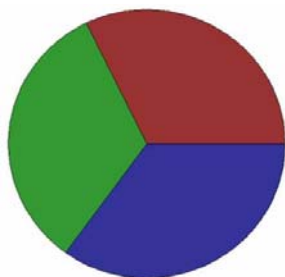


Devoted to information and portfolio strategies for the high relative strength asset class

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



Let every man divide his money into three parts, and invest a third in land, a third in business, and a third let him keep in reserve.

—Talmud

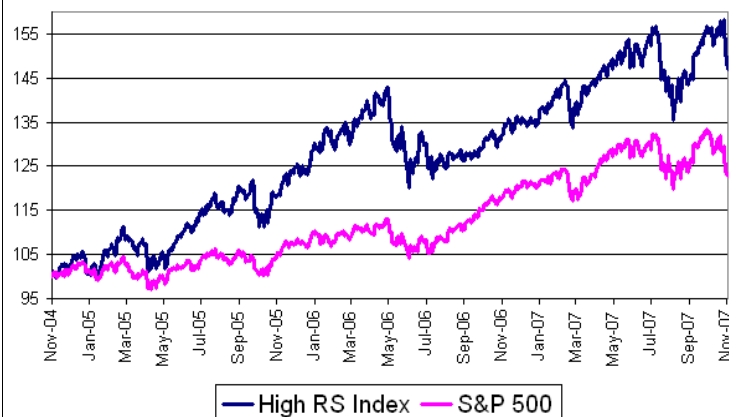
Circa 1200 B.C.-500 A.D.

The concept of asset allocation is not new, but it is certainly a key determinant of overall investment performance. Most people have a preference not just for high returns, but also for relatively stable returns. That is why creating an asset allocation of **high return, uncorrelated** investments is a prudent approach. For some, a 15 percent allocation to a high relative strength (RS) strategy is appropriate; for others, maybe an 80 percent allocation is appropriate. We believe **all** equity investors can benefit from making a RS strategy part of their allocation due to the tendency of RS returns to be dissimilar to the patterns of other investments. When implemented correctly, asset allocation gives investors the confidence to stick with each of their strategies for the long term (assuming the investor has reason to believe in the long-term viability of each of the components).

High RS Asset Class:

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 11/12/07:

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 11/12/07

Sector Performance

S&P 500 GICS Sector	12 Month	6 Month	1 Month
Energy	23.13%	9.20%	-8.03%
Materials	19.36%	1.17%	-7.53%
Utilities	14.87%	-2.45%	-0.60%
Telecommunications	11.78%	-4.80%	-8.33%
Industrials	11.25%	1.29%	-6.59%
Technology	10.73%	2.85%	-7.55%
Consumer Staples	10.46%	3.83%	-1.16%
Health Care	7.96%	-3.27%	-3.28%
Consumer Discretionary	-9.12%	-13.68%	-10.36%
Financials	-14.99%	-19.58%	-14.49%

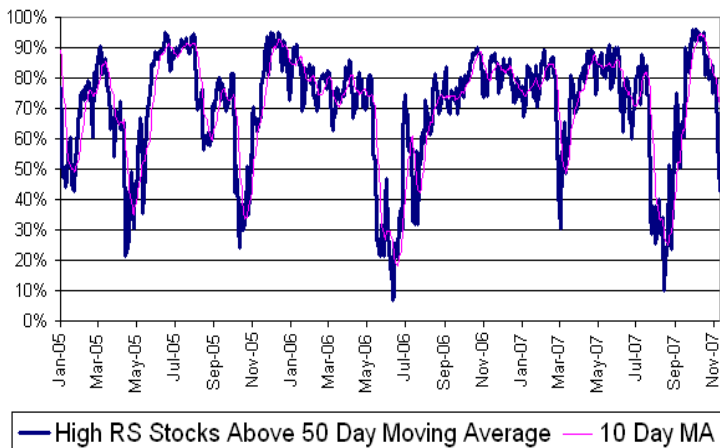
Performance by Capitalization

S&P Mid-Cap	5.94%	-5.48%	-7.41%
S&P Large-Cap	3.95%	-4.75%	-8.08%
S&P Small-Cap	1.28%	-7.87%	-9.57%

