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Introducing

MAGIC FOREX CANDLESTICKS

Trading Guide

Your guide to financial freedom.



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Chapter I: Introduction to candlesticks

I.1. Understanding the candlestick chart

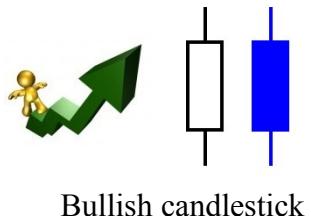
Most traders focus purely on technical indicators and they don't realize how valuable the original candlesticks are. Technical indicators are derived from nothing but charts. Candlestick charts! If you know how to translate the information stored in one simple candlestick chart, you will be light years ahead of the crowd. With candlesticks, you can't go the wrong way. So let's start with some basics. If you have already fallen in love with candlestick charts, jump to the next paragraph. The next steps are to set up the most popular MetaTrader platform, but all modern platforms allow you to display candlestick charts.



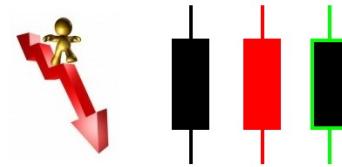
A single bar or candlestick represents the price change within one hour, a minute, 5 minutes, one day, week, month, etc. There is a standard bar chart on the left and a modern candlestick chart on the right. They both provide us the same information.

Anatomy of a candlestick

The first thing important about candlesticks is to distinguish between *bullish* and *bearish* candlesticks.



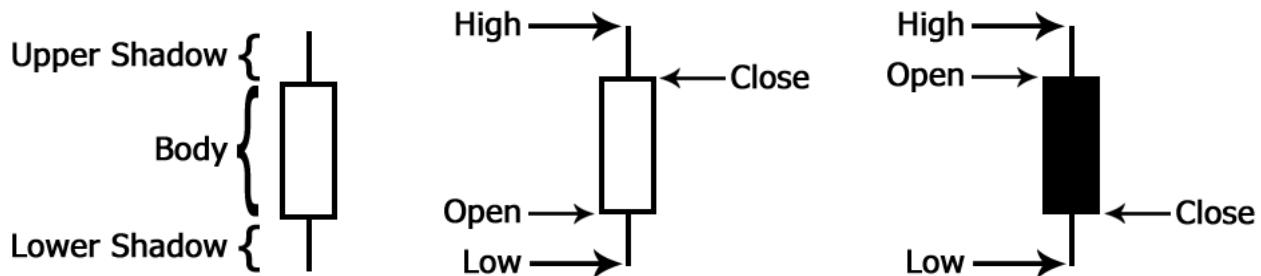
Bullish candlestick



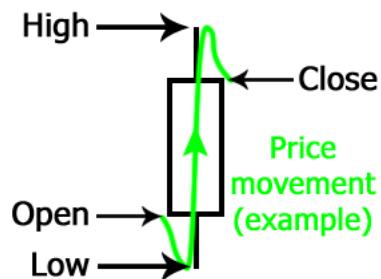
Bearish candlestick

Generally, a *bullish* candlestick is colored white, blue or blank. It is telling us that the price has *moved up* in one hour, one minute, five minutes, etc. (depending on current time-frame being set on the chart). A *bearish* candlestick is colored black, red or dark. It is telling just the opposite – the price has *moved down*.

Now let's talk about some widely used terms.



In the hourly time-frame, a candlestick opens at the beginning of the hour and closes at the end of the hour. The portion between the *open* and *close* is called *the body*. During that hour, price can move up or down to the highest and lowest point and forms *the shadows*.



We don't see how the price was moving inside the candlestick. We only see the overall picture.

One important note: Always wait until the candlestick closes. Never make trading decisions based on current candlestick as it is still forming. A seemingly bullish candlestick can turn to bearish in no time! This is the most common mistake traders do. Be patient.

I.2. Candlestick patterns really work!

Candlestick charting was developed in Japan hundreds of years ago. For more information about the history and overview, check out Wikipedia:

[Candlestick chart - Wikipedia](#)

Professional traders focus on candlestick analysis and there was great research done. Look at the proof that **one simple candlestick pattern** works and gives positive results!

Proof: [How Profitable Are Candlestick Strategies in Currency Trading?](#)

And here are the 1-year results (2007) on EUR/USD, 30 minute time-frame, 150 pips target for **all known candlestick patterns together!** No confirmation, no filtering, no trade management, no smart things at all.

