

The Real Way To Trade Supply And Demand

Hello traders of forex factory

I've wrote this small guide to cut through some of the bs that's floating around on forex factory and the internet in general about how to trade S+D.

the way of trading supply and demand I propose in this book is built on a more conceptually sound basis than the typical ideas proposed in most s=d systems found online, the main idea supply and demand trading is based on is the assumption that there are pending orders left at places where the market has moved up or down is I think highly inaccurate.

Let it be known that I am not a great writer so you may find some mistakes throughout this small book.

If S+D zones have pending orders placed at them by banks or whatever institution you can think of then these order will not move the market.

The reason for this is that pending orders add liquidity to the market.

Liquidity is the ability to buy or sell something without affecting the price by a large amount. Whenever the market moves in one direction it is due to a lack of liquidity, caused by people placing market orders, the exception being stop orders.

If pending orders are placed at these zones the when the market returns to them it should consolidate for a

while as institution's can now mask the trades there placing due to there being liquidity present.

Quite a few times you may of seen this happening if your a supply and demand trader, but im betting that 7/10 times what you see when the market hits these zones is a quick move away (well that is if the zone works out at all) this can only be achieved due to market orders.

My Way Of Trading Supply And Demand

The way I trade supply and demand and also the way I trade in general is based upon using factual data to make trading decisions.

Facts are unfortunately hard to come by in the world of forex trading.

You know, anytime you draw something on your chart weather it be a trend line, support and resistance level, supply and demand zone Fibonacci grid or anything else ive failed to mention those things don't actually exist in the market, now im not saying they cant be useful or help in decision making but when you first downloaded MT4 or whatever charting platform

They only exist in your head.

A famous trader who s name I cant recall once said that “we dont trade the market we trade our beliefs”

This is very true

Oanda Order book

There are valid arguments against using oanda's orderbook to make trading decisions.

One of them is that it only shows information from traders who are using oanda as their broker which means that it only represents a small portion of the overall market.

This is a fair and very true argument, it does represent only a fraction of the market but at the same time we know that 90% of traders lose money overall so if we have the order placements of lets say 10,000 people we can use that as a proxy for a lot of the traders who are using other trading brokers.

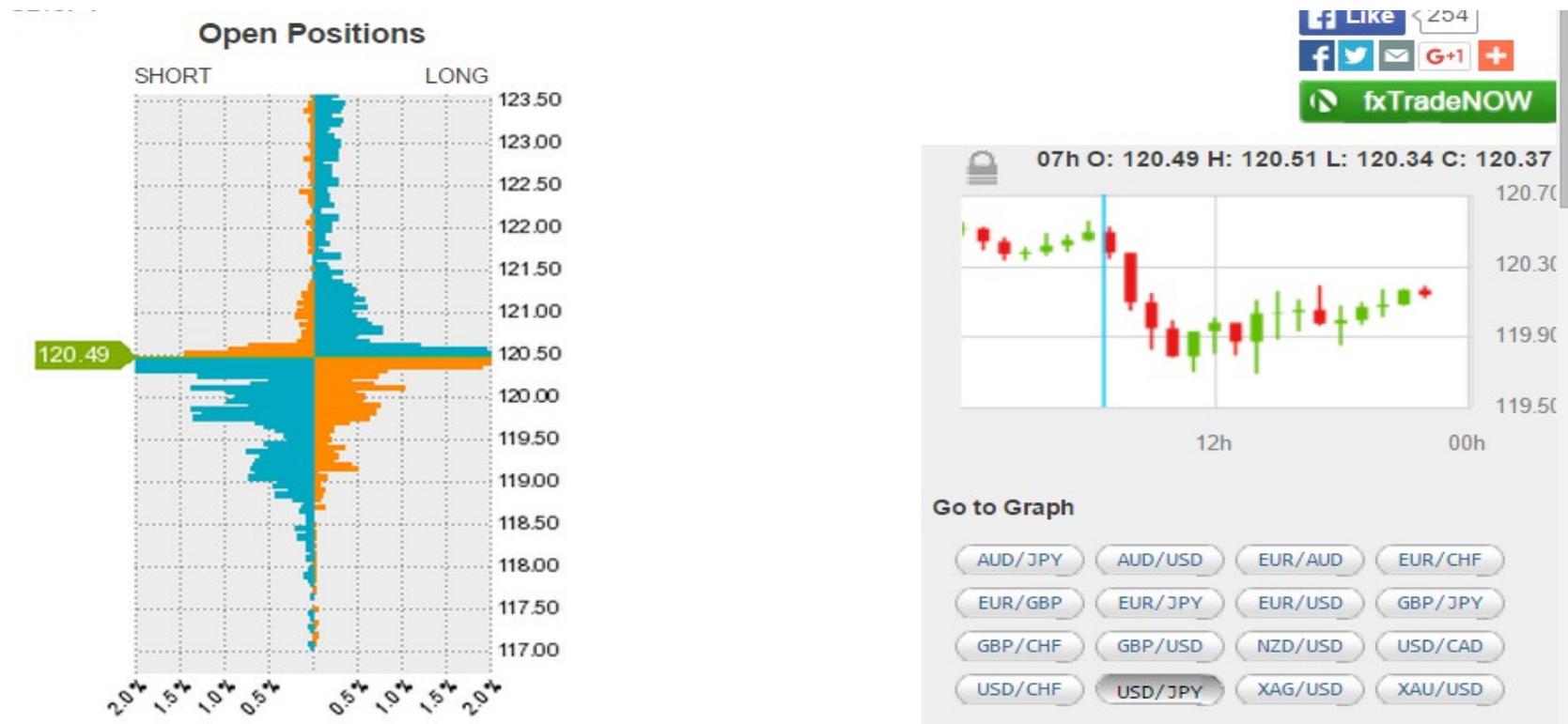
Because if 10,000 people see the same thing happening on their chart and place a trade, who's to say that another 50,000 haven't done exactly the same thing.

