Why Top Traders Use
The Relative Strength Comparison (RSC)
& Desperately Want To Keep It A Secret!

Discover The Best Performing Sectors &
The Strongest Stocks In Those Sectors
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We both know that, regardless of what the market is doing, there are always profitable trading opportunities. What's more, MetaStock has the ability to identify these opportunities, assuming you know how to use it. Yet, if you're like most people, even though you've invested in MetaStock, you probably don't use it to its full potential.

Within this report we'll show you how you can find these profitable trading opportunities by using MetaStock to its full potential. You too will employ the techniques usually only exploited by the professionals.

What is sector analysis?

In very basic terms, sector analysis is a top down stock selection method. Market sectors expected to outperform the rest of the market are identified, and then stocks from these sectors are selected. The belief is that if you can select securities in superior sectors, these securities will perform along with their respective sectors. This follows the truth that money flows from underperforming areas of the market, to more profitable areas.

This is further illustrated by Stan Weinstein who said:
"*... my studies have consistently shown that two equally bullish charts will perform far differently if one is from a bullish sector while the other breakout is in a bearish group. The favourable chart in the bullish group will often quickly advance 50 to 75 percent while the equally bullish chart in a bearish group may struggle to a 5 to 10 percent gain*"
– from Secrets for Profiting in Bull and Bear Markets

How can you use sector analysis within MetaStock?

Remembering our aim is to identify market sectors that will outperform the market; we must first compare the strength of each sector against a chosen market index. Next, we need to then rank these sectors, find out which ones are performing the strongest, and from here we can identify securities that fall within these sectors. These individual securities can also be ranked against their respective sectors and in doing so, we can effectively select the best performing securities in the best performing sectors.

The best way to compare the strength of one security against a market index is to use the Relative Strength Comparison (RSC). The RSC actually compares a security's price change with that of a "base" or benchmark security (shown in figure 1.1 on the next page).

When plotted on a chart, the RSC line can be interpreted as follows:

- If the RSC is increasing, it indicates that the security is performing better than the base security.
- If it moves sideways, it indicates that both securities are performing the same.
- If it is decreasing, it indicates that the security is performing worse than the base security.
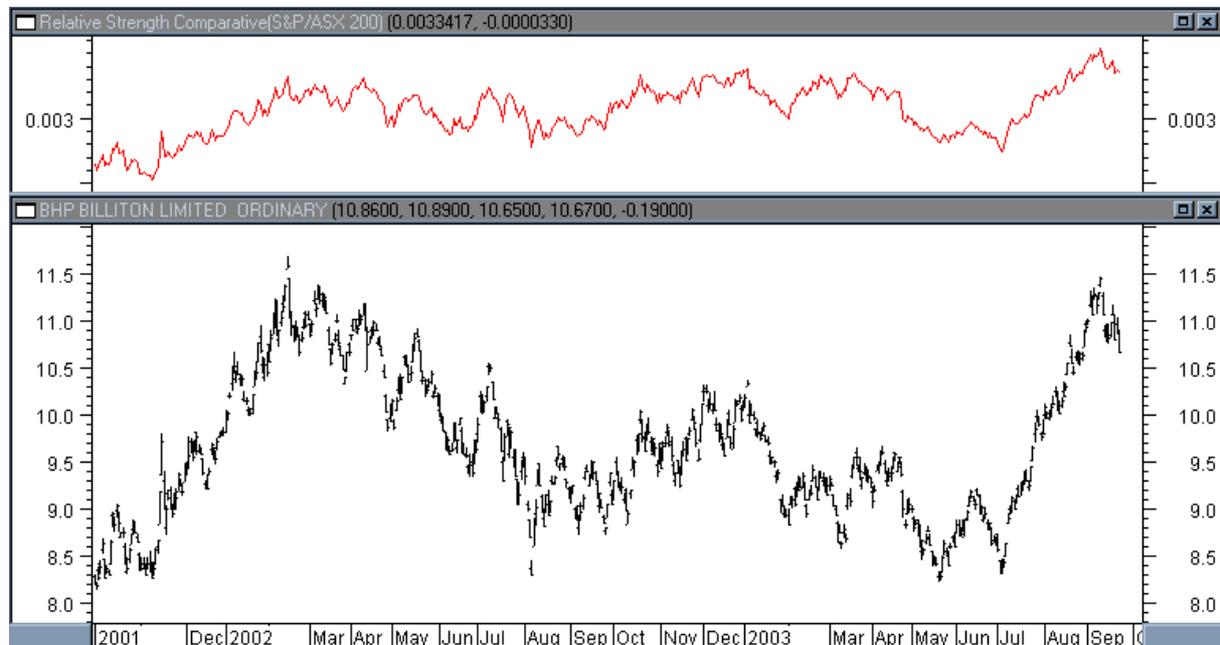