Bars in test	13277	Ticks modelled	25552	Modelling quality	n/a
Mismatched charts errors	0				
Initial deposit	10000.00				
Total net profit	9116.50	Gross profit	36252.50	Gross loss	-27136.00
Profit factor	1.34	Expected payoff	38.47		
Absolute drawdown	897.40	Maximal drawdown	4101.30 (21.51%)	Relative drawdown	21.51% (4101.30)
Total trades	237	Short positions (% of total)	99 (27.27%)	Long positions (% of total)	138 (36.23%)
		Profit trades (% of total)	77 (32.49%)	Loss trades (% of total)	160 (67.51%)
		Largest profit trade	1525.20	loss trade	-439.20
		Average profit trade	470.81	loss trade	-169.60
		Maximum consecutive wins (profit in money)	4 (594.40)	consecutive losses (loss in money)	11 (-1864.70)
		Maximal consecutive profit (count of wins)	2055.20 (2)	consecutive loss (count of losses)	-1864.70 (11)
		Average consecutive wins	2	consecutive losses	3

This report was created with the [IntelligentEA Expert Advisor](#).

So what is a candlestick pattern?

Candlestick pattern is a group of candlesticks that signal potential trend reversal or trend continuation. Traders are trying to identify patterns in the chart and looking to enter or exit their position. Candlestick patterns give more insight into the current market psychology and help traders to make immediate decisions. The next example shows well-known candlestick patterns in the chart.



This chart was created with [Candlestick Pattern Recognizer](#).

As you can see, the patterns often forecast the market tops and bottoms. When a candlestick reversal pattern appears, you should exit before it's too late!



Chapter II: High profit candlestick patterns

Here we will cover the well-known candlestick patterns for informational purposes only. The schematics on the left shows how it may look in the real chart. Every pattern has a funny name and brief description. You don't have to remember them all! We will talk about one very simple but effective pattern in **Chapter IV: Simple scalping strategy**. Just keep an eye on some reversal and continuation patterns.

II.1. Bullish reversal patterns

This category of candlestick patterns signals a potential trend reversal from bearish to bullish. Before a pattern appears, you should identify a short-term *downtrend*. We will talk about trend definition later in **Chapter III: What is the market trend?**. Important to note, a reversal pattern does not necessarily result in complete trend reversal, but a minor change or pause in price action.



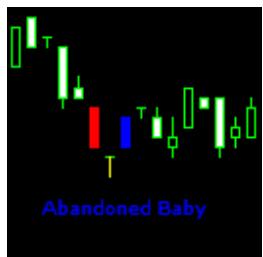
Morning Star

A small body that gaps downward implies indecision between buyers and sellers and potential trend reversal. The reversal is confirmed by bullish candlestick on the third day.



Piercing Line

A long bearish candlestick is followed by a long bullish candlestick that opens below the previous day's low and closes within the first day body (and above the midpoint of this body). The market feels uncertain to make new lows.



Abandoned Baby

A **Doji** (candlestick with very small body) appears and completely gaps below the bearish candlestick. The reversal is confirmed by the second gap and bullish candlestick.



Three Inside Up

A bullish **Harami** pattern (discussed later) appears in the first two days. The reversal is confirmed by bullish candlestick on the third day that closes higher than previous candlestick.



Three Outside Up

A bullish **Engulfing** pattern (discussed later) appears in the first two days. The reversal is confirmed by bullish candlestick on the third day that closes higher than previous candlestick.



Three White Soldiers

Three consecutive bullish candlesticks. Each opens within the body of the previous candlestick and closes at a new high.



Concealing Baby Swallow

Very rare pattern. Two consecutive bearish **Marubozu** candlesticks appear (**candlesticks with long body and short shadows**). The third candlestick with long upper shadow gaps downward. The fourth bearish *Marubozu* candlestick completely engulfs the previous candlestick.



Engulfing

Simple. The body of the bullish candlestick engulfs the body of the previous bearish candlestick.



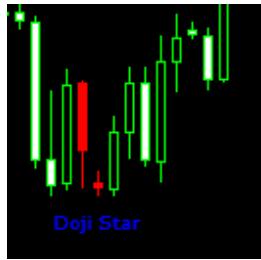
Dragonfly Doji

A **Doji** with long lower shadow and no (or very short) upper shadow looks like a dragonfly. It implies indecision between buyers and sellers and it seems that buyers took the price back for a moment.



