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How do banks use supply and demand method ? (Text Lesson)

LESSON 7 MODULE 2

The markets are ruled by the law of supply and demand in much the same way the law of gravity rules our planet. Prices go up and down because of the imbalance in supply and demand. If supply is higher than demand, the price goes down, and if demand is higher than supply, price goes up.

The markets are dominated by big investors such as central banks, hedge funds, market makers, and other financial institutions. These investors are also affected by some factors that influence their trading decisions such as daily news that affects the world's economies, economic data about some countries. And when they take their trading decision they move price strongly and create an imbalance in supply and demand. The greater the imbalance the greater the move in price.

How many times have you seen a market retrace back to a level where a recent major move started from, only to respect that level almost exactly before making another strong directional move, it happens frequently in the market. Look at this example below to understand more fully:



As you can see in the chart above, the red big candle represents a big bank sell order, this selling decision was influenced by big economic news. We don't care about news, we only care about big moves like this, because this is the footprint of banks and financial institutions.

When the bank takes this sell order and drops the market down, it can't liquidate all the quantities, so it leaves some quantities to sell from the same zone. The amount of quantities left in the zone depends on buyers. If the bank found a big number of buyers to sell, it can liquidate all quantities and nothing will be left in the zone. But in most cases, banks leave quantities as limit orders in the same zones they sell from.

The beginning of the big move becomes a very interesting price to sell from, because there are some limit orders left in that price, other banks and financial institutions will sell from the same zone when the market pulls back to test this zone. Because they know that there are other financial institutions that will sell from the same zone, and this is the easiest way to make money without being in a conflict. Look at another example to understand more:



In the chart above, you can see a big blue candle that represents a bank buy order. This big buy order was influenced by an economical news. Don't bother yourself with trying to analyze economic news and how they will affect the market. You are not a bank trader, you are only a retail trader with a small trading account. What you have to do, is to identify interesting prices where banks and financial institutions will buy or sell from.

As you can see the bank made the first buy order, and because of the lack of buyers, it can't liquidate all its quantities, so it makes another limit order.

Other banks and financial institutions will see this zone as an interesting price to buy from because they already know that there are banks who bought from it and they still have limit orders on it. Look at what happened when the market pulls back to test this zone.

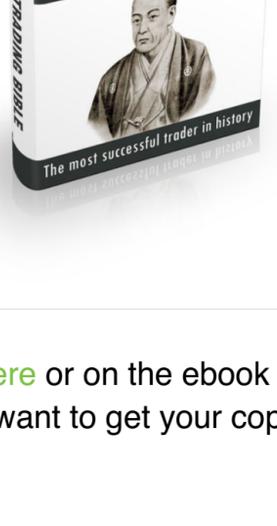


As you can see when the market pulls back to this zone, it got rejected because there are some quantities left as limit orders in this zone, and other financial institutions will buy from the same zone because it is considered to be a very interesting area to buy from.

When the market goes up from this zone, other retail traders will join the move, and if you are aware of how banks and financial institutions trade the market you will join the move and make money by following the big participants in the market.

This is how supply and demand strategy works, in the next lessons you will learn everything you need to master this strategy and start using it in your trading.

Ps: If you are a complete beginner and you want to learn more about price action, i highly recommend you my best seller ebook below :



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