

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



“Whether the question is what to do with an empty popcorn box in a movie theater, how fast to drive on a certain stretch of highway, or how to eat the chicken at a dinner party, the actions of those around us will be important in defining the answer.”

--Robert B. Cialdini, Ph.D., Influence

Information cascade is a term used to describe the tendency of people to be influenced by actions of other. Consider its effect on the dismantling of the Berlin Wall:

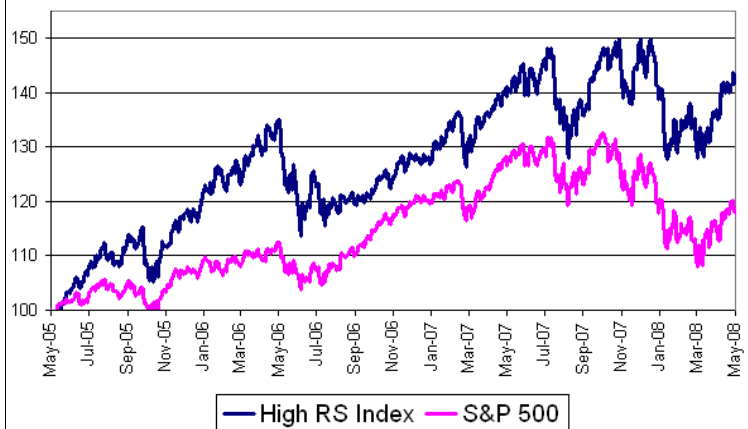
Small protests began in Leipzig, Germany in 1989 with just a handful of activists challenging the German Democratic Republic. For almost a year, protesters met every Monday growing by a few people each time. By the time the government attempted to address it in September of 1989, it was too big to squash. In October, the number of protesters reached 100,000 and by the first Monday in November, over 4,000,000 people marched the streets of Leipzig. Two days later the Berlin Wall was dismantled.

Information cascading is also a big factor in causing long-term price trends. Relative Strength is simply a disciplined way of identifying the strongest of those trends.

High RS Asset Class:

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 5/9/08:

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 5/9/08

Sector Performance

S&P 500 GICS Sector	12 Month	6 Month	1 Month
Energy	26.25%	11.16%	6.43%
Materials	9.28%	4.99%	2.26%
Consumer Staples	2.39%	-0.91%	-1.07%
Technology	-0.12%	-4.57%	7.26%
Industrials	-1.45%	-3.15%	0.14%
Utilities	-5.48%	-4.38%	1.24%
Telecommunications	-12.48%	-9.28%	4.93%
Health Care	-14.39%	-9.91%	-1.02%
Consumer Discretionary	-18.63%	-5.34%	3.24%
Financials	-31.68%	-14.48%	0.76%

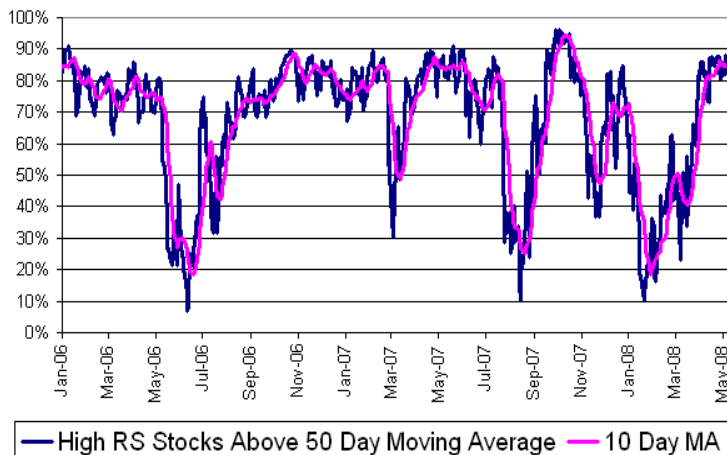
Performance by Capitalization

S&P Mid-Cap	-5.05%	-0.84%	5.90%
S&P Large-Cap	-8.11%	-4.30%	2.26%
S&P Small-Cap	-12.47%	-5.13%	2.57%

