

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.

Emerging Markets

While the dominant form of indexing remains cap-weighted-indexing (for now), companies like PowerShares have revolutionized the concept of indexing by bringing to market a number of ETFs based on alternatively-weighted indexes.

Among those ETFs currently in the market that offer an alternative approach to weighting an index is our own line-up of relative strength-weighted *Technical Leaders ETFs* (PDP, PIE, and PIZ)—all of which are performing very well in 2010.

In particular, the PowerShares DWA Emerging Markets Technical Leaders ETF (PIE) is well ahead of its benchmark this year.

YTD Performance (through 9/17/10)

PIE - PowerShares DWA Emerging Markets Technical Leaders ETF	14.12%
EEM - MSCI Emerging Markets ETF	3.66%

A review of the top country allocations for PIE provides insight into how it has been able to stand apart from its benchmark (large overweights in Malaysia, and Indonesia, while being underweight China).

Top Country Allocations

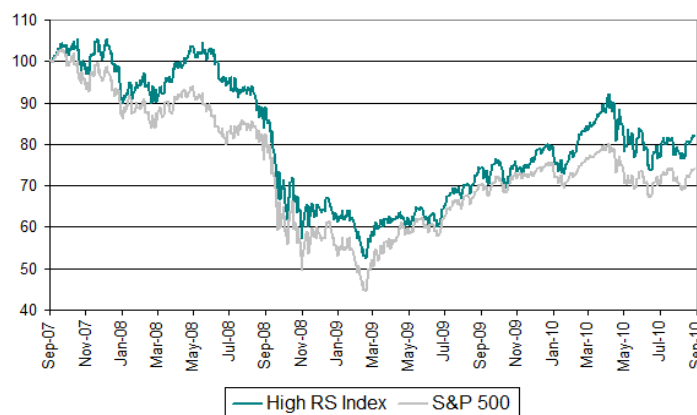
Country	PIE Weight	EEM Weight	YTD Performance (through 9/17/10)*
Malaysia	16.75%	2.91%	27.97%
South Korea	11.25%	13.09%	7.85%
Indonesia	10.85%	2.58%	35.89%
China	9.35%	18.36%	-0.71%

More information about PIE can be found at www.powershares.com.

High RS Asset Class

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 9/17/2010:

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 9/17/2010

Sector Performance

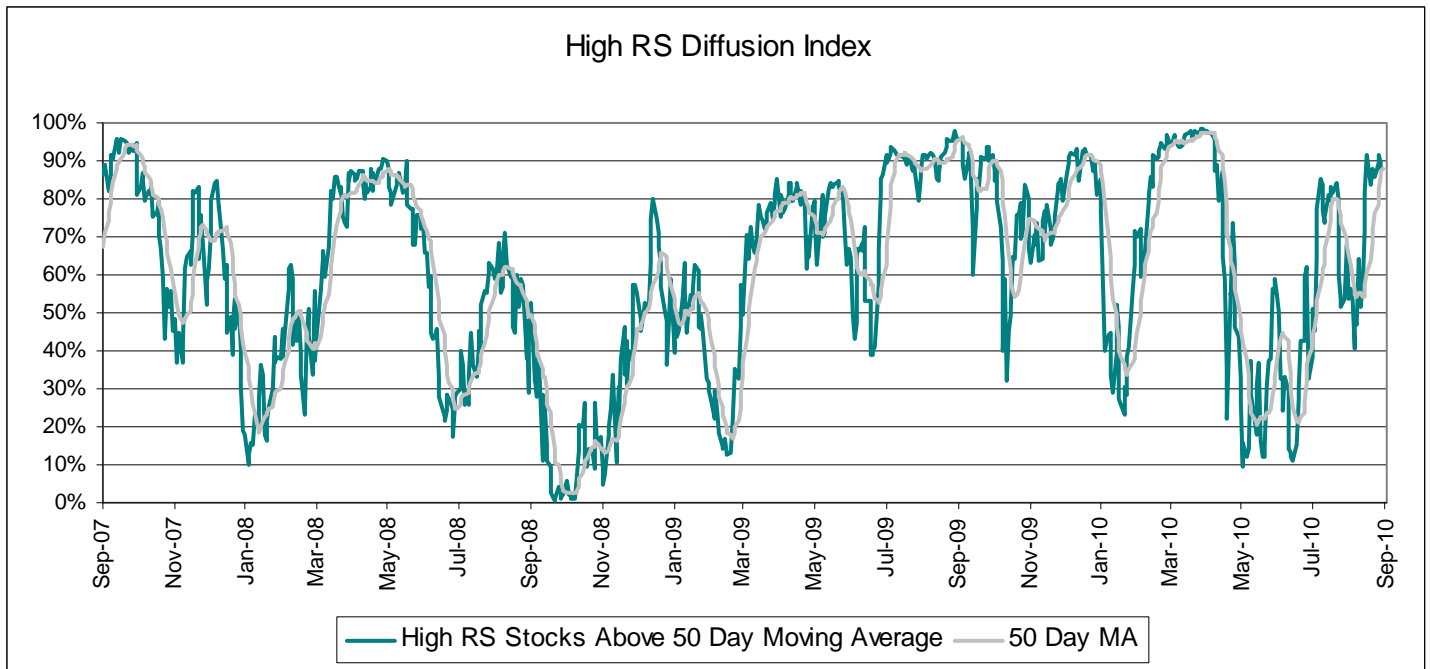
S&P 500 GICS Sector	12 Month	6 Month	1 Month
Consumer Discretionary	19%	1%	5%
Telecommunications	13%	11%	5%
Industrials	12%	-1%	3%
Consumer Staples	10%	-1%	3%
Technology	7%	-4%	5%
Materials	4%	-1%	4%
Utilities	4%	2%	0%
Health Care	4%	-7%	2%
Energy	-4%	-8%	0%
Financials	-4%	-8%	3%

