Twitter Thread by Quant Guy

Quant Guy
@QuantMan_

Lets talk about returns (risk adjusted!)

We are used to seeing % returns made against capital or even % made against margin blocked.

This is a wrong way to see the strategy performance due it doesn't take into account the risk taken to generate that return.

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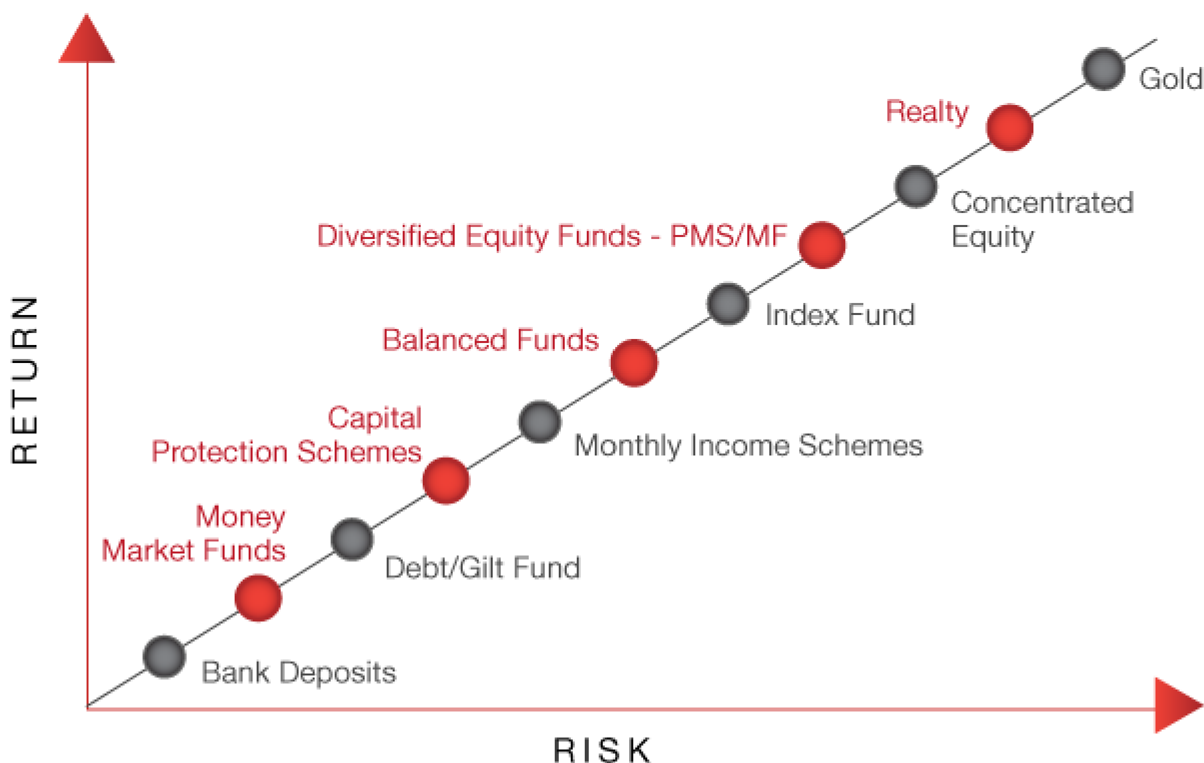

Thus the formula to calculate the "risk adjusted return" is:

Sharpe ratio = (Current Return - Risk Free Rate)/ Stdev(Historical Returns)

Lower Sharpe ratio means the strategy is unsustainable even if profit factor and win% are satisfactory.

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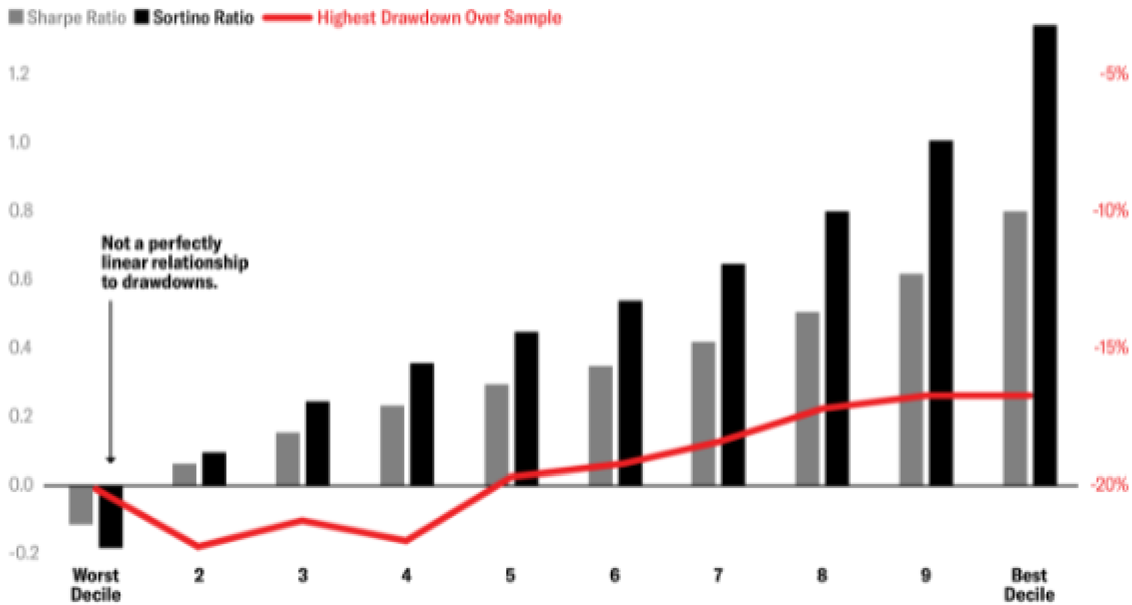

Some tips:
- Calculate the Sharpe Ratio of the entire portfolio vs individual stock
- Track the Sharpe Ratio regularly as it can vary based on historical performance
- Even a low return portfolio/strategy can have higher Sharpe Ratio if the risk undertaken is less!

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