

## TRANSCRIPT

# Identifying Chart Patterns

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**ANDREW MCGOWIN:** All right, welcome back, everyone, for now part three of our technical analysis beginner's classroom. Once again, my name is Andrew McGowin, part of the Trading Strategy Desk here at Fidelity. You can find us, as always, at [Fidelity.com/coaching](https://www.fidelity.com/coaching). We are a group of about a dozen or so traders specifically dedicated for your education around a broad variety of topics, especially technical analysis. So welcome back, as mentioned, to now part three.

We will be taking a look at, what some may say, the more fun part of technical analysis, drawing chart patterns, maybe at least the more subjective part of technical analysis, what we've discussed previously with respect to, say, indicators and things to that extent. That tends to be more of the scientific side of technical analysis. This is maybe more the artistic side of things, taking a look at the perspectives of chart patterns and what that looks like on the charts themselves. So we'll be discussing a few different things here today.

First and foremost, we will start with understanding patterns and their limits. Next, we will take a look at techniques for trading those patterns and then, as well, construction of common chart patterns. Before we dive into the slide deck, though, I want to introduce my co-host for this session in particular. James Savage joining me one more time. How's your day going so far there, James?

**JAMES SAVAGE:** Hey, Andrew, going well here, happy to continue the journey in technical analysis. And I like how you mentioned this is more so the art side of TA, where, in the prior session, it certainly was science, right? We spent a lot of time with mathematical calculations going over those indicators. But in this event, we finally get the opportunity to maybe put some of the subjectivity of technical analysis to work. So I'm excited to get started with this.

**ANDREW MCGOWIN:** Absolutely. As mentioned, understanding patterns in their limits, first and foremost the thing that we are going to discuss here today. So when we are looking at the world of chart patterns, what ultimately is a pattern? How do we define a pattern? A pattern itself is something on a chart bounded by at least two trend lines. So that can be a straight trend line, horizontal. That can be a curvature trend line, like a moving average like we discussed in the last session, but some sort of trend line that is bounding this ultimate pattern that we are looking at.

And then, from there, it is a combination of entry and exit points. When we are discussing these patterns later, it is imperative that we remember that the breakout itself is the originating perspective of the pattern. That is when the pattern has completed, and then we're looking for the resolution of that pattern. It is natural, a lot of the times, one, for a trader to sometimes front run patterns, thinking that we're seeing something that is fitting

into our outlook, and then, two, making sure that we understand what the type of pattern that it is.

Is it a continuation pattern? Is it a reversal pattern? That is going to help inform what type of trade that we may put on if given the choice there. And again, always remembering, this is part of the grand scheme of decision making factors. Just because something happened does not mean that the resolution must then happen. It is a market. It is traders all making decisions on a variety of different perspectives. And we'd look at it from a variety of different time frames. That fractal word we mentioned in the first two sessions, still important.

These patterns can be found on a multitude of different time frames. The issue, though, that we always have to keep in mind, we are humans. When we are looking at these chart patterns, when we are looking at the different types of technical considerations that are out there, we have to make sure that we remember that it is natural for us to sometimes look for things out there in the markets and, for lack of anything else, anything out there, from the lens of bias.

We are naturally, as humans, inclined to be biased. We are naturally, as humans, to sometimes look for patterns where they may not exist. If we think about different patterns that we observe in real life, sometimes our own thought processes inform those decisions. So we have to try to remain as objective as we can when we are looking at these chart patterns. And again, just remember that nothing by any means is any sort of guarantee in the markets. Just because these patterns are taking place does not mean that now the price has to go up or has to go down.

Generally speaking, when we are trading from a technical perspective, what we're trying to do is shift those probabilities slightly better in our favor. If the thought process generally is that a stock has a 50/50 chance of going up and down, could we shift those probabilities to be slightly better in our favor? And does that help inform that next decision that we are making? From there, too, something that we as traders are very susceptible to is what's called market law, just the thought process that certain things have to happen in a certain way at certain times of the year or if given certain parameters.

And we have to remember that the market, in its infinite wisdom, can still do whatever the market ultimately wants to do. It is a clashing of decisions at all moments in time. Buyers and sellers are interacting. And they are doing so and voting with their dollars accordingly. So, keeping in mind too, it is always a historical perspective. Everything in the world of technical analysis is looking at historical price action.

We assume, to some degree, that what has happened in the past has a relation to what could happen in the future. But it's that old quote of sorts that history does not always repeat itself, but it tends to rhyme. We're looking for scenarios where something may have happened in the past that hopefully we can learn from and utilize going forward. But also, what is a natural bias that we run into from time to time that, not only informs our own bias, but actually informs some of these chart patterns, that we will take a look at Is price-having memory.

So much of what drives these levels that we will take a look at, support and resistance like we've looked at previously, it's because price has memory. Traders remember where they bought things at, where they sold things at. And they make decisions accordingly. There's a psychological component to a lot of what we will discuss today. That being said, there are some techniques, though, that we want to make sure that we understand before we dive deeper into the patterns themselves. So I'll bring my colleague James back in. If you don't mind, James taking a look at some of those techniques.

