Finding Supply And Demand Zones That WORK

Introduction

Supply and demand trading remains one of the most popular trading strategies 6 years after it first came to prominence.

In that time there has been very few changes in how people actually trade supply and demand zones. If you go online and search for supply and demand trading strategies you'll see that for the most part there is very little difference between how different traders trade supply and demand zones.

The differences can be anything like the time-frame used to trade the zones or the entry method used to actually enter trades at supply and demand zones themselves.

I think I speak for the majority of traders when I say that the current most popular method of trading supply and demand zones promoted by Sam Seiden does not result in consistent trading profits. Traders are under the impression that the reason why they're not making consistent profits from trading supply and demand zones is because of something they're doing wrong when trading the zones.

The reality is the reason why people trading supply and demand zones are not making consistent profits, is because the understanding they have of been given about how to find supply and demand zones that are going to result in successful trades is incorrect.

With this book, I'll give you the understanding you need to find supply and demand zones that are likely to give you profitable trades. Most of the information you have picked up on finding zones which are likely to work is wrong, things like the size of the move away from a zone and the strength of a move into a zone are virtually meaningless and focusing on them is not going to help you achieve better results.

What I'm going to do is break down the mechanics of what causes supply and demand zones to form along with showing you the different reasons why the market will return to the zones once they have been created.

In addition to this, you'll see that the length of time it takes for the market to return to a supply or demand zone is the most important factor in knowing weather the zone will work out successfully or not.

Hope you enjoy the book.

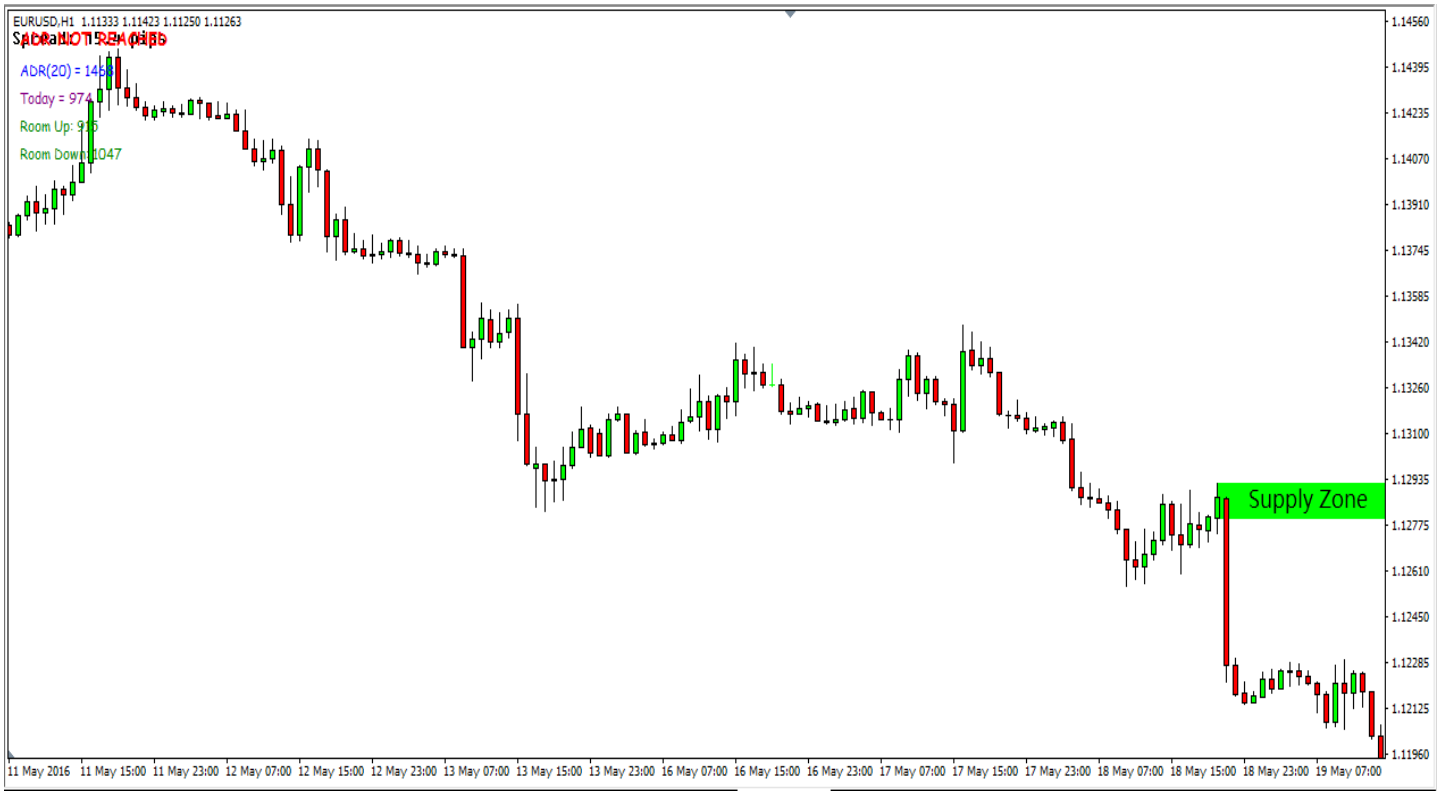
How To Determine If A Supply Or Demand Zone Is Going To Result In A Successful Trade

I think the best way to start the book, is by revealing to you what the most important factor is in trying to identify if a supply or demand zone is going to result in a successful trade.

In one article on my site "The Essential Guide To Supply And Demand Trading" I dispel many of the myths purported by the people who teach supply and demand trading on the internet.

One of the main concepts which supply and demand traders teach, is the idea that the strength of a zone is determined by how long the market has been away from the zone itself. The teachers say *"The longer the time the market has spent away from the zone, the stronger the zone becomes"*

This concept is the number one reason why most supply and demand traders are not making consistent money trading supply and demand zones. The reason why is because it causes people to favour placing trades at zones which formed a long time ago over ones that have been created recently, when it's the zones which have formed recently that have the best chance of providing people with successful trades.



