

“Learning and Remembering the Signals – Fast and Easy”

The Candlestick Forum E- Book Series

**For Teaching Investors High Probability
Investment Methods**

Candlestick Forum LLC Copyrighted Information – January 12, 2002

All rights reserved

Introduction

Learning the Candlestick patterns has been the biggest deterrent for the method to be widely used in the United States. It has had the stigma of being a hard-to-learn program, especially trying to memorize all the signal patterns. That may have been true until recently. The advent of the computer has made the learning process very simple. Plus, experienced tutors are now becoming more available. The lack of proper understanding of how the signals operated has led to many misconceptions about the signals' accuracy. Like any other process, the effectiveness of that process is directly attributable to how well it is put into place.

Because there has not been a forum, until now, to be able to learn the signals correctly, the majority of investors who have attempted Candlesticks find themselves having more questions than when they started. Learn how to interpret the signals correctly and you will be amazed at the accuracy of your results. Successful Candlestick analysis inherently enhances your investment perceptions. These perceptions will give you a whole new perspective, forever giving you an analytical edge. The very simple techniques demonstrated in this book will appear to be overly simple. The straightforward method for learning and remembering the signals will save you hours and hours of non-productive mind-cramming exercises. Put your efforts to better use. The uncomplicated methods used to remember the signals are incorporated throughout the Japanese Candlestick reasoning.

Keep in mind that the signals were not developed using highly sophisticated charting material. Hundreds of years ago, charts were scratched out on rice paper. Until the last few Candlestick books, it was not uncommon to have part of the text explaining how to build backlit boxes for better chart viewing. Computers have made searching and viewing Candlestick formations an easy process. The learning curve has been dropped to a matter of days, if not hours. The development of excellent "search" programs provides an invaluable service. Candlesticks can be learned and found in a very rapid process.

Fortunately, the same human emotions that the signals exploit, FEAR and GREED, act as the best learning catalyst. "Learning the signals" has been one of the major reasons that investors have not taken advantage of Candlesticks. It has been thought that understanding and remembering each signal was too much of a task. In addition, until now, there has been very few places or people to confer with to verify whether one is understanding and learning the signals correctly. www.candlestickforum.com, the leading Candlestick education website on the Internet, provides the Candlestick student a place to refer to when trying to master this trading technique.

Take advantage of years of trial and error. We'll stretch your mind. Cash in on the time saving techniques that you will learn here. Do you sincerely want to grow your investment wealth into the millions? Turn your time and knowledge into wealth. You know that the professional investors extract money from the investment markets consistently. Having the Candlestick analytical skills in your arsenal gives you a dramatic competitive edge. Become your own self-master of investments.

Common Sense Practices

Following the basic premise of the Candlestick system, **common sense**, some of the processes for learning different signals become very simple. It was my GREED to maximize profits that led me to a basic learning process. Where is the best place to buy? At the bottom, of course! Where is the best place to sell? Obviously at the top! When I was trying to learn the signals, that was the extent of my thought process. IF THE SIGNALS ARE EFFECTIVE, THEN THEY SHOULD BE EASILY SEEN AT THE TURNS. This may sound very elementary, but it is the most effective method for remembering the signals.

The desire to be in a position at the lowest point and selling at the highest point produced a very quick method for identifying the signals.

Step one is easy. On your computer, go to a Candlestick chart. Most software services provide them as an option along with Bar Charts and Line Charts. If you do not have an investment information provider, there are free charting services. www.bigcharts.com is a good chart provider. Most on-line brokerage firms have some sort of access to charts. Most charting services will be end-of-the-day results.

End-of-the-day results will encompass 80% of the needs of most investment situations. Live charts are beneficial for many trade implementations, but not required in the function of learning the signals.

Once you have pulled up the Candlestick charts, most charting services allow you to customize indicators. The most useful and revealing confirming indicator is Stochastics. Stochastics is a parameter that can be set to the sensitivity required. However, setting the sensitivity to a too sensitive level results in garbled information. The common input for overall best results is to set stochastics to 14, 5, 5. Or 12, 3, 3 for the swing trader, two to five day holds.

