

*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**

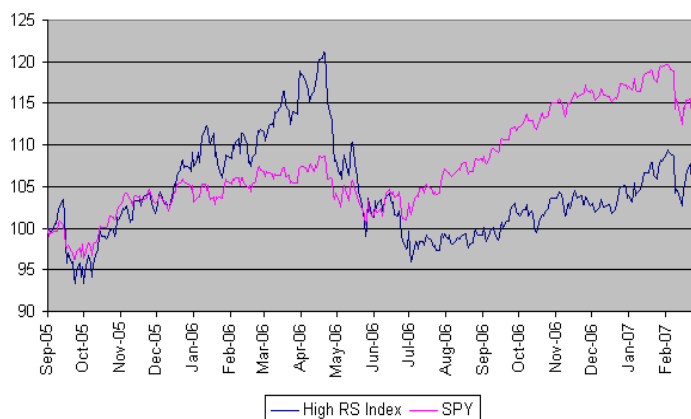


Pete Gardner, a race horse owner in Fairfield, Kentucky, had some decisions to make about which of his horses he would keep. Due to space and financial constraints he simply could not keep all of them. He could decide which horses to sell based on their physical appearance. He could keep the horses who's names he liked best. He also considered keeping the horses with the best pedigree. **Or, he could keep those horses who had performed the best in races over the past 6-12 months.** If Pete was thinking like a Dorsey, Wright money manager, he would keep those horses who had performed the best in races over the past 6-12 months.

**High RS Asset Class:**

High RS stocks, as an asset class, often move independently of broad indexes. Recent performance through 3/19/2007:

High RS Index vs SPY (Trailing 18 Months)



SPDR Trust (SPY) is an exchange-traded fund that holds all of the S&P 500 Index stocks. "High RS Index" is a proprietary Dorsey, Wright Index composed of stocks that meet a high level of relative strength

**Sector & Capitalization Snapshot**

As of 3/19/07

**Sector Performance**

S&P 500 GICS Sector	12 Month	6 Month	1 Month
Utilities	20.67%	14.89%	1.68%
Telecommunications	19.65%	13.46%	-0.84%
Materials	16.62%	20.48%	-1.24%
Consumer Discretionary	11.16%	10.15%	-5.18%
Energy	10.05%	10.28%	-1.29%
Consumer Staples	8.29%	1.84%	-2.81%
Financials	6.71%	3.41%	-6.36%
Industrials	4.61%	7.51%	-3.11%
Health Care	2.31%	0.91%	-3.48%
Technology	2.12%	6.27%	-3.65%

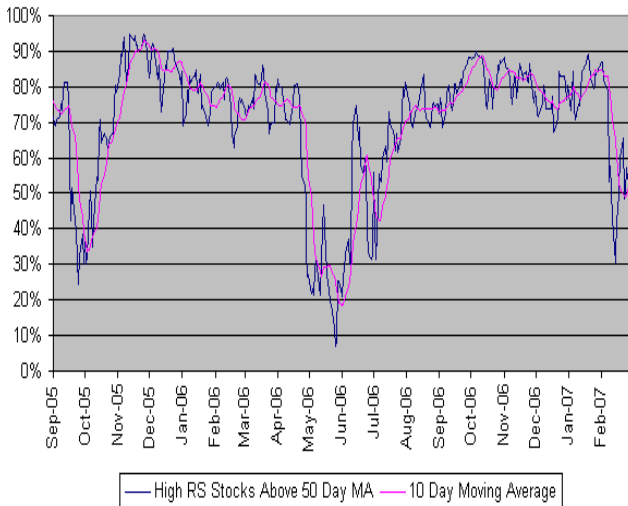
**Performance by Capitalization**

S&P Large-Cap	7.33%	6.37%	-3.79%
S&P Mid-Cap	5.85%	10.88%	-3.20%
S&P Small-Cap	4.93%	8.52%	-3.20%

## High RS Diffusion Index

For high RS strategies, dips are often a good time to add exposure. As of 3/19/2007.

