



THE

JANUS

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FACTOR

# Jan



**“In some seasons trend following is good; in others, reversing is good.”**

Victor Niederhoffer, The Education of a Speculator

# **1. Feedback systems**

**1. Feedback systems**

**2. A binary method for  
calculating relative strength**

**1. Feedback systems**

**2. A binary method for  
calculating relative strength**

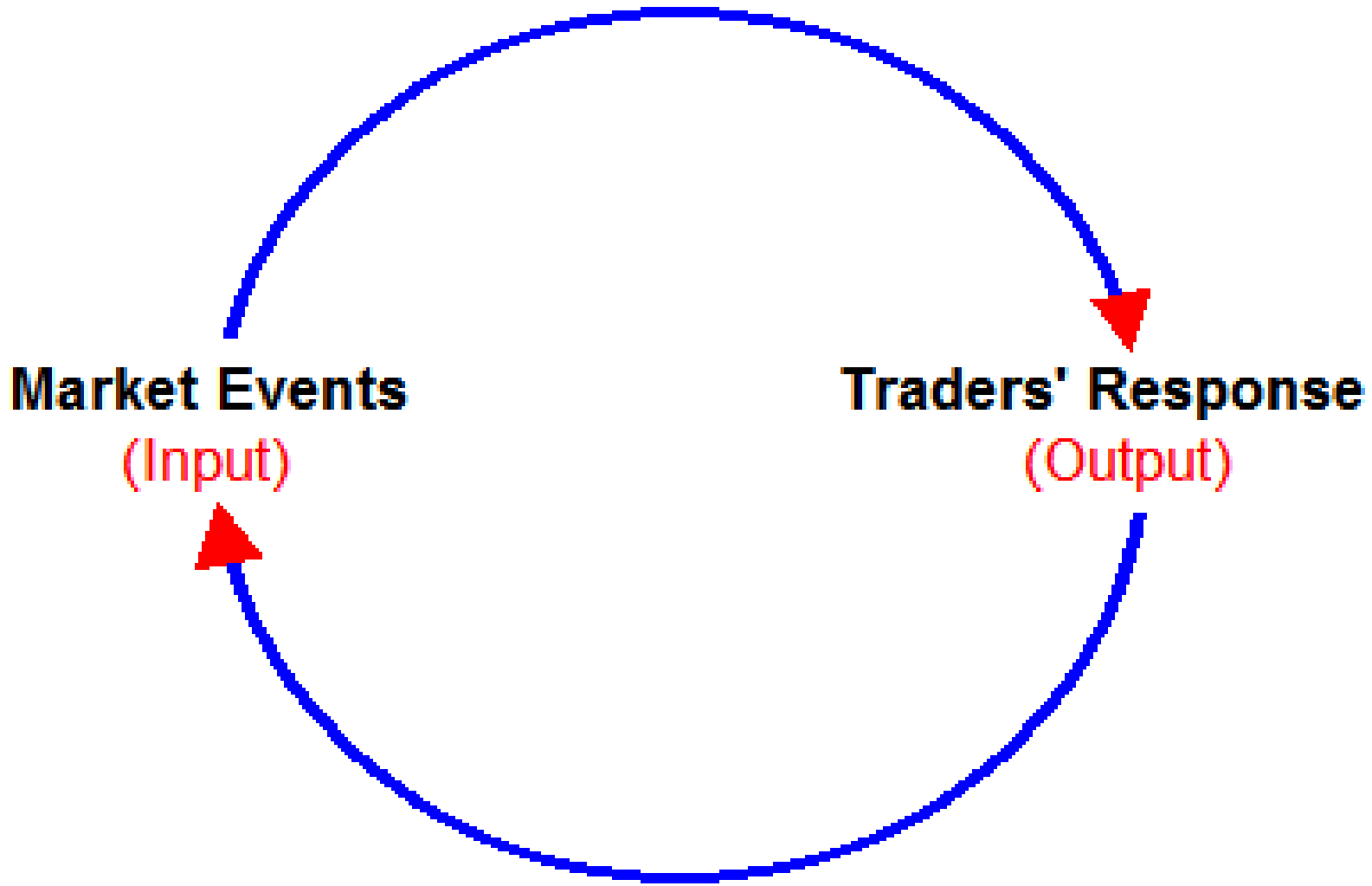
**3. Key indicators**

- 1. Feedback systems**
- 2. A binary method for  
calculating relative strength**
- 3. Key indicators**
- 4. A long strategy**

