Liquidity Part 1

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Content

What is Liquidity and why is it Important

Liquidity basically describes the degree to which an asset can quickly be bought or sold close to a bided or asked price. A bid is the highest price a buyer will pay to buy an asset and an ask is the lowest price a seller is willing to sell an asset.

This might sound complicated but it can be broken down very easily. Cash is generally seen as the most liquid asset, so when you go and buy yourself something it is easy to exchange cash to the wished good (f.e. a bicycle). On the other side if you try to exchange a sheep with the bicycle you will have a hard time finding someone willing to do because the sheep/bicycle market is not very liquid.

How does that reflect in trading? Whenever you want to sell an asset there needs to be someone willing to buy it from you. If there is no one buying from you, you will never sell anything.

If let's say you want to sell your BTC for 20'000$ but there are only buyer wanting to buy for 18'000$ you either sell to them with a Market order with a slippage of 2000$ or you have to set a limit order and wait until someone bids you your asked 20'000$.

From this we can conclude, the more market participants there are who set Limit orders, the more money is available in the Orderbooks, the more liquid a market is and as such the faster and closer to your ask price you will be able to sell.

We can also conclude that liquidity is the only thing which can move price, not a line or an indicator, only liquidity, hence why this is the most important concept to understand in trading.

To make that even more clear.

When there are no buyers at a given price the price moves down, when there are no sellers at a given price the price moves up. If the market is flooded with sells, there won't be enough buyers to buy that up at that price so the price drops and vice versa.

To fill your buy Limit order, there has to be enough Liquidity available in form of sellers, else you get a partial fill or no fill at all if there is no one left willing to sell at that price. Instead if you Market buy you buy from the next best seller and accept to get a worse or better price (slippage) for a guaranteed fill like explained above. I know I repeat myself but this is important to fully understand

As all orders in the Orderbook are liquidity that means that every Limit Buy/Sell Order and every Fair Value Gap (which are nothing else than skipped orders as we learnt in the Marketstructure PDF) is liquidity.

Difference between Maker and Taker

You surely already heard the Terms Maker fees and Taker Fees. A Maker is a person who makes liquidity available through a Limit Order a Taker is someone who Takes liquidity through a Market Order. To incentivize people to make liquidity available, you mostly pay less Maker Fees than Taker Fees

Take profits as well as Stop losses are Market Orders, as such they get execute at the first best available price.

What is a Market Maker

A Market Maker is an entity which provides Liquidity to the Market. They fill the Orderbooks with Bids and Asks and profit from the spread between those. So for example they offer to buy BTC for 10'000$ and simultaneously they offer to sell BTC for 10'100$ the 100$ spread between their buy and sell offer is their profit. Normally there are different Market Maker which compete with each other as such resulting in lower spreads. Exchanges hire Market Maker in order to stay competitive. This said Market Maker aren't bad or after your money, they are simply provider of liquidity and as such make sure that you're always able to change your money against an asset and Vice Versa

How to use Liquidity in Trading

If you think about the above, the only logical conclusion is that Price always gravitates towards liquidity, without liquidity no price movement.

Knowing this, we can understand the concepts showed before like the AMD Model, FVGs and Draw on liquidity much better.

Let me explain

We differentiate between 2 sorts of Liquidity, Buy Side Liquidity (BSL) which are the stops of the shorts (they buy back in when triggered) and Sell Side Liquidity (SSL) which are the stops of the Longs (they sell they position when triggered), those levels can be used as TP targets or be monitored for potential Draw on Liquidity and subsequent reversal

In order to fill their Big orders, Banks and big institutions need to have enough counterparties. This is why the market moves in cycles of Accumulation and Distribution and this is also the reason why popular Retail concepts don't really work very well.

Imagine, most of the people use the same strategy, they sell at resistance and buy at support.