**JAMES SAVAGE:** Of course, because what's the point of knowing all of these patterns if we don't know how to trade them? So we want to go over a few of these terms and concepts because they're going to be crucial for you to take advantage of your understanding of a pattern. And these are going to be breakouts, entry stops, protective stops, and retracements.

So one of, I guess we'll say the assumptions that Andrew was talking, one of the basics of pattern analysis is waiting for the pattern to get formed. And that is oftentimes relying on the breakout to occur. And that is the violation of a particular trendline, support or resistance line, or any prior reversal point that is part of that pattern, part of the construction of that pattern.

And what this does is it signifies a change in the buyer and seller behavior, that bullish and bearish dynamic. And this can be a signal for possibly the beginning or an end of a prior trend. Now, in our example here, we have a horizontal resistance line where price first reaches it and then reverse. So we can see at that time the sellers overpowered the buyers, if you will.

But upon the second attempt to maybe become resisted by that same line, well, what did price do? It continued to move through it. And that is what we call the breakout. So that breakout is the key concept. That is going to be when oftentimes the pattern is considered actionable. Now, all because that breakout occurs, we oftentimes need to find some way to confirm to ourselves that this breakout has now become a valid entry signal for us or exit signal for that matter.

And there are a few types of filters we can use. Now, this isn't an all-inclusive list. We're trying to just go over some of the most common, most popular categories. But it's going to be left up to you to determine just which one is more appropriate for your own trading style. So there is what's called the intrabar type of filter. And that is oftentimes one of the soonest, the earliest ways to take advantage of a breakout.

That would be the intraday, oftentimes, movement of price through this support or resistance line. So think of a price at a point. And in the morning, maybe we're still being held under the resistance. And throughout the day, by the end of the day, we've already broken through that resistance in that prior example. That's considered an intrabar type of breakout.

Now, there are the approach of waiting for multiple closes. So again, thinking back to that example, imagine we're stuck under resistance, and we close above it on one day. And then we wait, maybe, another close and possibly another close. So that could be an idea of waiting for, say, three closes outside of that prior area of support or resistance to tell ourselves, OK, this breakout is, in fact, a valid trading signal form.

Now, you could also think of that as time, maybe in intraday trader or a day trader, if you will, could say, I want to see that resistance line broken and remain broken for at least five minutes or 10 minutes. So that is that time perspective. There is the percentage point or a certain dollar amount above that I think is very common.

If we go back to that example of resistance, say it was \$100, and the trader is thinking to themselves, well, if we can get \$5 above that or 5% above it, or maybe 5 points above it, whatever makes more sense in your own trading plan, that's going to be the signal for you to get in. Now, we're going to talk about why it's important to have a type of confirmation filter later on because, all because there's a breakout, that doesn't mean that it's going to go in that new direction.

So let's talk about, maybe, a few of those confirmation filters in the next concept that we wanted to talk about. And that is the idea of entry stops. And this is somewhat of an idea that goes, maybe, contrary to the popular way of thinking for investors out there, where we want to buy low and sell high. I'm sure many of you have heard of that term. It's almost investing 101. Buy low, sell high, that's how you profit.

Well, an entry stop is a technique to enter the trade after a breakout. So you'll use whatever confirmation filter that you find appropriate for you. And you will be, in the example that we're showing here of a bullish breakout, so move where it's going higher through one of those different trend lines here. We've got an example of a resistance breakout, which is horizontal, and a trendline breakout, which was drawn diagonally.

They're both breakouts. So we can view them as almost one event here. And the entry stop would be the buy-stop order to get you in at that high point. And if you're thinking to yourself, well, James, why would I want to buy at the high? That doesn't make sense. You're telling me I'm going to be buying at the highest price at the time on the chart? Why would anyone do that?

Well, that goes back to an important idea with technical analysis in that we want to buy high and sell higher. Sometimes that is going to be the approach. And that is one of the basic concepts that we discussed earlier of trend trading. It's not trying to pick and time those bottoms, but waiting for these bullish trends to occur, in today's example, waiting for the breakout to occur before we get into that trade.

Now, in this example, we can see a few different candlesticks here. So imagine, when it first broke through that line, either the resistance or the trend line, when would you get in? When would be the right time? Would it be that first candle, that intrabar piercing of resistance?

Maybe. Would you want to wait until we get one close? Possibly. What about two closes above it? We can see dollar value here. It looks like it broke out around 49.

Do we want to wait until it's \$2 above that or \$3 above that? That's going to be up to you. That is, again, going back to that personal approach that you want to add here. And it's oftentimes a balance. There's no right or wrong way to do it. We can imagine the trader that might try to get in sooner, in this example, might be rewarded. Why? Because we can see in hindsight that the trend continued to move upward after that breakout.

Other traders might say, no, I want to wait. I want to see what happens after the breakout, just to ensure that the breakout does continue in that direction. And the reason is because not all breakouts have to go our way. There is this idea of both a false and failed breakout. And you can almost think it's self-explanatory in the name. The false breakout is when price breaks but almost immediately falls back through that breakout price.

