

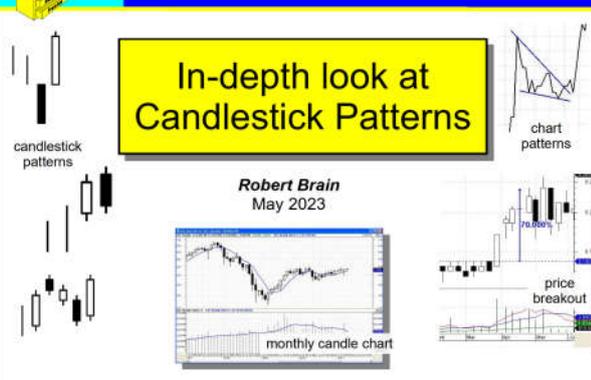
In-depth look at candle patterns

Brainy's Share Market Toolbox

In-depth look at Candlestick Patterns

Robert Brain
May 2023

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Candlestick Charts **Introduction**

About this presentation

This set of slides has been assembled from multiple presentations (with many new slides) for an international Convention/Workshop in Kuala Lumpur, July 2022; and with further update tweaks for the Melbourne ATAA webinar, August 2022, and some significant updates for STANZ in May 2023.

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Candlestick Charts **Introduction**

Candlesticks and candle patterns

- One candlestick on a price chart summarises the price action in one period (day, week, etc.);
- A *single candle* can tell a whole story about the opinions of the market participants;
- Multiple candles can form a specific *candle pattern* and tell even more of a story;
- But there are lots of candle patterns, so
- How to go about it?
- Here's an in-depth look at candle patterns.

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In-depth look at candle patterns

Candlestick Charts **Introduction**

Today's agenda

- Technical analysis "fundamentals" recap
- Candlestick basics:
 - origins
 - bars and candles
 - candle features (body, shadows)
 - candle interpretation
- Candle patterns – there are many!
- Candlestick addition

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Brainy's Share Market Toolbox

About... Robert Brain

Nimble Short term Investor
consultant, educator and part-time* share trader
web-based sharemarket-support business

- Many years experience as trainer, presenter, conference facilitator (*Scouts*)
- Share Market – active 15++ years* (slowly at first)
- Chartist ie. technical analyst (ATAA member and ex-national director)
- Provide support and tuition to traders and investors **Brainy's Share Market Toolbox**
- Member Mensa (former)
- Engineering Degree (structured thinking with an eye for charts and diagrams)
- 30+ years – professional experience (IT and management)
- **No AFS license! (Can't give advice)**
- **BullCharts software (convenor Australian BullCharts User Group and authorised reseller with special pricing)**

Conflict of interest?

* - Not yet enough capital to live off the proceeds of trading (after trading as a hobby until a career change in 2008).
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In-depth look at candle patterns

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- (3) This presentation is pure education, only for your general awareness. 
- (4) There are no recommendations to take any action, or to invest any money in any way.
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 **TA "Fundamentals"**

Technical Analysis "fundamentals" recap

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In-depth look at candle patterns

TA "Fundamentals"

TA principles

1. "Price charts summarise the underlying opinions and emotions of the real market participants. Every chart tells a story."
2. Share price trends are important:
 - Share price: up, down, or nowhere?
 - Higher peaks, higher troughs, versus lower peaks /troughs
 - Use Moving Average to assist?
3. Support and Resistance levels
4. Volume is very important!

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TA "Fundamentals"

Support and Resistance

Why can we identify support and resistance levels on a price chart like this weekly chart?



(see larger version next slide)

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TA "Fundamentals"



\$80 - Nov 2013 - Opinion:
CBA not worth more than this resistance level on the chart

\$78 - Opinion:
CBA now not worth more than this resistance level on the chart

\$73 - Opinion:
CBA worth more than this.

April 2014 Opinion:
CBA is now worth more than \$80.

Uptrend line

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In-depth look at candle patterns

 TA "Fundamentals"

Opinions of participants

Price charts summarise the underlying opinions and emotions of the real market participants.

And the candlesticks can clearly show this!