High RS Diffusion Index

As of 11/12/07

Dorsey Wright Diffusion Index

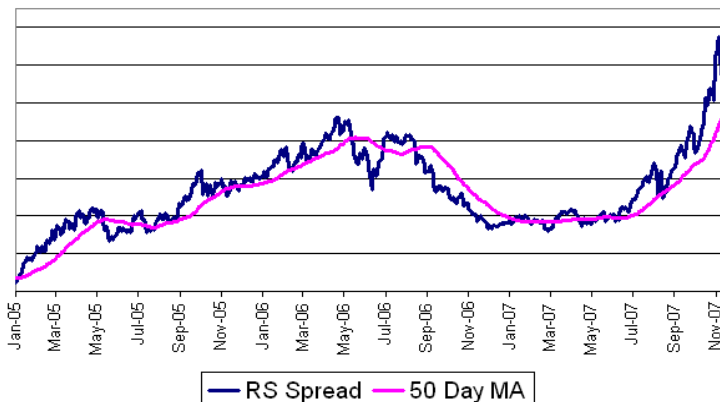


Currently, 43% of high relative strength stocks are trading above their 50 day moving average (down from 95% in early October). While we do not know whether we will see further deterioration from here, we do know that dips in this indicator have historically been good opportunities to add to relative 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. When investors are confident in market leadership, they continue to buy into strength and sell into weakness. When investors are risk averse, they tend to sell into strength and buy into weakness. As of 11/12/07

Relative Strength Spread



While the spread has pulled back some in recent days, the overall trend remains strongly in favor of RS leaders over RS laggards.




Playing the Probabilities

The next time you're watching a football game, pay attention for a situation where your team is on offense and it's fourth-and-1-or-2 somewhere around midfield. While the replay is on your screen, the announcers will spend a second or two discussing the possibility that they might go for it. You're not sure what's going to happen. When the TV cuts back to live action, you see the punter trotting onto the field. Seeing your team punt is the most likely outcome, but is it the optimal decision?

Such was the analysis of David Romer, an economist at the University of California, who concluded that football teams are far too conservative in play calling in fourth-down situations. His hunch about human behavior in general was that although people say they have a certain goal and are willing to do everything they can to achieve it, their actual behavior regularly departs from the optimal path to reach that goal. In his analysis of football teams, Romer concluded that, on average, teams that take the risk seem to win more often than lose. Data from a large number of NFL games show that coaches rarely follow what Romer's calculations predict would give them the best chance of victory (*Vedantam, Nov. 07*). His calculation suggest that teams should regularly be going for it on fourth down, even if it is early in the game, even if the score is tied, and even if the ball is on their own side of the field! Why do coaches persist in doing something less than optimal, when they say their only goal is to win? Romer suggested that coaches, like many stock fund managers, actually have different goals than the people they lead and the people they must answer to. Managers are held to different standards than followers when they lose, especially when they lose after trying something that few others are doing. For investment managers, this concept is typically manifested in an unwillingness to deviate too far from the benchmark, resulting in a large number of "closet indexers."

However, there are exceptions in football-New England Patriots coach Bill Belichick is among those who agree with Romer and happens to be one of the more successful coaches in the league. Likewise, systematic relative strength adherents will often differ from their peers and their benchmark, but we believe will also be able to generate superior performance over time.

Investor Sentiment

	11/7/2007 Results	Long-Term Average
Bullish 	36.19%	39%
Neutral 	12.38%	32%
Bearish 	51.43%	28%

The AAI Sentiment Survey measures the percentage of individual investors who are bullish, bearish, and neutral on the stock market short term; individuals are polled from the AAI web site on a weekly basis. Results as of 11/7/07.

Investor Sentiment among individual investors continues to deteriorate. The current bearish reading of 51.43% is the second highest bearish reading of the year (54.29% were bearish on May 3, 2007).

We find it useful to track the sentiment among individual investors because they tend to be wrong at the extremes.

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 ETF (PDP)

- New ETF follows trends based on technical factors, *MarketWatch*, Mar 2, 2007
<http://tinyurl.com/2qt6cd>

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

- Is a bottom in place?, *MarketWatch*, Aug 8, 2007
<http://tinyurl.com/3c6yoo>
- Can Relative Strength Be Used in Portfolio Management?, *Technical Analysis of Stock & Commodities*, Aug 2005
<http://tinyurl.com/38ooq3>
- Systematic Relative Strength Investment, *The Wall Street Transcript*, Jan 29, 2007
<http://tinyurl.com/2m7cls>

To Request Info

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