

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.

Good vs. Best

Relative Strength is just that--a method of measuring strength not in absolute terms, but in relative terms. It is one thing to attempt to assign an intrinsic value to a given security in isolation and another thing entirely to assign a relative value, or relative rank, within the context of a universe of securities.

I am reminded of a [line from the film Crocodile Dundee](#), when a street hoodlum pulls a switchblade against our hero, Paul Hogan. "You call that a knife?" says Hogan incredulously, withdrawing a bowie blade from the back of his boot. "Now *this*," he says with a sly grin, "is a knife."

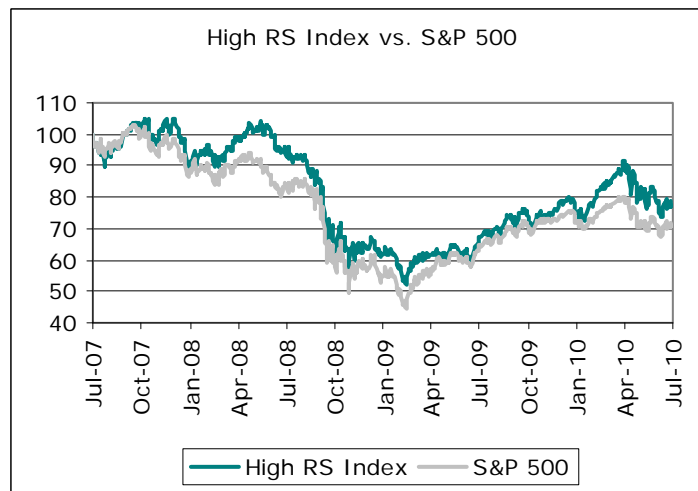
One of the biggest challenges for an investor is to be able to make the best use of limited resources. After all, the value of every investment portfolio is finite. How can you be sure that you are allocating your finite resources to those securities that represent the "best" investment opportunities and not just "good" or "acceptable" investment opportunities?

The elegance of systematic relative strength models is that all securities in the investment universe are evaluated relative to *every* other security in the investment universe. With this knowledge you can be sure that each of the final holdings has superior relative strength characteristics and, therefore, gives you the [best probabilities of successful investment results](#).

HT: Dan Ariely, *Predictably Irrational*

High RS Asset Class

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 7/22/2010:



"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

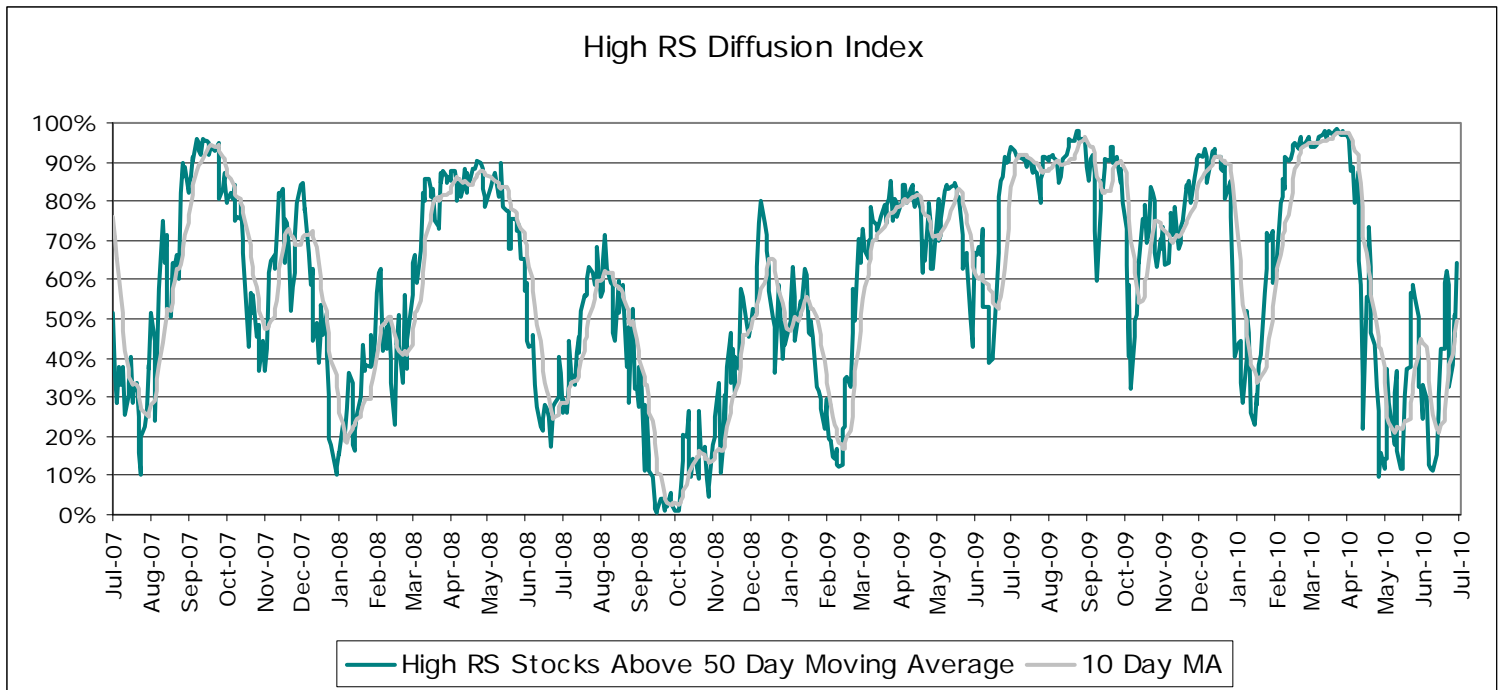
As of 7/22/2010

Sector Performance			
S&P 500 GICS Sector	12 Month	6 Month	1 Month
Industrials	29%	5%	0%
Consumer Discretionary	27%	7%	-1%
Financials	19%	2%	-1%
Technology	15%	1%	0%
Materials	15%	0%	3%
Consumer Staples	12%	2%	2%
Utilities	7%	2%	4%
Health Care	6%	-10%	-3%
Energy	5%	-5%	-1%
Telecommunications	4%	2%	1%

Performance by Capitalization			
S&P Mid-Cap	12 Month	6 Month	1 Month
S&P Mid-Cap	25%	4%	0%
S&P Small-Cap	22%	4%	-1%
S&P Large-Cap	15%	0%	0%