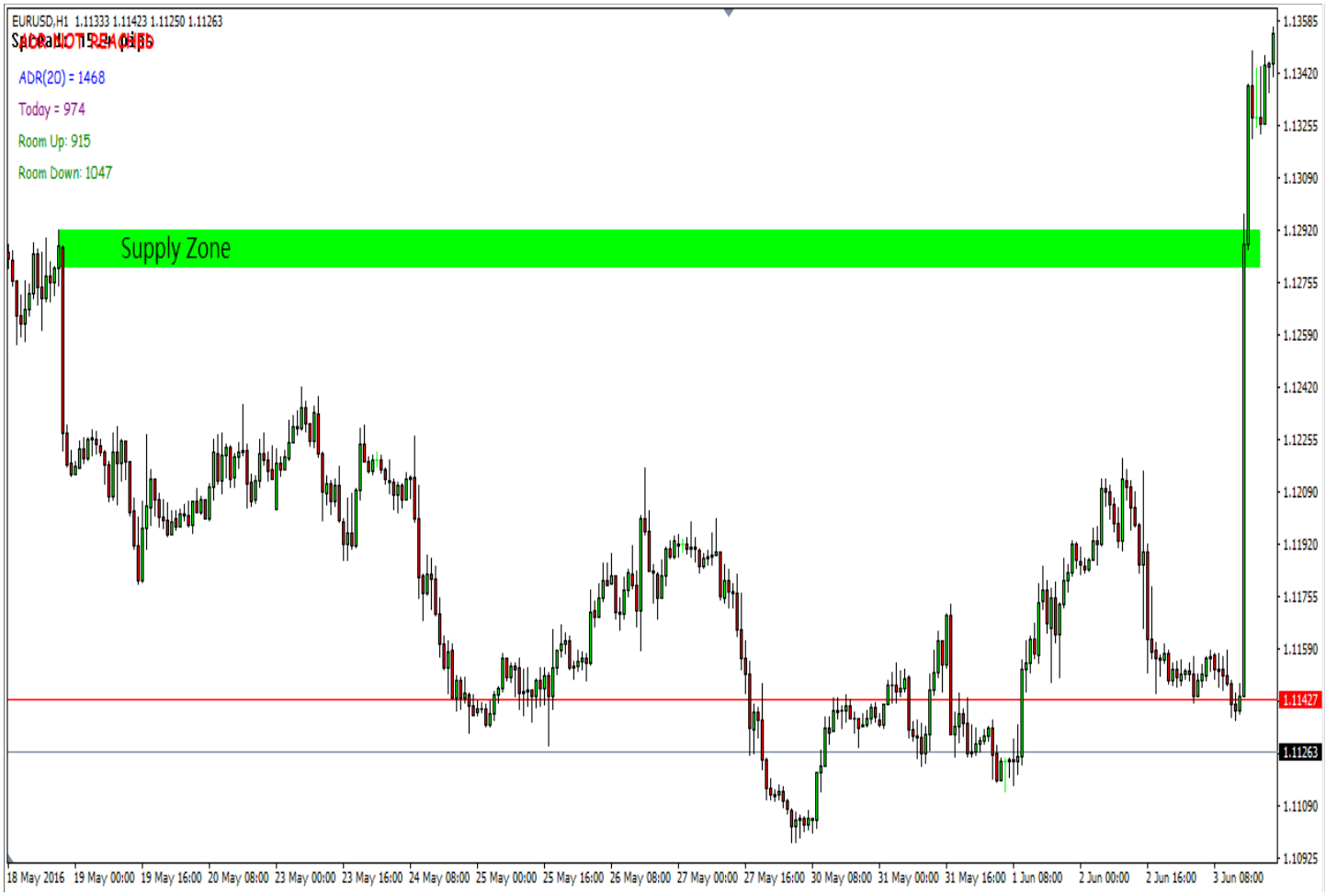
The image on the previous page shows a supply zone which formed during a large swing lower on the 1 hour chart of EUR/USD.

This supply zone formed due to the bank traders placing sell trades, we can confirm this to be fact because the market continued to fall after the zone formed.

Now the only reason why the market would come back to this supply zone, is because the banks were not able to get all of their sell trades placed when the price dropped creating the zone.

If they wanted to get these remaining sell trades placed they'll make the price move up into the zone soon after it has been created, they will not wait for the price to drop a large distance before making it come back to the zone as it would negate the point of placing the sell trade in the first place.

The banks want to place the sell trade at the zone to make money from the price falling, so why make the price drop by a large amount before causing it to come all the back to the area just to get their sell trade placed ?



Look what happens when the market returns to the supply zone.

It breaks straight through it without even the slightest hint of stopping or pausing.

The funny thing about this supply zone is it actually meets the criteria most supply and traders use to gauge whether a zone has a high probability of working out successfully or not.

It has a large drop away, the strength of the move into the zone is very strong and the zone has not been revisited for a long duration of time. All of these things are supposed to signal the zone has a high probability of working out successfully, yet as we can see, the market is easily able to break through the zone upon it's return.

This is because the banks did not have any sell trades left which they needed to get placed at the zone, if they did we would have seen the market return to the zone soon after it formed instead of it taking 11 days.

Another point to make is the fact the supply zone had been created by the bank traders placing sell trades.

When the banks have placed a trade into the market, they'll stop any attempt by the market to break past the point where their trade has been placed because it could jeopardize their position and cause them to lose money.

What this means is, even if the banks did not have any more sell trades to get placed at the supply zone when it formed, a move up towards the zone soon after it was created would cause the banks to enter the market and place more sell trades just to stop the price from breaking through the high of zone and causing the sell trades which they already have placed to go into a loss.

However, the thing to remember is the only time the banks will only come into the market and protect the trades they have placed is if they have not already closed the trade.

In our example, the sell trade the banks had placed that created the supply zone had been closed by the time the market returned to the zone 11 days later.

This means there's no point in the banks coming in to the market and placing more sell trades to stop the market from breaking past the point where their sell trade was placed as their trade has been closed.

Here's another supply zone which formed a little earlier in the same down-move as the supply zone seen in the previous image.

This supply zone also formed because of the banks placing sell trades.

You can see how the market returned to this supply zone soon after it formed as opposed to taking a long time like we saw in the previous example.

It takes a total of 26 hours for the market to return to this supply zone whilst it took 283 hours for the market to return to the supply zone seen in the other example.

The reason why the market fell upon hitting this zone was not because the banks had sell trades left which they needed to fill, it was because they had to come into the market and protect the sell trades they placed which created the supply zone in the first place.

The spike into this zone was caused by the NFP news being released. When the news came out lots of traders placed buy trades which caused the price to move into the supply zone. When it enters the zone the banks come into the market and place more sell trades to purposely push the price back down.

Had they not done this the market would have kept moving up through the zone and caused the sell trades the bank traders had placed which created the zone to begin losing money.

Here's another example of a demand zone which would be said to have a high chance of causing the market to reverse using the typical rules surrounding supply and demand trading.

Like the other example the zone above has a strong move away and we can see from the image below that not only does it take the market a long time to return to the zone, the move into the zone is very strong as well.

You can see from the image that when the market returns to the zone it just falls right through it.

This zone would have probably resulted in a successful trade had the market returned to it soon after it formed. If the price had continued to drop on the first retracement we see after the market shot up creating the zone, it's likely the market would have reversed upon hitting the zone because we know if the banks have trades left which they need to get placed they'll make the market return to a supply or demand zones quickly as opposed to taking a long time.

How Long Should It Take For The Market To Return To A Supply Or Demand Zone ?

So now you know why the time it takes for the market to return to a supply or demand zone is the most important thing to take into account when trading supply and demand zones, the question is how long should it actually take the market to return to the zones ?

If you have read some of the articles on my site you'll see I say the market should return to supply and demand zones found the 1 hour chart within 24 hours of them being created.

This isn't a cold hard rule, if the market returns to a zone 25 – 27 hours after it has been created then it's fine for trading but as a guideline I would say that the market can definitely not return to a 1 hour zone 30 hours after it has been created.

The only exception is for zones which form when the banks are gearing up for a big reversal. In these situations the market can come back to the zones 2 weeks after they have formed but no more than that.

Supply and demand zones which form on the daily must have the market return to them 30 days after they have been created. This goes for all daily supply and demand zones no matter where they form in the market.

Understanding Why The Market Returns To Supply And Demand Zones

Now you understand why the market must return to supply and demand zones quickly as opposed to taking a long time, the next thing we need to look at is why the market has a tendency to return to supply and demand zones once they have formed.

If you currently trade supply and demand zones, you'll know the reason why the market is said to return to the zones after they've been created, is because the banks were not able to get all of their trades placed when the zone formed.

To get their remaining trades placed, the banks leave pending orders at the zones so when the market returns to the zone, the trades which they were not able to get placed initially are executed, and the market moves back in the direction to which the zone was created.

Now I don't want to get into a discussion as to why this idea of pending orders being placed at the zones is incorrect (read this article for a more detailed answer) what I will say is the reason why the market comes back to supply and demand zones is not always because the banks have trades left which they need to get placed.

