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## What Is RSI? Identifying Overbought and Oversold Conditions in All Markets

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Article Level: Intermediate

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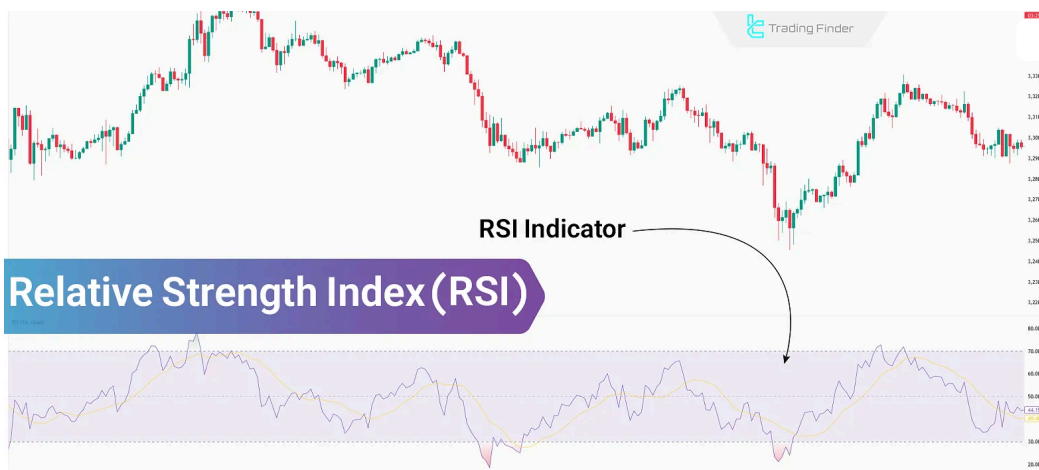
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The **Relative Strength Index (RSI)** evaluates the strength of a trend by analyzing the **open and close** prices of candles over different timeframes (**14 days by default**).

Therefore, this indicator is used in most **trading strategies**, including **divergence, trendlines**, and more.



RSI is an oscillator used to measure the strength of a price trend

This **indicator** consists of five components including **RSI line, moving average, level 50, level 70**, and **level 30**.

By analyzing the movement of these elements, it becomes possible to identify **divergence**, **overbought** and **oversold zones**, **support** and **resistance**, and more.



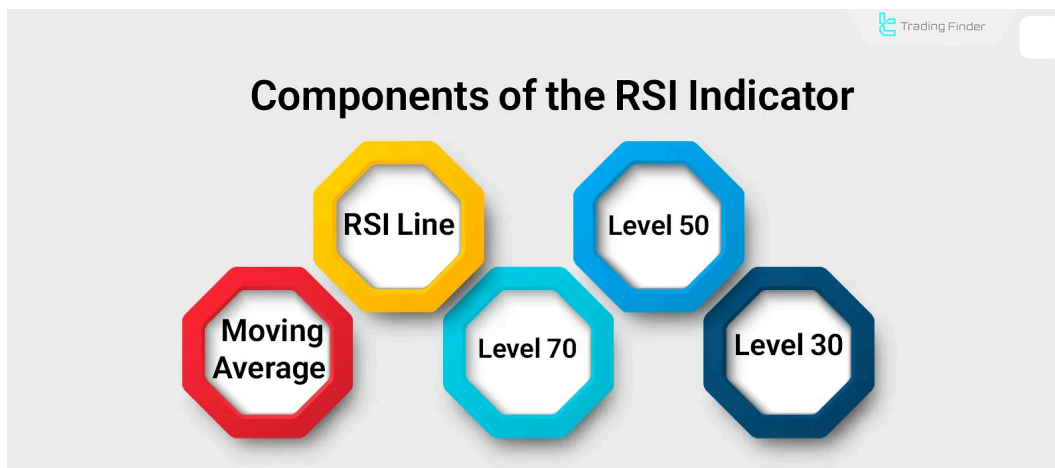
## What Is RSI?

**RSI** is an **oscillator** used to evaluate the strength of a price movement. This indicator identifies **overbought** or **oversold** zones by analyzing historical market factors such as **momentum**.

RSI moves **between 0 and 100**. Therefore, when it rises above the **70** level, it indicates **overbought** conditions, and when it drops below **30**, it signals **oversold** conditions.