High RS Diffusion Index

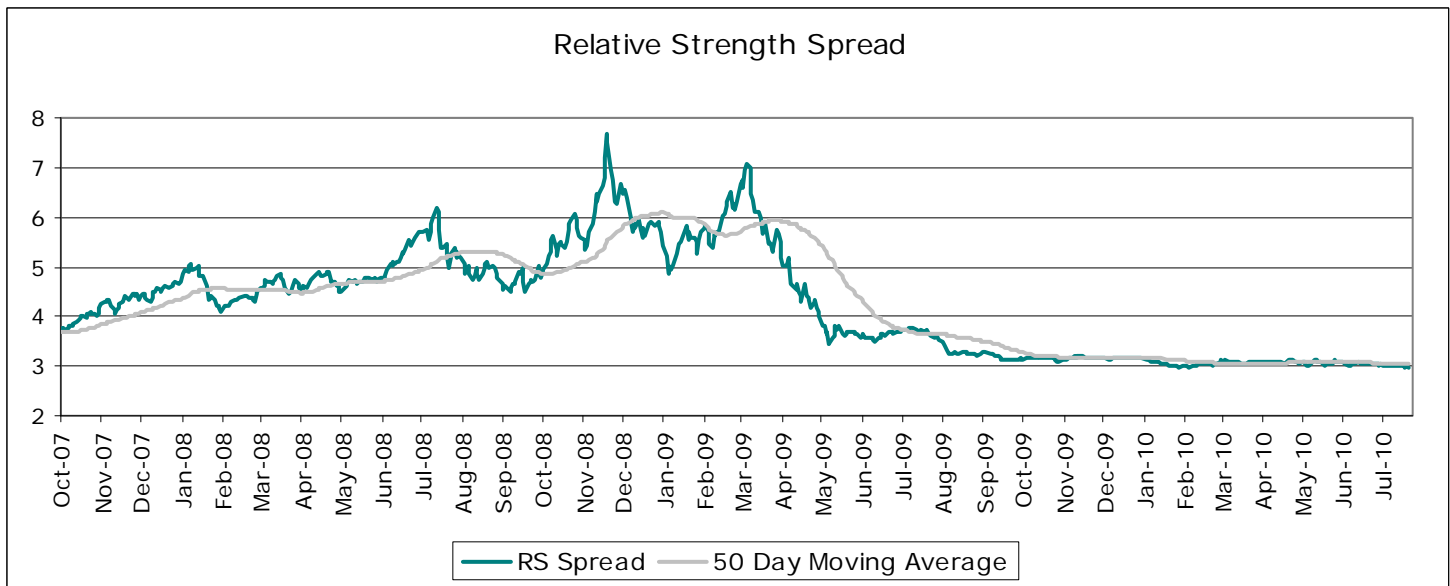
As of 7/22/2010



The 10-day moving average of this indicator is 50% and the one-day reading has now risen to 64% after spending the last two months in deeply oversold territory. 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 7/22/2010:



No change this week—or for much of the past year for this indicator. The relative strength spread continues to reflect the fact that neither the relative strength leaders nor the relative strength laggards have been able to pull away. For now, both groups continue to generate similar performance.

The Next Shoe To Drop? Perhaps Not.

For months, the talk about commercial real estate centered around the fear that this could be "the next shoe to drop." With that backdrop, I was surprised to come across Jeff Fox's recent article [Commerical Real Estate's Death Knell May Have Been Premature](#).

In the face of some otherwise-daunting obstacles, commercial real estate is proving to be an attractive area for investors looking for bargains as loans come due and foreclosures mount.

Analysts have been warning for months that commercial real estate could be the next shoe to drop in the subprime mortgage collapse that came to a head in 2008.

*But with signs of thawing in the securitization markets and indications that investors are ready to come to auction when properties are on the block, **the idea that the industry represents a major looming danger for the economy is losing traction.***

Prudential Financial executives, speaking at a market outlook discussion Tuesday in New York, said they are "reluctant optimists" on the space. Marc Halle, the firm's managing director of real estate investments, compared the industry to a "fly wheel" that likely will accelerate in the years ahead.

"As it cranks up, it's going to start going pretty quickly in the next three, four years," he said. "We think the recovery is going to be very different this time."

Symbol	Last 12 months	YTD
ICF - iShares Cohen & Steers Realty Index	61.81%	12.05%
RWR - DJ Wilshire REIT	57.57%	10.40%
IYR - DJ U.S. Real Estate Index	51.19%	9.15%
S&P 500	14.63%	-1.92%

My emphasis added. At the time that we were buying commercial real estate ETFs in our Global Macro strategy in early 2010 articles like this were nowhere to be found. However, we bought it anyway because that what we do--buy and sell securities based solely on their relative strength. Performance in the table below is for the period 7/22/2009 - 7/22/2010 and YTD through 7/22/2010.

One of the realities of employing relative strength strategies is that we often buy and sell securities well before such action is being trumpeted in the main stream media. Waiting for the blessing of the main stream media before taking action is a recipe for disaster.

To receive the brochure for our Global Macro strategy, click [here](#). For information about the Arrow DWA Tactical Fund (DWTFX), click [here](#).

Click [here](#) and [here](#) for disclosures. ICF, IYR, RWR and other real estate securities are current holdings in products managed by Dorsey Wright Money Management. Past performance is no guarantee of future returns.

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 7/14/2010. *Millions of dollars*

	7/14/10	YTD
Taxable Bonds	5,381	144,547
Hybrid	430	12,572
Municipal Bonds	415	20,566
Foreign Equity	-113	26,496
Domestic Equity	-3,157	-23,094

The story of the year, in terms of asset flows, has been \$144 billion into taxable bond funds and \$23 billion out of domestic equity funds.

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 Arrow DWA Balanced Fund](#), Jun 17, 2010

Arrow DWA Tactical Fund (DWTAFX)

- [The "All-in-One Fund" With a Twist](#), Jun 16, 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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