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Enlightened Stock Trading

The Art (and Science) of Building a Diversified Trading Portfolio

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Founder
Enlightened Stock Trading

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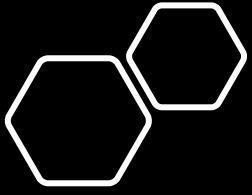
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The Art (and Science) of Building a Diversified Trading Portfolio

Adrian Reid
Founder – Enlightened Stock Trading



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How many of you want to build a more robust portfolio that generates good returns and helps you sleep at night?

Learning
Requires
Energy

My Results

- Trading stocks profitably for over 20 years
- Paid off all debts and built a 7 figure trading account
- Escaped the corporate world in 2012 based on trading profits
- Coach and mentor hundreds of traders from all over the world to profitability every year
- Still trade just 20-30 minutes a day
- Allowed me to spend all of 2019 travelling around the world with my family
- We have since settled in one place (for a few years) because after 7 different schools our kids told us that was enough!



My goals for you today

My goals for you today

1. Show you the trading essentials you must have in place to be successful (The 'Ticket To Play')

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My goals for you today

1. Show you the trading essentials you must have in place to be successful (The 'Ticket To Play')
2. Highlight common issues systematic traders face and how to eliminate them
3. Demonstrate how to construct a portfolio of strategies using a combination of art and science
4. Give you the process to implement and manage this in 20-30 minutes a day



What is the “Ticket to Play” for Systematic Trading?

The “Ticket to Play” for Systematic Trading



The “Ticket to Play” for Systematic Trading



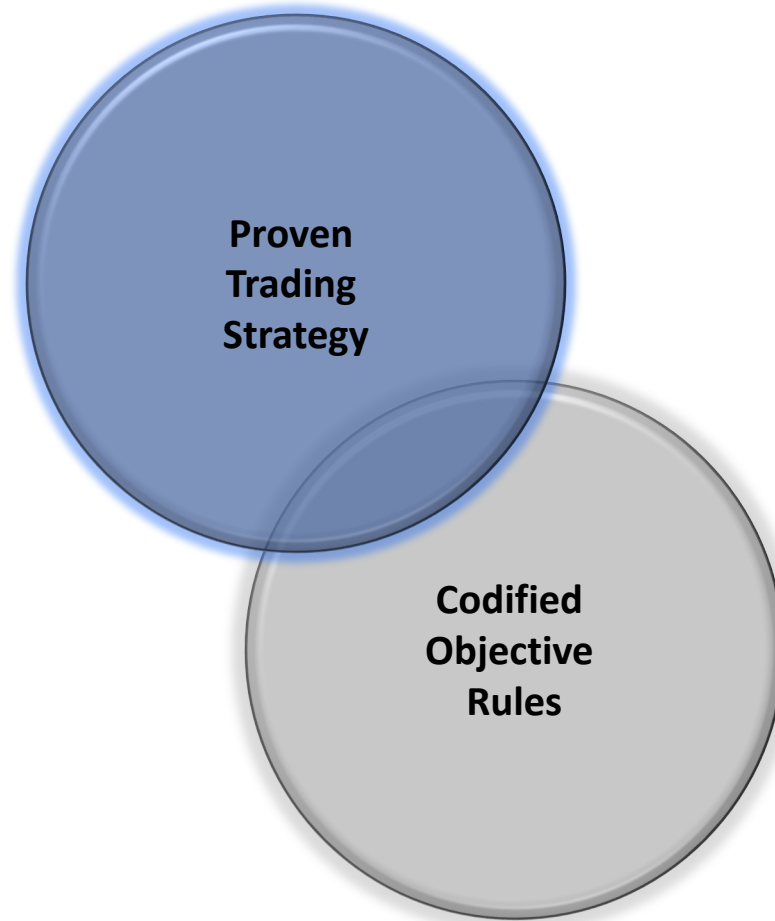
Ensure you have a solid foundation
be starting with a proven strategy:

- Trend Following
- Mean Reversion
- Rotational Momentum
- Seasonality

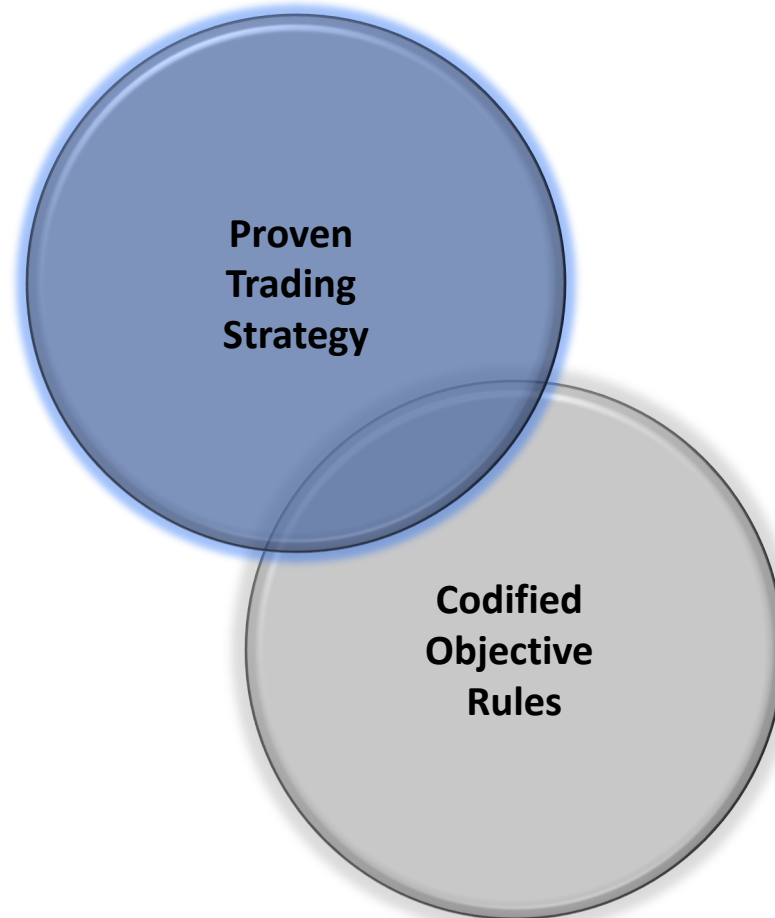


This provides the foundation for
everything that comes next

The “Ticket to Play” for Systematic Trading



The “Ticket to Play” for Systematic Trading



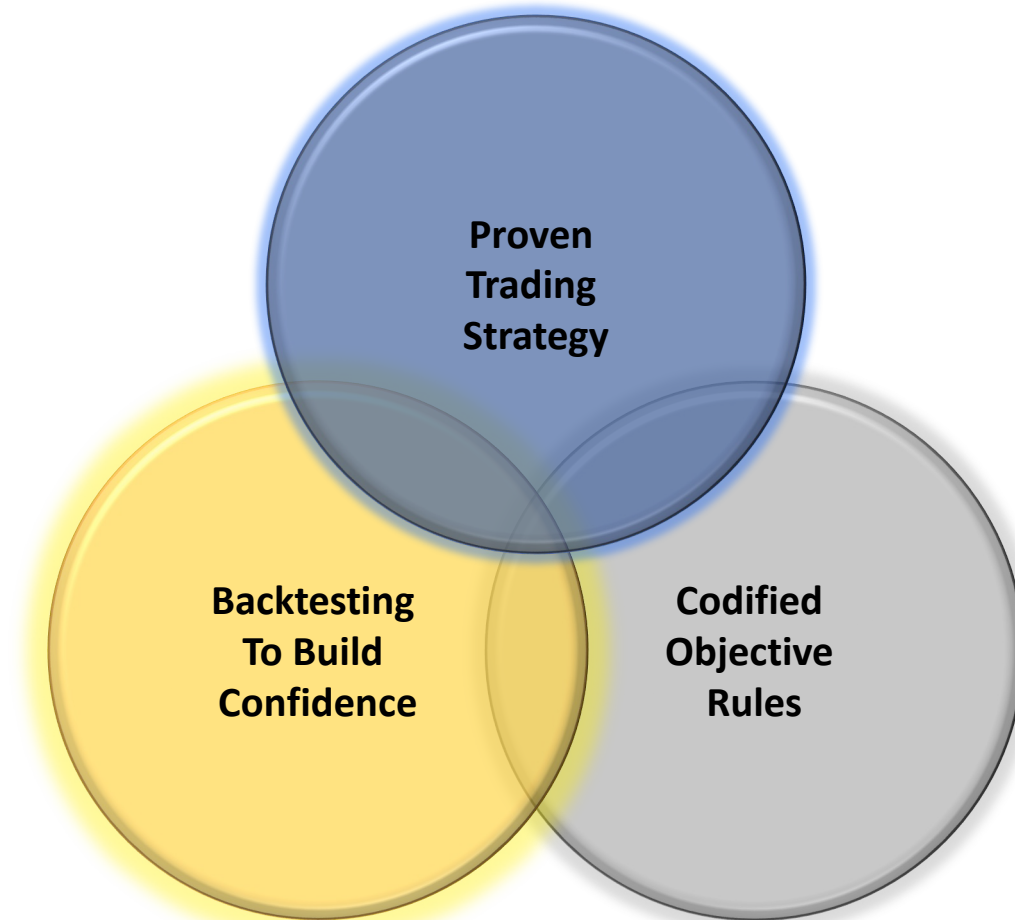
Create a complete trading system around your chosen strategy:

- Market Regime Filter
- Trend Filter
- Entry Trigger
- Initial Stop
- Exit
- Position Size
- Position Rank / Score



Codify all of this so that you can take the next step...

The “Ticket to Play” for Systematic Trading



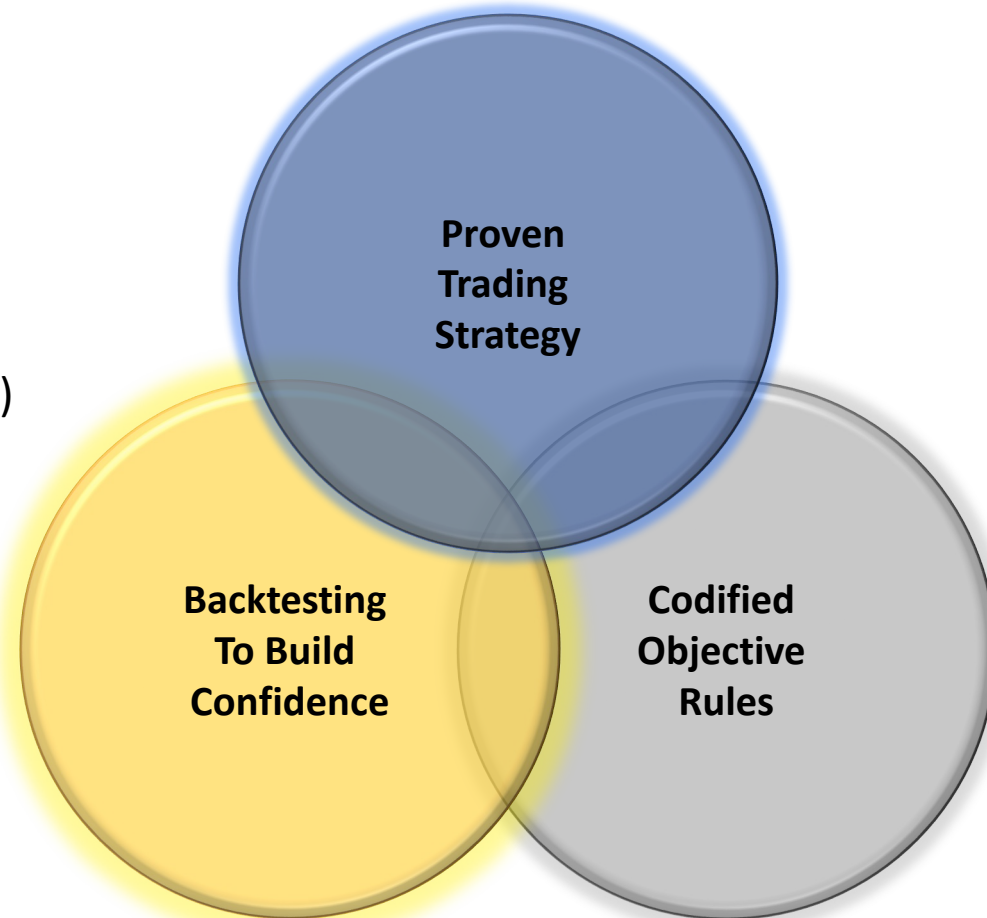
The “Ticket to Play” for Systematic Trading

Backtest your system deeply over many market cycles:

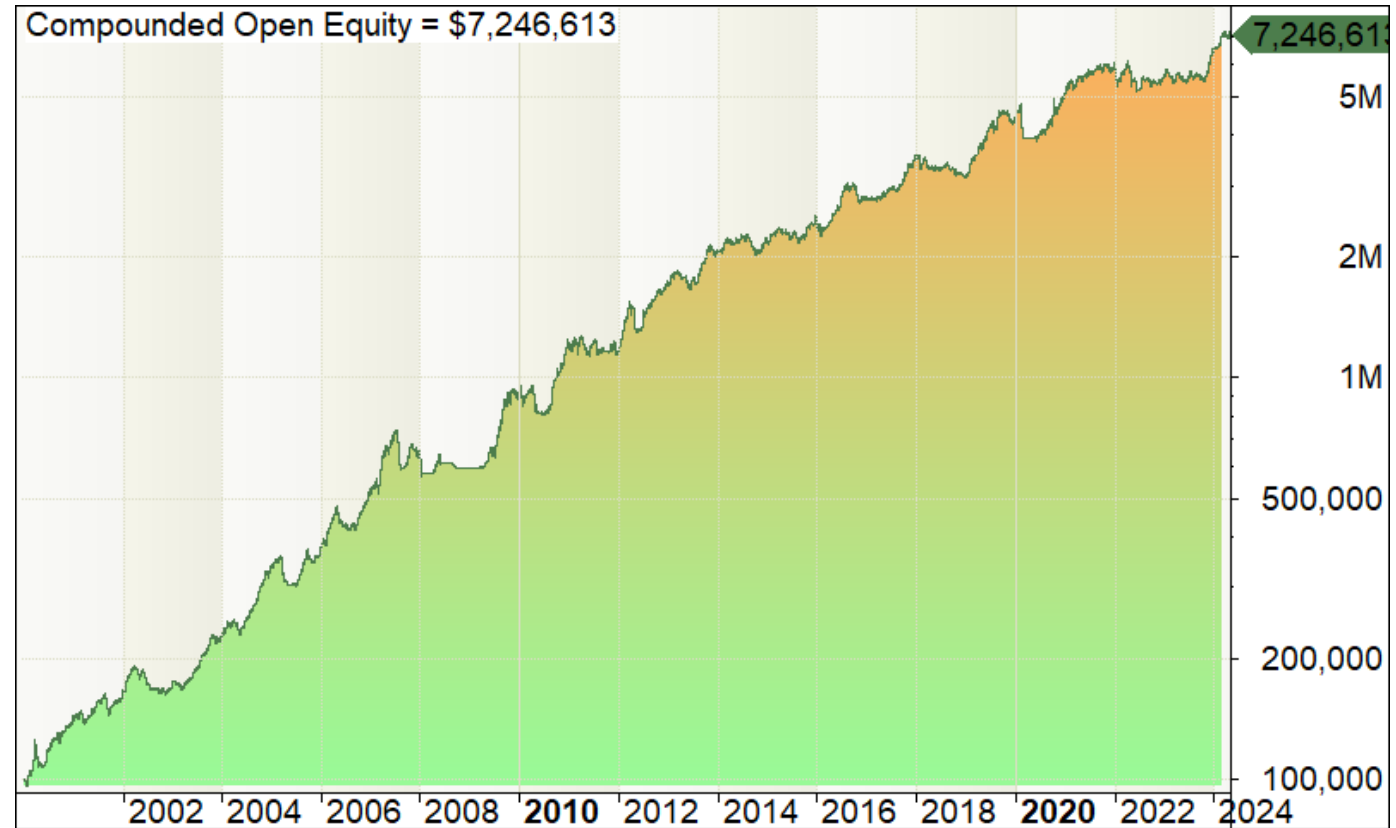
- 20-30 years of history
- Thousands of trades
- Optimized for stability (not profit)
- Every rule is significant
- System is robust
- Validated on out-of-sample data
- Validated on adjacent markets



