

Candlestick Analysis

Designed, authored and published by



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FREE STOCK MARKET EDUCATION

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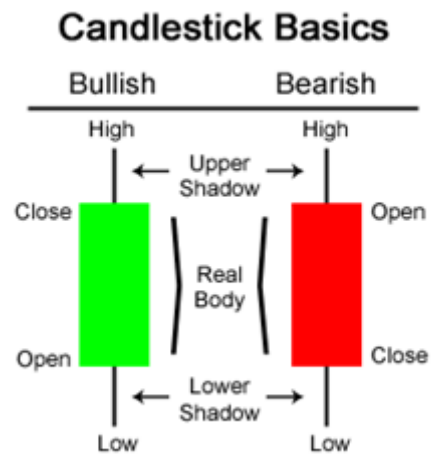
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WHAT ARE CANDLESTICKS?

Put simply, candlesticks are a way of communicating information about how price is moving.

Bullish Candle: When the close is higher than the open (usually green or white)

Bearish Candle: When the close is lower than the open (usually red or black)



There are three main parts to a candlestick:

Upper Shadow: The vertical line between the high of the day and the close (bullish candle) or open (bearish candle)

Real Body: The difference between the open and close; colored portion of the candlestick

Lower Shadow: The vertical line between the low of the day and the open (bullish candle) or close (bearish candle)

WHY DO CANDLESTICKS WORK?

Price action traders rely on candlesticks because they convey a great deal of information about each trading period in a visual format that is easy to interpret, allowing traders to compare the behavior of price in different time periods with a quick glance at a price action chart. Each candlestick can be “read” as a meaningful part of the developing narrative of price. They communicate the “market sentiment”: whether (and to what extent) bears or bulls were in control, and how far traders managed to push price in both directions. For example, a long candle’s body with no wicks indicates a

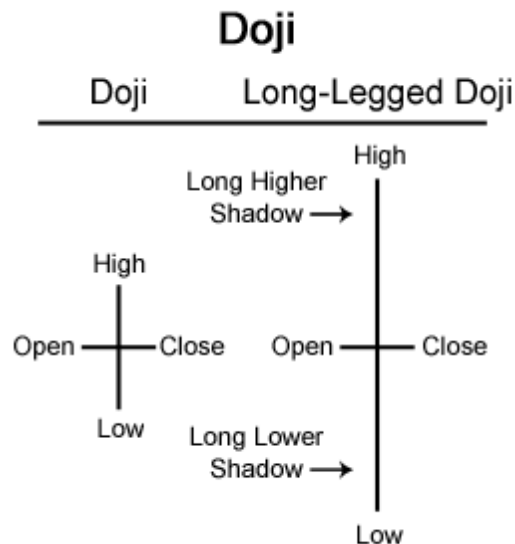
definitive shift in this struggle for power, whereas a candle with a long upper wick beyond its body indicates a more contentious period with an effort by bulls to push price higher that was pushed back by pressure from bears before the close of the candle. Certain re-occurring candlestick patterns have become popular among traders as reliable signals of future market behavior. This guide is intended as an introduction to some of these patterns, which help traders make sense of market conditions and recognize advantageous times to enter trades.

The ability to read candlesticks allows the price action trader to become a meta-strategist, taking into account the behaviors of other traders and large-scale market-movers. In other words, candlestick patterns help traders.

Candlestick Patterns Candlestick patterns can be made up of one candle or multiple candlesticks, and can form reversal or continuation patterns.

Detailed explanations of these candlestick patterns; the links are given below:

DOJI



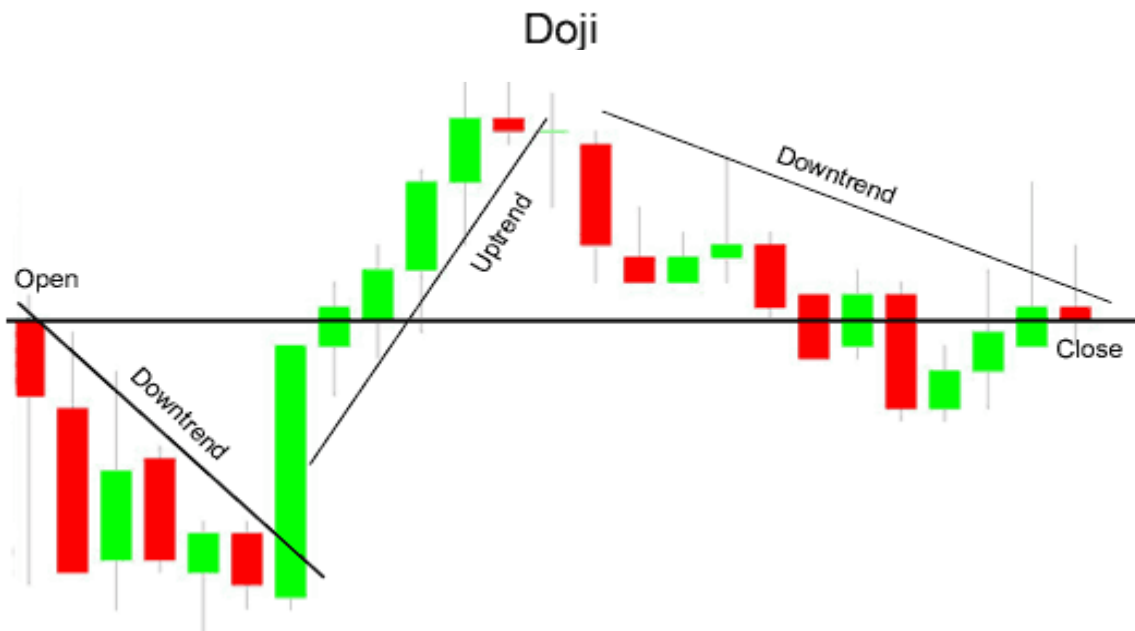
This candle has zero or almost **zero range between its open and close**. Rather than implying potential reversal or the clear dominance of either bears or bulls, these candles suggest balance between the two forces. Neither buyers nor sellers are fully in control. A Doji that occurs in the context of a strong trend implies the weakening of the dominant force that resulted in that trend.

A “long-legged Doji” has long wicks in both directions, implying strong, balanced pressure from both buyers and sellers.

The “dragonfly” and “gravestone” Doji imply, respectively, that sellers and buyers controlled the market for most of the trading period, but then the opposite group managed to push price back to the open before the close. While tradition and long-

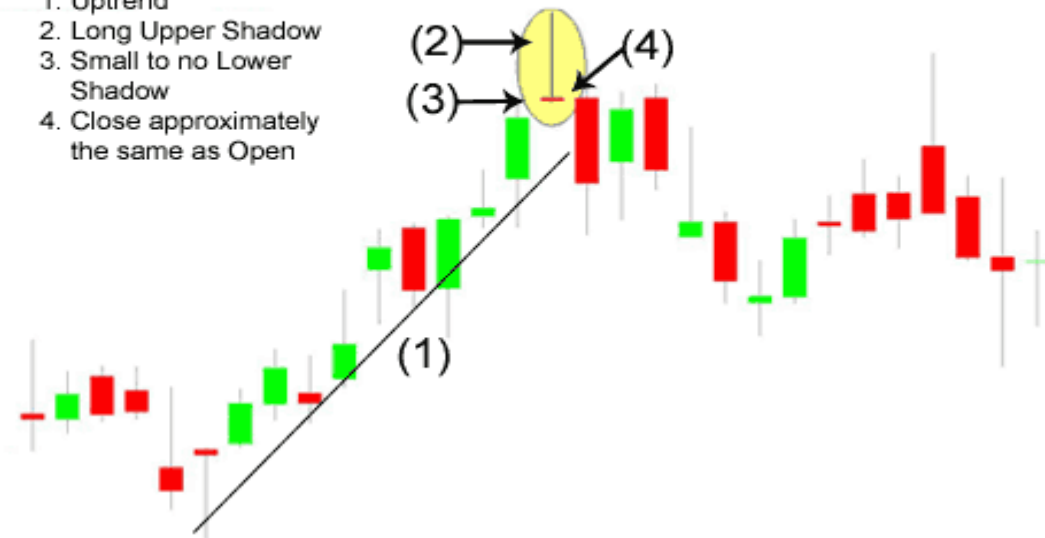
legged Dojis are reflective of indecision and stalling, gravestone and dragonfly are generally clearer, stronger indicators that a force is stepping in to push the market in the direction of the wick and away from the body.