# Feedback Systems



# Feedback System



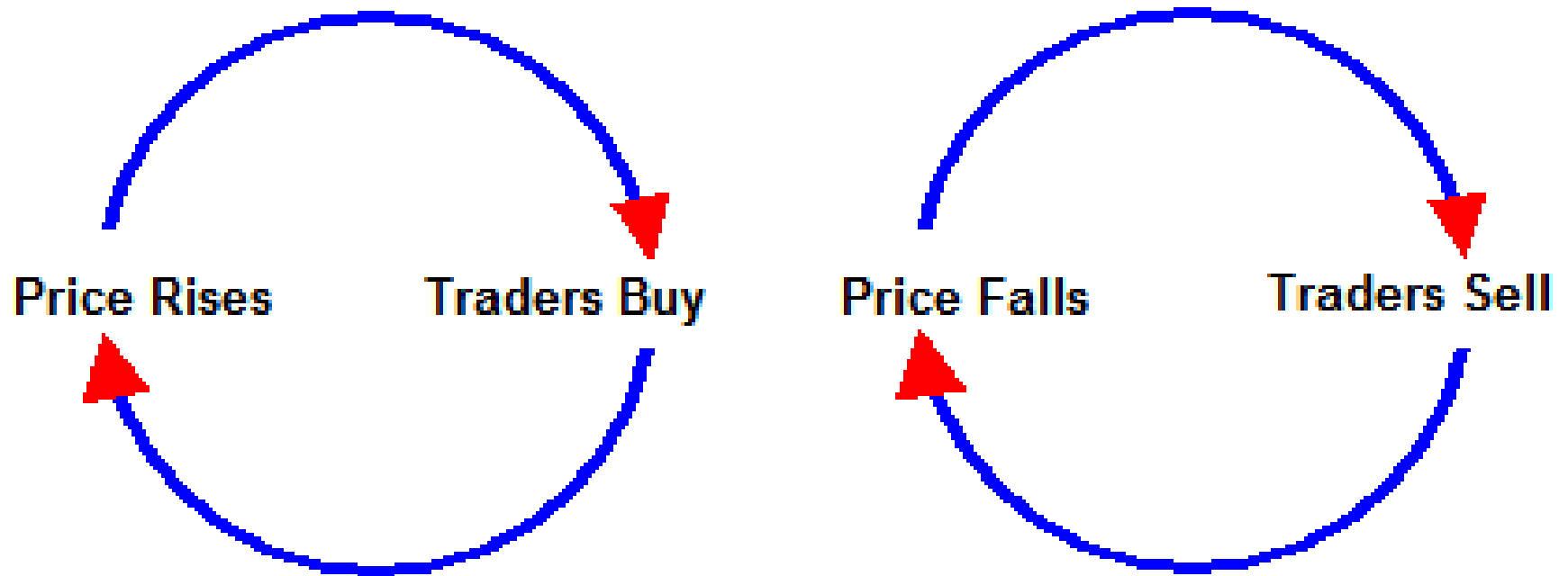
# Positive Feedback

**Amplified Audio Screech**

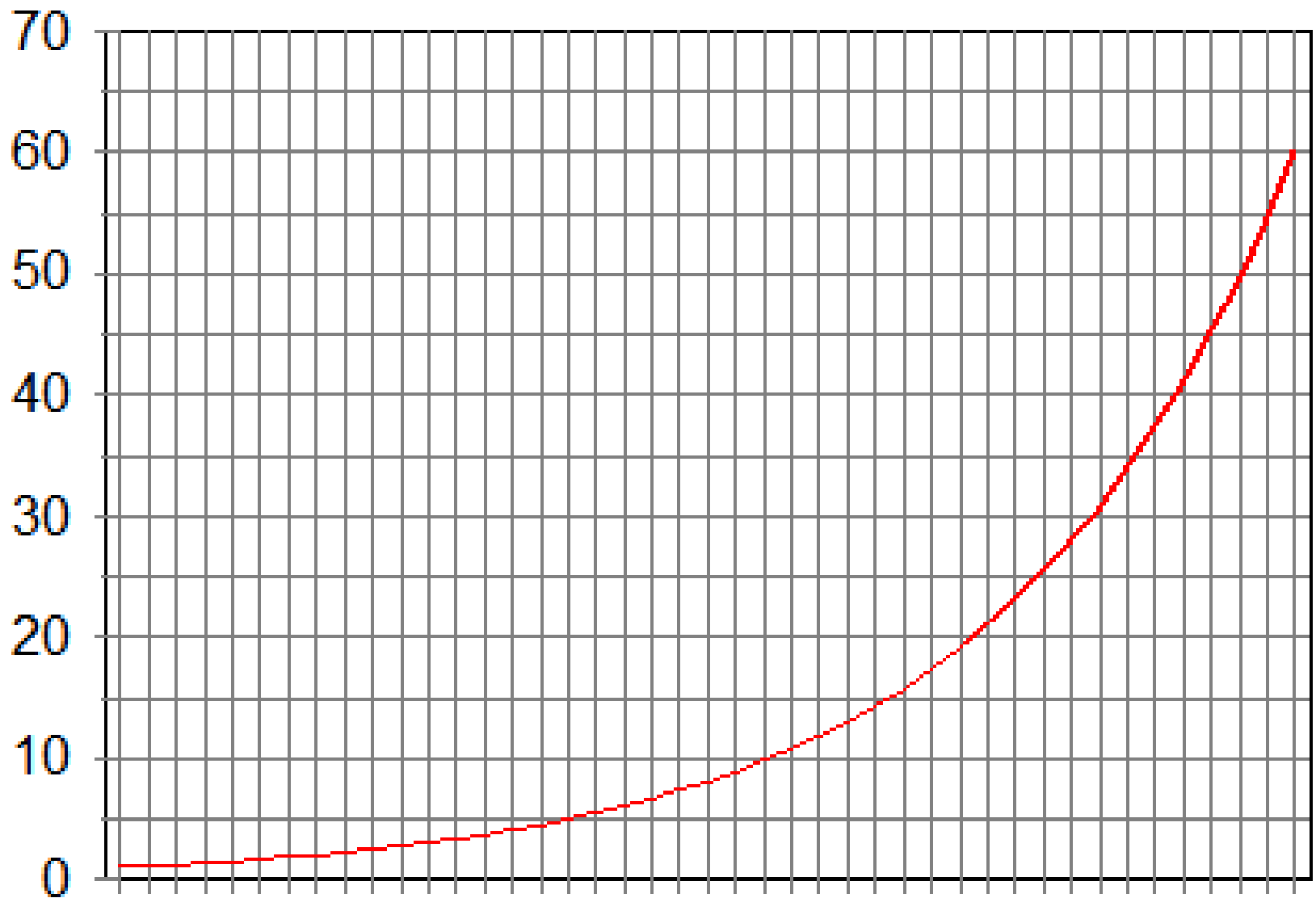
**Thermonuclear Bomb**

**Burning House**

# Positive Feedback



# Positive Feedback = Acceleration



**Positive feedback creates  
a trend.**

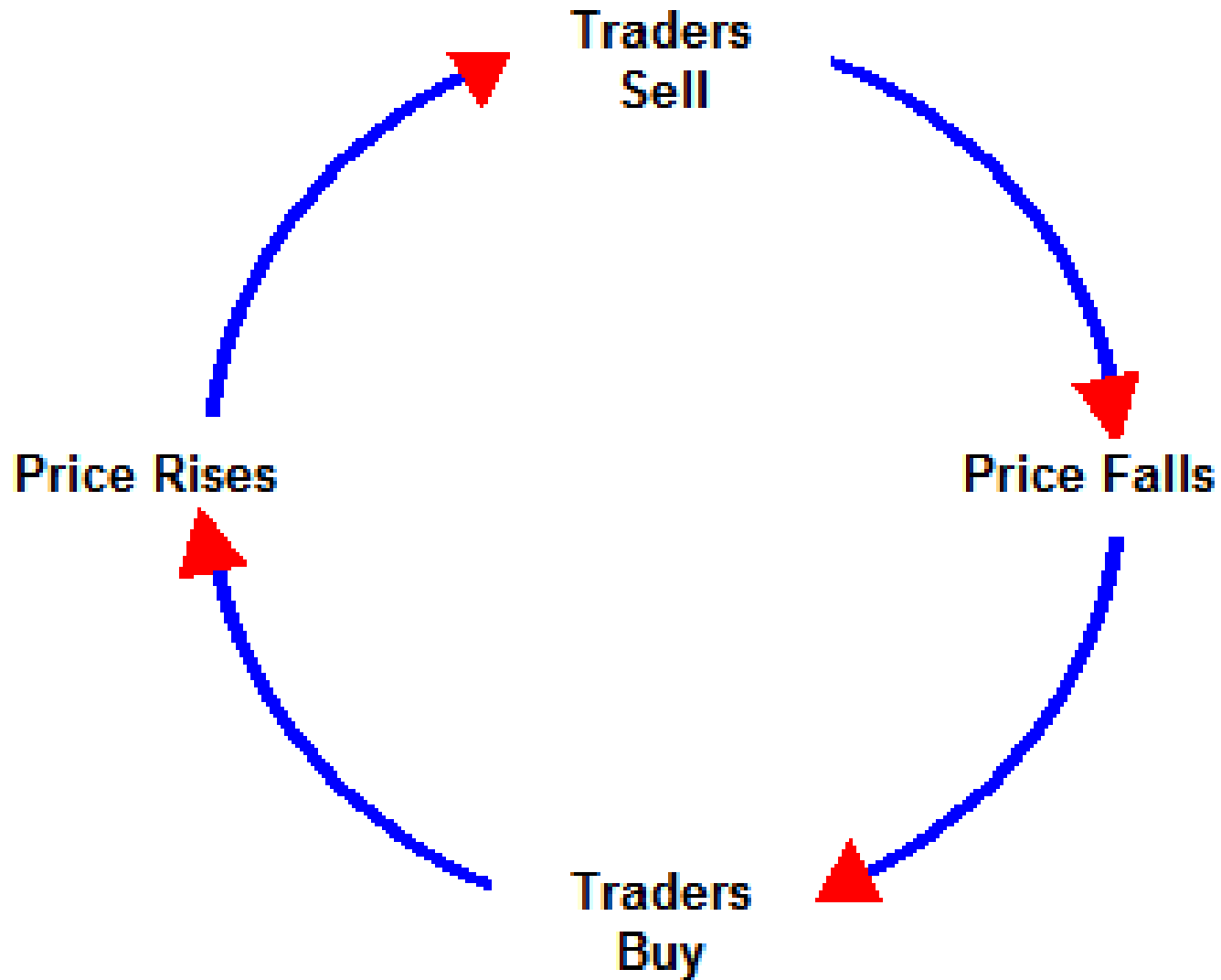
# Negative Feedback

**Thermostat**

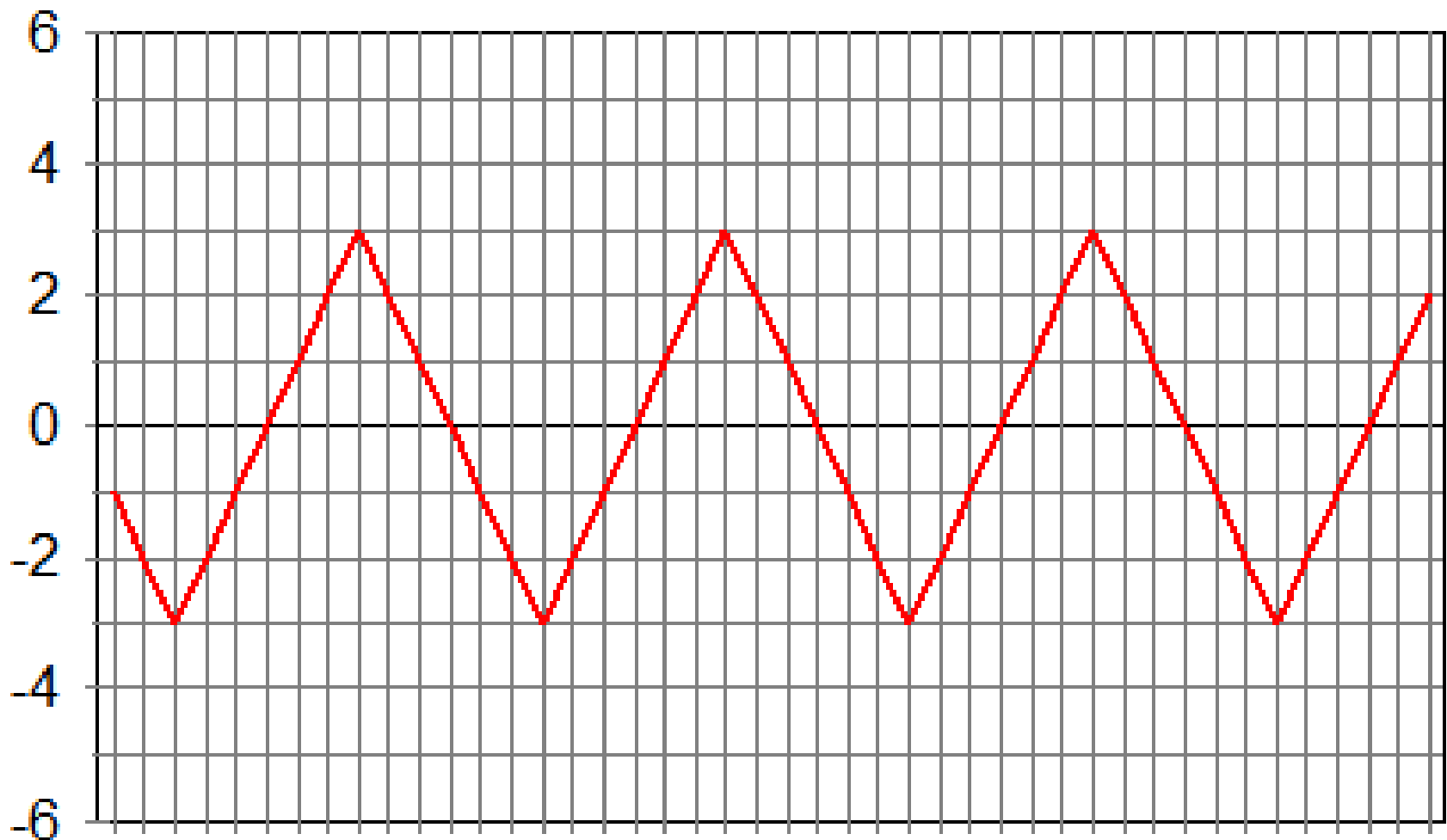
**Engine Governor**

**Predator-Prey**

# Negative Feedback



# Negative Feedback = Stable (Cycle)

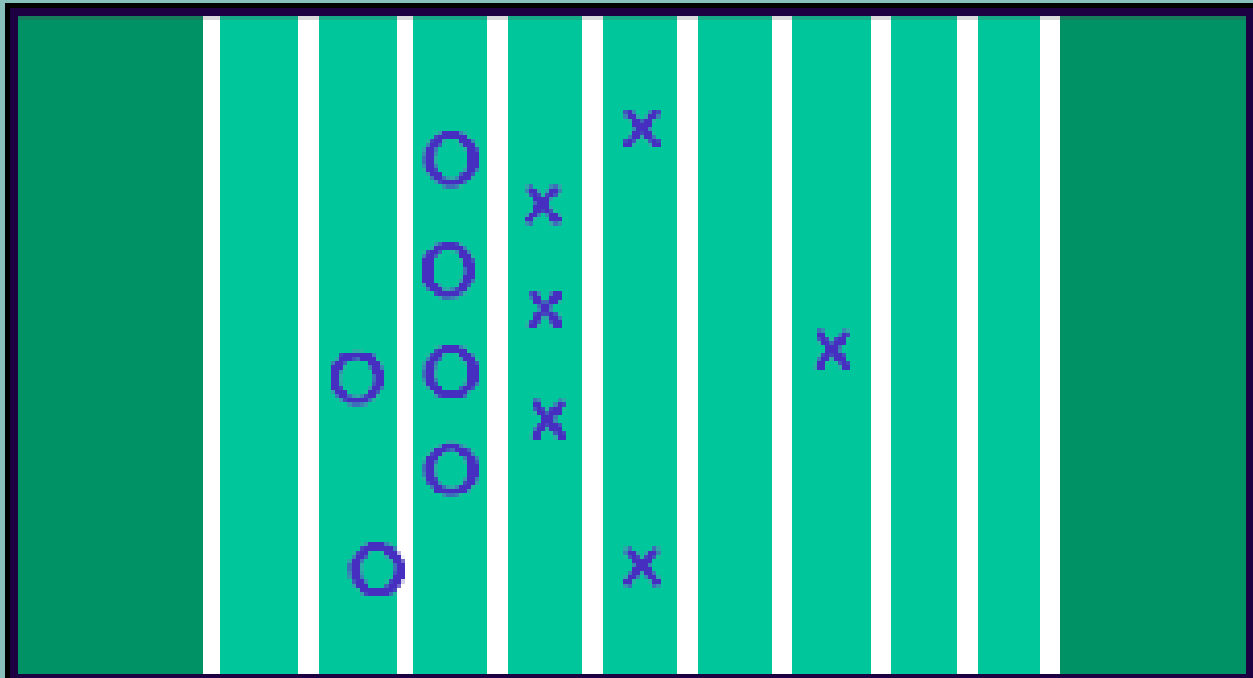




**Negative feedback counters  
the trend.**

