CONNORS RESEARCH

Five Statistically-backed Theories on "How Markets Really Work"

Larry Connors, Co-author

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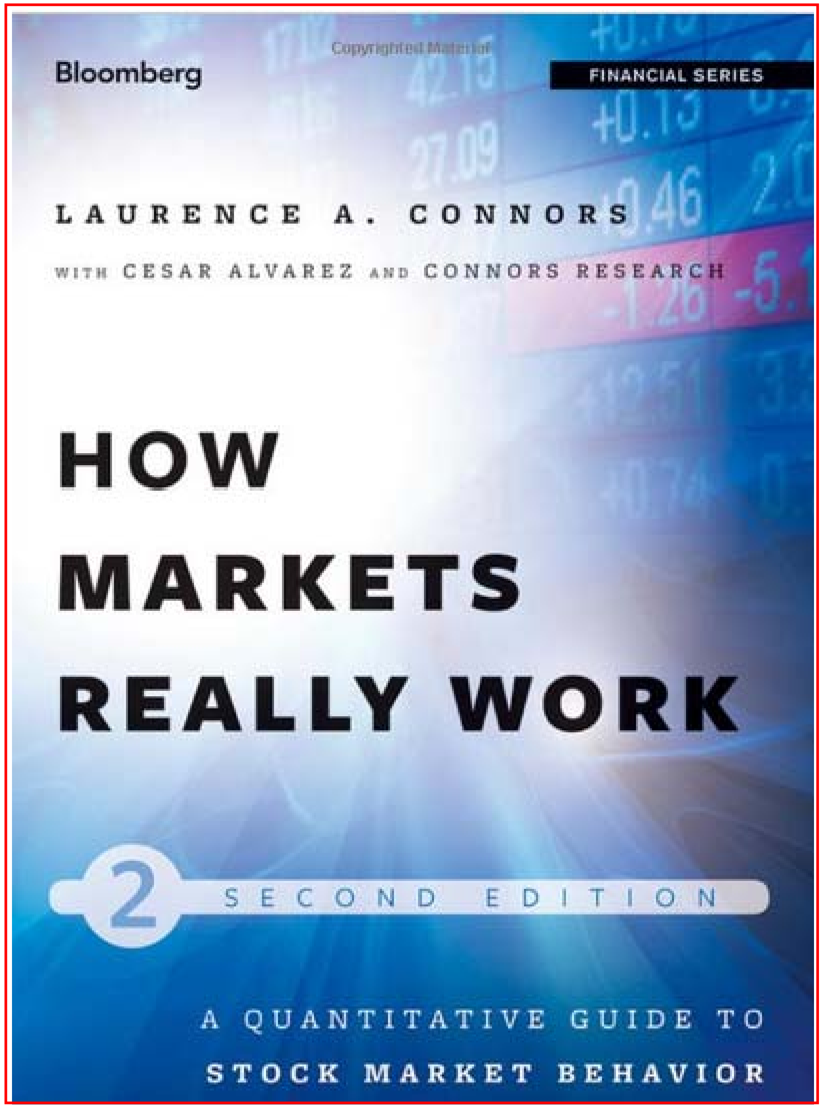
Welcome!

My Background

- 30 years of experience working in the financial markets industry starting in 1982 at Merrill Lynch.

- Managing Partner of LCA Capital, an asset management firm, and Connors Research, a financial markets research company.

- Authored top-selling books on market strategies and volatility trading, including *How Markets Really Work*, *Street Smarts* (with Linda Raschke) and *Short Term Trading Strategies That Work*.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MARKETS
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2 SECOND EDITION
A QUANTITATIVE GUIDE TO
STOCK MARKET BEHAVIOR

Table of Contents

Table of Contents (con't)

What *Moneyball* did for baseball, *How Markets Really Work* does for the stock market.

It’s not about emotion,
it’s about statistical results!

Ed Thorp – (from Wikipedia)

Since the late 1960s, Thorp has used his knowledge of probability and statistics in the stock market by discovering and exploiting a number of pricing anomalies in the securities markets, and he has made a significant fortune.

