PRICE ACTION CONCEPTS

<u>Price Action</u>

Price action is the movement of a security's price plotted over time. Price action forms the basis for all technical analysis on any asset's chart. Many short-term traders rely exclusively on price action and the patterns from it to make trading decisions. Technical analysis as a practice is a derivative of price action since it uses past prices in calculations that can then be used to make informed trading decisions.

What Does Price Action Tell You?
Price action can be seen and interpreted using charts that plot prices over time. Traders use different chart compositions to improve their ability to spot and interpret trends, breakouts, and reversals. Many traders use candlestick charts since they help better visualize price movements by displaying the open, high, low, and close values in the context of up or down sessions.

Candlestick patterns are examples of visually interpreted price action.

<u>How to Use It?</u>
Price action is not generally seen as a trading tool like an indicator, but rather the data source off which all the tools are built. Indicators lag, price action leads.

Swing traders and trend traders tend to work most closely with price action, eschewing any fundamental analysis in favor of focusing solely on support and resistance levels to predict movements. Even these traders must pay some attention to additional factors beyond the current price, as the volume of trading and the time periods being used to establish levels all have an impact on the likelihood of their interpretations being accurate. Throughout your trading career you will find which confluence factors you find the most useful to implement in your strategies.

<u>Limitations of Price Action</u>
Interpreting price action is very subjective. You need two participants to have a valid market: one side must be willing to sell and the other must be willing to buy, and each side will have its own reasons to do so.

It's common for two traders to arrive at different conclusions when analyzing the same price action. One trader may see a bearish downtrend, and another might believe that the price action shows a potential near-term turnaround. Of course, the timeframe being used also has a huge influence on what traders see as a stock can have many intraday downtrends while maintaining a higher timeframe uptrend.

The important thing to remember is that trading predictions made using price action on any time scale are speculative. The more tools you can apply to your trading hypothesis to confirm it, the better, this is what traders call confluence. In the end, however, the past price action of a security is no guarantee of future price action. High probability trades are still speculative trades, which means traders take on risks to get access to potential rewards.

Now, let's define some basic price action concepts and shed some light on how to interpret and execute them properly.

<u>Ranges</u>

Ranges are the zones where price consolidates after a time of trending price action. After an expansive move, you start looking for ranges to form.

How to spot them?
1. Wait for the pump/dump to end and then you proceed to:
    a. Mark the first swing high / first swing low
    b. Mark the first swing low / first swing high
        i. This may not be perfect at first, this is why you need to be redrawing them to gain the most confluence
        ii. The range must be established where the majority of swing highs and lows are; you are looking for the majority of points of contact
2. The EQ (equilibrium level) mark also must make sense
    a. How does price behave around it?
    b. Is it an area of reaction?
        i. Candles closing above the EQ = bullish
   ii. Candles closing below the EQ = bearish
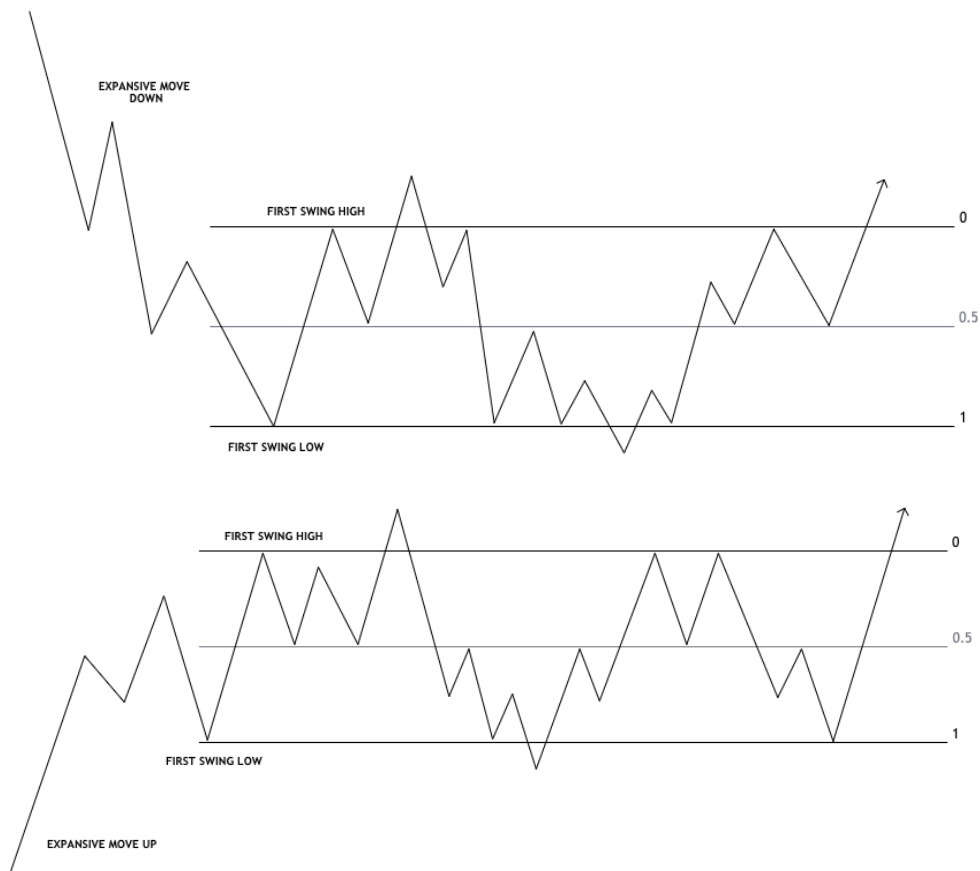
*As you can see**, there is no golden rule when it comes to drawing ranges**. Most of the times you'll find yourself redrawing them until you find what makes the most sense.*

Flipping Ranges Setup

For both macro and micro ranges, their ceilings/bottoms represent areas of high interest to the market. This is where the Flipping Ranges Setup comes to light. It's basically a S/R flip you can spot by extending the levels of previously broken ranges.

