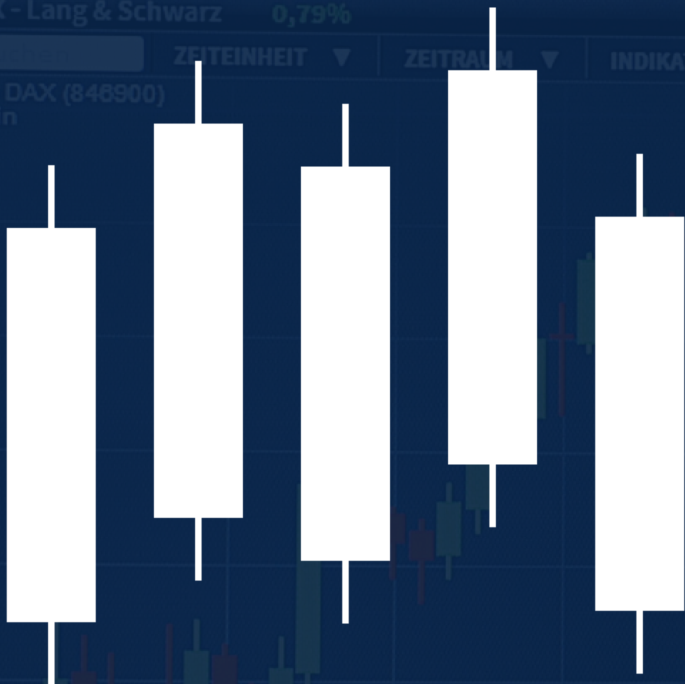
FEEL THE CANDLESTICKS

A BEGINNER'S GUIDE TO CANDLESTICK CHARTS



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In the world of trading and investing, there are two main ways to analyze financial instruments:

1. Fundamental Analysis

Fundamental analysis focuses on evaluating the real-world factors that affect the price and value of a financial instrument. This includes things like:

- Government policies (e.g., tax reforms, regulations).
- Economic indicators (e.g., inflation, GDP, unemployment rates).
- Company performance (revenue, profits, management quality).
- Industry trends and market conditions.

In simple terms, fundamental analysis helps you understand the intrinsic value of a stock or asset based on its underlying data. Investors use this method to find out whether a stock is undervalued or overvalued based on its true worth.

2. Technical Analysis

On the other hand, technical analysis is all about studying price charts and using charting tools to predict future price movements. It doesn't focus on the actual financial health of the company or the broader economy.

Instead, technical analysts believe that everything is reflected in the price, and by studying historical price data, they can predict future trends.

Some key tools used in technical analysis include:

- Candlestick patterns.
- Support and resistance levels.
- Indicators like moving averages, RSI (Relative Strength Index), etc.
- Trend lines and chart patterns like head and shoulders, triangles, etc.
- SMC (smart money concept)

In simple words, technical analysis is like reading a map or a graph to figure out where the price of a stock or any financial instrument might go next. It's all about understanding market psychology and using past price data to make predictions.
Both methods are valuable, and many traders often combine fundamental and technical analysis to get a complete picture of the market.

Price action is considered one of the best methods for analyzing charts. In this book, we will focus exclusively on price action.

In recent times, SMC (Smart Money Concepts) and ICT (Inner Circle Trader) have gained popularity. These methods are part of technical analysis, specifically price action, and focus on the micro-movements of price, usually observed on lower time frames.

Does this mean that candlestick patterns and traditional chart patterns are useless? Absolutely not. Candlesticks represent the action of buying or selling and provide valuable insights.

Price action can be classified into two categories:

1. **Macro Price Action** – This involves focusing on chart patterns and candlestick patterns in higher time frames such as monthly, weekly, daily, or even 4-hour charts. This approach helps in understanding the overall trend and larger market moves.

2. Micro Price Action – This is where SMC or ICT strategies are applied. These methods allow for precise entries by using concepts like liquidity raids, Fair Value Gaps (FVGs), or order blocks. These theories focus on the detailed price movements often visible on lower time frames for identifying key opportunities.

