CANDLESTICK PATTERNS

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BULLISH HAMMER

Definition

- This pattern occurs at the bottom of a trend or during a downtrend and it is called a Hammer since it is hammering out of a bottom. It is a single candlestick pattern that has a long lower shadow and a small body at or very near the top of its daily trading range.

Recognition Criteria

- 1. The market is characterized by a prevailing downtrend.
- 2. A small body at the upper end of the trading range is observed. The color of the body is not important.
- 3. The lower shadow of this candlestick is at least twice as long as the body.
- 4. There is (almost) no upper shadow.
- Pattern Requirements and Flexibility
- The body of the Hammer should be small. The lower shadow should be at least twice as long as the body, but not shorter than an average candlestick. It is desired that there is no or a very tiny upper shadow. The bottom of the Hammer's body should be lower than both of the two preceding black candlesticks.

Trader's Behavior

- The Bullish Hammer appears in a downtrend and it sells off sharply following the market open. After the decline ceases, the market almost returns to the high of the day. Apparently the market fails to continue on the selling side. This observation reduces the previous bearish sentiment causing short traders to feel increasingly uneasy with their bearish positions. If the body of the Hammer is white, then the situation looks even better for the bulls.

Buy/Stop Loss Levels

- The confirmation level is defined as the top of the Hammer's body. Prices should cross above this level for confirmation.
- The stop loss level is defined as the last low. Following the BUY, if prices go down instead of going up, and close or make two consecutive daily lows below the stop loss level, while no bearish pattern is detected, then the stop loss is triggered.

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BULLISH ENGULFING

Definition

- This pattern is characterized by a large white body engulfing a preceding smaller black body, which appears during a downtrend. The white body does not necessarily engulf the shadows of the black body but totally engulfs the body itself. This is an important bottom reversal signal.

Recognition Criteria

- The market is characterized by a prevailing downtrend.
- A black body is observed on the first day.
- The white body that is formed on the second day completely engulfs the black body of the preceding day.

Pattern Requirements and Flexibility

- The length of the first black candlestick in Bullish Engulfing is not important. It can even be a Doji. However, the second one has to be a normal or long white candlestick. Either the body tops or the body bottoms of the two candlesticks may be at the same level, but in any case, the white body should be longer than the previous black body.

Trader’s Behavior

- While the market is characterized by a downtrend, lower volume of selling is observed with the occurrence of a black body on the first day. The next day, the market opens at new lows. It looks as if there’s going to be more bearish trading, however the downtrend loses momentum and the bulls take the lead during the day. The buying pressure overcomes selling and finally the market closes above the open of the previous day. The downtrend is damaged.

Buy/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross above this level for confirmation.
- The stop loss level is defined as the last low. Following the BUY, if prices go down instead of going up, and close or make two consecutive daily lows below the stop loss level, while no bearish pattern is detected, then the stop loss is triggered.

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BULLISH MORNING DOJI STAR

Definition

- This is a three candlestick pattern signaling a major bottom reversal. It is composed of a black candlestick followed by a Doji, which characteristically gaps down to form a Doji Star. Then, we have a third white candlestick whose closing is well into the first session's black real body. This is a distinctive bottom pattern.

Recognition Criteria

- The market is characterized by a prevailing downtrend.
- We see a black candlestick on the first day.
- Then, we see a Doji on the second day that gaps in the direction of the downtrend.
- A white candlestick is observed on the third day.

Pattern Requirements and Flexibility

- The Bullish Morning Doji Star starts with a black candlestick and it should continue with a doji that causes a gap opening lower than the close of the first day. The third day of the pattern is a white candlestick, which has the same or higher opening price with the Doji, and it should close well into the black candlestick that appears at the beginning of the pattern. The extent of how high this candlestick must close is defined according to the other candlesticks belonging to the pattern. The third day's closing must reach the midpoint between the first day's opening and the second day's lowest body level.

