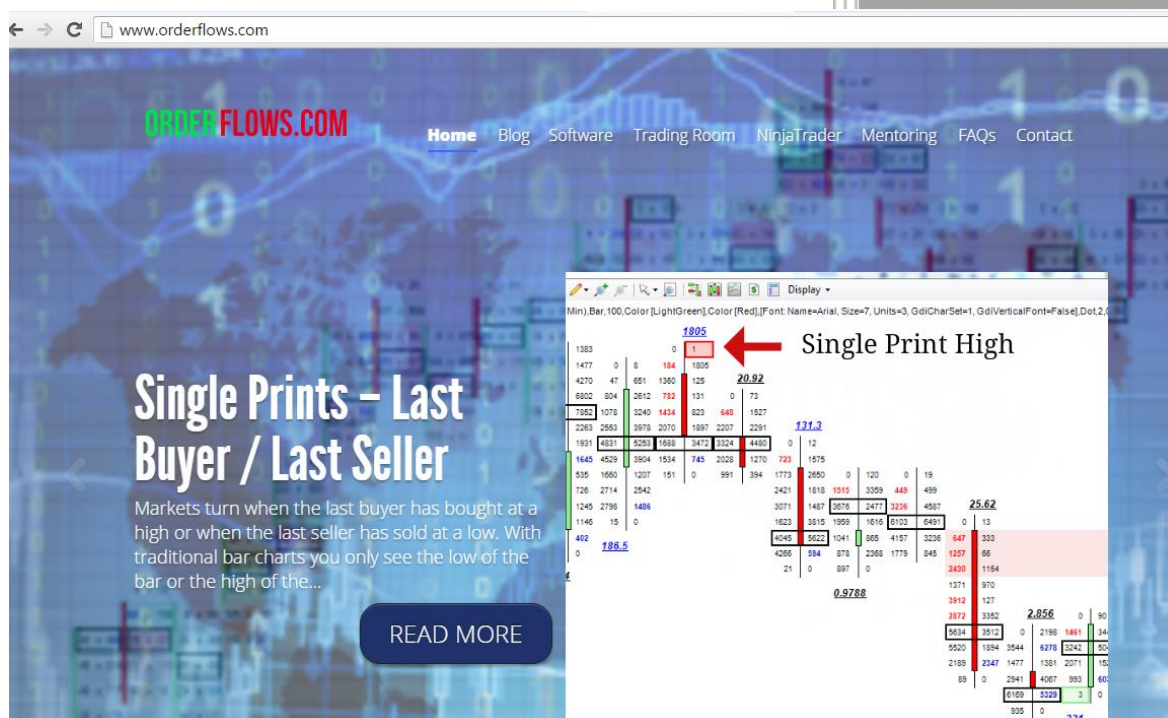


The Importance Of Ratios In Orderflow Analysis



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Single Prints / Small Prints Ratio

Here is how the futures markets work. You have a number of different participants trading different times frames in the markets. You have the institutions which are banks, hedge funds, commercial end users, legitimate hedgers and a few others. Then you have the retail traders.

The retail traders are in the market trying to trade the market back and forth, usually closing their positions by the end of the trading day. Most retail traders are in the markets for the shorter term trying to take some money out of the market using their lagging indicators.

The institutions, the big players, generally have a firm grasp on the fundamentals that move the markets mainly because that is their business. Their intimate knowledge of the fundamentals is priced into their analysis of the market. When a big institutional commercial end user like Cargill comes in is buying 3000 bushels of corn they are doing it because they often have a need for the commodity. It can be for a delivery or they may have a view that the price may be going up due to increased demand or whatever it doesn't really matter what their reason is. What you are looking for in order flow is when the institutions come in and start building their positions. Now it doesn't mean that this level of institutional buying is going to become support in the market, they have to start buying somewhere. These guys don't sit in front of a chart looking at squiggly lines on their charts, when they want to get in, they get in.

Why do prices stop? It stops because there is no more buying or selling. No more orders coming into the market. Its not complicated.