And at least by using oanda's order book we have actual data about the market which we can use in our decision making, this is much better than the fallacy and assumptions most trading strategies are based off.

The second problem is that there's a 15 minute delay for the orders updating, so unfortunately if your someone who likes to trade lower time frames then this strategy may be hard to implement

if you downloaded my first book then by now you should be familiar with oandas order book.

You might have noticed in my last book I talked about using the open positions graph to find true supply and demand areas, but there's another strategy we can use with the information found in the graph to the left of the open positions, yes I'm talking about the open orders graph.



Notice that there is a large amount of people in short positions between the 119.70-119.80 level.

These traders are currently at a loss on their trades as evidenced by the bars being coloured blue. We can gather two pieces of information from this graph.

The first, is that these traders must of placed their trades the last time the market was at the 119.70 area, which is you can see on the chart on the previous page.

The second is the decisions these traders are likely to make in the future are going to be determined by fear.

Imagine yourself in their situation, you've placed a trade without a stop and almost instantly the market shoots up, your trade is at a loss and it stays at a loss for the next 30 hours!! what do you think these traders are going to do if the market returns to the point where they placed their trade?

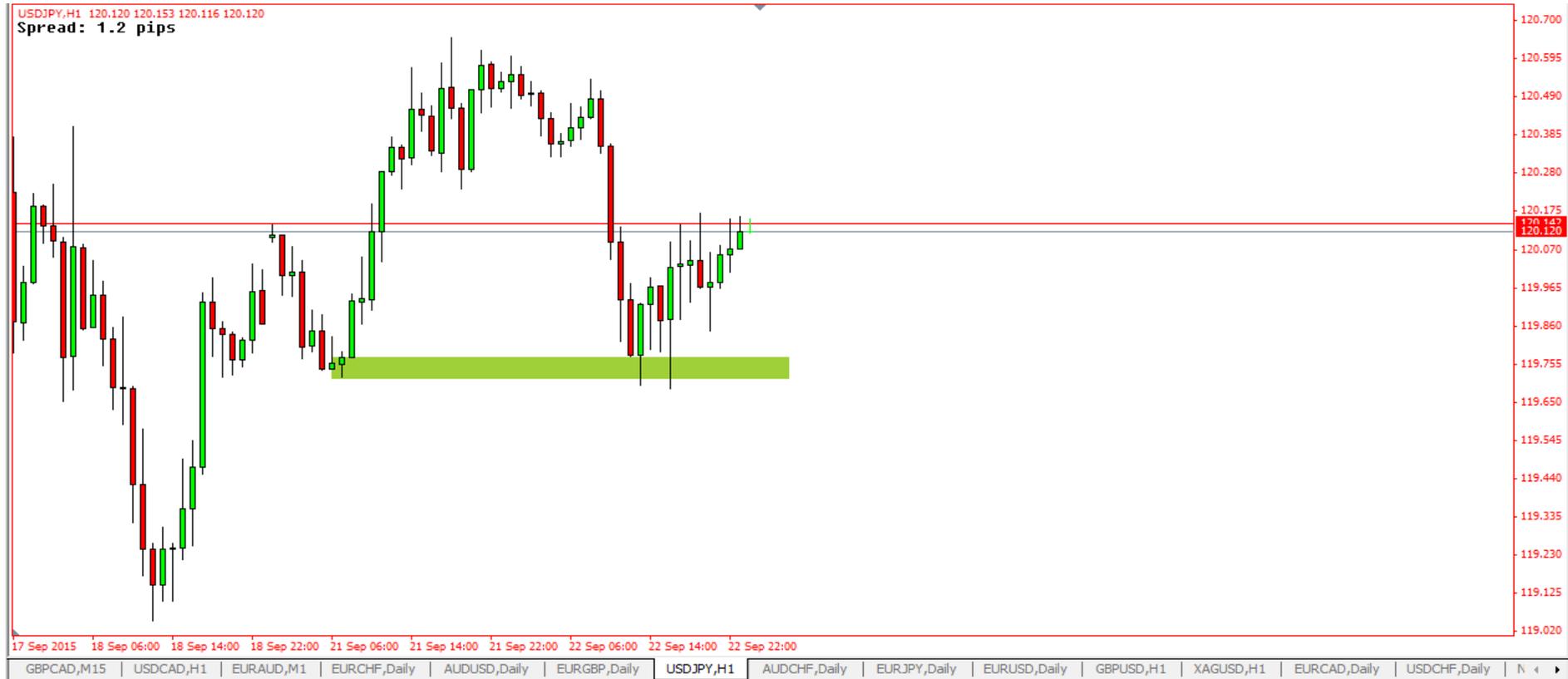