To consider:
- Time + Space is key
  - Just as in a S/R flip, the more time and space elapses before a retest = higher probabilities to succeed
- This can also happen near to HTF levels (adding confluence is key)
- Untested SSR often offer high-probability setups
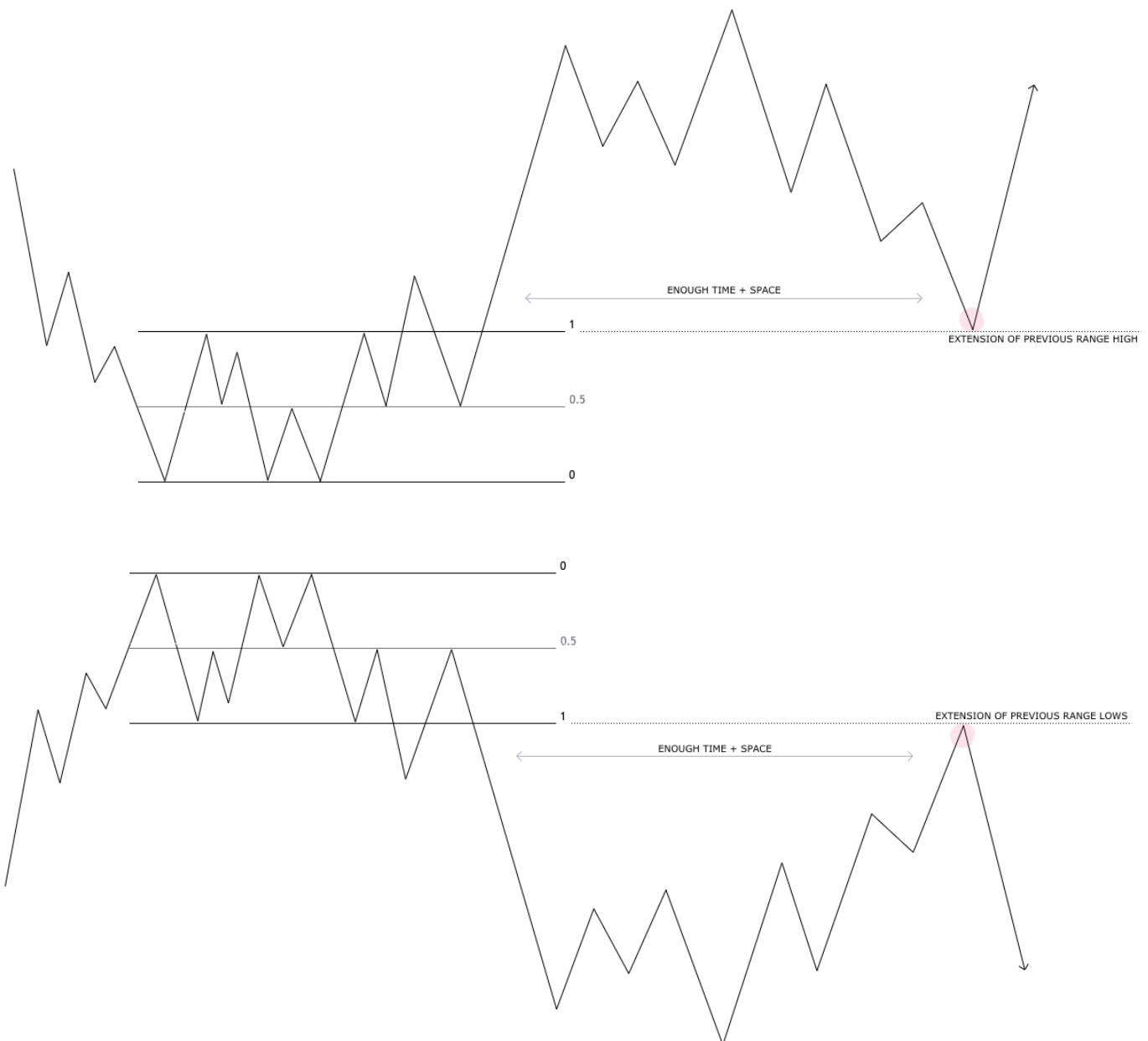
Ranges tend to offer high-strike plays as long as we can keep up with structure and recent price action. Some basic approaches:

- The market is always looking for liquidity, and most of the times it bounces between the areas where it finds it before making an expansive move (ranges are formed under this premise)
  - Fact: markets only trend around 30% of the time, while ranging the most of it (this is probably a made-up statistic, but it works)

Playing Ranges Effectively:

1. Anticipate the formation of the range
   a. Redraw constantly until it makes sense
2. All levels in a range represent reaction areas, watch your trades if price comes near these levels:
   a. Range highs
   b. Range lows
   c. EQ
3. Make sure price has collected liquidity before making moves
   a. DON'T GET TRAPPED
4. Ranges allow you to flip bias constantly, since there isn't a clear HTF trend.
   a. Probability enhancers:
      i. Directional bias market structure
      ii. Patterns and MSB Setups
         1. Trading in tandem with HTF structure assures you are not counter-trend trading. Trades in the same direction as HTF market structure are high probability plays.
5. Avoid breakout trading, violent moves may occur to trigger stops at the extremes of the range
6. Be aware of HTF S/D zones, price may look for liquidity in those areas before coming back to the range
7. Follow this mantra until the range is invalidated:
   a. Bullish/cautious at the lows
   b. Bearish/cautious at the highs

<u>Market Structure</u>

Market structure allows you to determine the flow of the market, for the most of traders it determines the trend direction. Market structure allows you to be in sync with the market and avoid counter-trend trading, which enhances the probability of your setups.

There are three stages in the market:
1. Uptrend
2. Ranges
3. Downtrend

> *Remember, the market only trends around 30% of the time. The remaining 70% it ranges.*

What is an uptrend?
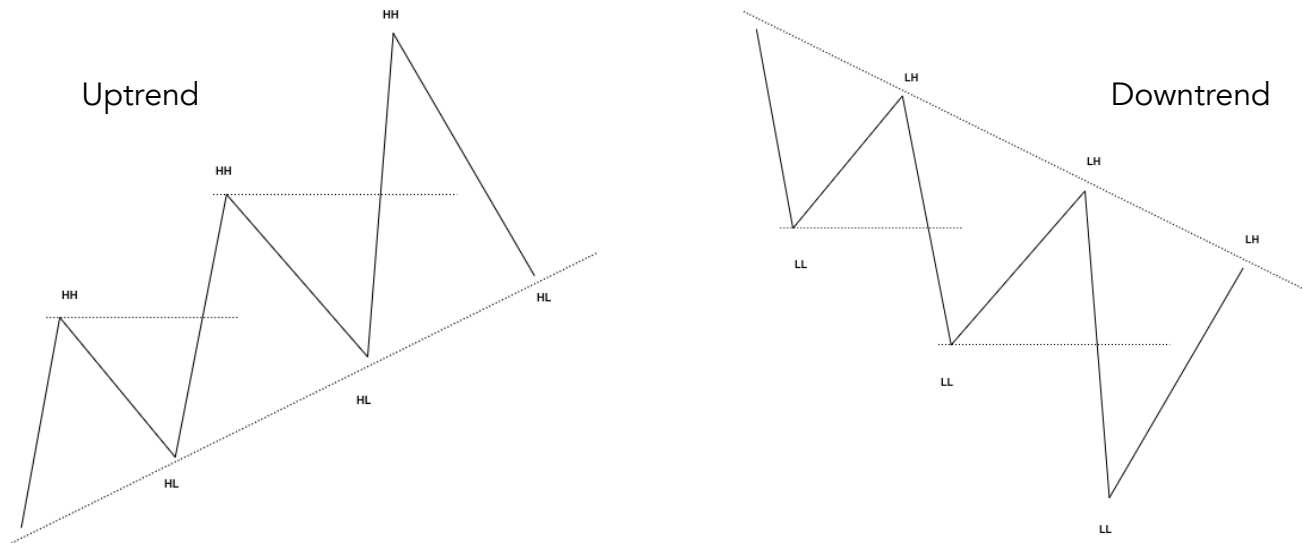Series of higher highs followed by higher lows

What is a downtrend?
Series of lower highs followed by lower lows

What is a range?
As previously explained, a range is where price finds itself bouncing between two clear levels (range highs and range lows)

> *After a trending period price usually will re-accumulate or distribute through a period of ranging*

For an uptrend to stay intact, it must preserve its ascending structure. Higher lows must be followed by higher highs. Lower highs are allowed as price starts to compress, or manifest re-accumulation patterns,

In the case of a downtrend, these are governed by their series of lower highs. It remains intact as long as no lower high is broken. Higher lows are allowed as they may be re-distribution patterns.