So in the order flow you see that price is starting to move higher on bigger passive bids and some aggressive buying which is usually the short term traders who sold earlier and are now covering their losing positions. The retail trader noticed price has stopped going down so they need to cover their positions which then gives price an extra little boost. Other short term traders notice price start to move up and by now their indicators are saying that the market is going to go higher and they start to buy, but the move has already happened.

So what happens when the last buyers come into the market? The order flow shows you that the last buyers have come into the market because of their decreased volume. Often times it culminates in a single print or a small print ratio.

Institutional traders are fully aware of any weakness in the market. If you see a small print at or around the high, this is indicating no more demand, a sign of weakness and you have a potential short position.

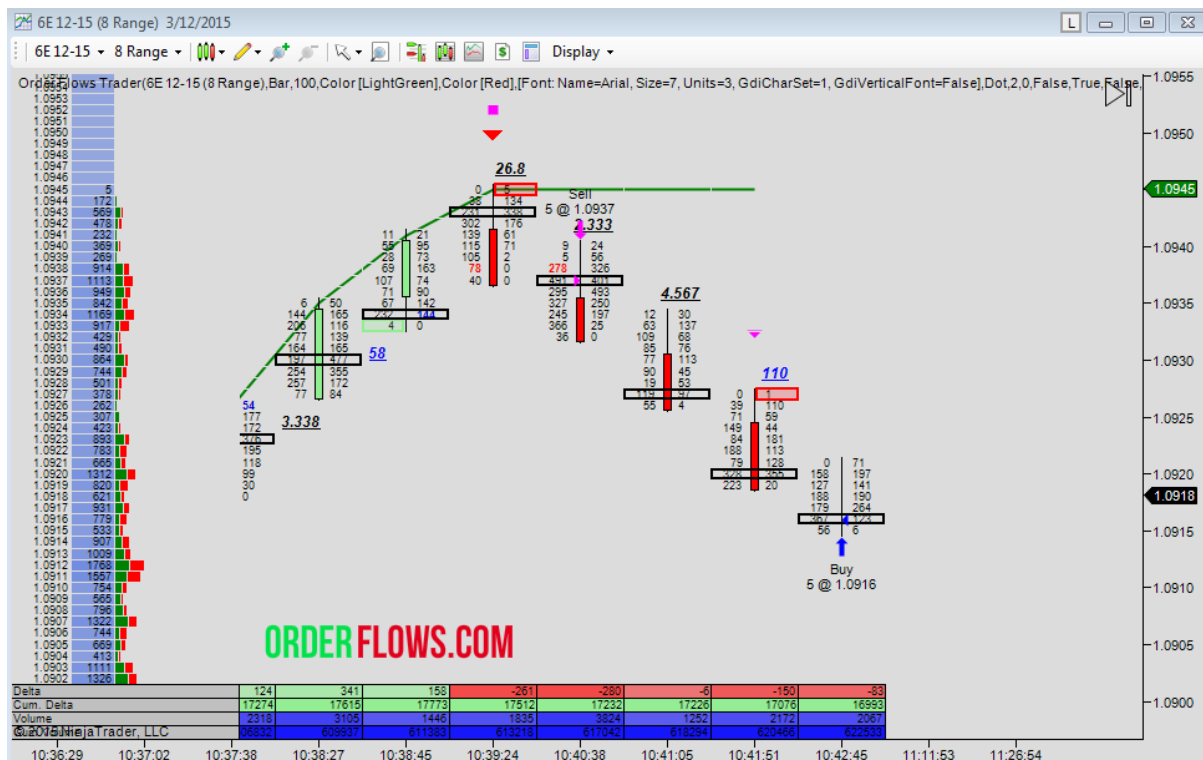
For a market to continue to rally there needs to be increasing volume. If the volume is low this shows no demand from institutional participants. They are not interested in the up-side. This is why looking at volume is so important. Institutional traders cannot hide the volume of trades executed. Institutional participation is seen in the volume and when their volume does not back a move higher, more often than not the reason the institutions are not buying is because at this moment, they are not bullish.