Their going to close the position out of fear that the market might move higher again.

When they close the trade what order do they have to use?

A buy order

What do buy orders do?

Push the market higher right.



You can see the market returns to the area and proceeds to move higher, we knew that there were people trapped here before the market hit this area, we didn't know if the market was going to turn when it hit this area but we we did know something was likely to happen because there were a lot of people trapped in their trade here.

A Couple Of Things To Remember

There are two really important things to keep in mind if your going to trade this method.

The first is time.

You see the longer the amount of time that traders are in a losing position the more eager they become to close their their trade.

So if you have placed a trade and a couple of hour's later the market hasn't really moved anywhere then your level of anxiety is far lower than someone who has placed a trade and just after placing it the market has gone 600pips against them.

The longer the amount of time someone has been in a losing position the more likely they are to close their trade

The second thing to keep in mind is you want to see the positions accumulated at one maybe two prices, you don't want to try and trade areas that are across a large price range.

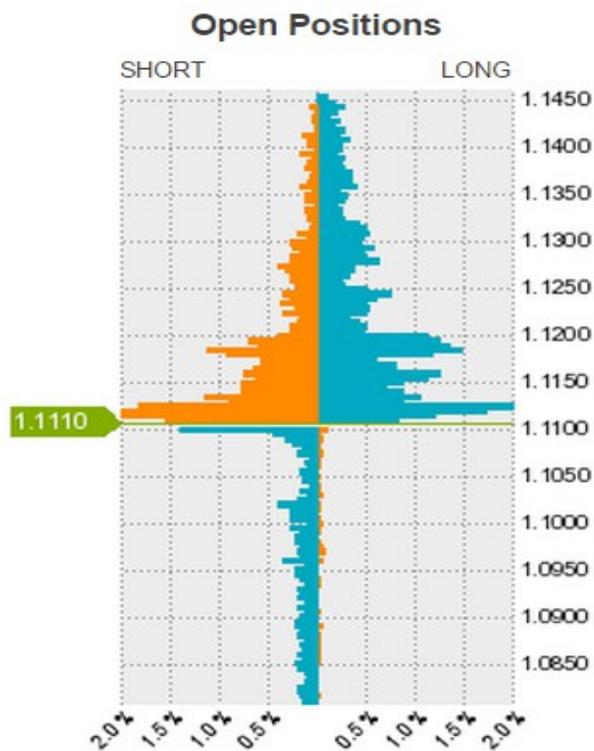
Like if you look at the graph on the previous page you can see that there are people who are short between the 119.00 level and the 119.50 level but there is no definitive place where you can say most of these people are short from, its all kind of spread out over a 500 pip range.