TYPES OF DOJI



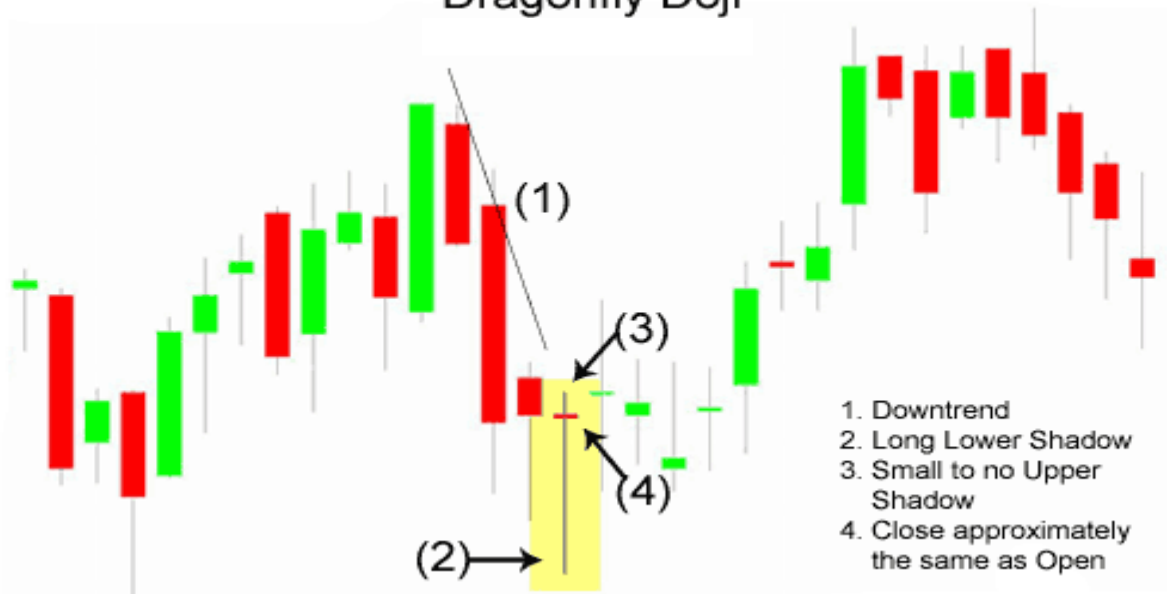
Gravestone Doji

1. Uptrend
2. Long Upper Shadow
3. Small to no Lower Shadow
4. Close approximately the same as Open



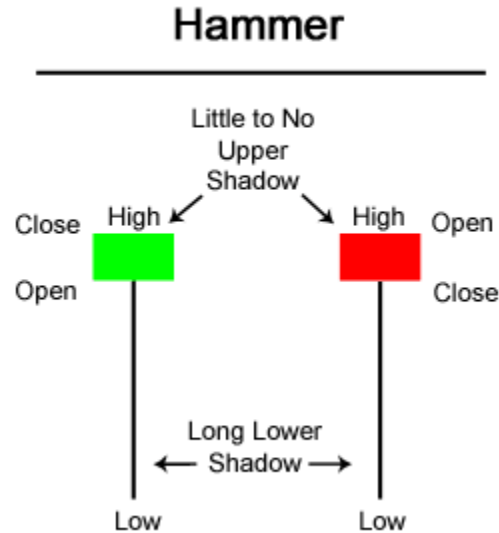
Dragonfly Doji

1. Downtrend
2. Long Lower Shadow
3. Small to no Upper Shadow
4. Close approximately the same as Open

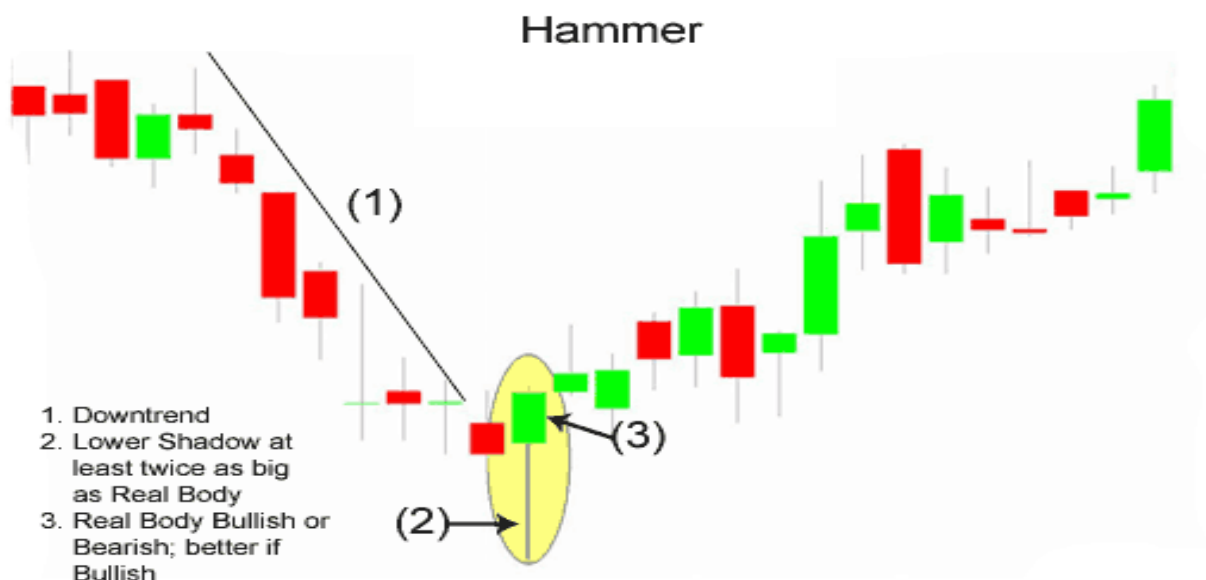


HAMMER

The Hammer candlestick formation is viewed as a **bullish reversal candlestick pattern** that mainly occurs at the bottom of downtrends.

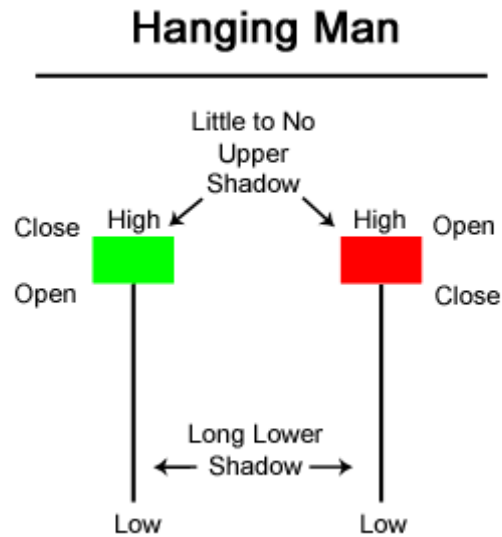


The Hammer formation is created when the open, high, and close are roughly the same price. Also, there is a long lower shadow, twice the length as the real body. When the high and the close are the same, a bullish Hammer candlestick is formed and it is considered a stronger formation because the bulls were able to reject the bears completely plus the bulls were able to push price even more past the opening price. The long lower shadow of the Hammer implies that the market tested to find where support and demand was located. When the market found the area of support, the lows of the day, bulls began to push prices higher, near the opening price. Thus, the bearish advance downward was rejected by the bulls.

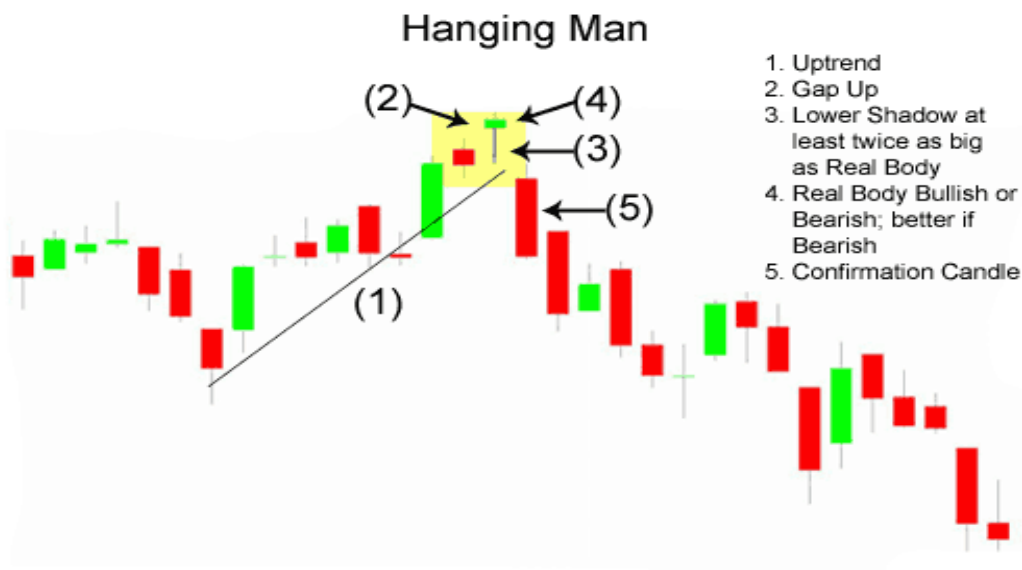


HANGING MAN

The Hanging Man candlestick formation, as one could predict from the name, is **viewed as a bearish sign**. This pattern occurs mainly at the top of uptrends and can act as a warning of a potential reversal downward.

