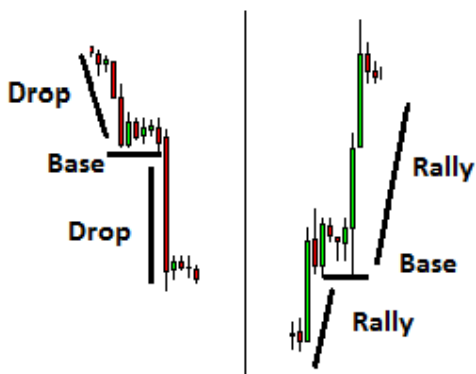
DBD means Drop Base Drop

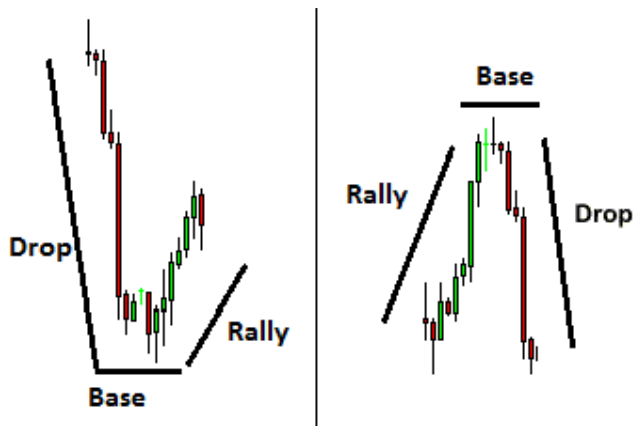
RBR means Rally Base Rally

DBR means Drop Base Rally

RBD means Rally Base Drop

Let's look at some chart and find an example of each.





Balance VS Imbalance

Now that we know how to identify a Supply/Demand level, we should ask ourselves what the level represents...

When the level/zone is being formed, we consider price to be Balanced . There are as many sellers as buyers present in the market. However a decision to push price lower or higher has to be made.

So sooner or later, the balanced cluster that we saw will become imbalanced as there would be more seller then buyers.

This will cause a rise or drop in price and therefore price will break the cluster.

The best possible scenario is price breaking the cluster in a strong, violent way because if that happens then we would know for sure that there were more buyers/sellers at this precise point.

Therefore we can expect price to bounce from there when the Level/Zone is revisited.

How to trade a Supply/Demand Level/Zone?

They are different ways to trade a Supply/Demand level/zone but the highest probability trade is to trade the first visit of the zone because since it's the first visit, the level/zone will still be fresh/untested. Furthermore, it is up to the trader to decide whether they want to take a "Touch Trade", trading the touch of the level/zone or wait for confirmation PA when price arrives at the level/zone.

When a level/zone is getting tested for the first time, we know that this "freshness" gives us the highest probability trade, however this doesn't mean that you have a 100% guarantee that it will bounce there as nothing is 100% in trading.

Also, it is possible that price will bounce at the 2nd or 3rd visit... We don't know how many times it will be tested until the level/zone breaks. Every time a level is tested, it gets weaker and weaker, this is why the first visit gives the highest probability trade...

Broken Supply/Demand

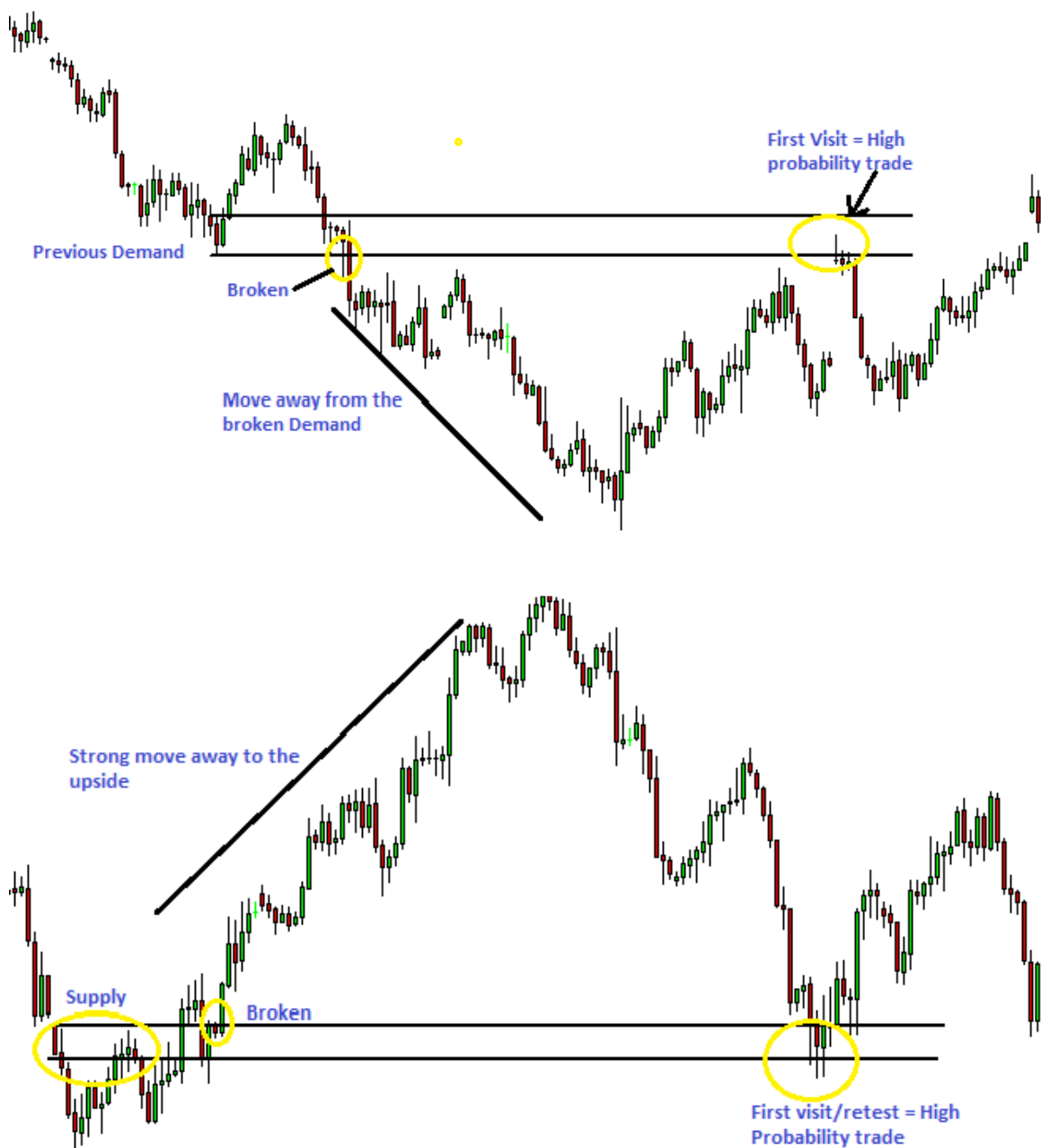
When a Supply/Demand gets tested multiple times we know that soon or later the level/zone will eventually break.

When we see a strong break from a supply zone, we know that bulls did buy there, therefore, we don't consider this zone as Supply anymore but instead we consider it to be a Demand zone now and vice versa for a broken Demand zone.

Supply became Demand or Demand became Supply, this is also called a swap level. If the level was broken in a strong fashion, then we would look to buy/sell from a swap level when price will come to visit the level.

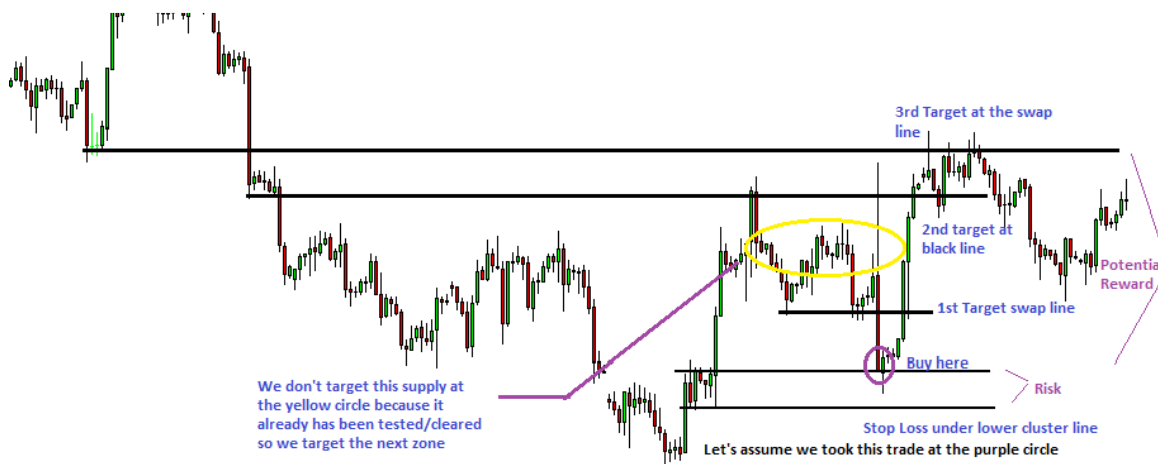
Important Note:

We also look at swap levels for targets, those are important decision points too.



The Profit Margin

Having a good Supply/Demand level/zone alone isn't enough to take a trade blindly... You have to make sure that the potential profit on the trade will be high enough. Make sure that the R:R is good enough by identifying where a previous decision point, Supply/Demand point was.



As a final word, I would like to mention that supply and demand opportunities can be found in every timeframe and in any trading market.

Now that you know what to look for, I suggest that you go and find some examples for yourself on your charts. Try to master this as I believe this is what will take your trading to some new levels... At least it was the case for me...

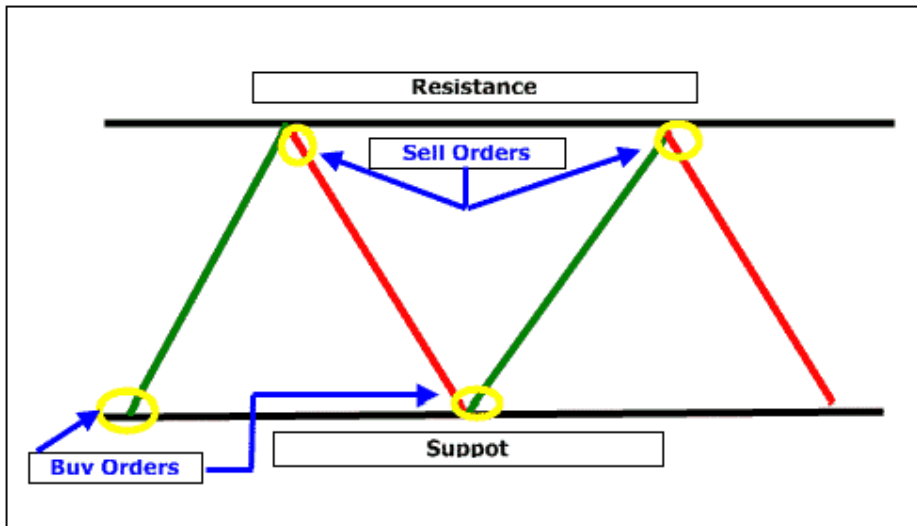
WHAT IS SUPPORT & RESISTANCE?

A Support also referred as “floor” and Resistance also referred as “Ceiling” is nothing more than a decision level that first gets tested and then either “accepted” or rejected, thus “broken”.

When Price bounces from a Support level, it does so because there was much more Buying Pressure than Selling Pressure at that particular point and vice versa for a Resistance level.

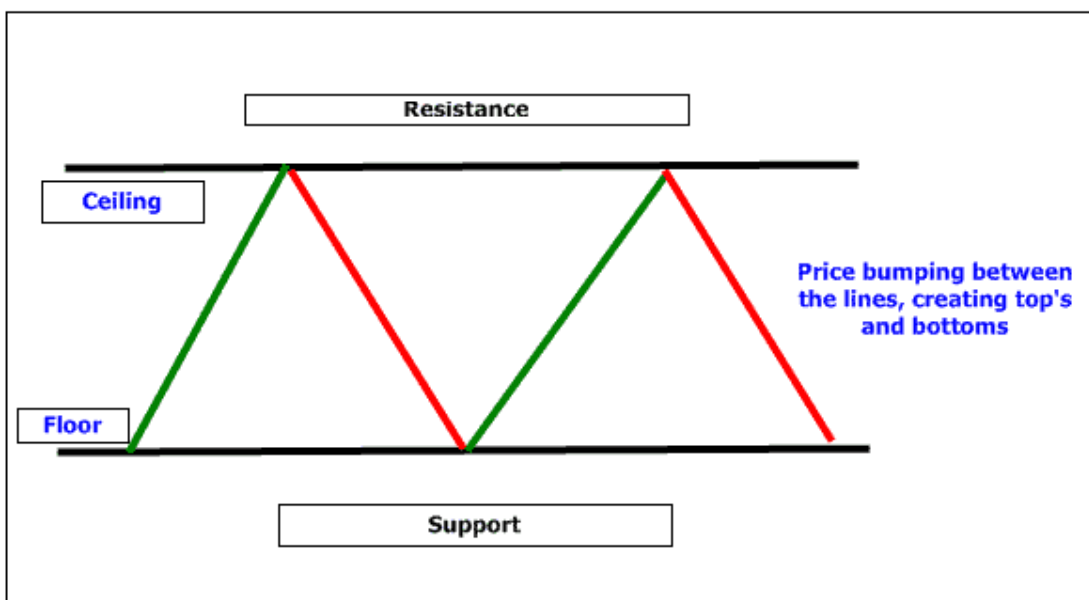
It's as simple as that...

What do Support & Resistance look like?



As you can see on the above picture, when price came to test the Resistance level, a decision was made. In this case the decision was that price was too high, forcing price to trade down until it found a Support level.