So try not to trade these kinds of levels, look for the ones which you can clearly see there is a high concentration of people long or short from.

A Few Examples

I'm going to run through a couple of examples demonstrating this method.

I want to direct your attention to the long positions just above the 1.1150 price on the graph.



You can see that there is a collection of traders who have been in a losing trade for quite some time I think the last time the market was at that price was around 19-20 hours ago.

So we know that when the market returns to this level its likely that these people are going to close their trade, so what we do now is go onto MT4 and mark a rectangle around that area



You can see that when the market returned to this price zone it began to fall.

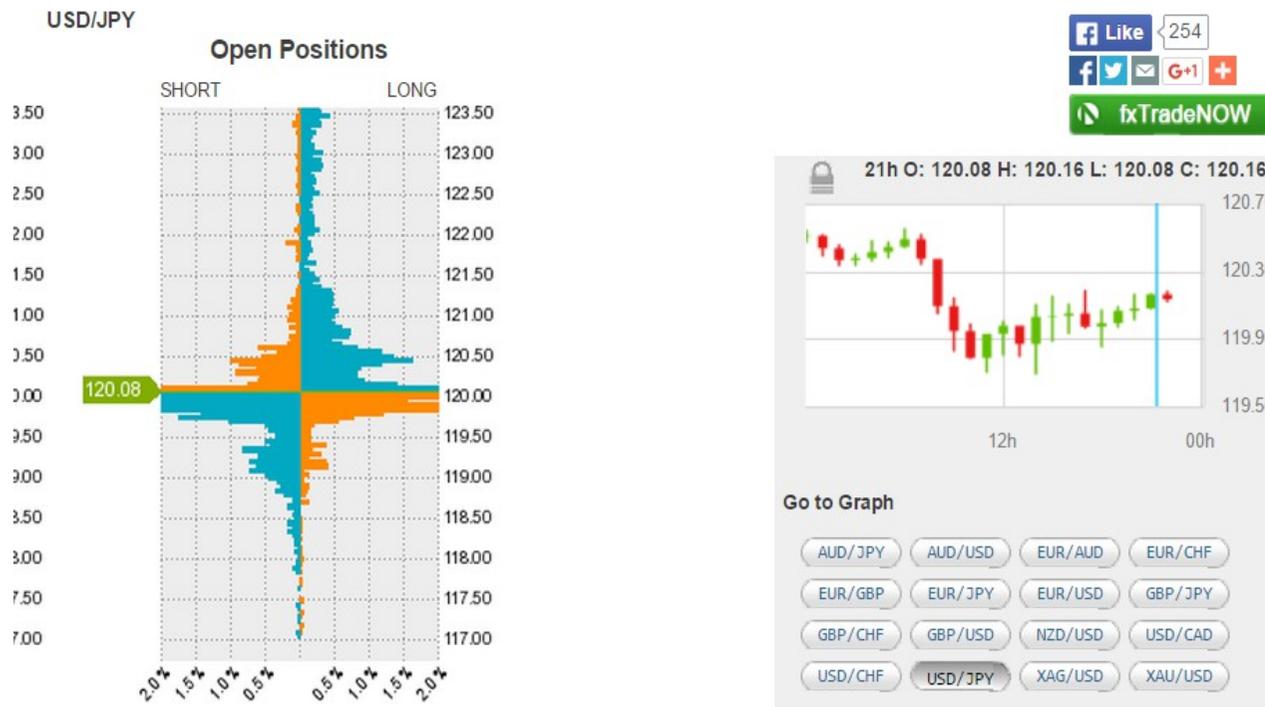
Now i'm not saying that the only reason the market fell here was because of these traders exiting their trade's, but any other reason we come up with is just theory and guessing.

You could say the market fell here because it was a resistance level but there's no way to confirm that, there isn't any data behind that theory.