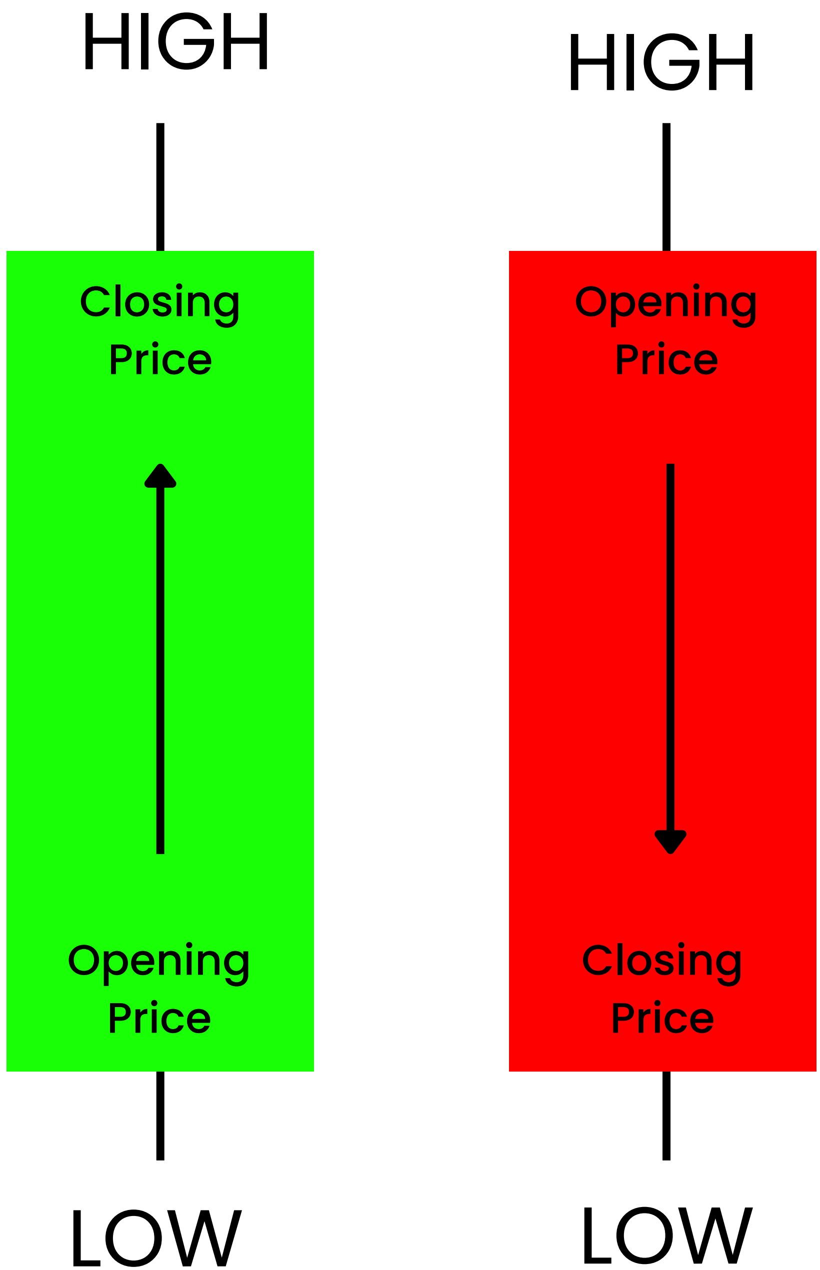
INTRODUCTION TO CHARTS

There are many types of charts available in the financial market, such as line charts, bar charts, and area charts. Each of these has its own benefits for analyzing price movements. However, candlestick charts are the most widely used among traders and investors. This is because candlestick charts provide more detailed information about price action.

Candlestick charts are a fundamental tool in the world of trading. They help traders visualize price movements and identify patterns that can signal potential market trends. Understanding candlestick patterns is essential for anyone interested in trading, as these patterns can provide valuable insights into market behavior.

WHAT IS A CANDLESTICK?