Gravestone Doji

Similar to **Dragonfly Doji**, but the upper shadow is long and the lower shadow is very short or none.



Doji Star

A **Doji** with small trading range gaps below the previous bearish candlestick. It implies indecision between buyers and sellers.



Harami Cross

A bullish **Harami** pattern (discussed later) appears. Additionally, the second candlestick is a **Doji**.



Three Stars In The South

Very rare. The first bearish candlestick has long lower shadow and very short upper shadow. The second candlestick is similar to the first one, but it's a bit smaller and its low is higher than the previous low. The third candlestick is also bearish and lies within the range of the previous candlestick.



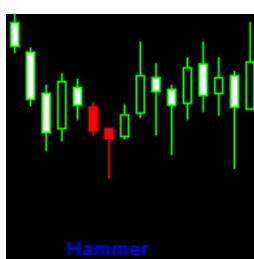
Breakaway

Long bearish candlestick is followed by a gap. The next three consecutive bearish candlesticks make new lows. Suddenly, a long bullish candlestick appears and closes inside the gap between the first two candlesticks.



Harami

Simple. The body of the bullish candlestick is engulfed by the body of the previous bearish candlestick.



Hammer

Hammer is a candlestick with a small body, long lower shadow as compared to the body and very short or no upper shadow. This implies that sellers cover their positions. Color of the hammer is not important here.



Inverted Hammer

Inverted Hammer is a candlestick with a small body, long upper shadow as compared to the body and very short or no lower shadow. This implies that sellers can't push price lower. Color of the Inverted Hammer is not important here.

II.2. Bullish continuation patterns

Bullish continuation patterns signal that the established trend will continue. Before a pattern appears, you should identify a short-term *uptrend*. We will talk about trend definition later. A continuation pattern often lead to consolidation.



Rising Three Methods

A long bullish candlestick is followed by some small candlesticks forming a brief downtrend that does not exceed the low of the first candlestick. The fifth bullish candlestick closes at a new high. It confirms that the bullish mood has resumed.



Three Line Strike

Three consecutive bullish candlesticks, each closing at a new high, are followed by a bearish candlestick that opens at a new high and closes below the first day's open.



Mat Hold

A long bullish candlestick is followed by a gap and then by some small candlesticks forming a brief downtrend that does not exceed the low of the first candlestick. The fifth bullish candlestick gaps upward and closes at a new high. It confirms that the bullish mood has resumed.

II.3. Bearish reversal patterns

This category of candlestick patterns signals a potential trend reversal from bullish to bearish. Before a pattern appears, you should identify a short-term *uptrend*. We will talk about trend definition later. Important to note, a reversal pattern does not necessarily result in complete trend reversal, but a minor change or pause in price action.



Evening Star

A small body that gaps upward implies indecision between buyers and sellers and potential trend reversal. The reversal is confirmed by bearish candlestick on the third day.



Dark Cloud Cover

As opposed to **Piercing Line**, a long bullish candlestick is followed by a long bearish candlestick that opens above the previous day's high and closes within the first day body (and below the midpoint of this body). The market feels uncertain to make new highs.



Abandoned Baby

A **Doji** (candlestick with very small body) appears and completely gaps above the bullish candlestick. The reversal is confirmed by the second gap and bearish candlestick.



Three Inside Down

A bearish **Harami** pattern (discussed later) appears in the first two days. The reversal is confirmed by bearish candlestick on the third day that closes lower than previous candlestick.



Three Outside Down

A bearish **Engulfing** pattern (discussed later) appears in the first two days. The reversal is confirmed by bearish candlestick on the third day that closes lower than previous candlestick.



Three Black Crows

Three consecutive bearish candlesticks. Each opens within the body of the previous candlestick and closes at a new low.



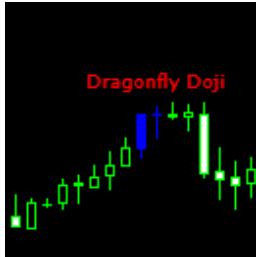
Upside Gap Two Crows

A long bullish candlestick is followed by an upward gap and a bearish candlestick. The body of the third bearish candlestick engulfs the body of the previous candlestick and closes above the first day's close. Weakening of the uptrend is evident.



Engulfing

Simple. The body of the bearish candlestick engulfs the body of the previous bullish candlestick.