Thorp's first hedge fund was Princeton/Newport Partners. He is currently the President of Edward O. Thorp & Associates, based in Newport Beach, CA. In May 1998, Thorp reported that his personal investments yielded an annualized 20 percent rate of return averaged over 28.5 years.

- This is an over 18,000% return since the original investment was made!

From Chapter 2…

It's better to buy stocks on pullbacks than on breakouts.

Why?

Because the statistics back it up.

Figure 2-1. S&P 500. 5-Day Lows in the S&P 500 Significantly Outperformed 5-Day Highs

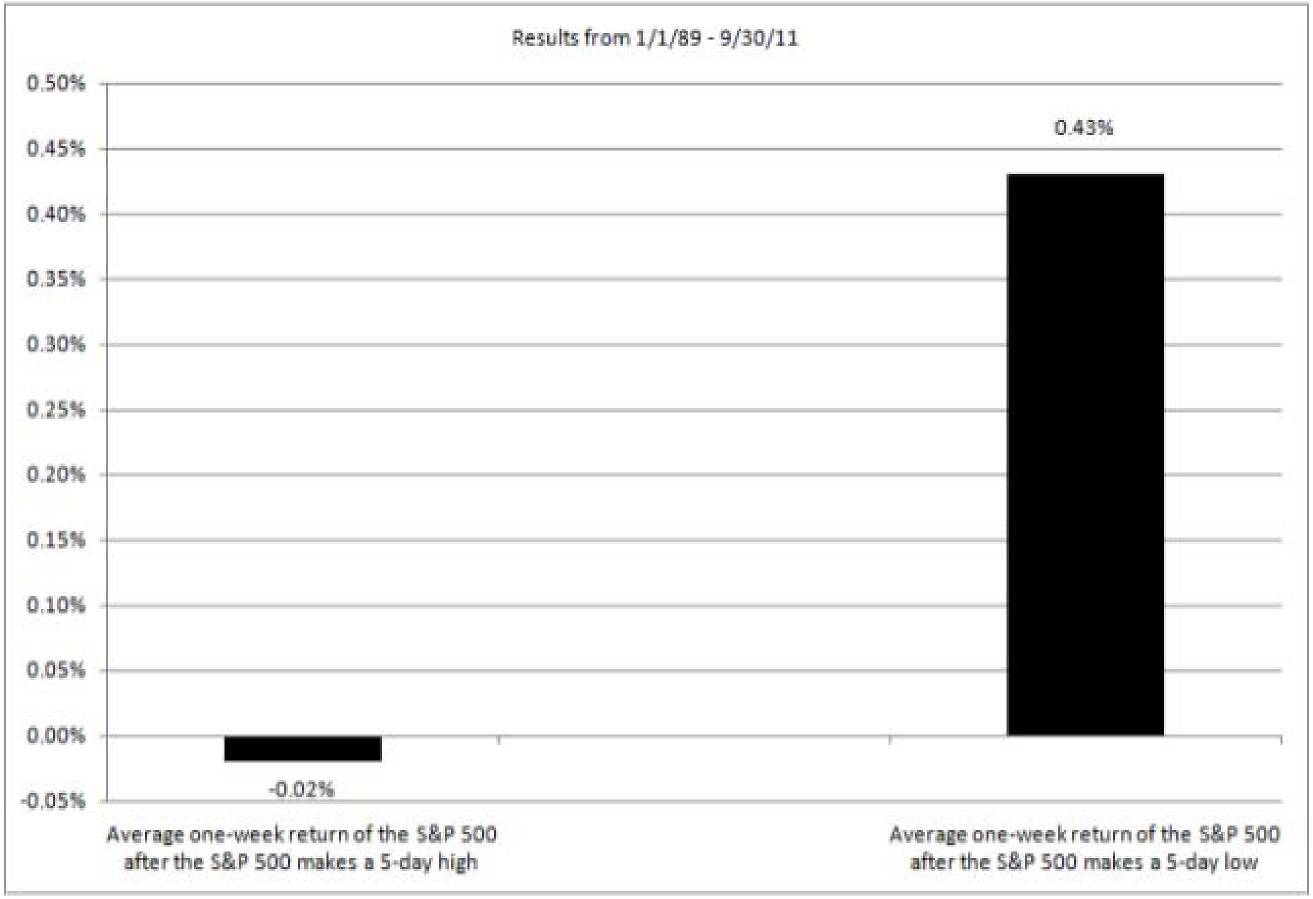
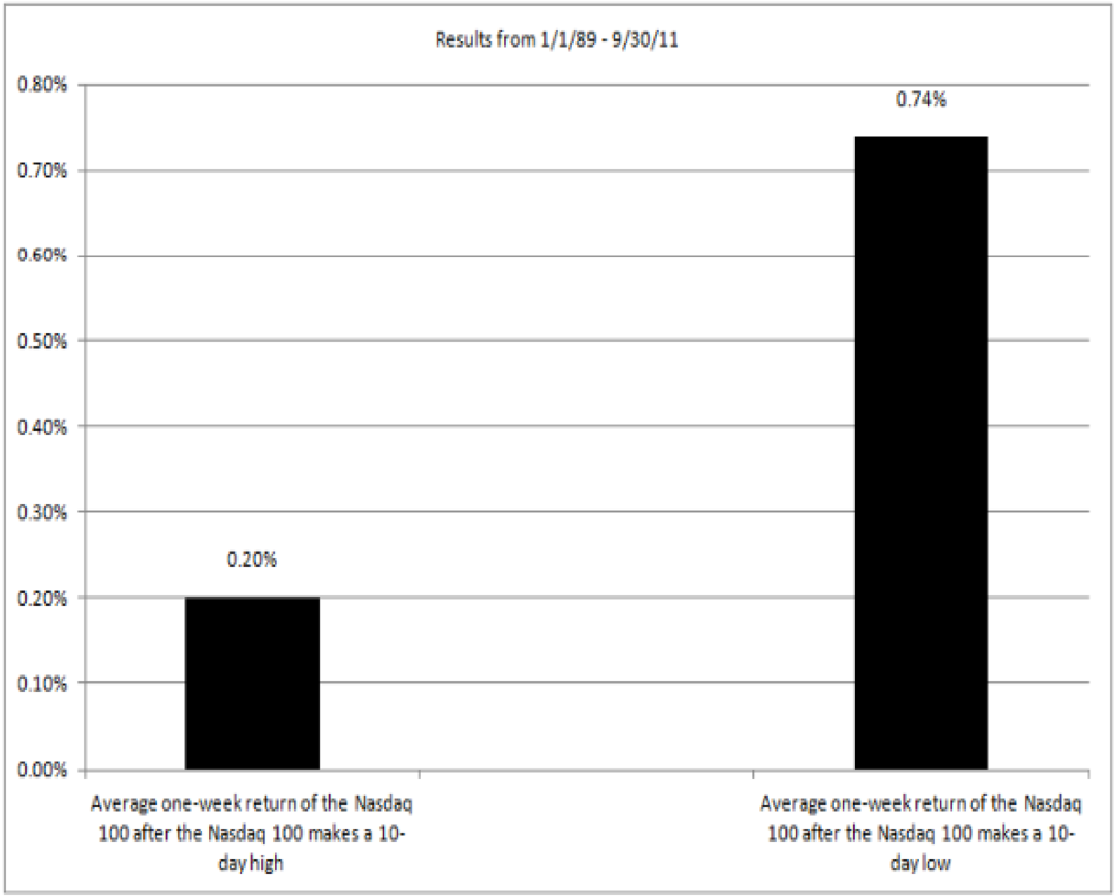


Figure 2-4. Nasdaq 100. 10-day Lows Outperformed 10-Day Highs by a Better Than 3-1 Margin



From Chapter 4…

It’s better that the market has gone down today than gone up.