The failed breakout, we can also refer to this as a bit of a trap, is when the breakout occurs. But price not only breaks back into the prior range but then moves into the opposite directions, breaks out in the way that we initially didn't think was going to take place. So what I love about this example here is that we have both a false and a failed breakout all in one. There was a definable resistance line. Price breaks out to the upside.

And how many candles did we see above that line? Well, 1, 2, 3, 4 candles where we closed above the breakout. So this is again going back into that confirmation filter. If a trader were saying, hey, as long as we get one candle closing above it, I'm in. Great. They would've gotten in. And in hindsight, they would've likely closed the position because it became a false breakout.

But what if someone was saying to themselves, I need to see price remain above this line for at least five closing periods? Did they get in? They did not. They avoided getting, I guess we could say, allured in to this false breakout. So I think this is a great example of that balance, that seesaw that you need to weigh within your decision making process.

Do you want to get in earlier with the potential of a better price, but more apt to be a victim of a false or failed breakout? Or do you want to wait for a little more validity, wait for a little more time? You might not get in as great or as advantageous of a price should it continue to go in the direction you're hoping for. But you could possibly minimize the type of false or failed breakouts that occur.

Now, we've talked about the confirmation filters, the entry stops, the idea of a false and failed breakout. Those are oftentimes what we're going to be thinking of getting in the entry stop. But if you've ever heard of stops before, you're probably thinking of the more common version. And that is the protective stop. So traders could use the entry stop to get in, possibly when a breakout is occurring, and then use, once that entry order has executed and they've been filled, a protective stop to possibly get out of a trade should it start going in the opposite direction that you were hoping to go.

So here we have an example here where there was a breakout that occurred. And we can see in hindsight that the breakout had a bit of a nice run on it. But a protective stop is that stop-loss order that you might've heard before. And that's where you are setting in order to get you out of the position, should it move against that way that you were intending it, because this idea of, well, if it starts going against me, I'm just going to hold on to it because I'll just wait for things to get better, well, that's not always the case.

Oftentimes, when we see these breakouts, if that trend continues and you don't have a way to get out of the trade, you could be left holding on to a position as it continues to take further and further losses in. We can see that in, unfortunately, not the greatest, I guess we could say, bullish trade in our next slide here. And that is we're getting to see both a false and failed breakout again, and why having some type of protective stop could have helped a trader from taking on significant losses.

In this chart pattern that we're going to be talking about later on in the session today, we can see price breaks out above initially. We had one candle close above, two candle closes above it. That third candle, not only did it fall back into the prior range, but broke out to the downside. So what was looking promising is a bullish breakout upward turned into a bearish breakout to the downside.

So if a trader had got in and didn't create some type of, maybe, exit plan, whether you want to use a stop loss or your own disciplined approach to, say, I'm going to get out if it falls back beneath that prior breakout price, the key is to have some type of plan in place to protect yourself should losses start to substantialize. As a retail trader, our primary objective isn't just always trying to make profits. It's capital preservation. And having an exit plan should be one of the first things that you think of before you even get in to the trade.

Now, before we go forward, there's an interesting-- I don't want to call it a phenomenon because it makes it seem like it's a rare event. But it's something that happens quite a bit. And it could even be used as a confirmation filter. Do you notice how, when price experienced that downward breakout, it rallied back up to that trend line and reversed? It almost looked like it was going to reverse yet again.

But what did it end up doing? It just turned around and continued moving downward. And that concept of price returning to a prior resistance or support level is referred to as retracements. We can become a little more granular with our definition by calling it a pullback or a throwback, depending on whether it's a breakout down or breakout up.

But this is somewhat common of an event. And we talked about this quite a bit when we were going over support and resistance earlier. Thinking back to that idea, when support becomes resistance and when resistance becomes support, well, these are our retracements. So we can even use this as a possible confirmation filter. So what do I mean by that? Well, looking at our example, we saw breakout to the downside, a trendline breakout.

Now, a trader might've decided to take a bearish trade, possibly shorting a stock, maybe even moving to some type of bearish options trade. And again, going back to that

confirmation filter, at what point do you feel confident in entering that bearish trade? Would it wait for an intrabar piercing, maybe one close, two close, a certain dollar amount below, or possibly a retracement?

And that would be an individual waiting for price to try to go through, in this case, a pullback, test, retest that prior level of support, and ensure that it is turned into resistance. And that can be a confirmation filter, where someone could say, now I feel comfortable getting into my bearish trade. So this is somewhat bringing back the concepts that we went over in support and resistance.

Now, this is, of all the examples that we covered today among the confirmation filters of intrabar, multiple closes, time, percentage points, or money, this can be sometimes one of the slowest examples out there. But of course, as we discussed, that also has the benefit of possibly providing a little more validity than some of the other examples that we covered. So keep these techniques in mind as we talk about, and maybe as you're visualizing entering and trading in some of these patterns that we're going to be discussing.

So, Andrew, with that being said, now that, I think, we've had a good, solid foundation on the basics, the definitions, the assumptions of patterns, some techniques to trade them, why don't we talk about some of the most common chart patterns?