**RISK**  
**VIEW**

# Offense and Defense

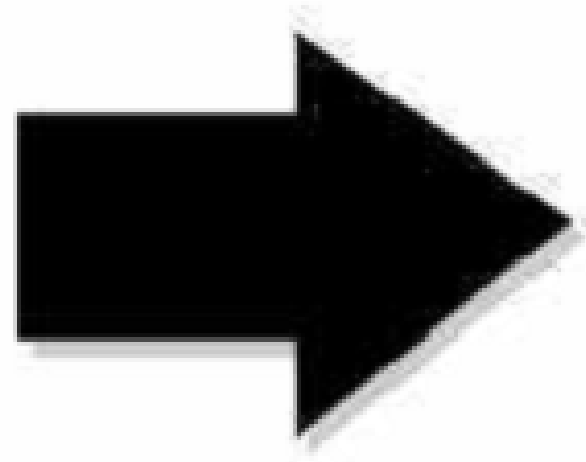
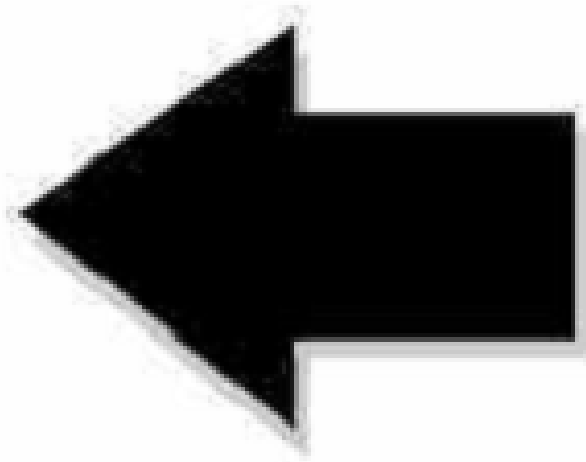


# DEFENSE

**The defensive qualities of a stock/group are most severely tested during periods of market weakness, when the risk of loss is most acute.**

**Stronger Defense**

**Weaker Defense**



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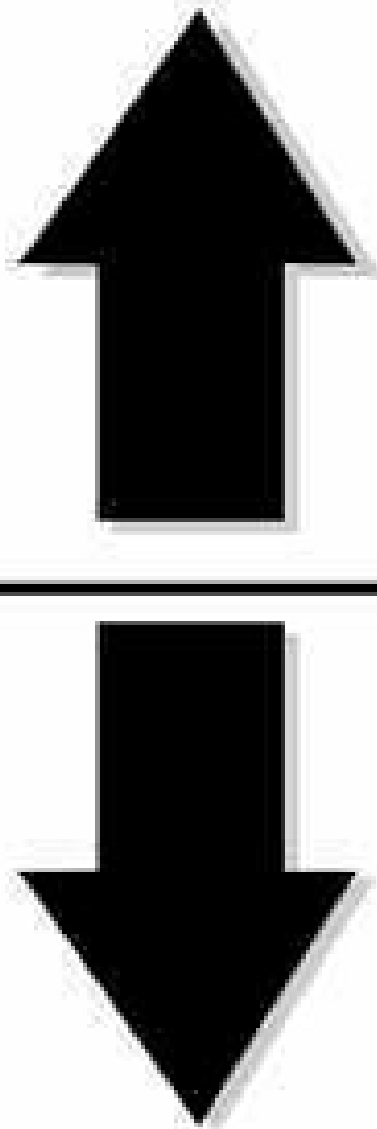
**DEFENSE**

# OFFENSE

**Since the risk of lost opportunity is greatest as the market rises, the offensive qualities of a stock/group are best measured as the market advances.**

