Volume Spread Analysis

By Danny K

Introduction

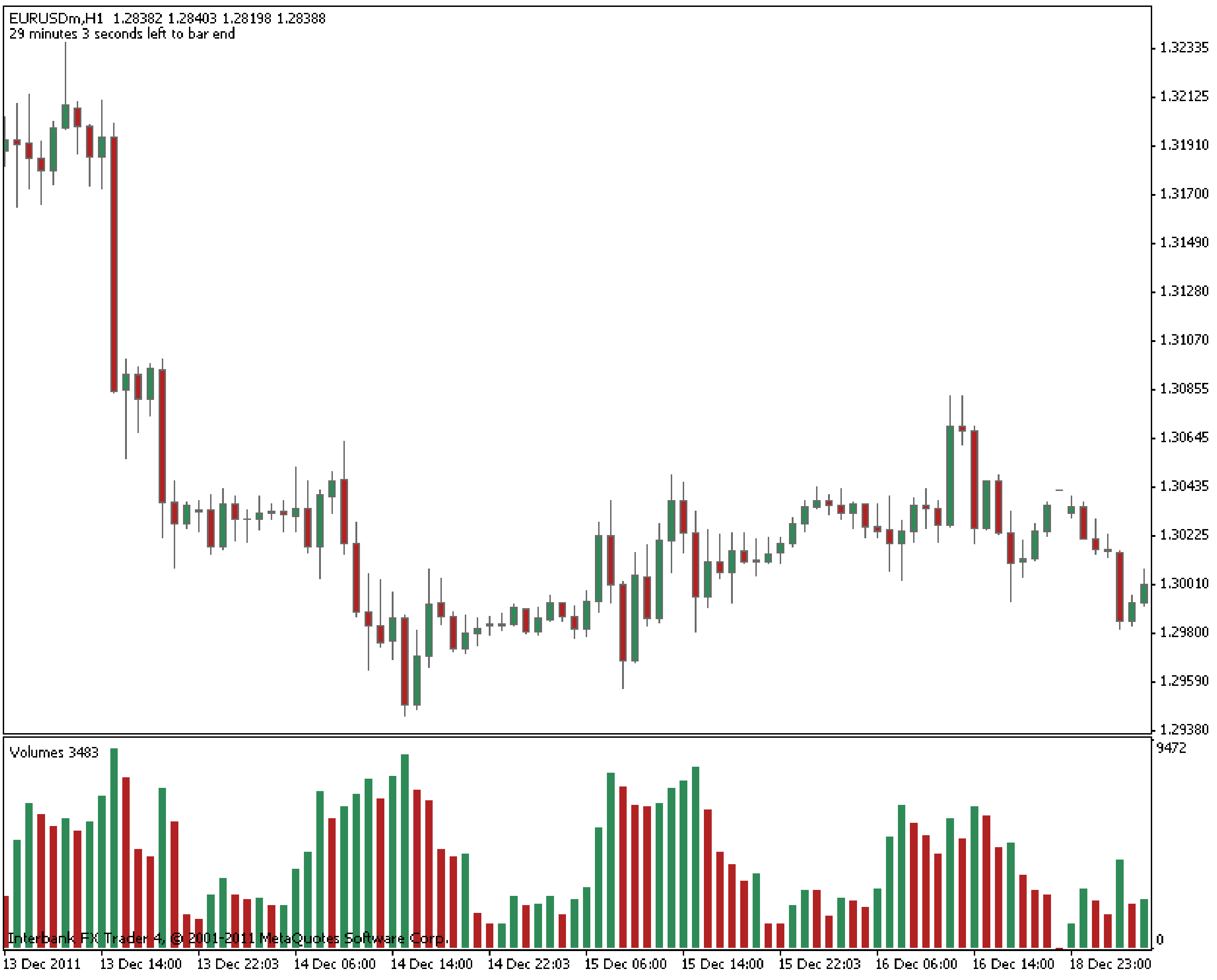
I trade using Volume spread analysis or VSA as it's called. This is a way to determine how the 'Smart money' is moving the market, simply by using the Volume indicator that comes with almost every platform. Smart money is the term for the people that control the market. Another word for them is 'Professional money' and this usually involves banks, market makers and institutional money. This is a system, rigged to take your money, that's why it's there. With VSA you're going to learn how to read the market and trade along the Smart money, this will increase your success significantly.

Let's begin!