**ANDREW MCGOWIN:** Absolutely. And when I think about a lot of the topics you were discussing, it's natural for a lot of people out there to think, all right, well, if this breakout happens and it doesn't go higher, this failed breakout, what's the point? What's the point of these breakouts if it's going to have a potential for a failed breakout? And the fun thing about what technical analysis ultimately is is that is still useful information for us. I know it is so natural for us to want to have something that is predictive, to say, if x happens, then the price is going to go to y. If it gets above 100, then it's going to go above 110 or something to that extent.

But the issue is that we can't predict the future. We can't predict what is going to happen next. We can only react. And that's what I think is the value of technical analysis, that it is not predictive. It is reactive. It is allowing us to have a system that helps make these decisions, to help us have a more informed decision based on price action at that moment in time. As we discussed in the first event, by all means, some people use different types of analysis, like fundamental analysis.

But if you've ever had a company beat their earnings estimate but go down, sometimes that decision-making process is also very difficult. So we're using price as that final determining factor of, are people buying or are people selling? And if so, why? Is it for a fundamental reason? Is it for a technical reason? Is it for any other potential reason? So we use all of these different pieces to help inform those decisions that we are indeed making and to have something that helps us make those decisions.

But from there, we want to look at some actual fun patterns. So there are, I mean, dozens, plethora of different patterns that we can take a look at. We will only hit some major,

popular, well known, different types of patterns. They will start slow. I will start slow with these. But they'll become somewhat repetitive as we go through these. But ultimately, a lot of what it is going to come down to is that breakout component and then, two, what is the psychology behind what is driving this price action, which I'll try to illustrate.

So first and foremost, we mentioned this in the first event, is that there are periods of time with no discernible trend that we're seeing what is essentially called horizontal congestion, just the concept of consolidation, congestion, price, finding some sort of equilibrium in this case. And when we are looking at important levels of support and resistance, the first one that we tend to take a look at is what is called a double top.

So what is a double top chart pattern? It is two successive peaks separated by one area of support, one trough in the middle of it. And effectively, we're looking for those reversal points like we mentioned in the first week. So let's illustrate what ultimately happens here. Imagine you're seeing a stock. It got above the level that you expected to get to. But it sells off at a horizontal level. a level of resistance is now defended at that secondary support.

Why could that be the case? Well, imagine you're someone who said, if this stock gets above 100, I think it's going to go to 110. And then it happens. It goes from 100 to 110. And you're thinking, man, I should've bought it at 100. And what ends up happening? Maybe you buy it at 100. And it goes right back to 110. And then you're worried. Well, hey, it went to 110 twice. 110 seems to be what feels like a ceiling of sorts.

Maybe I shouldn't be in this position if it can't get much higher from here. Maybe I decide to take that position off the table if it gets below 100. Or maybe we can just effectively see that sellers are outweighing buyers at that level of resistance. There's more supply than there ultimately is demand at these important levels. So buyers get out of the way of this secondary test of 100. And we see that breakout to the downside.

For these chart patterns that we will take a look at here today, the common scholastic approach for its target breakout price in this case tends to be taking the height between these two values. I mentioned 100 to 110. \$10 is what we're effectively looking at as a breakout target to the downside. I would not get too tunnel visioned about the calculated target price because, again, it goes back to that function of predictive, which we're not effectively trying to do.

We're trying to use this to be decisive to help react to these levels effectively. It being below our breakout price means that we have broken out of that double top formation. That is important to us from a trading perspective. Now, what's the opposite of a double top? It's a double bottom. Imagine, in the same sort of scenario, that you see a level of support. You buy this stock at \$50. And it goes immediately to 60. And you're thinking, man, I should buy more if it gets back down to 50 again.

I was a genius for buying this at 50. If I'm given the opportunity, I'll buy more at 50. And what do buyers do? They step back in at \$50. And sellers, again, they kind of just get out of the way of this demand freight train of sorts. They are getting out of the way of this demand.

Buyers are in control of the situation. And that breakout is getting back above that level of resistance. There's enough demand at that level of support to get back above that level of resistance.

Now, you might be thinking, all right, cool, double tops and double bottoms. If it touches twice, then you're good to go. Unfortunately, not quite. Because what can also happen? Well, we can get a triple top. What is the difference between a double top or triple top? It's one more top in the sense that we get up to level resistance, test support, test resistance, test support, test resistance again. Buyers say no thank you. They get out of the way on this third try because they are realizing that this buying that they keep doing at support is not fruitful enough for them.

Enough supply is outweighing this overall perspective because, again, imagine you are someone consistently buying what you think is a level of support. And it's just not going higher. It has a failure every single time at the exact same level. Do you maybe just decide not to buy it if it gets back down to that level one more time? Or maybe you decide to sell it because you're worried that this can't go on forever, and that there's enough of an overhang of sorts weighing on the price to keep it from being able to get back above that level?

And the same sort of thing as we move to the next one, what is the next iteration that we would imagine seeing here? It's a triple bottom. Why would it be a triple bottom? In the same sort of way. Tests of support, test of resistance, support, resistance, support. Resistance gives up. Enough demand is outweighing that supply on that move. Higher people defending that price, traders defending that price, it allows for enough demand to outweigh that supply.