What does Smart Money do? They push price below resistance, so that people actually sell to them at a cheap price, then they know exactly that people who are long will have their Stop below this accumulation so they place their orders there and push price down and as such trigger the Stops which now are forced to sell to them at an even cheaper price and simultaneously trap breakout traders which now short (so sell to Smart money for cheap) and place their stop above "resistance".

Now as they were able to fill all their Buy Orders they then distribute to the upside, triggering the Stops of the people who where short and as such buy the assets at a premium which Smart money got at a discounted price and they will target areas where people put their SL to sell them at a premium. Once they sold all their assets at a Premium they Accumulate shorts and the whole party starts again.

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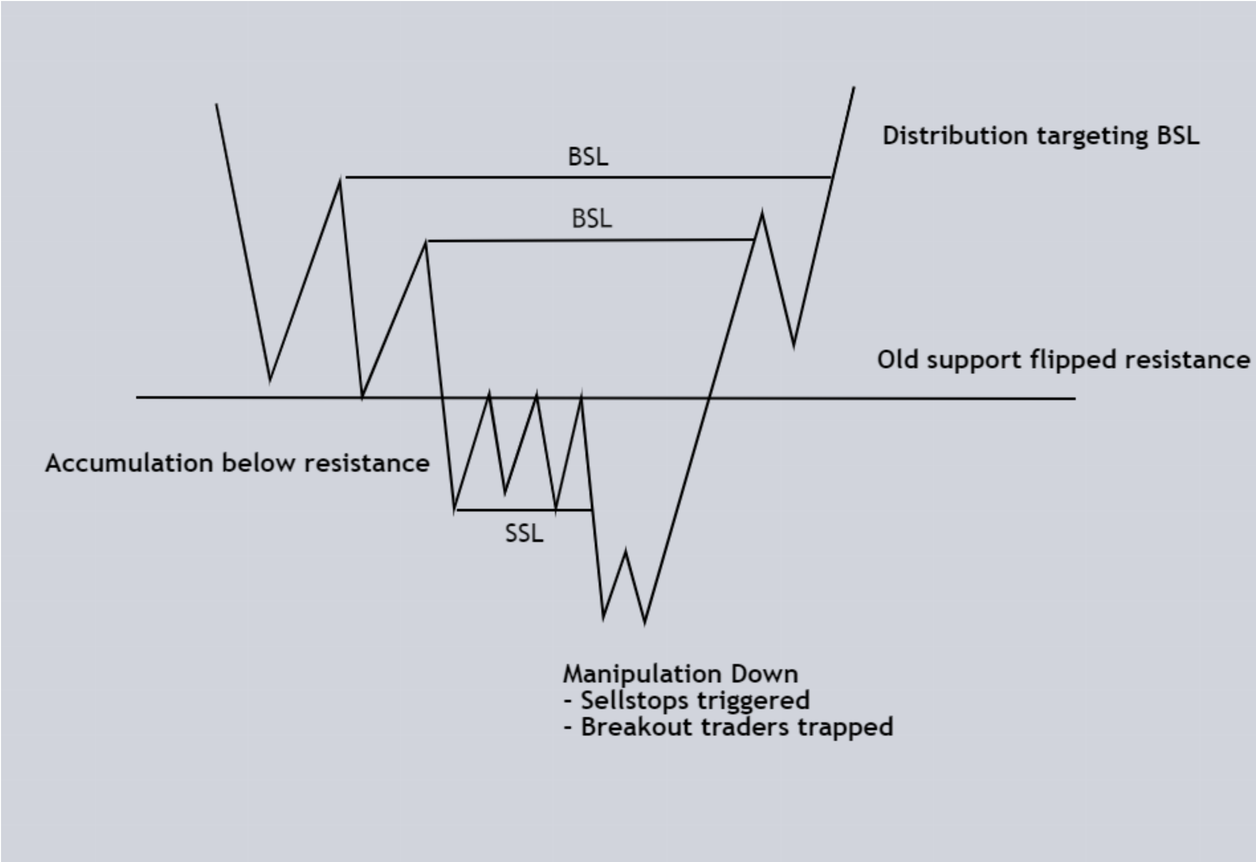
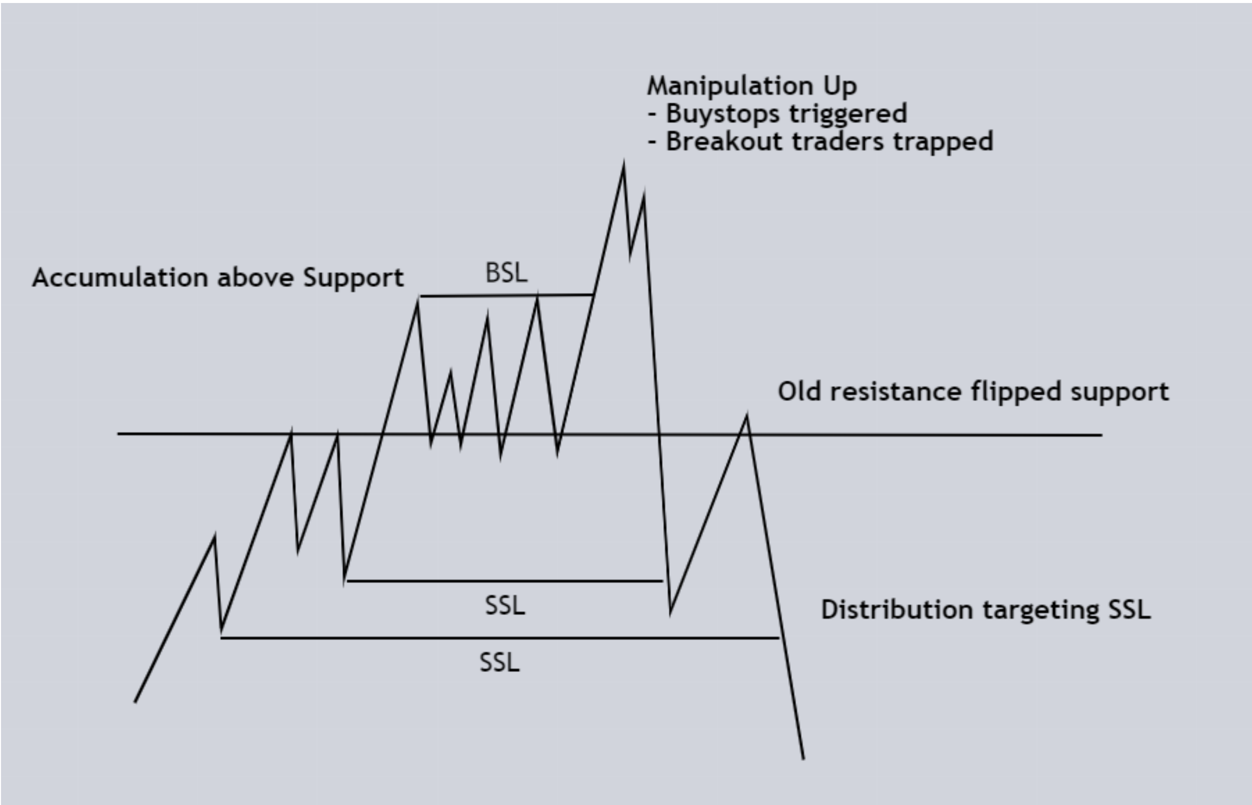
I will illustrate this on Chart for better understanding in the next pages


Distribution targeting BSL
BSL
BSL
Old support flipped resistance
Accumulation below resistance
SSL
Manipulation Down
- Sellstops triggered
- Breakout traders trapped