The purpose for the stochastics settings is to have a reasonably good indicator as to when a stock is overbought or oversold. Using stochastics, on their own, is a reasonably good valuation for detecting when a trend change may occur. As far as finding the best Candlestick reversal signals, stochastics act as a guide. Start

looking for the “buy” signals when stochastics show oversold characteristics and look for the “sell” signals when stochastics show overbought indications.

The learning process becomes as easy as visually studying the charts. Look at the bottom reversal points. Is there a signal there? If some formations look familiar, leaf back through the “signals” section to see if you can locate them. Also take notice of the location of the stochastics. You will find that a vast majority of the reversal signals occur when the stochastics are in the oversold or overbought area.

A major deterrent for most investors has been the number of signals that have to be learned. Fortunately, the number of signals required for successful investing is small. Of the thirty or forty Candlestick signals, approximately six to ten of them will be more than you will need. These signals provide more than enough supply of excellent “buy” or “sell” positions each day.

The major signals that you will most often witness are:

The Doji

The Hammer and Hanging Man

The Shooting Star

The Bullish Engulfing pattern

The Bearish Engulfing pattern

The Dark Cloud Cover

The Piercing Line

The Harami

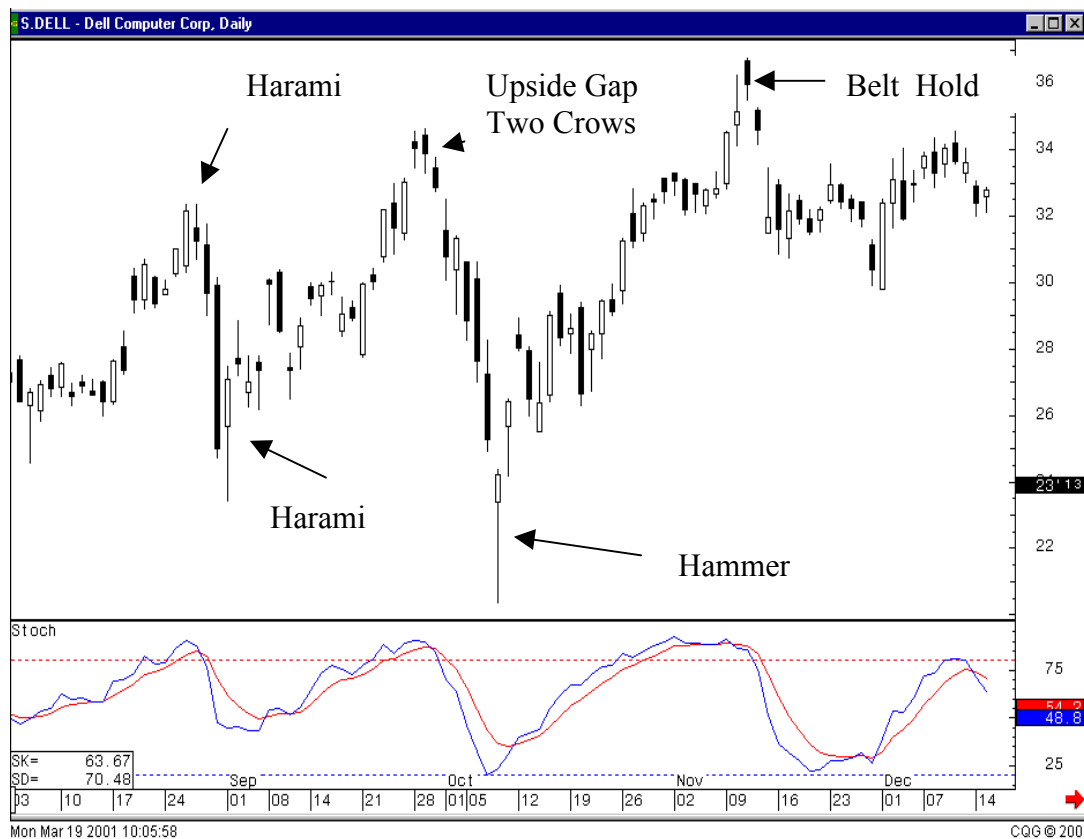
The Kicker Signal

These signals will probably provide more than 75% of all the reversal situations. They are also the **obvious** Candlestick signals. Obvious in the sense that they visually depict a change in direction. The Engulfing patterns have a different colored body that stands out against the color of the current trend. The same can be said for the Dark Cloud Cover and the Piercing Line.