## Components of the Relative Strength Index

The **relative strength index** consists of five main components, and the interaction between these elements, plays an essential role in analyzing **momentum** and **pricetrends**.



Key components of the RSI indicator include RSI line and moving average

**Components of the Relative Strength Index** Key components of the RSI indicator include RSI line and moving average **Index:**

- ⚡ **RSI Line:** The main element of the RSI indicator, **calculated using a specific formula** to reflect the relative strength of price;
- ⚡ **RSI Moving Average:** This line represents a **moving average** of the RSI line. Its intersection with the RSI line may generate a trend reversal signal;
- ⚡ **Level 70:** Defines the upper area of the **RSI display**; when the RSI line crosses above this level, it indicates **overbought** conditions;
- ⚡ **Level 50:** Divides the indicator display into **two halves**; reaching this level signifies a potential **support or resistance** area;
- ⚡ **Level 30:** Represents the oversold zone; when the RSI line enters this region, it signals an early indication of **potential price reversal**.

## Advantages and Disadvantages of RSI

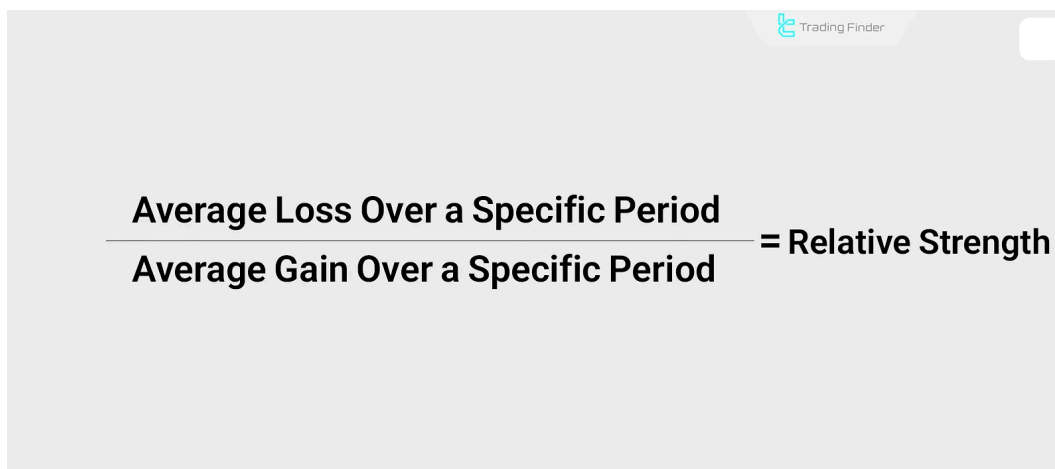
Using the **RSI indicator** is straightforward due to the clarity of its signals. However, **relying solely** on this indicator may not yield a high success rate in trading.

Therefore, to enhance **effectiveness**, it should be combined with other **technical analysis** concepts.

Advantages	Disadvantages
High clarity of signals	Delay in signal generation
Easy to use	Possibility of false signals
High compatibility with other tools	Requires combination with other analysis methods
Usable in all financial markets	Weak performance in ranging markets

## How to Calculate the RSI Indicator?

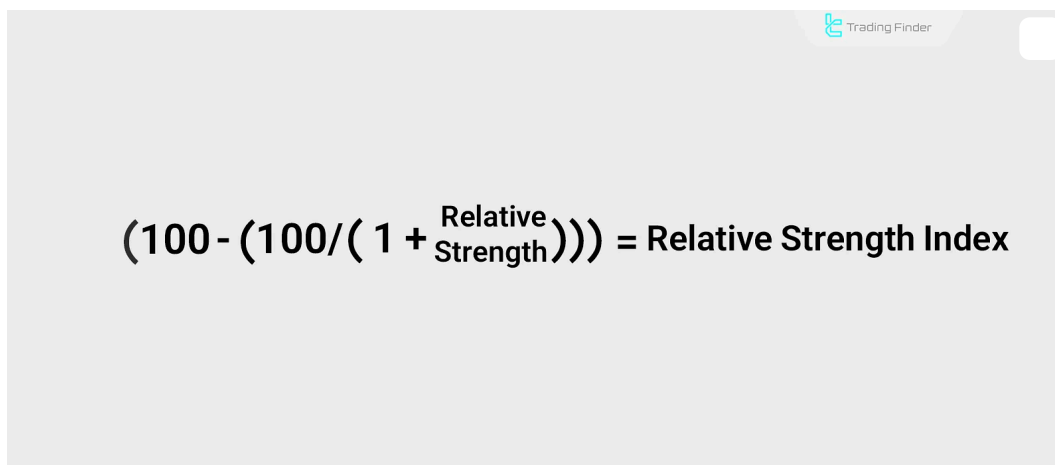
The **RSI indicator** is calculated using two formulas. The first formula computes the **relative strength (RS)**. Then, using the relative strength in the main formula, the **Relative Strength Index** is determined.