Now you can have confidence in your trading system


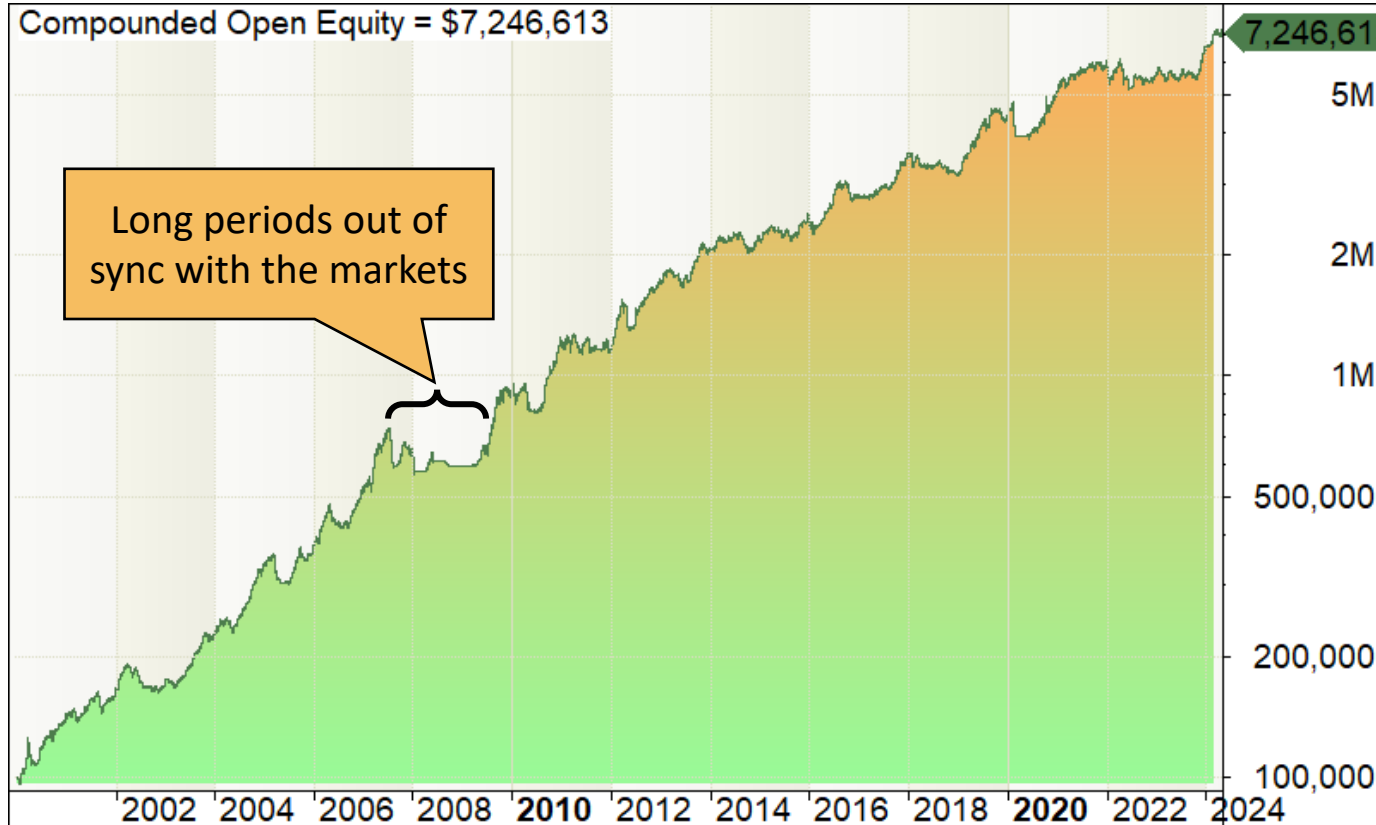


Finally You Can Have Confidence in Your System



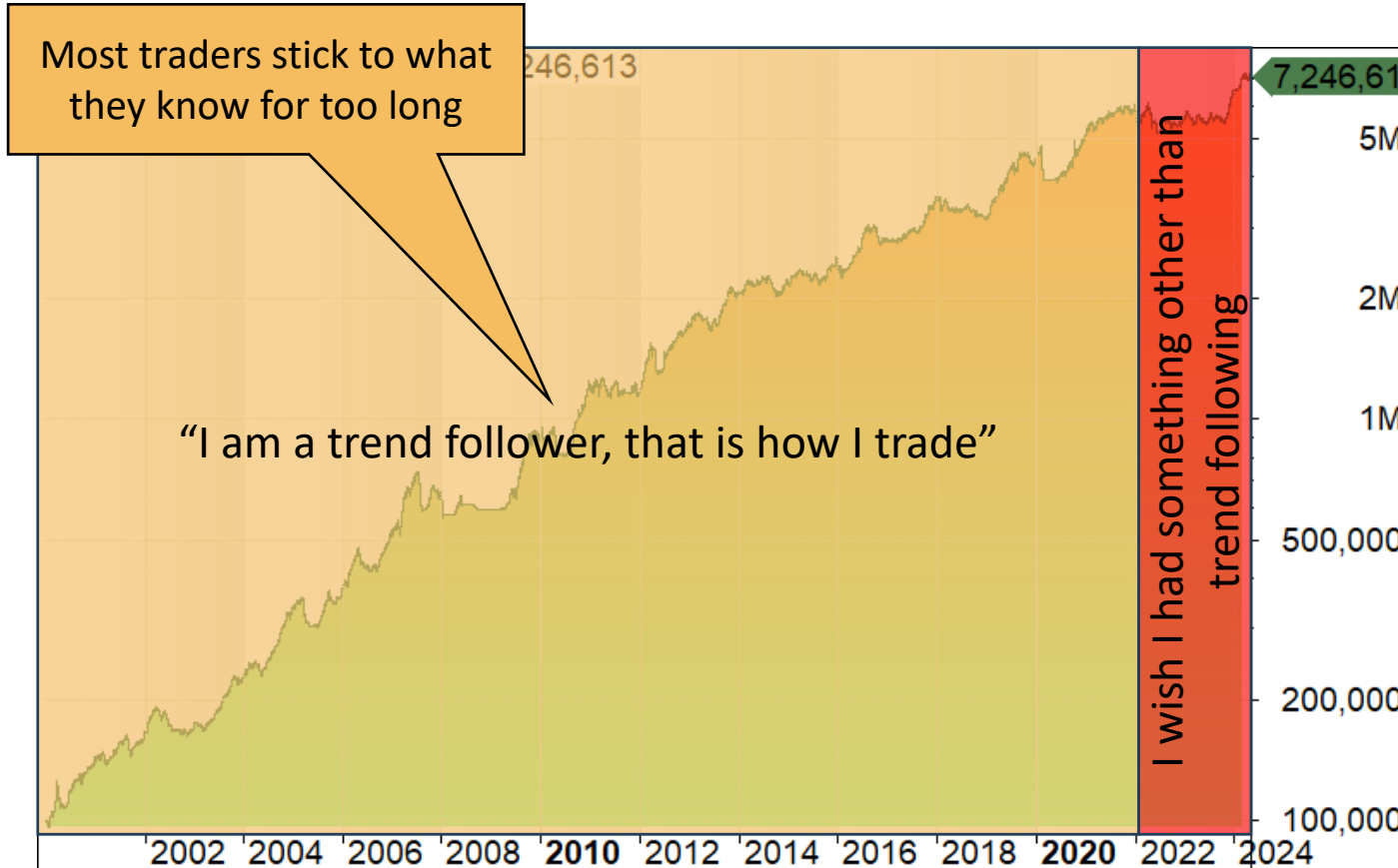
But Wait!
Now the next level of issues emerges

The next level of issues (1)



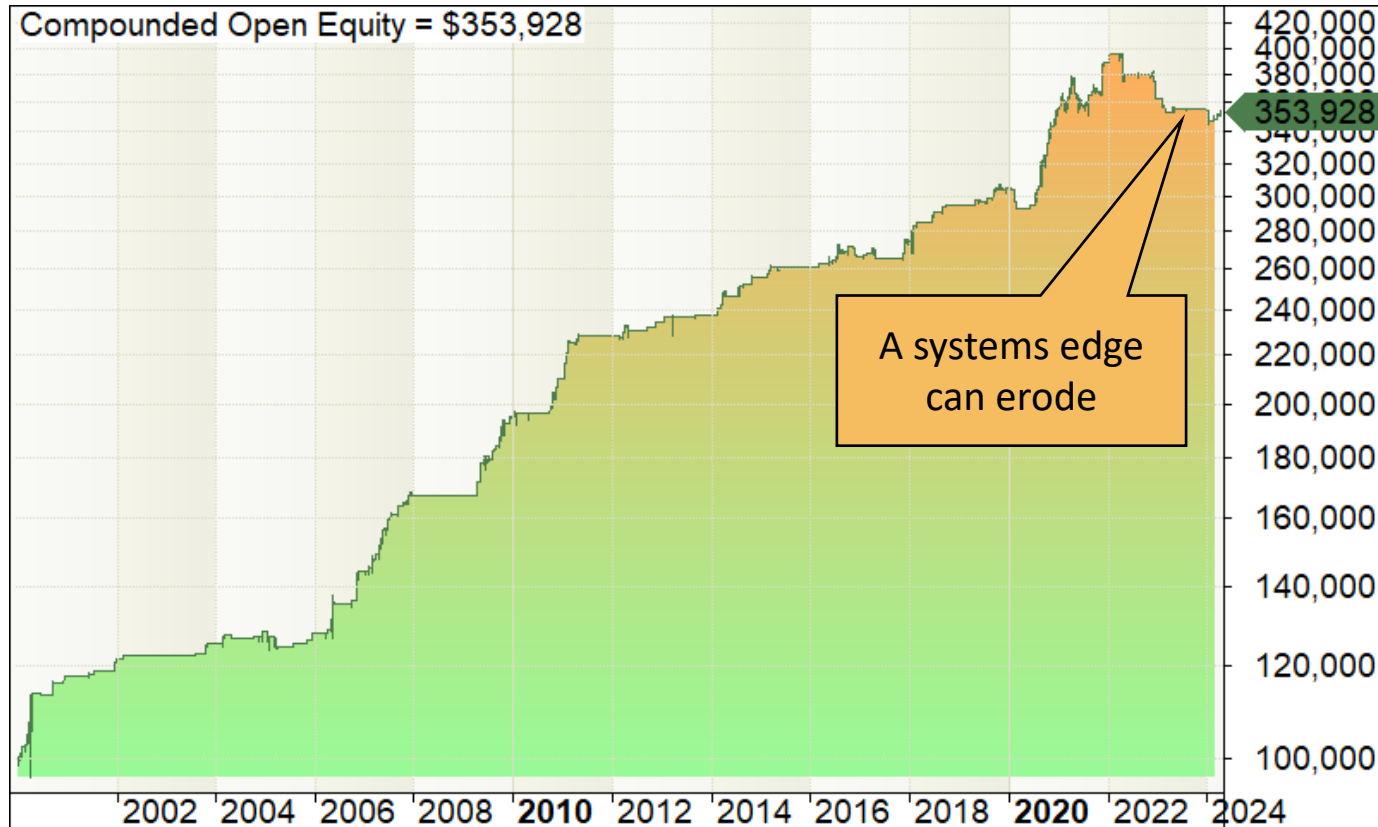
One system is not enough. We need to spread our capital across a portfolio of systems