The Doji is unique in itself. A cross, with shadows as its predominant feature. The Hammers, Hanging Man, and Shooting Star have long shadows that make them stand out. Anytime a long shadow or shadows appear, they should get the investor's attention.

To get clear visual descriptions and interpretations of the signals, refer to my main book "Profitable Candlestick Trading" or The Candlestick Forum's E-Books, "The Major Candlestick Signals" and "The Secondary and Continuation Signals." Having this reference material on hand is important when learning the signals. Being able to refer back to the material when first studying where and when the signals may occur is vital. You want to be able to quickly identify signals that you anticipate should or could be pertinent signals when going through past charts.

Figure 1



(Dell Corp. trades in conjunction with the stochastics)

Not all stocks have good chart patterns. A good chart pattern will correspond with the peaks and bottoms of the stochastic cycles. Notice the easy-to-see oscillations in the Dell chart. There will be good charts to trade using the Candlestick signals. Dell is one (Figure 1). If you run through the chart history of Dell's stock

movement, it will be easy to see the reversal signals. Most of the signals will coordinate with the stochastics at the bottoms and the tops.

This will create two important learning results. First, you will quickly remember what signals appeared at points that you would have liked to buy. If your purpose for reading this book is to make money, then remembering those signals should become an automatic process. It is much easier to remember what occurs at a bottom or a top when it results in money in your pocket. Secondly, witnessing a buy signal, occurring at a bottom, when the stochastics clearly indicate that the stock was oversold, will dramatically start changing your investment psychology. Why buy a stock when all the stars do not line up?

You will find that there is an inordinate amount of Japanese Candlestick signals that can be identified at the very tops and the very bottoms. Once you are set up with a chart service, whether online or a subscription service, start going through the history of chart movements of stocks that you are familiar with or the heavily traded stocks that you constantly hear about: IBM, Microsoft, Ford, GM, etc.

As you review their charts, identify any signals you think are appearing at the reversal points. It will take just a matter of minutes to start recognizing the major signals. Upon seeing the Hammer, with its distinctive long tail to the downside, you will begin to recall it easily after seeing it act as the reversal point a few times. The same with the other major signals. The more you see them, the more they will become ingrained in your memory. Envision committing funds at the time these signals appeared. How much of a profit would you have made before the next “sell” signal appeared?

The majority of the time the signal will appear at the very bottom. However, as explained in my book “ Profitable Candlestick Trading”, not all trends reverse on a dime. Sometimes the momentum of that trend has enough power built up in it that it takes a couple of signals to instigate the reversal. The Double Bottom formation is the prime example of this phenomenon. This produces an excellent method for the Candlestick investor to load up on profitable trades. Being able to witness a Double Bottom, identifying buying after a long down trend, watching the short term bounce, a pullback, then another strong buy signal provides a high profit, low risk investment.

Because of the limited number of major signals, learning how to recognize them is minimized time-wise. Being able to recognize those alone will be more than most investors will need to have many profitable trades each day. But in analyzing the charts, the investor will see many secondary signals appearing at the tops and bottoms. Use this experience to at least familiarize yourself with the other signals. The same process, seeing a reversal that “might” have a possible