Let's look at the picture below. Look at the “pattern” in which price behaves between and at the lines, It is almost like a bouncing ball that is bouncing from the floor to the ceiling...



Support and Resistance breakout

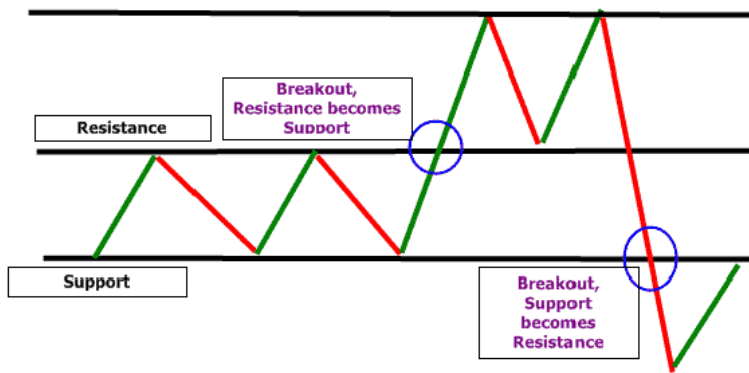
If you search for Support and Resistance on the internet, you will probably find that lots of sources/traders think that the more a Support or Resistance level gets tested, the better...

Obviously, this doesn't make sense at all, because every time price comes to test an S/R level, it consumes the Sell/Buy orders at every touch/retest. So sooner or later all the orders will get filled and a breakout will have to take place.

When a breakout will happen, Support will often become Resistance/ Resistance will become Support.



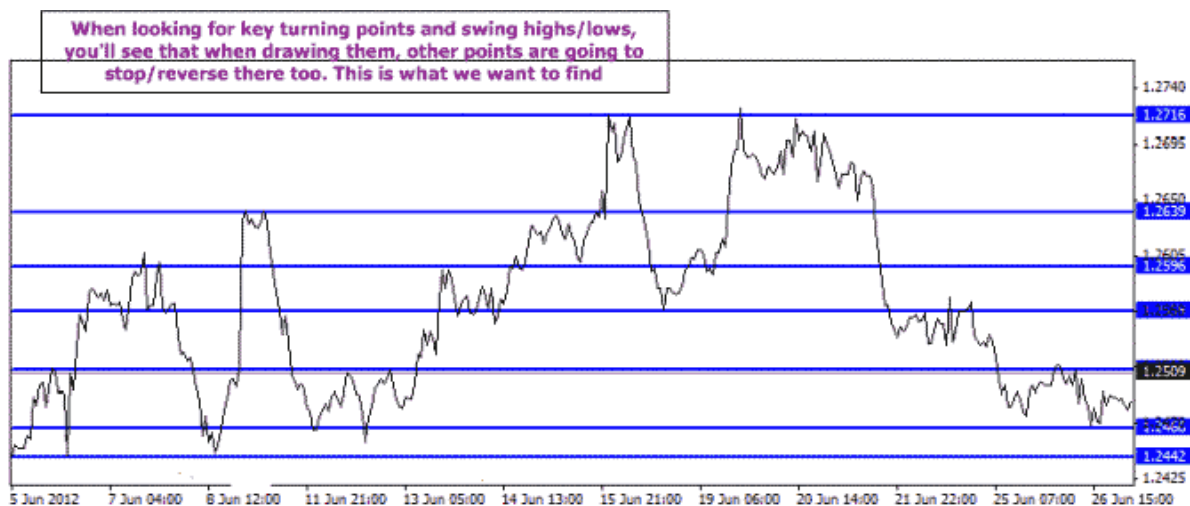
When we went over the Trends topic, you learned that in order to have an uptrend, price had to keep on making Higher Highs and Higher Lows and Lower Highs and Lows for a downtrend, Now you will understand that the highs in an uptrend, and the lows in a downtrend, will have to get broken for the trend to continue it's direction.



How to draw a Support/Resistance level?

There are really no fixed rules to draw Support and Resistance levels. Often the easiest way to draw a Support/Resistance level, is to use a line chart.

Let's look at a line chart and find some Support and Resistance levels. Looking for Key tops and bottoms with at least 2 touches in order to draw a horizontal line. What we want to find are turning points or swing points and mark them.



Sometimes you will see price arriving at a support or resistance level and trying to break the line, trading above the resistance or below the support and than quickly pulling back and closing under the resistance line or above a support line. This is what is called a “false breakout” , or fakeout. A fakeout happens for different reasons. One of the reasons is that price is looking for liquidity (a stop loss hunt). We are not able to know how many touches a support or resistance can accept, we can only know that it often becomes the opposite once it is clearly broken.

Extra Comments:

- When we get a False Breakout at a support or resistance level, while it's breaking out, it will very often react to a previous decision point.

- A support/resistance area is not totally the same as a Supply or Demand level.

A supply or demand level is an area where the real orders are placed while a support or resistance area is where we can spot the retests of the fresh supply or demand levels.

However, we believe that every historical price lines such as Support & Resistance are based on a historical Supply or Demand level.

-Support and Resistance areas can be spotted on any chart and on any timeframe. However, the Higher Timeframes supply and demand zones are much stronger than the Lower Timeframe ones.

Key Levels and Price Action There

What is a price level?

A price level on chart could be defined by plotting a horizontal line, but in fact the level is an area or zone and not a specific price value.

What is a key level?

Key level is a level that has a great history acting as support and resistance, in other words "a level of flip between support and resistance".

Are there any other terms for Key levels?

Yes, it's also known as Pivot Zone, S/R Flip and Swap Zone.

Are there different types of key levels?

Yes, there is a major key level and a minor key level depending on clarity and efficiency of the level.

How do we locate key levels on chart?

A picture worth a thousand words, the first type of key levels are the major key levels which you can locate easily from the first glimpse at any chart by defining swing highs and swing lows. The following chart shows daily major key levels for the pair EUR/USD, some prefer to set levels at the nearest round number if possible.



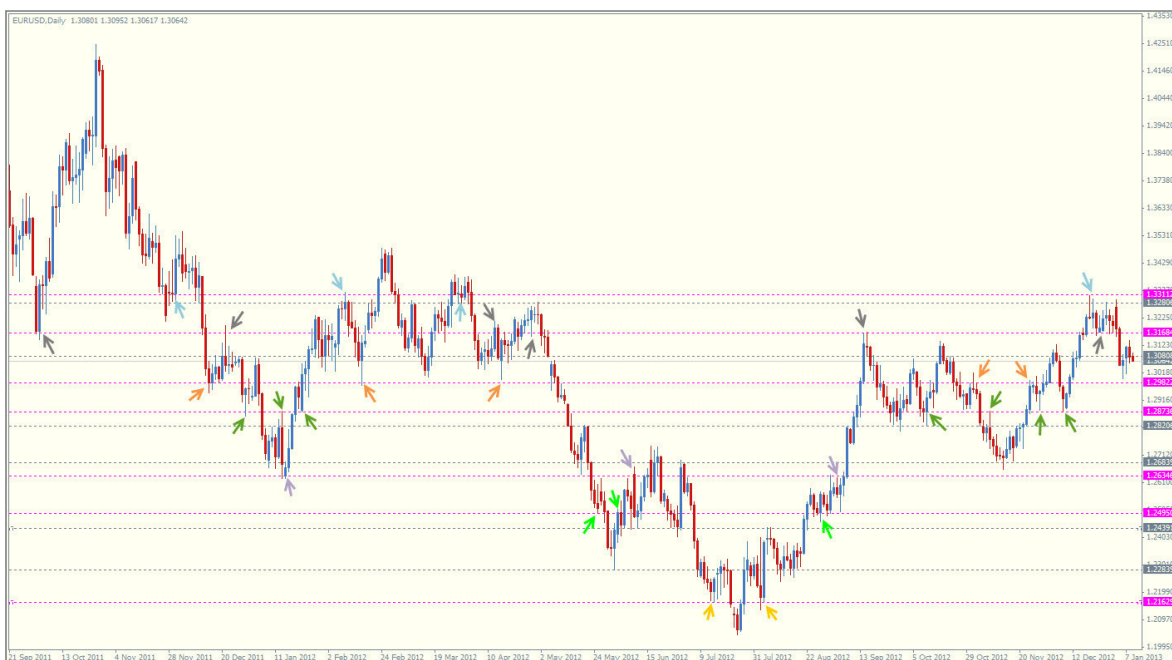
If it's still not clear how to locate these levels, then don't worry because the next chart has the same levels with added coloured markers to indicate the key areas above and below the levels. Each group of pointers of same colour is assigned to one level.



The second type of key level is the minor key level, which in some cases acts as a second option for a major key level and when combined together they form a key zone, although they have a less significant history compared to major key levels, and could cut through a wide range of candles. In the following chart minor key levels were added, using a different colour to differentiate them from major levels.



Once again, the next chart with added coloured markers for a better visual explanation.



Price Action:

We have taken the chart which has both major and minor key levels and we divided it into two sides by a vertical black line. From the left side of the chart to the divider shall be considered as history and the right side as present time. The location of the separator was intentionally chosen because the same levels could have been located up to this stage without the existence of the right side.



Now, we will study the candle closes in relation to the key levels starting from the orange pointer where is written "start":

Price was moving above the lowest major key level then it moved up breaking through the higher major level with momentum and closed above it [1], the next candle retested the level and closed above the higher minor level [2] followed by multiple retests of the same level without any close below the level, later it tested the next minor level and failed to close above. Price consolidated in between the two minor levels [3]. When the decision was made price broke through the upper minor level and the next major level with high momentum and closed above the two levels and below the next major level [4], third candle broke through the major level closing above it and below the next minor level, followed by a retest of major level and a close above the higher minor level [5], the next candle broke through the higher minor level and closed slightly above it and retested with the second candle [6] before moving up with momentum breaking through the next major level and closing above it [7]. Price failed to break the higher minor level and broke down through the major level with a close below followed by a retest and drop [8]. Price continued dropping breaking through lower levels till [9] where it failed to break the major level and closed above it, this was the first retest of this historical major level after a long time and we can see price bounced from it to [10]. Now we'll speed up the process a bit and concentrate on bigger moves. At [11] price had another retest of the same major level failing to close below it and it went up to [12] where it broke through the major level with a close above, but the next candle broke through the same level in the opposite direction and closed below, after a retest price declined to [13] where it closed above the major level and this was a fresh retest of a historical major level, a retest was done by the fourth candle and price rallied up to [14] and this is where we stop. I think now you can see the importance of key levels and candle closes, I left enough candles for you to read by yourself.

Conclusion:

Key levels are highly respected by price, and if price breaks through it and close above or below then it's a sign of where price will go next, in most cases it will travel to the next level.

More often price will give another chance for entry when it retests the strength of broken level before moving to the next.

When price breaks through a level with high momentum and closes above or below without a retest then it's a sign of big buying/selling.

Homework

Mark 40 different key levels on your charts, and explain the PA that occurred on approach and reaction to them. If they broke, mark the PA that occurred in the break and after. Put the homework in your Journal.

Momentum Away / Liquidity Gap

This article will answer any questions you might have about what is the definition of liquidity gap, and how (and why) you expect price reaction in relation to it.

There is no easy way to answer this question as it requires a study of the market microstructure which explains how the exchange occurs in financial markets and the order flow process, but we'll try to make it short and simple.

First of all, here are some the terms that have the same meaning or definition to avoid any confusion:

Base = Cluster = Equilibrium = Indecision = Balance = Stable = Normal = Efficient = Range = Consolidation = Flag.

Decision = Imbalance = Unstable = Abnormal = Inefficient = Momentum = Impulse = Liquidity Gap/Spike = Engulf = Pole.

Corrective Moves = Rebalancing.

Second, refer to the [Order Flow](#) article before reading this article, and the [Key Levels & PA](#) after reading this article.

Now back to basics; we know that in a normal liquid market there is a seller for every buyer and vice versa, this is considered a stable state of the market as it creates a balance between supply and demand and maintains a stable price value, and as the imbalance occurs in supply and demand the value of price increases or decreases. The balance state on a chart is represented by a consolidation in price, and the imbalance is presented by a high volume/momentum candle (also known as a sign of Pro money / Institution's buying or selling). If we zoom into the consolidation (LTF) we'll find other states of balance and imbalance.

The order flow article has explained the execution of orders, and to recap; to have your orders executed at current price you need someone on the opposite side with the same number of orders otherwise price will move too much from your entry until it finds an opposite stack of orders. Retail traders have a big advantage over Pro money since their orders get executed at current price, a benefit that Pro money doesn't have due to their mass orders which gets executed at different prices as the price moves away from their initial entry. Hence they tend to accumulate/distribute their orders through positioning, re-entering on retracements or even creating them as well as fakeouts.

By now you should understand why the sign of pro money buying/selling is presented by high momentum candles aka liquidity gaps, but if you don't then continue reading.

A liquidity gap means low liquidity! How?! You know that in a liquid market for every buyer there is a seller and vice versa, but you also know that online brokers don't guarantee a non-slippage or a no requote during the time of volatile news due to low liquidity, and you can clearly see it on charts during such news when a long spike or a high momentum candle is created in seconds. A broker wouldn't take the risk if you're buying because they can't find you a seller unless they are willing to take the risk by selling to you as a dealer.

So how could we say it's a low liquidity when price moves in a high volume?! Again, we know that high volume candles are signs of big money, institutions etc. entering the market or in control of the market pushing price in their direction...that is true. However, the liquidity in this case is being injected from one side only (the dominant side) hence the name liquidity gap and the equation "Volatility = High Volume + Low Liquidity".

Now bear with me...The "normal or balanced state" of the market is to have a seller for every buyer thus maintaining an efficient change in price value, so when the market moves up or down either in consolidation or in a ladder steps behavior then it's a "normal balanced state", but if it moves up or down with a high volatility and momentum then it's "abnormal or imbalanced state" and it's a sign of domination from one side.