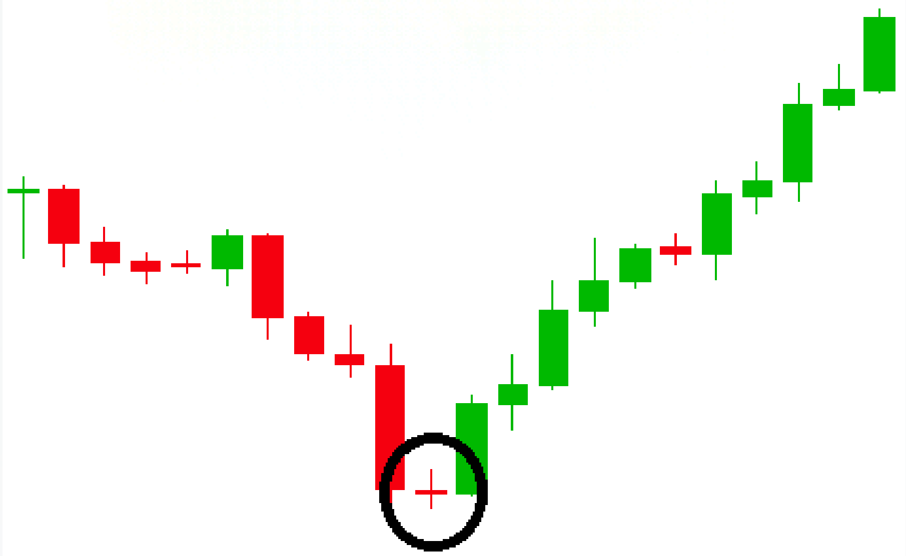
Trader's Behavior

- A downtrend is already established, and the black candlestick confirms the continuation of the downtrend. The appearance of the Doji that causes a gap indicates that bears are still pushing down the price. However, this tight price action between the open and the close shows indecision as well. On the third day, the body of the candlestick is above the previous day, trying to cover some of the ground from the down day. A significant trend reversal has occurred.

Buy/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross above this level for confirmation.
- The stop loss level is defined as the lower of the last two lows. Following the BUY, if prices go down instead of going up, and close or make two consecutive daily lows below the stop loss level, while no bearish pattern is detected, then the stop loss is triggered.

source: candlesticker.com



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BULLISH MORNING STAR

Definition

- This is a three-candlestick pattern signaling a major bottom reversal. It is composed of a black candlestick followed by a short candlestick, which characteristically gaps down to form a Star. Then we have a third white candlestick whose closing is well into the first session's black body. This is a meaningful bottom pattern.

Recognition Criteria

- The market is characterized by a prevailing downtrend.
- We see a black candlestick on the first day.
- Then, we see a short candlestick on the second day that gaps in the direction of the downtrend.
- A white candlestick is observed on the third day.

Pattern Requirements and Flexibility

- The Bullish Morning Star starts with a black candlestick and it should continue with a short candlestick (white or black) that opens with a gap down. The white candlestick appearing on the third day should open at or higher than the lowest level of the body of the second candlestick, and it should close well into the black candlestick that appears at the beginning of the pattern. The extent of how high this candlestick must close is defined according to the other candlesticks belonging to the pattern. The third day's closing must reach the midpoint between the first day's opening and the second day's lowest body level.

Trader's Behavior

- A downtrend is in progress and the black candlestick confirms the continuation of the downtrend. The appearance of the short candlestick that causes a gap indicates that bears are still pushing down the price. However, the tight price action on the second day between the open and the close shows indecision. The third day is a white body that moves into the first day's black body. A significant trend has occurred.

Buy/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross above this level for confirmation.
- The stop loss level is defined as the lower of the last two lows. Following the BUY, if prices go down instead of going up, and close or make two consecutive daily lows below the stop loss level, while no bearish pattern is detected, then the stop loss is triggered.

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BULLISH PIERCING LINE

Definition

- This is a bottom reversal pattern with two candlesticks. A black candlestick appears on the first day while a downtrend is in progress. The second day opens at a new low, with a gap down and closes more than halfway into the prior black body, leading to the formation of a strong white candlestick.

Recognition Criteria

- 1. The market is characterized by a prevailing downtrend.
- 2. A black candlestick appears on the first day.
- 3. A white candlestick opens on the second day with a gap down and closes more than halfway into the body of the first day.
- 4. The second day fails to close above the body of the first day.

Pattern Requirements and Flexibility

- The first day of the Bullish Piercing Line pattern is a normal or long black candlestick. The second day should open well below the close of the first day and close more than halfway into the prior black candlestick's body. However, the close of the second day must stay inside the body of the first day.

Trader's Behavior

- The market moves in a downtrend. The first black body reinforces this view. The next day the market opens lower via a gap, showing that the bearishness still persists. After this very bearish open, bulls decide to take the lead. The market surges toward the close, prices start to go up resulting in a close way above the previous day's close. Now the bears are losing their confidence and are reevaluating their short positions. The potential buyers start thinking that new lows may not hold and perhaps it is time to take long positions.