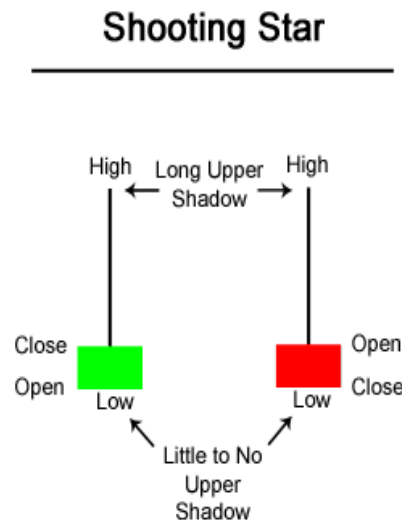


The Hanging Man formation, just like the Hammer, is created when the open, high, and close are roughly the same price. Also, there is a long lower shadow, which should be at least twice the length of the real body. When the high and the open are the same, a bearish Hanging Man candlestick is formed and it is considered a stronger bearish sign than when the high and close are the same, forming a bullish Hanging Man (the bullish Hanging Man is still bearish, just less so because the day closed with gains). After a long uptrend, the formation of a Hanging Man is bearish because prices hesitated by dropping significantly during the day. Granted, buyers came back into the stock, future, or currency and pushed price back near the open, but the fact that prices were able to fall significantly shows that bears are testing the resolve of the bulls. What happens on the next day after the Hanging Man pattern is what gives traders an idea as to whether or not prices will go higher or lower.



SHOOTING STAR

The Shooting Star candlestick formation is viewed as a bearish reversal candlestick pattern that typically occurs at the top of uptrend.



The Shooting formation is created when the open, low, and close are roughly the same price. Also, there is a long upper shadow, generally defined as at least twice the length of the real body. When the low and the close are the same, a bearish Shooting Star candlestick is formed and it is considered a stronger formation because the bears were able to reject the bulls completely plus the bears were able to push prices even more by closing below the opening price.

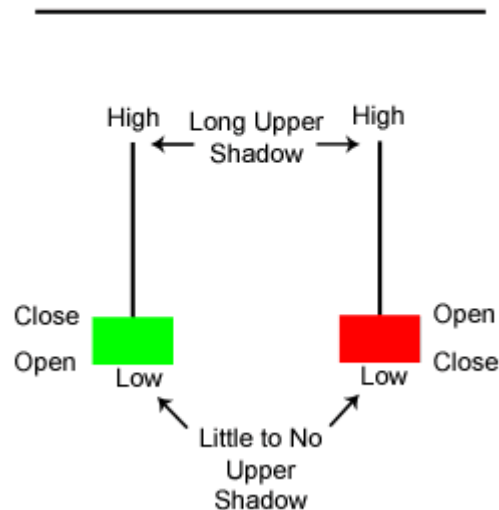
The Shooting Star formation is considered less bearish, but nevertheless bearish when the open and low are roughly the same. The bears were able to counteract the bulls, but were not able to bring the price back to the price at the open. The long upper shadow of the Shooting Star implies that the market tested to find where resistance and supply was located. When the market found the area of resistance, the highs of the day, bears began to push prices lower, ending the day near the opening price. Thus, the bullish advance upward was rejected by the bears.



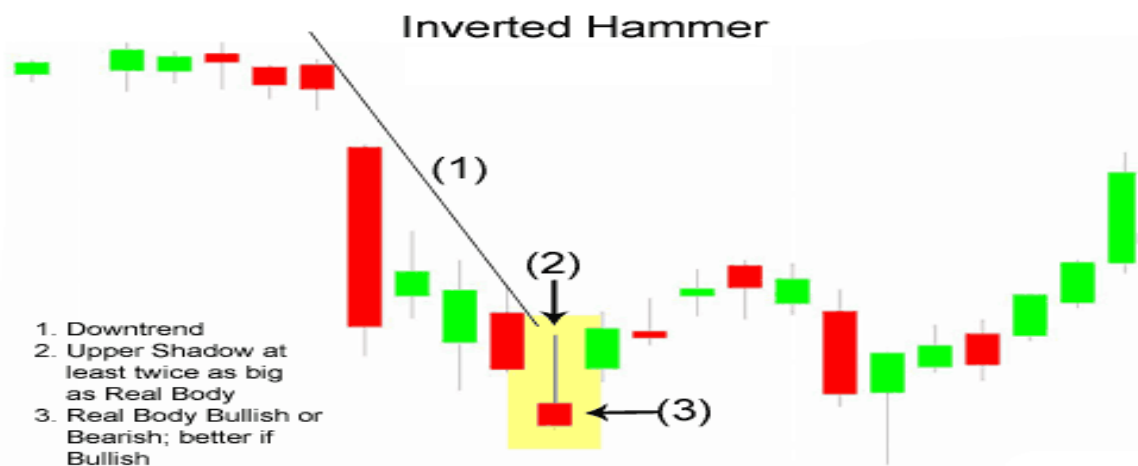
INVERTED HAMMER

The Inverted Hammer candlestick formation occurs mainly at the bottom of downtrends and can **act as a warning of a potential reversal upward**. It is important to note that the Inverted pattern is a warning of potential price change, not a signal, in and of itself, to buy.

Inverted Hammer

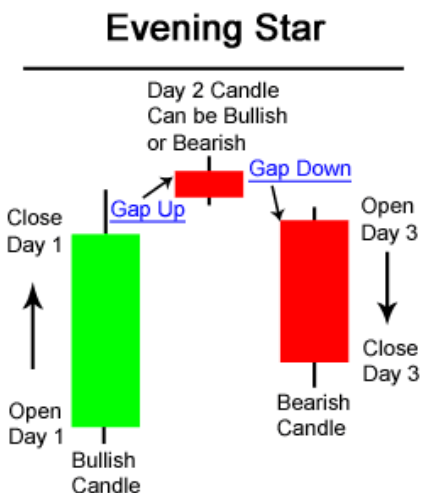


The Inverted Hammer formation, just like the Shooting Star formation, is created when the open, low, and close are roughly the same price. Also, there is a long upper shadow, which should be at least twice the length of the real body. When the low and the open are the same, a bullish Inverted Hammer candlestick is formed and it is considered a stronger bullish sign than when the low and close are the same, forming a bearish Hanging Man (the bearish Hanging Man is still considered bullish, just not as much because the day ended by closing with losses). After a long downtrend, the formation of an Inverted Hammer is bullish because prices hesitated their move downward by increasing significantly during the day. Nevertheless, sellers came back into the stock, future, or currency and pushed prices back near the open, but the fact that prices were able to increase significantly shows that bulls are testing the power of the bears. What happens on the next day after the Inverted Hammer pattern is what gives traders an idea as to whether or not prices will go higher or lower.

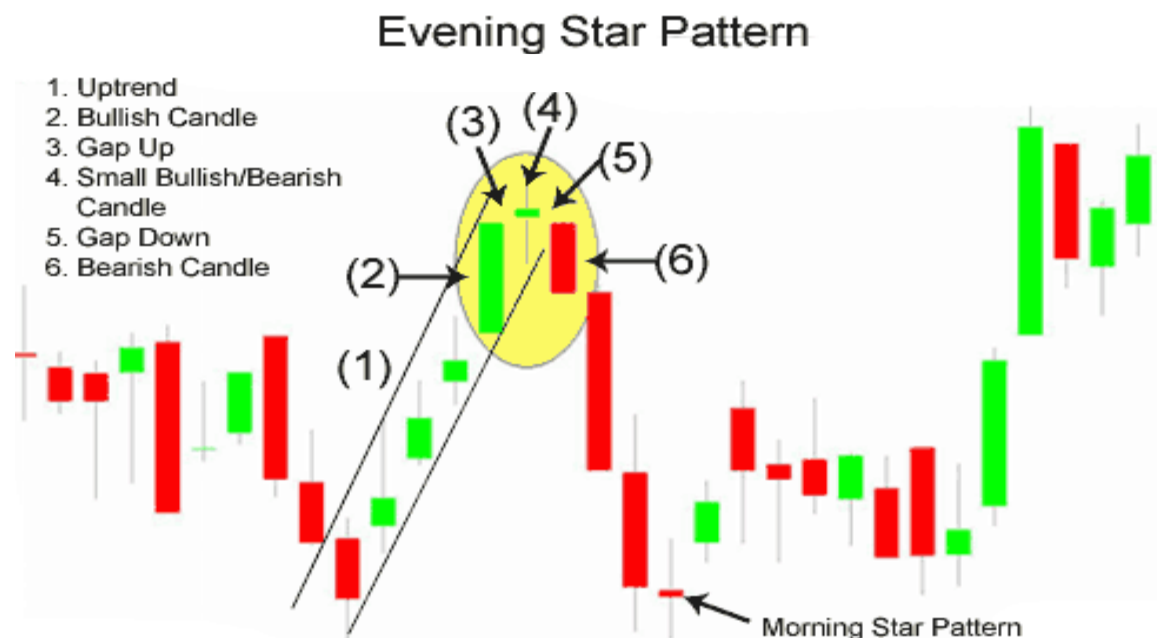


EVENING STAR

The Evening Star Pattern is **viewed as a bearish reversal pattern** that usually occurs at the top of an uptrend. The pattern consists of three candlesticks:

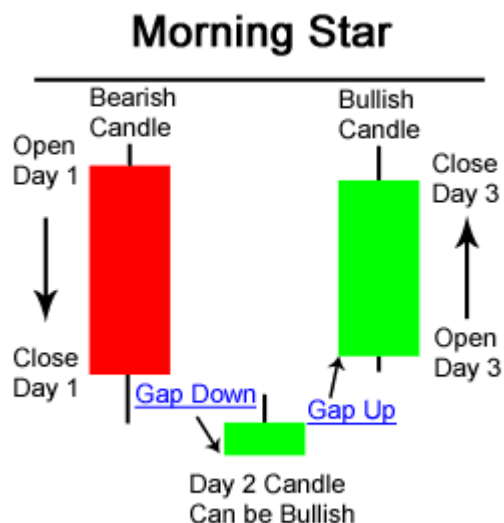


Bullish Candle (Day 1) Small Bullish or Bearish Candle (Day 2) Large Bearish Candle (Day 3) the first part of an Evening Star reversal pattern is a large bullish green candle. On the first day, bulls are definitely in charge, usually new highs were made. The second day begins with a bullish gap up. It is clear from the opening of Day 2 that bulls are in control. However, bulls do not push prices much higher. The candlestick on Day 2 is quite small and can be bullish, bearish, or neutral (i.e. Doji). Generally speaking, a bearish candle on Day 2 is a stronger sign of an impending reversal. But it is Day 3 that is the most significant candlestick. Day 3 begins with a gap down, (a bearish signal) and bears are able to press prices even further downward, often eliminating the gains seen on Day 1.

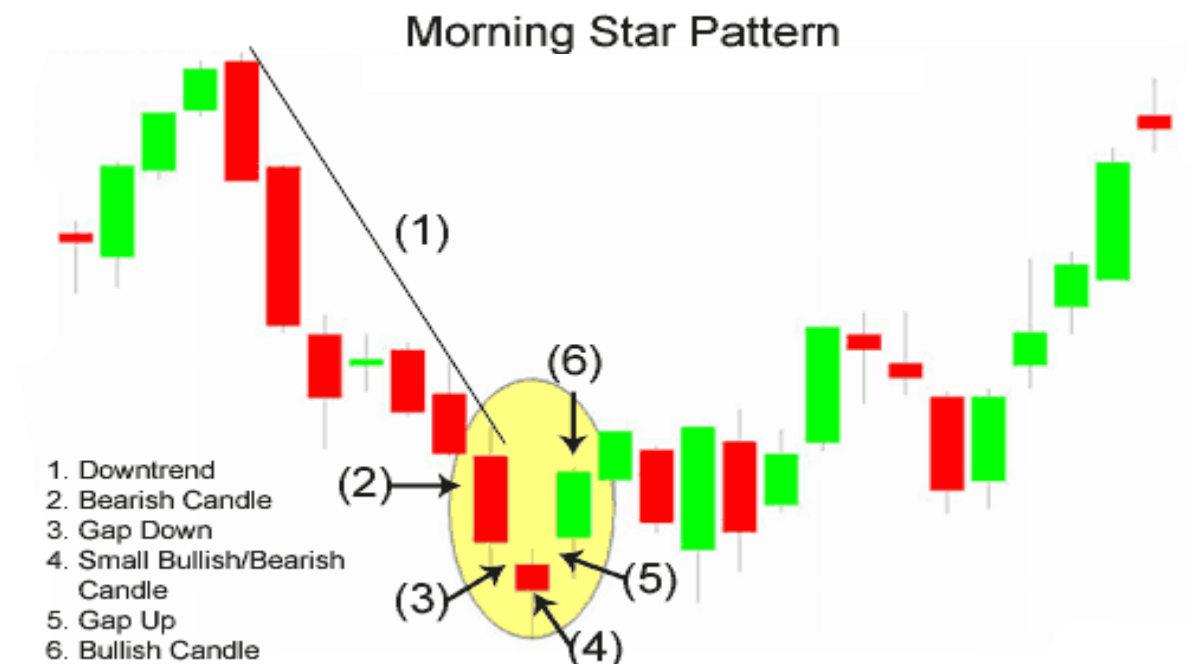


MORNING STAR

The Morning Star Pattern is **viewed as a bullish reversal pattern**, usually occurring at the bottom of a downtrend. The pattern consists of three candlesticks:



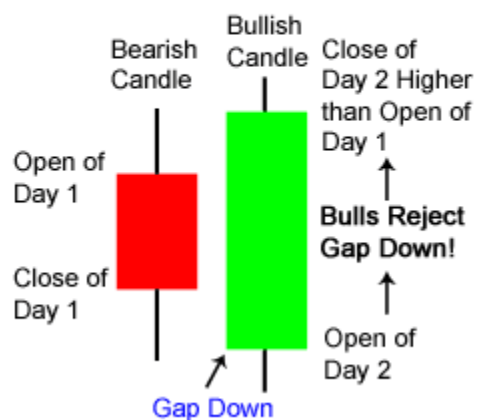
Large Bearish Candle (Day 1) Small Bullish or Bearish Candle (Day 2) Large Bullish Candle (Day 3) The first part of a Morning Star reversal pattern is a large bearish red candle. On the first day, bears are definitely in charge, usually making new lows. The second day begins with a bearish gap down. It is clear from the opening of Day 2 that bears are in control. However, bears do not push prices much lower. The candlestick on Day 2 is quite small and can be bullish, bearish, or neutral (i.e. Doji). Generally speaking, a bullish candle on Day 2 is viewed as a stronger sign of an impending reversal. But it is Day 3 that holds the most significance. Day 3 begins with a bullish gap up, and bulls are able to press prices even further upward, often eliminating the losses seen on Day 1.



BULLISH ENGULFING

The Bullish Engulfing Candlestick Pattern is a **bullish reversal pattern**, usually occurring at the bottom of a downtrend. The pattern consists of two Candlesticks:

Bullish Engulfing Pattern



Smaller Bearish Candle (Day 1)

Larger Bullish Candle (Day 2)

The bearish candle real body of Day 1 is usually contained within the real body of the bullish candle of Day 2.

On Day 2, the market gaps down; however, the bears do not get very far before bulls take over and push prices higher, filling in the gap down from the morning's open and pushing prices past the previous day's open. The interpretive power of the Bullish Engulfing Pattern comes from the incredible change of sentiment from a bearish gap down in the morning, to a large bullish real body candle that closes at the highs of the day. Bears have overstayed their welcome and bulls have taken control of the market.

Bullish Engulfing Pattern

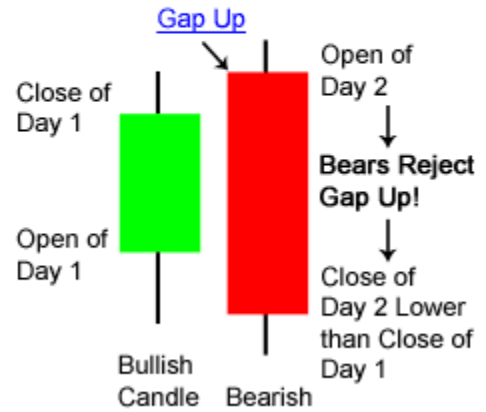


BEARISH ENGULFING

The Bearish Engulfing Candlestick Pattern is considered to be a **bearish reversal pattern**, usually occurring at the top of an uptrend. The pattern consists of two Candlesticks:

- Smaller Bullish Candle (Day 1)
- Larger Bearish Candle (Day 2)

Bearish Engulfing Pattern



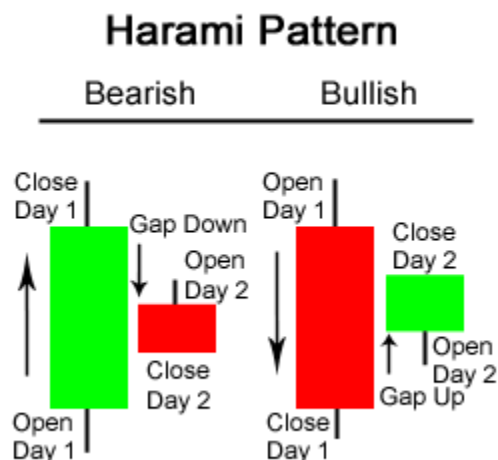
Generally, the bullish candle real body of Day 1 is contained within the real body of the bearish candle of Day 2. The market gaps up (typically interpreted as a bullish sign) on Day 2; however, the bulls do not push very far higher before bears take over and push prices further down, not only filling in the gap down from the morning's open but also pushing prices below the previous day's open (viewed as a bearish sign). With the Bullish Engulfing Pattern, there is an incredible change of sentiment from the bullish gap up at the open, to the large bearish real body candle that closed at the lows of the day. Bears have successfully overtaken bulls for the day and possibly for the next few periods.