So what is the conclusion?! The dominant side (pro money) would want to collect their profits as soon as price reaches their targets which results in market returning to its previous state (rebalancing) on a wider scale and filling up the liquidity gaps.

The definition part of the question has been answered; now let's answer the other part related to price reaction.

Look below at the Gold daily chart and see the price behavior when it broke through a decision area/major key level of significance, creating a high momentum candle as a sign of one side in control, bulls or bears, and how they wanted to push it higher or lower. Of course price will return to fill the LQ gaps, but later in the future, not at the present time of the incident, especially not when it starts creating a new DP/Supply/Demand as pro money position their entries. On the other hand you can notice larger high momentum candles (LQ gaps) getting filled the same day or next day, but this happens when price fails to break through a major DP or key level and this is when pro money are accumulating/distributing (bottom and top side of the chart).



The market is in a constant state/phase shifting from normal to abnormal, balanced to imbalanced and back again, just the same as in ranging to trending and back again (refer to Wyckoff Market Theory), and every range contains the two phases if you zoom in, the same applies to the bottom consolidated area in the chart.

Supply & Demand trading style is in harmony with order flow and it works according to this stuff.

Caps - RBD/DBR

When price makes a rally with a strong pole up (this whole lesson works vice versa for poles etc down), there's sure to be some profit taking by the institutions, allowing price to drop back into the pole.

Price will very often flag at the top of the pole, as the institutions either begin to add long positions to take price higher, or begin to hide short positions to turn price.

To understand the break of a flag, be aware of [Order Flow](#) and [Liquidity gaps](#)



This article deals with the latter scenario; price rising (rally), flagging (base), and then dropping (drop!)

The flag was a way for the institutions to keep retail traders buying in the expectation of an advance in price, giving them lots of orders to sell against.



Seen in a slightly higher timeframe, this is a very uniform cap on price, and in every TF there's a really strong pole moving down from it



The cap price is obviously way too high, so when price returns to it, the sellers are waiting.

There are often other signs that a cap will hold, such as the [engulf](#) in the chart above, or [compression](#) on approach

Caps are simply excellent places to look for price to turn!



Here's a video on Price Caps
<http://youtu.be/469ZS2YxjhE>

Homework:

Mark at least 200 caps on your charts - there are so many to see that it won't take long. Draw a box from the cap to where price hit it later. Note how price approached the caps, and how it reacted. If price broke the cap, note what happened next. Was the cap still relevant?

Flag Limits

Price spends more time in consolidation ranges than moving and trending.

Until recently i would wait 'til price breaks out of these ranges and i would wait for a retest of the break.

But these ranges are tradeable, so why not benefit?

A few months back Ifmyante posted an image of a BEFL and he said price should bounce at this area and he pointed at a DBD hiccup in the way down.

I said i have noticed a lot of these and asked what is the name, he said "we don't have a name for it, just a decision point".

I told him "i think i found me some new homework, i'll go find many examples of it and report back."

I guess this is it now.

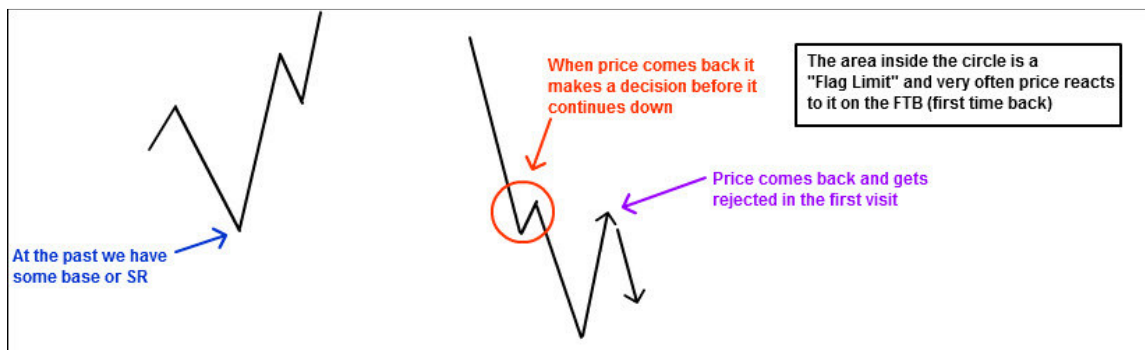
So here is a short article of what is a "Flag Limit" since it is widely used lately. It should help avoid confusion.

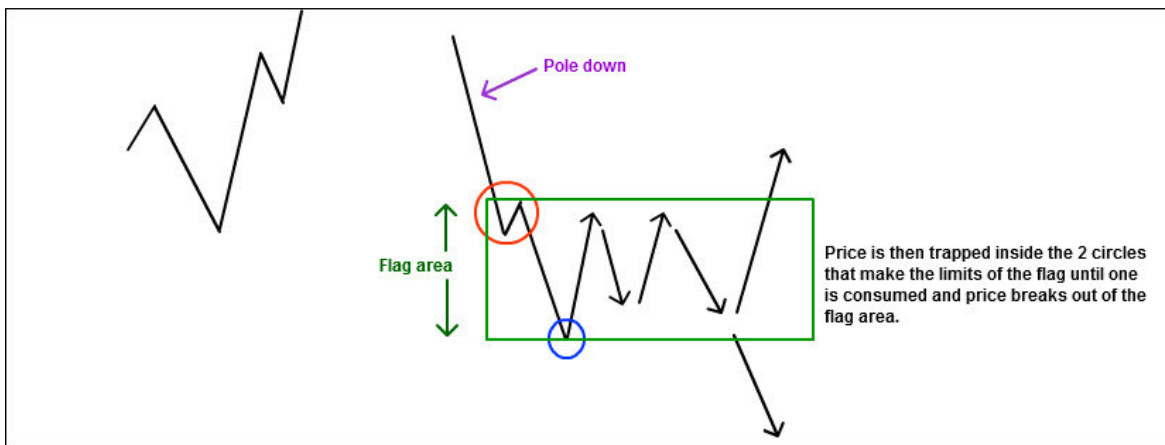
As Ifmyante said a while back: "If there's an area of indecision, it manifests itself as a flag. The limits of this flag then become the new zones."

He also said that "the Flag Limit represents the end of the momentum".

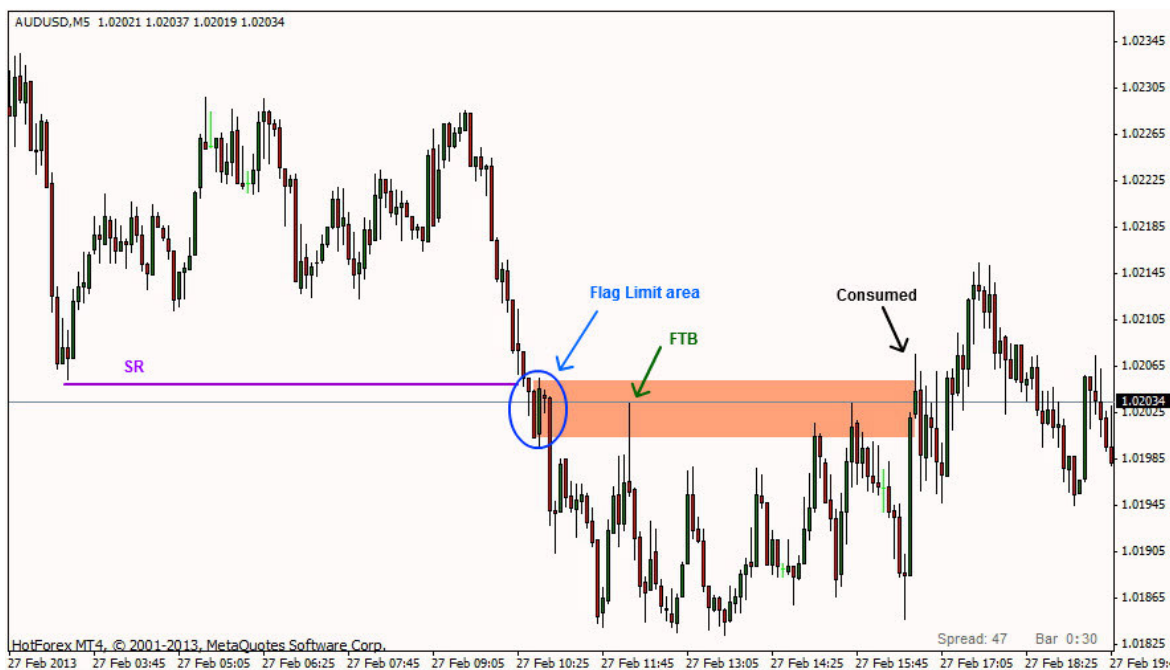
All credit goes to him, for bringing it to my attention.

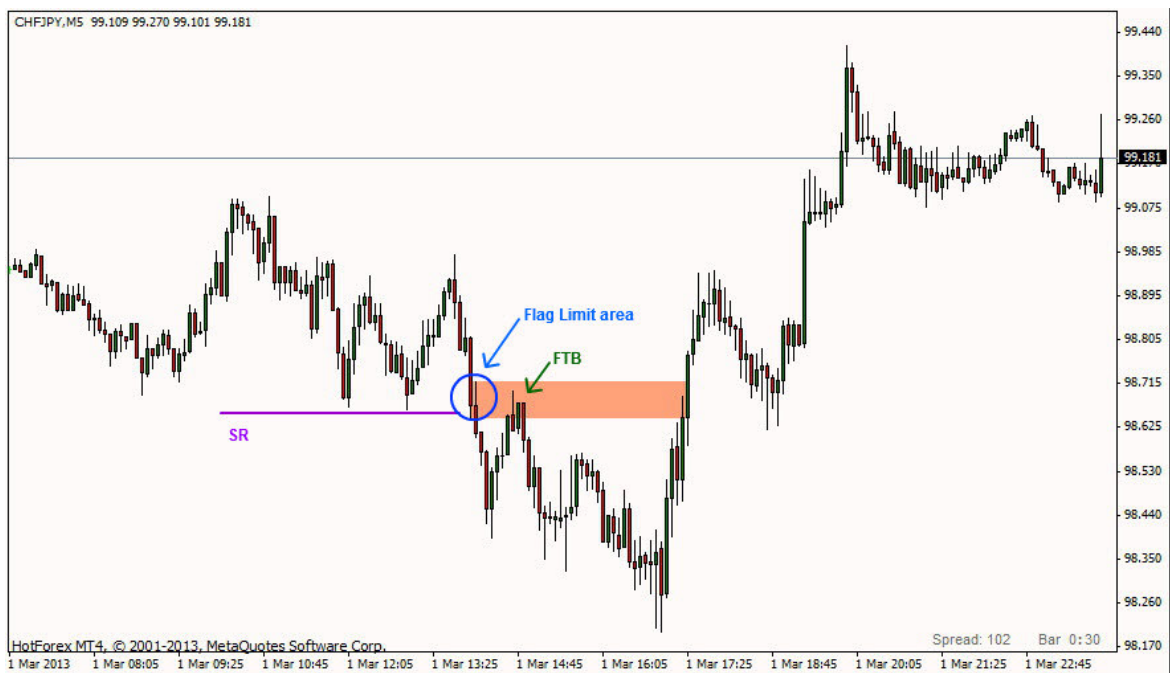
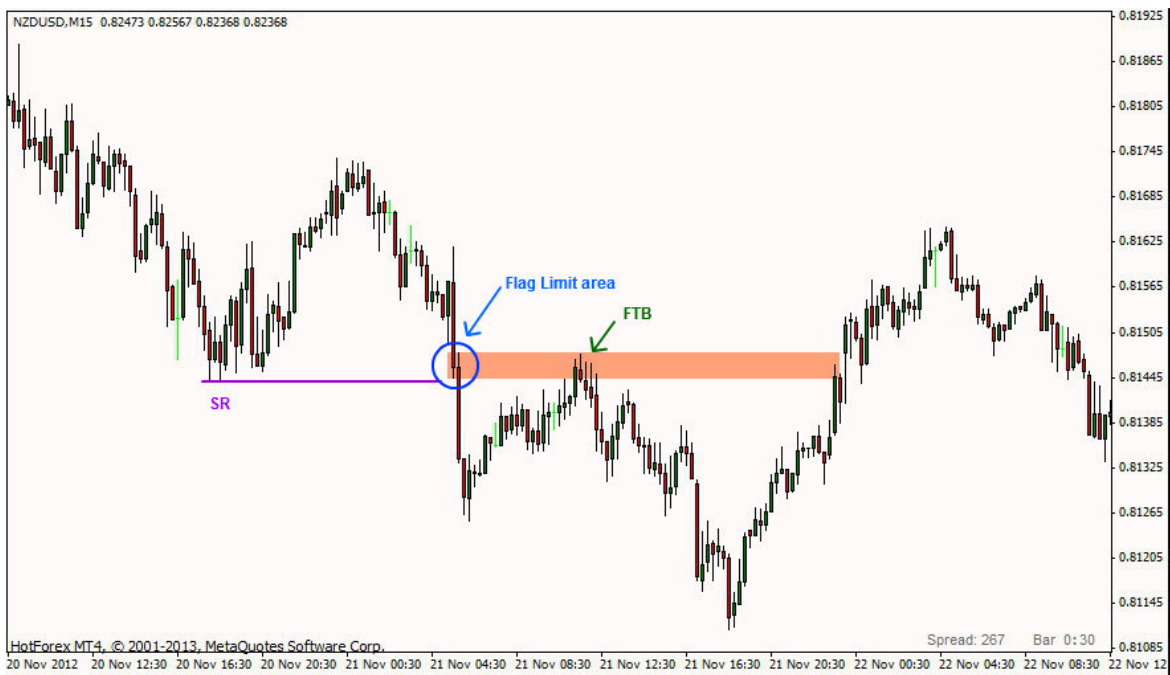
Below are some graphic representations to simplify things before we go on real examples.





and some real examples follow





Some of course are more messy than others, the trick here is to take the best shaped and clear ones.