Its just a line that you've drawn on your chart which you think will do something when the market returns, same as any other technical tool really.

Example 2

Take a look at this .



This is a snapshot of usd/jpy orders on the 23 September.

You can see that there is a high concentration of people trapped short at the 120.50 area.

So if we go on to our charts we should be able to identify what they did to get trapped short



Here I have marked the bit of market structure where these traders are trapped short from.

We can see that this candle has a wick on it, which means at some point during the time this candle was forming it would of looked quite bullish so I assume that the traders who trapped in these long positions are the reactive type.

You know the type who just see the market start to move quickly and jump in to a position out of their fear of missing out on what they think is potential profits .

Another thing just to note is, when you see a large bullish or bearish candle which has a wick on it there is guaranteed to be traders trapped in their trades from the length of the wick, just thought I'd mention that if someone wants to look into it more.

Okay cracking on then.

So far we have identified that there are a portion of traders trapped in long positions roughly around the 120.50 level.



We know what decisions they made which got them trapped and we also know that they have been at a loss for a reasonably long amount of time, all we need to do now is mark the area on our charts and look for some kind of structure we can use as an entry trigger.

Now you can clearly see the market moves up into the area pretty strongly then proceeds to move lower.

There are two ways you could trade this.

One would be to use a pending order at the zone which to be honest I don't really recommend because the size of the areas and the price range they encompass aren't exact but if you do decide to trade them like that then just make sure you keep a close watch on the market in the event that things begin to change.

The second way to trade them would be to use candlestick patterns as an entry trigger.

This can be done by using a lower time frame, what I would look for is an engulfing candle which in size is bigger than the other candles so in other words the engulfing candle wants to be significant compared to the other candles around it, instead of something like a small candle which only just gets engulfed by a candle a bit bigger than it.

You can use pin bars as an entry trigger if you like but I'm not the biggest fan of them so I tend not to use them.

This is what happened later on.

USDJPY,H1 119.521 119.521 119.383 119.441

Spread: 0.2 pips



! 1 Sep 2015 21 Sep 22:00 22 Sep 06:00 22 Sep 14:00 22 Sep 22:00 23 Sep 06:00 23 Sep 14:00 23 Sep 22:00 24 Sep 06:00 24 Sep 14:00

119.441
119.473

119.340

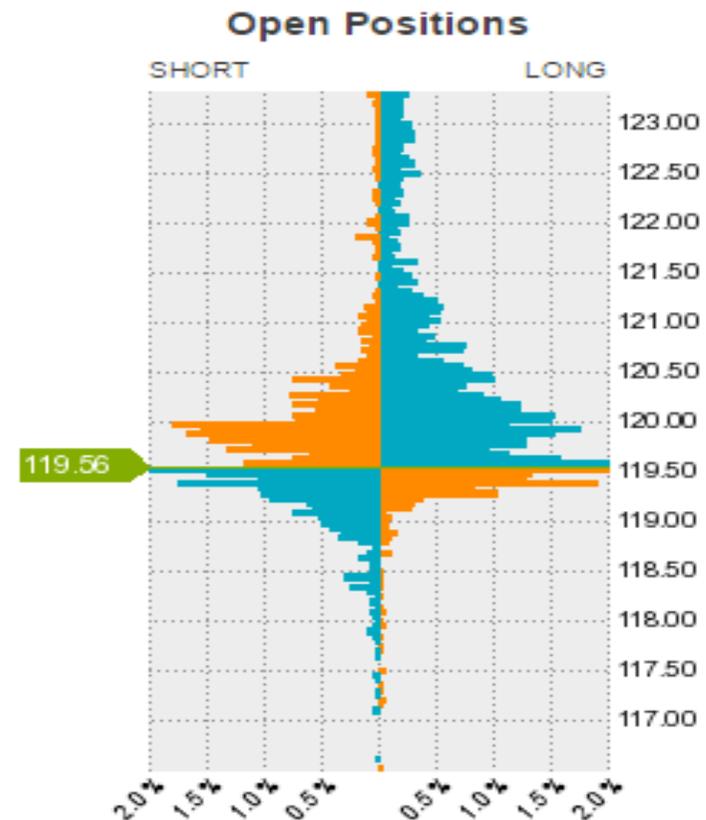
Finding historic supply and demand zones

As I mentioned earlier people who trade supply and demand often draw zones from past price history.