Bearish Engulfing Pattern



HARAMI/ INSIDE BAR

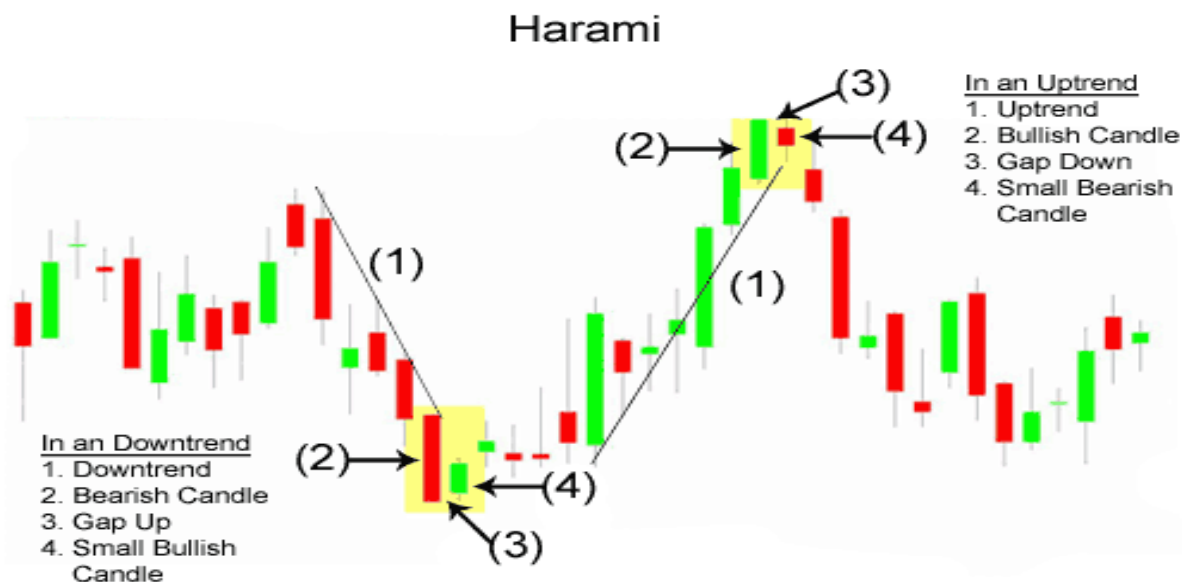
The Harami (meaning "pregnant" in Japanese) Candlestick Pattern is considered a reversal pattern. The pattern consists of two Candlesticks:



Larger Bullish or Bearish Candle (Day 1) Smaller Bullish or Bearish Candle (Day 2) The Harami Pattern is considered either bullish or bearish based on the criteria below:

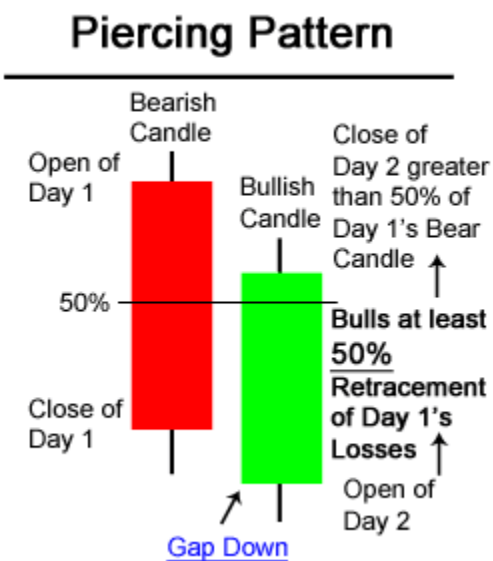
Bearish Harami: A bearish Harami occurs when there is a large bullish green candle on Day 1 followed by a smaller bearish or bullish candle on Day 2. The most important aspect of the bearish Harami is that prices gapped down on Day 2 and were unable to move higher back to the close of Day 1. This is a sign that uncertainty could be entering the market.

Bullish Harami: A bullish Harami occurs when there is a large bearish red candle on Day 1 followed by a smaller bearish or bullish candle on Day 2. Again, the most important aspect of the bullish Harami is that prices gapped up on Day 2 and price was held up and unable to move lower back to the bearish close of Day 1.



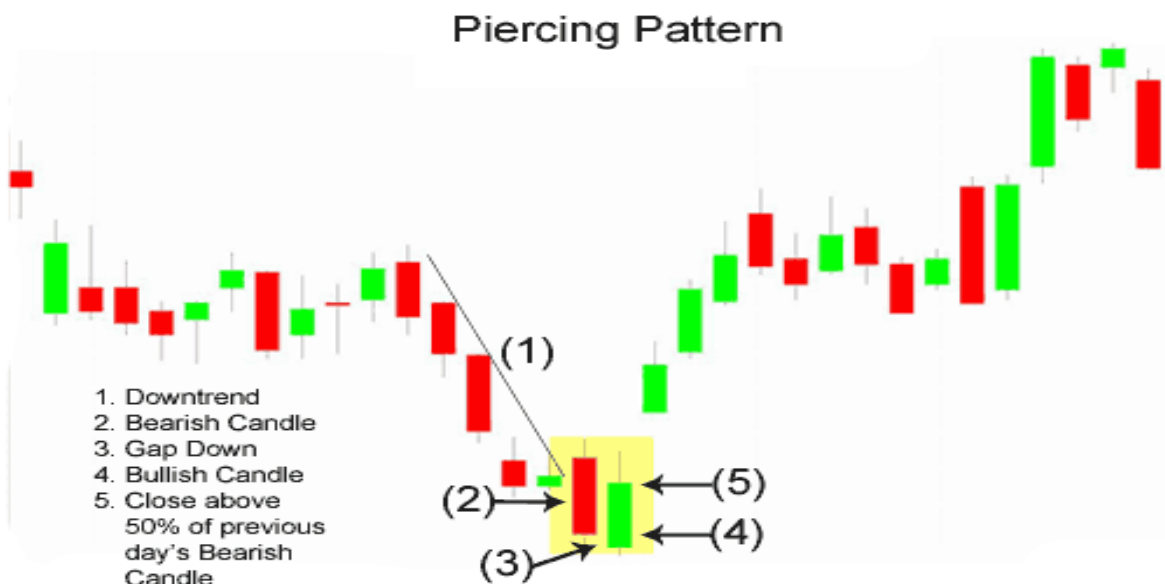
PIERCING LINE

The Piercing Pattern is **viewed as a bullish candlestick reversal pattern**, similar to the Bullish Engulfing Pattern (see: Bullish Engulfing Pattern Page No.13) There are two components of a Piercing Pattern formation:



Bearish Candle (Day 1) & Bullish Candle (Day 2)

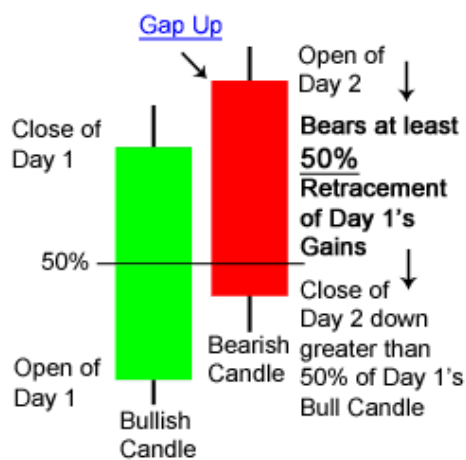
A Piercing Pattern occurs when a bullish candle on Day 2 closes above the middle of Day 1's bearish candle. Moreover, price gaps down on Day 2 only for the gap to be filled (see: Gaps) and closes significantly into the losses made previously in Day 1's bearish candlestick. The rejection of the gap down by the bulls typically can be viewed as a bullish sign, and the fact that bulls were able to press further up into the losses of the previous day adds even more bullish sentiment. Bulls were successful in holding prices higher, absorbing excess supply and increasing the level of demand.