The whole Flag area has a lot more plays than the FTB alone.

Its your job, if you like, to take this basic setup and expand on it.

I don't list any other plays here because it will only confuse you for now and miss the basic point.

Discussion will continue in your blogs, if you have questions post in the school room.

Best of luck to everyone.

by Harry

Homework:

Find and chart 20 flag limits that bounced price on return.

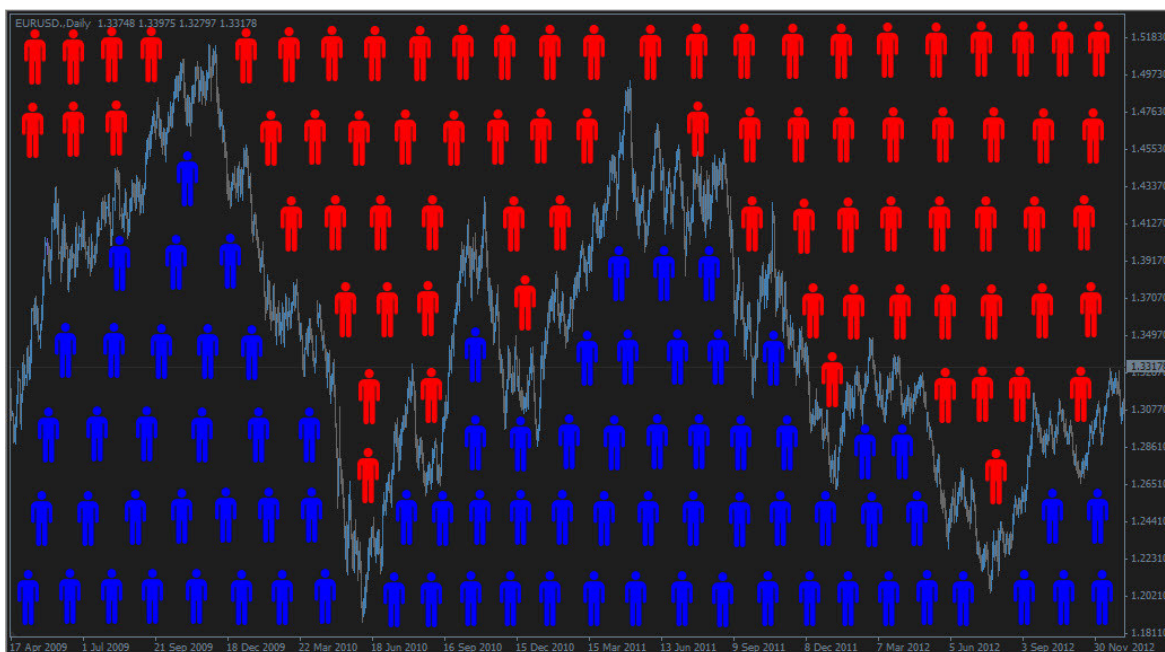
Find and chart 20 flag limits that bounced price on subsequent returns - note the PA.

Find and chart 20 flag limits that failed to hold price on first or subsequent return - note the PA, and where price then went.

Stacked Orders/Zones

Price in a chart reflects filled orders and the empty space surrounding it is full of unfilled orders. As explained in the [Order Flow](#) article, unfilled orders move market price, so we need to focus on the big unfilled orders.

The image below represents unfilled buy/sell orders; we can see the buyers (blue figures) are stacked up and increasing at lower prices, also the sellers (red figures) are stacked up and increasing at higher prices, "BUY LOW, SELL HIGH!".



Stacked buy orders form zones of demand, and stacked sell orders form zones of supply. Moreover, every demand zone has a stack of unfilled bids, and every supply zone has a stack of unfilled offers.

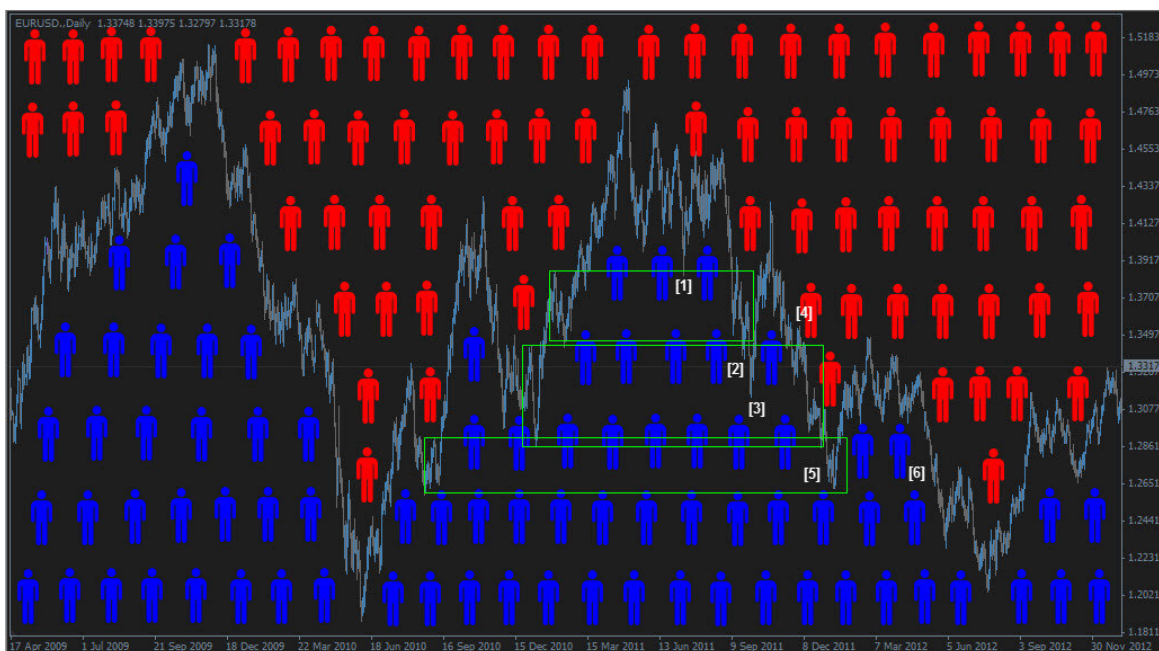
The following examples apply to stacked zones as well as to stacked orders in a zone;

In a demand zone scenario, bids would be stacked below each other (the wider the zone the more buy orders at different prices) the majority would buy low and this is why unfilled orders would increase lower into the zone, and with every return of price to the zone the buy orders are decreased until they're all consumed...now this doesn't mean the pro money would be sitting at the lowest prices...not necessarily...they are the smart money and they know where to position their bids, it could be among the lowest bids i.e. where a compression ends and price rises, or it might be among the highest offers and this is when we see a spike or a quick touch of the zone's higher edge followed by a bounce and price rise for a certain distance before returning back and starts pressuring or forming a descending triangle consuming the entire zone. However, pro money will always be present at lower zones to buy cheap.

In a supply zone scenario, offers would be stacked above each other (the wider the zone the more sell orders at different prices) logically the majority would sell high and this is why unfilled orders would increase higher into the zone, and with every return of price to the

zone the sell orders are decreased until they're consumed...now this doesn't mean the pro money would be sitting at the highest prices...not necessarily...they, as stated before, are the smart money, and they know where to distribute their offers. It could be among the highest offers i.e. where a compression ends and price drops, or it might be among the lowest offers and this is when we see a spike or a quick touch of the zone's lower edge followed by a bounce and price drops for a certain distance before returning back and starts pressuring or forming an ascending triangle consuming the entire zone. However, pro money will always be present at higher zones to sell more expensively.

In the below image we have located three stacked demand zones (green boxes) to study price behavior when it returned to it;



Starting with highest demand, price returned for a 2nd visit at [1] with a quick touch forming a spike into demand followed by buying pressure, 3rd visit was accompanied by high selling momentum and price dropped deeper into the zone consuming remaining bids 'til it reached lower demand at [2] (note this was a 2nd visit, look left) and first reaction pushed price higher but not far, and it came back for a 3rd visit dropping deeper into demand at [3] and here you can see a stronger reaction than [2] pushing price a higher distance. Later price came back for a 4th visit but notice how price was basing (consolidating) above demand at [4] creating a new supply cluster resulting in high selling pressure, and price dropped all the way to the last demand zone for a 2nd visit and deep into it, staying inside the zone for some time until a decision was made and price rose out of it. When price returned for a 3rd visit at [6] preceded by high momentum selling and it was clear that demand was consumed at [5] allowing price to drop further.

The strength of buyers and sellers plays a big role in this process every time it happens, hence the importance of how price leaves a zone, and how it's approaching it.

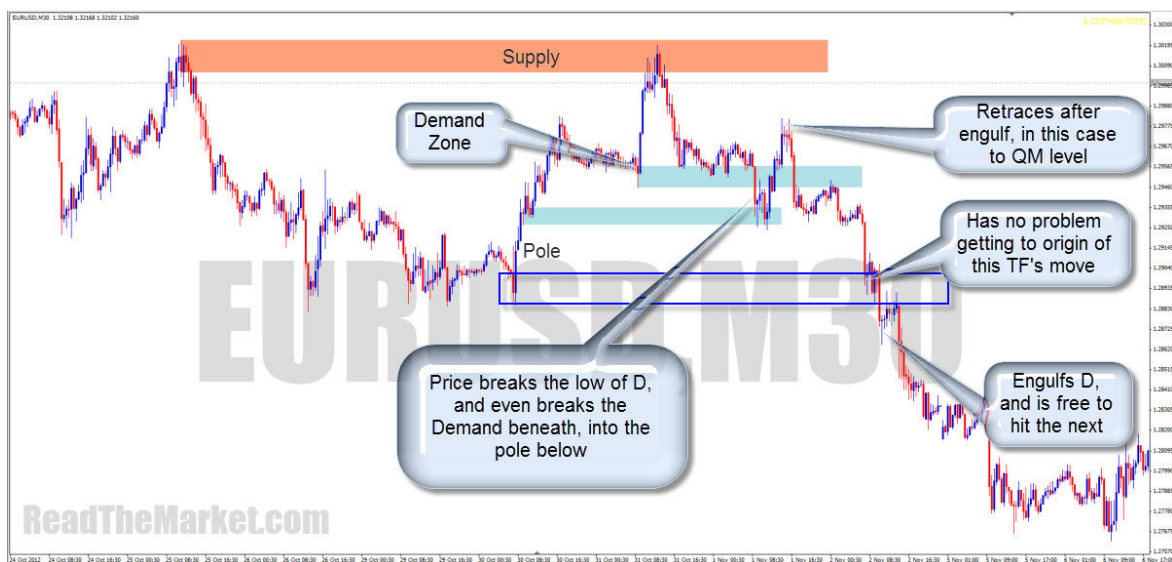
Engulf

If you're not one to simply trade on the touch of a zone, but would rather wait for confirmation that price has rejected, there are some brilliant PA patterns you can look for before you enter a trade.

The best ones we'll cover involve an **Engulf**

Simply put, an engulf involves price making a lower low on reaction to [Supply](#), or higher high from [Demand](#)

This is a very powerful sign that price is on the turn. They say that a **trend** is a succession of LL's and HH's, or vice versa, so if you get a Lower Low from Supply, it's a great first sign that the uptrend may be over, and of course flip the scenario for an HH from Demand.



If you didn't have the patience to wait for that engulf, see the Lower timeframe for another lovely engulf showing the way much earlier!



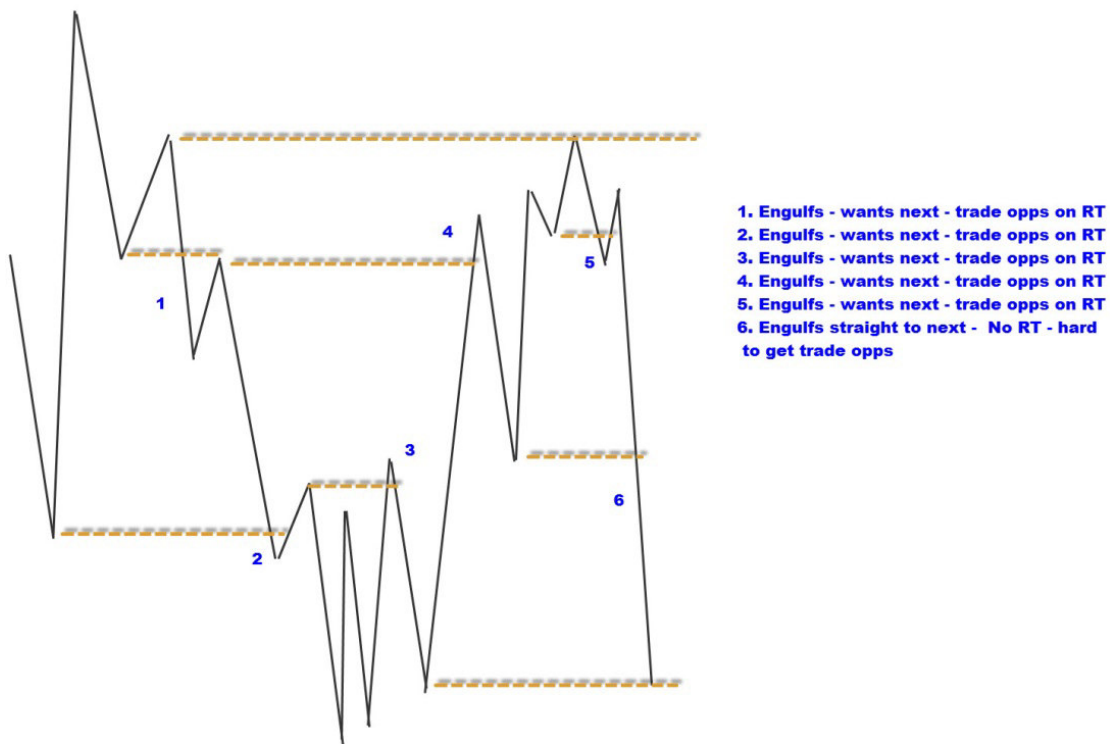
Can you trade an engulf as a breakout trade?