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Candlestick Charts **Candlestick Basics**

Candlestick Basics

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Candlestick Charts **Candlestick Basics**

Candlestick origins

- Are said to have been developed in the 18th century by legendary Japanese rice trader Munehisa Honma from the town of Sakata (in the late 1700s – a long time ago);
- He is reputed to have used **candlestick charts** to record **rice trades** within specific time periods, and then to predict **future rice prices** in the developing **rice futures exchange**, including the Dojima Rice Exchange in Osaka (reputed to be one of the world's first futures exchanges).

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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Candlestick origins

- Are said to have been developed in the 18th century by legendary Japanese rice trader Munehisa Homma from the town of Sakata.
- He is reputed to have used candlestick charts to record rice trades within specific time periods, and then to predict future rice prices in the developing rice futures exchange, including the Dojima Rice Exchange in Osaka (reputed to be one of the world's first futures exchanges).
- The Japanese feudal war-time origins of candlesticks helps to explain the Japanese names given to a number of candle patterns. For example:
 - **doji**,
 - **marabozu** (meaning close cropped or close-cut – a candle with no shadows),
 - **hirami** (meaning pregnant woman),
 - “advancing soldiers”, etc.

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Candlestick Charts **Candlestick Basics**

Candlestick origins

- Are said to have been developed in the 18th century by legendary Japanese rice trader Munehisa Homma from the town of Sakata. He is reputed to have used candlestick charts to record rice trades within specific time periods, and then to predict future rice prices in the developing rice futures exchange, including the Dojima Rice Exchange in Osaka (reputed to be one of the world's first futures exchanges).
- The Japanese feudal war-time origins of candlesticks helps to explain the Japanese names given to a number of candle patterns – eg. doji, marabozu (meaning close cropped or close-cut – a candle with no shadows), hirami (meaning pregnant woman), “advancing soldiers”, etc.
- The history of candlesticks has references to war-like situations. Some people use green and red coloured candles instead of white and black respectively – reputedly the red is drawn from the red of blood in battle (as in the battles of the bulls and bears when related to real life battles).

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Candlestick Charts **Candlestick Basics**

Caution: there are many “patterns”

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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Caution: there are many "patterns"

Which ones to look at?
How to learn all these?

How to USE them?
How to master candles
and all these patterns?

patterns Downtrere patterns

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Candlestick Charts **Candlestick Basics**

Firstly...

Let's look at some ***candle basics***
before
we look at ***candle patterns***

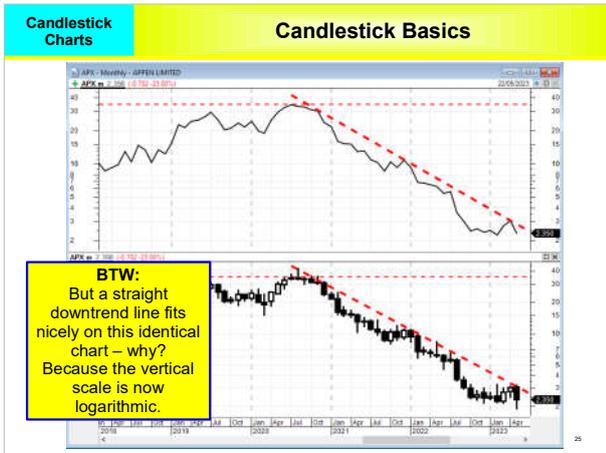
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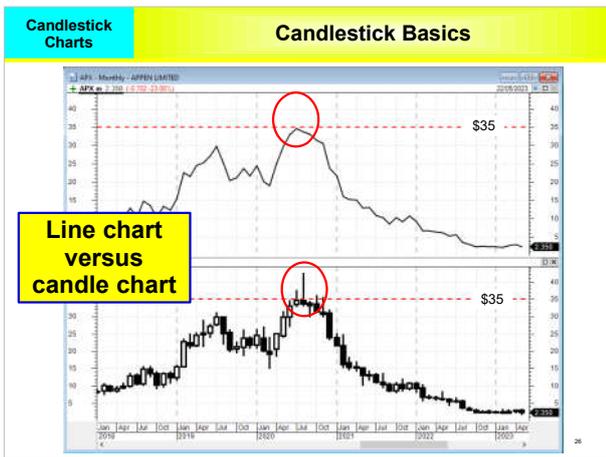
Candlestick Charts **Candlestick Basics**