Figure 1.1

It is important to note that just because the RSC may be rising in value, doesn't mean the security is necessarily rising in value too. It simple indicates that the security is performing better than the base security. For example, a security may be falling in price however it may not be falling as fast as the base security, the result being that the RSC would strengthen. Conversely, if the RSC is falling the security may not be reducing in value; instead it may be that it's increasing at a slower rate than the base security.

To create an exploration that uses the RSC you need to first open a chart of the base index (e.g. S&P/ASX200 for the Australian market, Straits Times Index for Singapore etc) that will be used as the comparison point between market sectors. Once open, left click on the price plot to highlight the price information. You'll know it's selected when a series of small dark squares appear on the price plot. It's important to note that each time you wish to do an exploration of this kind, you must first highlight to MetaStock what our base index is.

Next, open The Explorer dialog and select 'new'. Name the explorer the 'MetaStock Guide Sector Analysis,' (shown in figure 1.2) click within 'Column A' and enter the following formula:
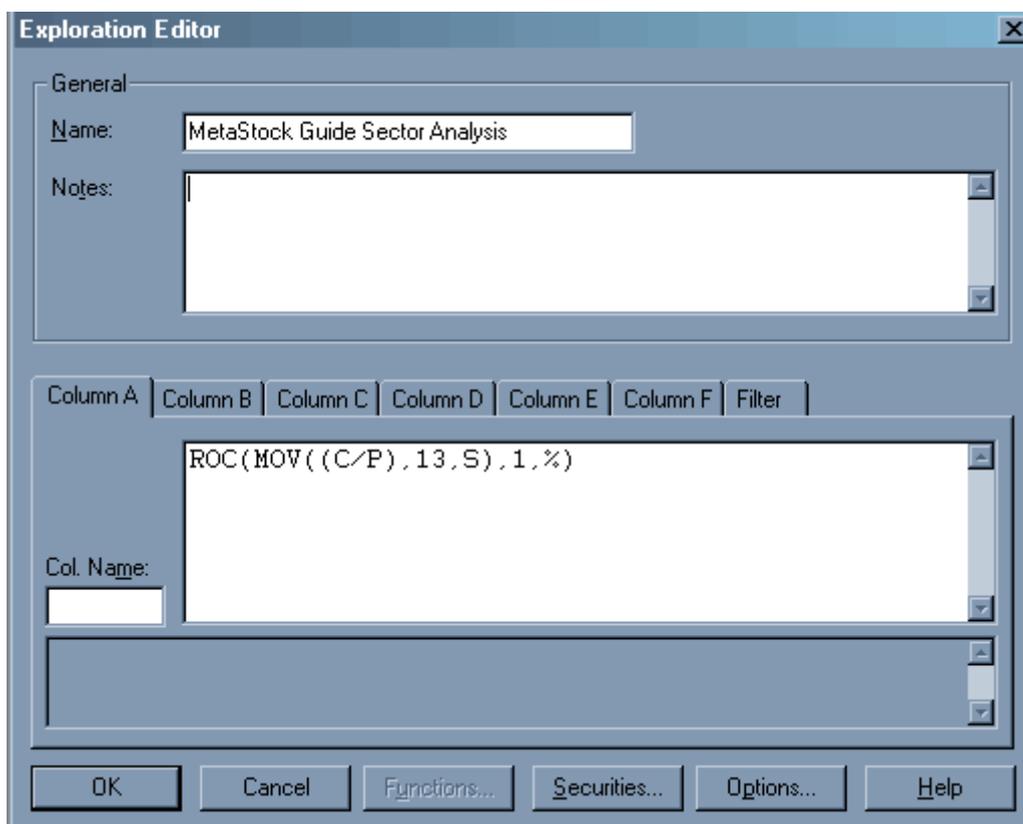
ROC(MOV((C/P),13,S),1,%)