A candlestick is a type of chart used to represent the price movements of a stock over a specific period. Each candlestick shows the opening, closing, highest, and lowest prices during that time. The body of the candlestick represents the difference between the opening and closing prices, while the wicks (or shadows) show the highest and lowest prices. Candlesticks are typically green, indicating an upward trend, or red, indicating a downward trend. However, the color of the candles can be customized. What truly matters is identifying bullish candles, which indicate rising prices, and bearish candles, which indicate falling prices.


HIGH
Closing Price
Opening Price
LOW
HIGH
Opening Price
Closing Price
LOW

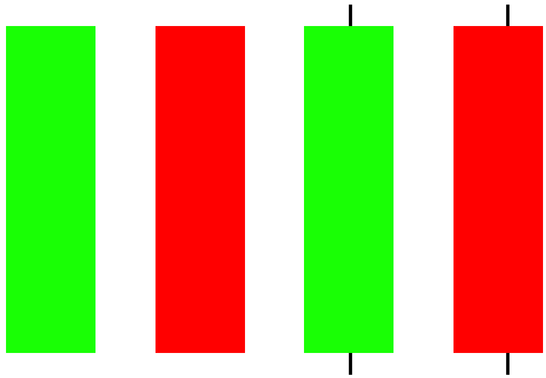
HISTORY OF CANDLESTICK CHARTS

Candlestick charts have a rich history that dates back to 18th-century Japan. They were developed by *Munehisa Homma*, a rice trader who observed that market prices were influenced by the emotions of traders. To capture this, he created candlestick charts that recorded price movements and market sentiment. These charts eventually spread beyond Japan and became a standard tool in financial markets worldwide.

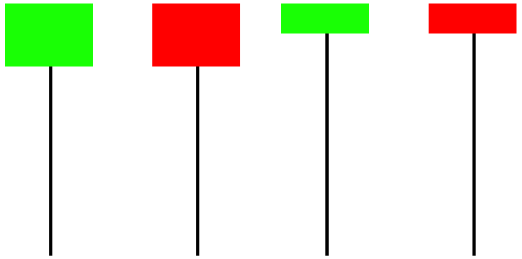
TYPES OF CANDLESTICKS

- Strength Candles (Marubozu)
- Rejection Candles (Pinbars)
- Indecisive Candles (Doji)

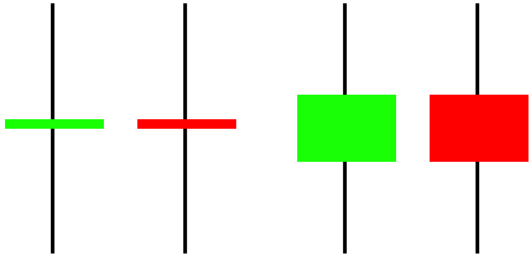
- **Strength Candles (Marubozu)**



- **Rejection Candles (Pinbars)**



- **Indecisive Candles (Doji)**



CANDLESTICK PATTERNS BASED ON THE NUMBER OF CANDLESTICKS

All logical candlestick patterns are created using the three types of candlesticks mentioned above.

Candlestick patterns can be classified based on the number of candlesticks involved. These patterns are important for swing trading, as they help traders predict potential market movements.

1. Single Candlestick Patterns

- **Hammer:** Appears after a downtrend, with a small body at the top and a long lower wick. It suggests a potential upward reversal.
- **Shooting Star:** Appears after an uptrend, with a small body at the bottom and a long upper wick. It indicates a potential downward reversal.
- **Inverted Hammer:** Similar to the hammer but appears after a downtrend, with a long upper wick.
- **Hanging Man:** Appears after an uptrend and looks similar to the hammer. It has a small body at the top with a long lower wick. It suggests a potential downward reversal, indicating that the market may be losing momentum.

- **Marubozu:** A candlestick with no wicks, indicating strong buying or selling pressure.
- **Doji:** A candlestick with a very small or no body, showing **indecision** in the market.