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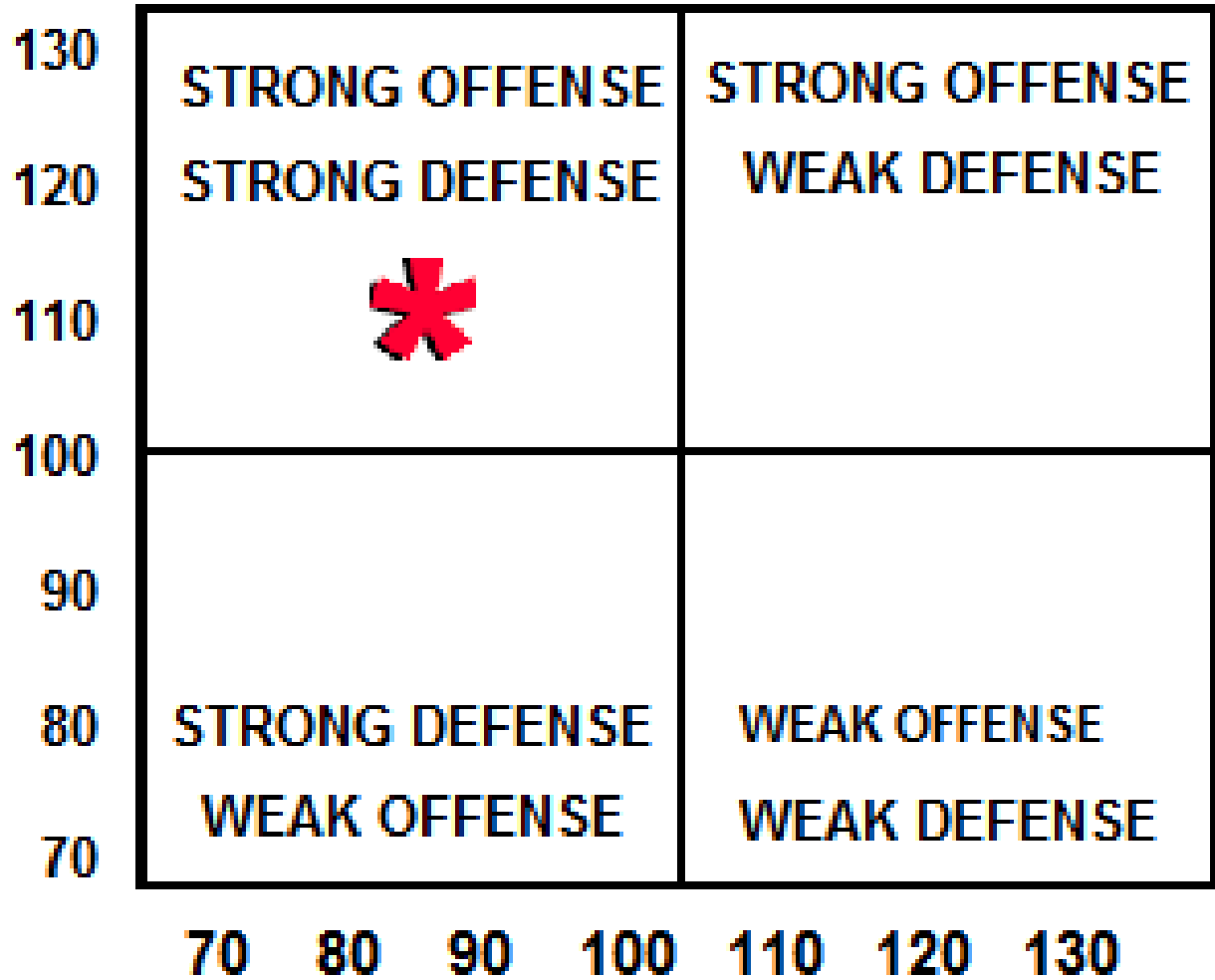


**Stronger Offense**

**BENCHMARK**

**Weaker Offense**

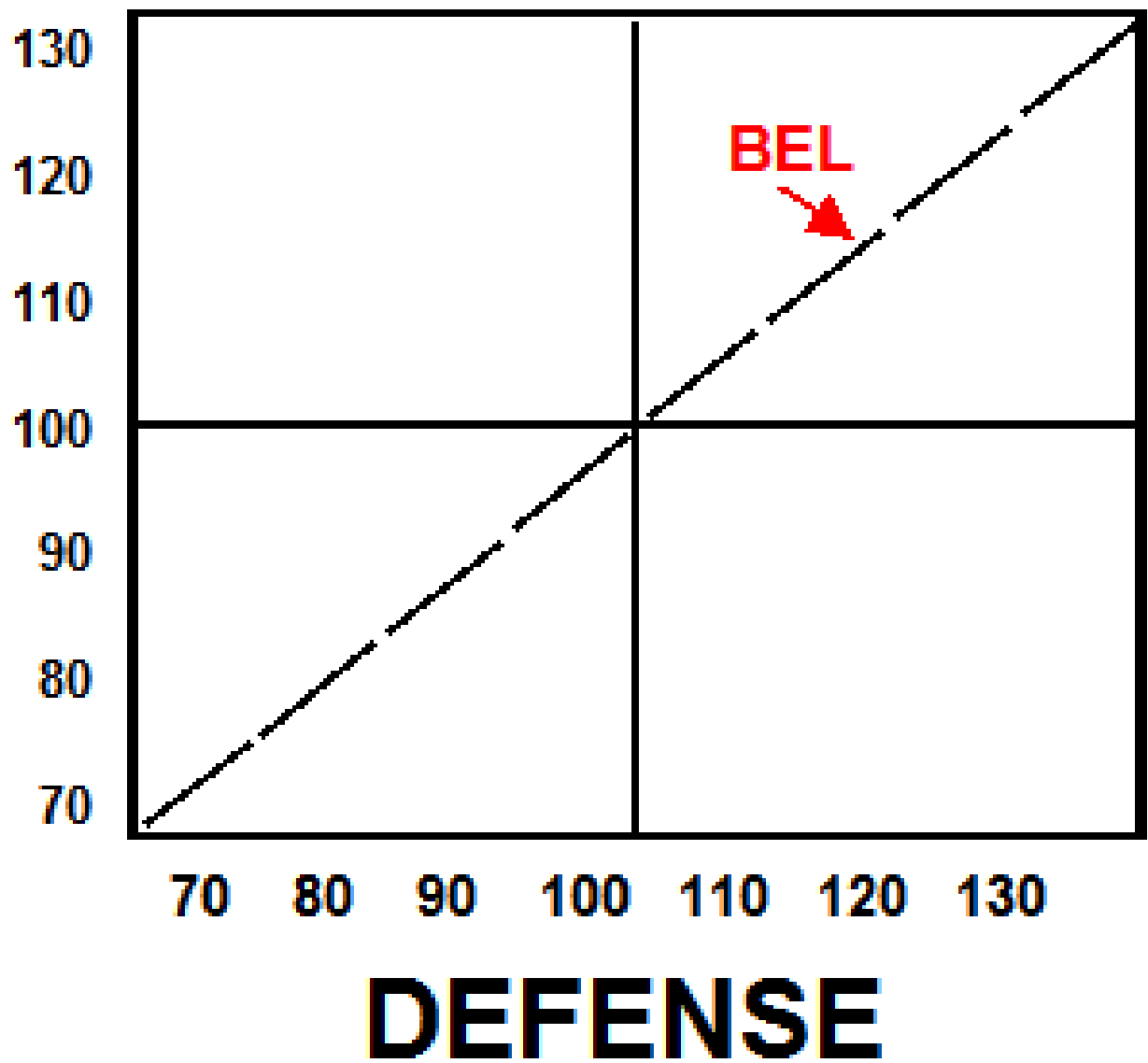
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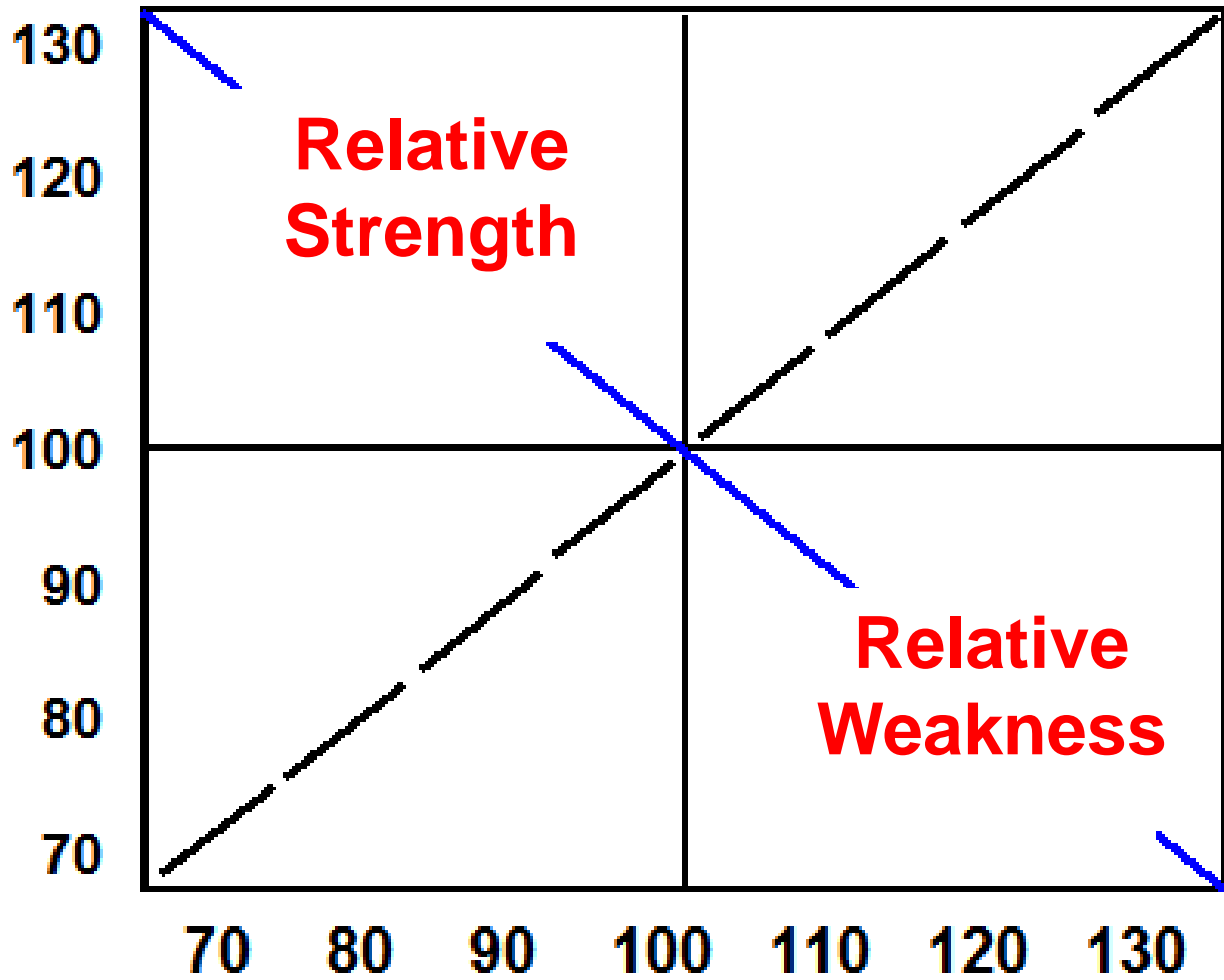
**DEFENSE**



