



Candlestick Patterns

Analysis Toolbox



Reversal Chart Patterns

Disclaimer

The candlestick patterns explained in this presentation are for information purposes only. Candlestick patterns are used to supplement your chart analysis and are not meant to be used on their own without other confirmations.

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Reversal Chart Patterns

Notes

We learned that there are two types of patterns: Continuation and Reversal. Reversal patterns occur at the end of a trend. Continuation patterns occur during the trend and are merely pauses or consolidations in the trend.

Several things occur at market reversal points: At market tops, traders are greedy and at market bottoms, traders and investors are fearful – both sentiments lead to market extremes, even in currencies!

At either extreme, there is a major trend line break – so plot those trend lines! Also, price tends to deviate from the moving averages so look for the rubber band effect! Certain candlestick patterns emerge at the end of the trend – this is where you tend to see long wicks and patterns such as bullish and bearish engulfing, morning and evening stars, hammers, shooting stars, and tweezer tops and bottoms.

Finally, the longer the pattern takes to materialize, and the larger the pattern, the further the prices will move outside of that pattern, and the greater its importance. That doesn't mean that these patterns aren't found on shorter time frames – they are, but they need to be traded nimbly with definitive profit objectives and stop losses.



Reversal Chart Patterns

Reversal Chart Patterns

Markets are fractal, meaning that chart patterns form repeating arrangements or shapes in any time frame.

Classical technical analysis books defined chart patterns in the 70's that are still true today.

Correctly identify these patterns to determine future trading opportunities.

Reversal chart pattern recognition helps determine change in market sentiment and time entries and exits.

All chart patterns have measured objectives.



Reversal Candlestick Patterns

Reversal Candles

Reversal Days are also called Top or Bottom Reversal Days, Buying or Selling Climaxes, and Key Reversal Days. Learning how to trade them can get you into a trend reversal early.

Two Day Reversals are also quite common, as sometimes it takes two days for the market to reverse itself.

Topping and bottoming fractals are 3-day formations found at the top and bottom of markets and can get you into the new trend early.

Reversal Candlestick Patterns

Reversal Candles – Reversal Days

Reversal Days are also called Top or Bottom Reversal Days, Buying or Selling Climaxes, and Key Reversal Days. Learning how to trade them can get you into a trend reversal early.



In the case of a market top, a new high forms that period, but price closes in the bottom 25% of that period's trading range. The longer the wick, the more powerful the move will be in the opposite direction.



In the case of a market bottom, a new low forms that period, but price closes in the top 25% of that period's trading range.

Trade entry: For a market top, place a sell stop order below the low of the reversal day. For a market bottom, place a buy stop order above the high of the reversal day. Place the stop just above the high of the top or below the low of the bottom.

Reversal Candlestick Patterns

Reversal Candles – Topping and Bottoming Fractals

Topping and bottoming fractals are 3-candle formations found at the top and bottom of markets and can get you into the new trend early.



In the case of a market top, the fractal high (candle 2) is higher than the high of the previous candle (candle 1) and the high of the subsequent candle. (candle 3)



In the case of a market bottom, the fractal low is lower than the low of the previous candle and the low of the subsequent candle.

Trade entry: For a market top, place a sell stop order below the low of candle 3. The stop is above the candle 2 or 3 highs, preferably above the candle 2. For a market bottom, place a buy stop order above the high of candle 3. The stop is below the candle 2 or 3 lows, preferably below the candle 2.



Reversal Candlestick Patterns

Candlestick Patterns

The Japanese have used candlesticks as a charting and analysis technique for centuries.

Candlesticks mostly help pick tops and bottoms and are most powerful when they confirm a western indicator.

Candlestick patterns are psychological imprints of what traders are thinking at any given time.

There are approximately 40 reversal candle patterns that vary from single candlesticks to groupings of up to five candlesticks.