$$\frac{\text{Average Loss Over a Specific Period}}{\text{Average Gain Over a Specific Period}} = \text{Relative Strength}$$

Relative strength is calculated by dividing the average gain and loss over a specific period

**Relative Strength Index Calculation formula:**



$$(100 - (100 / (1 + \text{Relative Strength}))) = \text{Relative Strength Index}$$

After calculating relative strength, the RSI value can be determined

## RSI Settings

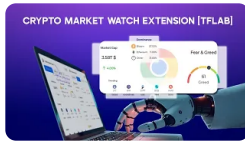
The **RSI indicator** performs its calculations using a specific timeframe. Therefore, **changing** this timeframe can adjust the indicator's performance for **short-term or long-term** trading strategies.

By default, RSI uses a **14-day period**. Reducing this period increases the indicator's **sensitivity** and produces more signals. On the other hand, increasing the **period reduces** the number of signals but helps minimize false signals.

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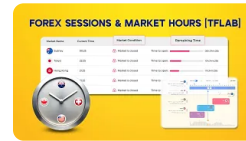
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## What are the Applications of RSI?

By measuring trend strength, the **RSI indicator** is used in various scenarios such as identifying **support and resistance levels, overbought and oversold conditions, divergences, and more.**

Applications of RSI:

- ⚡ **Support and Resistance:** When the RSI line reaches the middle of the display, it suggests an **equilibrium** between buyers and sellers, forming support and resistance zones;
- ⚡ **Overbought and Oversold:** Entering the areas **above 70** and below 30, indicates overbought or oversold conditions;
- ⚡ **Identifying Take Profit and Stop Loss Zones:** By observing how price reacts to the main RSI levels, traders can place **take profit** and **stop loss** orders using the 0–100 RSI scale;
- ⚡ **Trend Continuation Confirmation:** The **50 level** is used to confirm the trend. For example, if the price is **above 50**, it confirms the **continuation of a bullish trend**;
- ⚡ **Divergence Detection:** The RSI can detect both **regular and hidden divergences**, in both bullish and bearish scenarios.

## Divergence in RSI

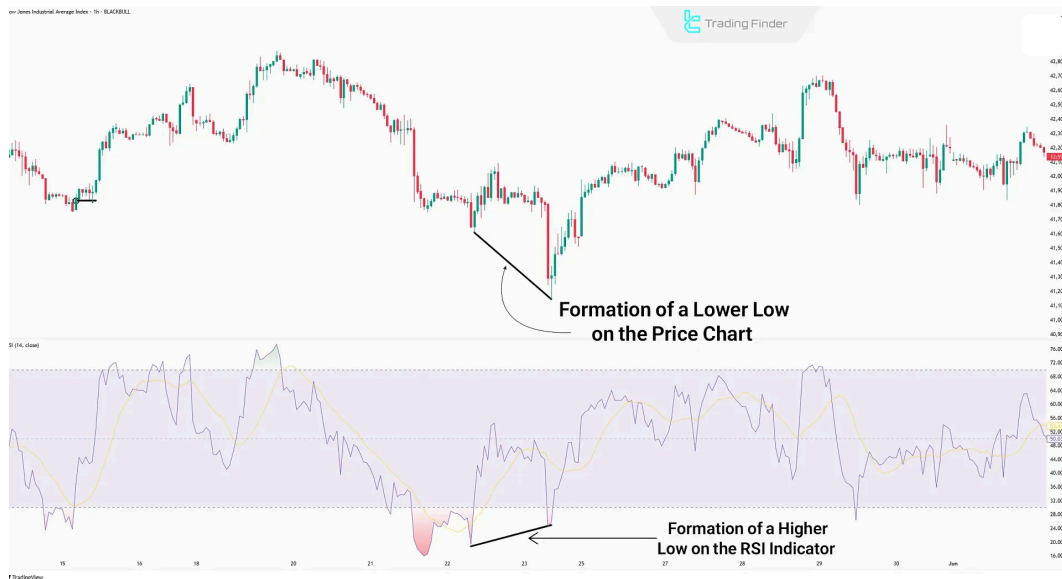
In general, **divergence** refers to a lack of **alignment between** price movement and the indicator.