As we've mentioned, every price that you see in the market is a clashing of decisions, buyers versus sellers. In essence, if there are more buyers than sellers, can it push price to the levels that we want it to be able to find? And that breakout getting above that level is the important breakout perspective. Now, you might be thinking, all right, is he just going to keep doing this? Double, triple, quadruple, how far can we take this? Well, after those tests, we just call it a rectangle. It is just a horizontal congestion. It is just a rectangle of sorts.

Buyer stepping in it, support, seller stepping in a resistance, support, resistance, and this continues until, effectively, some side of that transaction gets out of the way of it. And a lot of the times, there's two different ways that we can approach scenarios like this. Maybe we're trading that horizontal congestion. We mentioned that in the first session, that sometimes there's value to be found of being able to buy support, sell resistance, rinse and repeat for an indefinite amount of time. But also, maybe it gives you the permission to wait it out, to not having a position in this position that is just moving sideways.

It's just consolidating. It's just in an area of congestion. And maybe you're just waiting to see if enough potential energy can build to break us out one way or the other. In this case, the breakout is valid both upward and downward. It is important to observe, effectively, who's in control at this moment in time. Are buyers going to take control of the situation? Or are sellers going to take control of the situation?

I mentioned, too, this concept of potential energy building. To me, that is what is the driving force of this next type of chart pattern. Rather than horizontal congestion, what if those lines of support and resistance we're drawing are more diagonal in their approach? What if we have declining highs but improving lows? And we're seeing this pattern of sorts forming that we effectively call a triangle. So it's the same sort of perspective as a rectangle, of course, different shape, but converging trend lines.

Why is that important to us? Well, it is an eventuality of sorts that a breakout occurs. Unfortunately, the rectangle, that could technically happen forever if buyers and sellers just agree to an equilibrium price of sorts. A triangle has to break out eventually. It doesn't mean that it will be a substantially large breakout. But it will resolve at some point in time. Because, effectively, what is happening? Sellers are willing to sell at incrementally lower prices, but buyers are willing to buy at incrementally higher prices.

Someone is eventually going to be in control. We call this a triangle, but sometimes we also call it what is called a coil because it has that potential energy feel to it. Potential energy is building like it would if we were winding a coil, waiting to see if that does expand. We're waiting to see which side can ultimately win out in these buyers versus sellers. We're seeing that bounded distinction of price touching each side of these. It mentions here, price must touch each bound at least twice.

The thing that I always remember, the phrase I always remember is. Once is chance. Two's a coincidence. Three's a pattern. That is the way that we tend to think about a variety of these different types of patterns. And this triangle is an important breakout that we're looking for for it to take place. Now, it does not always happen as clean as that, improving lows, descending highs. Sometimes we get the function of level highs or level lows with improving highs or lows on the other hand.

That is, in this case, what we effectively call an ascending triangle. What is the difference? Rather than two diagonal trend lines converging on one another, we are getting one level, in this case level area of resistance, horizontal resistance. But we are getting a diagonal support line, a diagonal trend line. What drives that? Well, sellers are willing to sell at level prices. But buyers are willing to buy at incrementally higher prices.

Let's think about that. Let's think about the psychology of what that looks like. Imagine if you see a stock that it just can't get above 100 for some reason. But every time it dips-- first it dipped to 80, went to 100. 85 to 100. 90 to 100. 95 to 100. You can feel that building of buying pressure mounting to hopefully get that breakout higher. It doesn't mean that it will breakout higher. It can also breakout lower if that resistance remains intact.

Imagine if you had been a buyer, again, 80, 85, 90, 95. It just doesn't break 100. Do you eventually give up? Do you eventually say, all right, well, I just can't get any more money out of it? Buying at 98, 99 to 100, I should look for a different opportunity. Does that mean demand wanes? That's another function of that. We can't emphasize enough, what we've gone through so far today, how important that breakout is. Just because we're seeing the

beginning stages of an ascending triangle does not mean that it'll break out higher. Just because there's that demand function on an incrementally moving higher level, it doesn't mean they'll eventually not get out of the way.

Same thing can be said on a descending triangle. What's the difference here? Level support but declining resistance. Again, sellers are putting the pressure on the buyers. Buyers keep stepping in at any level area. Sellers keep selling it at incrementally lower prices. I can imagine a scenario where you're buying it at 50. You sell it at 60. Then you buy it at 50 again. You sell it at 67. 50 to 65. 50 to 63. You're feeling how much that is waning against you. And you start to say, is it worth it for me to buy it at 50 if it only gets maybe to 55? Maybe buyers don't step in.

Now, things don't always work as cleanly as that. Sometimes we see a wedge of sorts, a triangle that's effectively moving upwards or even downwards. But it's converging. You can feel how much that is converging. Essentially, buyers and sellers are clashing with one another. We are narrowing the range, again, that potential energy building, and how important that can be for its overall chart pattern.

A couple other fun patterns that we always take a look at, though, we always like to talk about some ones that you might've have heard of as well, chart-pattern wise, the head-and-shoulders top. What is a head-and-shoulders top? It's effectively four different important variables. So there's four different things that have to happen before we actually see a head and shoulders. We need a higher high, a secondary higher high, one that is higher from the first one, followed by a lower high, and then finally, a breakout of an important area of support. Left shoulder, head. Right shoulder, neckline.