Reversal Candlestick Patterns

Determining Who Won The Battle

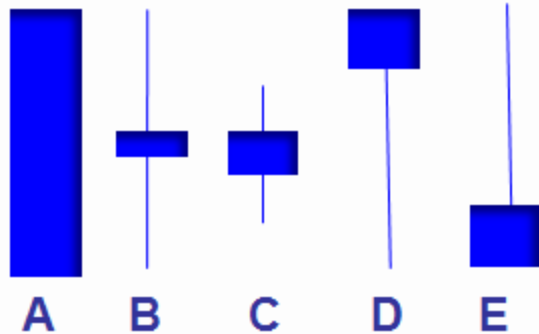


Bulls or Buyers
Win

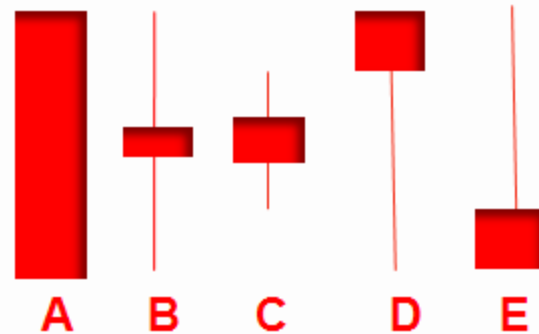
Bears or Sellers
Win

Understanding Candlesticks

Buyers Win



Sellers Win



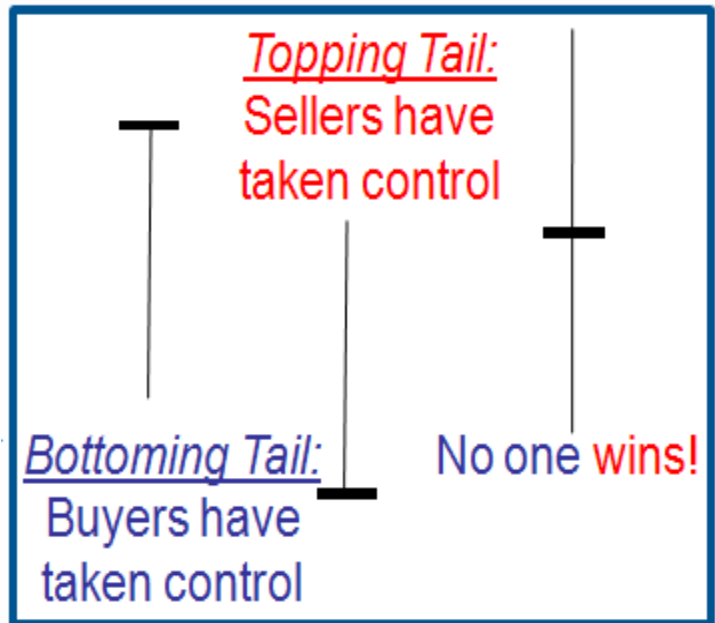
"A" – wide range body with no tails or shadows – very bullish or bearish for a trend move

"B" - opening and closing prices are practically identical – no real control – a pause

"C" shows a very small trading range with a narrow-range body – a pause with no major follow-thru

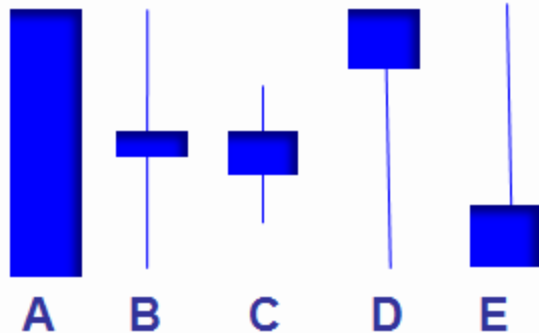
"D" shows the opening and closing near the high with a long bottoming tail or shadow

"E" shows the opening and closing near the low with a long topping tail or shadow

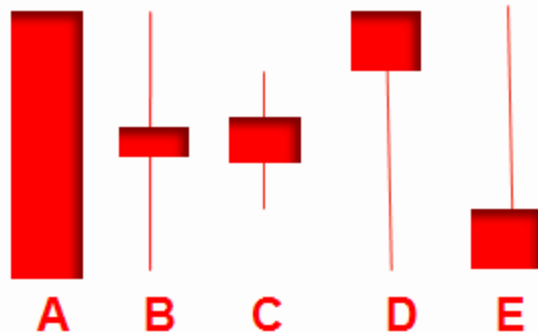


Understanding Candlesticks

Buyers Win



Sellers Win



Which is 'most' bullish or bearish of these candles?

You might say that "A" is the most bullish or bearish candle. And it is very bullish or bearish in a strong up- or down-trend. But in some cases, "D" on the left can be more bullish and "E" on the right can be more bearish.

In the case of "D", a battle was fought, and at one point, the shorts were in control. By the end of the bar, the longs fought all the way back and actually brought the currency pair above the opening price. This candle, if located at the bottom of a down-trend, can potentially signal a reversal in the trend. The same is true for the sellers in "E" on the right.