Buy/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross above this level for confirmation.
- The stop loss level is defined as the last low. Following the BUY, if prices go down instead of going up, and close or make two consecutive daily lows below the stop loss level, while no bearish pattern is detected, then the stop loss is triggered.

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BEARISH HANGING MAN

Definition

- The pattern occurs at the top of a trend or during an uptrend. The name Hanging Man comes from the fact that the candlestick looks somewhat like a hanging man. It is a single candlestick pattern that has a long lower shadow and a small body at or very near the top of its daily trading range.

Recognition Criteria

- 1. The market is characterized by a prevailing uptrend.
- 2. A small real body at the upper end of the trading range is observed. The color of the body is not important.
- 3. The lower shadow of this candlestick is at least twice as long as the body.
- 4. There is (almost) no upper shadow.

Pattern Requirements and Flexibility

- The body of the Hanging Man should be small. The lower shadow should be at least twice as long as the body, but not shorter than an average candlestick. It is desired that the upper shadow is very small, or better nil. The top of the Hanging Man's body should be above both of the two preceding white candlesticks.

Trader's Behavior

- The Hanging Man is a bearish reversal pattern. It signals a market top or a resistance level. Since it is seen after an advance, it signals that selling pressure is starting to increase. The long lower shadow indicates that the sellers pushed prices lower during the session. Even though the bulls regained their footing and drove prices higher by the finish, the appearance of this selling pressure after a rally is a serious warning signal. If the body is black, it shows that the close was not able to get back to the opening price level, which has potentially more bearish implications.

Sell/Stop Loss Levels

- The confirmation level is defined as the midpoint of Hanging Man's lower shadow. Prices should cross below this level for confirmation.
- The stop loss level is defined as the higher of the last two highs. Following the bearish signal, if prices go up instead of going down, and close or make two consecutive daily highs above the stop loss level, while no bullish pattern is detected, then the stop loss is triggered.

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BEARISH ENGULFING

Definition

- This pattern is characterized by a large black body engulfing a preceding smaller white body, which appears during an uptrend. The black body does not necessarily engulf the shadows of the white body but totally engulfs the body itself. This is an important top reversal signal.

Recognition Criteria

- 1. The market is characterized by a prevailing uptrend.
- 2. A white body is formed observed on the first day.
- 3. The black body that is formed on the second day completely engulfs the white body of the preceding day.

Pattern Requirements and Flexibility

- The length of the first white candlestick is not important. It can even be a Doji. The second one, however, has to be a normal or long black candlestick. Either the body tops or the body bottoms of the two candlesticks may be at the same level, but in any case, the black body of the Bearish Engulfing Pattern should be longer than the previous white body.

Trader's Behavior

- While the market is characterized by a definite uptrend, lower volume of buying is observed with the occurrence of a white body on the first day. The next day, the market opens at new highs. It looks as if there's going to be more bullish trading, however the uptrend loses momentum and the bears take the lead during the day. The selling pressure overcomes buying and finally the market closes below the open of the previous day. The uptrend is damaged.

Sell/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross below this level for confirmation.
- The stop loss level is defined as the last high. Following the bearish signal, if prices go up instead of going down, and close or make two consecutive daily highs above the stop loss level, while no bullish pattern is detected, then the stop loss is triggered.

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BEARISH EVENING STAR

Definition

- This is a three-candlestick pattern signaling a major top reversal. It is composed of a white candlestick followed by a short candlestick, which characteristically gaps up to form a star. Then we have a third black candlestick whose closing is well into the first session's white body. This is a meaningful top pattern.

Recognition Criteria

- 1. The market is characterized by a prevailing uptrend.
- 2. We see a white candlestick on the first day.
- 3. Then, we see a short candlestick on the second day that gaps in the direction of the uptrend.
- 4. A black candlestick is observed on the third day.

Pattern Requirements and Flexibility

- The Bearish Evening Star starts with a white candlestick and it should continue with a short candlestick (white or black) that opens with a gap up. The black candlestick appearing on the third day should open at or lower than the highest level of the body of the second candlestick, and it should close well into the white candlestick that appears at the beginning of the pattern. The extent of how low this candlestick must close is defined according to the other candlesticks belonging to the pattern. The third day's closing must reach the midpoint between the first day's opening and the second day's highest body level.