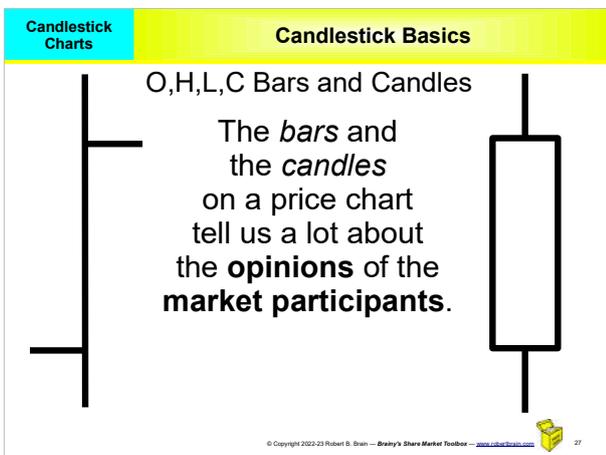
Line chart
versus
candle chart

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In-depth look at candle patterns







In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

OHLC Bar and Candle...

Each **bar** on a bar chart, and each **candle** on a candle chart

summarises the price action in any one period (a day, week, month, etc.)

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Candlestick Charts **Candlestick Basics**

OHLC Bar and Candle...

Each **bar** on a bar chart, and each **candle** on a candle chart

summarises the price action in any one period (a day, week, month, etc.)

Should I use bars or candles??

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Candlestick Charts **Candlestick Basics**

Candlestick basics

- A candle on a *candlestick chart* summarises the price action in one “period”.
- On a **Daily** chart – one candle summarises one **day's** price action to show:
 - Open,
 - Close,
 - High,
 - Low.
- On a **Weekly** chart – one candle summarises one **week's** price action.

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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Candlestick features — the White candle

"open" price for the period (bottom of candle body)

"close" price for the period (top of candle body)

A "period" is a day, week, month, etc.

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Candlestick Charts **Candlestick Basics**

Candlestick features — the White candle

"open" price for the period (bottom of candle body)

"close" price for the period (top of candle body)

"high" price for the period (top of candle tail)

"low" price for the period (bottom of candle tail)

A "period" is a day, week, month, etc.

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Candlestick Charts **Candlestick Basics**

Candlestick features — the Black candle

"open" price for the period (top of candle body)

"close" price for the period (bottom of candle body)

"high" price for the period (top of candle tail)

"low" price for the period (bottom of candle tail)

A "period" is a day, week, month, etc.

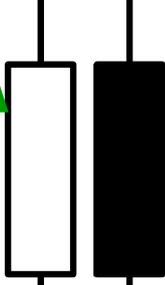
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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

White, Black — How to remember?

White candle opens low and price rises during the period, closing higher.



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Candlestick Charts **Candlestick Basics**

White, Black — How to remember?

White candle opens low and price rises during the period, closing higher.

Black candle opens high and price falls during the period, closing lower.

Black suggests doom and gloom.



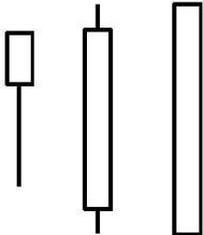
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Candlestick Charts **Candlestick Basics**

All shapes & sizes

Candle body and tail(s)

- Their presence or absence is important
- Their length (ie. their height) is important.



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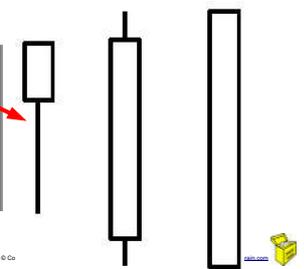
In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Candle *body* and *tails*

- Their presence or absence is important
- Their length (ie. their height) is important.

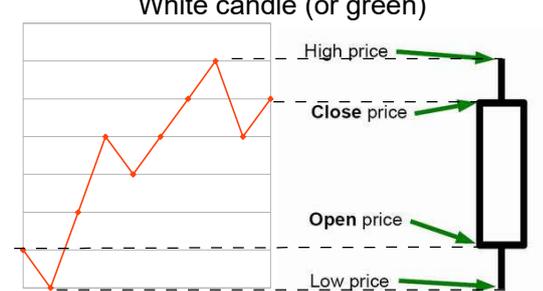
For example:
This long lower tail shows the presence of sellers in the "period", who were "defeated" by the buyers by the close of the period.