They draw areas that could be weeks old or even a year old and try and trade these areas when the market returns to them. Most of the time these areas tend not to work, and the reason for that is because you have no idea if there is any orders there which could move the market.

To combat this we again use can order graph to see which areas contain potential market force in them.

Lets take a look at the graph again



USDJPY,H1 119.296 119.307 119.237 119.286

Spread: 0.2 pips



On this chart I have marked all the zones based on the data provided on oandas graph.

The green zones show where the highest amount of people who are trapped in a losing position are located.

The blue zones show where there are indeed people trapped but not a significant amount.

One of the rules of typical S+D trading is that the stronger the move away from a price level the stronger that level tends to be.

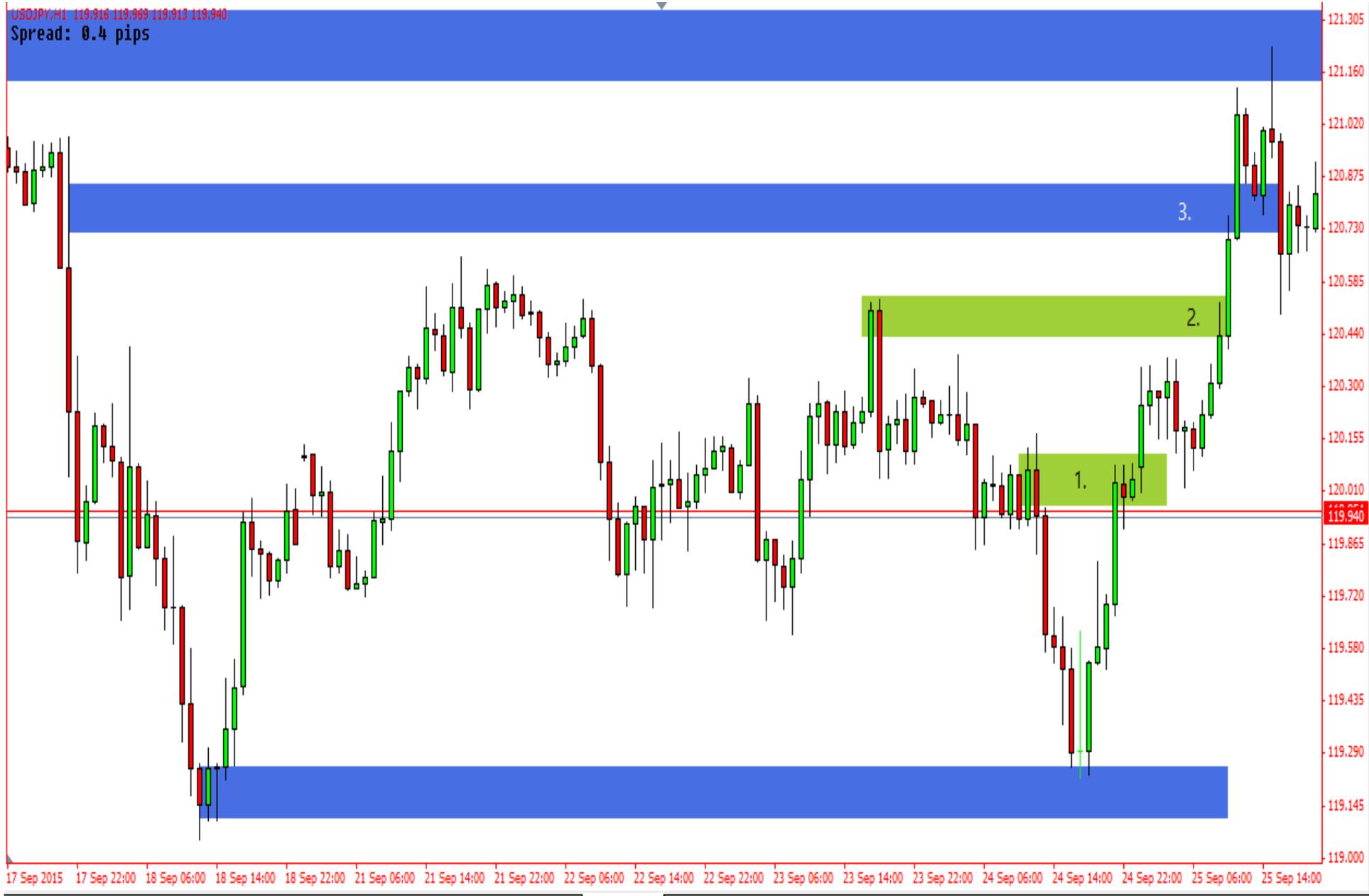
If you trade supply and demand I gaurentee that at some you have placed a trade at a level which has a really strong move away from it with the idea that the market will return to this point and react very strongly to it, you believe this because that's what you have been told right.