What my Orderflows Trader software does is it highlights when a single print appears and also when a small print appears. Ok I know what you are thinking, a single print is easy to see on a chart, I agree, but sometimes you miss it. Orderflows Trader will put a box around it, a red box if it bearish or a green box if it is bullish. That is just for an easy visual of the single print. The important number is the small print ratio, which is the number above the red bar or below the green bar.

What is so important of the small print ratio? The small print ratio shows you that when buying or selling has dried up in a move. How does the software show you? You will see a number in BLUE above a red candlestick when it is bearish or a BLUE number below a green candlestick when it is bullish. If the ratio is neutral it will appear in black.

The small print ratio is calculated using the numbers at the top of the bar for a down bar or in the case of a bar that is trading higher, a green candlestick, the numbers on the bottom of the bar. The result is a number which if it is 30 or greater will be printed in BLUE. I have found when the ratio is greater than 30 that it is a very good indication that buying or selling has dried up and the market is ripe for a move. I used to use a ratio of 25 but have 30 to be slightly better. The ratio is not a line in the sand that has to meet the requirement, what is important is the numbers that make up the ratio.

Here is trade I took in the 6E this morning. We hit a high, there was divergence, there was a single print, but the ratio was 26.8. It wasn't 30, but close enough for me to look more closely at the volume itself and determine if I should take a trade or not.



You can actually adjust the ratio if you want to make the ratio to show when the ratio number is much higher, like say 100. In the software the setting is called RATIO BOUNDS HIGH. It is adjustable. 30 is my starting point. Even though a ratio might be 31 and on another bar it might 760. I would treat them the same for the most part. They are both important. I don't necessarily find that the more higher the ratio the better the signal.

As I said earlier, order flow analysis should be in context of the market. When looking at single prints / small prints it signals buying or selling has dried up. So where do you want to see those prints? You want to see them at highs or lows. Seeing them in the middle of a move is great for confirmation but what you are really looking for a reason to buy when the last seller has sold or sell when the last seller has sold.

Think of small prints as lack of demand. It is the lack of demand from the institutional traders that causes a market to drop from highs. There is no institutional support to help move the market higher.

If selling has decreased on any down move, the market will then want to go up as there is no selling pressure. If institutional money was still bearish there would be an increase in selling on the downside not a decrease.

If buying has decreased on any up move, the market will want to fall as there is no demand.

Small prints / Single prints usually means the market is not accepting the higher or lower prices and could indicate a turn. A market that is topping or bottoming out does not spend much time at the extremes, so there will be little volume at these price points.