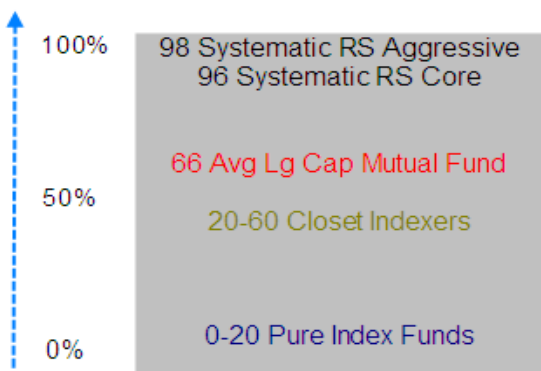
Dorsey, Wright High RS Diffusion Index



## Active Share

High RS strategies tend to have high Active Share. Active Share is calculated by matching the holdings reported by a fund in Securities and Exchange Commission filings against the components of an index, and then measures the percentage of overlap. The more a portfolio differs from an index, the higher the active share percentage. Relative Strength forces you to move to where the strength is, regardless of that area's weight in the broad market. Active Share is a measure that was created by Antii Petajisto and Martijn Cremers from the Yale School of Management. Their analysis of Active Share was published in 2006: "How Active Is Your Fund Manager? A New Measure That Predicts Performance"

### Active Share Percentage



As of 12/31/06

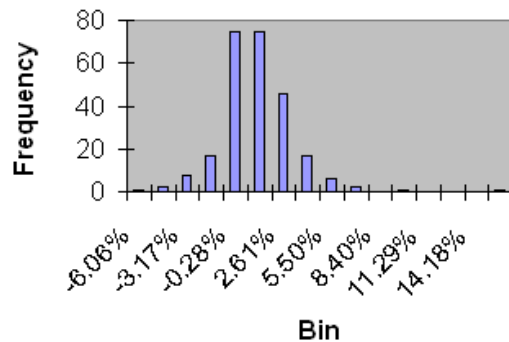
## Skew Data

In the stock market, at any given time, there are stocks in strong uptrends, stocks in strong downtrends, and a majority whose trends are currently static. The main objective of high relative strength investing is to find and capitalize on as many strong stocks as possible.

Interestingly, high relative strength stocks often have a proportion of up days to down days of about 50 percent. One could be fooled into thinking that the price movement is random. However, the trend does not depend on having a lopsided number of days up versus the number of days down. The relative performance achieved by major winners is the result of the days up being persistently larger in percentage terms than the days down.

For example, over the past 12 months, the strongest component of the S&P 500 Index is Goodyear Tire (GT). Over the past year, 51% of the trading days it has been up and 49% of the days it has been down, but the stock is up 107% over that time!

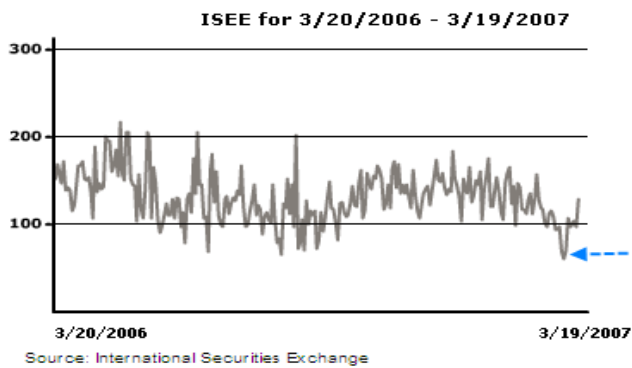
### Goodyear Tire Daily Price Change Histogram



Date Range: Mar 16, 2006 - Mar 16, 2006

You'll notice the positive skew of the histogram (the right tail is the longest). So, whether GT had an up day or a down day over the past year may have been random, but the distribution of percentage return definitely was not.

## Sentiment: On the Analyst's Couch



### Calculating the ISEE

ISEE is computed by dividing opening long call options bought by customers by opening long put options bought by customers.

$$\frac{\text{Long Calls (Opening Position)}}{\text{Long Puts (Opening Position)}} \times 100 = \text{ISEE}$$

The put-call ratio is a contrary indicator. When market participants are fearful, as they are now, it is very bullish for prices 6 months and 12 months later. (*Colby, The Encyclopedia of Technical Market Indicators*)

## 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, *CBS Marketwatch*  
<http://tinyurl.com/2qt6cd>
- New ETFs start trading on the NYSE, AMEX, *Reuters*  
<http://tinyurl.com/2uw4mu>

### Arrow DWA Balanced Fund (DWAFFX)

- Fund of ETFs Leads Way for Moderate Allocation, Arrow Funds  
<http://tinyurl.com/2j56ow>

### General

- Can Relative Strength Be Used in Portfolio Management?, *Technical Analysis of Stock & Commodities*  
<http://tinyurl.com/38ooq3>
- Systematic Relative Strength Investment, *The Wall Street Transcript*  
[PDF available upon request](#)

## To Request Info

To request information about our Systematic Relative Strength accounts, please call us at 626-535-0630, or e-mail us at [moneymanagement@dorseywright.com](mailto:moneymanagement@dorseywright.com).

Dorsey, Wright Money Management  
595 E. Colorado Blvd, Suite 307  
Pasadena, CA 91101  
(626) 535-0630