The Naked Chart

The first thing I was taught when I started with VSA was "All you need is a naked chart and Volume to realize" and that is what I love about VSA. You don't need to use all these indicators that you probably are used too. The only thing you need is Volume to actually realize what's going on in the market and what's going to happen next. When you master these concepts you'll be irresistible on the market! Remember, it takes time to master the market, it won't happen overnight! This book will help you get there and you'll probably have to read it a couple of times to make it stick in your head, good thing it´s short then, right?

All you need is a clean chart like this!

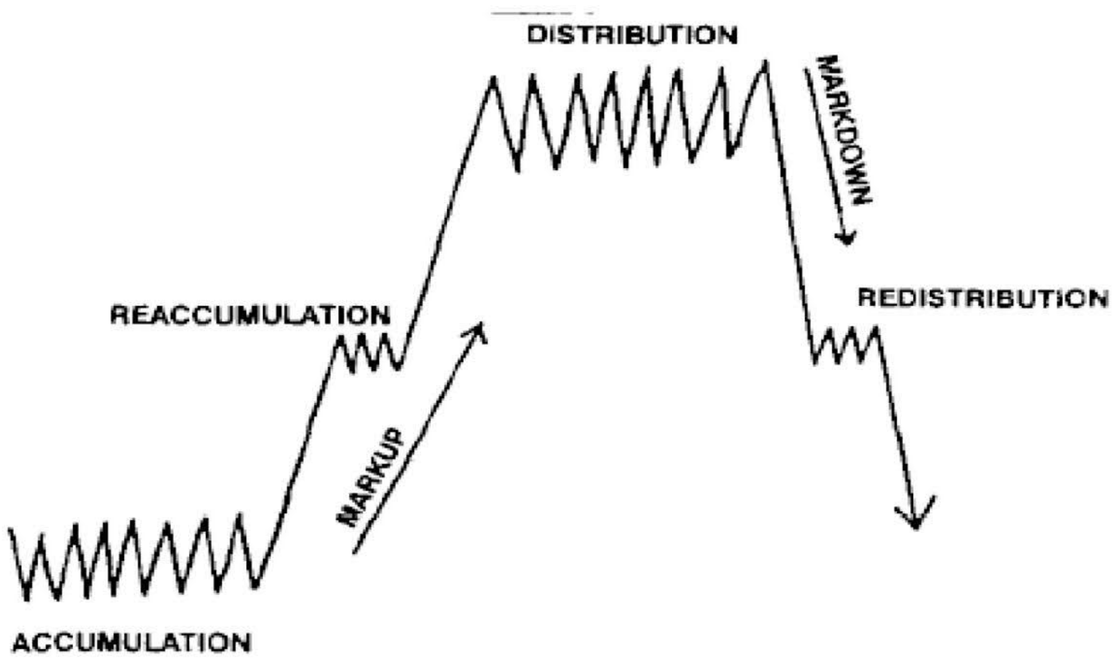


Market Phases

The market goes through different phases and cycles and this is all controlled by the Smart money. I bet you've been in a situation when you just have to buy! You think that the lasting up-trend is going to last forever! But it's usually too late by then. This is exactly what the Smart money wants, otherwise they wouldn't be able to run you over and take your money. The primary thing about Smart money is that they sell into up-moves and buy into down-moves, this is because they want to trap the "herd" as they are called, the people that get their stops eaten up by Smart money.

This image below is from the early 1900's and it still holds true…

Conception of Primary Market Phases



Accumulation: The establishment of an investment or speculative position by professional interests in anticipation of an advance in price.

Markup: A sustained upward price movement.

Distribution: the elimination of a long investment or speculative position.

Markdown: A sustained downward price movement.

Accumulation – This is where Smart money build up their long (buy) positions before they begin with the markup (up-trend). This is also a place where the “herd” is short and where they believe that the markdown (down-trend) will last forever. The Smart money buys on down candles to make it look like there’s still selling going on and that the market will continue downwards, this causes the candles with a big wick on the bottom.

Markup – This is where the “up-trend” begins and the Smart money has now the control over the buying and selling in the market. They now start to run over all stop losses on short positions which is help by the “herd”.

Reaccumulation – The Smart money starts to Reaccumulate the market, trapping everybody to think that the market will turn and go down again, but that is not the case, they build up more positions to continue the markup. When they do this the “herd” is usually stationed short again. All they want to do is to trap the “herd” so they can get as much money as possible from them.