RANGING PERIOD
(IN THIS CASE PRICE DISTRIBUTED AT THE TOP)

DOWNTREND
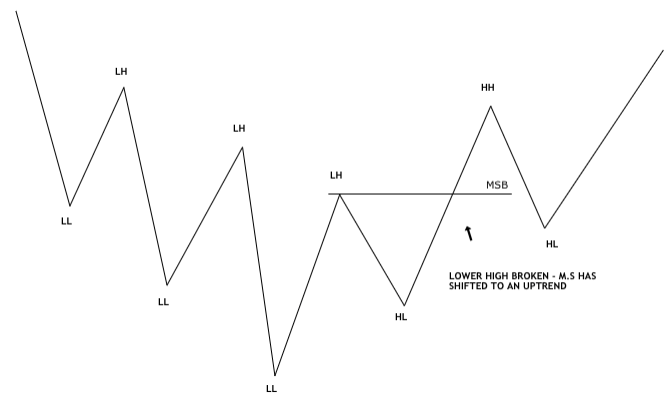
UPTREND
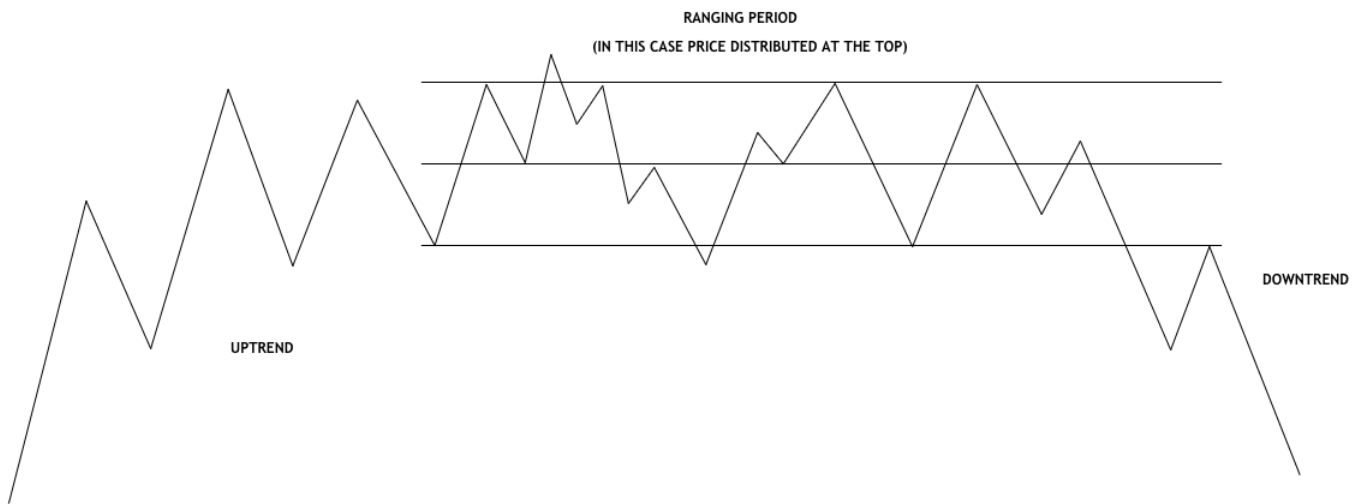
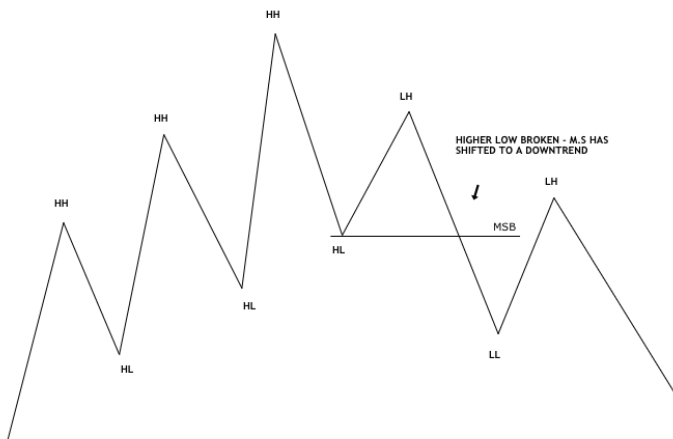## Market Structure Break (MSB)

A market structure break can easily tell us when the market has shifted from one trend to another. It allows us to plan our setups in the same direction as the trend. But how can we effectively tell if the market structure has been broken?

Market structure break (MSB) to the downside.
Price shifted an uptrend to a downtrend.

Market structure break (MSB) to the upside.
Price shifted a downtrend to an uptrend.

HH

LH

HIGHER LOW BROKEN - M.S HAS
SHIFTED TO A DOWNTREND

HH

LH

MSB

HH

HL

HH

HL

HL

LL

HL

LH

LH

LH

HH

MSB

LL

LH

LOWER HIGH BROKEN - M.S HAS
SHIFTED TO AN UPTREND

LL

HL

HL

LL

Avoid being caught in a fake MSB
1. For an upside MSB to occur *price must close above the previous lower-high wick*
   a. Beware of SFP's (explained further)
2. For a downside MSB to occur *price must close below the previous higher-low wick*
   a. Again, beware of SFP's

<mark>Tip:</mark>
Don't overcomplicate what constitutes a valid proper higher-low or a proper lower-high, as you begin to chart *use the most obvious to the market structure* and you'll be more than fine.
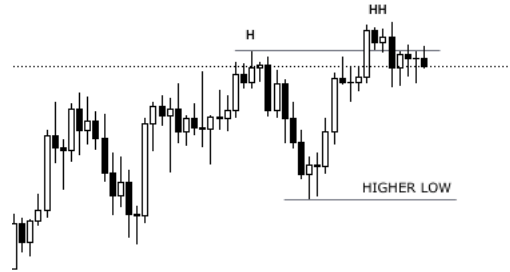
Criteria for a Lower High to be Valid

- It must be a swing high
  - A higher wick in-between two lower candles
- It must lead to a new or equal low

Criteria for a Higher Low to be Valid

- It must be a swing low
  - A lower wick in-between two higher candles
- It must lead to a new or equal high

Extra Notes:

To anticipate future price action, watch how the current structure is developing

- If in an uptrend:
  - Is price making higher lows but failing to print higher highs? Those are signs of compression
  - Is price struggling to print higher lows while making subsequent lower highs? Potential signs of reversal
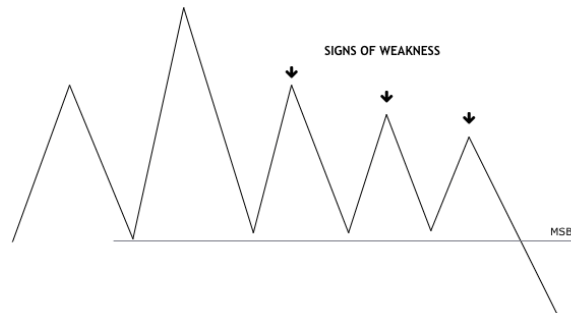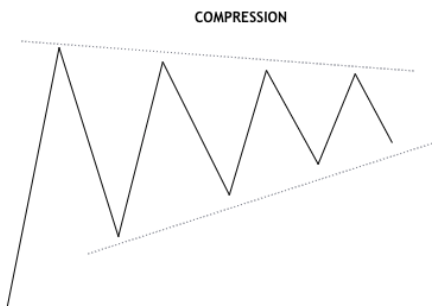
- If in a downtrend:
  - Is price making lower highs but failing to print lower lows? Those are signs of compression
  - Is price making subsequent higher lows? Potential signs of reversal

Tw: @mgvcapital
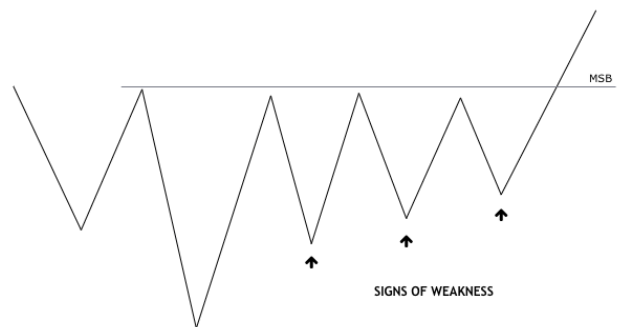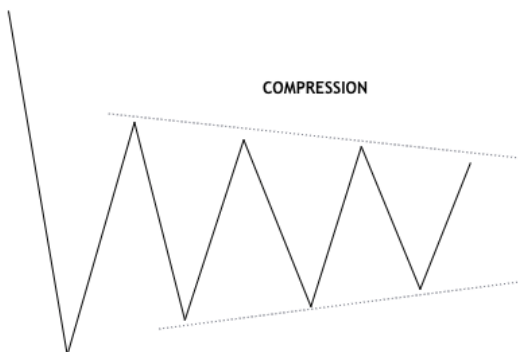
Support and Resistance

These are pivotal zones to the market. Whether it is a psychological level, or some area derived from a Fibonacci extension, these areas represent high-interest prices to the market. Therefore, you can anticipate reactions from them.