A breakout below the neckline is the completion of that head-and-shoulders pattern. Why is this one a popular pattern that people tend to know about and look for? Well, logistically speaking, it has the same sort of conceptual building blocks of just what a market top looks like. More often than not, tops are not an event. They tend to be more of a process. All of those traders who have been rewarded for incrementally buying higher lows to find higher highs, they have to see something shift. Don't they?

They need to see something waning, that rounding of a top to say that, hey, that function of trend is starting to dissipate. And maybe I need to start being protective rather than looking for opportunities to buy the dip. And that's what that head-and-shoulders top is really signifying. The left shoulder, head, right shoulder is, again, higher-high, higher-high, lower-high. And that means that that trend is waning, the neckline being the final line in the sand that those buyers were waiting to see if it would hold up at. And breaking out below that maybe gives enough holders, buyers permission to get out of that position to push prices lower.

Now, if you remember, I went from double top to double bottom. Same thing on head and shoulders, the same sort of driving force to a bottoming process. lower-low, lower-low, higher-low, ability to get back above an important area of resistance. That's what that

bottoming process can sometimes feel like. We were in that distribution phase, and we're starting to see accumulation round out at the bottom end of this.

And that ability to get back above an area of resistance is good enough for some traders to say, all right, maybe the distribution, maybe the selling is waning off. And maybe that is enough of a permission structure for me to allow myself to get back in the position, assuming all of these levels continue to hold. A lot of what technical analysis boils down to, again, is you're wanting to see certain criterias continue to be met because we sometimes forget that every single day that we choose to have a position on is an active choice.

It's a choice to have that position. It's a choice not to have another position. There's an opportunity cost for every single thing. And we want to make sure that whatever positions that we have deserve a spot in our portfolio. We want to make sure that what we're seeing happening is continuing to confirm all of those pieces of evidence that allow us to put our hard-earned capital at risk with this position.

Final one before I bring James back in to take a look at some candlesticks and different types of perspectives out there, the cup-and-handle pattern. What is the fun part of a cup and handle? Well, it's generally that process of a long-term, rounding effect, bottoming process with a short period of consolidation. So we see price go in distribution, move to accumulation, get back to its original resistance level, sell off slightly. But buyers decide to step back in.

You can see that perspective of that rounding bottom, short handle here, the cup-and-handle style pattern, and then waiting to see if it can get back above that level of resistance. Now, you might be thinking, all right, is he going to look at an inverse cup and handle?

Unfortunately, no. There's not technically an inverse cup-and-handle pattern, I think, for no other reason except that, if you had a cup of coffee and you turned it over, well, the coffee falls out. So there's no fun in an inverse cup-and-handle style pattern.

But it's all important to us when we think about the variety of different patterns that are out there, when we think about the variety of different perspectives that we combine. We can find in this example. Hey, they were in a rectangle. We saw a breakout of that rectangle. Now we're in that accumulation trend that we can combine with pieces of evidence from the first and second session, trend itself. Then we start seeing a triangle form, then another triangle, then a wedge, and another wedge. It's important to remember that there's not always a perfectly clean chart. Every single day is a different battle of sorts.

We're looking to see, what is the current event itself? What are some things that we need to take a look at? What are some other perspectives that we want to keep in mind? That being said, I'll pause for a brief moment. Anything that you wanted to add, James, to some of these patterns? Or anything you want to take a look at with the next perspective?

**JAMES SAVAGE:** Well, Andrew, I love the analogy about the cup and handle. I guess you're right. You really can't turn a cup and handle upside down. I never thought of it like that. But it

makes perfect sense why there's not an inverse of the cup and handle. But, no, I'm ready to jump into the next category of patterns. And that is going to be candlestick patterns, a bit of a niche type of pattern analysis.

So I don't think they get as much popularity as the head and shoulders, for example, or some of the triangles. But we do want to talk about them because there are a large number of traders that find candlestick patterns useful. Now, similar to what we wanted to talk about when it came to just the general patterns earlier, talked about some of the assumptions and the basics, candlestick patterns aren't going to have those type of rules, I would say, when it came to we need our two trend lines. There has to be the breakout in order to activate it.

So with candlesticks, it's going to be a little different. Now, these are ideas that came from Japanese rice traders. And what they're oftentimes used for is to identify reversals. Now, doesn't mean it's the only way that you can use them. They can be used for continuation patterns as well. But many traders find that looking for reversals with candlestick patterns can be helpful.

Now, this is something that is just scratching the surface of the sheer number of candlestick patterns that exist. I might talk about a few others as we go through some of the slides here. And even though they're oftentimes used with longer term trends, you can still use these for you aspiring day traders out there that are going to be looking at very short time frames.

And, like with everything, we can't say this enough. A singular pattern, a singular signal shouldn't be the reason why you buy or sell. So just because you see a candlestick pattern out there doesn't mean that's going to be the sole reason that you enter or exit a position.