Manipulation Up
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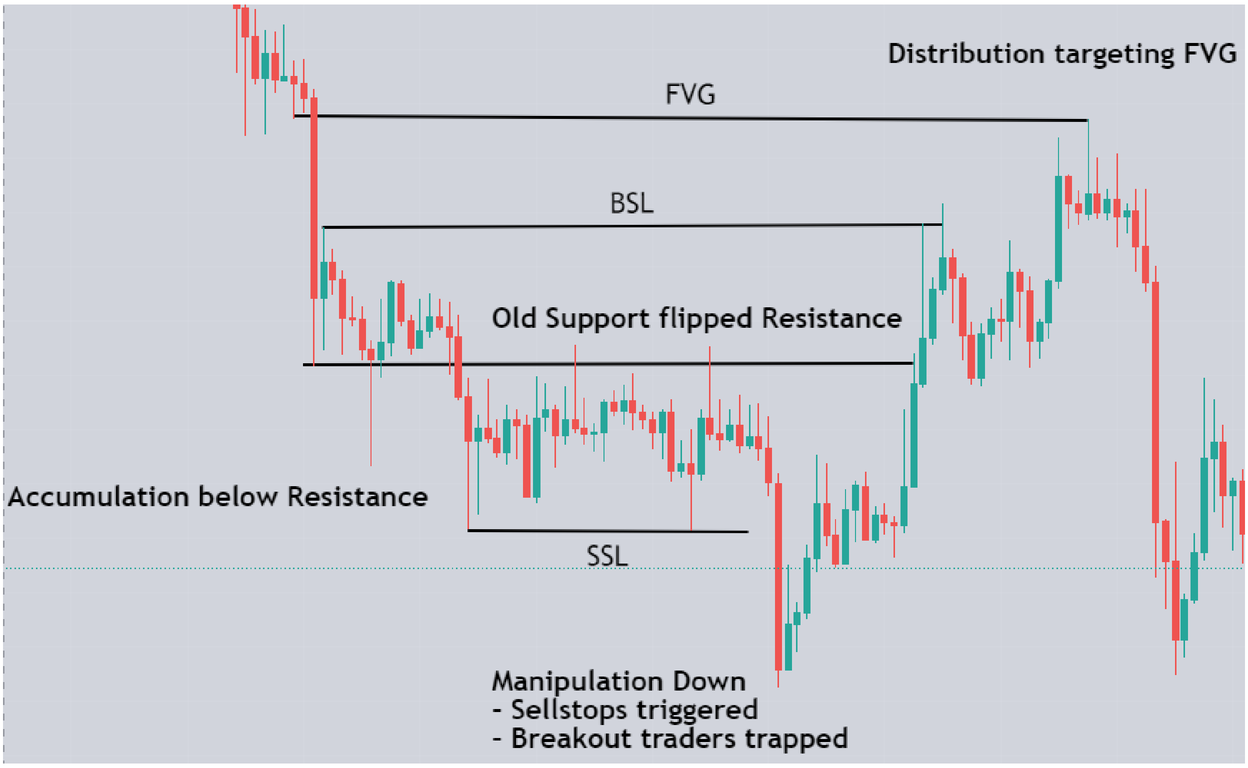
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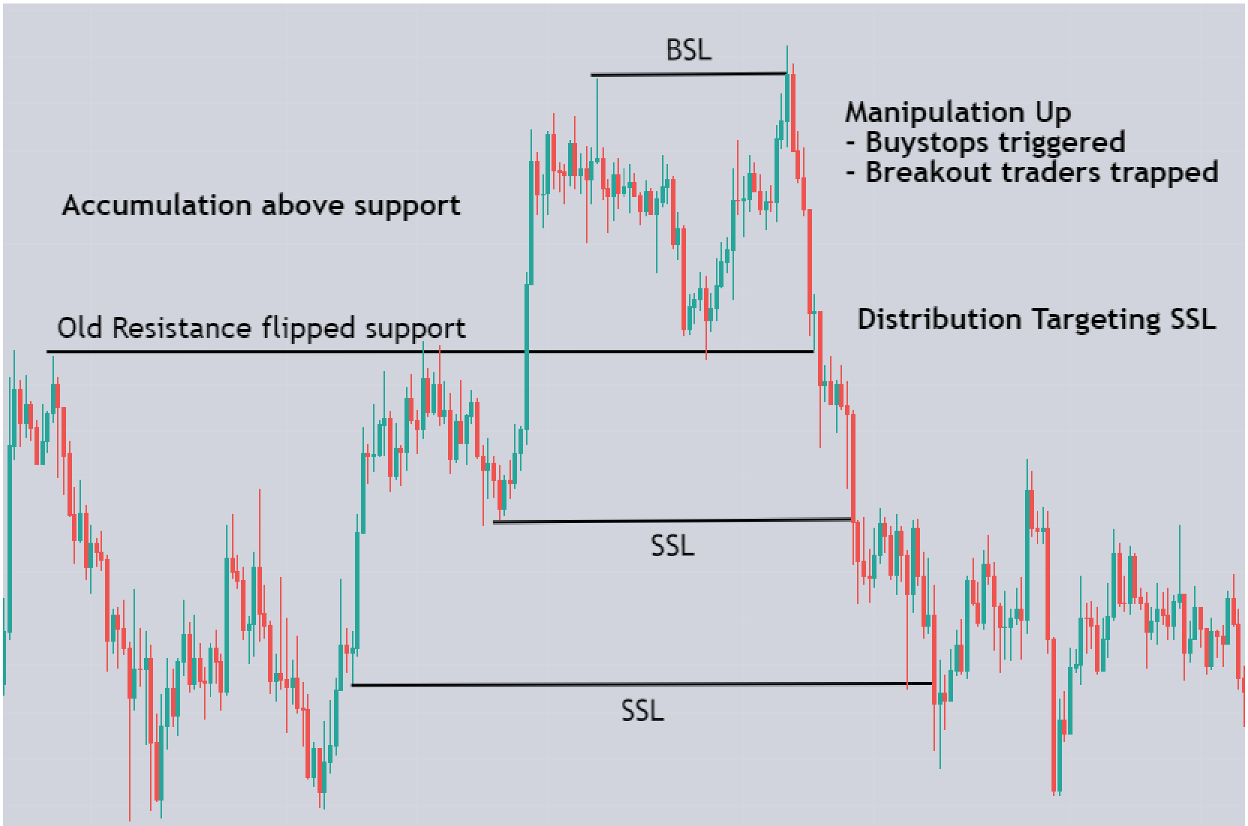
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Distribution Targeting SSL
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Some final Words