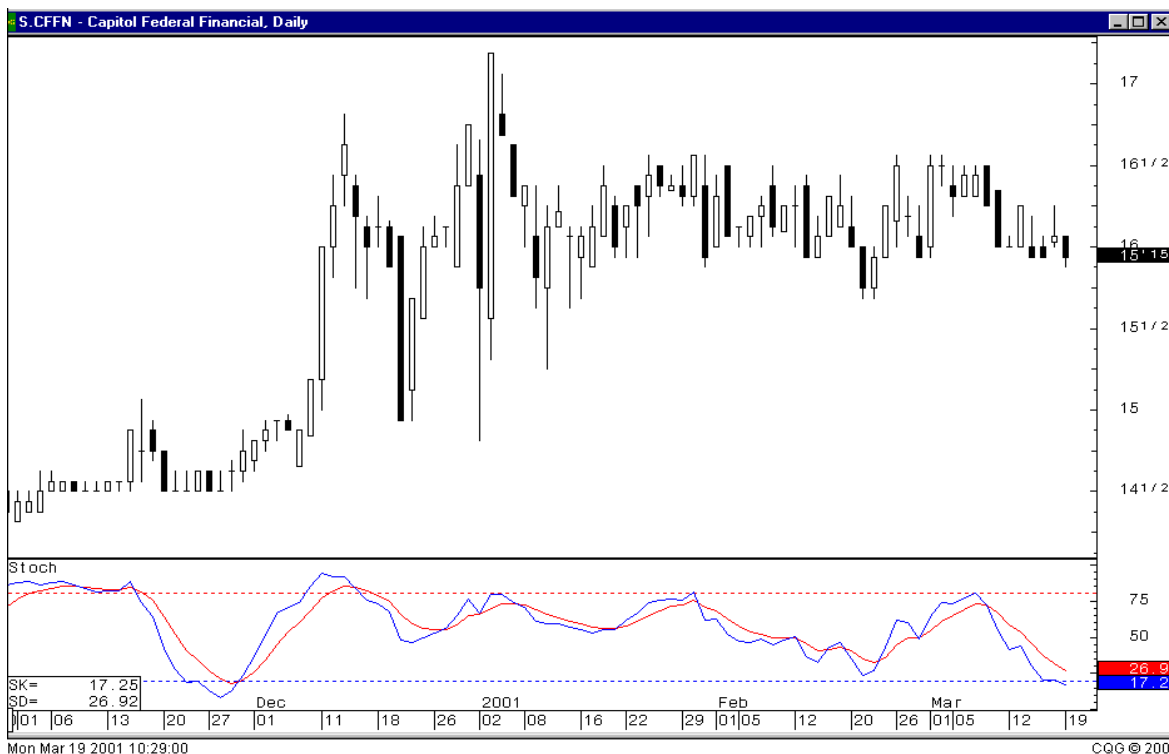
signal, can be confirmed or non-confirmed by leafing through the signal sections of our publications.

The secondary and continuation signals can be learned at a less aggressive pace. They will not occur as often. However, when they occur, four hundred years of statistical study has verified that they will probably produce a change of direction. The learning process remains the same. Simply identify what happened at the reversal point. Is it a signal? And what was the status of the stochastics?

To reiterate, you will discover that the Candlestick signals will be observed an inordinate percentage of the time at the reversal points. But there will be some qualifications. Not all stocks or trading entities will have clear trading patterns. Some are just “junky” traders. Leave them alone. There are thousands of stocks, commodities and futures that work extremely well in providing good Candlestick signals.

As seen in the Capital Federal Financial chart, Figure 2, there is absolutely no reason to be trading this stock. All stocks, no matter how volatile, will go through dead periods. If a chart starts going flat, leave it alone for a while. There will be plenty of other places to put funds.

Figure 2



(CFFN – not a trading chart)

If you come across a chart that is hard to evaluate, skip it. There are 10,000 stocks to trade. You will have more excellent signals than you can handle. Go find those stocks and eliminate the sloppy trading stocks.

As you study the charts, the stocks that have easy-to-read reversal signals will become evident. Put those stocks on a list somewhere. Some investors may utilize the Candlestick signals to trade a limited number of stocks, going long or short, at well defined signal reversals. This style of trading eliminates the extra few minutes each day doing searches for new buy or sell positions. Becoming well versed in the trading habits of a few select positions has its advantages. Support and resistance levels are better identified. Correlating Candlestick formations with these levels produces an extremely high prospect of profiting from pinpointing the reversals. The positions can be exploited both ways, bullish moves and bearish moves.

Whether looking for short-term trades or long term positions, the charts will demonstrate signals on different time periods - daily, weekly or monthly. You will be pleasantly surprised how quickly you will recognize and remember the important signals. Learning the signals can take as little as a couple of hours. A couple of hours reviewing past reversal points on your charts will act as an excellent way to retain the signal's formations. That forceful emotion, GREED, will produce the impetus for retaining the signal images. The process of remembering the signals is now driven from the desire of producing profits, not a mechanical exercise. Wanting to remember what will make money produces a strong motivational factor.