Figure 4-5. Nasdaq 100. Two Down Days in a Row in the Nasdaq Outperformed 2 Up Days in a Row After 1 Week

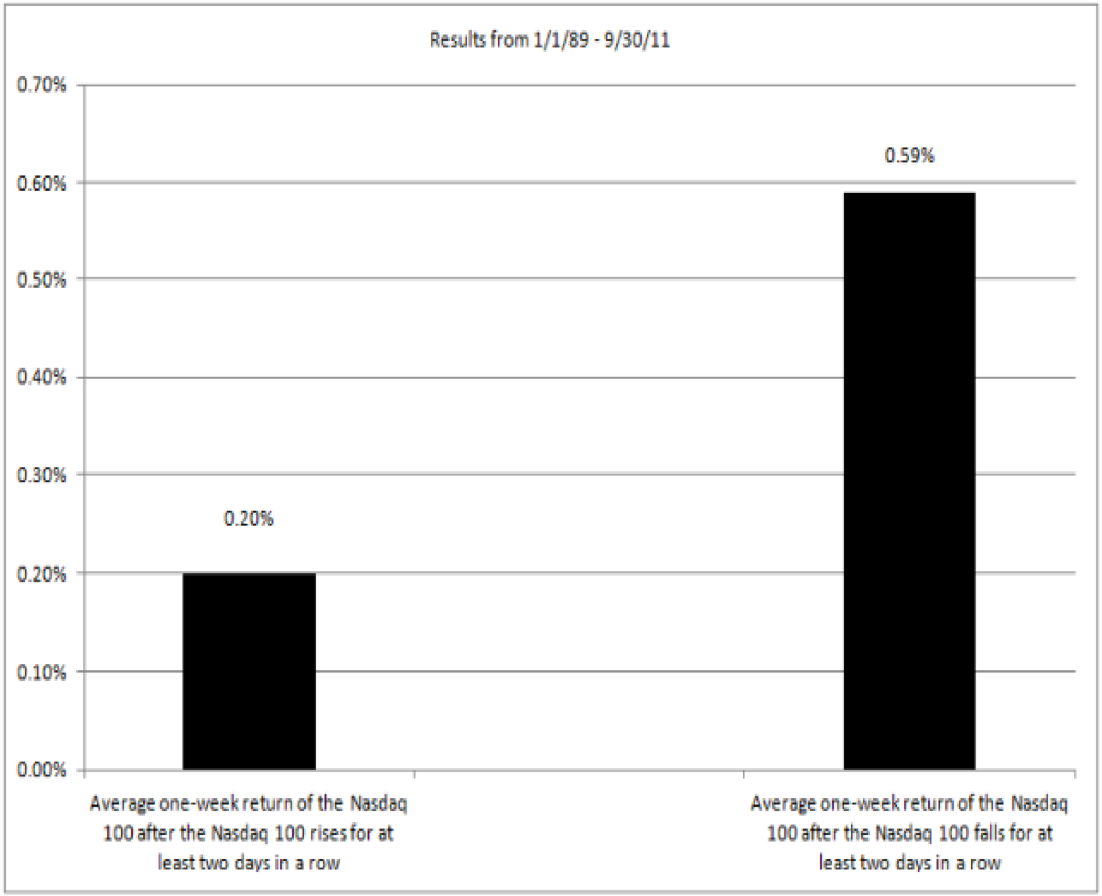
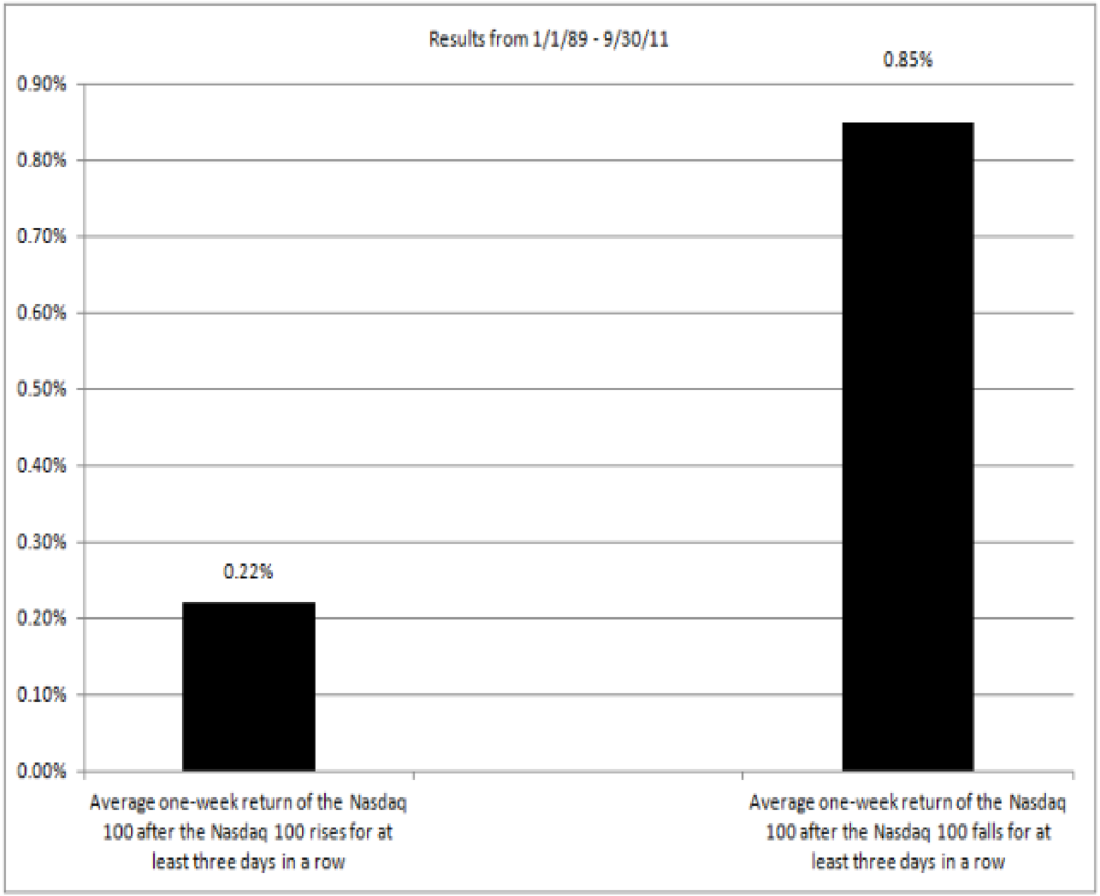