Thank you for reading this PDF. I hope you found it useful and learned something new. This was only Part 1, in Part 2 we will dive even deeper into liquidity.

If you have questions don't hesitate to ask. More Educational PDFs are in the work so make sure to join my community on Twitter and Telegram in order to stay up to date.

Twitter:

https://twitter.com/SMCrypt1c

Telegram:

https://t.me/Cryptics_TradeLearn

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Or join me in the Lions Trading Discord if you want to chat, chart and

learn with us:

https://discord.gg/4eZMmgJuJx

Also, if you find my work valuable and want to support me while taking advantage of low trading fees, exclusive events, deposit and trade bonuses amongst other Perks Trade with me on BingX.

You get some perks while still paying the same amount of fees and I get 40% of your trading fees, which other ways would go to the exchange. A good part of those fees is going to be used to give back to the community in form of some projects I have in mind for the future

Register through this link:

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Then Join the deposit and trade Event here and get up to 4000$ in bonuses

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Credits

At this point I want to credit Opsec (https://twitter.com/opsec_crypto) who is a great teacher and Mentor to me teaching me his knowledge for free.

Much respect and appreciation from my side to him.

Disclaimer

Everything shown here is strictly Educational purpose only and not financial advice. Don't try to trade live funds if you aren't 100% sure of what you're doing.

Best of luck

Cryptic