I don't consider S/R as a reliable strategy by its own, but being aware of where they are located adds confluence to your ideas.
- Orderblocks found at S/R levels give high-probability setups
  - This allows you to play S/R flips more effectively
- Over-and-Unders can be found at these levels

It's all about enhancing the probability of your setups, and S/R areas surely offer some help to it

Key facts:
- Consolidation above support is bearish
- Consolidation below resistance is bullish

Similar to support and resistance, we have the following concepts:
- First Obstacle (FO)
- Supply and Demand Clusters

All of these offer actionable areas and potential plays as long as we are acting in tandem with our strategy and count with sufficient confluence. Don't try to be a hero and predict a top/bottom, follow the trend and avoid getting rekt.

But first, let's define Supply and Demand.

<u>Supply and Demand</u>

The difference between resistance/support and supply/demand is that supply and demand tend to be fresh untouched areas of interest that can potentially provide short term liquidity (price power) to temporarily give the market a reversal. As for resistance/support, they represent historical pivot price lines that have played a crucial point in previous price outlining. How do we spot supply and demand zones? Through *orderblocks.*

Orderblocks constitute supply and demand areas in a visual way. They offer precise entries and easy invalidation levels; therefore, they are a fundamental pillar to price action trading.

But fundamentally speaking, orderblocks are zones in which price denotes a level of interest, as its name states: collective/group of orders can be found in them. In orderblocks, liquidity is injected to be used at a future time, therefore the reaction from them is usually aggressive.

How can we mark them in our charts?

An orderblock is a down/up candle near a key level that preceded an impulsive move up/down

- A bullish orderblock is a down candle near a support level that preceded an impulsive move up
- A bearish orderblock is an up candle at/near a resistance level that preceded an impulsive the move down
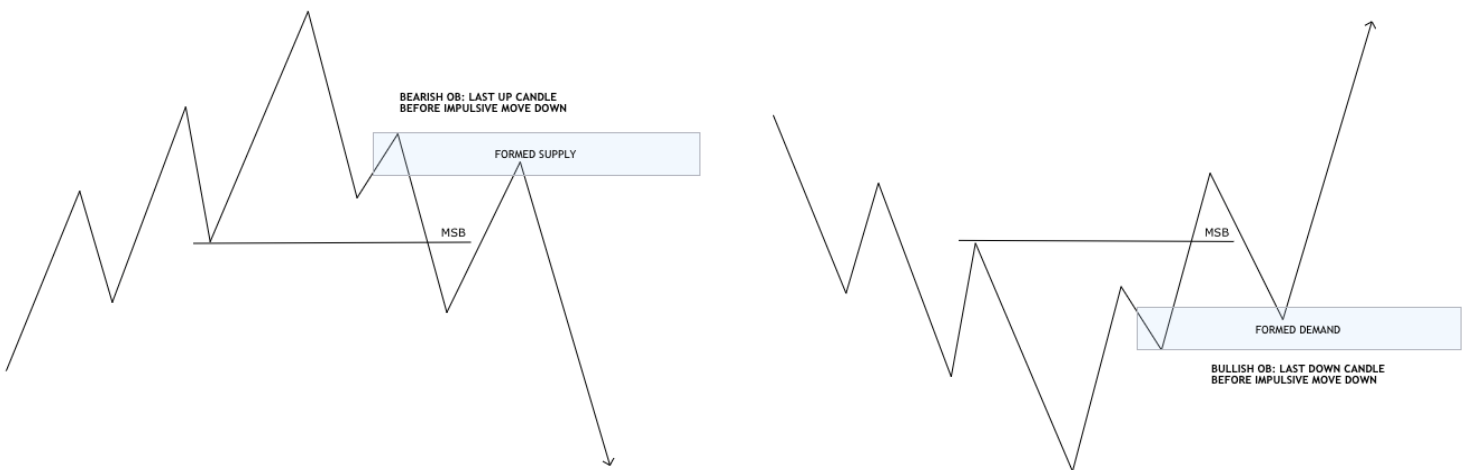
But not all orderblocks are tradeable orderblocks. What makes an orderblock valid? Well, there is some criteria to it.

<u>For an Orderblock to be valid</u>

1) It should be located near a HTF support or resistance level (at least on a directional TF)
2) The orderblock must precede a break in market structure
3) The imbalance preceded by the orderblock must be two times the OB (magnitude of reaction)
4) The orderblock must take out an opposing orderblock, this increases the interest in the level

Now, how to spot them?

Looking for Bullish Orderblocks:
1. Ensure that HTF M.S (according to your timeframe matrix) is bullish (explained at the end of the doc)
2. Start looking for areas of interest in your directional bias (S/R levels)
3. Drill down to your entry TF and begin to look for orderblocks around those levels
4. A bullish OB is identified as the *last down candle before the impulsive move up*
   a. IT HAS TO FIT THE DEFINITION
   b. Once it meets the basic criteria you validate it with the characteristics stated above

Looking for Bearish Orderblocks:
1. Ensure that HTF M.S (according to your timeframe matrix) is bearish (explained at the end of the doc)
2. Start looking for areas of interest in your directional bias (S/R levels)
3. Drill down to your entry TF and begin to look for orderblocks around those levels
4. A bearish OB is identified as the *last up candle before the impulsive move down*
   a. IT HAS TO FIT THE DEFINITION
   b. Once it meets the basic criteria you validate it with the characteristics stated above

But this isn't as easy it seems; the validity of the OB is key to its execution. Let's add some visual examples and further develop on the criteria

Valid Orderblocks:

MSB

VALID D1 DEMAND

VISUALLY, THIS IS HOW IT SHOULD LOOK:
LAST DOWN CANDLE BEFORE THE IMPULSIVE MOVE UP

What makes this Orderblock valid?

1. 30k is a SSR for BTC
   a. That makes it a high-interest level
2. It was the last down candle before the impulsive move up that broke market structure
3. The rally (imbalance) away from the OB is larger than 2x the OB
   a. This adds tremendous interest to the OB

Once it meets the validity criteria, we look forward to executing it

Invalid Orderblocks:

MSB

IT CERTAINLY IS THE LAST DOWN CANDLE BEFORE THE MOVE UP
BUT IS IT VALID? NO

What invalidates this Orderblock?

Even though it fulfills most of the criteria, the OB isn't the last down candle before the impulsive move up.

As you can see, in the next candle price went lower than our marked-out OB, this automatically invalidates the OB. However, *there certainly was a rally after that down candle*, so we proceed to do the following:

1. Drill down to LTF to find the correct OB that preceded the move
2. Mark it out

This was on CRV/USD 1D Chart, so we proceed in the following order:
1. 12h
2. 8-6h
3. 4h

We drilled all the way down to the 6H chart until we found the correct Orderblock. It previously met most of the criteria, but it was invalidated due to the lower wick in the following candle.