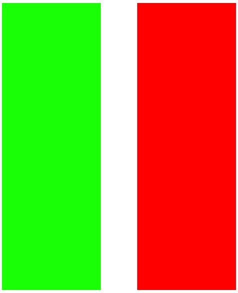
2. Double Candlestick Patterns

- **Engulfing Pattern:** Involves two candlesticks. In a bullish engulfing pattern, a small red candlestick is followed by a larger green candlestick, signaling a potential upward reversal. In a bearish engulfing pattern, a small green candlestick is followed by a larger red candlestick, indicating a potential downward reversal.

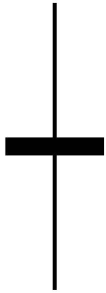
3. Triple Candlestick Patterns

- **Morning Star:** Appears after a downtrend and consists of three candlesticks. The first is a long bearish candlestick, followed by a small-bodied candlestick (doji or spinning top), and then a long bullish candlestick. This pattern suggests a potential upward reversal.

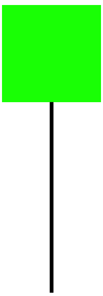
- **Evening Star:** Appears after an uptrend and is the opposite of the morning star. It consists of a long bullish candlestick, followed by a small-bodied candlestick, and then a long bearish candlestick, indicating a potential downward reversal.



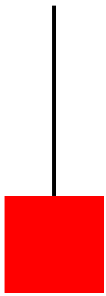
Marubozu



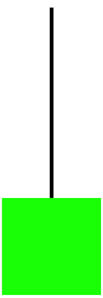
Doji



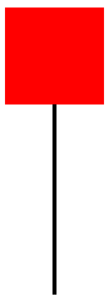
Hammer



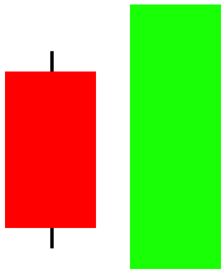
Shooting Star



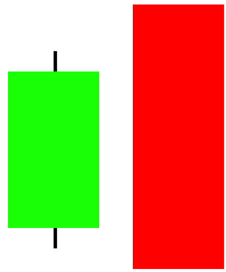
Inverted Hammer



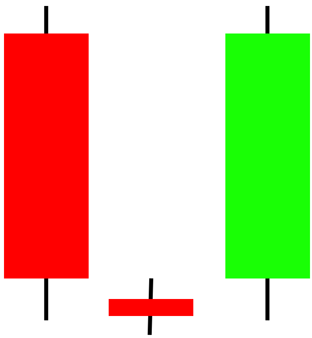
Hanging Man



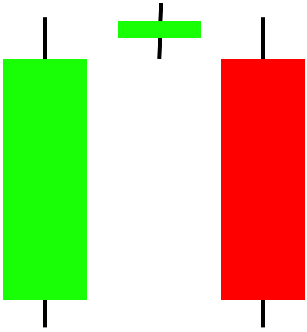
Bullish Engulfing



Bearish Engulfing



Morning Star

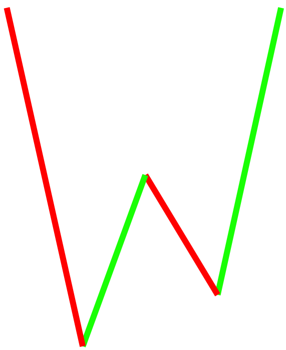


Evening Star

IMPORTANT CHART PATTERNS

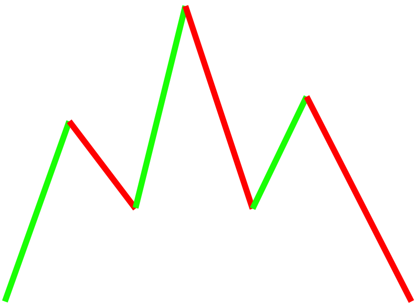
DOUBLE TOP

A double top usually signals that a strong uptrend may be ending. When the price fails to break the peak level a second time, it often starts to fall, indicating a potential trend reversal from bullish (upward) to bearish (downward).