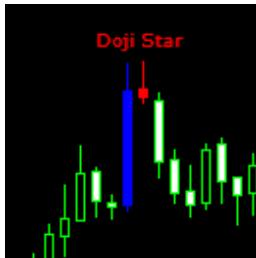
Dragonfly Doji

A **Doji** with long lower shadow and no (or very short) upper shadow looks like a dragonfly. It implies indecision between buyers and sellers.



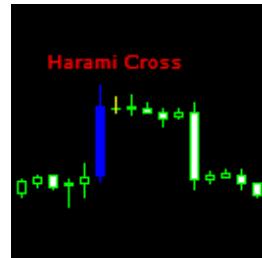
Gravestone Doji

Similar to **Dragonfly Doji**, but the upper shadow is long and the lower shadow is very short or none.



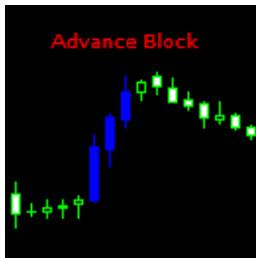
Doji Star

A **Doji** with small trading range gaps above the previous bullish candlestick. It implies indecision between buyers and sellers.



Harami Cross

A bearish **Harami** pattern (discussed later) appears. Additionally, the second candlestick is a **Doji**.



Advance Block

Three consecutive bullish candlesticks. Each opens within the body of the previous candlestick and closes at a new high. Each body is smaller than the previous day's body. It signals weakening of the uptrend.



Two Crows

A long bullish candlestick is followed by an upward gap and a bearish candlestick. The third bearish candlestick opens within the body of the previous candlestick and closes within the first day's body.



Breakaway

Long bullish candlestick is followed by a gap. The next three consecutive bullish candlesticks make new highs. Suddenly, a long bearish candlestick appears and closes inside the gap between the first two candlesticks.



Harami

Simple. The body of the bearish candlestick is engulfed by the body of the previous bullish candlestick.



Shooting Star

Shooting Star is a candlestick with a small body, long upper shadow as compared to the body and very short or no lower shadow. This implies that buyers cover their positions. Color of the Shooting Star is not important here.



Hanging Man

Hanging Man is a candlestick with a small body, long lower shadow as compared to the body and very short or no upper shadow. This implies that buyers can't push price higher. Color of the Hanging Man is not important here.

II.4. Bearish continuation patterns

Bearish continuation patterns signal that the established trend will continue. Before a pattern appears, you should identify a short-term *downtrend*. We will talk about trend definition later. A continuation pattern often lead to consolidation.



Falling Three Methods

A long bearish candlestick is followed by some small candlesticks forming a brief uptrend that does not exceed the high of the first candlestick. The fifth bearish candlestick closes at a new low. It confirms that the bearish mood has resumed.



Three Line Strike

Three consecutive bearish candlesticks, each closing at a new low, are followed by a bullish candlestick that opens at a new low and closes above the first day's open.



Mat Hold

A long bearish candlestick is followed by a gap and then by some small candlesticks forming a brief uptrend that does not exceed the high of the first candlestick. The fifth bearish candlestick gaps downward and closes at a new low. It confirms that the bearish mood has resumed.

Chapter III: How to find out the market trend?

The *Heiken Ashi* indicator is a popular tool that helps to identify the trend.



For better reading, hide the grid by pressing CTRL+G and zoom the chart to be overlaid with *Heiken Ashi* candlesticks.

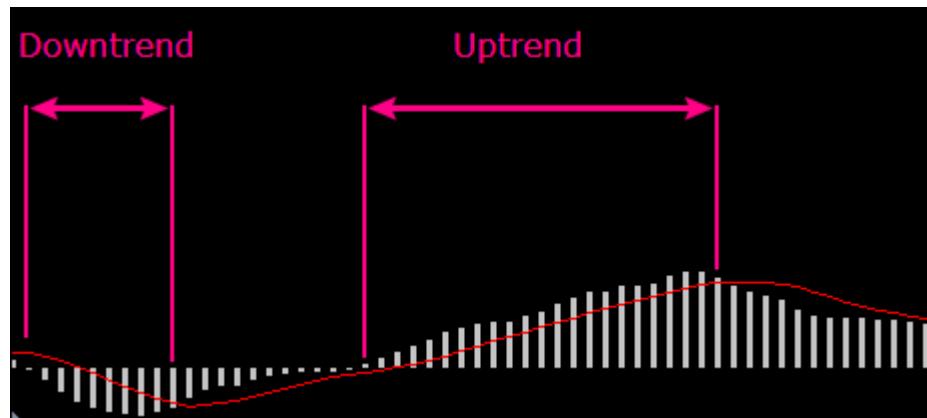
As you can see, uptrend is overlaid with white candlesticks and downtrend is overlaid with red candlesticks. The advantage is that *Heiken Ashi* quickly responds to trend reversal. The color changes almost immediately.