But you can use this with some of the other tools, with some of the other skills that you acquired, for example, from our session, and use that ultimately to make that final decision of entering or exiting. It's the preponderance of evidence that we want to accumulate before we make up our mind.

So, starting with what's possibly the most famous candlestick pattern, and that is the doji. This is a one-candle pattern. And what I mean by that is that, well, in the name, the pattern is comprised of just a singular candle. We're going to go over two candlestick patterns as well. But there are more. There are candlestick patterns that need three candlesticks before they can be called that pattern.

And in this case, what we're looking for is for the open and the close to be at the same price, or very close to the same price. And the high and low are roughly equidistant from the open. Now, in the real world, it doesn't have to be to the penny. Even better, though, if it is to the penny, of course. But think the general idea on this. The market opens up. Or the stock opens up trading. Or the period begins at that time.

It goes up. It goes down. And then, when the period ends, it's at the same price. So think of it from a daily candle perspective. The price that we opened at was the same price that we closed at. Well, it went higher and lower. Probably makes sense why it's viewed as a signal of Indecision in the marketplace, that there could be a warning, if you will, of a price change.

Now, there's a few different variations of this. There's what's referred to as a dragonfly doji or a gravestone doji. The dragonfly is, if you think of a dragonfly, it's open and closed at the high of the range. The gravestone is, well, at the low of the range. All of them are generally used to signify indecision within the overall underlying for that period. And hopefully, it makes sense, right? If we start and close while we had a wide range, the market didn't know where to move that price within that period of time.

So that is, again, a single candlestick type of pattern. So as we jump over to a two-candlestick pattern, we can go into the harami. Now, I might be saying that incorrectly. Forgive me for native Japanese speakers out there. And what we're looking at here, in this case, is a two-candle pattern, a large body of either color followed by a smaller body of the opposite color.

So in this case, that key differentiator is that the second candle, the full range of that price, that open and close is within the prior day's activity. Now, depending on just the prior movement, if you will, of price-- for example, were we on a bullish trend? Or were we on a bearish trend?

This could be viewed as a bullish signal or bearish signal. Now, many of these types of candlestick patterns can really go either way. Generally, it's viewed, though, that a bullish type of pattern would be when we see that big, red candle, so to speak, and then that smaller green candle.

Now, keep in mind that, when looking at this, because the candle body can either be black or white, and you could think of this as either hollow or filled-- we oftentimes like to switch it to say green or red-- that you're going to use this to maybe get an understanding of the narrative behind price, but still not rely solely on whether this is going to get you in or out of the position.

But let's jump into one of our other patterns as well. Again, it might be one of the more popular patterns that exist. And that's going to be the hanging man and the hammer. And I like to always put a bit of a narrative behind this to maybe explain why it's happening. So in this case, we've got back to a one-candle pattern, differentiated by the color of the body and the preceding, I guess we'll say, trend, if you will, the preceding direction of price.

Now, as some of the bullet points state here, it can be viewed as both a continuation and reversal pattern, which is what can be said for many of these. There's a lot of the subjectivity in this. This is where that art side of technical analysis really shines. But generally, what you'd expect to see is a hammer being a bullish reversal pattern, where you'd imagine, if price was declining, going down, we would find ourselves in this hammer.

And imagine, that's where price would be opening close to the top, moving on down, and then again, going back up to the top of that bar and closing right up at the high point. Now, if this is following a downward trend, well, that's letting you that price went further down, but managed to rally during that same period, and close up at a tie. That's why it's generally viewed as a bullish pattern.

And we can see, from the hanging man, oftentimes we will see that at the top of a bullish pattern as a signal of a bearish reversal. So it's very key in these pattern analysis, especially from a single candlestick, is to look at the prior trend. Did it happen as price was moving downward? Or did it happen as price was moving upward? And we oftentimes see the hanging man form at the top of what had been a bullish trend as a possible potential signal for a reversal.

Now, similar to what Andrew was talking about with some of the patterns that, where they happen at the top, there's a bottom. Well, we can also see this with the shooting star and the inverted hammer, again, patterns that are very importantly based on that prior trend, where we'll oftentimes see, say, a shooting star. You could possibly see it in the name there, that forms at the top of a direction of price.

So imagine a bullish trend with price rising upwards. We see our shooting star formed up at the very top where price climbed higher but then ultimately closed at the low of the day. It opened towards the low, climbed higher. But by the end of that day or that period of time that you're using-- we oftentimes use daily frequencies, daily candles. So I'm describing it almost interchangeably.

But candles can be any time frame that you choose-- or not any but a variety of different time frames that you choose, five minutes, 10 minutes, one day, one week, one month, for example. But as price opens, rises, and falls at the top of a range, that can be a bit of a warning sign. That's that possible flashing light there just to be careful because, despite price oftentimes viewed as closing higher, that's that shooting star.

Well, it's also closing that intraday activity. That intraperiod activity ended up closing at the bottom. So you have a bit of a concern with what the price might do next. So again, that was a single candle pattern. Now, to keep this somewhat back and forth changes, now to introduce the engulfing.