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Candlestick Charts **Candlestick Basics**

White candle (or green)



High price

Close price

Open price

Low price

White (hollow) candle
"up day"

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Candlestick Charts **Candlestick Basics**

Black candle (or red)



High price

Open price

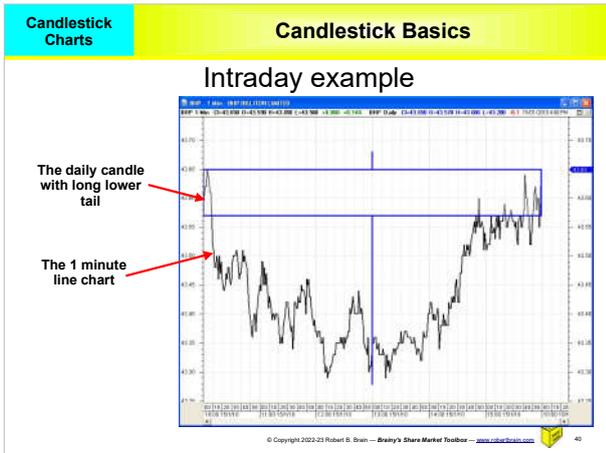
Close price

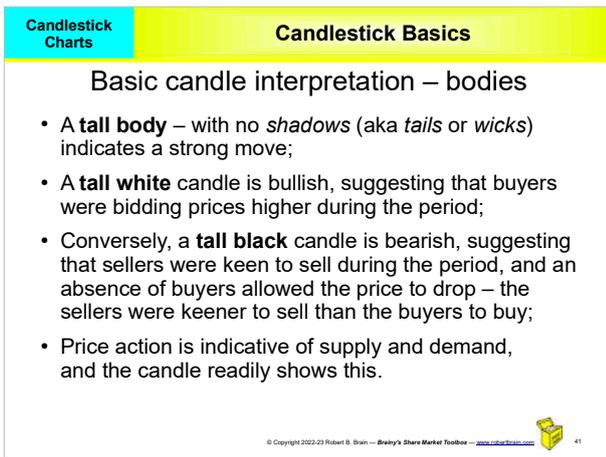
Low price

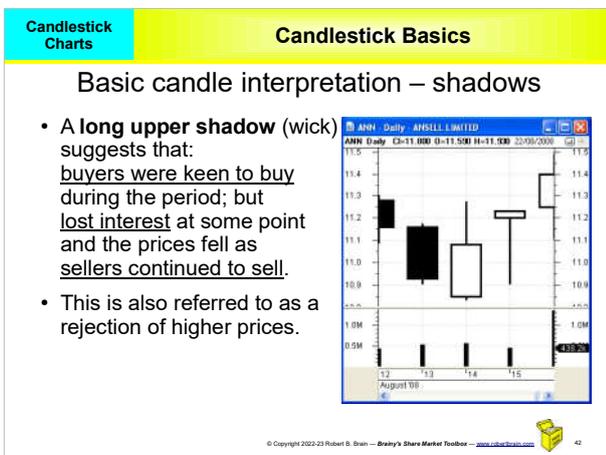
Black (filled) candle
"down day"

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In-depth look at candle patterns





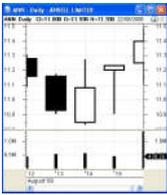


In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Basic candle interpretation – shadows

- Conversely, a **long lower tail** suggests that the sellers outnumbered the buyers early in the period; but extra buyers stepped in before the end of the session to close the session well above the session lows. This is also considered a rejection of lower prices because the buyers thought it was worth more and they were bidding the price higher.