**OFFENSE**

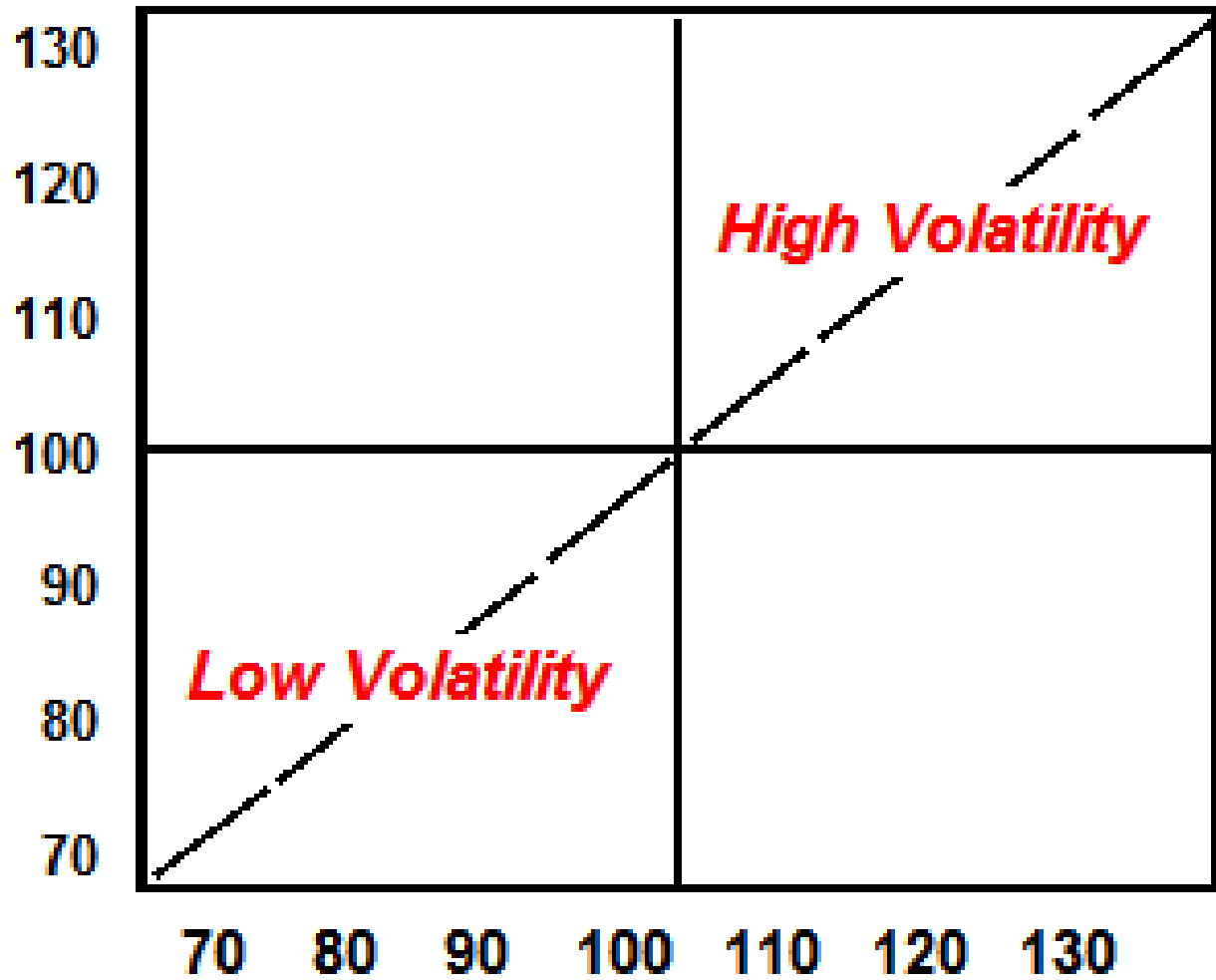


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**DEFENSE**

**OFFENSE**



**DEFENSE**

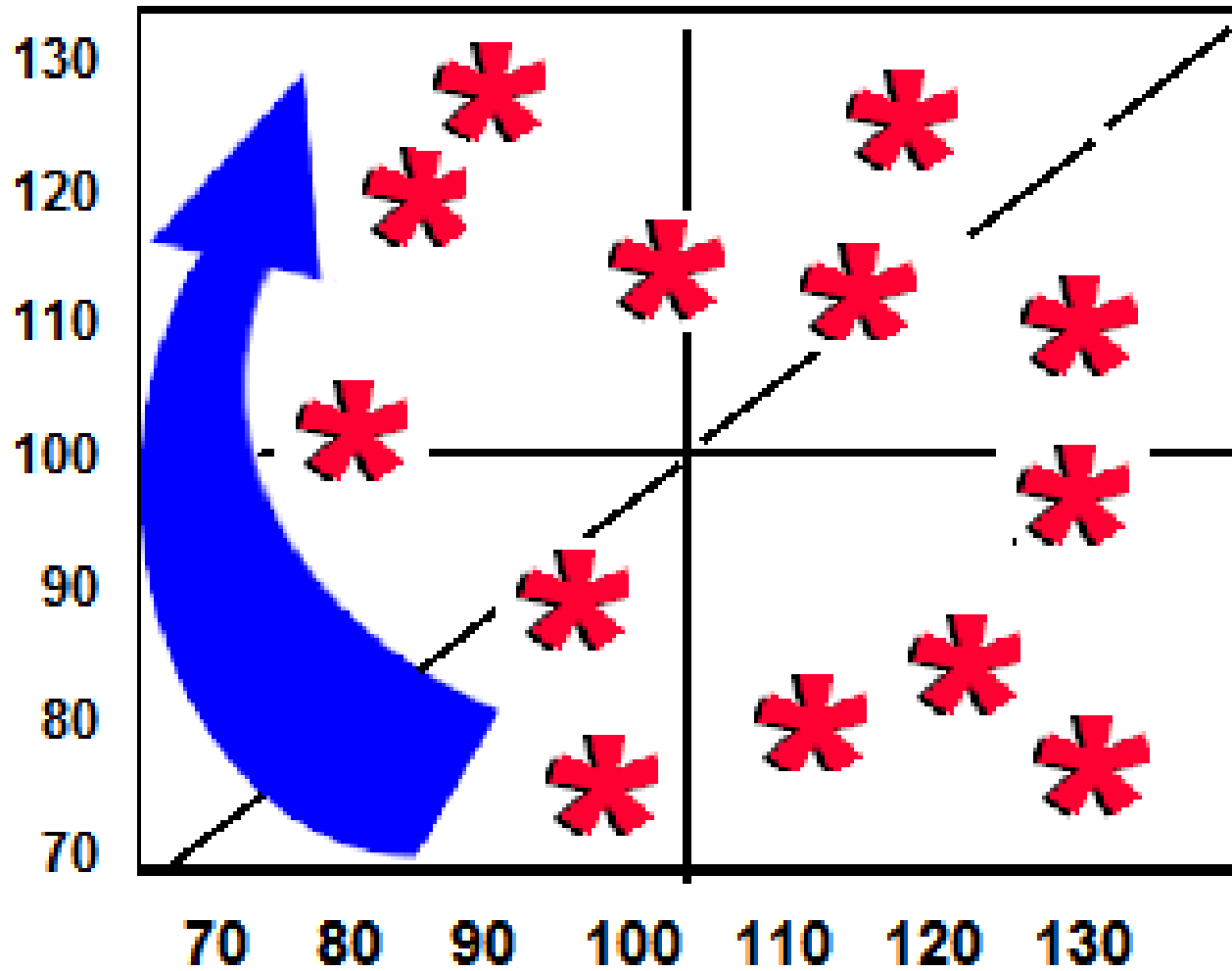
# How Feedback Generates Systematic

***CAPITAL FLOW*** 

# **Positive Feedback**