There are lots of zones which form as a result of the banks taking profits off trades they already have placed. The reason why the market comes back to these zones, is because the banks are taking additional profits off their trades, not because they are getting unfilled trades placed which they couldn't get placed when the zone formed.

Additionally there are other zones which have formed because of the banks placing trades.

The reason why the market has a tendency to return to these zone isn't always because the banks have not been able to get all of their trades placed (although a lot of the times this will be the case) it's because when the banks are placing multiple trades into the market they will usually try to get any additional trades placed at prices which they already have existing trades placed at.

Knowing what has caused a supply or demand zone to form is the only way to figure out the reason why the market should return it and reverse.

Lets now take a look at the two types of supply and demand zone that can form in the market and I'll show you the differences which come with trading each type of zone.

Profit Taking Supply And Demand Zones

The first type of supply and demand zone we are going to look at are zones created by the banks taking profits.

Profit taking zones will always form counter to the direction of the current trend. If the market was in a downtrend the banks profit taking will form demand zones near the swing lows. In up-trends, the profit taking will always form supply zones close to the swing highs.

The image above shows two supply zones which formed due to the banks taking profits off buy trades placed earlier in the move up.

How do I know these supply zones have been created by profit taking ?

One because the price had been moving up prior to these zones forming and two because the price continues to move up once the market has revisited the zones themselves.

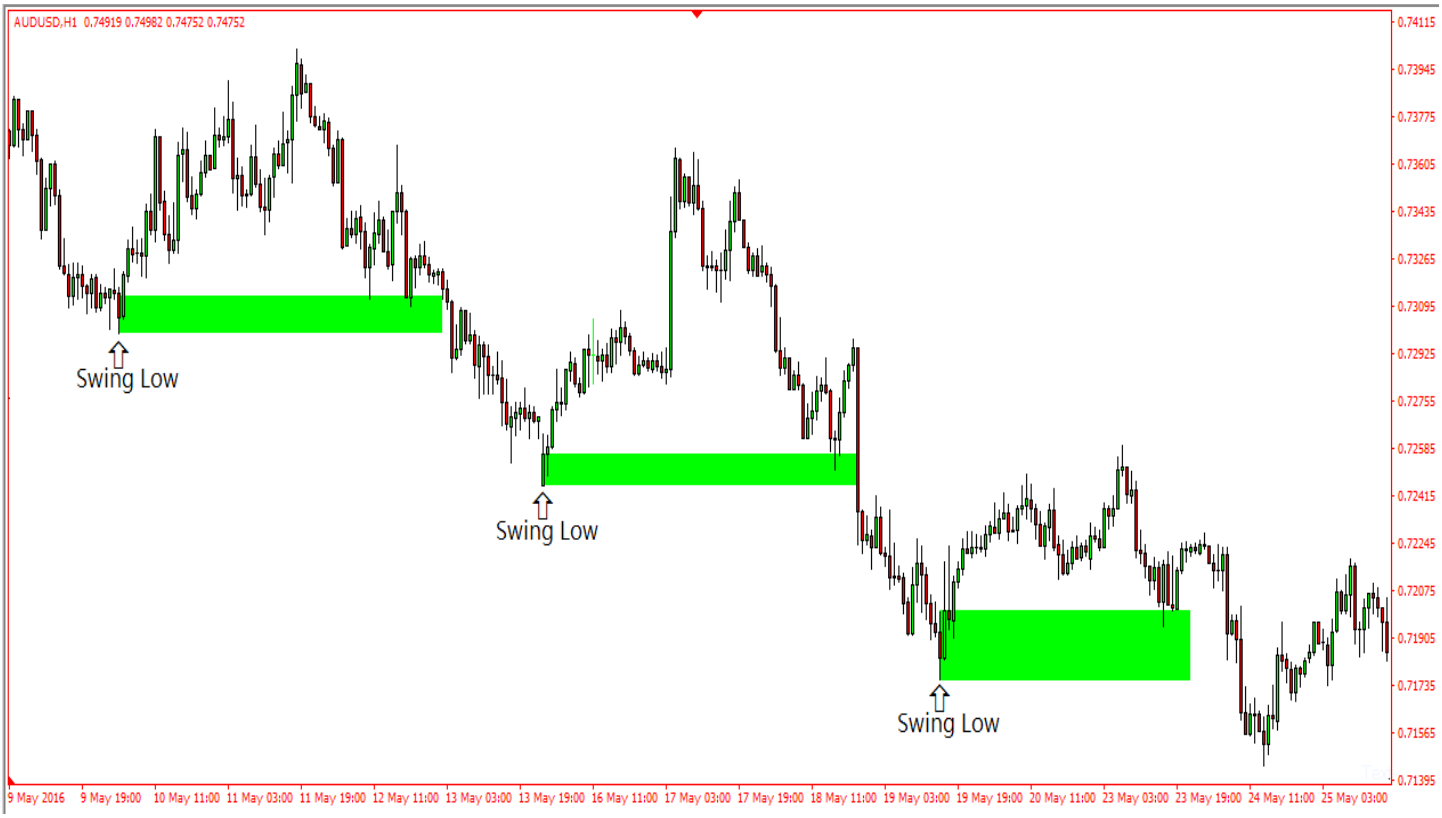
The reason why the market revisits these supply zones is because the banks were not able to take the required amount of profit off their long trades when the market was rising due to the fact not enough buy orders were coming into the market at that time.

When the banks decide to take profits off their long trades the buy orders currently coming into the market from other traders placing buy trades are consumed and the price starts to fall, which creates the supply zones we can see in the image.

The banks then use the profits which they have made by taking profits off their buy trade to get more buy trades placed in the direction of the up-move which is what causes the price to stop falling and move back up into the supply zone.

The move up makes a large number of traders place buy trades as they believe the price is going to continue rising. Once the market enters the supply zone created by the banks first bout of profit taking, they take profits again using the new buy orders that have come into the market from traders buying on the move up into the zone.

The price then drops again and either the same process will repeat itself or the market will continue moving higher and break through the supply zone.



Here are three demand zones which were created by the banks taking profits off sell trades.

Notice how all the zones form from swing lows and how they all generate a small reaction upon being hit.

The same process is taking place with these demand zones as was taking place with the supply zones in the previous image.

The banks decide to take some profits off their sell trades, this causes the price to begin moving up which in turn causes a percentage of traders to place buy trades.

The banks then place more sell trades using the buy orders generated from the traders buying because of the move up. When the banks sell trades have been placed, the price falls, which causes people to place sell trades. When the price has fallen back to the point where the banks took profits off their sell trades (the demand zone) they take the rest of the profits which they were unable to initially due to there not being enough sell orders coming into the market.

Their profit taking causes a small reaction to take place upon the market hitting the demand zone and the price is able to rise for a short amount of time before dropping below the swing low made by the banks first deciding to take profits off their trades.

There are two problems which come with trading supply and demand zones that are created by the banks taking profits.....

The first, and probably main problem you'll encounter, is the reaction the supply or demand zone will generate upon the market returning to it is likely to be small because the banks ultimately still want the market to continue moving in the direction of the trend once they have taken the required amount of profits off their trades.

This means if you take a trade based on a zone which has been created due to the bank traders taking profits, you must keep your expectations of how much money you'll make low as it will only be a matter of time before the price turns and begins moving back in the direction of the trend.

The second problem with trading zones created by profit taking, is there's a much higher chance of the market breaking past the high or low of the zone before reversing than there is of a zone created because of the bank traders placing trades.