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Candlestick Charts **Candlestick Basics**

Candle features summary

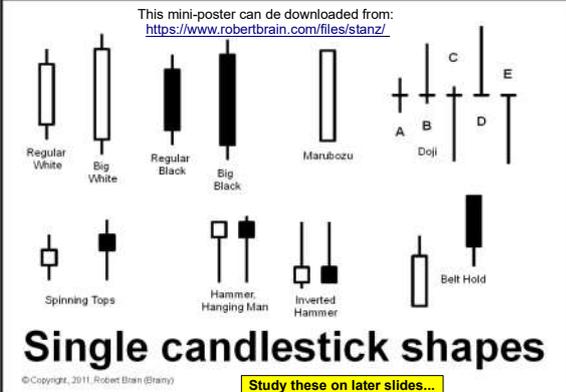
Individual candle features:

- Height of candle body – tall or short
- Candle colour – black or white (red or green)
- Presence (or absence) of shadows
- Length of shadows

Note these characteristics in the common examples on the next slide...

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This mini-poster can be downloaded from: <https://www.robertbrain.com/files/stanz/>



Single candlestick shapes

© Copyright, 2011, Robert Brain (Brainy) **Study these on later slides...**

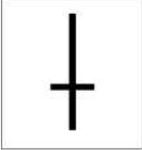
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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Basic candle interpretation – doji

- A very short body in the Doji candle indicates general agreement by the end of the session.
- If both tails are relatively short, it suggests basic agreement on price.
- If one or both tails are long, it suggests that there was potentially strong disagreement on price during the period, but by the end of the period there was agreement on price.

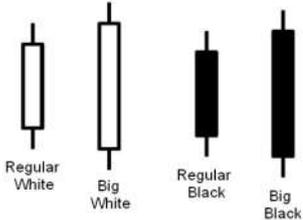


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Candlestick Charts **Candlestick Basics**

Big White, Big Black

- These are common;
- Short or no shadow is stronger.

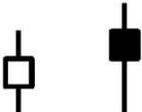


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Candlestick Charts **Candlestick Basics**

Spinning Top

- A definite body, and tails;
- Spinning Tops are quite common;
- Indicate indecision (lack of agreement);
- Can simply indicate a pause in a rally, or a potential trend change.



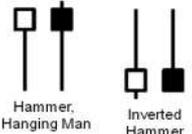
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In-depth look at candle patterns

Candlestick Charts **Candlestick Basics**

Hammer, Hanging Man

- Short body, one long tail, and tiny or no second tail;
- Hammer and Hanging Man are the same, but Hammers appear at market bottoms, and the Hanging Man at tops;
- Inverted Hammer – bullish reversal in downtrend.

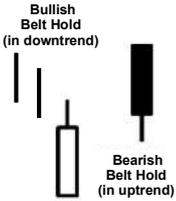


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Candlestick Charts **Candlestick Basics**

Belt Hold

- The Bullish Belt Hold opens lower in a downtrend;
- It indicates a likely trend reversal, especially if white candle with no lower shadow and a short upper one;
- Bearish Belt Hold is the converse (opens higher in an uptrend);
- Is reputed to be fairly reliable.



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Candlestick Charts **Candlestick Basics**

Candle features summary

Individual candle features:

- Height of candle body:
 - Tall or short?
- Candle colour – black or white (red or green)
- Presence (or absence) of tails:
 - One tail, or two?
- Length of tails:
 - Long or short?

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In-depth look at candle patterns

Candlestick Charts Candlestick Patterns

Candlestick Patterns

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Candlestick Charts Candlestick Patterns

Candle patterns

- **Single candles** can tell a “story”;
- **Multiple candles** together can form a specific *candle pattern* – which can tell more of a story, or yet a different story;
- The **price action prior** is important, whether *uptrend* or *downtrend*, or no trend;
- *“The trend is what sets up the psychology of traders for the candle pattern to develop”*
ack: Gregory L. Morris, “Candlepower: Advanced Candlestick Pattern Recognition and Filtering Techniques for Trading Stocks and Futures”, p213, Probus Publishing Company, 1992.

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Candlestick Charts Candlestick Patterns

Candle pattern “categories”

Reversal patterns:

- Hammer and Hanging Man
- Engulfing pattern
- Dark cloud cover
- Piercing pattern

Some examples shortly...