**Traders buy strength  
and/or sell weakness.**

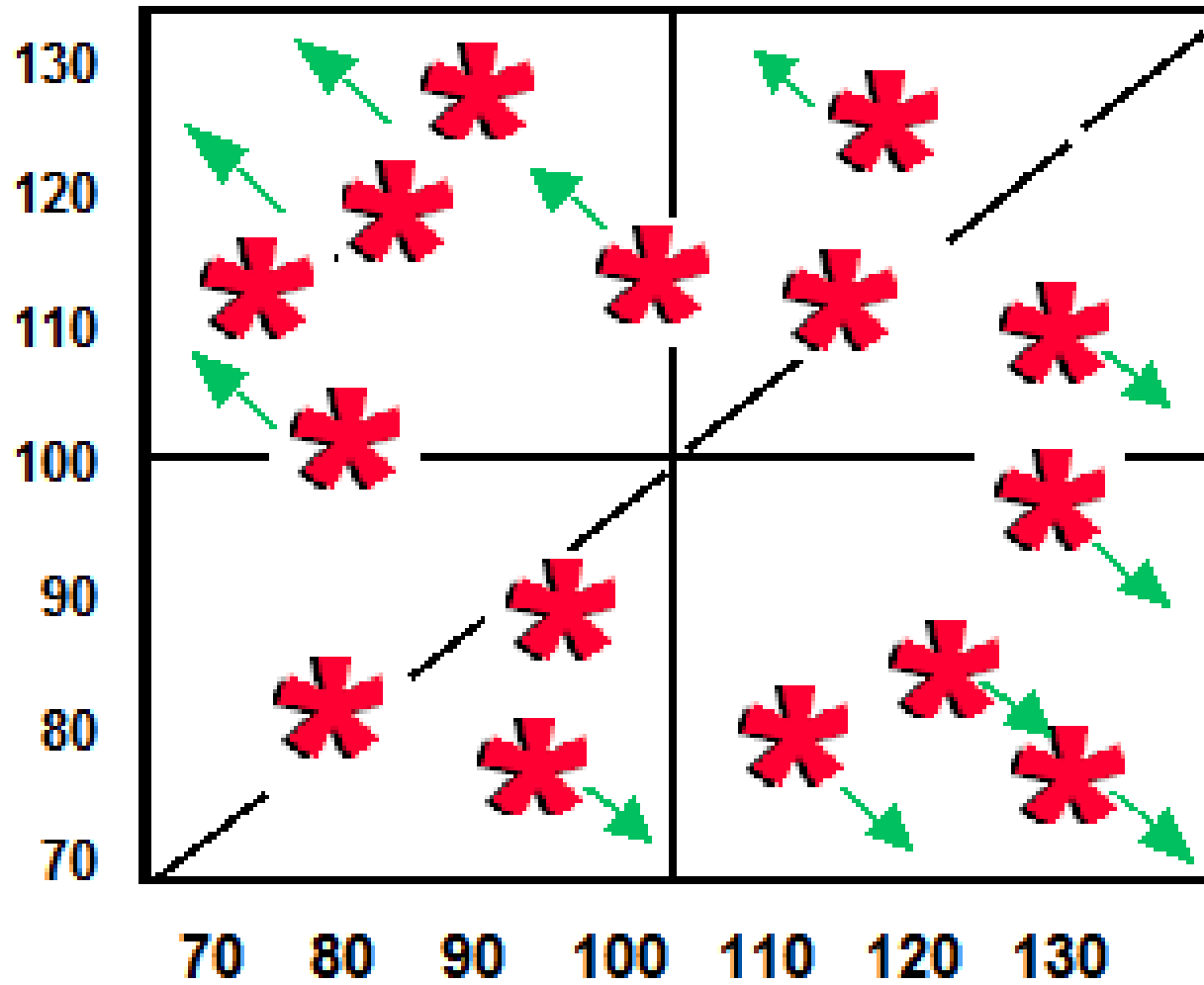
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DEFENSE

# Expanding Universe

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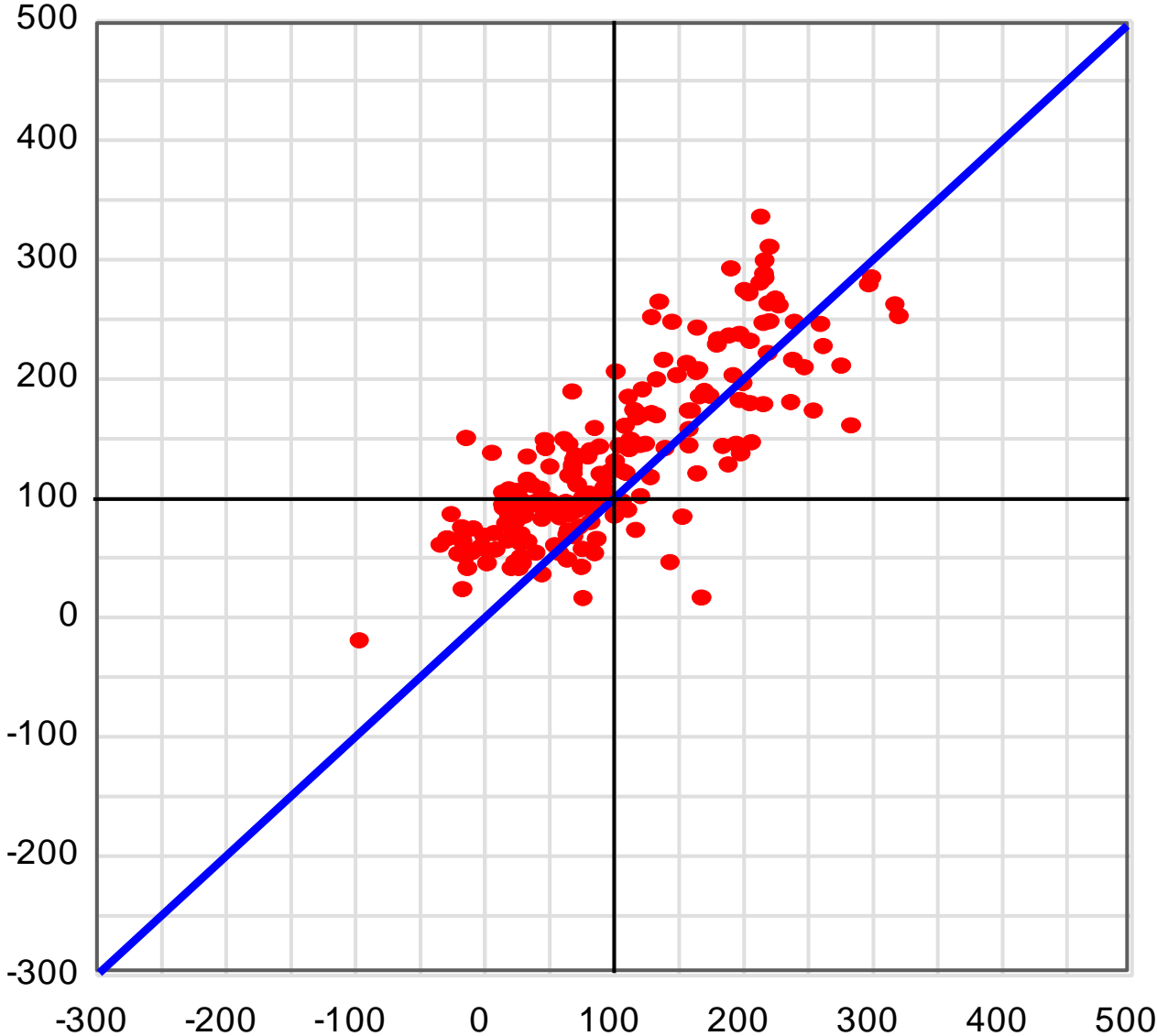
**DEFENSE**