The visual identification is the most important aspect of learning the signals. Knowing the name of the signal or the psychology of why the formation works is not a necessity for using the signals profitably. However, eventually knowing the name and becoming more knowledgeable about the psychology behind the formations will give the investor more confidence. It aids in the evaluation of whether a trade is in trouble or not, after you have put a trade on.

Search Programs

Using search programs has two major functions. First, it allows the investor to dissect the formations. This dissection process is a function of formulating the search parameters. It will implant the elements of each signal firmly into your mind. There are a number of excellent search software service companies; TC2000, Telescan, Trade Station 2000, just to name a few. All have excellent search capabilities.

The best one found for providing an easy-to-use format, at a very reasonable monthly fee, is TC2000. It doesn't bog down your system. And it is easy to

format for customizing Candlestick searches. It allows you to download all ten thousand or so trading symbols. From that list, the best buy or sell formations can be cultivated in a matter of minutes. Additionally, TC2000 has dozens of pre-formulated technical processes already built into its program. This permits the investor to tweak the searches for optimal trades by utilizing the best combinations of technical parameters. TC2000 makes finding those eight or ten, highest-profit probability trades amazingly fast, once the search parameters are in place. Spending an hour formatting the signals, the ones most likely to produce the best profits, (the major signals) is the best procedure for learning the signals.

Putting a signal's pattern formation into formula descriptions creates the best method for mentally understanding each signal. TC2000's customizing process is very simple to use. It can be set up to search the total universe of stocks or customized to search specific industries or sectors. It can eliminate all the small capitalization stocks or all the large capitalization stocks, depending upon your personal preferences.

The following is a method that has been most effective for searches, looking for the best possible trades available; no industry preferences, no sector preferences. There are stocks that do not fit basic parameters. Those basic parameters can be established for all searches.

First, liquidity needs to be addressed, to be able to get in and out of trades. A small account might build in the parameter that the daily average volume is greater than 200,000 shares per day.

Volume > 200,000 per day.

A larger account or an institutional account will probably eliminate all stocks that have less than a certain number of shares, for instance, 500,000 shares or 1 million shares per day. This will allow them to be able to get into or out of a stock position with affecting the price radically.

The next parameter is the price range that is in one's comfort zone. Because most brokerage firms do not margin against stocks trading less than \$5.00 per share, make that a minimum parameter. Other traders make excellent profits trading stocks in the \$2.00 to \$5.00 range. They would set their parameters lower. Yet other traders are more comfortable trading stocks in the \$20 to \$70 price range. The parameters can be set to each investor's preference.

Price > \$5.00

On the other hand, if you know you will rarely buy stocks greater than \$150.00 per share, why bother evaluating those charts? Put on a maximum price parameter.

Price < \$150

Once these basic parameters are put into the search function, you have reduced your universe of potentials down to approximately 3,600 stocks. Next, the search is oriented towards looking for longs or shorts. TC2000 makes it very simple to segregate those stocks. If looking for potential long positions, a customized stochastics parameter is added. The TC2000 search program permits you to add or eliminate stocks by the level of the stochastics. In the case of searching for long positions, the search would be limited to all stocks that do not have stochastics below 20 that day. If I wanted to get more specific, it could be set up as stochastics below 20 **AND** heading up. For the purposes of most searches, that extra tweak is not required.

Implanting the Signals in Your Memory

The exercise that will ingrain the signals into your memory is the next step. It is simple. Describe each signal in formula terms. Going through the process of creating the formula for each signal is easy. The actual process of creating the formulas will make the development of each signal very clear. It is a simple process. For example, the Bullish Engulfing pattern, how is it formed?

First, the open of today is below the close of the previous day. That formula would set up as:

$$O < C1$$

AND

the close of today is greater than the open of yesterday.

$$C > O1$$

That is easy. Once you have done this simple process, visualizing a Bullish Engulfing pattern should be clear from now on. It is now in your search program. You can name it “Bullish Engulfing patterns”. To further enhance the search criteria, you would add the stochastics parameter. Finding all Bullish Engulfing signals that occur in stocks where the stochastics are below the 20 level. Every time that you update the data, (depending upon the speed of your computer, it will take from one minute to three minutes), the scan list will show you how many stocks showed up in that particular search.

