

RSI Context Guide

Using RSI Correctly Across Market Conditions

Introduction

The Relative Strength Index (RSI) is one of the most popular indicators—and one of the most misused.

The standard teaching—"buy oversold, sell overbought"—works sometimes and fails spectacularly other times. This guide teaches you when RSI works, when it doesn't, and how to use it properly.

Part 1: RSI Fundamentals

What RSI Actually Measures

RSI measures the speed and magnitude of recent price changes.

Formula (simplified):

$$\text{RSI} = 100 - \left(\frac{100}{1 + \text{RS}} \right)$$

Where RS = Average Gain / Average Loss over N periods

Standard period: 14

RSI Scale

RSI VALUE	TRADITIONAL INTERPRETATION
70+	Overbought
30-	Oversold
50	Neutral midpoint

The Problem with Traditional Interpretation

"Overbought" doesn't mean "sell." "Oversold" doesn't mean "buy."

In strong trends, RSI can stay overbought/oversold for extended periods while price continues.

Part 2: Market Regimes & RSI

Trending Markets

In strong trends, RSI behaves differently:

Strong Uptrend: - RSI oscillates between 40-80 - "Oversold" is 40-50, not 30 - RSI can stay above 70 for weeks

Strong Downtrend: - RSI oscillates between 20-60 - "Overbought" is 50-60, not 70 - RSI can stay below 30 for weeks

Ranging Markets

In sideways markets: - RSI oscillates between 30-70 more reliably - Extremes (30/70) are more meaningful - Mean reversion works

The Key Insight

Trend strength determines RSI behavior: - Strong trend → RSI ranges shift - Weak trend/range → Traditional levels work

Part 3: RSI Range Shifts

Identifying the RSI Range

Bull Market RSI Range:

```
80 — Overbought in uptrend
70 — Warning zone
|
50 — Midpoint (often support)
|
40 — Oversold in uptrend (buy zone)
30 — Rarely reached in uptrend
```

Bear Market RSI Range:

```
70 — Rarely reached in downtrend
60 — Overbought in downtrend (sell zone)
|
50 — Midpoint (often resistance)
|
30 — Warning zone
20 — Oversold in downtrend
```

Practical Application

In uptrend: - Buy when RSI pulls back to 40-50 - Don't short just because RSI hits 70 - RSI below 40 = Trend may be breaking

In downtrend: - Short when RSI rallies to 50-60 - Don't buy just because RSI hits 30 - RSI above 60 = Trend may be breaking

Part 4: RSI Divergence

What Is RSI Divergence?

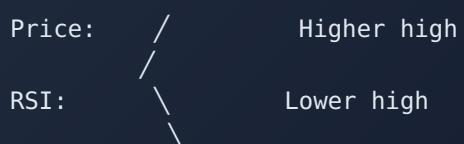
When price and RSI move in opposite directions.

Regular Bullish Divergence



Meaning: Momentum increasing even as price falls. **Signal:** Potential reversal up.

Regular Bearish Divergence



Meaning: Momentum decreasing even as price rises. **Signal:** Potential reversal down.

Hidden Divergence (Continuation)

Hidden Bullish: - Price: Higher low - RSI: Lower low - Signal: Trend continuation up

Hidden Bearish: - Price: Lower high - RSI: Higher high - Signal: Trend continuation down

Divergence Quality

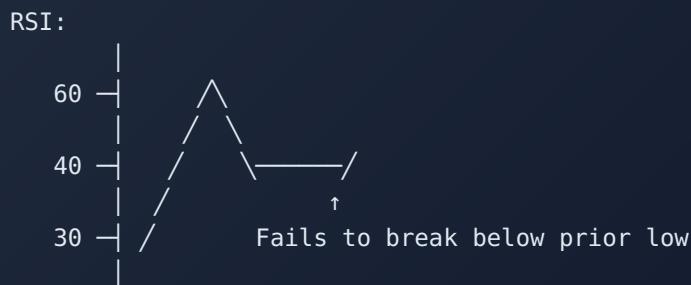
FACTOR	HIGHER QUALITY	LOWER QUALITY
Swing count	3+ swings	2 swings
Time span	10+ bars	3-5 bars
Extremes	At 30/70+	At 40-60
Trend context	Counter-trend	With-trend

Part 5: RSI Failure Swings

What Is a Failure Swing?

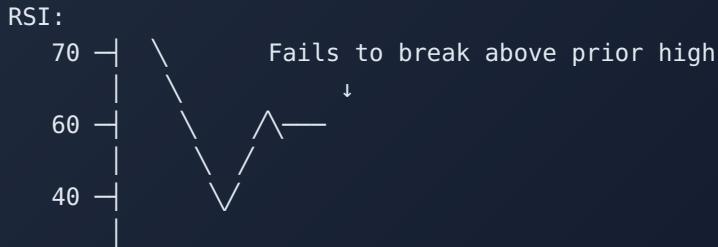
RSI breaks a support/resistance level without price confirming.

Bullish Failure Swing



Interpretation: RSI refuses to make new low = bullish signal.

Bearish Failure Swing



Interpretation: RSI refuses to make new high = bearish signal.

Trading Failure Swings

1. Identify the initial RSI extreme
2. Wait for pullback
3. Watch if RSI fails to make new extreme
4. Enter on the failure confirmation
5. Stop beyond recent price extreme

Part 6: RSI Midline (50)

The Importance of 50

RSI 50 is not just a number—it's a battleground.