# **Positive Feedback as the Market Advances**

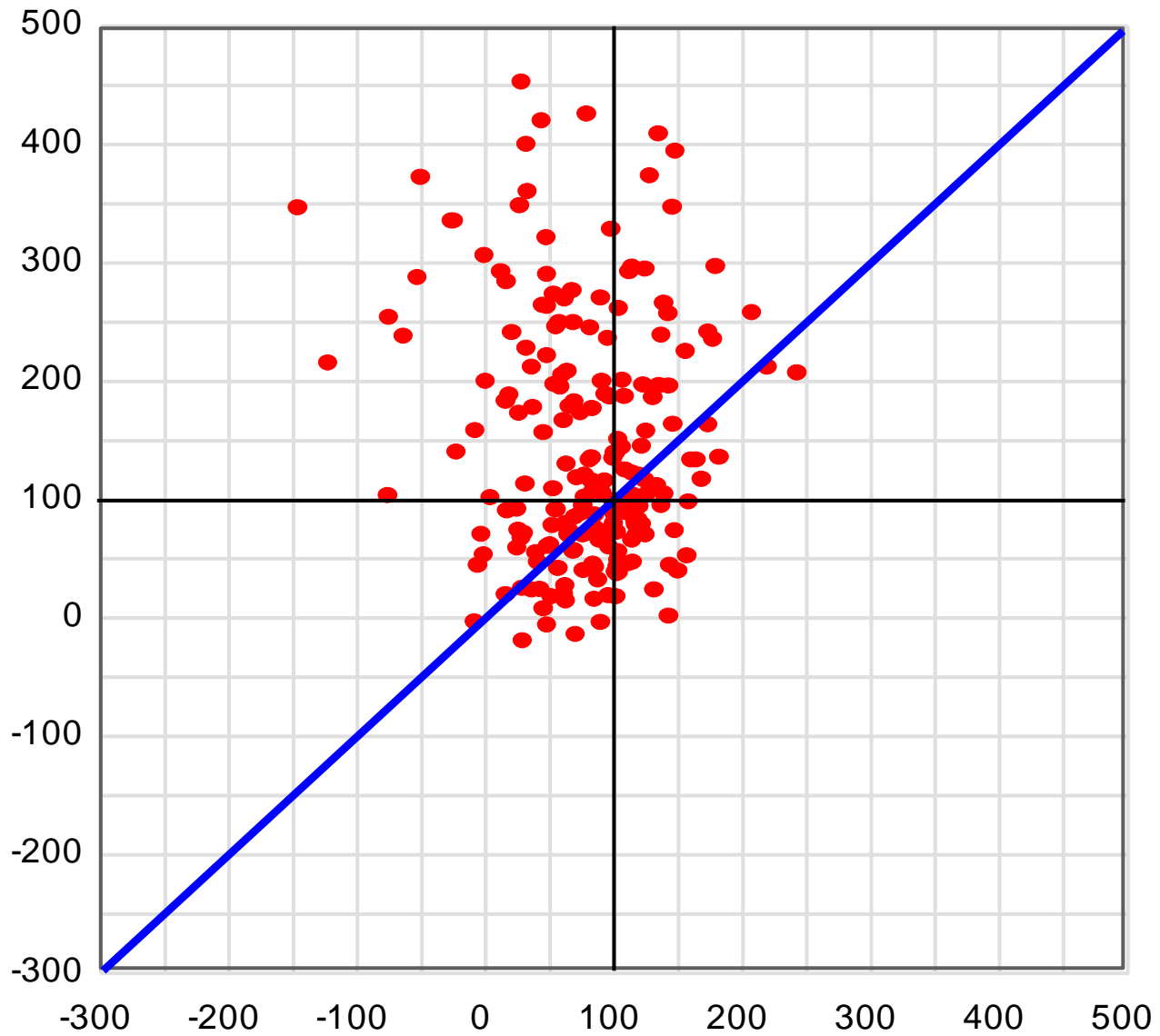
**Strongest stocks lead the way  
higher.**



# June 1999



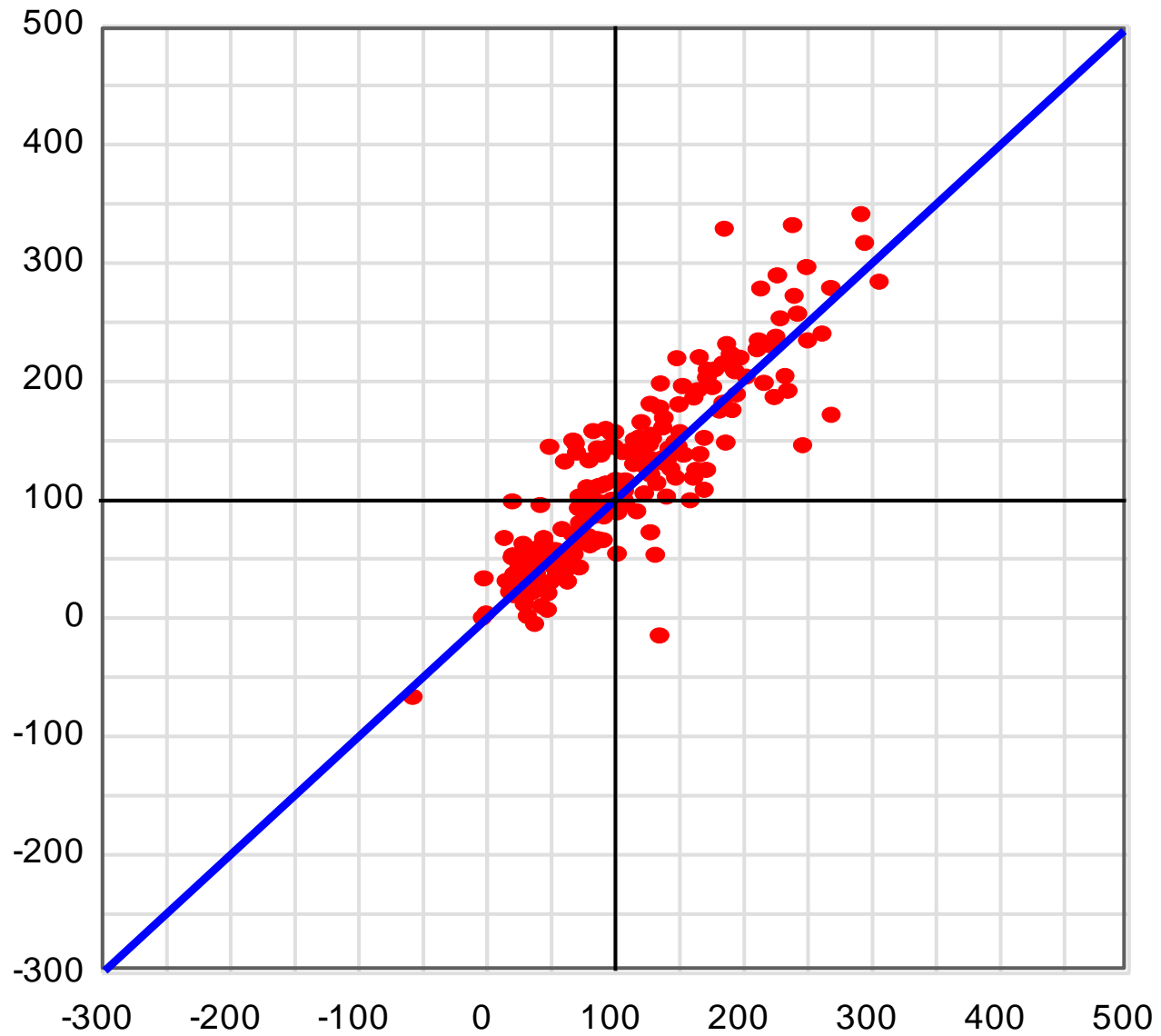
# March 2000



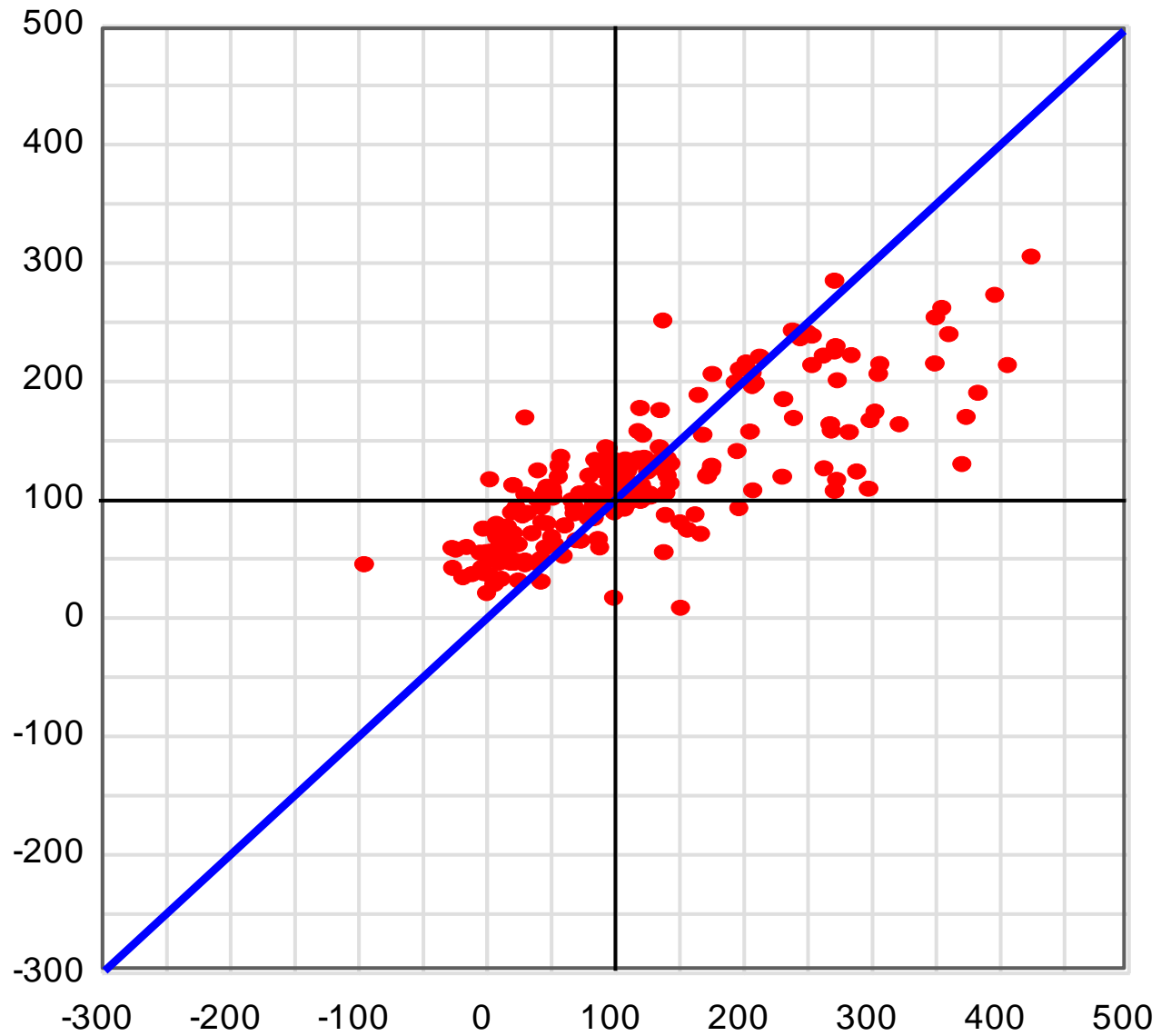
# **Positive Feedback as the Market Declines**