DOUBLE BOTTOM

The double bottom signals a potential end to a downtrend. When the price bounces off the same low point twice and then starts rising, it could mean a shift from bearish (downward) to bullish (upward) movement.

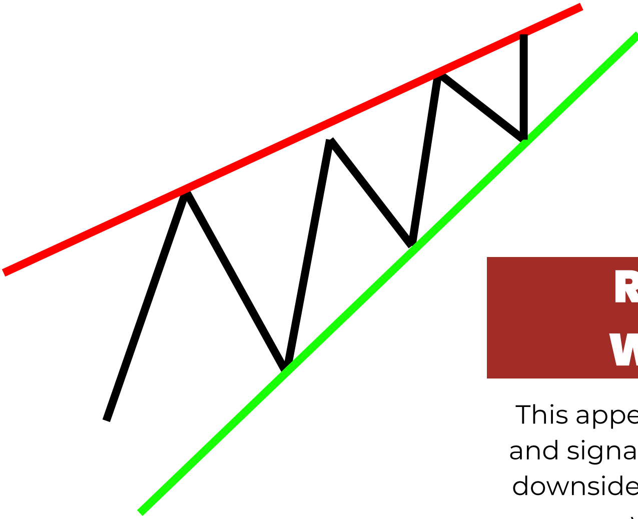


HEAD & SHOULDER

Head and shoulders is a bearish pattern that indicates a possible reversal from an uptrend to a downtrend. When the price reaches the left shoulder, rises to the head, then falls to the right shoulder, it's a sign that the buying pressure may be weakening, leading to a drop.

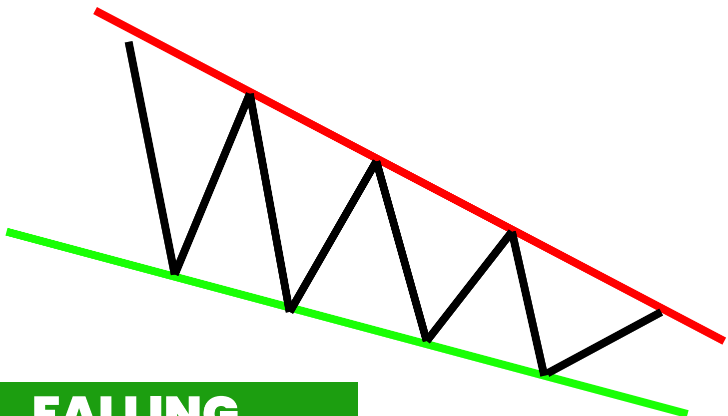
INVERTED HEAD & SHOULDER

This is a bullish reversal pattern, suggesting the end of a downtrend. After the inverted head and shoulders forms, the price usually starts to rise, signaling a shift from bearish to bullish momentum.



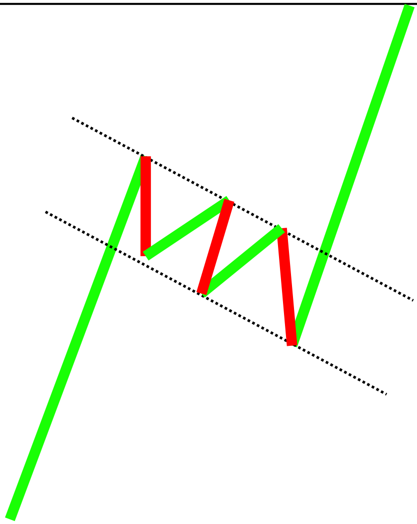
RISING WEDGE

This appears in an uptrend and signals a reversal to the downside, as buying power weakens.