Well, yes, but price very often retraces after the engulf, to confuse the breakout traders and hit their stop losses, creating more orders to take the other side of the big money's new direction trades.

This means that the [stop loss](#) would, in most cases, still need to be beyond the original zone.

Here's a video about the engulf

So, in essence, it's as simple as this



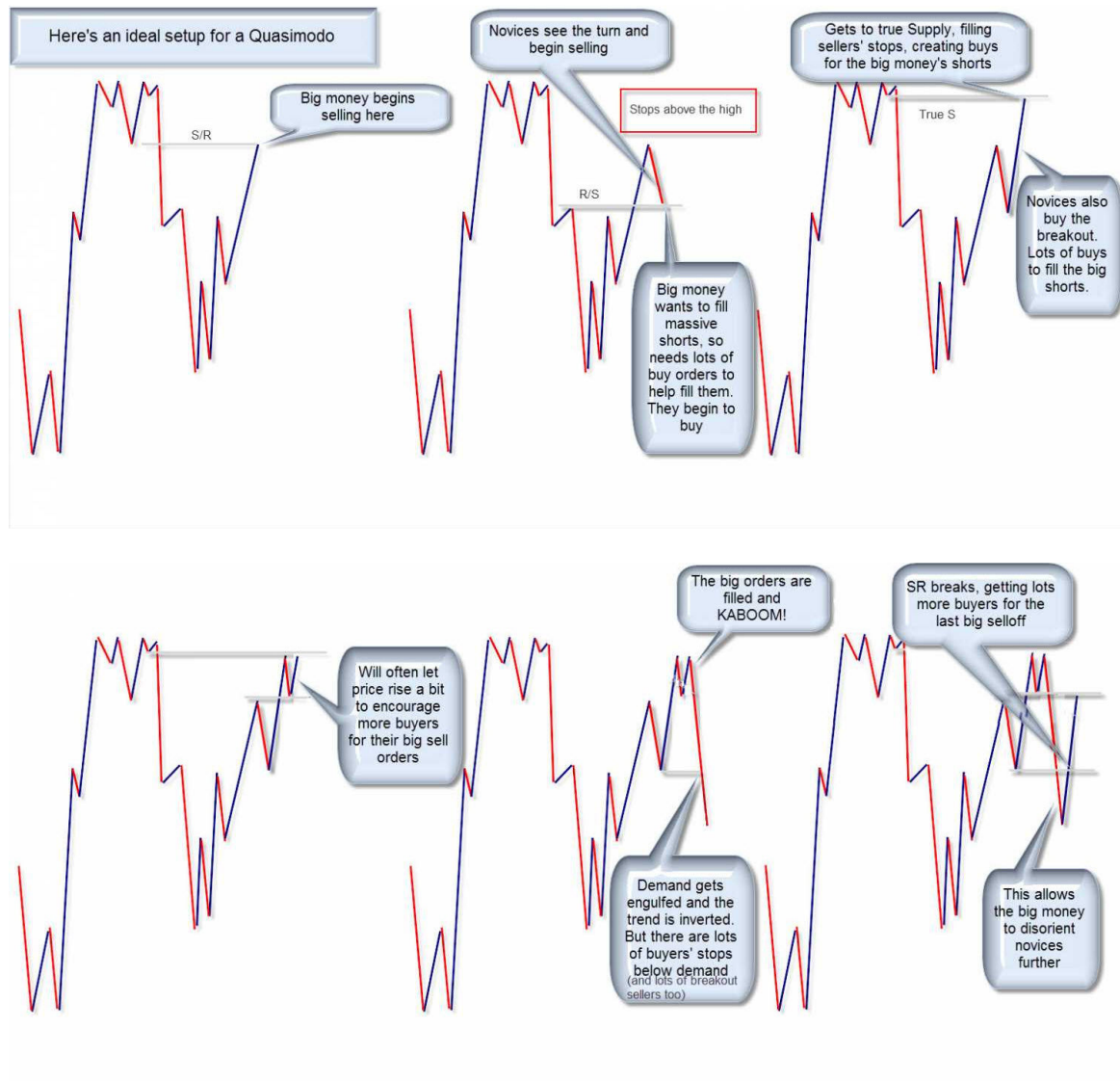
Two of our favourite Price Action structures based on the engulf are the [Quasimodo](#) and the [Diamond](#)

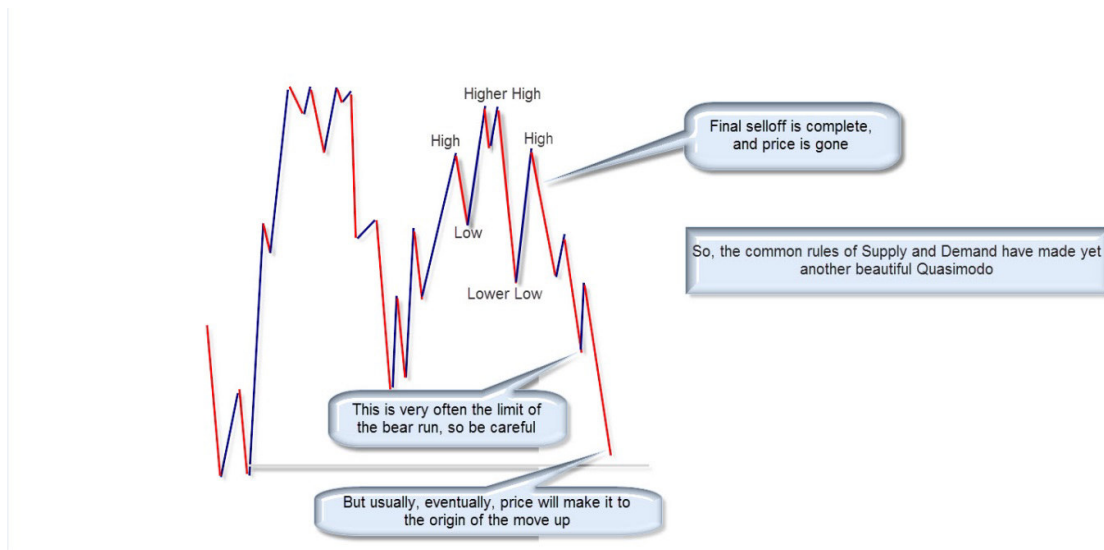
Quasimodo

The Quasimodo is a beautiful and powerful Price Action structure.

It gives a big sign that the big money is ready to change price direction. It often serves to trick the uninitiated into giving up good positions to them, allowing them to get big orders filled.

We look for them at areas of [Supply and Demand](#), where we look for all our trades, and use them as **confirmation** that price has turned, due to the [engulf](#) that occurs in their formation.





A QM doesn't need to form all at once either. Here's a video of one which took many months to form - it was also one of my favorite trades ever <http://youtu.be/JufS5cKBVng>

Homework:

Find at least 60 QMs through history and file them. Mark the zones they're reacting to, and where price went to next.

They can be in any TF, any pair. Find ones that worked, and ones that failed. You'll learn from both





The Diamond

The diamond is one of the most deceptive price structures there is in the market.

It catches both buyers and sellers alike, and can fill massive orders for the big guys.

At Supply, it involves an engulf South, fakeout North, and reversal South - vice versa at Demand

Since a picture tells a thousand words, here are some charts





This is one reason why you should know exactly where to place your stops, and have the faith in the zone to leave your stops there.

Homework:

Find and describe at least 40 diamonds at Supply or Demand.

Any pair, any tf

Candle PA

Have you ever wondered what people actually really mean when they say "I will look at PA for further signs/confirmation"?

Is it possible to fully understand how a market is moving and decipher the chart candles in order to read what they really mean?

In this article, we are going to take a deeper look at price action but particularly at **Candle Price Action**.

Before we dive in , I'd like to take a moment and give some credit to the Doctor and FX.Sniffer and IF who's work and teachings about "advanced" PA inspired me a lot and took my understanding to a higher level.

Let's get started...

So... What does Candle PA really mean?

- The words say it all: The action of price translated into a candle...I hear some of you say "but wait a minute, if this is true, does this means that Candle PA is in fact a sort of lagging indicator ? "

Maybe it is considered as "lagging " to some people but in my eyes, it does show you who is active , the Bulls or the Bears, it shows you if there is some intrest to take price higher/lower, if the entry you are eye balling is the best one and lots more.

However, not every candle that looks the same in terms of shape or length can be interpreted in the same way. To give you an example, I'd say that a Big Momentum Candle can actually mean 2 different things; A clear activity and true willingness to take price higher/lower or a fakeout to make you jump into a trade and be slaughtered ...

How do we know whether price is wanting to fake us or not?

Well, looking at the whole picture can help us understand what price is telling us. One of the most important thing to look at is the location of where certain candle forms.

What we want to do is see how the candles are closing at Key Levels and old Decision Points.

Click here to view FXS's article about [Key Levels](#) if you want to learn how to locate them.

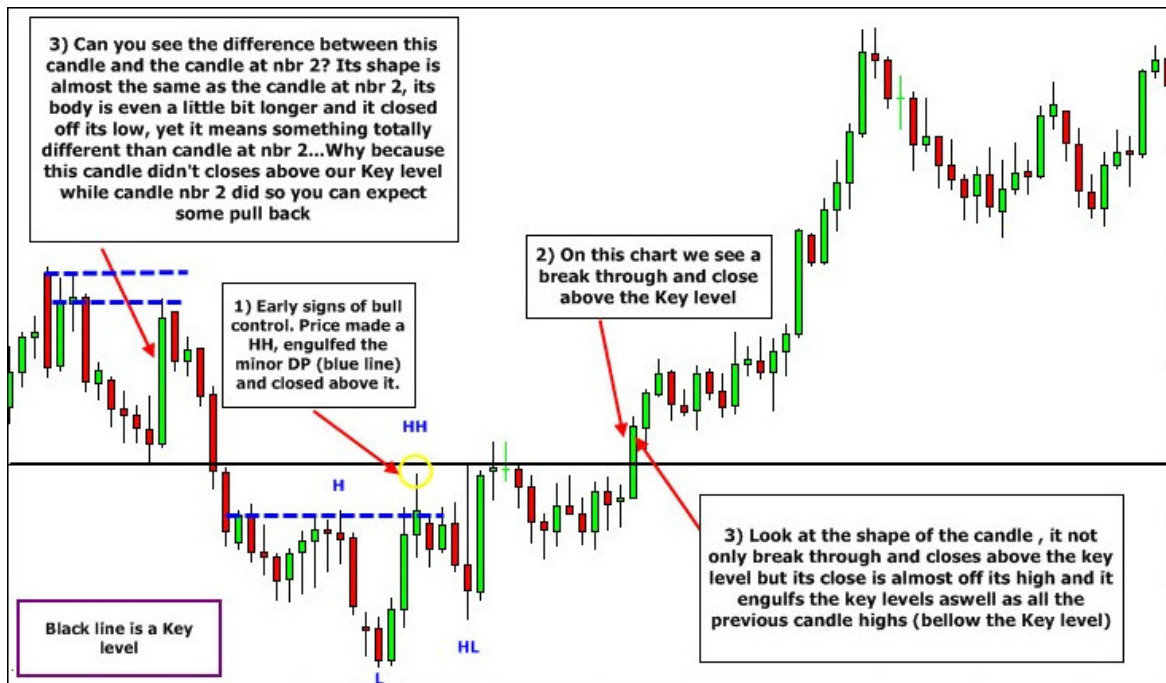
The Candle Close

- Looking for trades elsewhere than around previous decision points and key levels is not a wise choice and it will hurt you if you decide to take entries anywhere else.

A candle close at a DP or Key level will help us determine what price is willing to do, push through or bounce back. It takes a lot of money to push price through and close above a Key level. Only Big Money can do this and if they do it than it's certainly for a reason.

Let's look at charts and see if we can find some examples.





Where to look for candle close?

Using the Higher Time Frame close as a lead is extremely powerful. Once we have an HTF close, we can switch back to a lower Time Frame and look for an entry.

The Wick & Tail

Beside the candle close, the tail and wick of a candle also tell us what is going on in the charts.

A clear wick that pierces a Resistance/Supply and close below it is a potential sign of Selling.

A clear tail that pierces a Support/Demand and close above it is a potential sign of buying
Note, that I'm not talking about candle colors here because the only thing that has importance to us is the wicks/tails and close at Key levels.

Why do I say "Potential" sign of Selling/Buying? Because again the location is extremely important but the whole picture is even important too. Maybe you'll spot the perfect looking candle PA on the chart but if there is not a lot of room for price to move then the setup might not work.

So to recap, we know that the location, close, wick/tail as well as the whole picture is what we need to look at when doing our analysis.

Ask yourself this questions:

- Where is price trading at the moment? Are we at a Key level, Supply/Demand DP ?
- How did price close? Above/below a Key level?
- Was there a tail/wick on the candle and how and where was its close?
- Was there a momentum candle and how and where was its close?
- Was there a bearish/bullish looking candle that actually really meant the opposite (what I call a fakeout)
- Is there enough room for price to move? Is there a key level or previous decision point near the potential entry?

These are question that you should ask yourself when looking for trade setups...

Bar By Bar analysis

A bar by bar analysis can be very usefull when looking for trend entries. Here again, it's not something difficult to do , just look at what price is really doing, where and how it closes is also applicable.

Let's look at the charts below and find some examples.



