

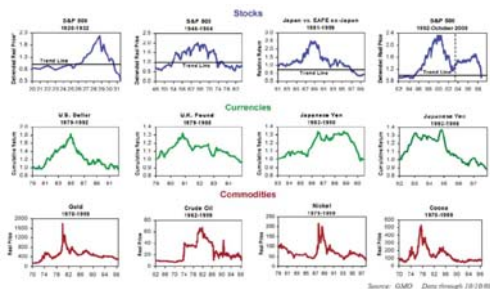
Devoted to information and portfolio strategies for the high relative strength asset class

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.

Anatomy of a Bubble

One characteristic of bubbles that lends itself to being exploited by trend-following methodologies is that bubbles generally unfold over the span of several years or more. This can be seen in the charts below of bubbles in various stock, currency, and commodity markets. These dynamic moves gain speed and often spike higher in the final year or two of the move before they begin their descent. **Trend-following strategies, like relative strength, are designed to start participating early enough in the move that the money made during the ascent more than compensates for the losses experienced during the trend deterioration phase.** Once the change in trend has become sufficiently apparent, trend-following strategies exit the trade and begin the search for the next dynamic move.



(Click to Enlarge)

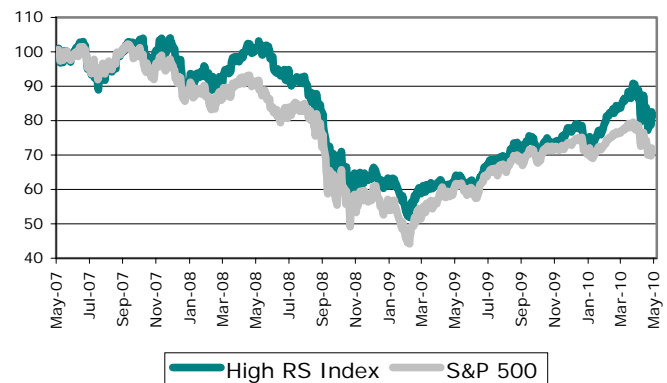
Source: James Montier, GMO Asset Management

The advantage of a global tactical asset allocation strategy is its ability to seek out dynamic trends in a wide variety of asset classes and **thereby increasing the probabilities of more consistent returns.**

High RS Asset Class

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 5/28/2010:

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 5/28/2010

Sector Performance

S&P 500	GICS Sector	12 Month	6 Month	1 Month
	Consumer Discretionary	42%	13%	-7%
	Industrials	33%	7%	-10%
	Technology	29%	0%	-9%
	Financials	22%	3%	-9%
	Materials	18%	-5%	-10%
	Consumer Staples	15%	-3%	-5%
	Health Care	13%	-7%	-7%
	Utilities	8%	-3%	-6%
	Energy	2%	-9%	-13%
	Telecommunications	0%	-7%	-4%