Trader's Behavior

- An uptrend is being observed, and the white candlestick confirms the continuation of the uptrend. The appearance of the short candlestick that makes a gap indicates that bulls are still pushing up the price. However, the tight price action on the second day between the open and the close shows indecision. The third day is a black body that moves into the first day's white body. A significant trend reversal has occurred.

Sell/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross below this level for confirmation.
- The stop loss level is defined as the higher of the last two highs. Following the bearish signal, if prices go up instead of going down, and close or make two consecutive daily highs above the stop loss level, while no bullish pattern is detected, then the stop loss is triggered.

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BEARISH EVENING DOJI STAR

Definition

- This is a three-candlestick pattern signaling a major top reversal. It is composed of a white candlestick followed by a Doji, which characteristically gaps up to form a Doji Star. Then, we have a third black candlestick whose closing is well into the first session's white real body. This is a meaningful top pattern.

Recognition Criteria

- 1. The market is characterized by a prevailing uptrend.
- 2. We see a white candlestick on the first day.
- 3. Then, we see a Doji on the second day that gaps in the direction of the uptrend.
- 4. A black candlestick is observed on the third day.

Pattern Requirements and Flexibility

- The Bearish Evening Doji Star starts with a white candlestick and it should continue with a doji accompanied by a gap opening higher than the close of the first day. The third day of the pattern is a black candlestick, which has the same or lower opening price with the Doji, and it should close well into the white candlestick that appears at the beginning of the pattern. The extent of how low this candlestick must close is defined according to the other candlesticks belonging to the pattern. The third day's closing must reach the midpoint between the first day's opening and the second day's highest body level.

Trader's Behavior

- An uptrend is being observed, and the white candlestick confirms the continuation of the uptrend. The appearance of the Doji accompanied by a gap indicates that bulls are still pushing up the price. However, this tight price action between the open and the close also shows indecision. On the third day, prices gap lower on the open and then close much lower. Bears have taken control of the market.

Sell/Stop Loss Levels

- The confirmation level is defined as the last close. Prices should cross below this level for confirmation.
- The stop loss level is defined as the higher of the last two highs. Following the bearish signal, if prices go up instead of going down, and close or make two consecutive daily highs above the stop loss level, while no bullish pattern is detected, then the stop loss is triggered.

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BEARISH DARK CLOUD COVER

Definition
- This is a top reversal pattern with two candlesticks. A white candlestick appears on the first day while an uptrend is in progress. The second day opens at a new high, with a gap up and closes more than halfway into the prior white body, leading to the formation of a strong black candlestick.

Recognition Criteria
- 1. The market is characterized by a prevailing uptrend.
- 2. A white candlestick appears on the first day.
- 3. A black candlestick opens on the second day with a gap up and closes more than halfway into the body of the first day.
- 4. The second day fails to close below the body of the first day.

Pattern Requirements and Flexibility
- The first day of the Bearish Dark Cloud Cover pattern is a normal or long white candlestick. The second day should open well above the close of the first day and close more than halfway into the prior white candlestick's body. However, the close of the second day must stay inside the body of the first day.

Trader's Behavior
- The market moves in an uptrend. The first white body reinforces this view. The next day the market opens higher via a gap, showing that the bullishness still persists. After this very bullish open, bears decide to take the lead. The market plunges toward the close, prices start to go down resulting in a close way below the previous day's close. Now the bulls are losing their confidence and are reevaluating their long positions. The potential short sellers start thinking that new highs may not hold and perhaps it is time to take short positions.

Sell/Stop Loss Levels
- The confirmation level is defined as the last close. Prices should cross below this level for confirmation.
- The stop loss level is defined as the last high. Following the bearish signal, if prices go up instead of going down, and close or make two consecutive daily highs above the stop loss level, while no bullish pattern is detected, then the stop loss is triggered.

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InVed (by Equity4Life IH Analytics Private Limited) is a SEBI registered Research Analyst (RN : INH000012351) firm based out of Jaipur.

We provide research/advisory services for short term trading as well as long term investing backed by a strong team of technical and fundamental experts.

InVed evolved by blending the Technical expertise of Equity4Life and Fundamental expertise of Investing Hut thereby giving wings to the Techno-Funda approach.

The company made a headway with like-minded people from diverse backgrounds with a mission to spread knowledge about investing through our research.

InVed is a combination of 2 words: “Investing” & “Veda” thereby depicting investing with knowledge and proper research.

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NEXT TOPIC

HOW TO IDENTIFY TREND

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