- 1) So the HTF just closed above the key level and this candle at 1 now closed above the HTF close but did not break the high of prev candle. Potential sign of buying but we wait.
- 2) This candle made higher high than prev one but did not close above it. In fact it closed into the candle body of nbr 1, we still wait.
- 3) This is what most retailers would call a bearish candle but look how it closed...not below candle 1 and it also failed to pierce the key level. In fact this just took a few sellers from a LTF decision point but as its body is so tiny and the close is poor, it's a sign that sellers are not interested.
- 4) Not really relevant except that the close was a pip above prev candle.
- 5) This one is an interesting candle; its tail pierced the Key level and closed above it. We see that this support is holding. An aggressive entry when the candle closes is an option.
- 6) This is a nice candle as well. We have a tail, not very big but ok, the close of the candle is above the prev 5 candles and it closed above the minor LTF DP at blue dashed line = Support is holding and buyers are present = potential entry 7 and
- 8) Closed above 6 but the candle at 8 closed also above all the highs of candles 1 through 6. After that price took off North.

Comments:

What you have to keep in mind is that it's important to have HTF "reasons" to look for a trade and then look at what the candle PA is telling you on lower Timeframes. Looking for just candle PA is not relevant, it's the combination of both that gives us clear signs.

looking at LTF to find a trade entry will help you find an entry very near the HTF key level but all the candle PA I just explained is applicable to any pair, any TF. You choose wich TF suits your appetite the best.

Fakeouts

For a better understanding of liquidity please refer to the [Order Flow](#) and [Momentum Away/Liquidity Gap](#) articles.

What is a Fakeout?

Fakeout is also known as False Breakout, Shakeout, Sellers/Buyers/Bull/Bear Trap, Stop Run, Stop Hunt and Liquidity Spike. It's a search of liquidity followed by a change in direction.

Why does it happen?

There are different scenarios and situations of why it happens. However, the main reason behind it is to create liquidity in an illiquid market - by big funds, to test a level's strength.

To elaborate more on that, a short example is required:

Let's say price of a financial instrument is rising to a value of significant history at 100 (resistance level) where the majority of traders will either buy a breakout with stops below 100 or sell on rebound with stops above 100. The price moves higher to 105 triggering on its way seller's stops and buyer's orders, but price doesn't get any higher and reverses back to 100 before dropping lower to 80.

So what has happened here?...Big funds were planning to sell from 100, but, due to significance of the level, so were the other market participants. So if the whole market is selling at 100 then there are no buyers (lack of liquidity). If pro money sold at 100 they would get a bad fill as price would quickly move away from their entry. In order to get buyers for their sells, they must create liquidity, by moving price a bit higher above 100, to induce buyers to jump in as well as triggering seller's stops which add to the buying pressure. This will help fill their mass sell orders.

At the same time they're able to test if the level holds against the buying pressure. The presence of other bullish big funds would've moved price up with momentum.

When pro money started selling, price fell below the 100 triggering buyer's stops and new sellers jumped in, all adding to the selling momentum.

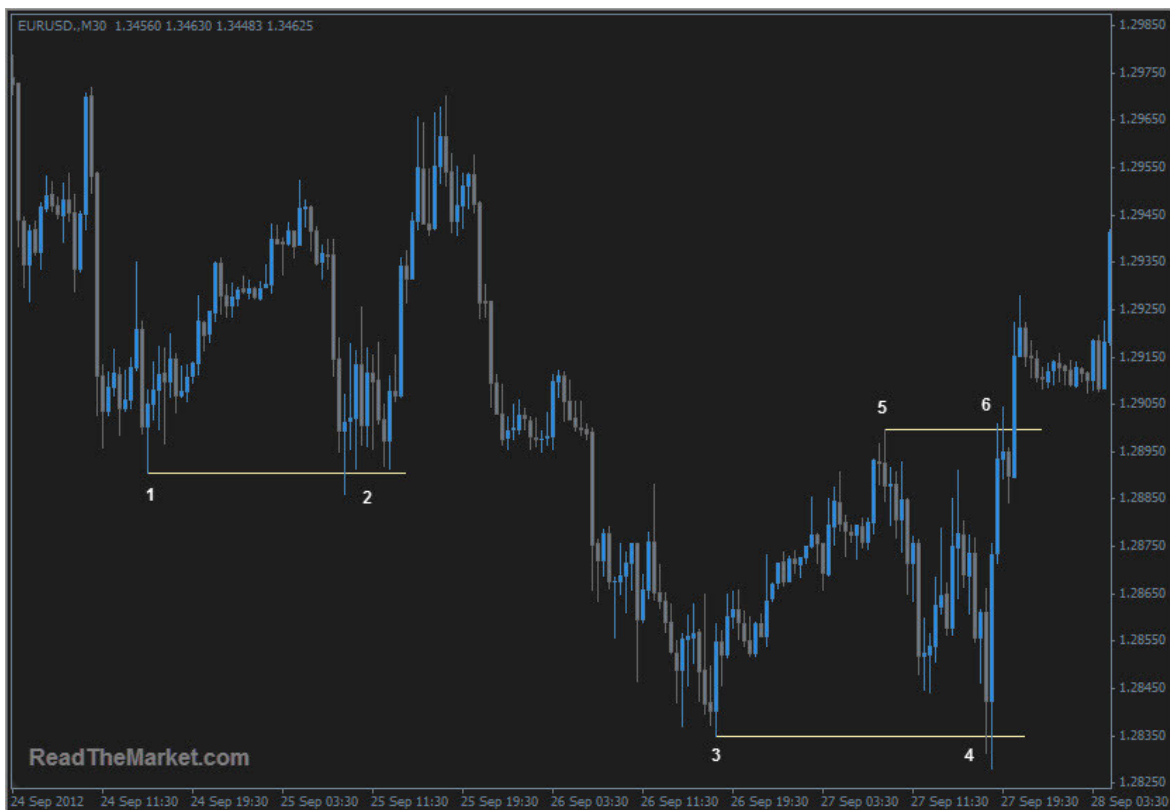
Where does it happen?

Around significant areas where stops are placed, and breakout traders await to buy/sell, at unconsumed Supply/Demand Zones, at Stacked Supply/Demand Zones, and at the end of a Compression into Supply or Demand.

How to identify a Fakeout?

It can be identified in different ways, such as candle close (or close of two combined candles) in relation to a previous Swing High/Low, or a Support/Resistance, or a Key Level.

Now let's go through some examples showing the different ways to identify a Fakeout:



At [1] price created a swing low then moved up and returned back at [2] in a curvy shape breaking through the swing low level but failed to close below and this is a Fakeout, next price consolidated above the level retesting if level will hold then moved up.

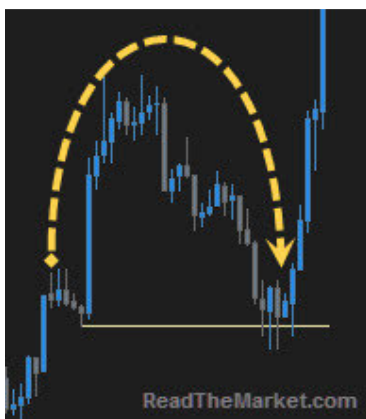
At [3] another swing low and a return at [4], considering the space and time price took to return at [4] and the acceptable curved shape, price created a Fakeout followed by a retest and a second Fakeout before moving up.

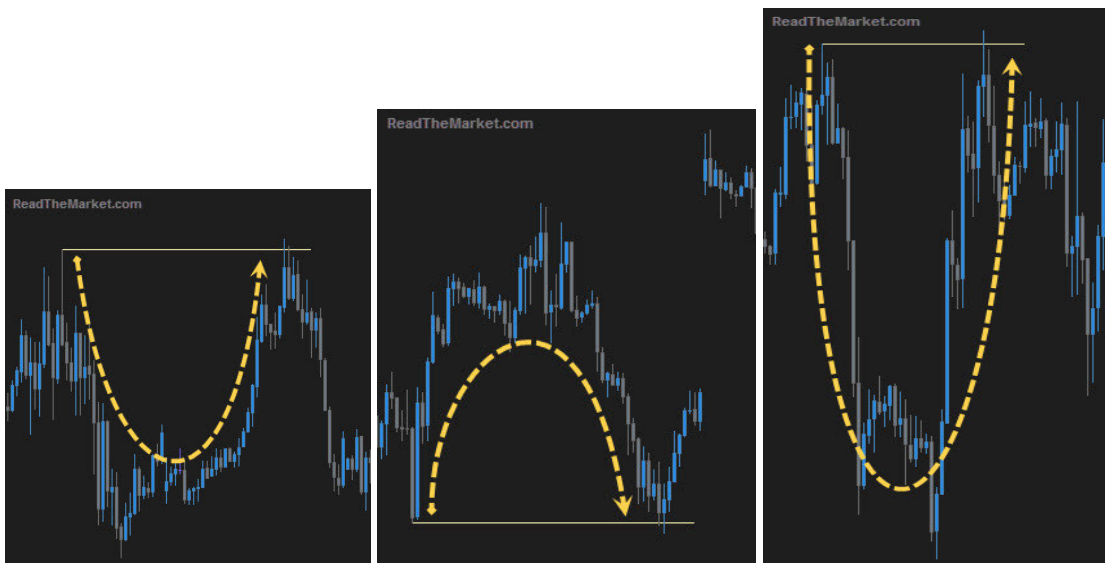
At [5] a swing high and the return at [6] wasn't a good acceptable curvy shape, the Fakeout at [6] was to test if level will hold and eventually it was broken.



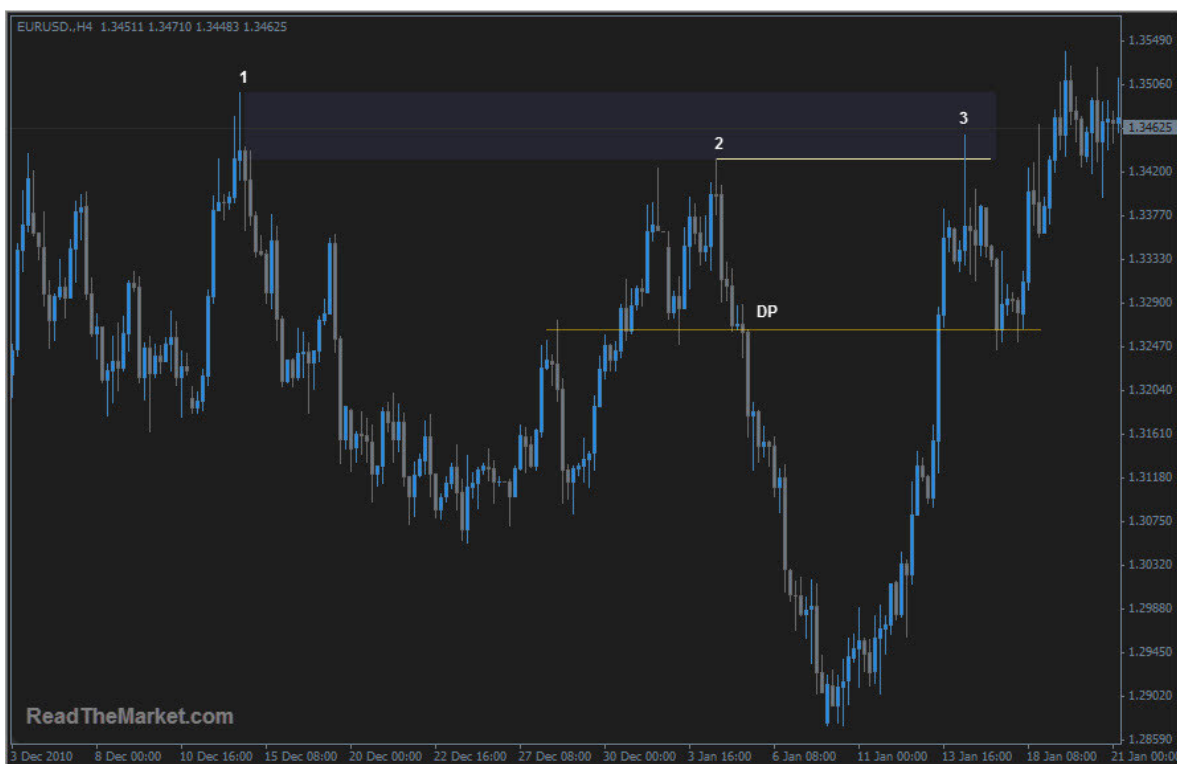
You can see two Fakeouts, one of a swing high level and another of a swing low level. Both cases had an acceptable curvy return to test the swing levels and without having to retest the Fakeouts price has changed direction at both levels.