Performance by Capitalization

S&P Mid-Cap	11%	-2%	4%
S&P Small-Cap	7%	-5%	4%
S&P Large-Cap	5%	-4%	3%

High RS Diffusion Index

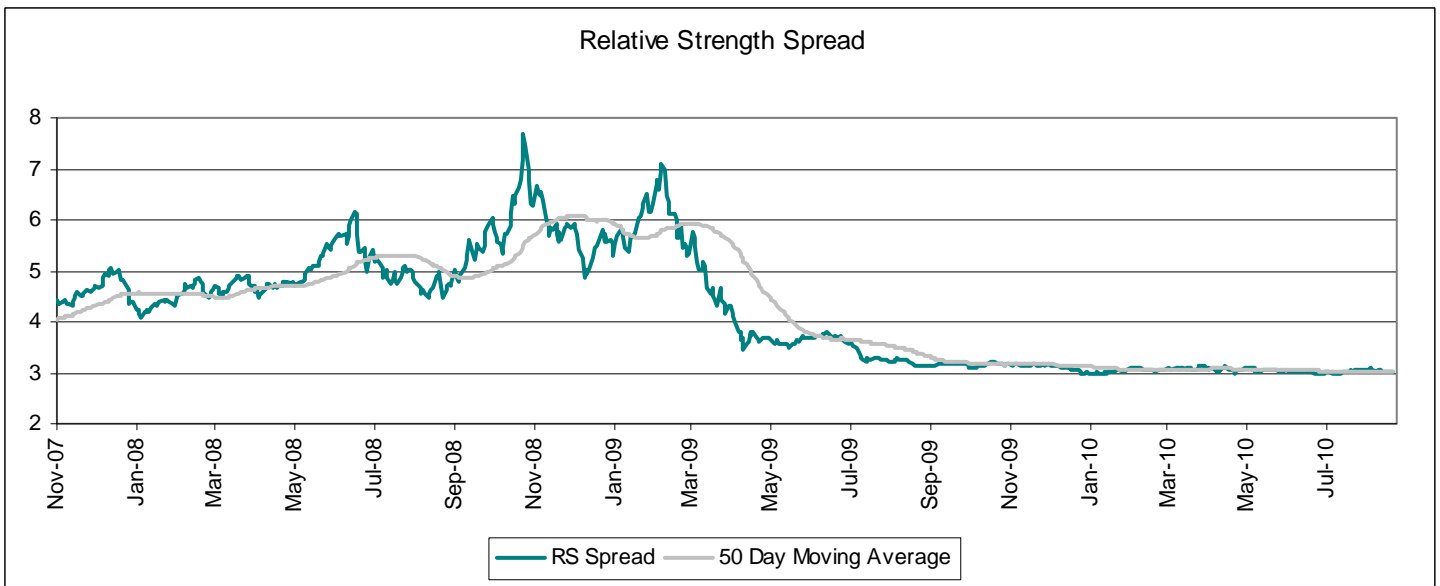
As of 9/17/2010



The 10-day moving average of this indicator is 88% and the one-day reading is also 88%. After pulling back to the middle of the distribution in August, this index has risen sharply in recent weeks.