All the signals can be dissected this way. The Shooting Star would have the opposite parameters. Stochastics would be set to find stocks with the stochastics over 80. The open and the close are within the lower 33% of the daily trading

range. This would make the upper shadow twice the size of the body. Obviously, it will not take more than a couple of times to pull up the Shooting Star search results to recognize a Shooting Star. The same can be done with all the signals.

Time and effort? With the simplicity of TC2000's system, it should not take any longer than fifteen minutes, at most, to formulate each signal. In two and a half hours you will have a search program that will spit out all the major signals every day. At that point, your job will be to evaluate the best of the best signals.

Hands – On Experience

Until recently, learning the signals and how to use them effectively was a lonely affair. There were no mentors to confirm or deny evaluations you made on a signal. The only way to learn was to watch a position's move after you did an evaluation. This was often not gratifying if your selection was correct and you watched potential profits slipping through your fingers. Or the contrary, thinking you found the perfect trade, you put money on the line but found out that you overlooked one little aspect. This aspect probably could have been averted by an experienced set of eyes.

Participating in the Candlestick Forum's Stock Picks of the Day can act as a major education product. On top of demonstrating high probability transactions, it provides daily exposure to successful trades. The trades will be initiated by a signal. You gain the experience of seeing how that signal was recognized, how other parameters were considered to make that pick the best of the total universe of stocks. This constant process will eventually give you a library of successful trades/signals to use for your future investing.

More importantly, the Stock Picks of the Day service also includes free access to the staff of The Candlestick Forum. Any questions or clarification of what signal/parameter combinations make for successful trades is at your fingertips. The soon to be established chat room will create a forum to cultivate your thinking. Other investors, in the same status of learning, will be able to talk signals until you have clearly in your mind what every signal looks like. Finally, whenever you have a specific question about a specific formation, where all your reading does not fully explain what you need to know, participating in the Stock Picks of the Day provides one more vital service. Talking directly to us, The Candlestick Forum. If you can't find the answer, ASK!!! We are here to educate those who want to master the Candlestick method.

Summary of Steps

1. Study past charts, find signals at the oversold and overbought area of the stochastics.

2. Formulate the search parameters for software search services. Knowing the specifics for creating a search format will engrain in your mind what the signal looks like forever.
3. Use the Candlestick Forum's assets. Watch the Stock Picks of the Day to see how and why the signals performed. Ask questions: on the chat room or to The Candlestick Forum Staff directly.

Conclusion

Learning the signals is easier than what the public's perception has been in the recent past. The number of important signals, or the signals that are most often observed, is less than ten. The remaining signals should be studied, but the time spent on them is a function of keeping them in the back of your mind. When one of the other signals appears, you want to be able to recognize that it might be a signal. After a few times identifying and verifying a signal (reviewing the signal pages) the formation will remain with you. Today's computer charting services make analyzing past charts an easy exercise. Recognizing the Candlestick signals at the reversal points of past price movements reinforces the memorization of the signals as well as confirming to the investor the frequency that the signals occur. Not being familiar with what the signals mean is the major reason for such a large percentage of investors not taking advantage of them.

The motivation of making profits will be a best stimulus for the learning process. Do not let the task of becoming educated on the signals be a deterrent. For the very few hours required to become acclimated to their identification, the profits developed from their use will be expeditiously massive.

Profits are made easier when identifying Candlestick signals in a common pattern. Wouldn't you like to be able to prepare for the next potential trade set-up? Knowing approximately when a Candlestick signal should be appearing, due to a common technical formation developing, multiplies your investment opportunities. Powerful investment fund allocation strategies can be properly scheduled. Trade implementation can be optimized. Your entry and exit decision processes will be reinforced when recognizing successful formations. Being able to perceive profitable trades, with proven results, expedites your usage of timely trading strategies.

See our other Candlestick Forum E-Books:

“ The Amazing Hidden Powers of Japanese Candlesticks”

Finding and Learning Signals

“ The Major Reversal Signals”

“ The Secondary and Continuation Patterns”

and be sure to frequent our website: <http://www.candlestickforum.com>