

Devoted to information and portfolio strategies for the high relative strength asset class

Relative Strength measures...

the price performance of a stock versus a market average or universe of stocks. A stock's relative strength can improve if it rises more than the market in an uptrend, or goes down less than the market in a downtrend.

Feature: Thought Process



We all know that waves are essential to surfing. The size of the waves are affected by a number of factors including the strength of the wind, pressure systems, the contour of the reef or sand bank, and tide variations. Should a surfer worry that waves will cease to exist in the future? Probably not. Likewise, market trends are essential to relative strength strategies (tight, choppy markets lead to whipsaws and underperformance of relative strength strategies, while markets with strong trends generally lead to outperformance.)

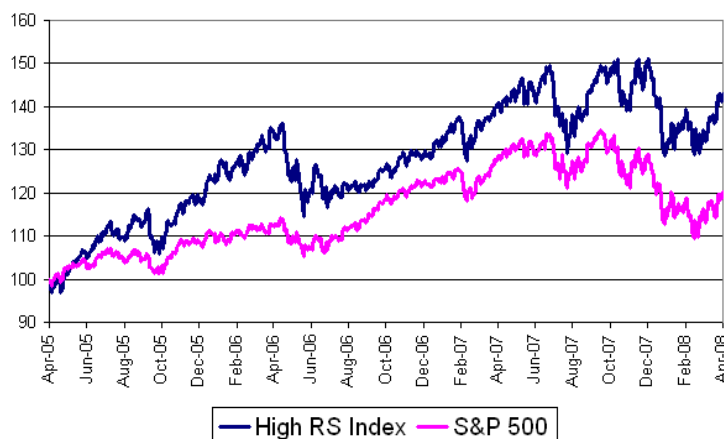
When we present our relative strength strategies, we often discuss a simple relative strength model published by Dr. Ken French of Dartmouth University. His simple relative strength model has had an average annual return of 21.14% over the last 80 years while the overall market has had an average annual return of 12.01% (<http://tinyurl.com/2szql6>.)

It is clear that a relative strength strategy **has** worked extremely well in the past. But, **will it continue** to work in the future? We believe market trends and ocean waves are about equally likely to cease to exist in the future.

High RS Asset Class:

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 4/25/08:

High RS Index vs. S&P 500



"High RS Index" is a proprietary Dorsey, Wright Index composed of stocks that meet a high level of relative strength. The volatility of this index may be different than any product managed by Dorsey, Wright. The "High RS Index" does not represent the results of actual trading. Clients may have investment results different than the results portrayed in this index.

Sector & Capitalization Snapshot

As of 4/25/08

Sector Performance

S&P 500	GICS Sector	12 Month	6 Month	1 Month
	Energy	26.34%	7.17%	13.32%
	Materials	12.10%	4.01%	7.70%
	Industrials	2.21%	-5.69%	0.79%
	Consumer Staples	2.09%	-0.77%	-0.71%
	Technology	0.57%	-10.67%	4.21%
	Utilities	-5.06%	-1.78%	7.11%
	Telecommunications	-11.24%	-15.45%	2.30%
	Health Care	-12.33%	-10.46%	0.79%
	Consumer Discretionary	-18.66%	-10.49%	0.30%
	Financials	-27.90%	-17.72%	1.19%

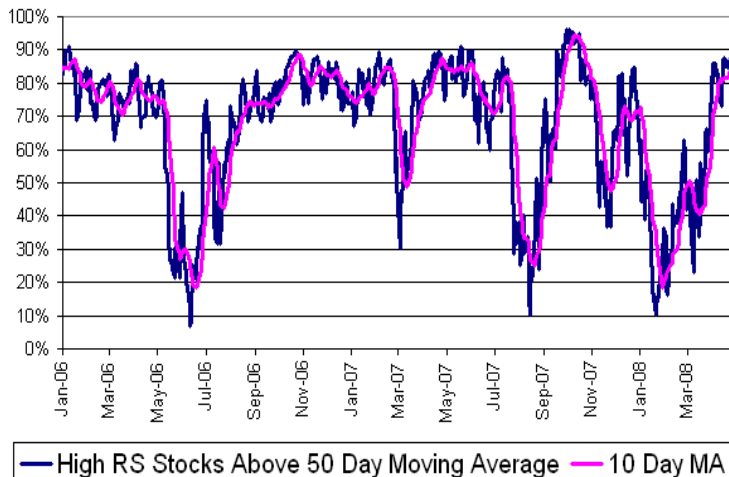
Performance by Capitalization

S&P Mid-Cap	-4.84%	-5.08%	6.50%
S&P Large-Cap	-6.61%	-8.06%	3.52%
S&P Small-Cap	-11.01%	-9.27%	1.96%