But instead of a strong move away what you get is small pause maybe consisting of a few candlesticks and then the market just blows through the level wiping out your stop loss in the process.

By using the order book we can get a rough approximation of how strong a level might be, im not guaranteeing that this is an exact method in the sense that zones which don t contain a lot of trapped traders will not move the market, many additional things come into play such as time, if the market moves into one of these zones at a time when liquidity is low and there generally isn't much activity in the market, then they do have the potential to cause movement.

USDJPY, H1 119.916 119.969 119.913 119.940

Spread: 0.4 pips



17 Sep 2015 17 Sep 22:00 18 Sep 06:00 18 Sep 14:00 18 Sep 22:00 21 Sep 06:00 21 Sep 14:00 21 Sep 22:00 22 Sep 06:00 22 Sep 14:00 22 Sep 22:00 23 Sep 06:00 23 Sep 14:00 23 Sep 22:00 24 Sep 06:00 24 Sep 14:00 24 Sep 22:00 25 Sep 06:00 25 Sep 14:00

You can see that three of these zone did not work out and like I said this is not a method that you can expect to use and not have losing trades, this will happen no matter what trading method you use.

One way to avoid this is by using engulfing candles as a confirmation entry.

Lets look at how the market reacted when it hit these three zones.



USDJPY/M5 119.900 119.900 119.864 119.870

Spread: 0.4 pips



These images highlight what I was talking about earlier.

You need the engulfing candle to be significant in relation to the rest of the structure.

In the first zone you can see that it got engulfed, but I personally wouldn't consider that a proper engulf, the second zone also contains an engulfing candle, but again its only marginally bigger than the bullish candle its engulfing and also has a small wick on it which means that somebody was buying.

What I would want to see is a large bullish candle get engulfed by large bearish candle.

Like in these two images.

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M1 M5 M15 M30 H1 H4 D1 W1 MN



This turn is from the the second example we looked at back in the beginning of the book.

Notice that this engulf is far bigger than what we saw in the initial example.

Also look at the candles its engulfing, they themselves are quite large.



To understand why this is important we must look at how the orders get placed into the market.

I want you to look at the consolidation before the up move.

What happening here is buy orders and sell orders are matched with one another, eventually the buy orders consume the sell orders which means the market has to move higher to fill the remaining orders.

So the market moves up then we begin see some hammer candlesticks so these remaining orders are now being filled. Then we see another rather big bullish candle which means more buy orders have entered the market and consumed the sell orders.

But the market only manages to move to the top of the highs of the hammer candles before getting engulfed back lower this means one thing

it confirms that there are sellers present around this structure, if there went then the bullish candle seen after the hammer candle's would continue higher until it found sufficient sell orders.



USDJPY,M5 120.087 120.090 120.049 120.052
Spread: 0.3 pips

3.

120.052

119.985

We see the same thing happen here, the market moves up just misses the area, then moves up into the area to then get engulfed back down, this is what I mean by a significant engulf, we get a large bullish candle followed by a big bearish engulfing candle.

Summary

Hopefully this small guide has shown you a better way to trade supply and demand, unfortunately this method should only be traded on USD/JPY and EUR/USD the reason being that these two currencies are the one's which oanda traders trade the most so the other currencies do not comprise of enough data for us to make decent decisions.

in the coming weeks I will show you how to distinguish between which supply and demand areas have a higher probability of working out without using oandas graph, the reasons that some areas work and some don't are based on the psychology of the people in the market coupled with what they intent to do which can be seen in the price structure.

A zone which has a strong move away is not more likely to turn price than a zone with a weak move away , it all depends on where the zone is in relation to the trend and the time frame of which the zone in question can be seen.

Thanks for reading look forward to your questions and ideas.