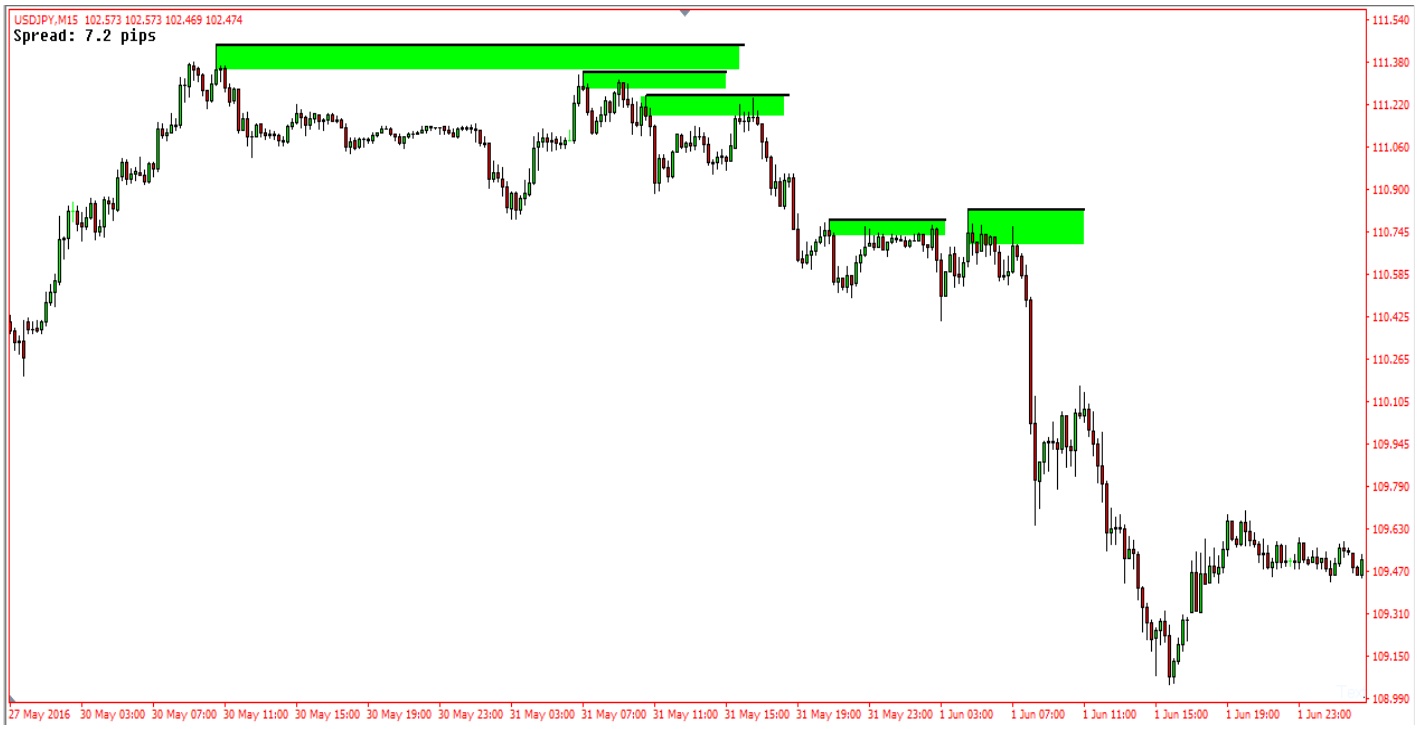
The reason why is because when the banks have placed a trade and caused a supply or demand zone to form, they have a great interest in not letting the market break the point where they have placed their trade as it has the potential to cause their trade to start losing money.

With zones that have been created by profit taking, there isn't really any need for the banks to take profits before the market reaches the high or low because they're not going to lose any money from doing so, which means you'll quite frequently see the price spike above the high or below the low of the supply or demand zone before reversing,

This can be really annoying as the most likely to place to put your stop loss when trading supply and demand zones is the high or low of the zone. To combat this I suggest you either don't trade zones created by profit taking or you add a few pips to the stop-loss when placing a trade at a supply or demand zone caused by the banks taking profits off their trades.

Supply And Demand Zones Created By The Banks Placing Trades

Now we're going to take a look at supply and demand zones which form due to the bank traders placing trades.



Here's an image of 5 supply zones which formed because of the bank traders placing sell trades into the market.

We know these zones were created by the banks placing trades because the market kept on falling once they had been created.

The reason why the market will return to zones created by the banks placing trades is similar to the reason why the market comes back to zones created by them taking profits.

Most of the time when the banks are getting trades placed, there will not be enough buy or sell orders coming into the market for them to get their entire trade placed. This means they must manipulate the price in order to drum up enough buy or sell orders to get their remaining trades placed.

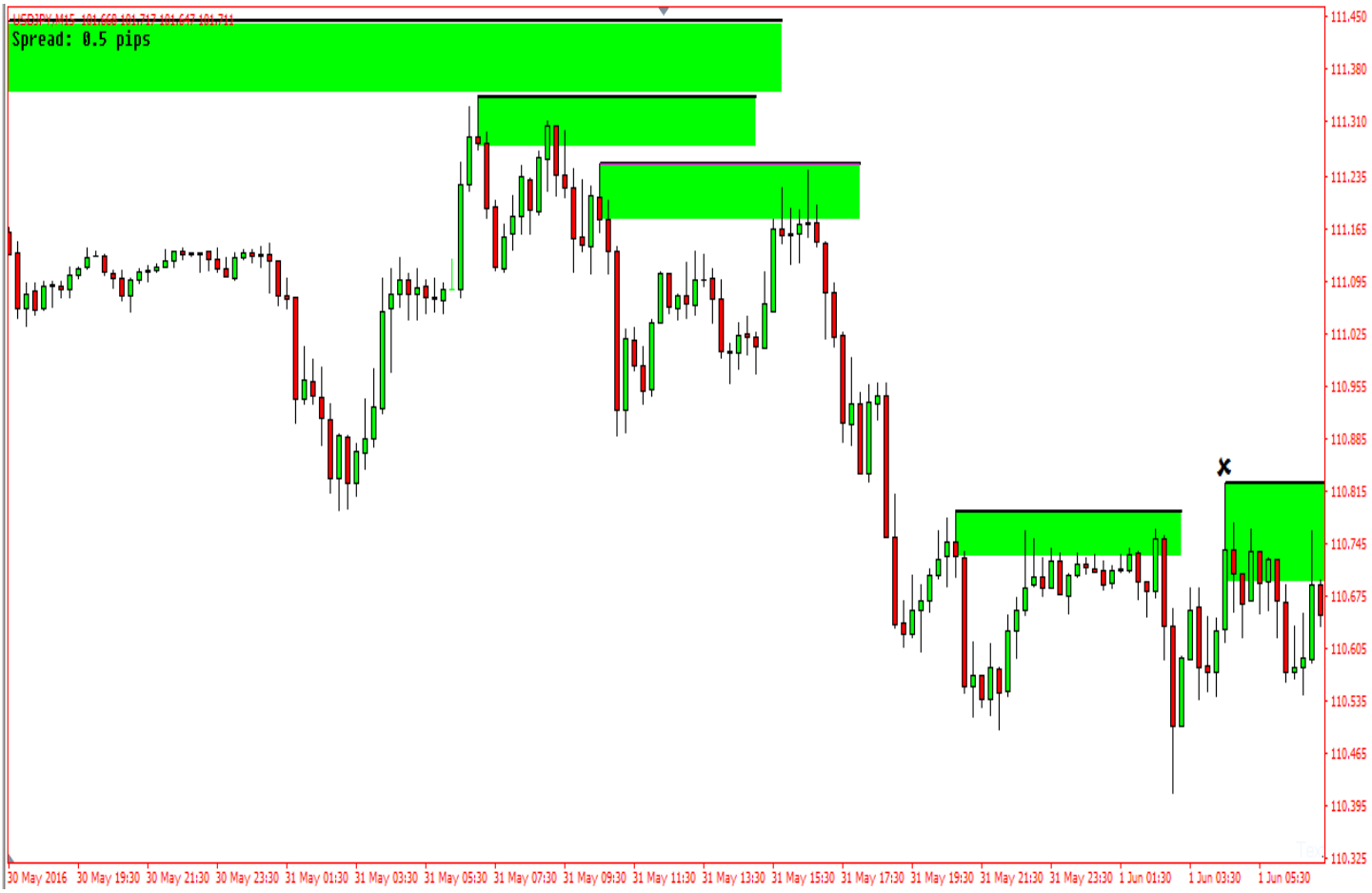
In our example the banks had placed sell trades which is what caused the supply zones to form. The problem was the banks were unable to get all of their sell trades placed due to the fact there were not enough buy orders coming into the market at the time of them wanting to place their sell trade.