Figure 4-6. Nasdaq 100. 3 Down Days in a Row Have Outperformed 3 Up Days in a Row in the Nasdaq by an Almost 4-1 Margin After 1 Week



From Chapter 7…

Large one-day moves down are better than large one-day moves up.

Figure 7-2. S&P 500. 2% Declines Have Outperformed 2% Gains in the S&P 500 After 1 Week

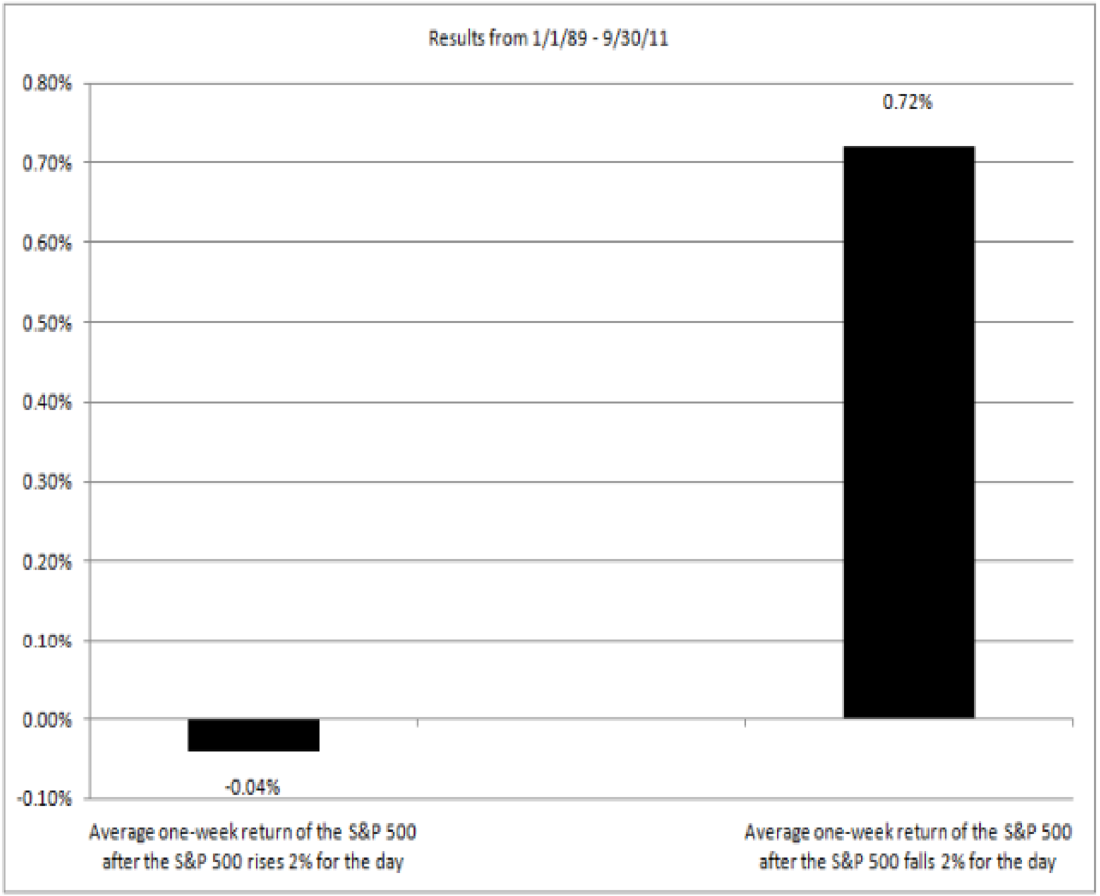
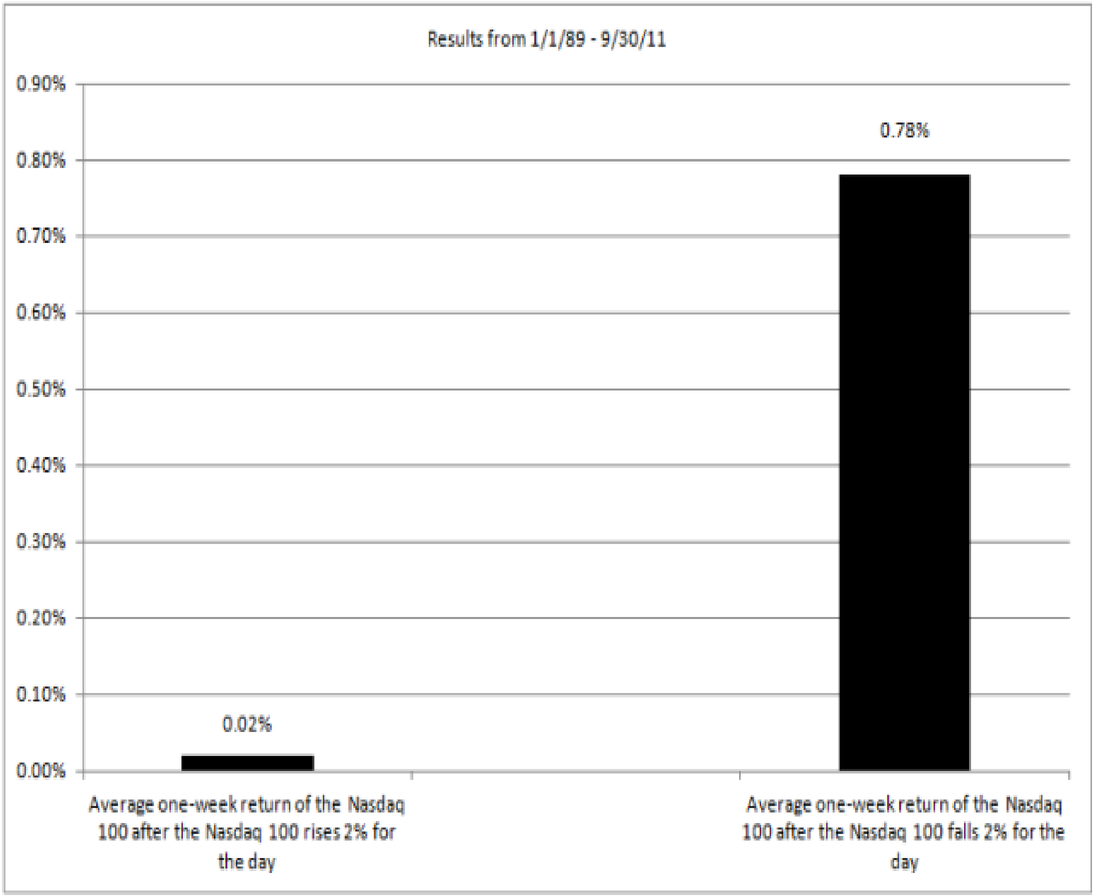