Therefore, in the **RSI indicator**, if the highs or lows formed are inconsistent with those on the **price chart**, divergence has occurred.

### Regular Divergence

**Regular divergence** forms in two stages:

1. Formation of new highs (**in an uptrend**) or new lows (**in a downtrend**);
2. Formation of RSI **highs and lows** in the opposite direction of **the levels formed** on the price chart.

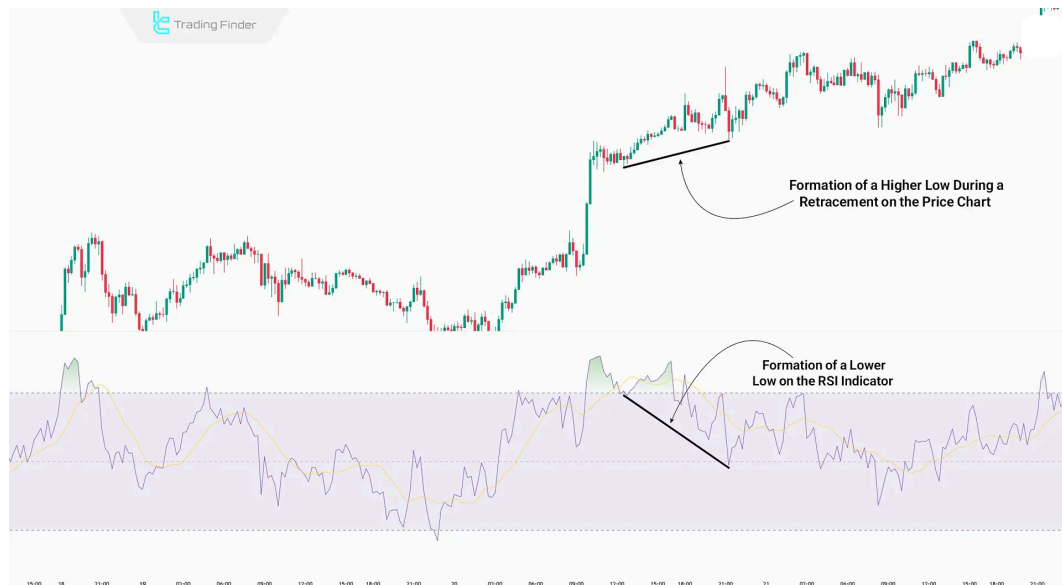


Inconsistency between price highs/lows and RSI signals the presence of regular divergence

### Hidden Divergence

In **hidden divergence**, the retracement of the trend is examined. It is formed through the following steps:

1. Formation of a low (**in an uptrend**) or high (**in a downtrend**) during a price retracement;
2. A mismatch between the **highs/lows** formed on the price chart and the RSI indicator.



Oposing highs and lows during retracement on the chart and RSI, indicates hidden divergence in the RSI indicator

### Trading Strategies Using the RSI Indicator

The **RSI indicator** is widely used in trading strategies due to its ability to identify **divergence, support and resistance levels**, and **overbought/oversold** zones.

Trading Strategies Using RSI:

- ⚡ **Divergence Strategy:** In this approach, a trade entry signal is generated after identifying **price divergence**;

⚡ **Trendline Strategy:** First, trendlines are drawn on both the RSI and **the price chart**. Then, when both the RSI and price hit these lines simultaneously, a trade entry **signal is triggered**;

⚡ **Overbought/Oversold and Support/Resistance Combination Strategy:** When price hits **support or resistance** zones and a divergence forms on the RSI, a **trade entry** signal is generated in the direction of the divergence.