Now the banks must make the price move back up in order to get people to place buy trades which will give them the buy orders they need to get their reaming sell trades placed.

They do this by taking a little bit of profit off the sell trades which they have already got placed. When they take profits the price begins to move up which causes retail traders to begin placing buy trades.

When the market comes back up into the supply zone the banks use the buy orders that have been generated from the move higher to place the sell trades they were unable to place when the zone was created initially.

The critical thing you need to understand about supply and demand zones that have been created by the banks placing trades, is the point where the banks have placed their original trade which created the supply or demand zone, cannot be broken when the market returns to the zone.



If you look at the supply zones above and you'll notice the market does not break the high of the zone upon it's return.

The reason why the high cannot be broken (at least by a large distance) is because the banks do not want to jeopardize the sell trade they placed which caused the supply zone to form in the first place.

If the market was to break above the high it would cause the sell trade which they already have placed to go into a loss and could make enough traders enter the market and place buy trades that the price would be pushed far higher than what the bank traders want, which could potentially mean they'd have to close their sell trade at a loss and lose a large amount of money.

It's important for you to know that when I 'break' I mean the market fails to close above the high for supply zones and below the low for demand zones. It's okay for the market to spike a small distance past the high of the zone for supply zones or the low of the zone for demand zones, but it must not close above or below it.

If it does the zone becomes invalid and it tells us the banks have either not placed any trades at the zone or any trades they did place at the zone have

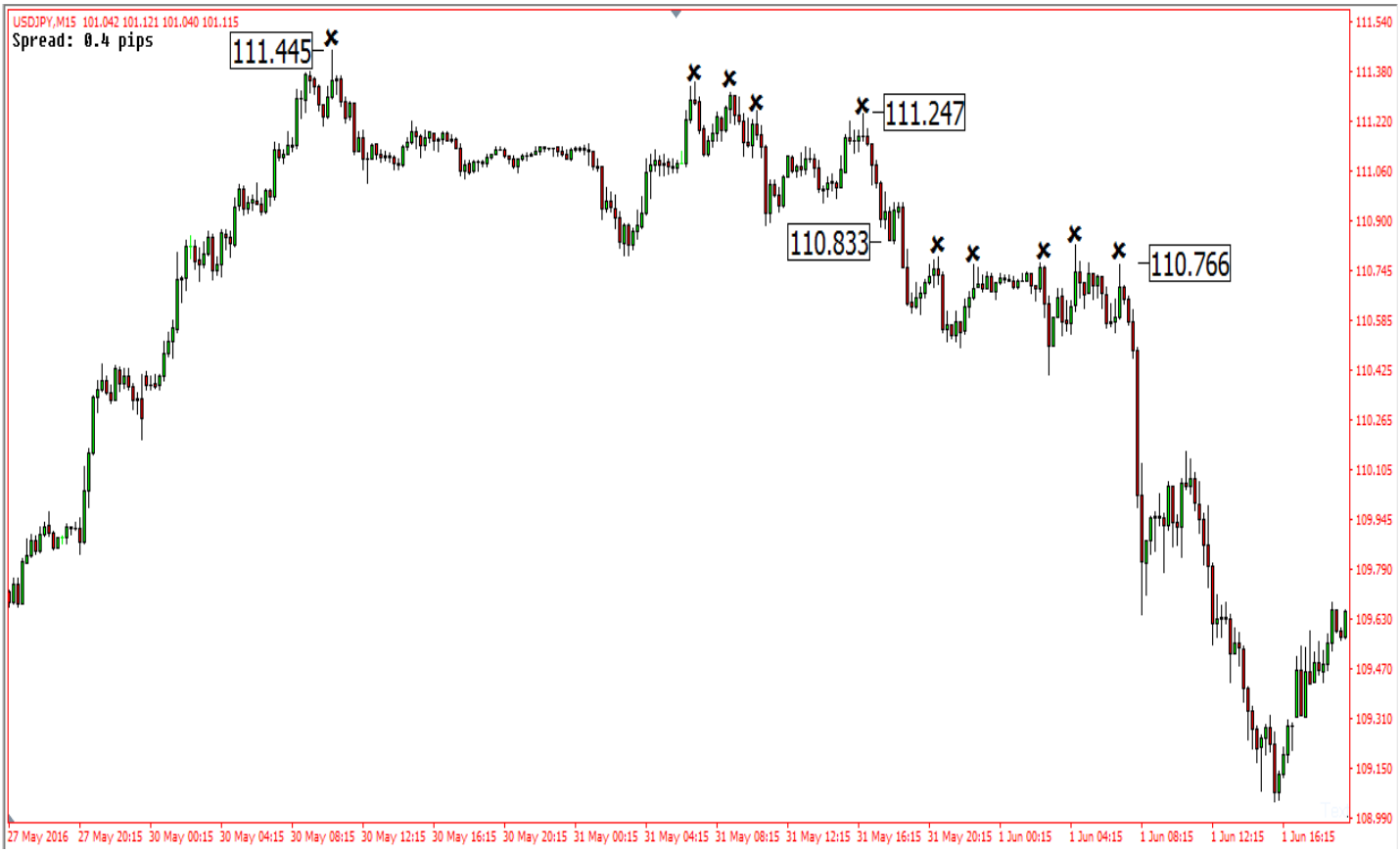
already been closed.

The last point I want to make about supply and demand zones created by the banks placing trades, is the reason the market comes back to the zones is not always because the banks have trades left to fill which they were unable to get placed when the zone formed initially.

This is something which I spend a great deal of time explaining in my [“How The Large Institutions Operate In The Forex Market Book”] When the banks are getting trades placed in anticipation of a reversal occurring, they'll try to get as many of their trades as possible placed at the same price.

I don't mean at the exact same price, but at prices which are close to each other.

The banks do this because it makes it easier for them to calculate how many buy or sell orders they'll need to take profits off their trades.



This is the image we looked at previously only I've removed the supply zones and instead marked all the points where the bank traders had placed their sell trades.

You can see there are two main price ranges where the banks were placing their sell trades before the reversal took got underway.

Their first set of trades were placed between the 111.247 - 111.445 price range (which is only around 20 pips) and their second set of trades were placed between the 110.766 - 110.833 price range which is only 6 pips.

This clearly shows how the banks get their trades placed similar prices.

The supply zones which formed due to the banks placing trades had the market return to them because the banks wanted to get their trades placed at a similar price, not because there weren't enough buy orders coming into the market when they wanted to get their trade placed initially.