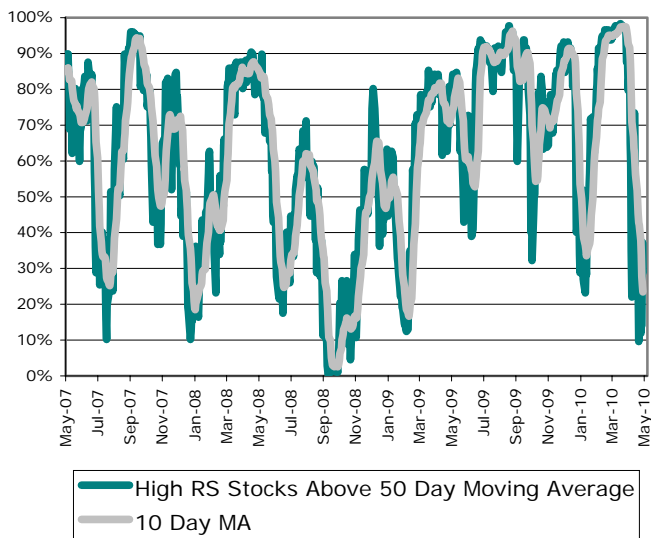
Capitalization Performance

S&P Small-Cap	36%	16%	-8%
S&P Mid-Cap	35%	12%	-8%
S&P Large-Cap	20%	0%	-8%

High RS Diffusion Index

As of 5/28/2010

High RS Diffusion Index

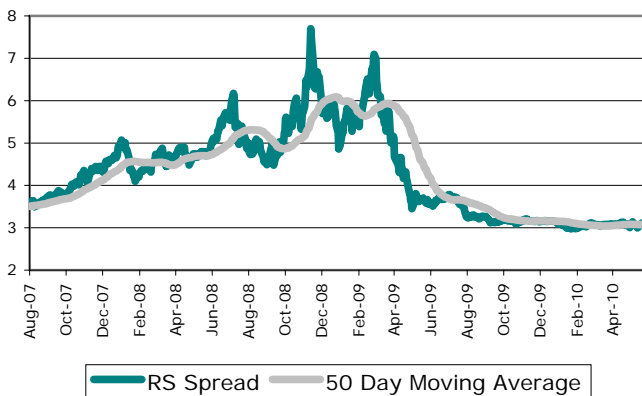


The 10-day moving average of this indicator is 23% and the one-day reading is 29% after reaching a single-day low of 10% on 5/20/10. Dips in this indicator have often provided good opportunities to add to relative strength strategies.

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 5/28/2010:

Relative Strength Spread



The sharp decline in the RS Spread during much of the first half of 2009 has transitioned into a flat spread, which may be setting the stage for a more favorable environment for RS investing.

What Explains the Difference?

What explains the difference between the calm investor and the scared investor?

With the market correction of the last month has come dramatically rising fear levels among individual investors. Case in point, the [5/27 AAI Sentiment Survey](#) reveals that over 50% of individual investors are now bearish. There are only a small number of times in the 23-year history of this particular sentiment survey when there has been more bearish sentiment than now. Surely, a large part of the fear comes from the realization that many have not adequately prepared for the possibility of bear markets. Proper preparation comes from constructing an asset allocation with an appropriate amount of the portfolio dedicated to strategies with strong risk management characteristics. Historically, only about twenty-five percent of 10 percent corrections turn into a 20+ percent bear market so it is quite possible that what we are experiencing now is simply a correction. **However, that doesn't change the fact that investors need to have that strong risk management component of their asset allocation in order to be able to have the intestinal fortitude to stay in the game through all the 10 percent corrections.** Seeking to be adequately prepared for the worst is the very reason that we have included inverse equities in the investment universe for our Global Macro portfolio. It is with this same logic that Ronald Reagan argued in 1984 for a strong national defense. Consider his famous "Bear in the woods" commercial. Click [here](#) to view. The text of the commercial is as follows:

There's a bear in the woods. For some people, the bear is easy to see. Others don't see it at all. Some people say the bear is tame. Others say it's vicious and dangerous. Since no one can really be sure who's right, isn't it smart to be as strong as the bear? If there is a bear....

To watch a 15-minute presentation on how we incorporate inverse equities into our Global Macro strategy, click [here](#) and then click on "Global Macro Presentation" (Financial Professionals Only.) What explains the difference between the calm investor and the scared investor? The level of preparation.

Click [here](#) and [here](#) for disclosures. Past performance is no guarantee of future results.

Fund Flows

The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). Flow estimates are derived from data collected covering more than 95 percent of industry assets and are adjusted to represent industry totals. The table below is ranked in descending order based on flows for the week ending 5/19/2010.

Asset Class	5/19/2010
Municipal Bonds	913
Hybrid	391
Taxable Bonds	-729
Foreign Equity	-1,883
Domestic Equities	-4,794

The market correction over the last month has sent retail equity fund investors for the exits. Even taxable bonds saw minor outflows for the week ending 5/19.

Other RS Sources

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

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

Berger, Israel, Moskowitz. "The Case for Momentum Investing." AQR Capital Management. 2009.

Jegadeesh and Titman. "Returns to Buying Winners and Selling Losers." Journal of Finance (1993).

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

Media Center

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

- [Four Alpha-Seeking ETFs Crushing SPY, ETFdb](#), Apr 30, 2010
- [Under the Microscope: Powershares DWA Technical Leaders ETF, Seeking Alpha](#), Mar 31, 2010

Arrow DWA Balanced Fund (DWAFFX)

- [The Endowment Portfolio Rides Again](#), Mar 12, 2010

Arrow DWA Tactical Fund (DWTFFX)

- [Core-and-Satellite](#), May 3, 2010

Dorsey Wright Money Management

- [Bringing Real-World Testing To Relative Strength](#), Jan 2010
- [Relative Strength and Asset Class Rotation](#), Mar 2010

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