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IDENTIFICATION OF STOCKS PERFORMING BETTER THAN THE MARKET

A fundamental problem in the area of capital market investment is the selection of stock for the portfolio. Two performance criteria are usually taken into account: maximum return and minimum risk. Practitioners who use technical analysis employ various types of so-called Relative Strength indicators for stock selection, which are supposed to yield a higher return than the market. This type of approach entails using a market index, such as DJIA or S&P500, as a gauge, and choosing those stocks which are performing – or which one hopes will perform – "better" than the gauge. A generalized revision of this approach underlies the current contribution, which consists of three stages, as follows:

1. Introduce the stock model where the smooth estimator of the stock profitability derivative, termed ***D****irect* ***S****trength*, *(**DS**)*, is shown as the balance of two other forces: an internal force specific to each stock, termed ***S****pecific* ***S****trength (**SS**)*, and the force of market – termed ***M****arket* ***S****trength (**MS**)*.
2. Define the aforementioned forces, and briefly discuss their possible interpretations
3. Show a practical example of such an application at the Warsaw Stock Exchange.

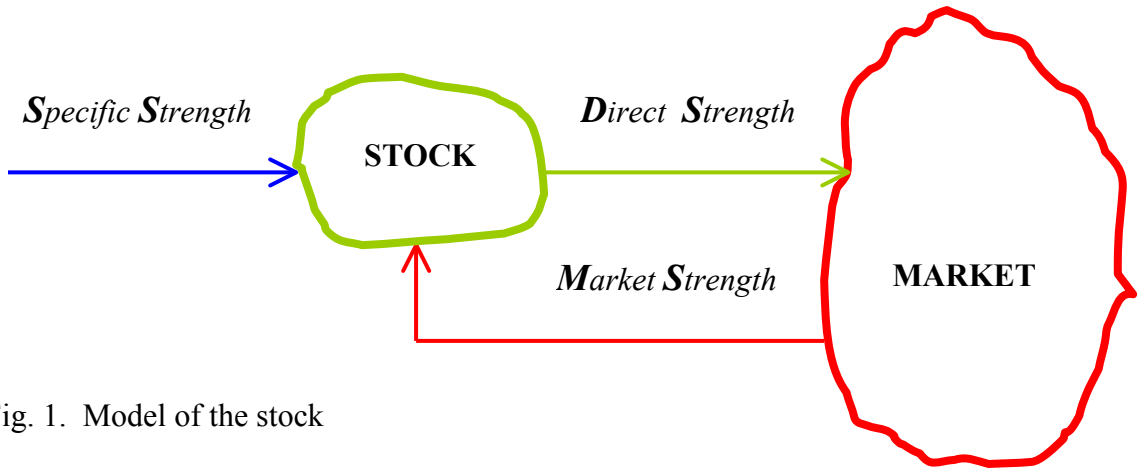

Fig. 1. Model of the stock