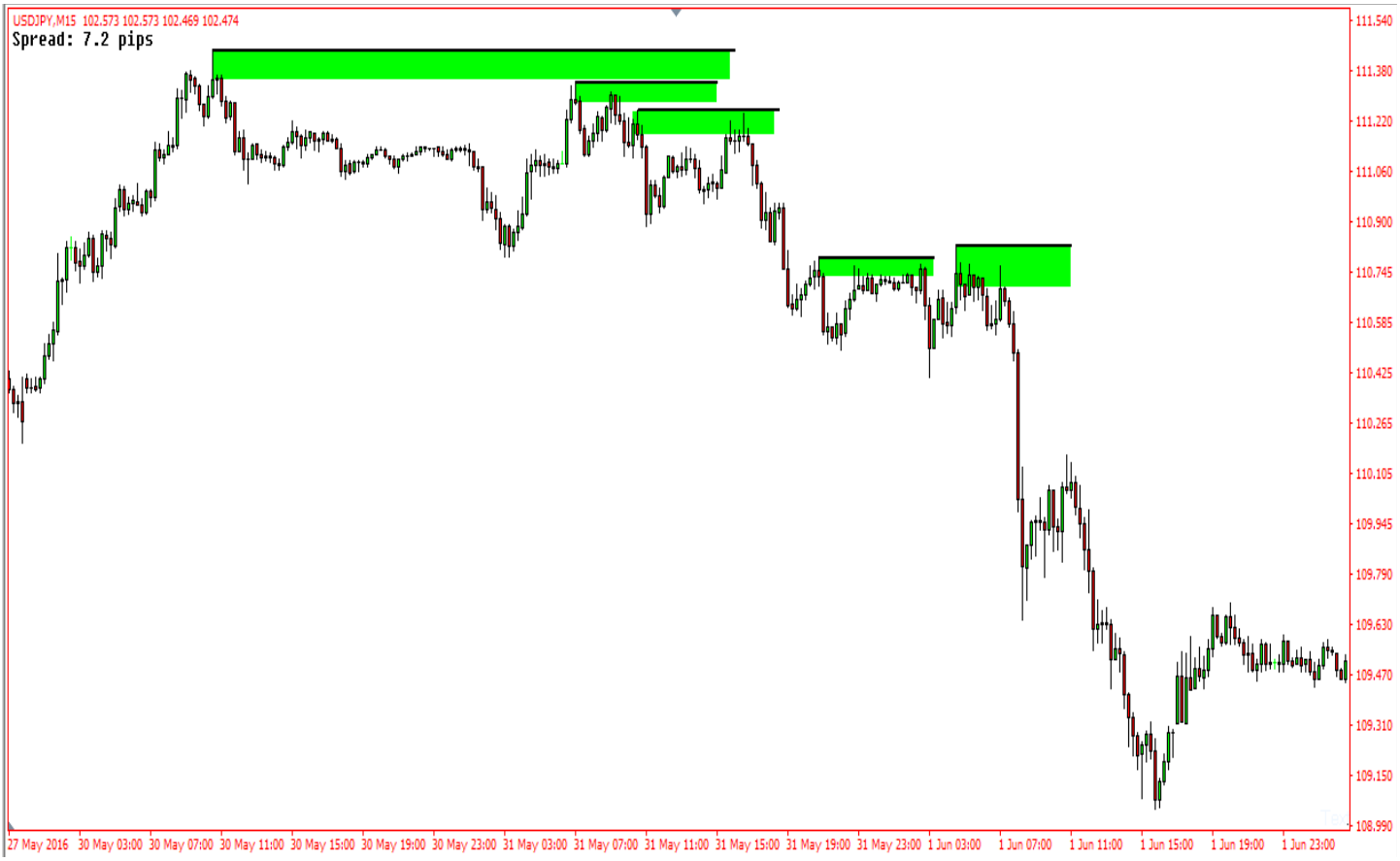
The only time you'll see the banks get their trades placed at similar prices is when they're setting up a major reversal to take place.

In times when the market is trending, the majority of the supply and demand zones that form will have the market come back to them not because the banks want to get their trades placed at a similar price, but because they have been unable to get all of their trades placed due to a lack of buy or sell orders coming into the market.

Understanding The Market Condition's Which Supply And Demand Zones Work Best In

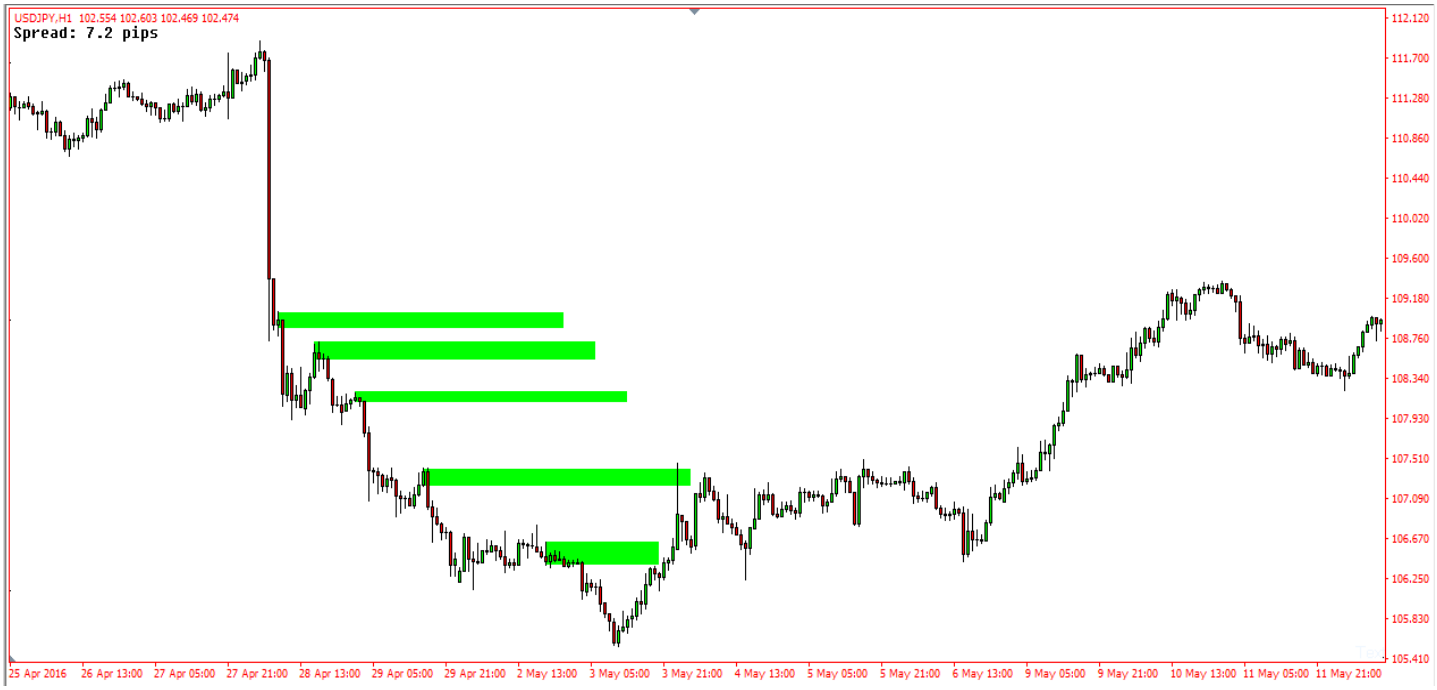
Something which I believe is integral to trading the forex markets profitably no matter what strategy you use, is knowing the market condition's your trading method works best in.

Supply and demand trading is a versatile strategy because it can give you successful trades in a variety of different market conditions. The problem is traders don't understand that the market condition's taking place play a large part in weather the supply and demand zones will work out successfully or not.