Now that we found ourselves a proper Orderblock, the next question is: *how to execute them?*

Our orderblock should contain a considerable number of orders waiting to be filled. If the orderblock is valid then price shouldn't be able to go lower than our marked-out zone. Therefore, here is one conservative way to play Orderblocks:

- Bullish OB: entry at the top of the OB, invalidation below the lowest price of the OB
  - Target next swing highs / liquidity areas
- Bearish OB: entry at the bottom of the OB, invalidation above the highest price of the OB
  - Target next swing lows / liquidity areas
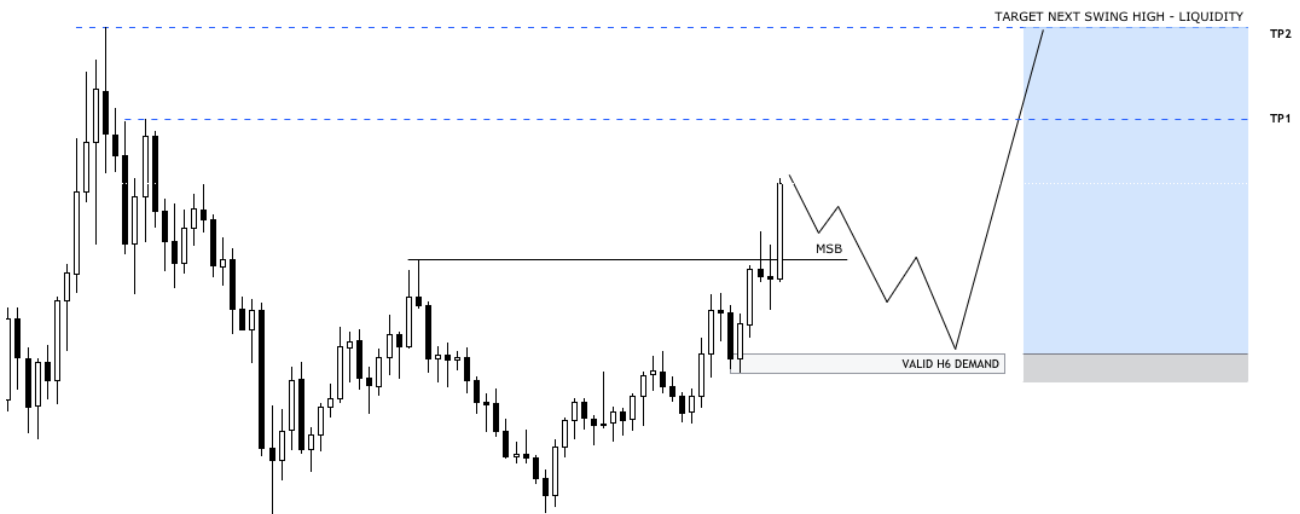
This is how we would wait for price to retrace with our limit orders set.

How can we avoid bidding/asking invalid Orderblocks?

You could have marked out a valid orderblock. However, that doesn't guarantee you that price will respect it
- No strategy has a 100% strike rate and orderblocks aren't the exception
- General market conditions and previous price action are key to determine if we should be entering our trades on aggressive or conservative entries

One of the most recommended things to do is to monitor LTF price action as price approaches our area of interest. If price is showing bullish price action patterns, that increases the probabilities of the demand orderblock to be valid, and *the opposite is true for supply orderblocks.* If we detect these patterns, then we look forward to entering our positions.
- If the OB fails as a Supply/Demand block that turns it into a breaker of the opposite nature, we will develop on those later

Remember: for all the previously mentioned, the opposite is true for Bearish Orderblocks.

Extra notes:

Choosing what timeframe to look for OBs

There is technically no right or wrong way to mark-out an OB, but here's a few tips:

- You want it as close to the MSB as possible
- The stronger the move away from the level, the better the Supply/Demand OB
- How much time did price spend at the level?
  o The less time spent at the level, the better the supply/demand OB

Often, you will likely get overlapping OB/breakers within multiple timeframes
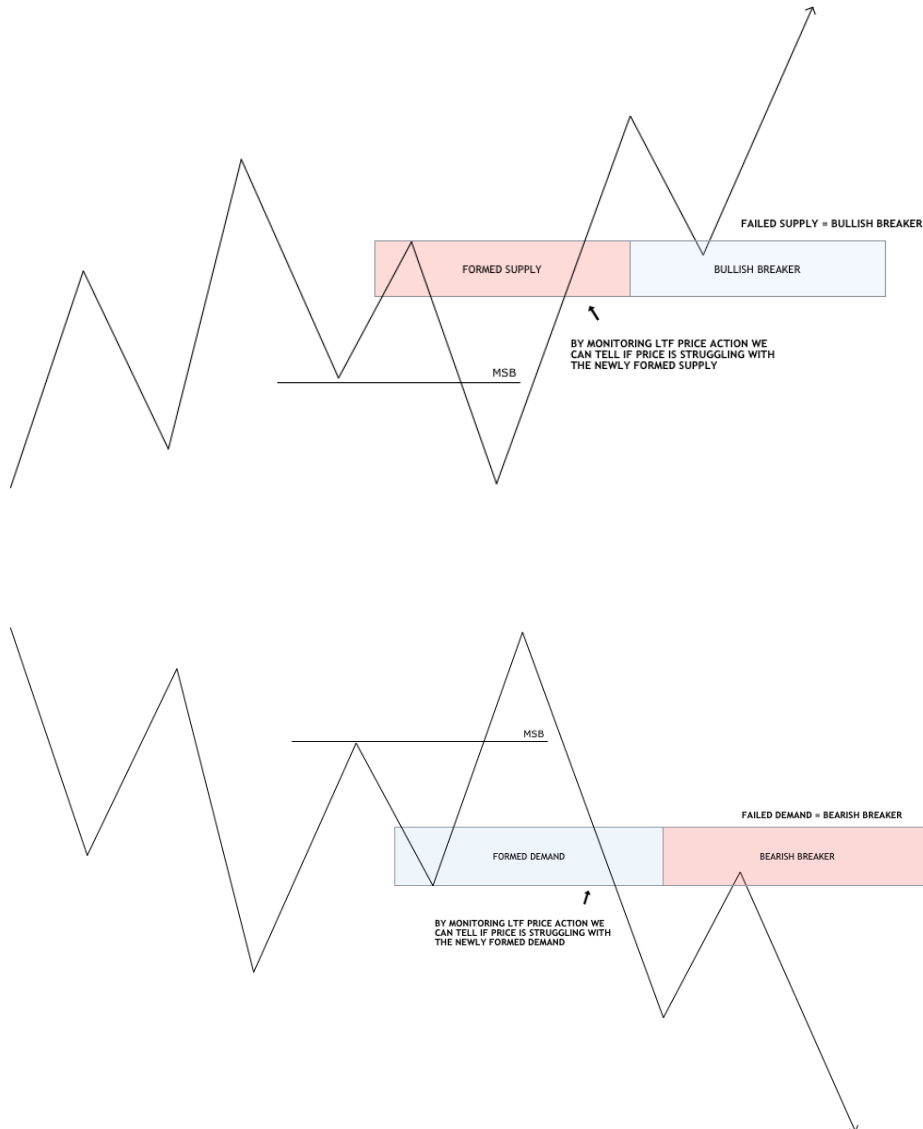
How to trade overlapping OBs?

- LTF OBs = good for optimal entries with higher R:R
- HTF OBs = good for setting stop losses.

<u>Breakers</u>

Easily put, breakers are failed supply and demand orderblocks that now act as a flipped level for traders. The most reliable breakers are the ones that offered little to no resistance when previously tested as supply/demand.