Above 50: Bulls in control **Below 50:** Bears in control **At 50:** Neutral, decision point

Midline as Support/Resistance

In uptrends: - RSI 50 acts as support - Pullbacks often bounce off 50 - Break below 50 = Warning

In downtrends: - RSI 50 acts as resistance - Rallies often reject at 50 - Break above 50 = Warning

Trading the Midline

Bullish setup: 1. Uptrend established 2. RSI pulls back to 50 3. RSI bounces from 50 4. Enter long 5. Stop if RSI closes below 45

Bearish setup: 1. Downtrend established 2. RSI rallies to 50 3. RSI rejects from 50 4. Enter short 5. Stop if RSI closes above 55

Part 7: Multi-Timeframe RSI

Why Multi-TF Matters

Lower TF RSI can be noisy. Higher TF RSI provides context.

Alignment Strategy

Best signals occur when: - Higher TF RSI supports direction - Lower TF RSI gives entry

Example: - Daily RSI: Above 50, rising (bullish bias) - 4H RSI: Pulls back to 40 - 1H RSI: Shows bullish divergence - = Strong buy signal

Avoiding Conflicts

Avoid: - Daily RSI overbought + trying to buy 1H oversold - Daily RSI oversold + trying to short 1H overbought

Part 8: RSI with Other Indicators

RSI + Pentarch

PENTARCH SIGNAL	RSI CONFIRMATION
TD	RSI oversold (30-40) or bullish divergence
IGN	RSI crossing above 50
WRN	RSI overbought (60-70) or bearish divergence
CAP	RSI extremely overbought (80+)
BDN	RSI crossing below 50

RSI + Price Action

PRICE PATTERN	RSI CONFIRMATION
Double bottom	RSI bullish divergence
Double top	RSI bearish divergence
Breakout	RSI above 50, preferably 60+
Breakdown	RSI below 50, preferably 40-

RSI + Volume

RSI PATTERN	VOLUME CONFIRMATION
RSI at extreme	High volume = valid signal
RSI divergence	Volume supporting reversal
RSI at 50	Watch for volume on break

Part 9: RSI Settings

Standard Settings

SETTING	DEFAULT	ALTERNATIVE USES
Period	14	7-21 range
Overbought	70	80 for strong trends
Oversold	30	20 for strong trends

Adjusting for Timeframe

TIMEFRAME	RSI PERIOD	LEVELS
1m-5m	9-10	80/20
15m-1H	14	70/30
4H-Daily	14-21	70/30
Weekly+	14	70/30

Adjusting for Volatility

VOLATILITY	RSI PERIOD	NOTES
High (crypto)	10-12	More responsive
Normal	14	Standard
Low	16-21	Smoother

Part 10: Common RSI Mistakes

Mistake 1: Shorting Overbought

The trap:

"RSI is at 75, I should short."
RSI stays at 70-80 for weeks as price doubles.

The fix: - In uptrends, RSI 70 is not a short signal - Wait for bearish divergence or trend break - Or use RSI 80 pullback to enter long

Mistake 2: Buying Oversold in Downtrend

The trap:

"RSI is at 25, must be a bottom."
RSI stays at 20-30 for weeks as price halves.

The fix: - In downtrends, RSI 30 is not a buy signal - Wait for bullish divergence or trend break - Or use RSI 20 bounce to enter short

Mistake 3: Ignoring Trend Context

The trap: - Using 30/70 in all conditions - Ignoring that ranges shift with trend

The fix: - Identify the trend first - Adjust RSI interpretation accordingly - 40-80 range for uptrends, 20-60 for downtrends

Mistake 4: Trading Every Divergence

The trap: - Divergence appears, immediately trade - Price continues against you

The fix: - Divergence is a warning, not a signal - Wait for price confirmation - Use other indicators for confluence

Part 11: RSI Decision Tree

Step 1: Identify the Trend

Is price above 50-period MA and making HH/HL?

- Yes: Uptrend (use bullish RSI rules)
- No: Continue to Step 1b

Is price below 50-period MA and making LH/LL?

- Yes: Downtrend (use bearish RSI rules)
- No: Range (use traditional 30/70)

Step 2: Apply Regime-Appropriate Rules

Uptrend: - Buy at RSI 40-50 (support zone) - Take profit at RSI 70-80 - RSI below 40 = Trend may be ending

Downtrend: - Short at RSI 50-60 (resistance zone) - Take profit at RSI 20-30 - RSI above 60 = Trend may be ending

Range: - Buy at RSI 30 with confirmation - Sell at RSI 70 with confirmation - Look for mean reversion

Part 12: RSI Checklist

Before Trading RSI

- [] What is the trend? (Up/Down/Range)
- [] What is the appropriate RSI range for this trend?
- [] Is RSI at an extreme for this regime?
- [] Any divergence present?

- [] What does higher TF RSI show?

At Entry

- [] RSI supports the trade direction
- [] Price confirmation present
- [] Other indicators align
- [] Position sized appropriately

During Trade

- [] Watch for RSI divergence against position
- [] Note RSI midline (50) reactions
- [] Monitor higher TF RSI trend

Part 13: Summary

Core Principles

- 1. Context determines interpretation** — Trend regime matters
- 2. Ranges shift with trends** — 40-80 bull, 20-60 bear
- 3. 50 is a key level** — Support in uptrend, resistance in down
- 4. Divergence is a warning** — Not a trading signal alone
- 5. Multi-TF adds clarity** — Higher TF provides bias
- 6. Overbought ≠ sell** — Oversold ≠ buy

The RSI Mindset

Old: "RSI 30 = Buy"
New: "RSI 30 in downtrend = Not a buy"

Old: "RSI 70 = Sell"
New: "RSI 70 in uptrend = Might go higher"

Old: "Divergence = Trade"
New: "Divergence = Get ready, wait for confirmation"

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