Here's the image we looked at earlier of some supply zones caused by the banks placing trades. We can see from this image how most of the supply zones which caused the market to reverse formed at the beginning of the swing-down.

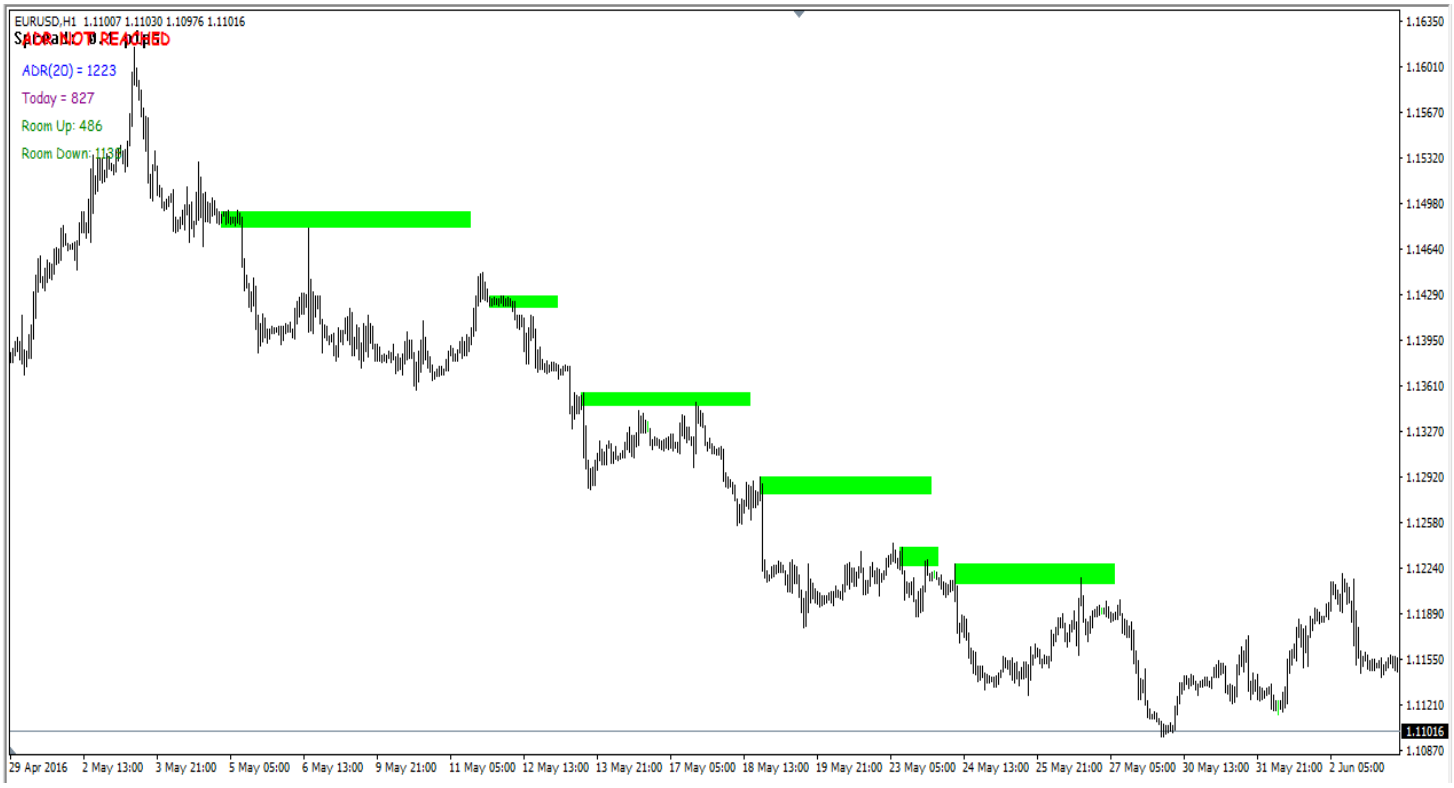
If you go and look on your charts you'll see most of the supply zones which formed later on in this move down didn't work out successfully because the market was unable to return to them in time.



In this image we can see how the supply zones started to form towards the end of a swing lower instead of at the beginning like we saw in the previous image.

None of these zones would have resulted in you having a successful trade if you had traded them because the market was unable to return to the zones soon after they were created.

By the time the market does return to the zones the trend is in a retracement phase and the trades which the banks placed that caused the zones to form have been closed, which means there is no point in them entering the market and placing more sell trades to stop the price from breaking above the zone.



Here we have another 6 supply zones which formed when the price was falling.

Hopefully you can see there is a clear difference between the way the market was falling in the previous images and the image on the previous page.

The down-move seen on the previous page has the market return to the supply zones through the whole duration of the move down and we also see the supply zones form in a consistent manner, by that I mean the zones are spread out quite evenly instead of only being found at the beginning of the move down or at the end like we saw in the other images.

In my article "The Two Types Of Supply And Demand Zone" I talk about the differences between zones which are constructed from a (rally – base – drop/ drop – base – rally) to zones which form from a (rally – base – rally / drop – base – drop)

I said how the zones which form from the market making a rally – base – drop or a drop – base – rally have a much higher chance of causing the market to reverse than the zones which form from a rally – base – rally / drop – base – drop.

In the image you can see there is a drop – base – drop zone that formed on the 12 May.

The reason this zone worked out successfully is because of the type of down-move that was taking place.

Most of the time rally – base – rally / drop – base – drop zones WILL NOT result in you having successful trades no matter which type of market conditions you find them in. The only reason we see one working out successfully in the example is because of the type of down-move that was taking place at that time.

Because it's not possible (at least not yet) to figure out how the market is going to move once a reversal takes place, it means we cannot determine which type of supply or demand zones are likely to work better in what market conditions.

Due to this I think it's best if you focus mainly on taking trades from demand zones which form from a drop – base – rally and supply zones which form from a rally – base – drop.

These are the types of zone that'll work no matter what market conditions are taking place. If you stick to only taking trades at these zones, supply and demand trading should be profitable for you in all market condition's.

The Reason Why Traders Believe Old Supply Zones Cause The Market To Reverse

A big problem with supply and demand traders is this belief that old zones have the capability to cause the market to reverse upon being hit.

Sam Seiden (the main S + D trading guru for those who don't know) says the reason why the market reverses at old supply and demand zones and all supply and demand zones in general, is because the banks have old pending orders placed at these zones due to the fact they were not able to get their whole trade executed when the zone formed.

Now even though this isn't true, (not for old zones at least) people still believe in this idea that old zones can cause reversals because when they look at their charts, they can see the price has reversed at the point where an old supply and demand zone formed in the past, therefore they assume the reason why the market reversed was because of the old supply and demand zone.

Here's an image of some supply and demand zones which formed on the daily chart of EUR/USD.