## How to Improve RSI Performance?

Using the **Relative Strength Index (RSI)** on its own can carry high risk when entering trades. Therefore, combining it with other tools and concepts in **technical analysis** improves the success rate of trading strategies.

Although the RSI is highly compatible with most technical analysis methods, combining it with tools like **classic chart patterns**, **candlestick patterns**, or **Average True Range (ATR)** enhances the win rate of strategies.

### Technical Tools and Concepts to Combine with RSI:

- ⚡ **Classic Patterns**
- ⚡ **Candlestick Patterns**
- ⚡ **Support and Resistance**
- ⚡ **Stochastic Indicator**
- ⚡ **Average True Range (ATR)**
- ⚡ **Moving Average Indicator**

## Conclusion

The **RSI indicator** is an **oscillator** designed to measure trend strength. By default, it analyzes price movements over a 14-day period.

RSI can identify **overbought and oversold conditions**, various types of **divergence**, and **support and resistance levels**. These features make it applicable across different analysis methods and financial markets.

Since RSI derives its signals based on past market data, it naturally has some **lag**. Therefore, combining it with other technical analysis tools such as **classic patterns**, increases the **success rate** of trading decisions.

### FAQs

What is RSI? ▼

**RSI** is an **oscillator** used to detect the strength of price trends.

How many components does the RSI indicator have? ▼

The indicator has five components:

RSI Line  
Moving Average  
What does it mean when the RSI line crosses above 70? ▼

Crossing above level 70 indicates an **overbought condition** in the market, suggesting a possible reversal from an uptrend to a downtrend.

Level 30  
What does it mean when the RSI line crosses below 30? ▼

Level 30  
Crossing below level 30 signals an **oversold condition**, indicating a possible reversal from a downtrend to an uptrend.

What is the role of the 50 line in RSI? ▼

When the RSI line reaches the 50 level, it suggests **equilibrium between buying and selling pressure**, forming potential **support or resistance zones**.

Why is there a delay in RSI signals? ▼

RSI generates signals based on **historical market data**, which naturally introduces **signal lag**.

What is the effect of reducing the RSI period? ▼

Reducing the RSI period **increases the number of signals**, making it more suitable for **short-term trading**.

Can hidden divergence be identified with RSI? ▼

Yes, by analyzing **retacement patterns** and comparing them to RSI, it is possible to detect **hidden divergence**.

In which market condition does RSI perform poorly? ▼

RSI performs less effectively in **sideways (ranging) markets** compared to trending markets.

Is RSI applicable across all financial markets? ▼

Yes, the **RSI indicator** can be used in **all types of financial markets**.



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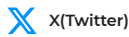


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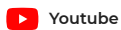
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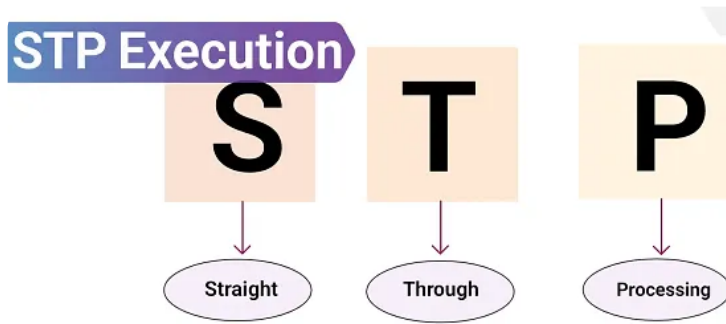
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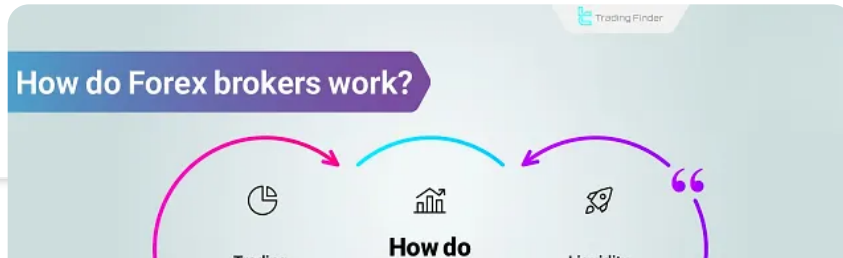
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