Figure 7-4. Nasdaq 100. 2% Nasdaq Losses Have Outperformed 2% Nasdaq Gains by a Significant Margin After 1 Week



From Chapter 12…

Don’t invest in high volatility stocks.

Table 12-1. Historical Volatility (100-day) Test Results, 1/1/1995 to 9/30/2011 (8,058 Symbols)

	Bucket	Return 252 Trading Days Later	% Winners	Avg % Loss of Losing Trades
Lowest HV	1	9.7%	66.0%	-19.8%
	2	10.3%	61.1%	-25.2%
	3	10.6%	56.7%	-30.9%
	4	9.8%	51.1%	-37.4%
Highest HV	5	5.4%	44.2%	-44.4%

There are 14 chapters of information like this in *How Markets Really Work, 2nd Edition,* recently published by Bloomberg Financial.

From the
Connors Research Trading Strategy Series

ETF Gaps Trading

A gap is simply a security whose opening price is either above or below the previous day’s high or low.

So when have gap reversals made money?

When the gap has occurred after the ETF was already oversold.

Here are the rules of our version of ETF Gap Trading:

1. We looked at every ETF from 2006-2011 that has had an average volume of at least 250,000 shares, and at least 50,000 shares per day, over the past 21 trading days (one month). We do this to assure we're only trading liquid ETFs.

Here are the rules of our version of ETF Gap Trading:

2. The 2-period RSI of the ETF closes under 5 today. This tells us that the ETF is oversold (some people consider this level to be extremely oversold).

3. Tomorrow buy the ETF on the open if it gaps lower (it opens below today's low).

Here are the rules of our version of ETF Gap Trading:

4. We look at multiple exit points in the *ETF Gap Trading Strategy Guidebook* but for today's meeting let's look at the test results if we exit on the close when the ETF closes above its 3-period moving average.

And here are the test results...

ETF Gap Trading Results, 2006-2011.

No. of Trades	Avg. % Profit/Loss	Avg. Trading Days Held	% Winners	Exit Methodology	Limit Entry %	Long/Short
2,170	1.17%	2.13	72.07%	C>MA3	0%	Long

If you would like to take a closer look at this strategy or any of our other strategies in the *Connors Research Trading Strategy Series*, please click on the links below:

Stock Gaps
http://tinyurl.com/tradestockgaps

Stock Pullbacks
http://tinyurl.com/tradestockpullbacks

ETF Gaps
http://tinyurl.com/tradeetfgaps

To Summarize What We Learned Today

1. Traders like Ed Thorp, James Simons of Renaissance Technologies, and many others have made fortunes by identifying and trading statistical anomalies.

2. Many of these statistical anomalies occur on a short-term basis in oversold conditions when fear is at it's greatest.

3. On longer-term investments, stability (low volatility) outperforms high volatility.

4. Statistical anomalies still exist today in a number of mainstream strategies as we just learned looking at ETF gaps.

5. **It's not about emotion, it's about statistical results!**

Questions and Answers

If you have any questions about this presentation or about our *Connors Research Trading Strategy Series*, please feel free to contact me at lconnors@connorsresearch.com

Thank You!

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