Reversal Candlestick Patterns

Bullish and Bearish Patterns

**Candlestick Patterns:
Illustrated Examples
that are opposites of
each other**

Bullish Patterns

Bullish Engulfing
Morning Star
Hammer
Inverted Hammer
Piercing Pattern
Tweezer Bottom

Bearish Patterns

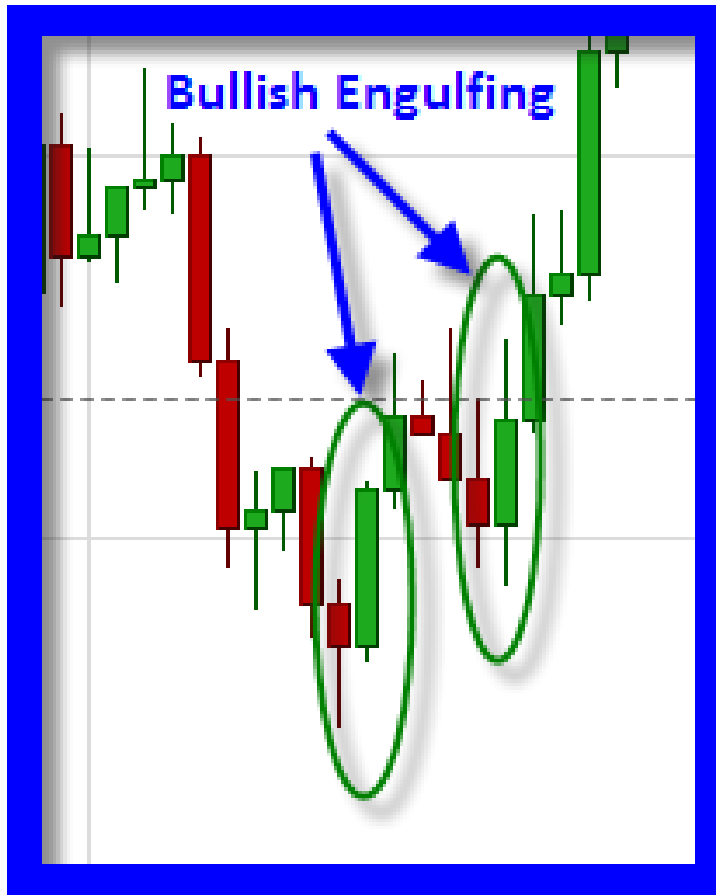
Bearish Engulfing
Evening Star
Hanging Man
Shooting Star
Dark Cloud Cover
Tweezer Top

Dojis – Candles of Indecision

Perfect, Long-legged, Dragonfly, Gravestone

Reversal Candlestick Patterns

Bullish and Bearish Patterns



Bullish Engulfing Pattern

Market is in a definable downtrend.

Candle 1 has a small red real body.

Candle 2 reverses where the green body completely engulfs the previous day's red body.

A stronger signal occurs when the green reversal candle body engulfs two or more bodies.

Reversal Candlestick Patterns

Bullish and Bearish Patterns



Bearish Engulfing Pattern

Market is in a definable uptrend.

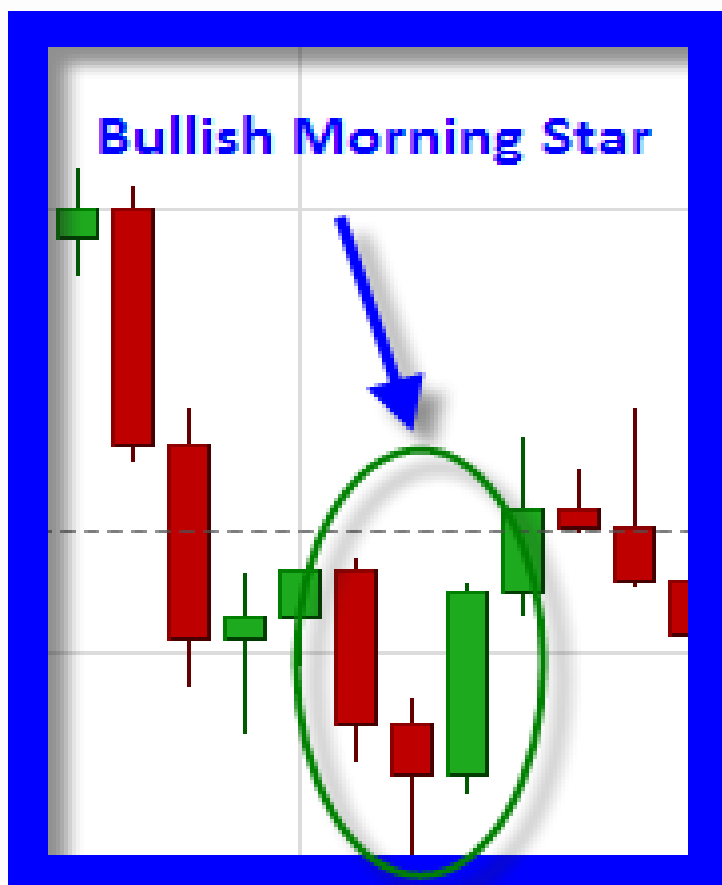
Candle 1 has a small green body in an uptrend.