The next level of issues (2)




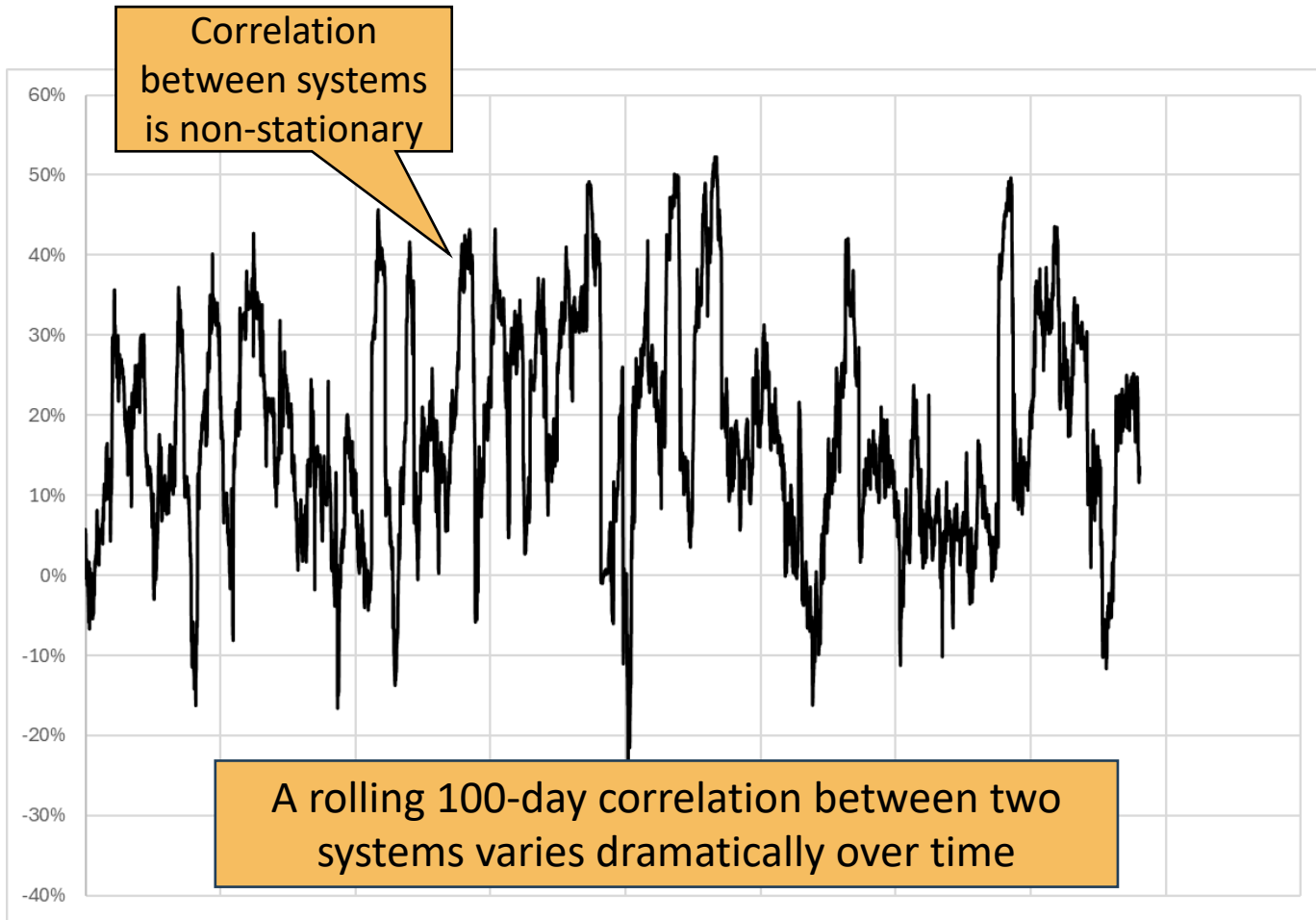
Establish a portfolio of different Strategies / Markets / Timeframes as soon as possible

The next level of issues (3)



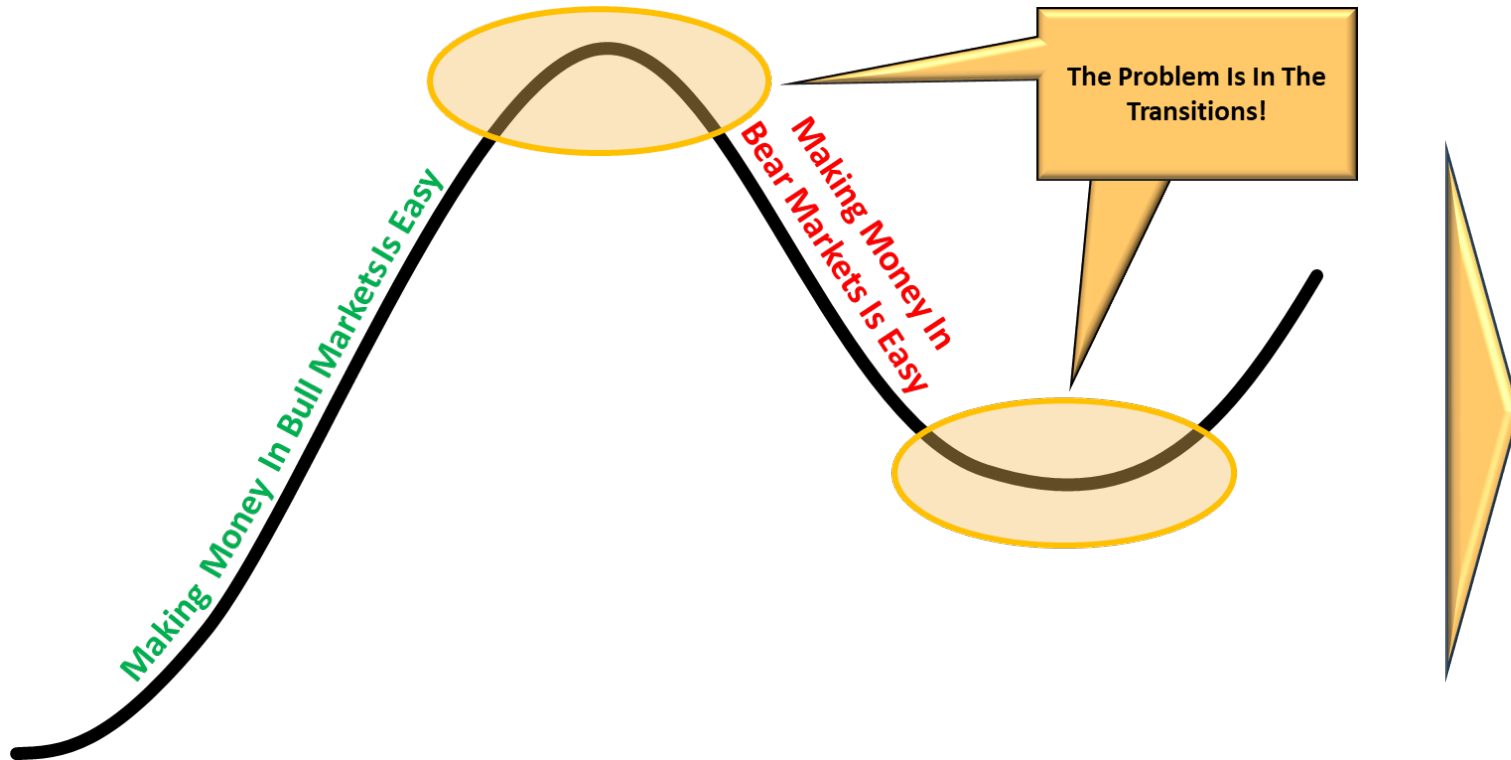
Diversify more broadly
so each system doesn't
hurt you if it erodes
(e.g. 10 systems instead of 3)