- *If it previously was a valid orderblock, that automatically means the breaker is valid*

FAILED SUPPLY = BULLISH BREAKER

| FORMED SUPPLY | BULLISH BREAKER |

MSB

BY MONITORING LTF PRICE ACTION WE CAN TELL IF PRICE IS STRUGGLING WITH THE NEWLY FORMED SUPPLY

MSB

FAILED DEMAND = BEARISH BREAKER

| FORMED DEMAND | BEARISH BREAKER |

BY MONITORING LTF PRICE ACTION WE CAN TELL IF PRICE IS STRUGGLING WITH THE NEWLY FORMED DEMAND

But not all failed orderblocks are reliable breakers. How can we find one? Up next we define some extra criteria

For Bullish Breakers
1. We find the preceding supply orderblock
2. Price must blow through the supply orderblock, automatically invalidating it
   (a) The OB should offer little to no resistance
3. If a market structure break occurs after the orderblock was proven invalid that turns the breaker into a high-interest area
   (a) For bullish breakers: a new higher high is made after a previous MSB to the downside
      (i) *This is optional but it is one of the greatest probability enhancers for breakers*

How to execute them?
1. Set your bids at the top of the orderblock (now our identified breaker)
2. Place stops below the breaker
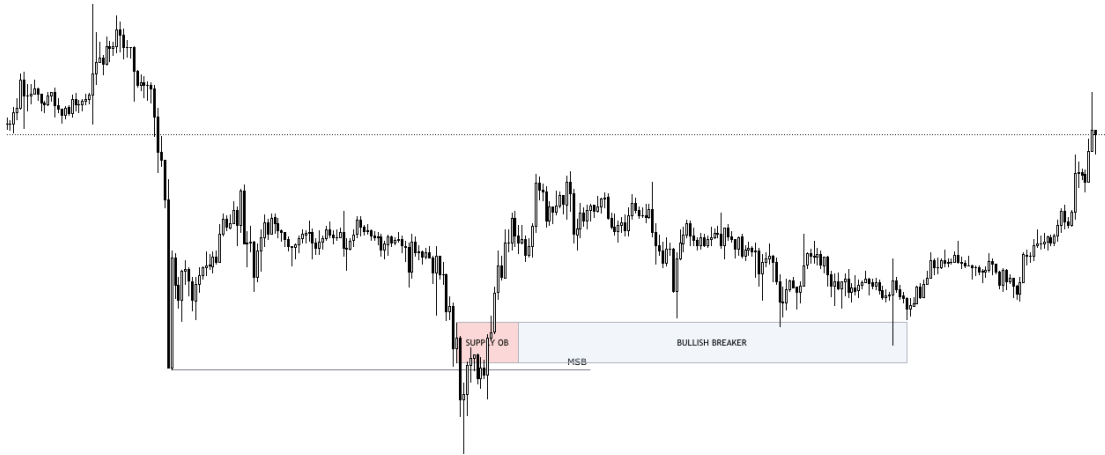
For Bearish Breakers
1. We find the preceding demand orderblock
2. Price must blow through the demand orderblock, automatically invalidating it
   i) The OB should offer little to no resistance

How to execute them?
1. Set your asks at the bottom of the orderblock (now our identified breaker)
2. Place stops above the breaker
3. If a market structure break occurs after the orderblock was proven invalid that turns the breaker into a high-interest area
   (a) For bearish breakers: a new lower low is made after a previous MSB to the upside
      (i) *This is optional but it is one of the greatest probability enhancers for breakers*

In the same case as S/D orderblocks, breakers can also be proven invalidated. The same principles that govern orderblocks apply to breakers:

Again, one of the most recommended things to do is to monitor LTF price action as price approaches the area of interest. If price is showing reversion patterns, that increases the probabilities of our OB to be valid. Therefore, we enter our positions.

Tips to Playing Breakers Effectively

1. Anticipate them
    i) Weak orderblocks tend to offer solid breakers once they are proven invalid
        (a) You look to play solid S/D orderblocks
        (b) You expect weak S/D orderblocks to fail (these tend to trap traders)
2. Add context to your chart
    i) If price is within a range
        (a) Could this be a deviation?
        (b) Is this a stop hunt/trap?
    ii) What has been the behavior of previous price action?
        (a) Are traders getting trapped constantly?
        (b) Is the asset trending?
3. Determine the strength of your breaker
   (a) Assess price action and market conditions

Note: If you had a previously valid orderblock marked out, that probably means that many traders also highlighted that area in their charts. Therefore, as price broke straight through the OB, many traders are now underwater and looking for a retracement to puke their positions and exit the closest they can to break-even.

First Obstacles

Price not always tends to retest S/D orderblocks or perfectly flipped highs/levels. Knowing that, we could mark out possible opportunities to join a strong trend by marking the First Obstacles.

What is a First Obstacle?

- In an uptrend, this is the first resistance after a break of a previous swing high
- In a downtrend, this is the first support after a break of a previous swing low
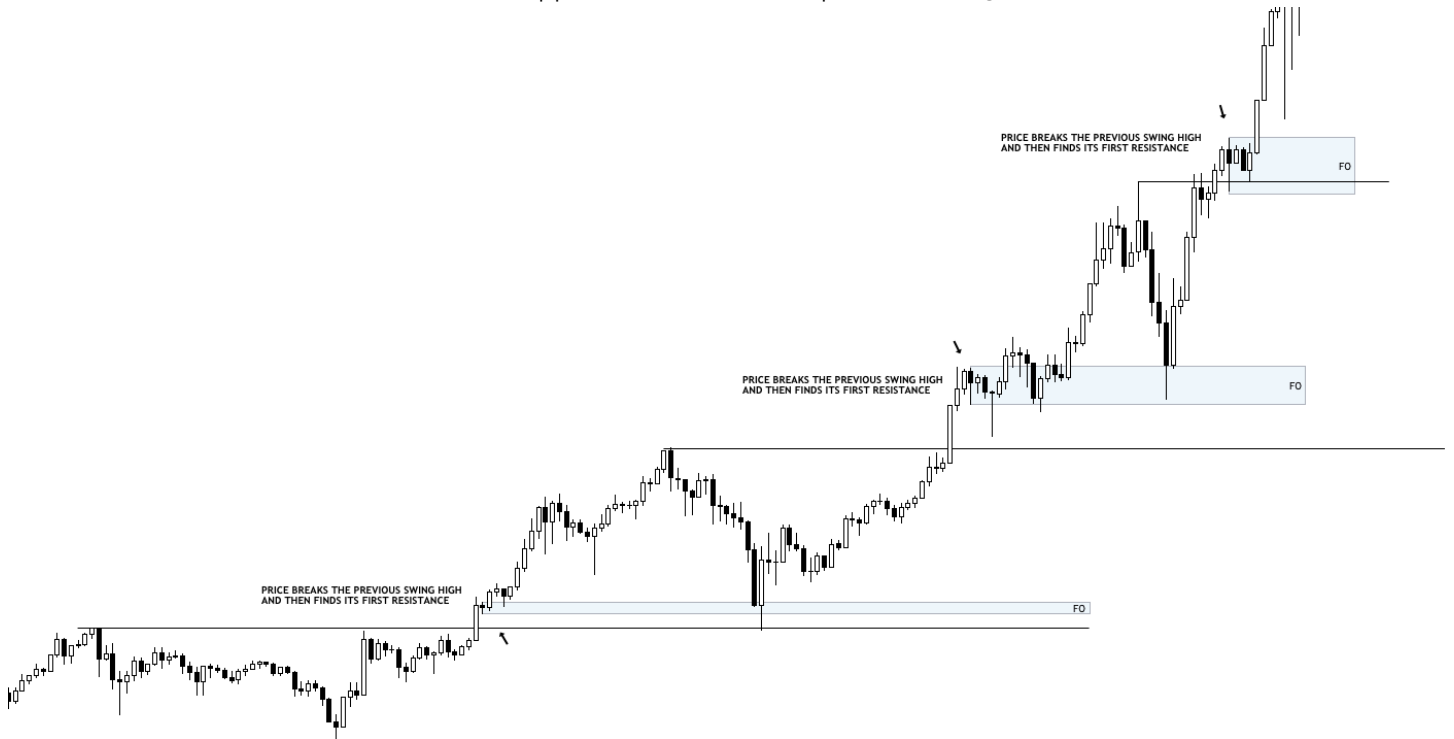
Supply and Demand Clusters