Along with the doji, this might also be one of my favorite candlestick patterns in that just how helpful it can be. And what we're looking at here is a top and a bottom engulfing pattern. And in these two bar patterns, the key thing is is that that second candlestick engulfs, as the name, the first bar of the body of that preceding candle.

Now, there's a bottom engulfing pattern with a short, you could say, black body, followed by a tall, white body. Or in other words, that could be considered a bullish and upward reversal pattern. And we can almost think of it from, again, the narrative. We try to explain it here, where imagine a day, where whether it was an up day or down day, let's work with a down day where the market closed down.

But then, the very next day, we opened up underneath it. We opened up lower, and then completely rallied and closed at the very top of the day's price range, or very close to the top. And that top was far higher than the price of the preceding day. So we can see, oftentimes, in a type of a bullish engulfing pattern, which is when we'll see this green candle

or this hollow candle that is preceding it, is to signify that the buyers out there that demand has now engulfed the prior bearishness of that preceding candle.

And we can say vice versa with the bearish engulfing candle, where we'll see a hollow or green candle completely engulfed by a red candle. And that's just to signify the amount of selling pressure or supply that has now overwhelmed the preceding demand. Now, it can be somewhat tough looking at these candlesticks just in a singular snapshot because it's very important to take them in the context of what price has been doing.

Now, we'll introduce one more pattern today. And that is going to be the dark cloud cover and the piercing line. And we can almost think of these as somewhat of borrowing from what we've talked about with the engulfing candle, where we're seeing the current day's activity, the current period's activity somewhat overpowering the preceding period.

And this is what's going to create the idea that, if we're looking at, say, a piercing line, for example, now, this is viewed as a bullish type of activity. And imagine a day where we closed down from an intraday perspective. The very next day, we opened up lower. So it was looking red. And then we rallied above, right?

We pierced that prior candle or, in this case, that prior closing price. And we ended up closing at a higher price, opening lower but closing at a higher price than the preceding candle. And that's where we can see that bullishness that gets formed. And why in this case, the dark cloud cover, which is on the left image here-- imagine that. When price has been rallying, so to speak, we close at a high point.

The next day, we open up higher to only then see price fall underneath that closing, where we have a red candle or, in this case, a black candle. And we have a lower close in the preceding day. So it's helpful to view these as how that buying and selling dynamic shifts between one period versus the other, whether you're looking at from a daily frequency, which is what I like to oftentimes use for examples, or even from an intraday frequency for all those aspiring day traders here.

So candlestick patterns are, just in summary there, they have a lot of subjectivity in there. And that's based on just the understanding of and the recognition of what price has been doing prior to those candlestick patterns forming themselves, and using that to then plan what could be the next course of action based on whatever forecast that you have on the underlying.

So, Andrew, we'll stop there. I mean, there are quite a few other candlestick patterns out there. Three black crows, three white soldiers, we start going into some of the popular three-candle patterns. But in the interest of time, I guess we'll have to take a pause there. Any further comments on, maybe, these candlestick patterns? Or possibly any closing thoughts on just candlestick, classic patterns, techniques in general here? I'd be curious to hear your thoughts.

**ANDREW MCGOWIN:** Hey, absolutely. So much can be said around the world of technical analysis, around the world of candlesticks, around the world of all of these different concepts that we've discovered in these last three sessions. Everything boils down to ultimately allowing ourselves some sort of decision-making process. We're observing what other traders are doing via price action, via what the price is doing itself. It is allowing us to see into the mind of the market in its infinite wisdom.

What is the totality of buyers and sellers interacting with one another? And can we use that, as mentioned, to make decisions? That's the fun part, as we mentioned in the first event, how this differs from fundamental analysis, because, as mentioned, when I think about what fundamental analysis ultimately boils down to is taking a look at how this company does, of course, and their balance sheets, and all of these numbers and everything to that extent, but effectively arriving at a conclusion of is this company overvalued or undervalued.

And is the market wrong, effectively, at this moment in time? Can I take advantage of the market mispricing something? Technical analysis somewhat just assumes the market has priced in every single bit of known information, and we're simply just trying to obtain. Are we in an accumulation phase? Are we in a distribution phase? Are we consolidating? Has there been short-term price action? But effectively trying to remove all of that noise and simply look at the signals themselves via price.

And, as mentioned, I am, by all means, a technician by trade. I appreciate technical analysis. I appreciate what that allows me to do to hopefully still be able to make all of these decisions without needing the fundamental background, the classical finance background. All the Wall Street analysts paid the big bucks to issue those buy or sell recommendations or things of that extent. We are simply just looking at price. We are making decisions accordingly with that price.

But appreciate, as always, everyone who has joined us for these three parts. As mentioned earlier, you can find James and myself and our team at [Fidelity.com/coaching](https://www.fidelity.com/coaching). We put on about seven to eight different sessions on a daily basis on these topics, like technical analysis, beginning and ending each day with a market briefing, taking a look at the events of the day, as well as you can find classrooms at [Fidelity.com/classrooms](https://www.fidelity.com/classrooms). I appreciate you all joining us. I appreciate James being my co-host for these three events. We look forward to seeing you all in these sessions. Take care.

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