The next level of issues (4)



Diversify broadly and 'force' low or negative correlation with very different strategies and directions

The next level of issues (5)



Don't put all of your capital in one market. Multiple markets spreads the transition risk

**So it should now be clear that you
need a portfolio of trading systems**

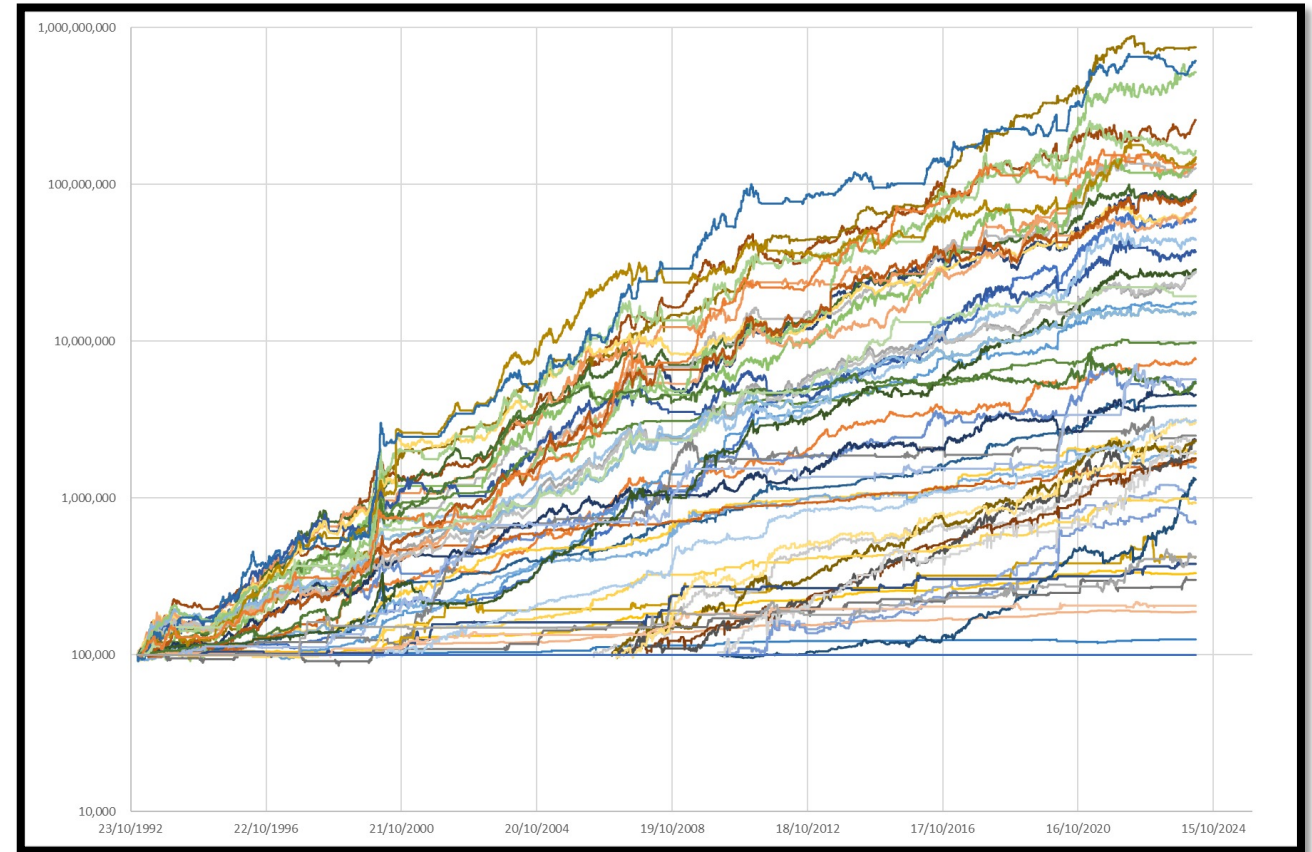
How to Construct a Portfolio of Systems



How to Construct a Portfolio of Systems

Step 1:

Source a broad range of systems covering different Strategies/Markets/Timeframes
(for example, I have 57 in this image)



How to Construct a Portfolio of Systems

Step 2:

Combine systems into a portfolio considering correlation & exposure (This is the SCIENCE)

- Outputs:
- Combined equity curve
 - Max portfolio drawdown
 - Portfolio statistics
 - Max portfolio leverage
 - Average exposure

Input: Daily system equity curve & exposure

Input: Weighting of each system

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The screenshot displays the ENLIGHTENED STOCK TRADING software interface. At the top left, the 'Capital Allocation Inputs' section shows: Starting Capital \$100,000, Allocation Start Date 1/1/2010, Allocation End Date 1/1/2010, Years Invested 10, Ending Capital \$101,160, and Target Max Exposure 5%. The main area is a table of systems with columns for System Number, System Name, Market, Capital Allocation, Timeframe, Strategy, Direction, and \$ Allocation. The table lists 57 systems, including Mean Reversion 1.1, Slippery Dip, and various Harvesters. To the right, an 'Outputs' summary table shows performance metrics for different periods: Whole Time Period, Last 10 Years, Last 5 Years, Last 2 Years, and Last 1 Year. Below the table are four charts: 'Portfolio Equity Curve - Linear Scale' showing a steady upward trend from \$100,000 to over \$1,000,000; 'Portfolio Equity Curve - Log Scale' showing the same trend on a logarithmic scale; 'Drawdown' showing a red line fluctuating between 0% and 15% drawdown; and 'Exposure' showing a blue line fluctuating between 0% and 150% exposure.