Figure 1.2

The formula entered into column A calculates the rate of change in the relative strength. It may seem complex but let's break it down into manageable parts beginning with the inner most brackets first:

C/P is the relative strength (or RSC component) of the tested sectors vs. the base security. The way it's calculated is by dividing the closing price of the sector, by '*P*', where '*P*' references the base index you highlighted before creating this explorer.

(MOV((C/P),13,S) calculates the moving average of the RSC over a 13 week period.

ROC(MOV((C/P),13,S),1,%) calculates the rate of change of the moving average of the RSC, in other words, the amount the sector has moved up or down as a percentage.

Looking back at MetaStock, notice that you didn't enter anything into the filter tab. The reason is that you do this only when you're looking to eliminate certain securities from your exploration results. Since you're not looking to exclude any sectors, but rather rank them, you should leave the filter blank.

Before running this exploration you must check the periodicity of this exploration. To do this click the 'Options' button at the bottom of the 'Exploration Editor' dialog and then select the radio button marked weekly. Click 'OK' twice to return to 'The Explorer' dialog.

Now you're ready to run the exploration, click 'Explore'. The 'Select Securities for MetaStock Guide Sector Analysis' dialog appears, and it's here where you must select the directory with your market sectors in it. This should be stored with your other market data and is usually one directory up from your equities folder. However this will vary, depending on who supplies your data.

When the market sectors are highlighted, click 'OK'. When the exploration is complete the 'Exploration Completed' dialog appears. Click the 'Reports' button and you will be given a summary of the exploration. The results shown in 'Column A' give us the rate of change of the relative strength (shown in figure 1.3)

Tip: by clicking the 'Column A' heading you can arrange the results in ascending or descending order.
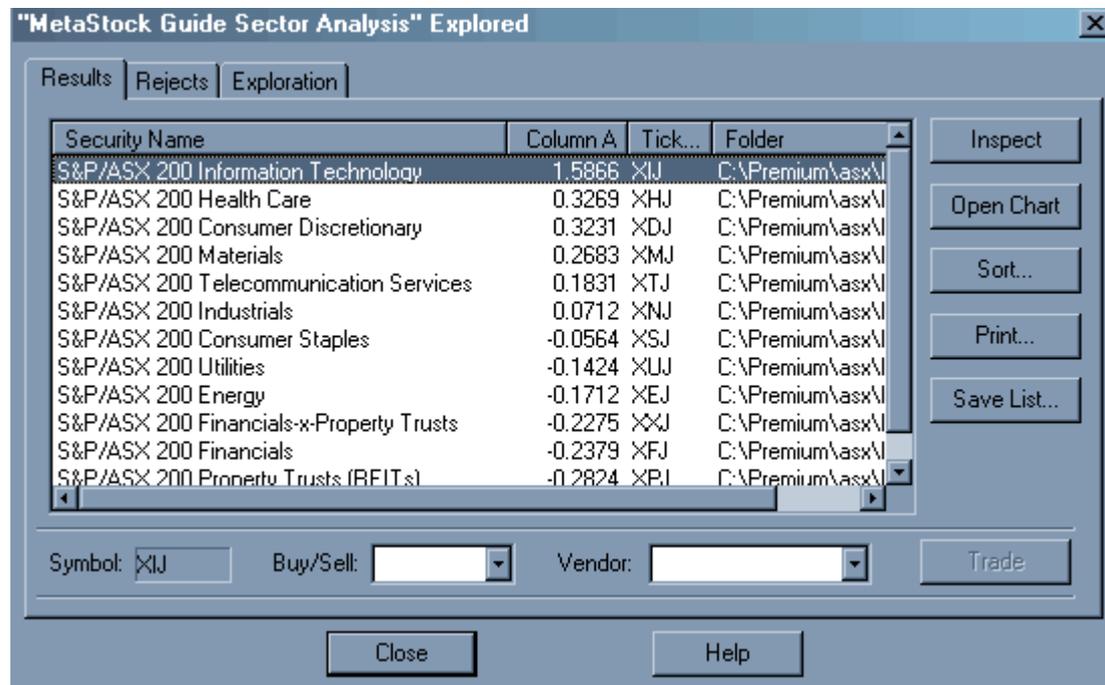