Different to orderblocks, these are structures (or candle clusters) that preceded an impulsive move. For them to be valid, you can apply the same criteria as with OB's.
- To execute more precise entries, dig into LTF's to find the exact OB you would like to bid/ask
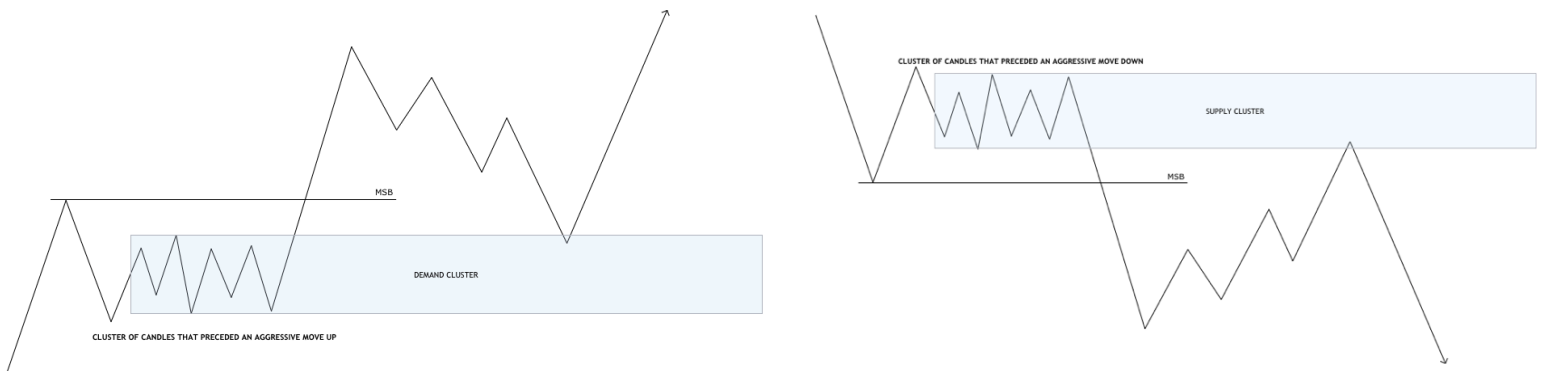
<u>The Timeframe Matrix</u>

Having a directional bias is one of the most useful things you can implement in your strategy. Price may not be having the same structure at all timeframes, so a directional bias allows you play in tandem with a HTF trend and knowing what side of the market is being favored and which isn't. Therefore, having a directional bias enhances your probabilities of succeeding.

When looking at a setup, you want to make sure you are not counter-trend trading. Therefore, **at least two timeframes should be pointing in the same direction**, it's not about catching perfect bottoms or shorting absolute tops, it's about finding high R:R plays.

HTF Structure	Directional Bias TF	Entry TF
M	W	D1
W	D1	H4
D1	H4	H1
H4	H1	M15
H1	M15	M5 / M3 / M1

How to implement it? A quick example

Let's say we have a whole day for ourselves and want to spend the day scalping at home. The steps would be:

1. Determine the HTF Structure
    a. In this case, finding the market structure at the H1 chart
2. Mark out the key levels at the HTF chart
    a. You don't want to find yourself shorting a 5-minutes supply block when price is approaching a H1 demand orderblock - *timeframes have hierarchy over each other*
3. Determine the Directional Bias structure
    a. In this case, finding the market structure at the M15 chart
4. Mark out the key levels at the Directional Bias chart
    a. In this case, we would highlight levels from the 15-minutes chart – remember timeframes hierarchy
        i. Look for orderblocks, S/R
5. Execute in your entry timeframe according to your directional bias:
    a. If the directional bias is bullish = look for longs
        i. Refine your entries within the M5, M3 and M1 chart
    b. If the directional bias is bearish = look for shorts
        i. Refine your entries within the M5, M3 and m1 chart
6. Happy trading

Tips:
- Always be aware of HTF market structure
- Don't trade against your directional bias
    o If your directional bias is bullish, you are looking for longs
    o If your directional bias is bearish, you are looking for shorts

Patterns and Setups

1. Over and Under / Quasimodos

Basically, it consists of shorting the right shoulder of a H&S pattern. In the case of a bullish O/U, longing the right shoulder.

How to spot it?
1. Price finds support or resistance
2. Price breaks through that level, grabbing liquidity
   a. Bullish O/U: price breaks up
   b. Bearish O/U: price breaks down
3. Price pulls back to retest
4. Price approaches previous support or resistance, depending on the case
5. Enter position placing your SL above/below the ''head'' of the pattern