How to Construct a Portfolio of Systems

The math to combine multiple systems:

Daily Portfolio Equity Change = \sum_1^N (Daily % Change in System N Equity Curve) x (System N % Weight)

Portfolio Equity Curve = $(1+\text{Day}_1) \times (1+\text{Day}_2) \times \dots \times (1+\text{Day}_A)$



Vary weights of each system to get the best results (Smoothest combined equity).
Do this with trial and error or optimize with constraints.

How to Construct a Portfolio of Systems

Step 3: Now comes the ART:

The backtests and historical system combinations don't tell us everything.



We need to do some 'thought experiments' to refine

How to Construct a Portfolio of Systems

Step 3: Now comes the ART: (Continued)

Perform qualitative scenario analysis:

- What would happen to this portfolio in an extreme 'Risk Off' scenario?
- Which of my systems will become correlated in an extreme event?
- What would happen if stocks fell 15% overnight?
- What would happen if one of your markets was rangebound for an extended period?
- What would happen if ???



Adjust system weightings based on your scenario analysis to improve worst-case outcomes not shown in the backtest.

**How can this all be implemented in
20-30 minutes a day?**

How to do this in 30 minutes a day

How to do this in 30 minutes a day

Step 1:

Eliminate discretionary trading



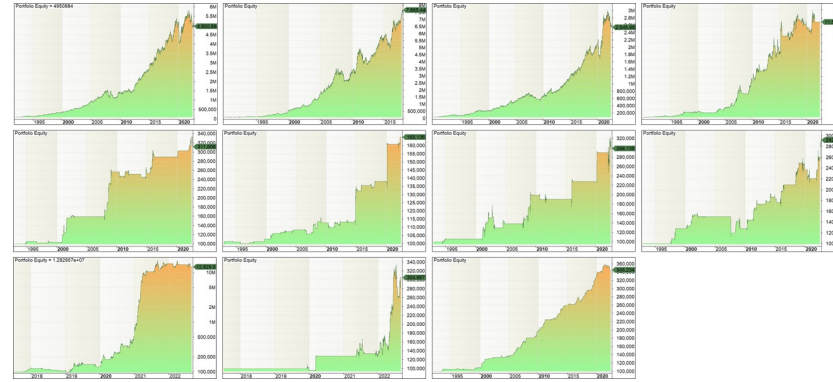
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How to do this in 30 minutes a day

Step 1:
Eliminate discretionary trading



Step 2:
Buy / Build a portfolio of trading systems
(strategies / markets / timeframes)



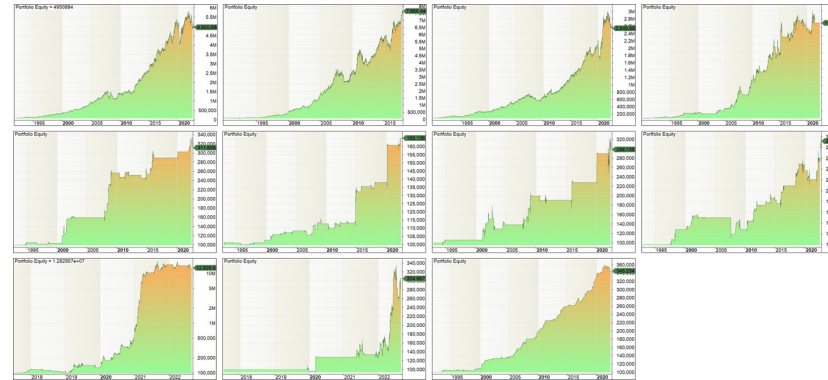
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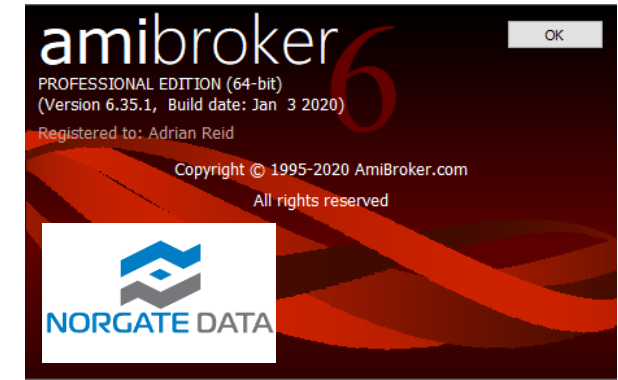
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Step 3:
Use Portfolio backtesting software +
Historical Data to build confidence



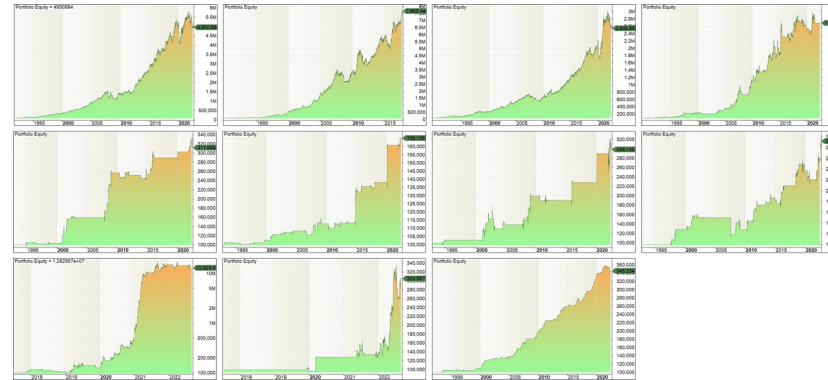
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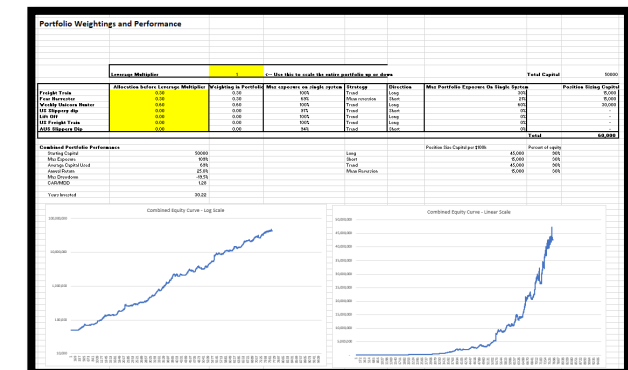
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Step 4:
Allocate capital between systems to
meet your return / risk goals