Hammer,
Hanging Man

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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Candle pattern "categories"

More reversal patterns:

- Harami and Harami Cross
- Tweezers Top and Bottom
- Belt Hold
- Three Black Crows
- Tower Top and Bottom
- Dumpling Top and Fry Pan Bottom

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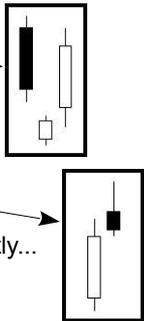
Candlestick Charts **Candlestick Patterns**

Candle pattern "categories"

Star patterns:

- Morning Star
- Evening Star
- Morning and Evening Doji Star
- Shooting Star and
- Inverted Hammer

Some examples shortly...



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Candlestick Charts **Candlestick Patterns**

Candle pattern "categories"

Continuation patterns:

- Rising (and Falling) Window
- Rising (and Falling) Three Methods
- Three White Soldiers

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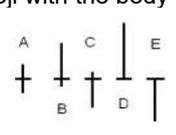
In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Candle pattern "categories"

Doji patterns:

- Long-legged Doji (B, C, D, E)
- Rickshaw Man (a long-legged doji with the body near the middle of the candle)
- Gravestone Doji (D)
- The Doji is a strong predictor of a trend reversal
- Look for confirmation in the following period.



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Candlestick Charts **Candlestick Patterns**

Candle patterns

Following are just a few of the recognised candle patterns ...

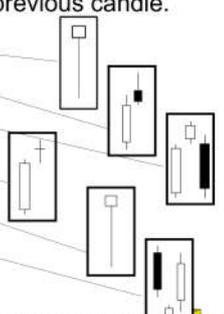
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Candlestick Charts **Candlestick Patterns**

Candle patterns – small bodies

- With or without a gap from previous candle.
- Hanging Man (at tops)
- Shooting Star (2-candle pattern)
- Evening Star (3-candle pattern)
- Doji Star (2-candle pattern)
- Hammer (at bottoms)
- Morning Star (3-candle pattern)

These candle patterns all tell a story. Can you read the story?



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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Patterns – engulfing and piercing

Reversal patterns in **UP Trends**:-

- Engulfing Bearish – “outside day” (2-candle pattern, very bearish)
- Dark Cloud (2-candle piercing pattern in uptrend)
- Harami Bearish (2-candle pattern)
- Doji Star

These candle patterns all tell a story. Can you read the story?

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Candlestick Charts **Candlestick Patterns**

Patterns – engulfing and piercing

Reversal patterns in **DOWN Trends**:-

- Piercing Line (2-candle bullish pattern)
- Engulfing Bullish (2-candle pattern)
- Harami Bullish – “inside day” (2-candle pattern)
- Harami Cross (2-candle pattern)

These candle patterns all tell a story. Can you read the story?

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Candlestick Charts **Candlestick Patterns**

Candle patterns – too many?

- There are many, many documented candle patterns;
- And several heavy text books;
- Also good websites like: www.thepatternsite.com ;
- This can make it difficult to learn all the patterns;
- BUT you don't need to learn them all!

Steve Nison's book has many great candle examples

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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

So, how to go forward?

On the price chart, observe:-

- 1) Individual candle *features*;
- 2) The price *trend*;
- 3) Identify a *candle pattern*.

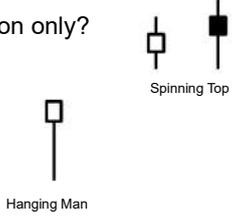
It is useful to have some awareness of the variety of *candle patterns*.

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Candlestick Charts **Candlestick Patterns**

Step 1. Study individual candle features

- Body size – short, normal, long?
- Shadows – short, long or none?
- Shadows – in one direction only?



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Candlestick Charts **Candlestick Patterns**

Step 2. The trend in the lead up

Observe the trend in the few prior periods:

- Is the trend up or down?
- Look for Dow Theory peaks and troughs, or
- Use a Moving Average – rising or falling?
(eg. 10 period EMA, Gregory L. Morris, *CandlePower*, p215)

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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Step 3. Identify a *candle pattern*

Look for a candle pattern, but note:

- The interpretation of candle patterns can be somewhat subjective;
- Various tests of the reliability of a candle pattern have suggested they might not be a reliable predictor of future price action;
- Some people can spot the patterns more readily than other people can, so don't feel bad if you can't spot them.