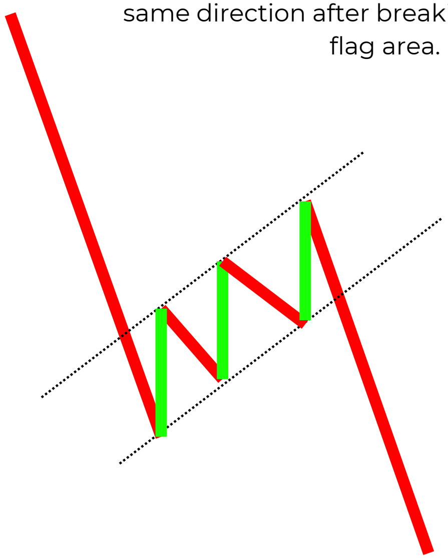
FALLING WEDGE

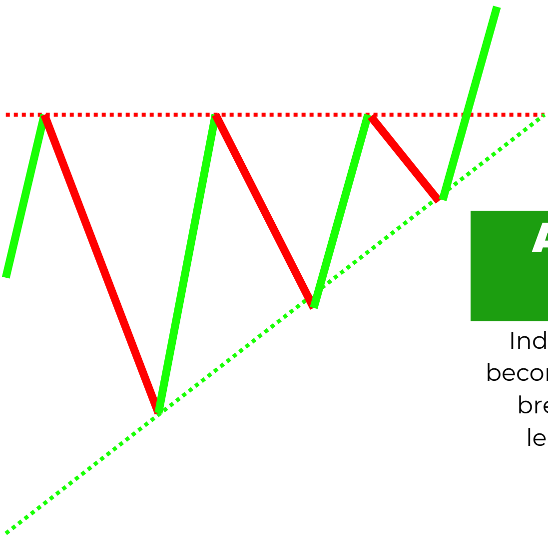
Found in a downtrend and signals a potential reversal to the upside as selling pressure starts to ease.



FLAG PATTERN

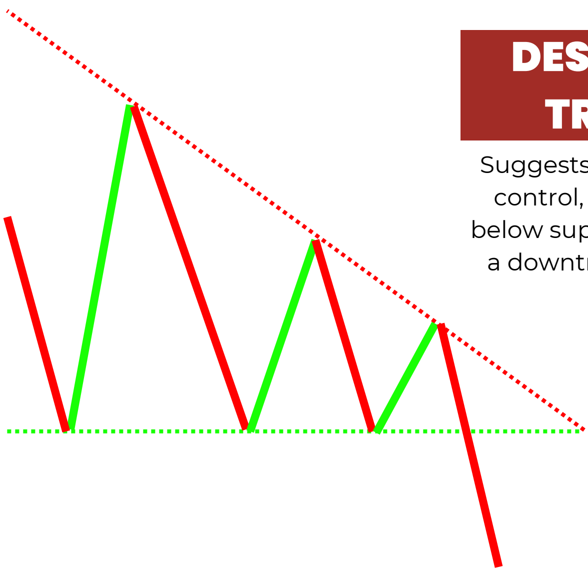
A flag pattern signals a continuation of the previous trend. When prices sharply rise or fall, then pause in a small range (forming the “flag”), they usually continue in the same direction after breaking out from the flag area.





ASCENDING TRIANGLE

Indicates that buyers are becoming stronger and may break above resistance, leading to an uptrend continuation.



DESCENDING TRIANGLE

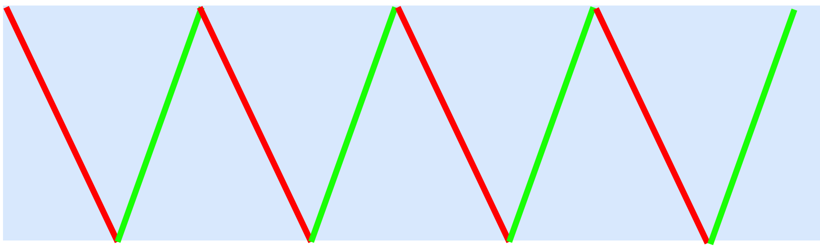
Suggests sellers are gaining control, possibly breaking below support and leading to a downtrend continuation.

RECTANGLE PATTERN / DARVAS BOX PATTERN

A rectangle forms when prices move sideways between a support and resistance level.

The Rectangle Pattern is also known as the Darvas Box Pattern.

This pattern indicates a period of consolidation, where buyers and sellers are balanced. A breakout above or below the rectangle suggests a continuation in the breakout direction.

