Module 2- Chapter 1 – Hammer

The Hammer candlestick pattern is a bullish reversal pattern that signifies a potential turnaround in price. It typically forms at the end of a downtrend and signals the possibility of a bullish movement starting. It's called a "Hammer" due to its shape, which resembles a hammer with a long handle and a small head.

What The Pattern Looks Like

The Hammer pattern is formed of a single candlestick, which has the following characteristics:

Small Real Body: The body of the candle, which is the difference between the opening and closing prices, should be small. This body can be either red (bearish) or green (bullish).

Long Lower Shadow: The most defining feature of a Hammer is its long lower shadow (wick). This shadow should be at least twice the length of the real body.

Little to No Upper Shadow: Ideally, a Hammer should have little to no upper shadow. If there's a small upper shadow, it can still be considered a Hammer, but the absence of an upper shadow is more ideal.

Position within a Trend: For the pattern to be considered a Hammer, it must form after a downtrend. If the same shape appears after an uptrend, it is called a "Hanging Man" and can be bearish.

Pattern Psychology

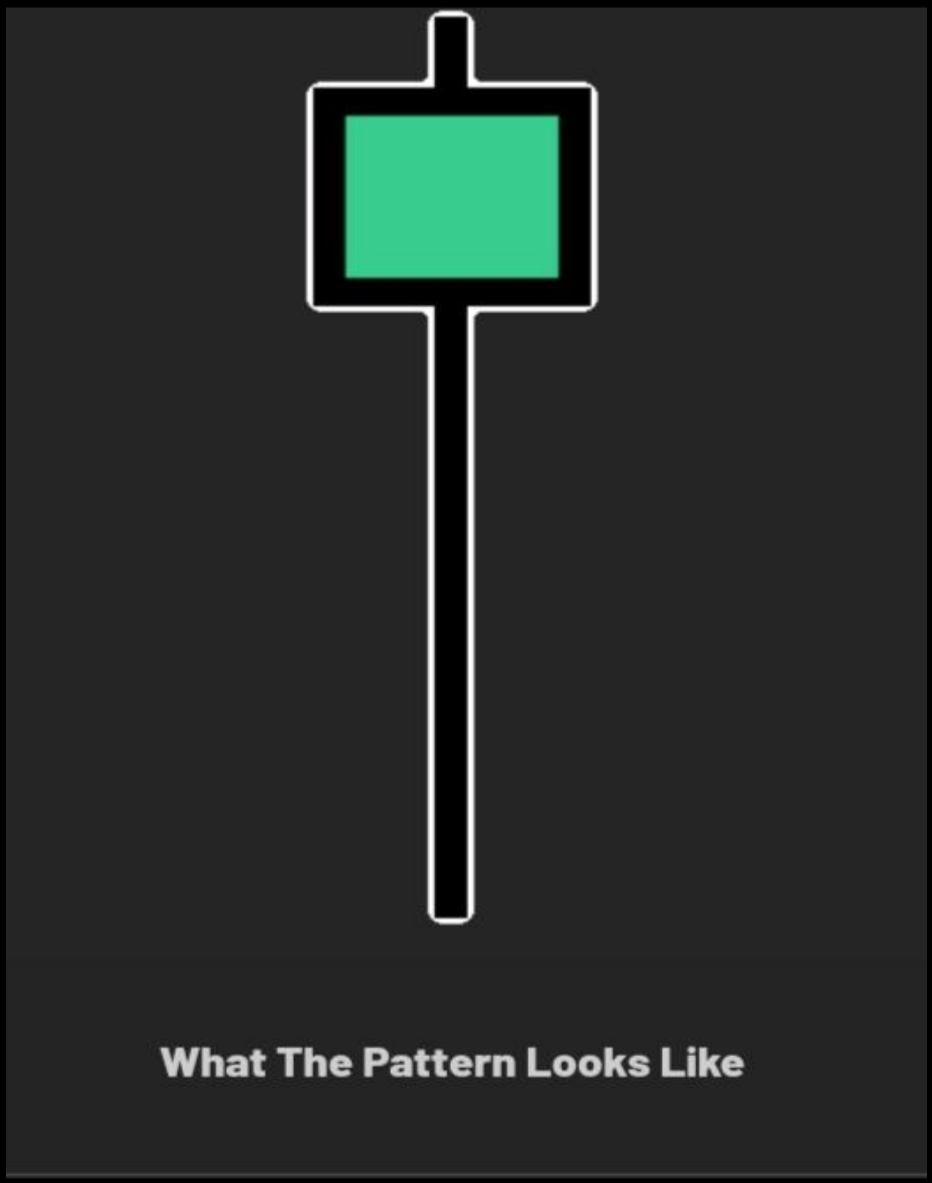
To fully understand the Hammer candlestick pattern, we need to delve into the market psychology behind it:

1) **Previous Downtrend:** Before the Hammer appears, there's a prevailing downtrend. This means that the bears have been in control, and the sentiment is pessimistic.

2) **Intra-day Decline and Recovery:** On the day the Hammer is formed, prices generally open and continue to move down, suggesting that bears are still trying to push the prices lower. However, at some point during the day, a change in sentiment occurs. Buyers step in, pushing the price back up, often closing near or slightly below the opening price.

3) **Bulls Take Control:** The long lower shadow represents the distance between the lowest traded prices of that day and the closing price, showing a rejection of the lower prices. This signifies that bulls are beginning to gain control and that bears are retreating.

4) **Potential Reversal Confirmation**: While the Hammer itself is a potential reversal sign, it's essential to look for confirmation on subsequent days. A bullish candle or a gap up the next day can validate the bullish reversal signal of the Hammer.



In conclusion, the Hammer candlestick pattern is an essential tool for traders and investors to identify potential bullish reversals after a downtrend. However, like all candlestick patterns, it's crucial to use the Hammer in conjunction with other technical analysis tools and not to rely solely on it for making trading decisions.