Candle 2 reverses where the red body completely engulfs the previous day's green body.

A stronger signal occurs when the red reversal candle body engulfs two or more bodies.

Reversal Candlestick Patterns

Bullish and Bearish Patterns



Bullish Morning Star Pattern

Bullish three-candle pattern at swing lows.

Candle 1 has a tall red real body.

Candle 2 has a small red or green body.

Candle 3 closes at least 50% into the first real body and is a tall green candle.

Reversal Candlestick Patterns

Bullish and Bearish Patterns



Bearish Evening Star Pattern

Bearish three-candle pattern at swing highs.

Candle 1 has a tall green real body.

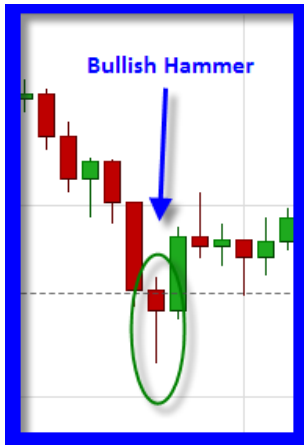
Candle 2 has a small green or red real body.

Candle 3 closes at least 50% into the first real body and is a tall red candle.

Reversal Candlestick Patterns

Bullish and Bearish Patterns

Bullish Hammer



Bullish Hammer

Small real bodies (either green or red).

Real bodies are near high of the session with very long lower shadows (at least 2-3 times the height of the real body).

A hammer appears at the bottom of the decline (market hammering out a base). It is bullish.

Bearish Hanging Man



Bearish Hanging Man

Hanging man appears after an uptrend. It is bearish.

Reversal Candlestick Patterns

Bullish and Bearish Patterns

Inverted Hammer



Shooting Star



Bullish Inverted Hammer

The Inverted Hammer is a bottom reversal candle, and the following day is a strong bullish day, that confirms the reversal signal.

Bearish Shooting Star

The Shooting Star is a top reversal candle, just like the hanging man. However, it displays a long upper shadow, and its small real body is at or near the lows of the session.

The Japanese say that the shooting star shows “trouble overhead”. Because of the bearish long upper shadow, we don’t need as much bearish confirmation as we do with a hanging man.

Reversal Candlestick Patterns

Bullish and Bearish Patterns

Piercing Line (not 24 hour Forex)



Dark Cloud Cover (not 24 hour Forex)



Bullish Piercing Line

The body of the first candle is red where the sellers are in control and the body of the second candle is green. In non-Forex markets, the 2nd candle gaps down to open lower than the previous candle close, and ends up closing more than half-way through the first candlestick. In Forex markets, the candle opens at the close of the previous candle, trades lower and ends up closing more than 50% higher.

Bearish Dark Cloud Cover

The 2nd candle gaps open above the 1st candle close and ends up closing at least 50% into the body of the 1st candle. In 24 hour Forex markets there are no gaps so this pattern looks different in Forex.

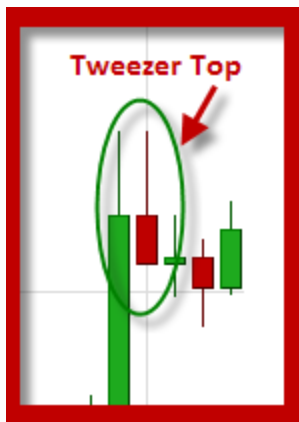
Reversal Candlestick Patterns

Bullish and Bearish Patterns

Tweezer Bottom



Tweezer Top



Bullish Tweezer Bottom

Any two candles qualify as Tweezer Bottoms providing they have the same price low and are situated in a downward price trend. The twin low price signals support for the market traded.

Bearish Tweezer Top

Any two candles qualify as Tweezer Tops providing they have the same price high and are situated in an upward price trend. The twin high price signals overhead resistance for the market traded.

Reversal Candlestick Patterns

Bullish and Bearish Patterns

Candlestick Patterns:

Patterns of Indecision

Dojis

Perfect Doji



Long-legged Doji



Dragonfly Doji



Gravestone Doji



Characterized by equal open and close prices.

When the Doji appears at a major trend line, channel line, key support and resistance, it is an indication of a potential reversal.