Before continuing the examples let's first elaborate more about the curvy shape. The main factors in a curvy shape to be taken into consideration are time & space which price took to return to a swing point. The efficiency of the shape itself could vary from a perfect arc to a triangle. Here are some examples of a perfect curvy shape;





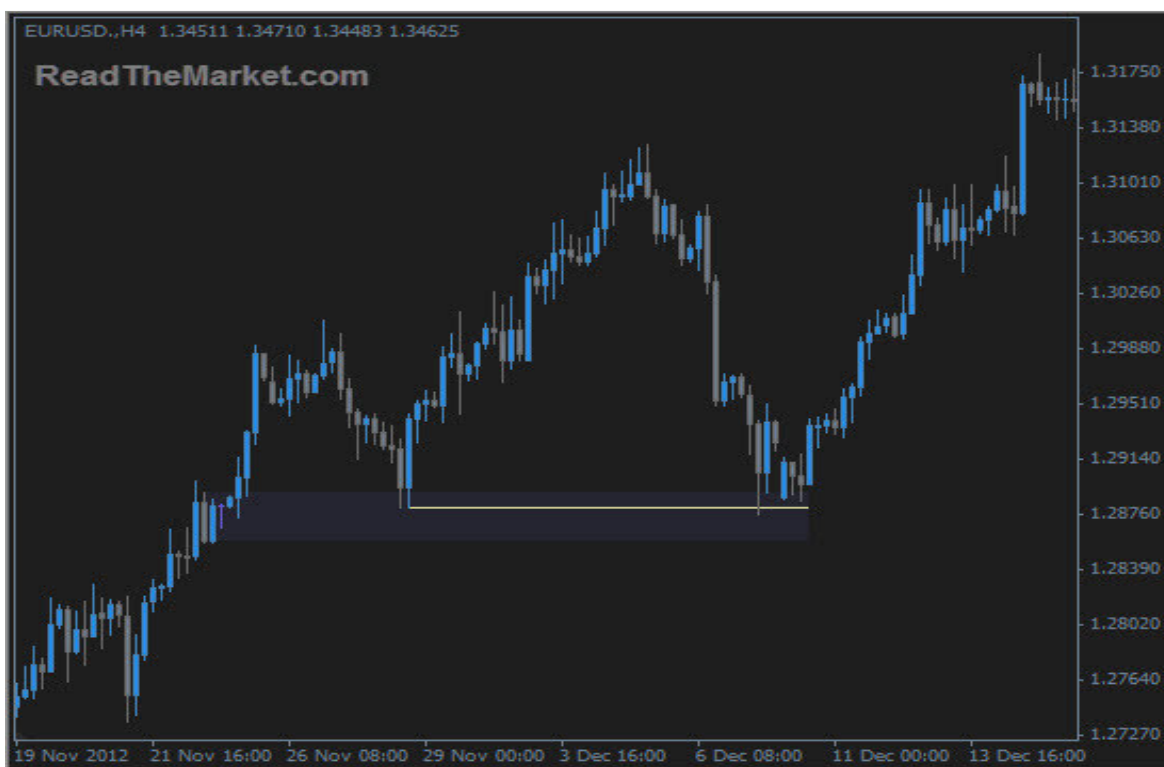
Now to continue with the Fakeout examples;



Price created a supply zone at [1] and returned at [2] creating a lower high before dropping and returning in a curvy shape for a 2nd visit at [3] creating a Fakeout of preceded swing high from [2] and into the supply followed by a drop in price. Considering the time frame; the move down was effective until it flipped from an S/R flip level and an ignored supply DP (Decision Point).



Price came back in a great curvy shape for a 2nd visit into demand at [2] creating a Fakeout of preceded swing low from [1] and a retest followed by a rally in price.



The same example zoomed out to the next higher time frame for a better visual of the DP (RBR) demand zone.



A demand zone at [1] and a 1st visit at [3] and a Fakeout of a preceded swing low from [2] followed by a change in direction. Notice the space and time between [2] & [3], not so big but still the curvy shape from [2] to [3] is considerable.



The same example zoomed out to the next higher time frame to show the difference between time frames when spotting the curvy shape.

In the following two examples you'll notice additional ways to identify a Fakeout:

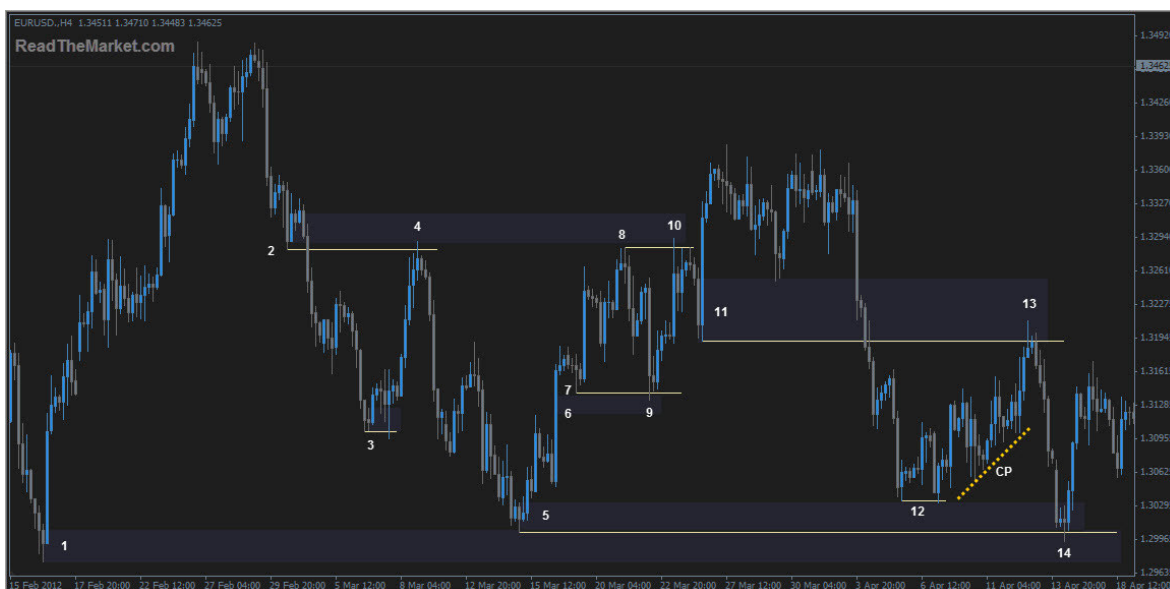


At [1] a demand zone that was ignored thus becoming supply, price dropped forming a support at [2] and an ignored demand pocket followed by a drop and retest of broken support becoming S/R flip and a Fakeout at [3] into ignored demand followed by another drop in price.

At [4] a demand zone was created followed by another demand at [5] and a rally to [2] a 1st visit to the ignored demand from [1] (now supply) then price compressed down into the fresh demand at [5] creating a Fakeout at [6] followed by a retest and a rally to [7] for a 2nd visit into supply and a Fakeout of the preceded swing high from [2] followed by a retest of the Fakeout and change in direction. Note that ignored demand at [1] is totally consumed now and [7] is a fresh supply zone.

At [8] we have a swing high and at [9] a DP (RBR) demand followed by a rally to [10] and a 1st visit into supply from [7], price moved down to [11] into demand from [9] creating a Fakeout into support from [8] followed by a move up to [12] back into supply for a 2nd visit and a Fakeout of the preceded swing high at [10] followed by a change in direction.

At [13] price returned back to the demand from [4] digging deep into it and the spike that broke through the zone with a close inside was a clear sign of consumption.



In this example we'll speed up the process and point directly at the Fakeouts;

At [2] a support point and a DBD (supply) followed by a drop in price to [3] creating a swing low and a Fakeout (the curvy shape could be seen on a lower time frame). Price returned to supply at [4] creating a Fakeout of the broken support point from [2] followed by a change in direction.

At [9] a Fakeout of the support from [7] and into a LTF DP (RBR) from [6] followed by a change in direction.

At [10] a Fakeout of preceded swing high at [8] and into supply from [2] followed by a retracement.

At [12] a tiny Fakeout of preceded swing low and into demand from [5] followed by a compression up. Note here that recent price reaction to demand from [5] makes of it a stacked demand above the lower demand from [1].

At [13] compression into ignored demand from [11] turned supply and a Fakeout of resistance (LQ Spike) followed by a change in direction.

At [14] another visit to stacked demand zones and a spike into the lower demand zone as well as a Fakeout of the swing low from [5] followed by a change in direction.

Proof of market manipulation from the Market Wizards Book:

Ref: Market Wizards - Paul Tudor interview;

That sounds like a general character-building lesson. What about specifics regarding trading?

"Tullis taught me about moving volume. When you are trading size, you have to get out

when the market lets you out, not when you want to get out. He taught me that if you want to move a large position, you don't wait until the market is in new high or low ground because very little volume may trade there if it is a turning point.

One thing I learned as a floor trader was that if, for example, the old high was at 56.80, there are probably going to be a lot of buy stops at 56.85. If the market is trading 70 and 75 offered, the whole trading ring has a vested interest in buying the market, touching off those stops, and liquidating into the stops—that is a very common ring practice. As an upstairs trader, I put that together with what Eli taught me. If I want to cover a position in that type of situation, I will liquidate half at 75, so that I won't have to worry about getting out of the entire position at the point where the stops are being hit. I will always liquidate half my position below new highs or lows and the remaining half beyond that point."

Ref: Market Wizards - Monroe Trout interview;

What else did you learn on the floor?

I learned about where people like to put stops.

Where do they like to put stops?

Right above the high and below the low of the previous day.

One tick above the high and one tick below the low?

Sometimes it might be a couple of ticks, but in that general area.

Basically, is it fair to say that markets often get drawn to these points? Is a concentration of stops at a certain area like waving a red flag in front of the floor brokers?

Right. That's the way a lot of locals make their money. They try to figure out where the stops are, which is perfectly fine as long as they don't do it in an illegal way.

Given that experience, now that you trade off the floor, do you avoid using stops?

I don't place very many actual stops. However, I use mental stops. We set beepers so that when we start losing money, a warning will go off, alerting us to begin liquidating the position.

What lesson should the average trader draw from knowing that locals will tend to move markets toward stop areas?

Traders should avoid putting stops in the obvious places. For example, rather than placing a stop 1 tick above yesterday's high, put it either 10 ticks below the high so you're out before all that action happens, or 10 ticks above the high because maybe the stops won't bring the market up that far. If you're going to use stops, it's probably best not to put them at the typical spots. Nothing is going to be 100 percent fool proof, but that's a generally wise concept.

Ref: Market Wizards - Richard Dennis interview;

Can you give me an example of how the lack of real world experience would hurt the researcher?

As an example, assume I develop a mechanical system that often signals placement of stops at points where I know there will tend to be a lot of stops, in the real world, it is not too wise

to have your stop where everyone else has their stop. Also, that system is going to have above-average skids. If you don't understand that and adjust the results accordingly, you are going to get a system that looks great on paper, but is going to do consistently poorer in the real world.

Ref: Market Wizards - Bruce Kovner interview;

Let's say you do buy a market on an upside breakout from a consolidation phase, and the price starts to move against you—that is, back into the range. How do you know when to get out? How do you tell the difference between a small pullback and a bad trade? Whenever I enter a position, I have a predetermined stop. That is the only way I can sleep. I know where I'm getting out before I get in. The position size on a trade is determined by the stop, and the stop is determined on a technical basis. For example, if the market is in the midst of a trading range, it makes no sense to put your stop within that range, since you are likely to be taken out. I always place my stop beyond some technical barrier.

Don't you run into the problem that a lot of other people may be using the same stop point, and the market may be drawn to that stop level?

I never think about that, because the point about a technical barrier—and I've studied the technical aspects of the market for a long time—is that the market shouldn't go there if you are right. I try to avoid a point that floor traders can get at easily. Sometimes I may place my stop at an obvious point, if I believe that it is too far away or too difficult to reach easily.

To take an actual example, on a recent Friday afternoon, the bonds witnessed a high-velocity breakdown out of an extended trading range. As far as I could tell, this price move came as a complete surprise. I felt very comfortable selling the bonds on the premise that if I was right about the trade, the market should not make it back through a certain amount of a previous overhead consolidation. That was my stop. I slept easily in that position, because I knew that I would be out of the trade if that happened.

Talking about stops, I assume because of the size that you trade, your stops are always mental stops, or is that not necessarily true?

Let's put it this way: I've organized my life so that the stops get taken care of. They are never on the floor, but they are not mental.

By FX.Sniffer

Here's a vidoe about Fakeouts by If
http://youtu.be/8eqgTjXa_jl

Homework

Find and mark at least 30 different fakeouts on your charts. Any pair, any timeframe.
Note the PA, where price faked to, and where the move eventually targeted
Post your homework in your journal

The CanCan

Very often price will move into, or even better, break out of a zone with strong momentum, creating a pole.

Usually a pole will have a flag on top, gathering orders for price to advance.

But if the flag breaks back into the pole, this is a significant turn in value.

A CanCan can often occur at such an event.

Price moves hard, flags briefly, and moves back quickly with a [Liquidity Spike](#). This liquidity spike will mean there may very well be orders left to be filled at the edge of the flag, so you'll very often see [compression](#) back towards it, with extra orders being hidden, so that when price hits the cap, it can shoot back through the compression and on to the base of the pole.

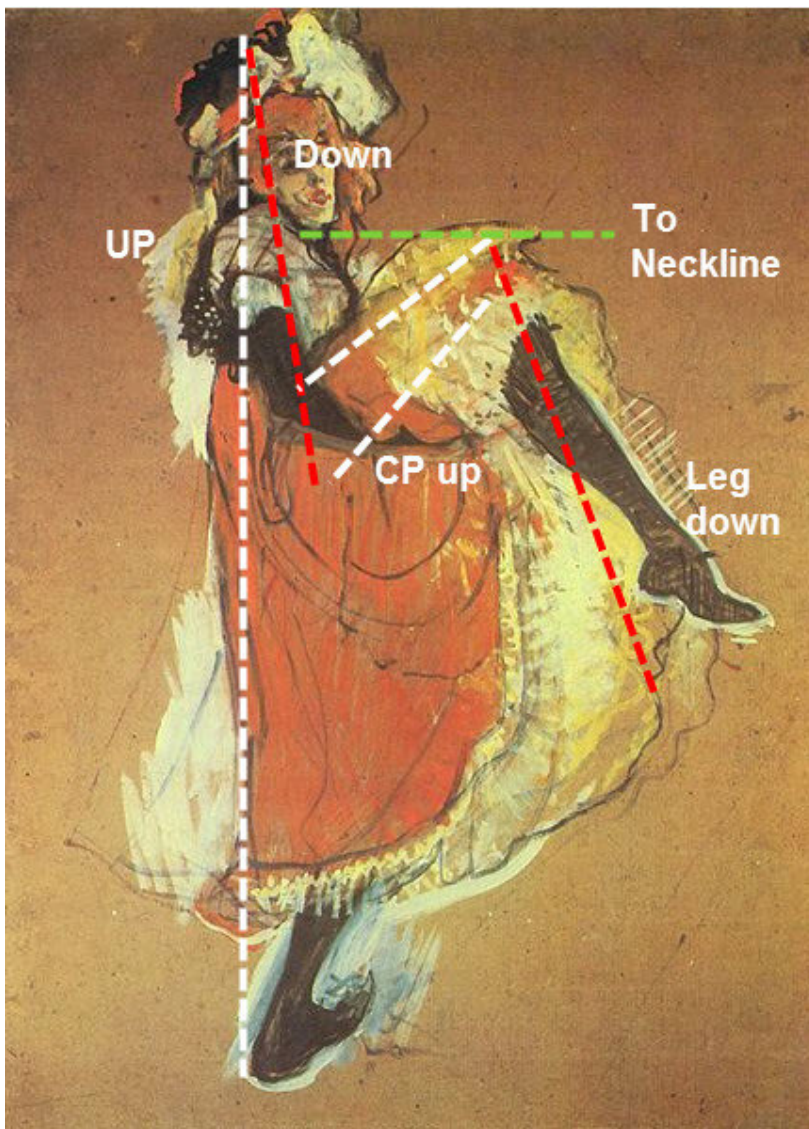
Here's an example



and another



and here's why it's called a cancan. Thanks Henri 😊



Homework:

Find and describe at least 20 cancan throughout history. Any pair, any timeframe

Trendlines

In this article, I will discuss how trend lines can be combined with supply and demand zones to confirm (or fine tune) an entry within a supply and demand zone. To explain this idea, I will use the charts in Mel's [Supply and Demand](#) article.