The disadvantage of this approach is that it does not include consolidation. The *Heiken Ashi* indicator shows either uptrend, or downtrend, but never consolidation. So, we get too much false signals in the choppy market! This is why we use another indicator called MACD, an acronym for *Moving Average Convergence / Divergence*. Sounds scientific, but nothing difficult.



The MACD indicator is displayed as a gray histogram by default. It's above the zero line in uptrend and below the zero line in downtrend. Sometimes the histogram looks “choppy” – quickly reversing up and down implying that the market is in chop zone. We will filter such situation using the so called *Signal Line* – simple moving average of MACD. We state the following rules:

Uptrend	Downtrend
<ul style="list-style-type: none"> • MACD is above the zero line • MACD is above the signal line 	<ul style="list-style-type: none"> • MACD is below the zero line • MACD is below the signal line



The same trend definition is built in the [Candlestick Pattern Recognizer](#).

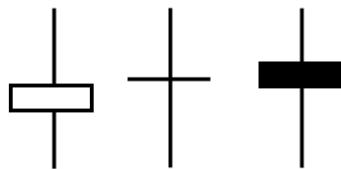
MACD is a *lagging* indicator. It means that it shows only the history and you shouldn't make trading decisions based solely on this indicator. One exception to this statement are *MACD divergences* – a strong weapon of successful traders. We will talk about *divergences* later. Unlike *Heiken Ashi*, MACD signals trend reversal too late. But remember, we actually trade candlestick patterns and we use MACD only as trend confirmation. We are just filtering signals that are based on candlestick patterns and that's OK.

You can use either *Heiken Ashi*, or MACD, or both... or your very own method to define the trend. Nothing is perfect and there are no paradigms. Stick to what you feel comfortable with!

Chapter IV: Simple scalping strategy

IV.1. Wow, Lucky Spike!

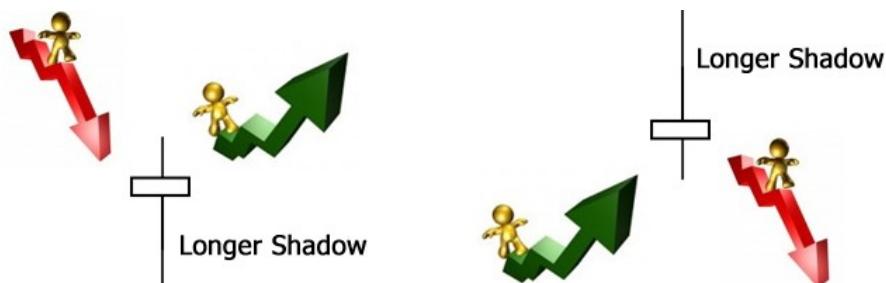
Now, we are going to reveal one very simple strategy based on a strong and easily noticeable candlestick pattern. Everyone can learn it, use it and make money with it. There are traders who make a living trading just this pattern. We called it *Lucky Spike*. The definition is simple. The shadows are longer than usual. Preferably, the trading range is at least three times longer than the body. The longer, the better.



Sometimes it looks like the Morning Star, Shooting Star, Hammer, Inverted Hammer, Doji, etc. A spike showing after strong trend signals that the trend is going to reverse or pause. Neither buyers, nor sellers dominate to drive the market higher or lower. Every extremely quick trend reversal is initiated by a spike.



We prefer one shadow to be longer, making a new significant low or high.



In the next paragraph, we will discuss where to enter, where to place Stop Loss and where to exit.

IV.2. Take a profit now!

Bullish Signal	Bearish Signal
<ol style="list-style-type: none">1. Strong downtrend.2. Lucky Spike, Buy!3. Place Stop Loss just below the Lucky Spike shadow.4. Take profit on the next candlestick's close.	<ol style="list-style-type: none">1. Strong uptrend.2. Lucky Spike, Sell!3. Place Stop Loss just above the Lucky Spike shadow.4. Take profit on the next candlestick's close.