Distribution – The market has now hit the highest ground on this current up-move and the Smart money will not be stationed long anymore. Now the cycle starts over, they start to Distribute the market and build up their short (sell) positions. At this point everybody (the herd) that was short before has now switched over to long… But it’s too late to buy…

Markdown – This is just the opposite of Markup. Smart money has yet again the control in the market so the “down-trend” begins and Smart Money run over everybody that is stationed long.

Redistribution – This is also the opposite of Reaccumulation and works just the same way.

When the market is in these phases you’ll see that price often bounce up and down or “range” as you can call it. This is because Smart money is trying to get the best price they can out of it. Let’s say that we’re in Accumulation phase and you see that price is ranging. This is because there’s still a lot of selling going on in the market, you know the herd is short so what the Smart money wants to do is to buy and then (depending on how many sellers there is) let price fall down again so they can buy even more, all to get the best price they possibly can.

Volume Spread Analysis - VSA

I want you to pull up a chart and add the Volume indicator to get a look on it. You'll see that some volume bars are red and some are green. Red means that the volume was lower than the previous volume bar and green means that the volume was higher than the previous bar, so nothing really fancy there, just makes it easier to spot higher & lower volume.
The bars that appear on your Volume indicator shows you the amount of activity that occurred during a specific candle. Low volume does not mean that the market will fall and High volume does not mean that the market will rise, it all lies in the candles. That means, a high volume UP candle with a wick on top usually means weakness in the market, especially when it's seen on an area of supply. When you've seen this you can in most cases expect a down-move in the near future (Just the opposite with a high volume DOWN candle into an area of demand). One key thing to always remember is that Weakness is shown in UP bars and Strength is shown in DOWN bars. Smart money wants to hide their actions, that's why they sell on up bars and buy on down bars. It's that simple.

When you see price entering an area of Supply or Demand on high volume, be careful to trade into that area because if the volume is high you'll probably see a reversal there.

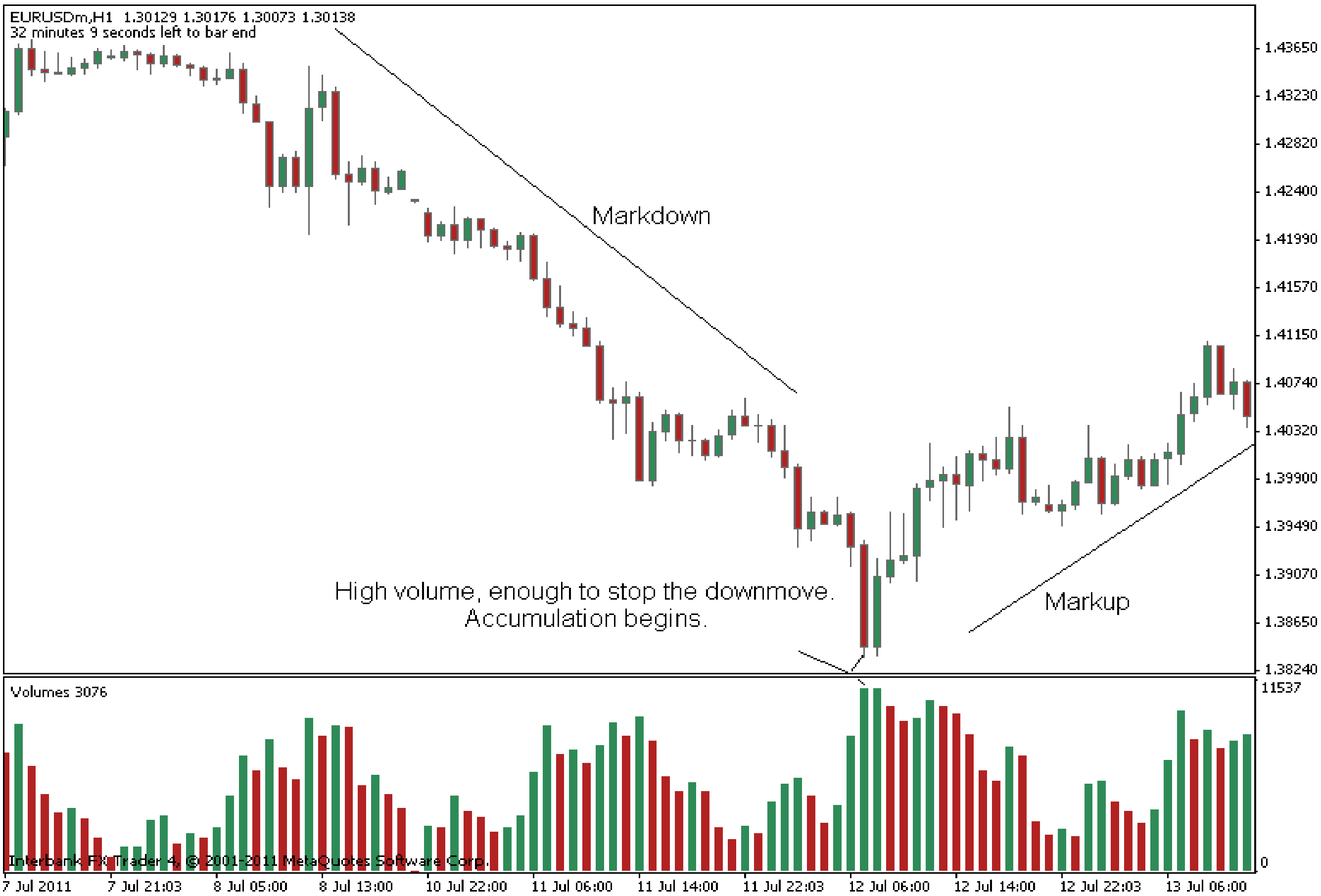
The tool I probably use the most (besides volume) is the Fibonacci Retracement tool, this is actually so powerful that you don't need anything else besides some hand drawn Supply & Demand lines. When spotting reversal points it's important to look for Supply and demand areas because this is where you're going to enter the market if volume tells you to. When I use the Fibonacci Retracement tool I ONLY look at the 50-61.8 levels. These levels are very important when it comes to reversals. Believe it or not but you'll probably see 80% of the reversals at these levels. *But why is that?* Many stop losses from the herd are hiding there and it's the Smart moneys "stop-hunt" going on. There're also a lot of orders between those levels, that's why we usually see an increase in volume there, because huge buying/selling appears.