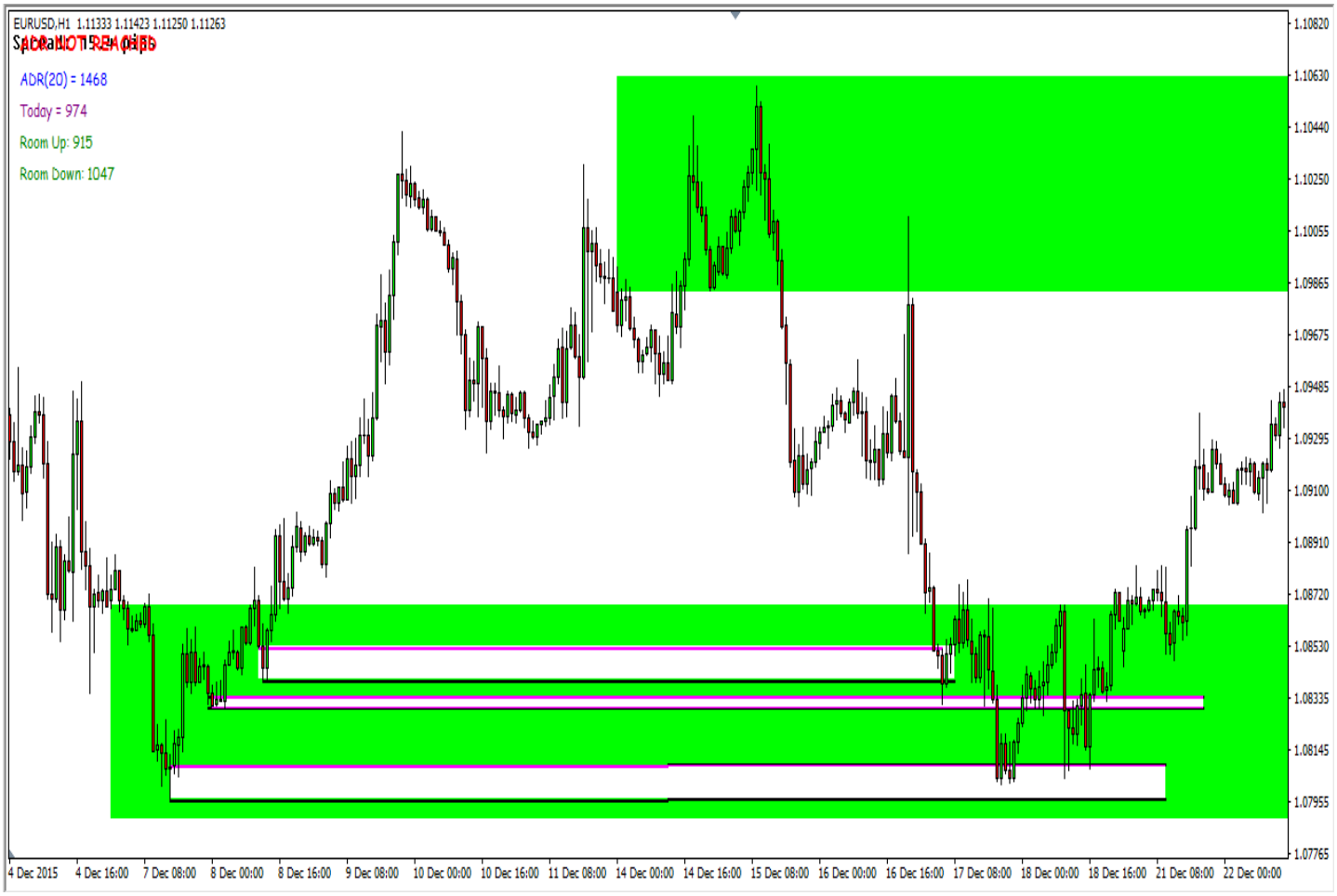
Remember what I said earlier about how the market will return to supply and demand zones quickly if the banks have got trades left which they were unable to place when the zone was forming ?

This rule of the market returning to the zones quickly is relative for the time-frame the supply or demand zone has formed on.

In other words, quickly for a zone on the 1 hour chart is 24 hours whereas quickly for a zone on the daily chart is 30 days.

Looking at the image you can see the market comes back to the majority of the daily supply and demand zones within a month of them being created, which means these zones were not considered to be old by the time the market returned to them.

Now contained inside these daily zones will be supply and demand zones on the 1 hour chart. These 1 hour zones are considered to be old by the time the market has revisited the daily zone they have formed in.



If we take a look inside the daily demand zone we can see there are three 1 hour demand zones.

The demand zone found at the bottom of the image was the one which eventually caused the market to reverse but the zone found above it also managed to generated a small reaction once it was hit.

The reason this 1 hour zone caused the market to reverse, even though it's considered to be an old zone, is because it's found inside a daily demand zone, not because old zones themselves have the ability to cause a reversal upon being hit.

This is why people sometimes see the market reverse at old zones. They don't realize the old supply or demand zone is contained within a supply or demand zone on a higher time-frame which is not considered to be old by the time the market has returned to it.

The 1 hour demand zones in the image were old, but the daily demand zone they were inside wasn't, which is why when the market comes back to the zones they have a high chance of causing a reversal to take place.

Take a look at the 1 hour demand zone above.

This zone is considered to be old due to the fact it has taken the market 17 days to return to it.

Typical supply and demand traders would say the reason why the market stopped falling and began retracing was because it encountered the demand zone.

They would see something like this occur and start believing that old supply and demand zones have the potential to cause reversals. If they couldn't, then what caused the market reverse ?

The reality is the demand zone had NOTHING to do with the reason why the market stopped falling and began retracing. The retracement was caused by the banks deciding to take profits off the sell trades they had placed at the swing highs of the move lower.

Their decision to take profits is not based on the fact the market has hit a demand zone, it's based on how many sell orders were coming into the market at the current time.

The banks will only be able to take profits once there is the necessary amount of sell orders in the market. Sometimes the point where enough orders are present is the same point where a supply or demand zone formed in the past.

When the banks take profits using the orders, it looks as though the market has reversed because it hit the demand zone, but really the demand zones played no part in the price reversing, because the banks decision to take profits off their trades was based solely on how many sell orders were entering the market at the time it was falling.

Hopefully this explains the reason why you've probably seen old supply and demand zones cause reversals to take place. Sometimes what you see on the charts is not necessarily the reality of what is taking place. People have this tendency to focus on things which prove their beliefs to be correct instead of being wrong, when traders see the market reverse at old supply and demand zones they automatically think old zones can cause the market to reverse.

When they see an old zone fail to cause a reversal, instead of questioning the concept of “whether old zones can actually cause the market to reverse or not” they blame the structure of the zone itself as being the reason why the price didn't turn.

This holds the traders back from acquiring the understanding they need in order to start making money trading supply and demand zones. If the traders would have known that a lot of the theory they have learned about supply and demand zones is wrong, they would not blame themselves for the failing of the strategy.

Summary

Finally we've reached the end of the book, I hope I've enlightened you on some new concepts and ideas which will make your supply and demand trading more profitable.

Below you'll find a round up of what I believe are the most important points to take away from this book.

Listed below are the main points I want you to take away from this book.

- Supply and demand zones form either because the banks have taken profits off existing trades or because they have placed trades into the market.

- Zones which form at the beginning of reversals have the market return to them because the banks like to get all of their trades placed at a similar price, not because the banks have trades left over which they need to get filled

- Rally – base – drop / drop – base – rally supply and demand zones have a higher chance of causing the market to reverse upon being hit than rally – base – rally / drop – base – drop zones.

- If a supply or demand zone is going to cause a reversal upon being hit, the market must return to the zone quickly. How quickly it must return is dependant on the time-frame which the supply or demand zone has formed on.

  For zones on the 1 hour chart the market must return to the zone within 24 hours of it being created.

  For zones on the daily chart the market revisit the zone within 30 days of it's creation.

- Old supply and demand zones do not cause reversals to take place in the

market. The only time they do is when the zone is found inside a higher time-frame zone which the market is returning to quickly.

- Just because you see the market reverse at the point where an old supply or demand zone has formed does not mean the old zone is the reason why the market has reversed. Most of the time the reason why the market has reversing has nothing to do with the supply or demand zone, it just happens to be chance the decision the banks made which caused the market to reverse has fallen in line with the point where an old supply or demand zone formed.