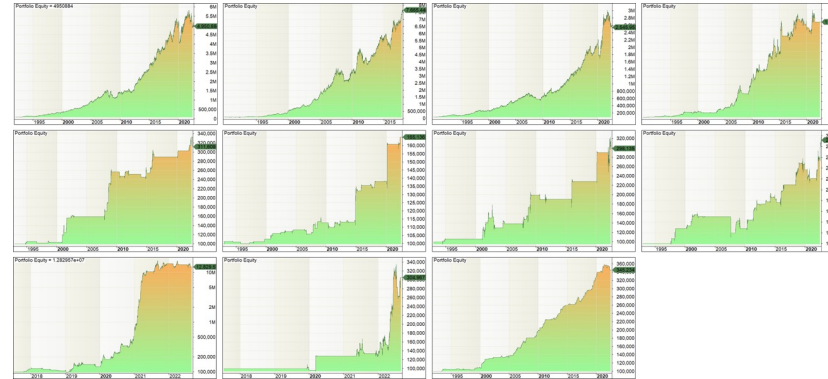
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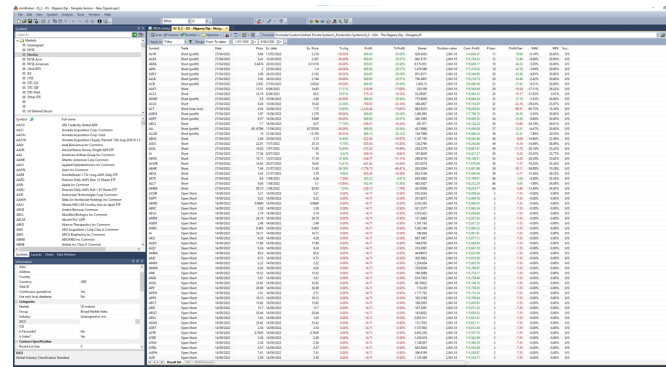
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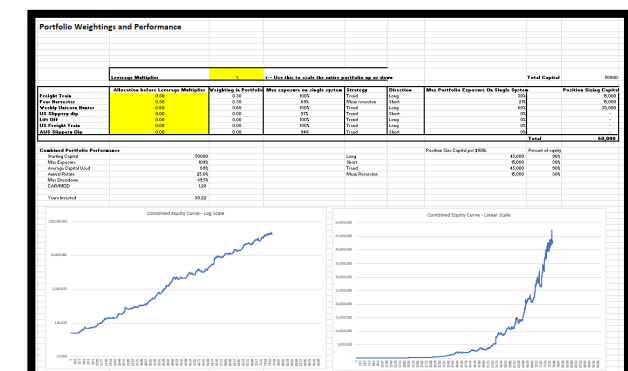
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Step 5:
Find your signals using the backtest so you know
exactly what trades to take (~30 seconds per system)



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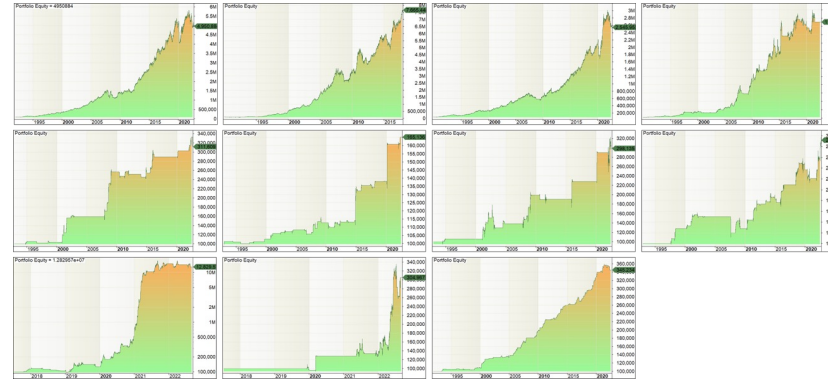


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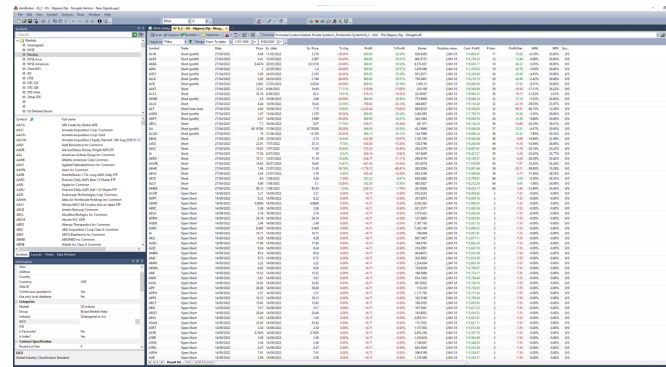
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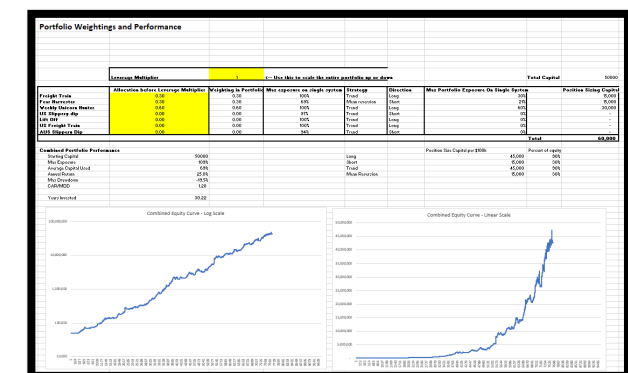
Step 6:
Place your trades with your broker
(2-3 minutes per system on average)
(Or automate order placement)



Step 5:
Find your signals using the backtest so you know
exactly what trades to take (~30 seconds per system)



Step 4:
Allocate capital between systems to
meet your return / risk goals



Key Messages To Take With You

- A profitable trading system is a 'ticket to play', but you need to take it further
 - One system is not enough >>> We need to spread our capital across a portfolio of systems
 - Most traders are slow to diversify >>> Establish a portfolio of different Strategies / Markets / Timeframes ASAP
 - Systems can erode over time >>> Diversify more broadly so each system doesn't hurt you if it erodes
 - Correlation is non-stationary >>> Diversify broadly and 'force' low or negative correlation with very different strategies
 - Market transitions hurt the most >>> Don't put all of your capital in one market. Multiple markets spreads the transition risk

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- Construct a diversified portfolio of strategies by
 - Source a broad range of systems covering different Strategies / Markets / Timeframes
 - Combine systems into a portfolio considering correlation & exposure (This is the SCIENCE)
 - Perform qualitative scenario analysis to ensure your portfolio weightings will hold up in the future (This is the ART)

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- A profitable trading system is a ‘ticket to play’, but you need to take it further
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 - Perform qualitative scenario analysis to ensure your portfolio weightings will hold up in the future (This is the ART)
- Implement this in just 20-30 minutes a day by systemizing all of your decisions, generating your signals from trading software (or automating) and monitor your systems as you trade them with Interactive Brokers.

Next Steps

SCAN ME



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How To Build Unshakeable Confidence In Your Stock Trading System
- **4 Trading Cheat Sheets to Improve Your Results Fast**
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Trading Mistakes Cheat Sheet: Increase your trading profits fast by identifying and eliminating trading mistakes
Portfolio CPR Cheat Sheet: Clean up your portfolio and get back on track fast
Trading Confidence Cheat Sheet: Increase your confidence and take decisive action in the markets
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The Trading Confidence Builder: 5 part video training series on how I build rock solid confidence in my strategies
- **The Trader Quiz:** The fastest way to get feedback on your trading - Get specific actions to improve your trading today
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