DARK CLOUD COVER

Dark Cloud Cover is a **bearish candlestick reversal pattern**, similar to the Bearish Engulfing Pattern (see: Bearish Engulfing Pattern Page No.14)

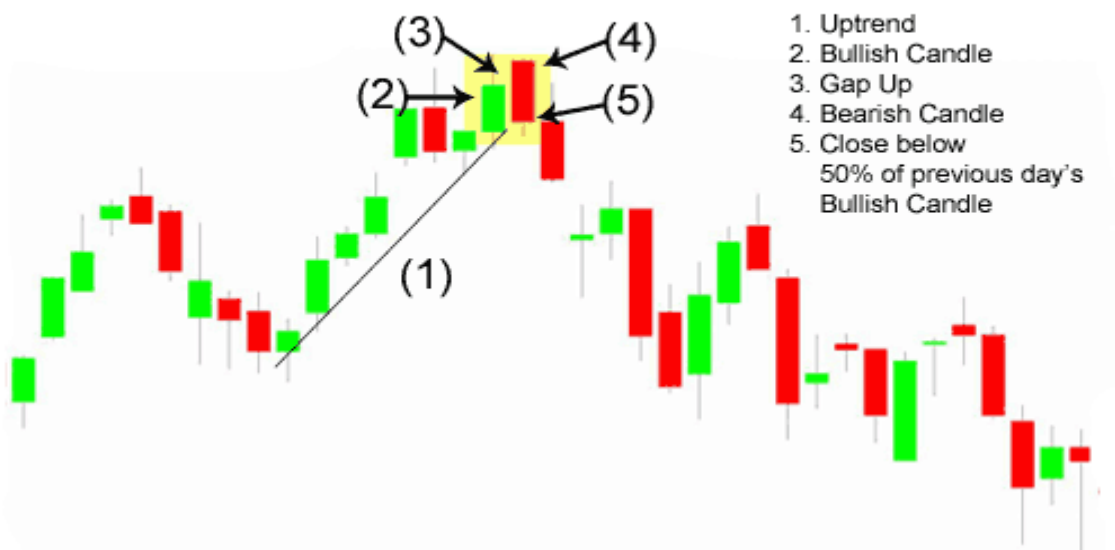
Dark Cloud Cover



There are two components of a Dark Cloud Cover formation:
Bullish Candle (Day 1) & Bearish Candle (Day 2)

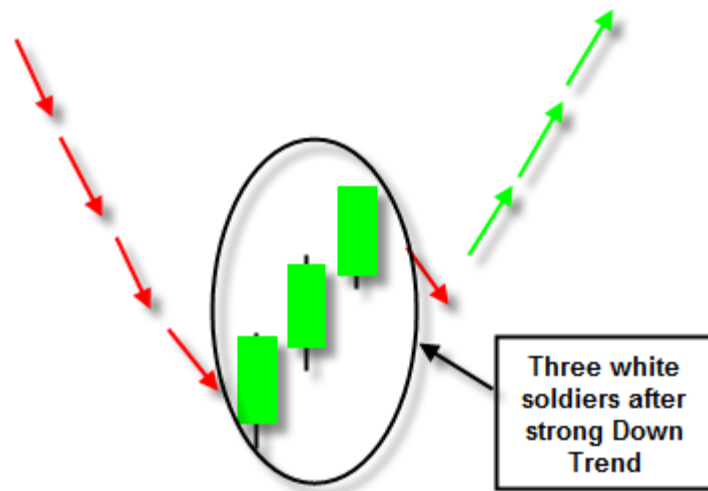
A Dark Cloud Cover Pattern occurs when a bearish candle on Day 2 closes below the middle of Day 1's candle. In addition, price gaps up on Day 2 only to fill the gap (see: Gaps) and close significantly into the gains made by Day 1's bullish candlestick. The rejection of the gap up is a bearish sign in and of itself, but the retracement into the gains of the previous day's gains adds even more bearish sentiment. Bulls are unable to hold prices higher; demand is unable to keep up with the building supply.

Dark Cloud Cover



THREE WHITE SOLDIERS

This is a 3-candle bullish pattern that **implies a reversal at the bottom of a down trend.**

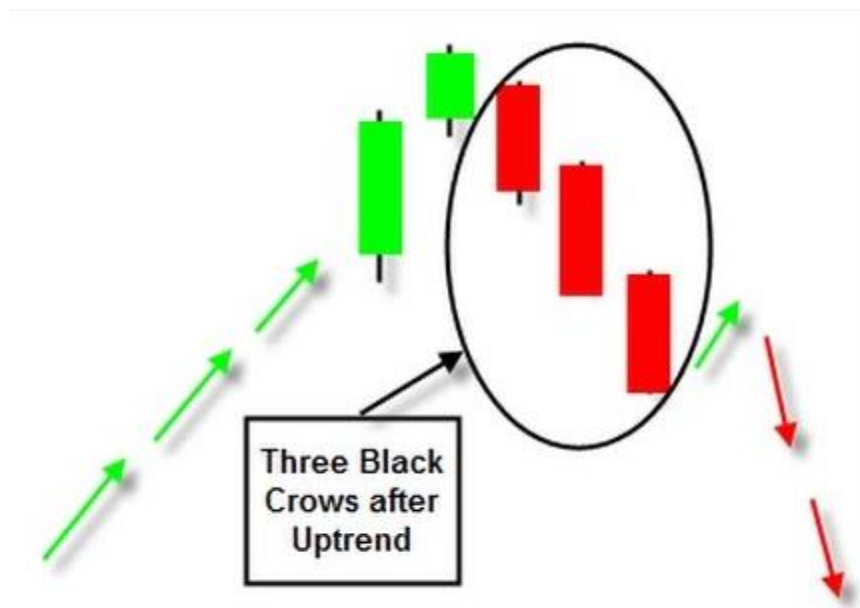


The three soldiers are bullish candlesticks that open within the body of the previous candlestick and close near the high of the day. This applies to all three candles; they should all be strong bullish candles, with small wicks and a close near the top. These high closes imply a strong reversal from bearish to bullish market sentiment.



THREE BLACK CROWS

This is a 3-candle bearish pattern that **implies a reversal at the top of uptrend**.

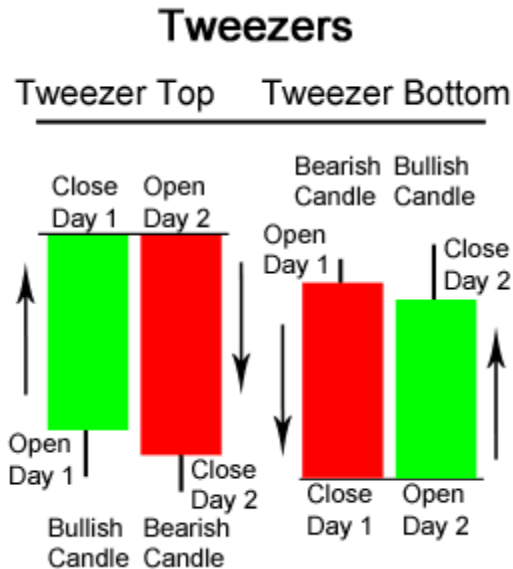


This 3-candle pattern is the opposite of “Three White Soldiers;” it signals the reversal away from bullish control at the top of an uptrend. It consists of three successive bearish bars that open within the preceding bar’s body and close below its close.



TWEEZER PATTERN

The **Tweezer Top** formation is viewed as a **bearish reversal pattern** seen at the top of uptrend and the **Tweezer Bottom** formation is viewed as a **bullish reversal pattern** seen at the bottom of downtrends.