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Candlestick Charts **Candlestick Patterns**

Candle-spotting tips

- The extreme level of a candle shadow can become a *support* or *resistance* level;
- Look for **Big White** candle with higher volume on a price **breakout**;
- Utilise candle pattern observation with other technical analysis methods: MA signals, with Oscillators (eg. RSI, Stochastic, Momentum, etc.) (refer: Nison).

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Candlestick Charts **Candlestick Patterns**

Candle patterns in uptrends

The more common patterns are shown on the next few slides...

My Approach:
First look for the *trend*,
then look for the *pattern*.

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In-depth look at candle patterns

Uptrend candle patterns

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Study these on next slides...

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Uptrend candle patterns

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Study these on next slides...

Candlestick Charts **Candlestick Patterns**

Study these few...

...noting the Open and Close of the black candle, compared to the previous (white) candle.

Very bearish Not so bearish Less bearish Less bearish again

Bearish Engulfing **Dark Cloud Cover** **Bearish Counter attack** **Bearish Harami**

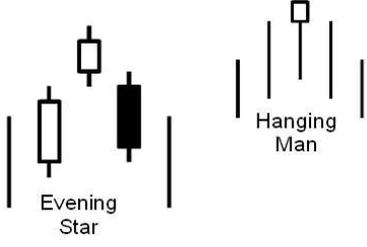
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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Likely trend reversal – bearish

In uptrend...



Evening Star

Hanging Man

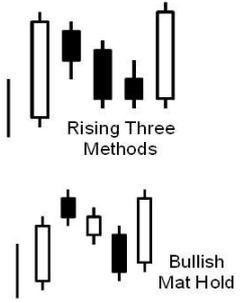
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This slide illustrates two bearish candlestick patterns. The 'Evening Star' pattern consists of three candles: a white candle, a black candle, and a white candle. The 'Hanging Man' pattern consists of a white candle with a long upper shadow and a short lower shadow.

Candlestick Charts **Candlestick Patterns**

Likely trend continuation – bullish

In uptrend...
price has marched
too far ahead.



Rising Three Methods

Bullish Mat Hold

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This slide illustrates two bullish candlestick patterns. The 'Rising Three Methods' pattern consists of a long white candle followed by three smaller black candles, each with a long upper shadow. The 'Bullish Mat Hold' pattern consists of a white candle, a black candle, a white candle, and a black candle.

Candlestick Charts **Candlestick Patterns**

Candle patterns in downtrends

The more common ones are
shown on the next few slides...

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This slide is a text-based introduction to candle patterns in downtrends, indicating that more common patterns will be shown in subsequent slides.

In-depth look at candle patterns

Downtrend candle patterns

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Downtrend candle patterns

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Candlestick Charts **Candlestick Patterns**

Study these few...

...noting the Open and Close of the white candle, compared to the previous (black) candle.

Very bullish Still bullish Bullish Still somewhat bullish

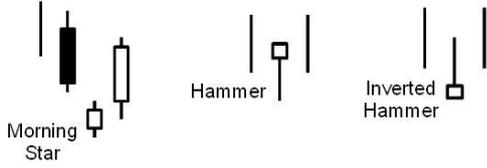
Bullish Kicker Bullish Engulfing Piercing Line Bullish Counter attack Bullish Harami

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In-depth look at candle patterns

Candlestick Charts **Candlestick Patterns**

Likely trend reversal – bullish



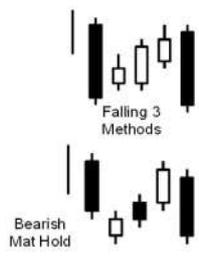
Morning Star Hammer Inverted Hammer

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Candlestick Charts **Candlestick Patterns**

Likely trend continuation – bearish

In downtrend...
Price has marched too far ahead.



Falling 3 Methods Bearish Mat Hold

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Candlestick Charts **Candlestick Patterns**

Candle Pattern Spotting – Tips

- Study a few popular/common patterns so you know what to look for;
- Study the O, H, L, C of one candle compared to the adjacent candle(s);
- Study body size and shadow size of adjacent candle(s);

Remember that one candle, and multiple candles, can show us the underlying opinions of the market participants.