Figure 1.3

What do these results mean?

Interpreting the results is easy: a value greater than zero indicates that the market sector is outperforming the base index. A zero indicates that the market sector is performing on par with the base index, while a negative number indicates the market sector is underperforming the base index.

Remember a rising RSC value only indicates that the market sector is outperforming the base index. Sometimes if the RSC is rising in value, so too is the market sector. However, this isn't always the case. Similarly, if the RSC is falling the market sector may not be reducing in value; it only indicates that it is underperforming the market index. This illustrates how important it is to also open the chart of the market sectors to analyse the trend.

This information on its own can complement your current trading. For example you may decide to only trade securities which are present in top performing sectors. Alternatively you could take it one step further and perhaps select the top 5 sectors and then simply use the 'MetaStock Guide Sector Analysis' explorer again. This time however, you could compare individual securities against their respective sector.

The difference in running this exploration, when compared to the last, is that the market index would now become the market sector chart; and the list of sectors would now become the list of securities that make up the top performing sectors.

By following the same steps as before you could run 5 separate explorations and rank securities against their respective sectors. The result would identify the top performing securities which are within the top 5 performing sectors.

The final stage in this top down analysis would be to open all the charts that have made it to our shortlist. You can whittle this down further by eliminating those securities that aren't in an uptrend or those that are too thinly traded. Finally you're left with only the cream of the crop, about 5-10 securities. These securities are the best performing securities in the best performing sectors.

These securities could now be placed on your watch list. I suggest you don't race out and buy these securities. Instead you should now wait for an appropriate trigger to enter. This could be based on candlestick pattern, and/or favourable combinations of other bullish indicators.

To sum up, the RSC exploration is a great way to utilise the power within MetaStock. Furthermore, it can be an extremely effective tool in identifying profitable trading opportunities. The downside for this type of exploration is that it is not a complete system on its own and would need to be combined with other entry, exit and money management rules. The potential is there however to create a very solid trading system that includes sector analysis.

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Adapted from the MetaStock Programming Study Guide
Written by Stuart McPhee & David Jenyns
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What's Your Next Step?

We've now looked at how the professionals employ both a top down RSC approach to trading. Nevertheless, if your like most people, since they're not familiar with MetaStock, this report may appear confusing.

Who Else Wants the Simple Secret to Make Metastock Easy & Identify Profitable Trades?

Sure you could waste months reading through the boring manual or worse not even bother. But why put yourself through that? Just visit...

www.meta-formula.com/Metastock-Programming-Study-Guide.html

> *"If you want Metastock programming explained in a clear way then David has the skills you require."*
> **Daryl Guppy** - Professional Trader & Educator **www.guppytraders.com**