# Piercing Pattern

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## What Is a Piercing Pattern?

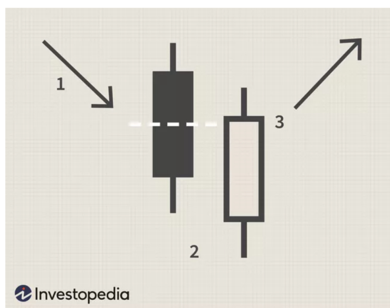
A piercing pattern is a two-day, candlestick price pattern that marks a potential short-term reversal from a downward trend to an upward trend. The pattern includes the first day opening near the high and closing near the low with an average or larger-sized trading range. It also includes a gap down after the first day where the second day begins trading, opening near the low and closing near the high. The close should also be a candlestick that covers at least half of the upward length of the previous day's red candlestick body.

KEY TAKEAWAYS

- The piercing pattern is a two-day candle pattern that implies a potential reversal from a downward trend to an upward trend.
- This candle pattern typically only forecasts about five days out.
- Three characteristics of this pattern include a downward trend before the pattern, a gap after the first day, and a strong reversal as the second candle in the pattern.

## How a Piercing Pattern Works

A piercing pattern features two days where the first is decidedly influenced by sellers and where the second day responds by enthusiastic buyers. This is potentially an indication that the supply of shares that market participants want to sell has been depleted somewhat, and price has been driven down to a level where demand for buying shares has increased and been shown to be evident. This dynamic seems to be a somewhat reliable indicator of a short-term upward forecast.

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## Piercing Pattern Formation

A piercing pattern is one of a few important candlestick patterns that technical analysts typically spot on a price series chart. This pattern is formed by the two consecutive candlesticks previously mentioned and also has three additional important characteristics (as noted in the illustration above).

1. The pattern is preceded by a downward trend in price. (This may be only a short down trend, but if the candles appear after an upward trend in price it is not an important reversal indicator).
2. The price gaps lower to begin the second day. (This pattern is mostly found in stocks because of their ability to have overnight gaps unlike currencies or other 24-hour trading assets. This pattern may occur in any asset class on a weekly chart however).
3. The second candle must close above the mid point of the first candle. (This signifies that buyers overwhelmed sellers on this day.)



The first candlestick is usually dark colored or red, signifying a down day and the second is green or lighter colored signifying a day that closes higher than it opened. When a trader is watching for a bullish reversal, any red candlestick followed by a white candlestick could be an alert, but the piercing pattern is a special indication because the reversal is likely unexpected for most market participants.

## Piercing Pattern Example

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A piercing pattern is known in technical analysis to be a potential signal for a bullish reversal. The formation in its strictest form is rather rare, but tends to perform better the longer the downtrend in front of it. When technical studies such as RSI, Stochastic or MACD are showing a bullish divergence at the same time a piercing pattern appears, it strengthens the likelihood that this two-day pattern is meaningful.

The second day's white candlestick rebound from a down gap to a midpoint closing high is expected to be a sign that a support level has been reached. This may occur because the market specialist or market makers set the opening price lower than the previous day's close. When this happens at the market open, enthusiastic buyers may step in and reverse the price action right from the beginning of the trading day.

Thus, a piercing pattern can be further confirmed if it occurs at the support trendline of a price channel, where buying has previously come into play. A piercing pattern is typically only a potential signal for reversal so following a piercing pattern a trader would want to watch for a breakaway gap.

A breakaway gap is a pattern that occurs in the first phase of a reversal. It is identified by two consecutive white candlesticks with a second day white candlestick that shows a substantial gap higher from the first day's closing price to the second day's opening price. A piercing pattern followed by a breakaway gap can be a strong affirmation that a reversal is occurring.

In a bullish reversal, traders generally have two popular options. They can buy the stock to benefit from the uptrend. They may also choose to buy an in the money call option with a strike price below the current market price.



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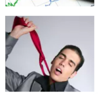
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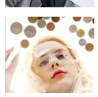
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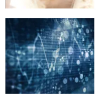
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