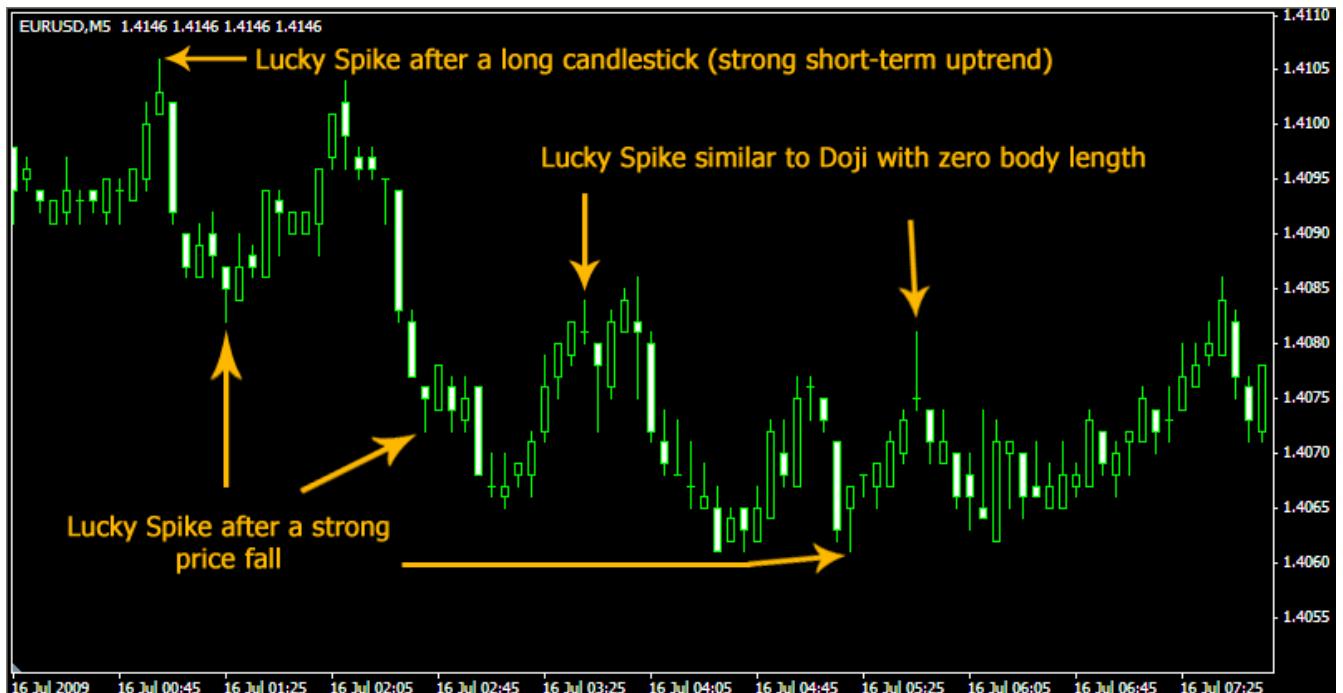


After a spike, there is often a longer candlestick – bullish after strong downtrend, or bearish after strong uptrend. Not every time, but it happens far more often than not. Whether the trend has reversed or not, trade just one candlestick for a few pips profit. That's easier and more effective than chasing the trend or watching how it is turning against you on the next candlestick. Successful traders keep it simple!

IV.3. Examples

This simple scalping strategy can be used with the smallest time-frame as well as daily, weekly or even monthly time-frame. Although the term *forex scalping* is referring to the smallest price movements, it works on higher time-frames as well. You trade no more than one candlestick. Enter on the open and exit on the close. The next examples show you not only trend reversal signals, but the Lucky Spike concept helps you to identify when the correction is over and the main trend is going to recover.

On lower time-frames, there is a lot of fun with Lucky Spikes:



Lucky Spikes work on higher time-frames as well. Look how we predicted important price movements on EUR/USD, Daily.





We trade commodities too. Lucky Spikes on CRUDE OIL, Weekly:





As you can see, it's all about patience and waiting for high probability trading signals. The less often you trade, the more consistent profits you make!

Chapter V: Candlesticks as a part of your own strategy

You can use candlestick patterns as an entry trigger with your own strategy that you already trade. First, let's talk about one very important thing.

Leading versus lagging indicators.

- **Leading indicators** are indicators that can be used to predict market movements. They show you what is the market doing **now** or just a moment ago.
Examples: fundamental news, candlesticks.
- **Lagging indicators** are derived from price and show the history. They show you what the market did **in the past**.
Examples: moving averages.