Based on the principle of supply and demand, we are looking for an entry long within a demand zone and an entry short within a supply zone. As Mel states *"it is up to the trader to decide whether they want to take a 'Touch Trade', trading the touch of the level/zone or wait for confirmation PA when price arrives at the level/zone."*

As an alternative to using PA to confirm a trade when price arrives at a zone, or as additional supporting confirmation, a trend line can be used. Although this can work well, as Mel mentions in her article, *"there is nothing 100% in trading."*

The chart below is from the Mel's article and shows an example of trade short on the first visit back to a supply level.



The following chart shows how a trend line (lines in red) can be used to help confirm (or fine tune) the entry. In this instance, price stopped a couple of pips from the lines, although it shows the idea.



The chart below is also from the Mel's article and shows an example of trade long on the first visit back to a demand level.



The following chart shows how a trend line (line in red) can be used to help confirm (or fine tune) the entry long.



The chart below is also from the Mel's article and shows an example of trade long at a demand level.



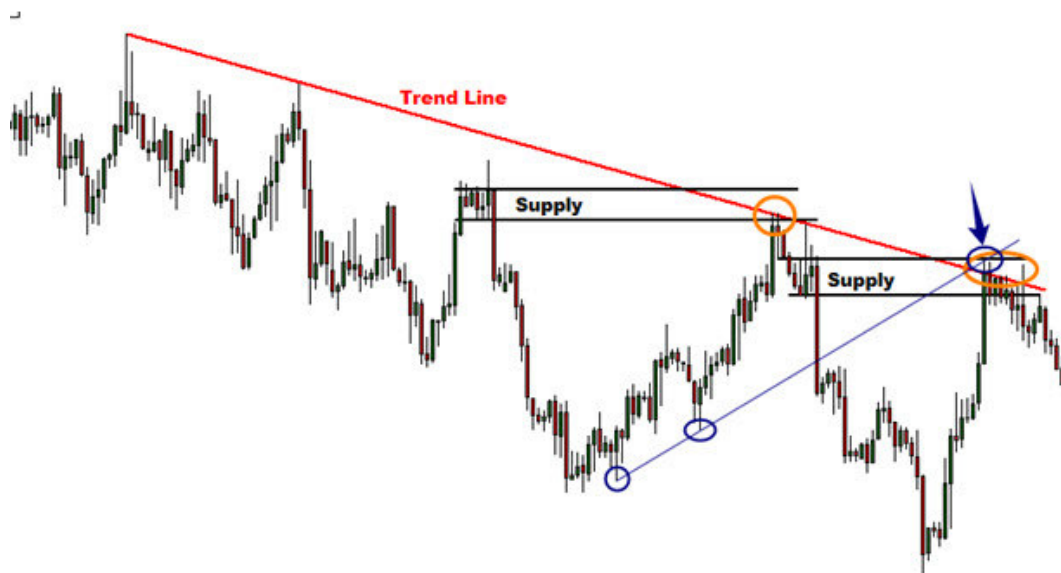
The following chart shows how a trend line (lines in red) can be used to help confirm (or fine tune) the entry long.



The chart below is a another example.



The chart below adds a second trend line to the chart to show that there are sometimes more than one line which can be added.



Fibonacci Levels

What is a Fibonacci Sequence?

This sequence is simply a series of numbers in which each term is the sum of the 2 numbers preceding it. The first ratios are : (1,1,2,3,5,8,13,21,34,55,89,144...). These numbers are recursive. There are also the Golden Ratios and those represent the measurement of any number to the succeeding higher number. For example $34 : 55 = .618$ and $89 : 144 = .618$

Golden Ratio

The Golden Ratio is used in lots of different areas. It, for example, describes the proportion of many of nature's designs. If you measure your height starting at your feet to your belly button, you will get 61,8% of your total height... Funny huh?

The ratios are also used in the Financial Markets because the market uses the same mathematical base. The most common used ratios are the 38,2% , 50% and the 61,8 .

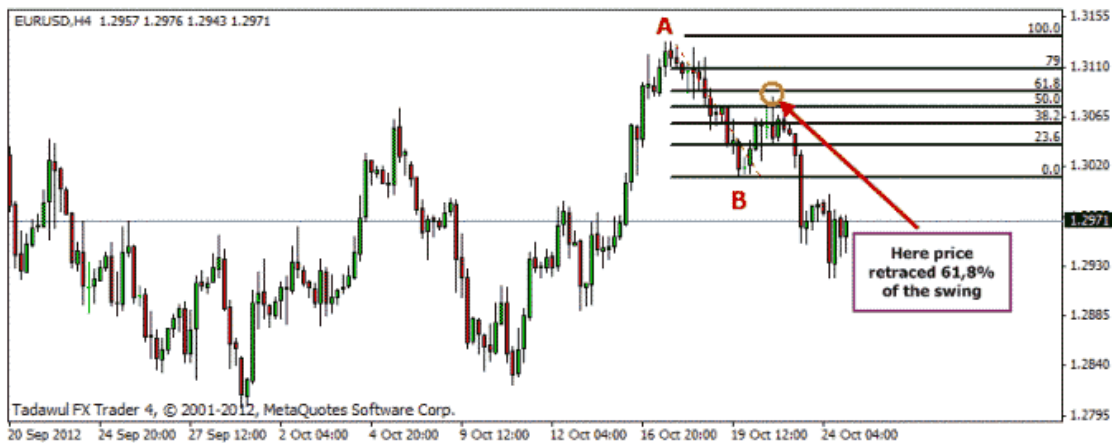
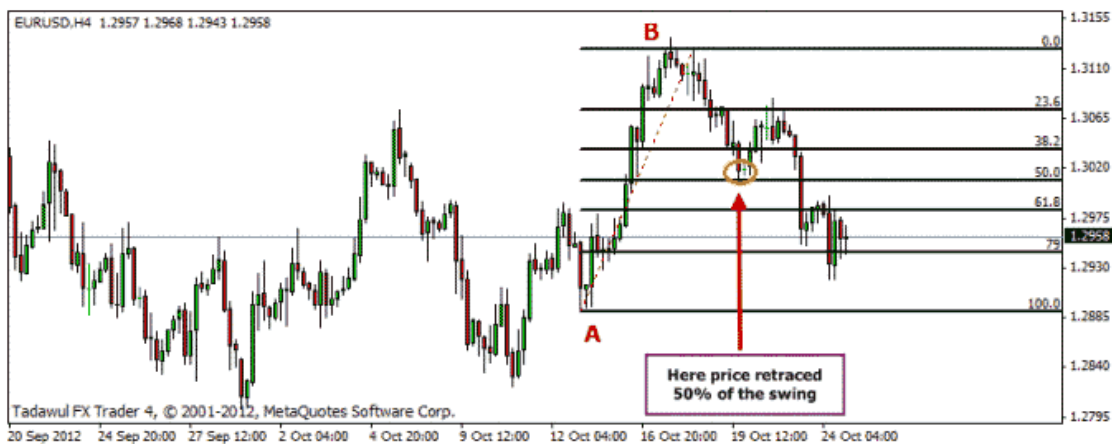
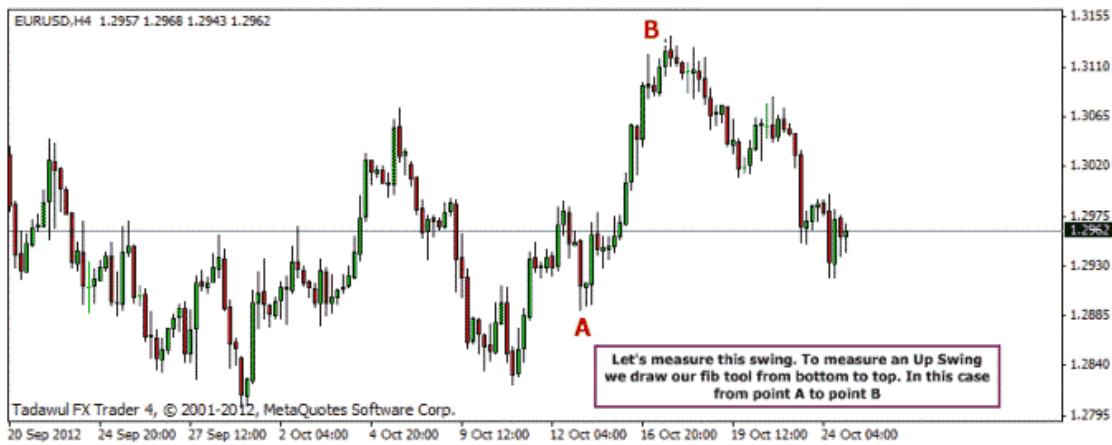
Fibonacci Retracements

Lots of traders look at Fibonacci retracements in order to find a potential trading entry. They rely on a tool and make decisions based on it. Some traders think that support or resistance can be created because of a Fibonacci level. RTM traders, however, know the laws of Supply & Demand. We do not believe that support and resistance are created from a Fibonacci level, therefore most of the traders here do not use the Fibonacci retracement as an entry signal. It is just a measurement tool not a magic entry producing machine, and if used should only be in confluence with Supply/Demand levels.

How to calculate the Fibonacci Retracement?

I could make a very long article just talking about "how to calculate a Fibonacci Retracement" manually but I honestly think that it is useless because most of the actual trading platforms have a Fibonacci Tool incorporated in there software. The tool will automatically calculate everything for you . You will only need to select the swing points that you would like to measure. The Fib Tool can be used on any chart and on any TimeFrame.

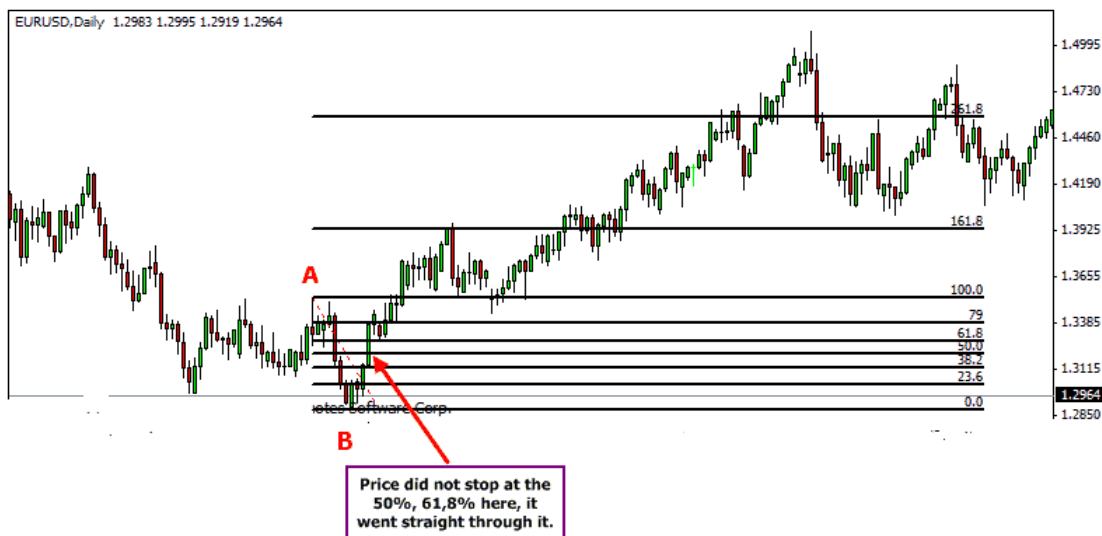
Let's take a look at the picture bellow for an example.



When Fibonacci Fails....

Do you remember when I said that Fibonacci was just a measurement tool? Well be aware that a Fibonacci level can fail; price will not always reverse at the Fibonacci golden ratio. This proves again that price reversal occurs because of the big orders that are left at the Supply & Demand levels and not because of a Fib Level.

Look at the picture below to see a failed Fib level.



Fib Extention:

Fibonacci extensions are also a part of the Fib Retracement Tool. The extensions are in fact the levels that are drawn beyond the standard 100% level. They are used by a lot of traders to find Target Points. The most used levels are 161,8% , 261,8% and 423,6% . For me extensions are just the same as retracement level; they are all about measurements not about entry or exit signals...

You can use it if you like to, to add confluence to your analysis.

In order to know where the extensions are for a particular swing point, draw the fib tool in the opposite way as the retracement tool. In this case you would measure a bullish swing from High to low and a bearish swing from low to high.

Below is an example on a price chart.



Fib Expansion

The Fibonacci Expansion tool is also one that is available on MT4. It is generally used to measure potential target points. While Fib Retracements show measurement of an ABC wave pattern (the swing high (A) , low (B) and the retracement (C).) Fib Expansion will measure and "predict" where wave C will end.

Bellow is an example on how to measure Fib Expansions.