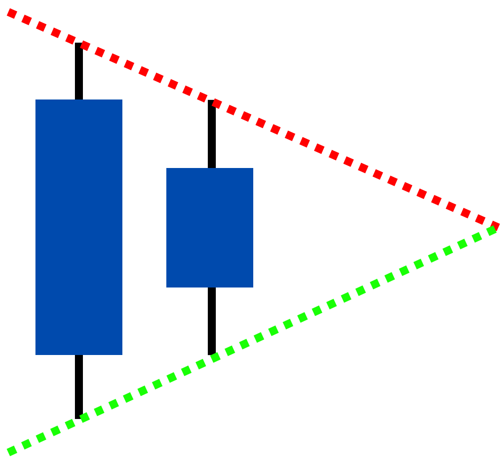


INSIDE BAR/SYMMETRICAL TRIANGLE/PENNANT PATTERN

Here is a special dedicated section for the inside bar candlestick pattern and the triangle pattern.

The inside bar candlestick pattern on a higher time frame often forms a triangle pattern on a lower time frame.

You can observe this by connecting the highs and lows of both the candlesticks.



The color of the candlesticks does not matter; they can be any color, but they must be of opposite colors to meet the criteria of an inside bar.

WHAT DOES AN INSIDE BAR INDICATE?

- **Consolidation**: The formation of an inside bar often suggests that the price is in a consolidation phase. This means that buyers and sellers are in a tug-of-war, and there's uncertainty in the market.
- **Potential Breakout**: An inside bar can signal that a breakout may happen soon. If the price moves above the high of the inside bar, it may indicate a bullish (upward) move. Conversely, if it moves below the low of the inside bar, it may signal a bearish (downward) move.
- **Market Strength**: If the inside bar forms after a strong price movement, it can show that the previous trend might continue. For example, if an inside bar appears after a strong uptrend, it might suggest that the uptrend will resume after the consolidation. This setup is also known as a Pennant Pattern.

SMART MONEY CONCEPT

ICT is a smart way to make entries, and SMC is also an effective method for entering trading positions. We will broadly discuss the Smart Money Concept and explore important aspects of modern-day SMC.

Smart money refers to the big players like banks, hedge funds, and large financial institutions. These entities have vast resources, in-depth market knowledge, and access to sophisticated data that allow them to make better-informed decisions. Retail traders, on the other hand, are usually at a disadvantage as they lack the same level of access to data and resources.

ORDERBLOCKS

It is the **last candle** before an upward or downward move.

Order blocks are valuable in trading because they indicate where the "smart money" has likely entered or exited. When price **revisits** these blocks, it's common to see strong reactions, such as reversals or bounces. For traders, these zones offer high-probability entry points for buying or selling.

FAIR VALUE GAP (FVG)

Fair Value Gaps (FVGs) or Imbalances refer to gaps in price where the market didn't have enough buying and selling orders to match. This results in a price range that wasn't fully "balanced" in terms of supply and demand. These imbalances often occur when the market moves too quickly in one direction, leaving areas where orders remain unfilled.

How to Identify a Fair Value Gap

Fair Value Gaps are generally spotted by looking at candlesticks on a price chart. Here's a simple way to find them:

1. Look for Strong Candles: When you see a large, strong bullish or bearish candle, there's often an imbalance in that area.
2. Examine the Price Action: An imbalance appears when there's a gap between the wicks of three consecutive candles.
   - For a bullish imbalance, the lowest wick of the first candle doesn't overlap with the highest wick of the third candle.
   - For a bearish imbalance, the highest wick of the first candle doesn't overlap with the lowest wick of the third candle.

This gap represents a "missed area" where price didn't trade as naturally, and it often draws the price back in the future as the market seeks balance.

Why Fair Value Gaps Matter

Fair Value Gaps act as magnet zones for price. Since these gaps represent unfilled orders, the price often revisits these areas to “fill” or balance them out. Institutional traders sometimes look for these zones to enter or exit trades, anticipating that the market will return to these levels.