Many losing traders are trying to use lagging indicators as entry triggers. Successful traders have an edge because they use leading indicators, so they can jump aboard the new trend sooner. Let's give a clear example.



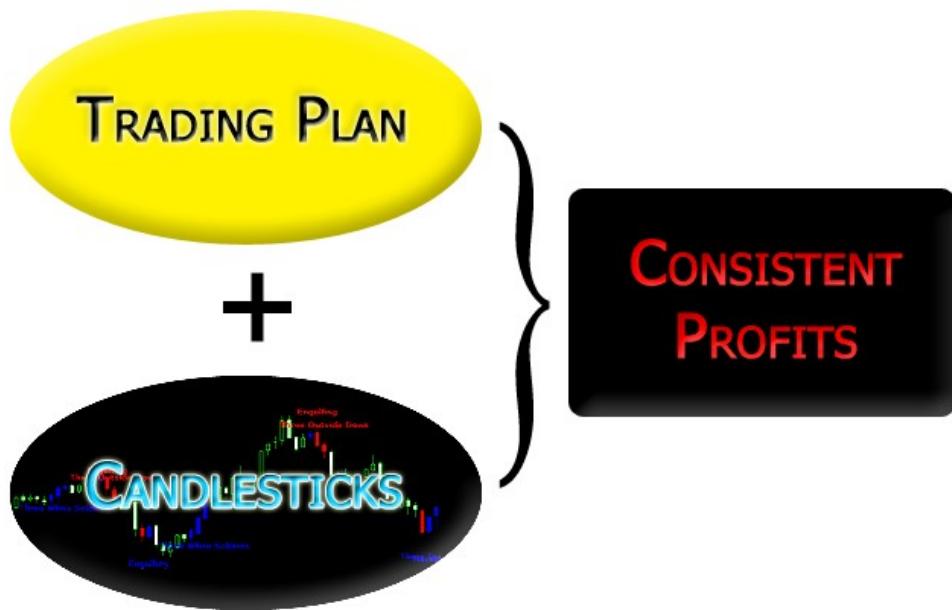
We have placed the following indicators in the chart:

- Simple Moving Average with period 20 (red);
- Simple Moving Average with period 5 (blue);
- Candlestick Pattern Recognizer.

We see that moving average crossover is not the best entry signal.

We have recognized a bullish *Harami* pattern before (and *Lucky Spike* of course!). This creates our buy signal. We went long with a very tight Stop Loss before the mass. This is a great advantage of candlesticks. Quick entry and tight Stop Loss compared to big profit potential.

Now the tricky part. It is best to use candlesticks to improve an already developed trading plan. Professional traders prefer to use their own basic trading plan and then add candlestick patterns as confirmation. Profitable trading strategies are based on technical analysis mixed with candlestick patterns to produce consistent profits.



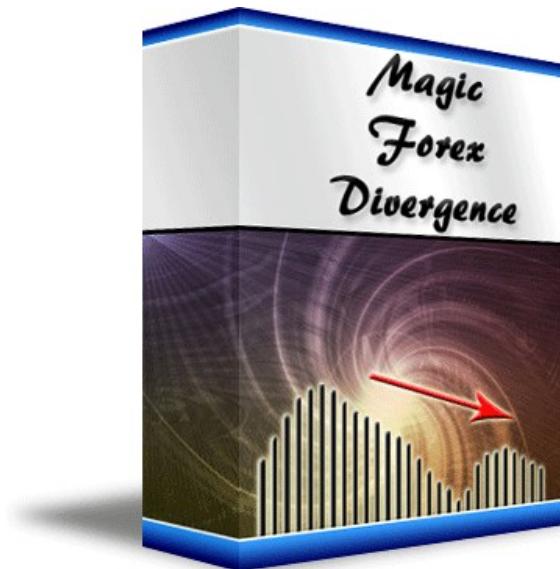
You can find trading plans with different approaches in the [Forex Candlestick Tactics](#) book.

Chapter VI: What's next...

You can start using candlestick patterns right now. Try it, experiment with it, master it. We recommend you to add a strong weapon to your trading arsenal, the powerful tool used by professional traders and the most profitable price pattern ever found:

The Divergence Pattern

Understand how the long-term trend ends and how to recognize the new trend.



If you haven't downloaded the Magic Forex Divergence,
get a free copy here:

www.forexmystery.com/magic-forex-books