High RS Diffusion Index

As of 5/9/08

High RS Diffusion Index

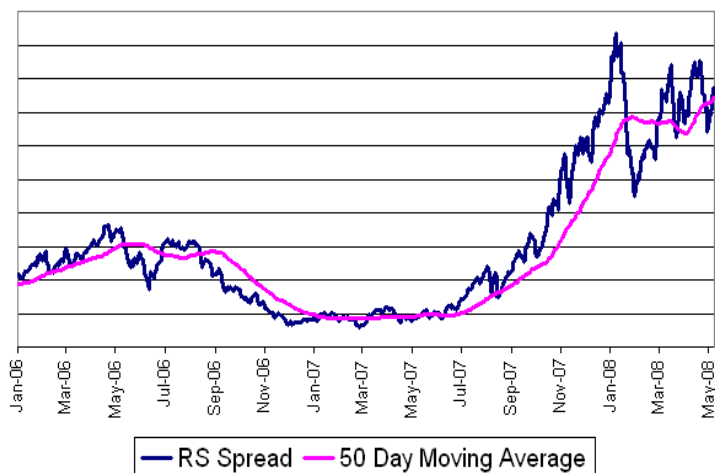


The 10 Day Moving Average of this Diffusion Index is now at 84 percent after seeing a low of 18 percent in late January of this year. It is not uncommon to see this indicator spike off the bottom, rally (as it has) and then remain extended during a sustained move in high relative strength stocks.

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 5/9/08:

Relative Strength Spread



RS leaders and RS laggards have each had their day in the sun (and the doghouse) so far this year. The RS Spread has now risen above its 50 Day Moving Average.

What Is Driving Crude Oil?

Now that the price of a barrel of oil is over \$120, oil is dominating the news. There are discussions about whether the price of oil is being driven by the falling world supply (known as "Peak Oil Theory") which is the idea that world oil production is now past peak production or whether it is being driven by speculation as a result of the development of unregulated international derivatives trading in oil futures over the past decade.

The US Senate even assigned a subcommittee to investigate! In a June 2006 US Senate Permanent Subcommittee on Investigations report on "The Role of Market Speculation in rising oil and gas prices" noted, "...there is substantial evidence supporting the conclusion that the large amount of speculation in the current market has significantly increased prices."

From an investor's perspective, does it really matter what is driving the price of oil? What is more important is to make sure that you are participating. Many portfolio managers who employ fundamental analysis often get hung up on where the market price of a security or commodity *should* be. Some never seem to get over the fact that markets rarely ever match the pure fundamentals.




Any relative strength strategy has likely had large exposure to the Energy sector for much of this decade. While there have been numerous corrections along the way, the overall trend has been decidedly higher. Crude oil is up over 500% this decade and the shares of many Energy companies are up more than that.

It actually takes a certain level of humility to embrace a relative strength strategy. We also have opinions about how things *should* be. But, those opinions will not impact the execution of our strategy. Strong relative strength is currently found largely in Energy, Basic Materials, and Industrials (and not in Financials and Consumer Cyclicals.) At some point, that trend will change. Perhaps that change will be next month. Perhaps that change will be in 2014. Relative Strength excels by forcing you to stay with the long-term trends—which always seem to go much longer than many think. Again, more important than a complete understanding of all the reasons for a trend is an organized way to participate in those trends.

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 5/7/08:

	5/7/2008 Results	Long-Term Average
Bullish 	52.81%	39%
Neutral 	22.47%	32%
Bearish 	24.72%	29%

Individual investors appear to now be less concerned that the credit crisis will continue to weigh on the stock market. The percentage of bulls are now above their long-term average and the percentage of bears are below their long-term average.

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 (DWA FX)

- 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

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