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 9/17/2010:



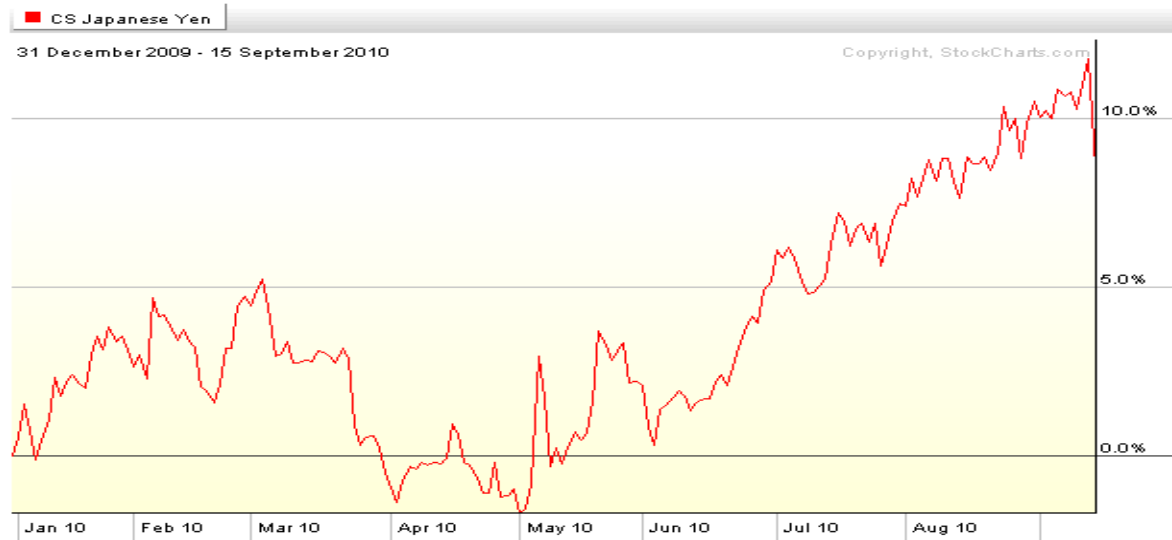
Over the past 12 months the relative strength spread has been pretty dull as both the relative strength leaders and laggards have generated similar performance. It is quite possible that the transition that we are seeing now could lead to an excellent environment for relative strength strategies.

Trend Following: Conceptually Simple, but Effective

Strong trends seem to always be surrounded by controversy. The current debate about the strength of the Japanese yen is no exception. The debate has become even more interesting over the past week as Japan has intervened in the currency markets in an attempt to halt the rise of the yen, which is causing problems for their export-reliant economy.

As shown in the chart below, the CurrencyShares Japanese Yen Trust (FXY) is currently +8.19% so far in 2010.

PerfChart: FXY



Source: StockCharts.com

Many of the arguments on both sides of the debate were summarized in a recent *Wall Street Journal* article, "[Bank of Japan's Maverick Move Not a Sure Bet](#)" on 9/16/2010.

It was noted that on Wednesday, 9/15, there was a wave of foreign-exchange market intervention by Japan estimated at \$20 billion which sent the dollar sharply higher against the yen. However, it was also noted that currency trading is now a daily \$4 trillion affair and that the daily trading in the dollar-yen market alone is now \$568 billion. **So, how much effect is the intervention of the Japanese government going to have in reversing the trend of their currency?**

Among the arguments for why the yen will continue to appreciate is the fact that [China is now buying Japanese bonds](#). Furthermore, last time Japan intervened in the currency markets in 2004 it pumped 35 trillion yen into the markets, or about \$320 billion in exchange rates at the time. In the end, intervention changed little, with the yen trading roughly where it did at the start of the operation. However, in 1995 when the yen hit a high of 79.75 against the dollar, Japan also intervened. Within a month the yen had weakened 8% and by the end of 1995 it had weakened 23%. Hmm, so there have been times when Japanese intervention seems to have been effective and times when it seemed to have little effect. **Which will it be this time?** There are many other factors at play, including the political pressure that Japan may receive from other members of the Group of Seven richest economies, of which Japan is a member, to refrain from currency intervention since nobody seems to want a strong currency.

This is just the another example of the complexity of issues surrounding strong trends. **Trying to trade them like you were judging a debate is likely to result in total frustration.** There are so many influences on the supply and demand relationship that it is nearly impossible to give adequate weight to each of the factors at play and then to properly manage the trade.

Trend followers take a much more pragmatic approach: **Stay with strong trends as long as they remain strong** and exit the trade when the trend sufficiently reverses. Simple, but effective.

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 9/8/2010. *Millions of dollars*

	9/8/10	YTD
Taxable Bonds	4,978	194,450
Foreign Equity	1,174	26,885
Municipal Bonds	756	29,343
Hybrid	565	12,811
Domestic Equity	-2,235	-52,826

The story of the year, in terms of asset flows, has been \$194 billion into taxable bond funds and \$52 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)

- [Time To Grab A Piece Of This PIE?](#), *Benzinga*, Sep 9, 2010
- [Four Alpha-Seeking ETFs Crushing SPY](#), *ETFdb*, Apr 30, 2010

Arrow DWA Balanced Fund (DWAFFX)

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

Arrow DWA Tactical Fund (DWTFX)

- [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

Blog

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