High RS Diffusion Index

As of 4/25/08

High RS Diffusion Index

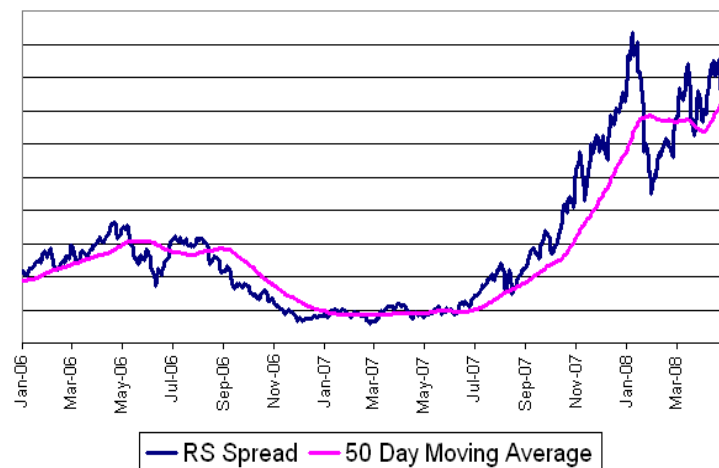


The 10 Day Moving Average of this Diffusion Index is now at 83 percent after seeing a low of 18 percent in late January of this year. It is not uncommon to see this indicator spike off the bottom, rally (as it has) and then remain extended during a sustained move in high relative strength stocks.

RS Spread

The chart below is the spread between the relative strength leaders and relative strength laggards (universe of mid and large cap stocks). When the chart is rising, relative strength leaders are performing better than relative strength laggards. As of 4/25/08:

Relative Strength Spread



RS leaders have regained their footing, after lagging in January, and the spread is now rising above its 50 day moving average.

Next Stop for Assets in Money Market Funds

Financial news over the past year has been heavy with news of write-downs and earnings declines of many large financial institutions and fear of impending recession. As investors are famous for doing, many have responded to the perceived risks by doing what seems to be the safe thing — they have sold risky assets and parked the money in money market funds. Sure, they are only earning a return on their money that is less than inflation, but it is the prudent thing to do, right? According to data recently presented by Louis Navellier, the amount of money invested in money market funds as a percentage of the total amount of money invested in the Wilshire 5000 Index, reached 26% at the end March of this year (*Navellier, April 2008.*) Last time this percentage was this high was early 2003, just as the United States was invading Iraq. As we all know, the stock market rallied strongly from that point. This is just one of the more recent examples of how many investors are the most bearish at just the time when they should be the most bullish.

I don't believe that all those investors who have poured money into money market funds will be content with those meager returns for an extended period of time. I wonder where that money will eventually find a home. Here are the obvious alternatives:

Real Estate: Over the past 10 years, real estate investors have been handsomely rewarded, at least until real estate prices began declining sometime in mid 2006. Given that real estate rapidly increased in value for nearly 10 years, followed by a relatively short correction, I think it likely that the money parked in money market funds will not rapidly return to this area.




Fixed Income: The 10-Year Treasury Note is currently yielding 3.86%, near record low yields. Again, I have trouble seeing investors remaining excited about this small of a yield.

Equities: This asset class is always the safe bet for attracting investor money as no other asset class has provided returns close to equities for long-term investors. Furthermore, given the unappealing prospects in real estate and fixed income, I think this is the likely destination for the hoards of money currently parked on the sidelines.

Investor Sentiment

The American Association of Individual Investors (AAII) is a non-profit association of more than 150,000 members. AAII produces a weekly sentiment survey of its members that measures the percentage of individual investors who are bullish, bearish and neutral on the stock market in the short term.

Results as of 4/23/08:

	4/23/2008 Results	Long-Term Average
Bullish 	46.67%	39%
Neutral 	25.83%	32%
Bearish 	27.50%	29%

For the first time this year, the percentage of bears are below the long-term average of 29%. Apparently, individual investors have recovered from believing "the end is nigh" as they thought at the end of January when nearly 60 percent were bearish. Not surprisingly, the market has since shown signs of stabilization and is now off the lows seen this year.

Other RS Sources

Relative Strength investing has a long history of well-documented testing. Some of the best known resources in the area are:

What Works On Wall Street, James P. O'Shaughnessy, McGraw Hill, 1997.

Earnings Growth, P/Es and Relative Price Strength, Robert A. Levy and Speros L. Kripotos, Financial Analysts Journal, 1967

Eight Relative Strength Models Compared, John S. Brush, Journal of Portfolio Management, 1986.

Momentum Strategies, Louis K.C. Chan, Narasimhan Jegadeesh, and Josef Lakonishok, Journal of Finance, 1996.

Media Center

Powershares DWA Technical Leaders ETFs (PDP, PIE, and PIZ)

- PowerShares Technical Fund Delivers on Promise, *TheStreet.com*, April, 24 2008
<http://tinyurl.com/3wnbxb>
- Concept ETFs provide Portfolio Stability
Seeking Alpha, April 23, 2008
<http://tinyurl.com/52qdt5>
- Powershares to Expand Family of DWA Technical Leaders Portfolios, *Yahoo! Finance*, Dec 21, 2007
<http://tinyurl.com/37cay2>

Arrow DWA Balanced Fund (DWAFX)

- Arrow DWA Balanced Fund Hits \$100 Million in Assets, *Marketwire*, September 11, 2007
<http://tinyurl.com/336e6u>

Dorsey Wright Money Management

- Can Relative Strength Be Used in Portfolio Management?, *Technical Analysis of Stock & Commodities*, Sep 2005
<http://tinyurl.com/38ooq3>
- Systematic Relative Strength Investment, *The Wall Street Transcript*, April 21, 2008
<http://tinyurl.com/2m7cls>

To Request Info

To request information about our Systematic Relative Strength accounts, please call us at 626-535-0630, or e-mail us at moneymanagement@dorseywright.com

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