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In-depth look at candle patterns

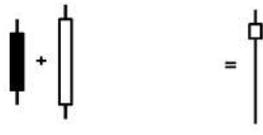
Candlestick Charts **Candlestick Addition**

Candlestick Addition

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Candlestick Charts **Candlestick Addition**

“Summarise” several candles?
How would it be if we could summarise multiple candles into just one candle, to make the analysis easier?

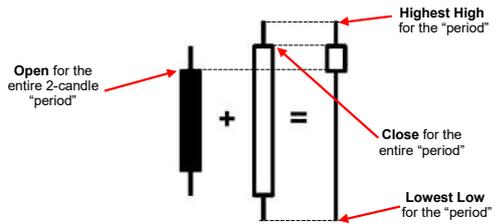


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Candlestick Charts **Candlestick Addition**

Candle addition

Candle addition results in a compound or composite candle.



Open for the entire 2-candle "period"

Highest High for the "period"

Close for the entire "period"

Lowest Low for the "period"

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In-depth look at candle patterns

Candlestick Charts **Candlestick Addition**

Candle addition

Candle addition results in a compound or composite candle.

Open for the entire "period"

Highest High for the "period"

Close for the entire "period"

Lowest Low for the "period"

Bullish Engulfing pattern

Hammer pattern (in downtrend) or Hanging Man (in uptrend)

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Candlestick Charts **Candlestick Addition**

Bullish Kicker pattern example

- The first candle is black.
- The second candle is a white that opens at the same level as the open of the black.
- The resulting compound candle has a reasonably sized body and a longish lower tail. This suggests a rejection of lower prices, and that buyers have overcome the sellers in the period.

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Candlestick Charts **Candlestick Addition**

Morning Star 3-candle example

- The first candle is black.
- Then a gap down to a white candle.
- The third candle covers the gap and pierces most of the way up the first candle.
- The resulting compound candle is a Hammer pattern (if in a downtrend).

In downtrend, likely trend reversal

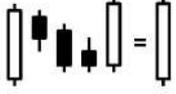
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In-depth look at candle patterns

Candlestick Charts **Candlestick Addition**

Rising Three Methods example

- The first candle is a Big White which pushes too high too soon.
- The intermediate candles a bidding time, within the range of the first.
- The fifth candle continues the rising trend.
- The resulting candle after adding these 5 candles together is a Big White. Over the 5 periods covered by the 5 individual candles, such a big leap in price is more reasonable.



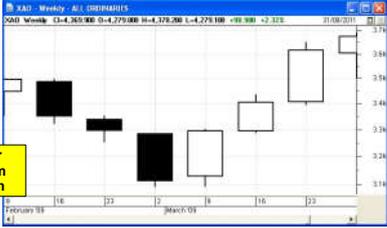
In uptrend, likely trend continuation

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Candlestick Charts **Candlestick Addition**

XAO index (March 2009)

Exactly what happened day-to-day in the two weeks in the middle of this weekly chart?



Tower Bottom pattern

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Candlestick Charts

Daily chart Rounding Bottom



Daily chart with two compound candles added



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In-depth look at candle patterns

Candlestick Charts **Candlestick Addition**

Candle Addition Summary

- It is possible to “add” two or more candles together to produce just one candle – a *compound* or *composite* candle;
- This can be useful to assist with the analysis of the price chart;
- It can help to understand the underlying opinions of the real market participants.

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 **Summary & Wrap up**

Candlestick summary – About

- Remember technical analysis principles
- Individual candlesticks:
 - Long or short bodies and body colour
 - Absence or presence and length of tails
 - Price trend
- Multiple-candle patterns:
 - bullish / bearish
 - possible reversal
 - presence or absence of buyers/sellers

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 **Summary & Wrap up**

Candlestick summary – To observe

Observe:

- Individual candle features;
- The price trend;
- Identify a candle pattern; and
- Make sure to look at volume also because the volume is important.

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In-depth look at candle patterns

Summary & Wrap up

THE END — Thank you

CREDITS

These slides prepared by: Robert Brain
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All of Robert's charts prepared with:
BullCharts software www.bullcharts.com.au



Summary & Wrap up

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