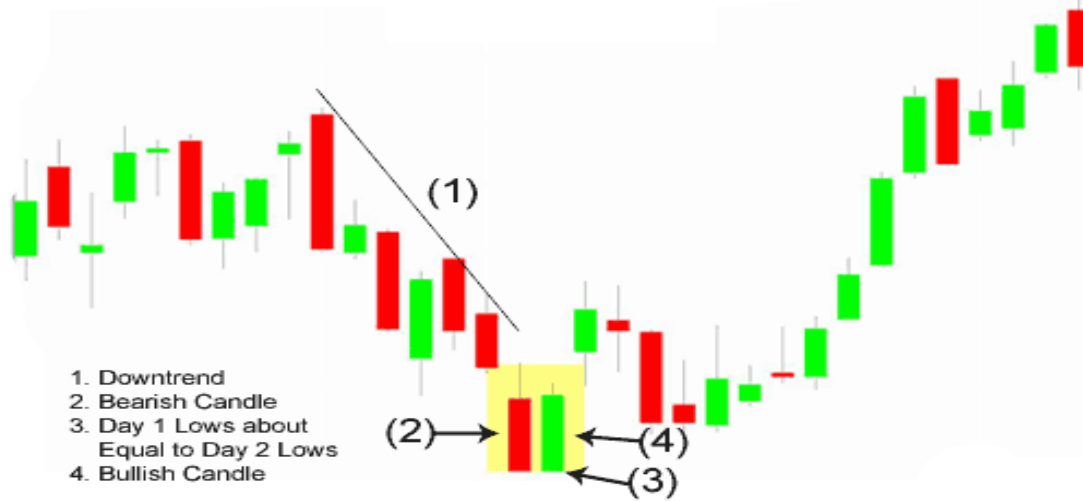
Tweezer Top formation consists of two candlesticks: Bullish Candle (Day 1) Bearish Candle (Day 2) Tweezer Bottom formation consists of two candlesticks: Bearish Candle (Day 1) Bullish Candle (Day 2) Sometimes Tweezer Tops or Bottoms have three candlesticks.

A bearish Tweezer Top occurs during an uptrend when bulls take prices higher, often closing the day off near the highs (typically a strong bullish sign). However, on the second day, how traders feel reverses completely. The market opens and goes straight down, often eliminating the entire gains of Day 1.

The reverse, a bullish Tweezer Bottom occurs during a downtrend when bears continue to take prices lower, usually closing the day near the lows (typically a strong bearish sign). Nevertheless, Day 2 is completely opposite because prices open and go nowhere but upwards. This bullish advance on Day 2 sometimes eliminates all losses from the previous day.

TWEEZER BOTTOM AND TOP

Tweezer Bottom

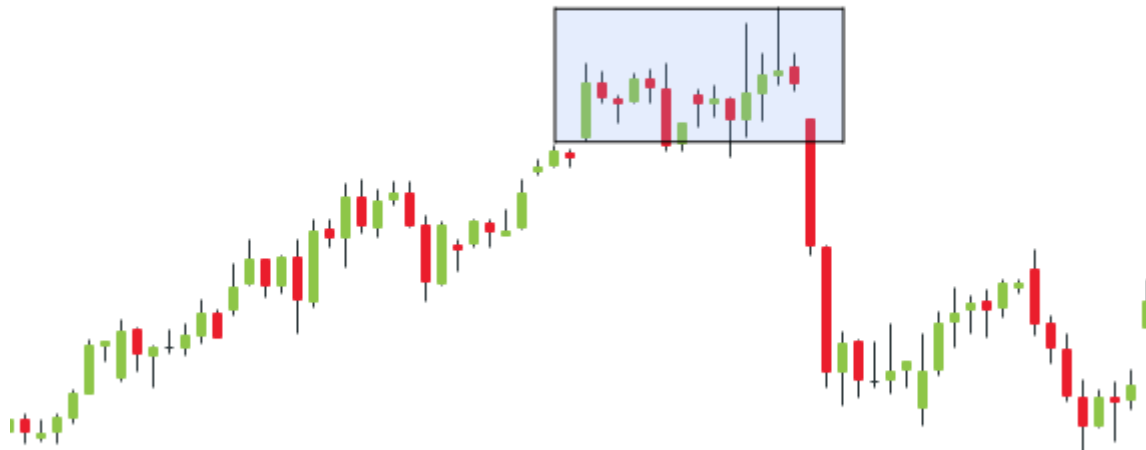


Tweezer Top



CHECKMATE

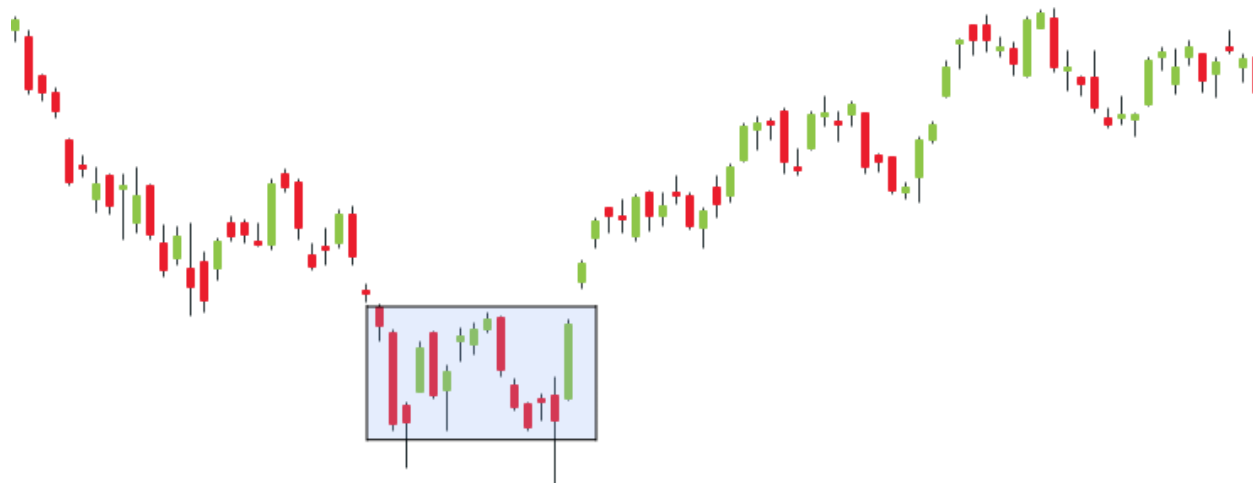
CHECKMATE BEARISH



Checkmates occur when price becomes locked in a narrow trading range **preceding a reversal in direction**. In a typical bearish checkmate, an uptrend meets a resistance level that is tested and then rejected due to consequent pressure from holding the level. In these cases, the checkmate begins as the first candle in the range reaches a high that the pressure from bulls is unable to surpass.

Price remains deadlocked in a tight trading range before the range is broken with a long bearish candlestick, indicating that the reversal has begun. As an entry signal, this pattern requires confirmation from one or two strong bearish bars.

CHECKMATE BULLISH



In a bullish checkmate, the opposite occurs, typically at a support rather than resistance level. The long lower wick of the first pin bar in the red box establishes a low that the bears cannot achieve; price is trapped thereafter in a narrow trading range, the checkmate, until bulls successfully reverse the trend. The tall Green candle immediately after the box confirms the bullish reversal.

KICKER

A kicker signal, also known as a professional gap, occurs when the following conditions are met:



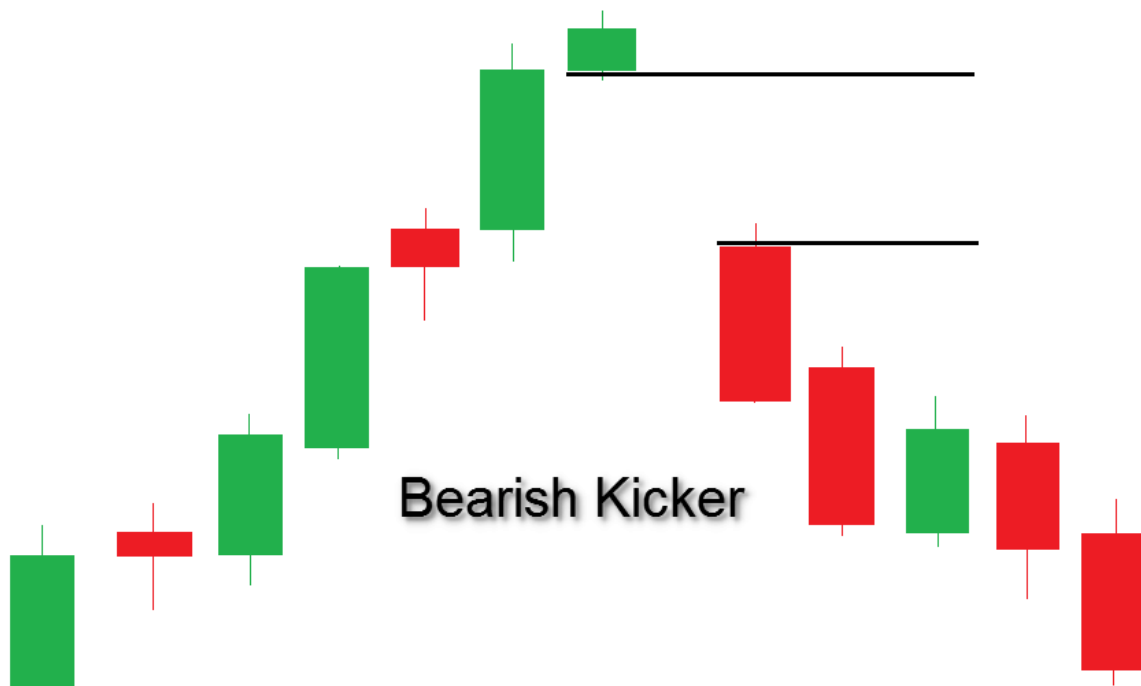
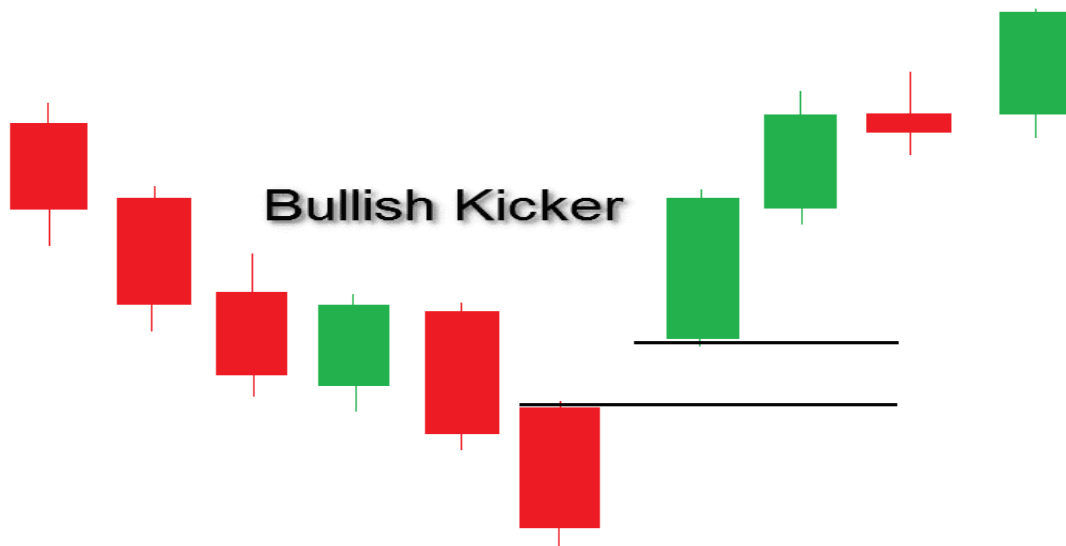
An indication that an increase in volatility is imminent. This affords traders the opportunity to create trades that speculate not so much on direction, but rather on an increase in volatility on a breakout in any specific direction.

In the context of a trend, a harami/ inside bar can be indicative of exhaustion and the onset of a reversal. In this manner, it is similar to long wick patterns and evening star/morning star patterns examined earlier in this guide.

Price is moving in a trend.

Suddenly, a gap appears in the chart. A gap is defined as when the open price of one candle is not equal to the close price of the candle that precedes it; there is a gap in the price movement. The gap is in the opposite direction of the trend. For instance, imagine that price closed at 10 after rallying over a number of days from 2. The next day, price opens at 8. In this instance, we have a gap down, or a bearish kicker. Conversely, if price fell from 10 to 3 and then opened the next day at 5, it would signal a bullish kicker, a bullish sign for traders.

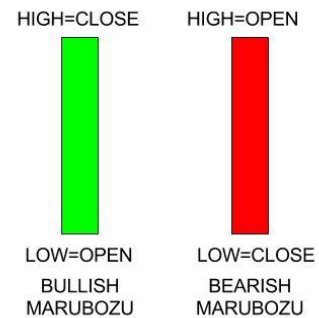
A kicker signal can be a very powerful sign that a trend is reversing. It is often interpreted as a sign that professional investors have quickly realized that a trend is over, and are looking to get out immediately. As such, this signal often precipitates a rapid reversal of the prior trend.



MARUBOZU

Marubozu candlesticks indicate that a stock traded strongly in one direction throughout the day. It either closed at its low price of the day or highest price of the day. Typically marubozu candlesticks have a long real body and no wicks or shadows. Although we know that real world charts aren't always so picture perfect.

A bullish marubozu has a long green real body. The bulls were in full control that day. The stock closed higher than it opened. It didn't have a higher or lower price that formed wicks.



MARUBOZU CANDLESTICKS

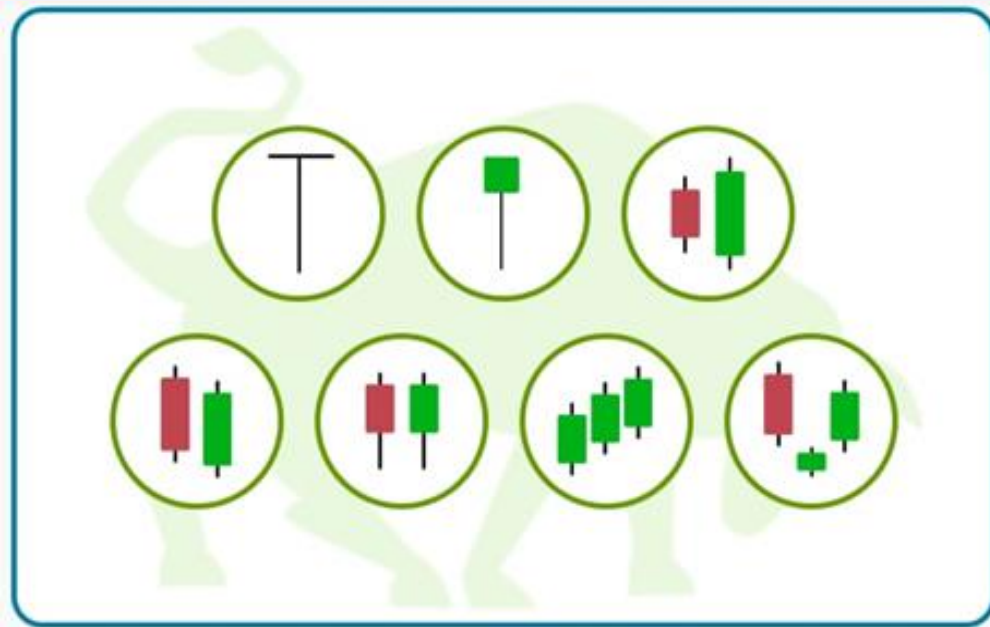
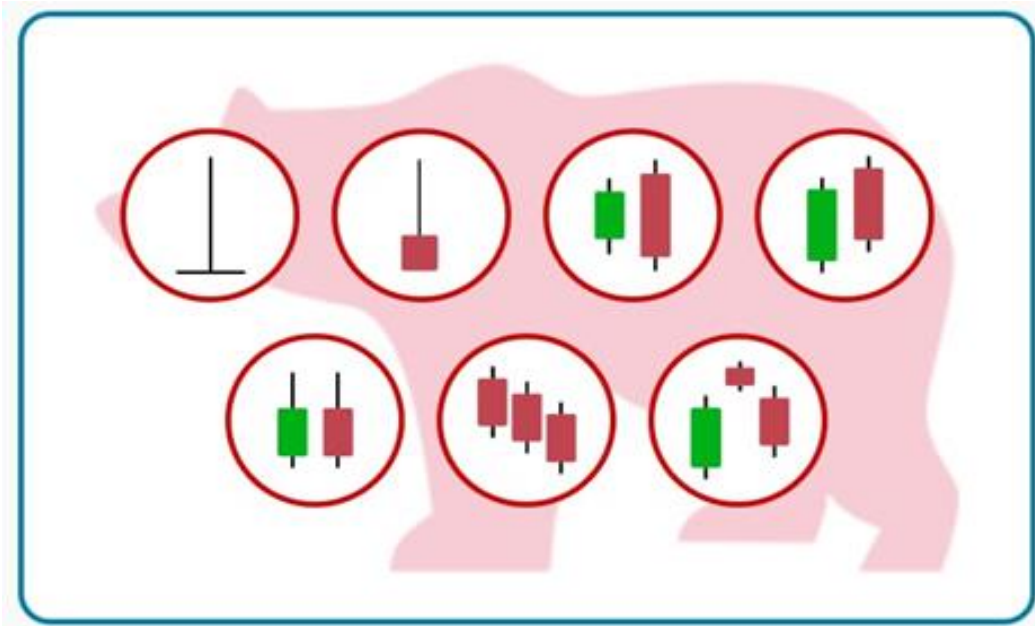
The bearish marubozu candle has a long red real body. The bears had control and drove price down. It closed lower than it opened. No high or lows formed wicks.

You can look at marubozu candlesticks by themselves but looking at the overall pattern they're apart of is important.

These candlesticks tell you who controlled the day. A bullish marubozu indicates that buyers controlled the price from open to close and is considered extremely bullish. Bearish marubozu candles indicate that sellers had control of price from start to finish and are a very bearish sign.



GUESS THE CANDLESTICK PATTERN ...???





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