Bearish Quasimodo / Over-and-Under Structure
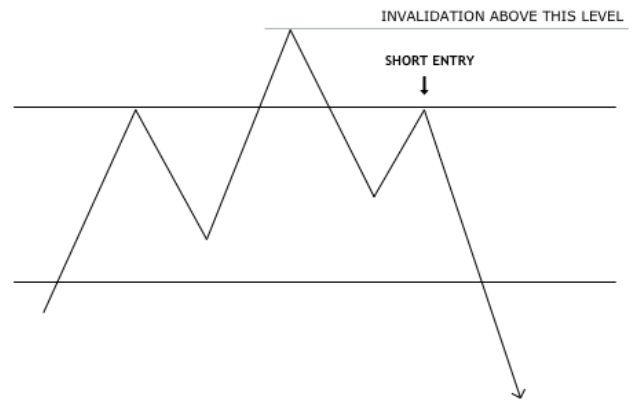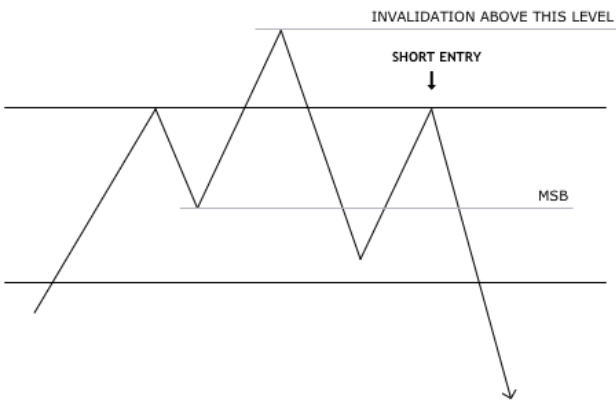
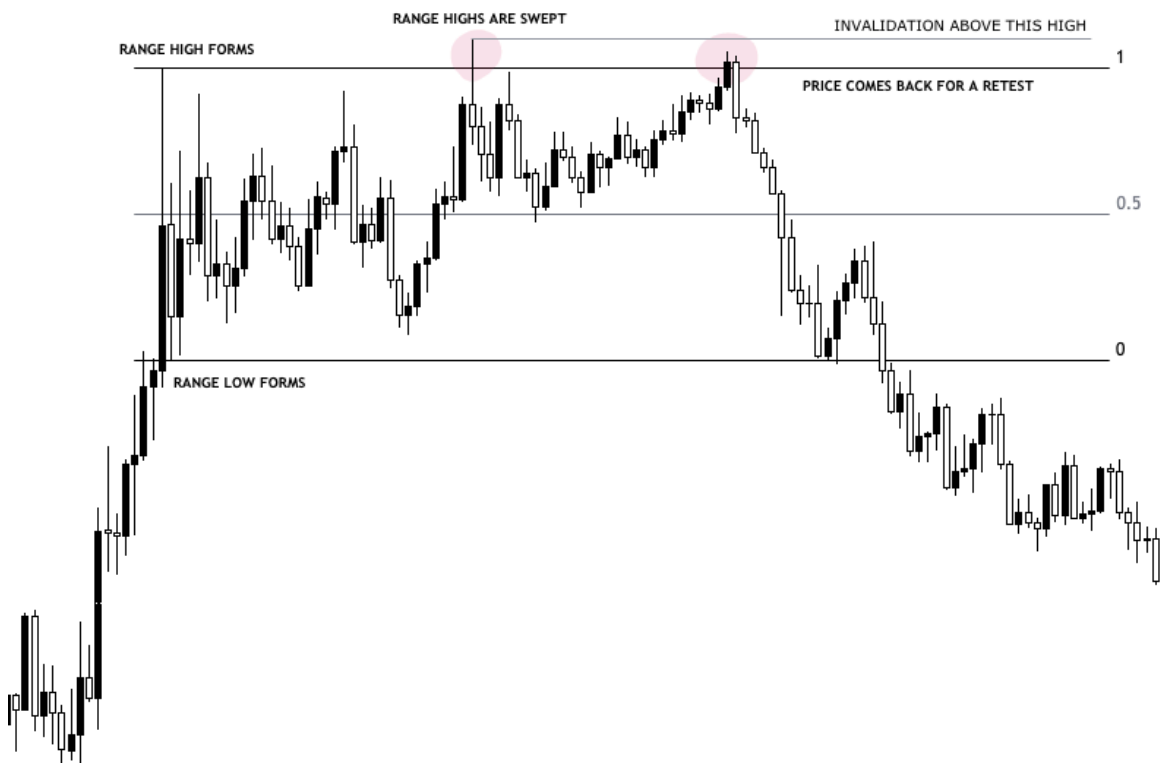Bullish Quasimodo / Over-and-Under Structure
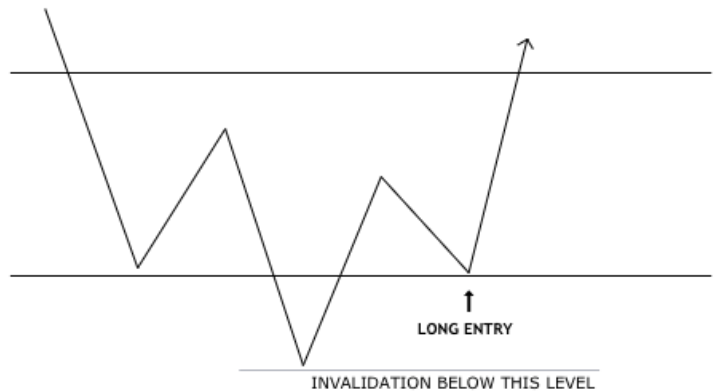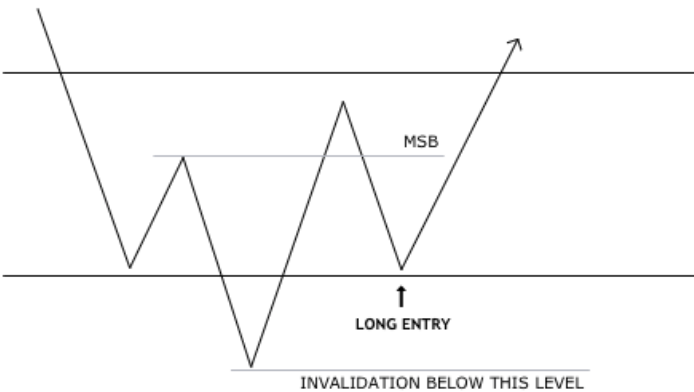
2. Three Tap

The three-tap setup has a high probability rate to predict a visit towards the opposite extreme of a range. It's tailored around trapping breakout traders and forming a base to retest after that (where they puke their positions)

How to spot it?
1. Identify your range
2. After a swing point is swept/deviated, prepare to bid/ask the original range low/high
3. Retest
    a. If you anticipated a price retest with bids/asks, place your stops below/above the wick that swept the swing
   i. Very similar to how you'd execute an Over-and-Under

For a bearish illustration, the opposite happens. *Inverted scale for representation*

RANGE HIGHS ARE SWEPT

RANGE HIGH FORMS

INVALIDATION ABOVE THIS HIGH

PRICE COMES BACK FOR A RETEST

1

0.5

PRICE IS NOW EXPECTED TO TREND TOWARDS THE OPPOSITE SIDE OF THE RANGE   0

RANGE LOW FORMS

RANGE HIGHS ARE SWEPT

RANGE HIGH FORMS

INVALIDATION ABOVE THIS HIGH

PRICE COMES BACK FOR A RETEST

1

0.5

0

RANGE LOW FORMS

3. Swing Failure Pattern (SFP)

A swing failure pattern occurs when a candle trades above/below a significant swing high/low, then fails to close above/below. These are basically failed attempts to break structure.

Exhibit: Bullish SFP - *Inverse logic applies to a bearish SFP*
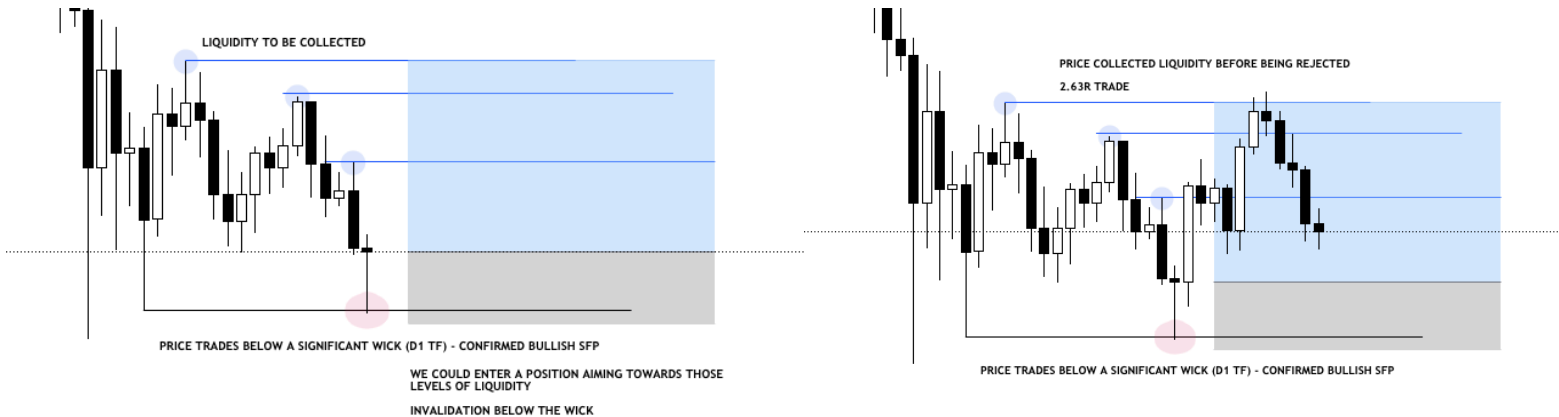
Over-and-Unders, Three Taps and SFP's are setups you can anticipate and execute. Remember, price is always telling a story, is up to you to get hints on what it may do next
- Watch LTF price action behavior
  - Changes in structure on LTF may give clues to what comes next on HTF

Some other basic setups include the following:
- Longing demand
- Shorting supply
- Failed demand orderblock = breaker (look for shorts from this level)
- Failed supply orderblock = breaker (look for longs from this level)

Abbreviations:

EQ = Equilibrium
LTF = Low/Lower Timeframes
HTF = High/higher Timeframes
MSB = Market Structure Break
OB = Orderblock
S/D = Supply and Demand
SSR = Significant Support/Resistance
S/R = Support and Resistance