Here’s why traders pay attention to FVGs:

- Potential Retracement Zones: Price often retraces to fill these gaps before continuing in its original direction.
- High-Probability Entries: For SMC traders, FVGs serve as ideal entry points in line with the trend.
- Indications of Momentum: Strong price movements that create these imbalances can indicate momentum and the presence of institutional orders.

MARKET STRUCTURE

In Smart Money Concepts (SMC) and technical analysis, terms like Break of Structure (BOS), Change of Character (CHOCH), Higher Highs (HH), Higher Lows (HL), Lower Highs (LH), and Lower Lows (LL) are essential for understanding market behavior. These concepts help traders spot potential trend continuations or reversals and are core to determining the direction and strength of a trend.

Higher High (HH) and Higher Low (HL):

- These terms are used to describe an uptrend.
- Higher High (HH): When each high point in the trend is higher than the previous high, indicating strong buying pressure.
- Higher Low (HL): When each low point in the trend is higher than the previous low, confirming that buyers are stepping in at higher levels.
- Together, HH and HL formations show a healthy uptrend where buyers are in control.

Lower High (LH) and Lower Low (LL):

- These terms describe a downtrend.
- Lower High (LH): When each high is lower than the previous high, showing sellers are maintaining control.
- Lower Low (LL): When each low is lower than the previous low, further confirming the downtrend.
- The LH and LL formations indicate sustained selling pressure, with sellers dominating the market.

Break of Structure (BOS):

- A Break of Structure (BOS) occurs when the price breaks through a previous high or low in the trend, signaling a continuation.
- In an uptrend, a BOS happens when price breaks above the last Higher High (HH), confirming the bullish trend.
- In a downtrend, a BOS occurs when price breaks below the last Lower Low (LL), reinforcing the bearish trend.
- BOS is a signal that the current trend (either up or down) is likely to continue.

Change of Character (CHOCH):

- A Change of Character (CHOCH) is a key point where the trend shows early signs of a reversal.
- For example, in an uptrend, a CHOCH occurs if the price suddenly breaks below a significant Higher Low (HL). This break can indicate that sellers are starting to gain control, potentially leading to a downtrend.
- Conversely, in a downtrend, a CHOCH happens when price breaks above a Lower High (LH), signaling that buyers might be taking control.
- CHOCH is an early warning that the current trend might be ending, making it a useful tool for identifying potential reversals.

LIQUIDITY ZONES

- **Buy-Side Liquidity**: This includes zones where there are many pending buy orders. These orders are often stop-loss orders placed by traders who are short (betting the market will fall). When the price reaches this zone, it can trigger these buy orders, causing the price to rally as short sellers exit their trades.
- **Sell-Side Liquidity**: This includes zones with a high concentration of sell orders. These orders are often stop-loss orders placed by traders who are long (expecting the market to rise). When the price drops into this area, it can trigger these sell orders, causing a decline as long traders exit their positions.

For institutional traders, liquidity zones provide opportunities to execute large trades with minimal slippage, as they can buy or sell in bulk without causing wild price swings. These zones are also important for retail traders because they can be areas of potential reversals or breakout points. By knowing where liquidity is concentrated, retail traders can anticipate where big moves might happen.

JOIN OUR YOUTUBE CHANNEL TO LEARN HOW TO IDENTIFY THESE THINGS ACCURATELY

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CANDLESTICKS AND TIMEFRAMES

Time is a powerful element in trading. **The larger the timeframe, the more reliable and accurate the candlestick patterns become.** It's important to start by analyzing patterns in higher timeframes, such as monthly or weekly charts. Once you've identified patterns in these timeframes, you can move down to daily, hourly, and even minute charts.

THE BOTTOM LINE

This ebook is created specifically for swing trading purposes. It covers almost all the important candlestick patterns. To get the most out of these patterns, start by identifying them in higher timeframes. Remember, patterns identified in higher timeframes are more reliable and can give you a better edge in the market.

DISCLAIMER:

The information provided in this ebook is solely for educational purposes. Don't blindly jump into trading without proper **experience** and knowledge. It is always better to consult a financial advisor.

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