What are candlesticks?

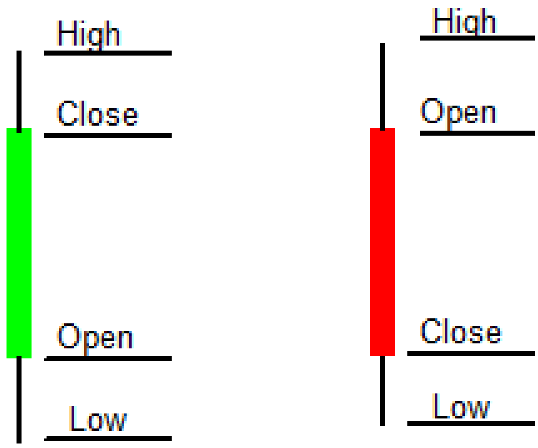
Candlestick Patterns

Candlestick charts provide the same information as the traditional bar chart–open, high, low, and close prices–but do so in a way that is a more visual depiction of price action during a single time period or series of time periods.

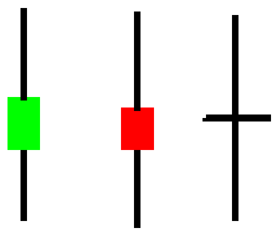
One candlestick can provide important information about the strength or weakness of the market during a given time interval, visually portraying where the close is relative to the open. A candlestick can represent a month, week, day, or intraday time interval. A green body indicates prices moved higher from the open to the close for the period and is a bullish sign. A red body indicates prices moved lower from the open to the close for the period and is a bearish sign.

Although the color of the body generally sets the bullish or bearish tone of a trading session, the wicks are also important, showing how far traders were willing to push prices during the period before coming back to close in the body.

If you study candlestick charting you will find there are several candlestick patterns that chartists use. Most of them can be classified as either indecision patterns or reversal patterns. Most patterns consist of multiple candles, but we are only interested in three patterns. All three of these patterns consist of one candle and the color of the candle is not important to us.



Doji Candles



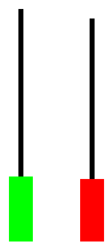
Doji's

Shooting Star

There are several names for various types of doji candles, but the three shown on the left are the only ones we are interested in. As long as the body is small relative to the wicks and the body is basically centered, we use this candle to represent as a candle of indecision. On all three of these candles, you can see that the market opened, price went above and below the open, and then closed fairly close to the open. This tells us for the moment supply and demand are in balance.

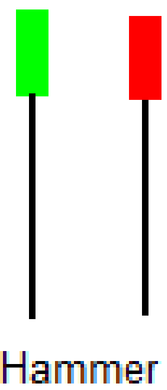
The shooting star is a bearish reversal pattern. The long wick at the top shows the buyers were in control until it hit the price indicated by the top of the wick. At this point, sellers were in control and pushed the price back down close to or below the open. This candle may have a small wick on the bottom.

The third pattern is the hammer. This is a bullish reversal pattern. At the open, sellers were in control until the price reached the point indicated by the bottom of the wick. At that point, buyers took over and pushed the price back close to the open or higher.



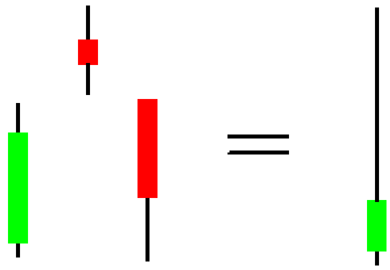
Shooting Star

Hammer

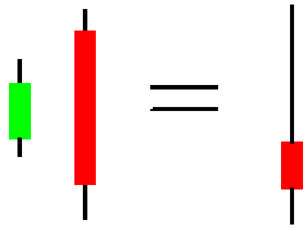


There are several other candlestick patterns, but there is no need to learn them. If you analyze all of the candlestick reversal patterns, you will find that if you add the candles together, they will form a hammer for the bullish reversal patterns and a shooting star for the bearish reversal patterns, except they are just forming over a longer period of time

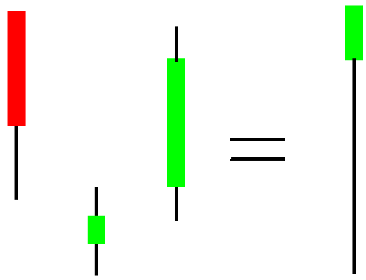
In later chapters when talking about supply and demand trading, you will learn that the faster the price moves in and out of a pivot point, the stronger the imbalance of supply and demand. For this reason, we only want to use the hammers and shooting stars for our trade set ups. The following shows a few of these reversal patterns. To add the candles together, you take the open of the first candle, the close of the last candle, and the highest high and lowest low in the pattern to draw the wicks. If the close is lower than the open, you have a red candle, otherwise you have a green candle.



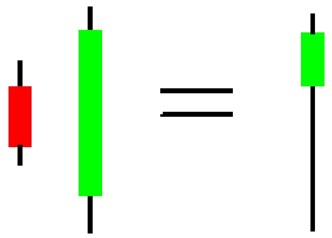
Evening Doji Star



Bearish Engulfing Pattern



Morning Star



Bullish Engulfing Pattern