BIG NUMBERS – EXCESSIVE VOLUME

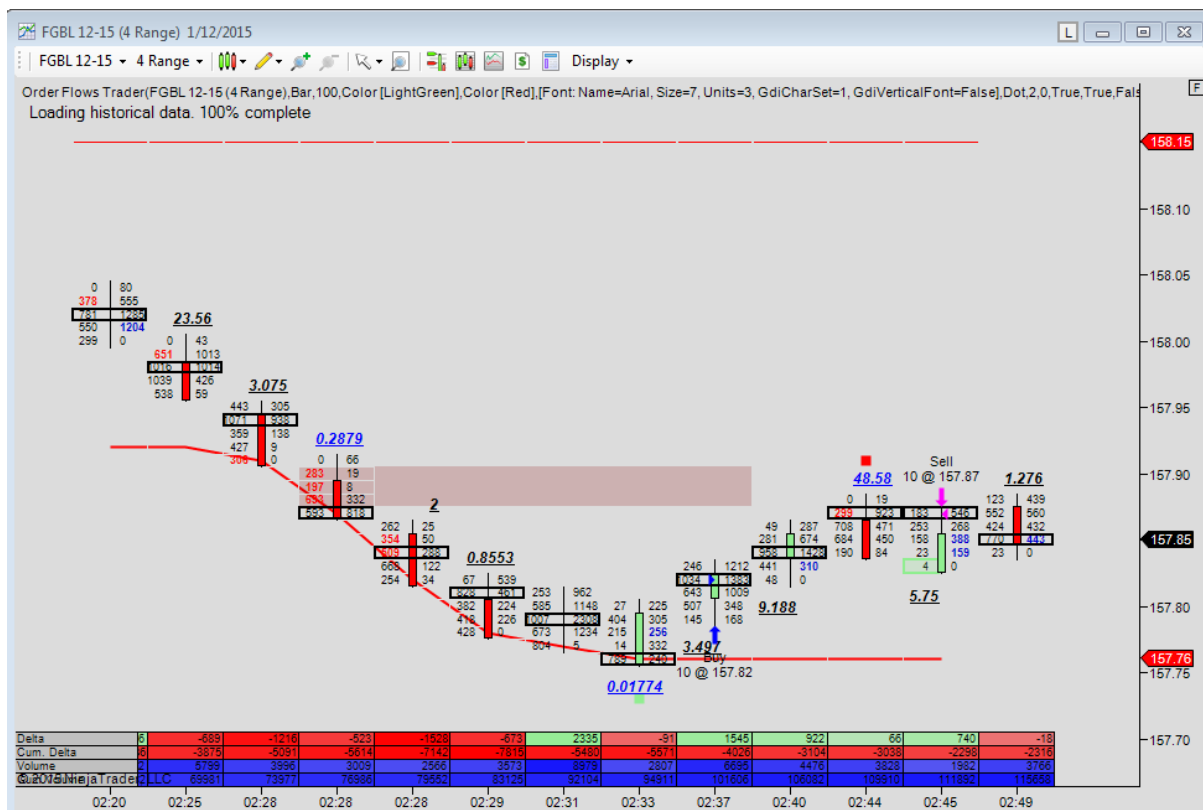
The beauty of Orderflows Trader is that it also allows you to see where the institutions can be accumulating a position either because it is a good price or distributing their inventory because they think the price is high and they want to book some profits (remember big institutions don't start selling when they think price is going to go higher). This is often seen when you get big numbers appearing at the top or bottoms of bars.

Orderflows Trader will show you when there is heavy volume at the top or bottom of a bar by printing a BLUE number that is less than 0.5. This is called RATIO BOUNDS LOW. What this indicates is that the market was moving but stopped and turned on heavy volume at the end of the bar.

Why is this important?

In a market that is rallying, one of the ways to stop the rally is for a big seller to come in and offer a ton of supply. That is not unique to the futures market. Imagine you sell fish and all of a sudden another person stands next to you with a big basket of fresh fish, there is all of a sudden a lot of supply on offer and if you want to sell your fish you more often than not have to lower your prices as less and less customers buy from you.

In a market that is selling off, think of it in the opposite terms. The way a declining market can stop is if a big buyer comes in usually in the form of an institution who has picked a price level they think the market is cheap and want to buy it.



Back to the RATIO BOUNDS LOW indicator set up. For a down bar or red candlestick if the number is below 0.5 the number will appear on top of the bar in BLUE, just like the RATIO BOUNDS HIGH number would, only it will be a small number of less than 0.5. For a number above 0.51 it will appear in black and is neutral. When you see a BLUE number less than 0.5 it indicates that there is strong buying at the bottom of the bar.

Excessive volume at tops indicates supply in the market which is most likely swamping demand and will cause the market to sell off.

Institutional buying, an absorption of supply, will usually stop a down move. This often marks the end of a down move.

Stopping volume is a good sign of strength – it results from big limit orders that are large enough to stop a down-move or up-move. Most of the time, only institutional participation can do this and is a good sign of strength.

Big volume numbers at the top of an up-move often indicates there is supply in the market and as a result prices should start to fall. The big volume should be more on the offer side than the bid side as evident by traders trying to buy and move the market higher but were met with strong sellers.

One caveat to note, just because we have a big volume top or bottom doesn't not necessarily mean the market will all of a sudden change direction and move 20-30 points. Sometimes it means the market may be resting before continuing its next move. Look for more information to confirm the market's strength or weakness.