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A momentum indicator like RSI aims to show which of the bulls (optimists) or the bears (pessimists) are currently the strongest in the market. Getting to know your market through an RSI indicator can let you pin point reversals more accurately and thereby let you position yourself accordingly.

The RSI indicator uses the closing prices of completed trading periods to determine who owns the momentum in the market. It assumes that prices close higher in strong market periods (bull markets), and lower in weaker periods (bears owning the scene) and computes this as a ratio of the number of higher closes to the lower closes during a certain period of time, most commonly used is the period of 14 days.

Most stock charts packages out there today include the RSI indicator. Here is how it is calculated manually.

$$\text{RSI} = (100 - (100 / (1 + \text{RS})))$$

Seems simple enough, but the RS part need to be calculated first.

RS = 14-day **EMA** of upday closing gains / 14-day **EMA** of downday closing losses

EMA stands for [Exponential Moving Average](#) and is used to smooth out an average of a series of values. So what we want to do here is to take a 14 day exponential moving average of the upticks days and downtick days respectively. This is typically done by taking the latest 100 tradingdays, going through them and finding out which ones of the where updays and downdays respectively, and then calculate the moving average using 14 days as parameter. Note! [To calculate EMA, see this article](#). It's quite easy.

Applying the RS in the first RSI formula, will give you a value between 0 and 100.

The real challenge with Relative Strength Index is to know what boundaries apply for when a market is overbought and oversold respectively. This is the real trick and usually only comes to you after having studied a market thoroughly. Then, and only then, do you know where it usually turns and can thereby learn to recognize when a new turn is coming.

Common rule of thumb levels for RSI are 20 for oversold and 80 for overbought, but that is just as a rule of thumb and will inevitably vary between markets and stocks.

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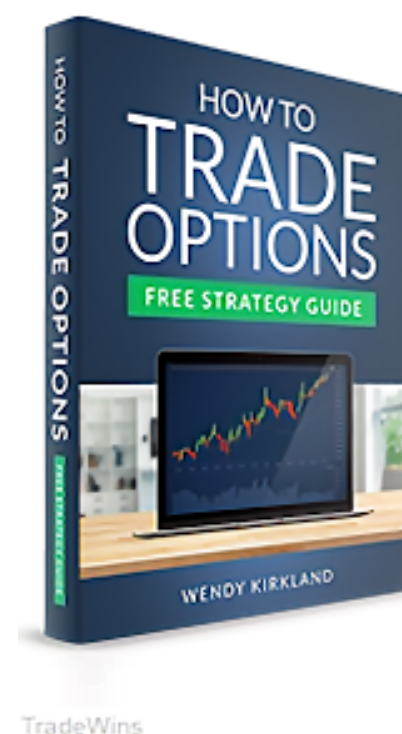
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