Let's say we are looking at Distribution, followed by the markdown. Later price hits a stop (on low volume) and retraces a bit, we now take out our Fibonacci Retracement tool and draw it from high to low and then watch how the volume evolve when price reaches the 50-61.8 levels. You'll get stunned when you see how often price retrace at these levels, try to spot it yourself and you'll see what I'm talking about! I will show you an example later.

VSA in action!

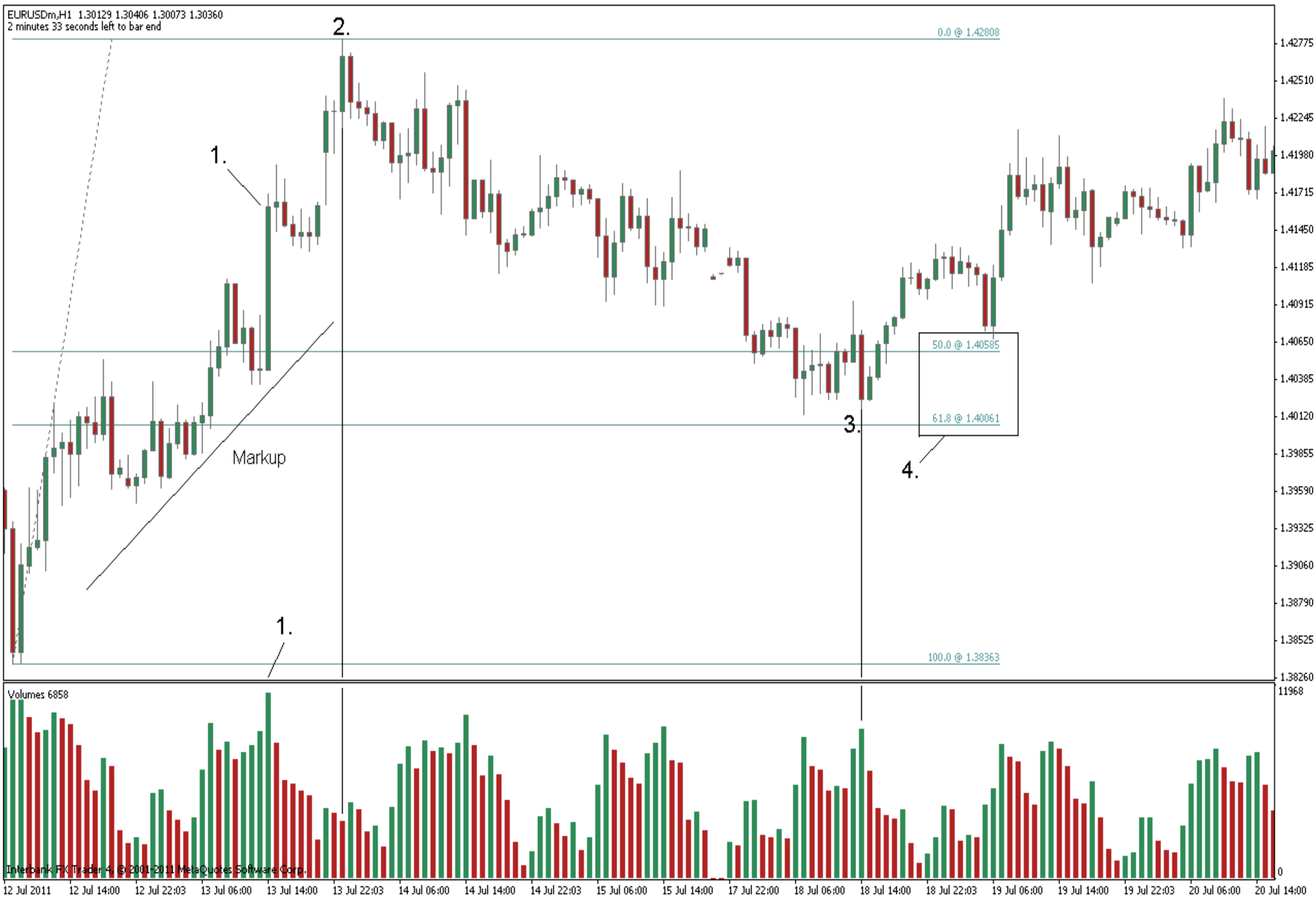
This is how I use volume to determine the phase.

Accumulation



The first thing you'll see in this picture is that it starts with a Markdown. The next thing you'll see is a wide spread down bar with high volume, higher than any volume during this markdown (which is crucial), we also see a bullish inside close (the bar to the right of the one that is marked). This tells us that there was enough buying to stop the down-move, otherwise there wouldn't have been a bullish inside close there. The inside close is crucial when determing stopping volume. If price would have continued down then we know that this was in fact not enough volume to stop the down-move. Now when we have an inside close we know that the Smart money will start accumulate price. In this case it went really fast from Accumulation to Markup as you can see, it usually takes some time and price will bounce up and down before shooting up.

Reaccumulation



We see the markup here from the previous picture.

(The one marked with 4. Is the Fibonacci Retracement tool with the levels of 50-61.8. It might be hard to see)

1. We see high volume and a wide spread up bar so this has to be the top right? No it does not have to be the top, remember what I talked about in the previous picture, It's all about the next candle and in this case the next candle closes Up (bullish) on relative low volume so that indicates that there was still buying going on.
2. Price continued up after hitting that potential end of the up-move and here you see it's very low volume on the top. This indicates that there was not much interest in selling by the Smart money, so we can expect higher prices to come, not necessarily right now but in most cases price would not be "done" up there and will test that area again (if not a high amount of supply appears). Now is a good time to draw your Fibonacci Retracements from low to high.
3. We see price entering the 50-61.8 Fibonacci Retracement on high volume and as I told you earlier, this is usually where price like to retrace and as you can see it does.

(Distribution and Redistribution works the same way as Accumulation and Reaccumulation that's why I won't include those examples aswell (keeping it short & simple).)

That's about it!
Now you know the basics of how you can benefit from trading with VSA, I hope this was short and simple enough for you, if you had a hard time understanding the concepts, read it again, if it still is hard to understand just ask me and I'll help you out as best as I can.

Thanks for reading,
Danny K

We have come to an end of this basic course. This is how it works and how you can benefit from trading with the phases instead of trading against them. With this knowledge you'll be a better trader and if you stick to the phases and trade along them, you'll suffer a lot lesser losses and your win percentage will increase significantly, at least it did for me!

Don't forget to read it again and again, until it sticks in your head!

Thank you for reading and may the phase be with you.
Good luck!

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