**Weakest stocks lead the way  
lower.**

# December 2001



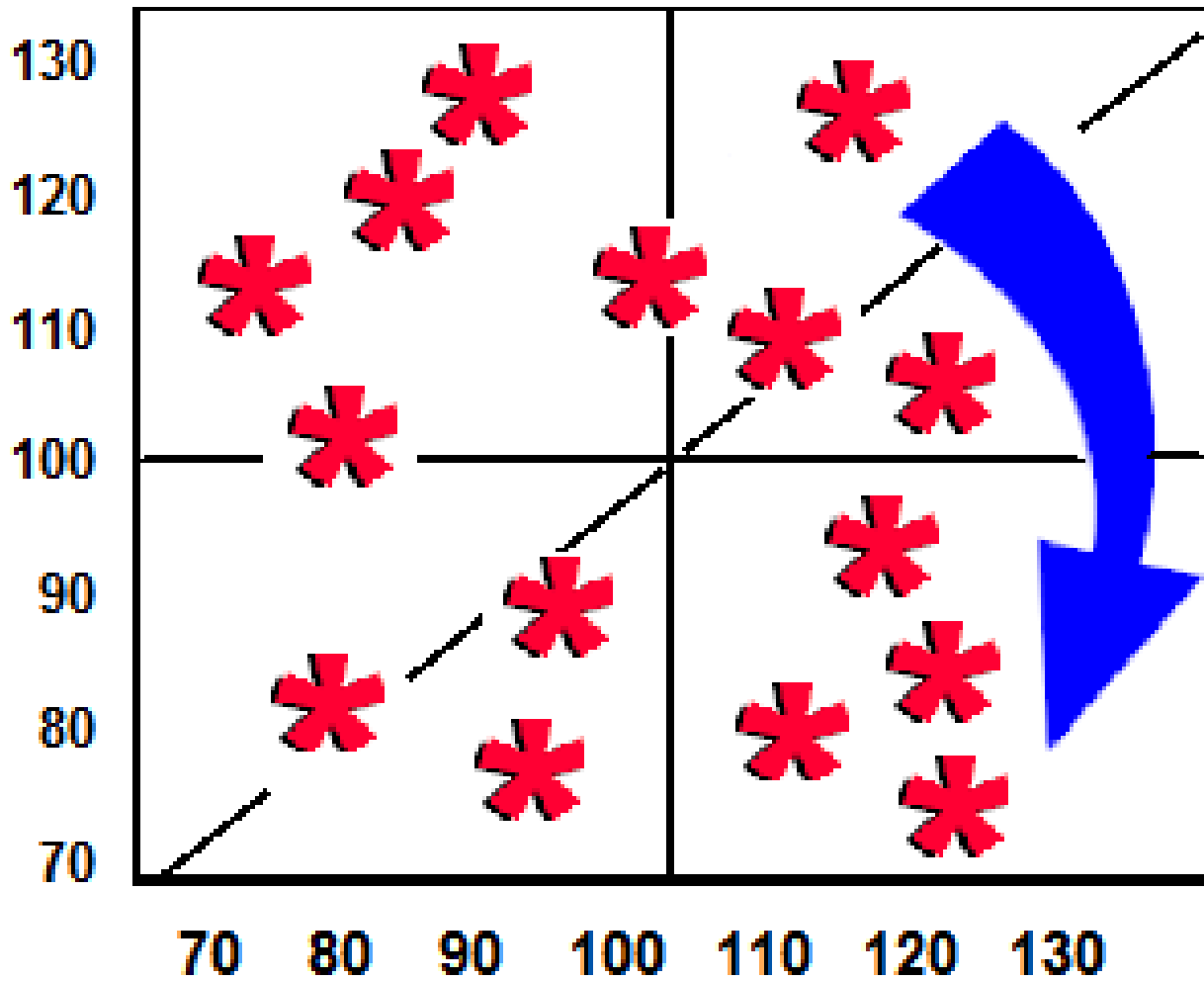
# May 2002



# **Negative Feedback**

**Traders sell strength  
and/or buy weakness.**

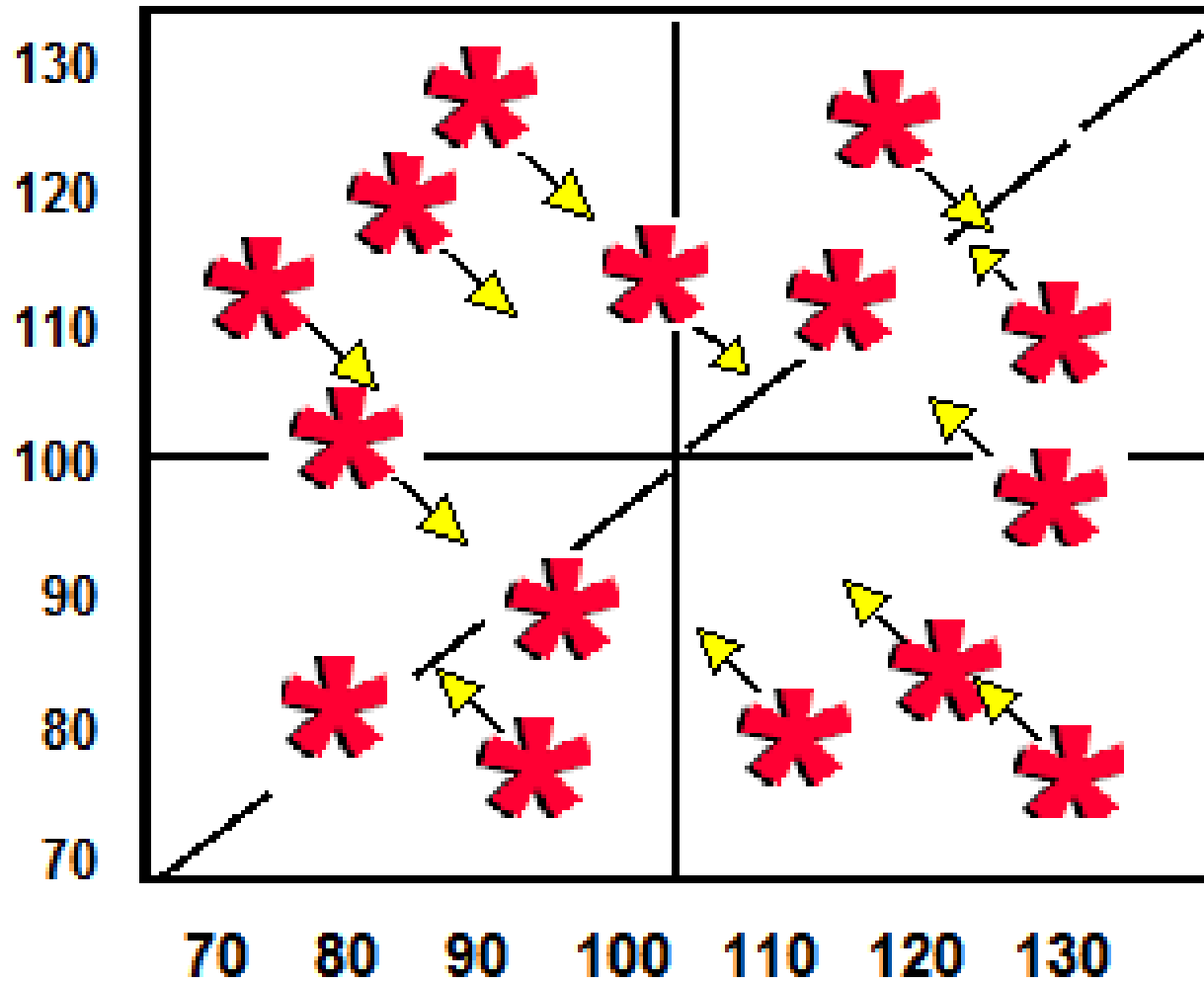
**OFFENSE**



**DEFENSE**

# Contracting Universe

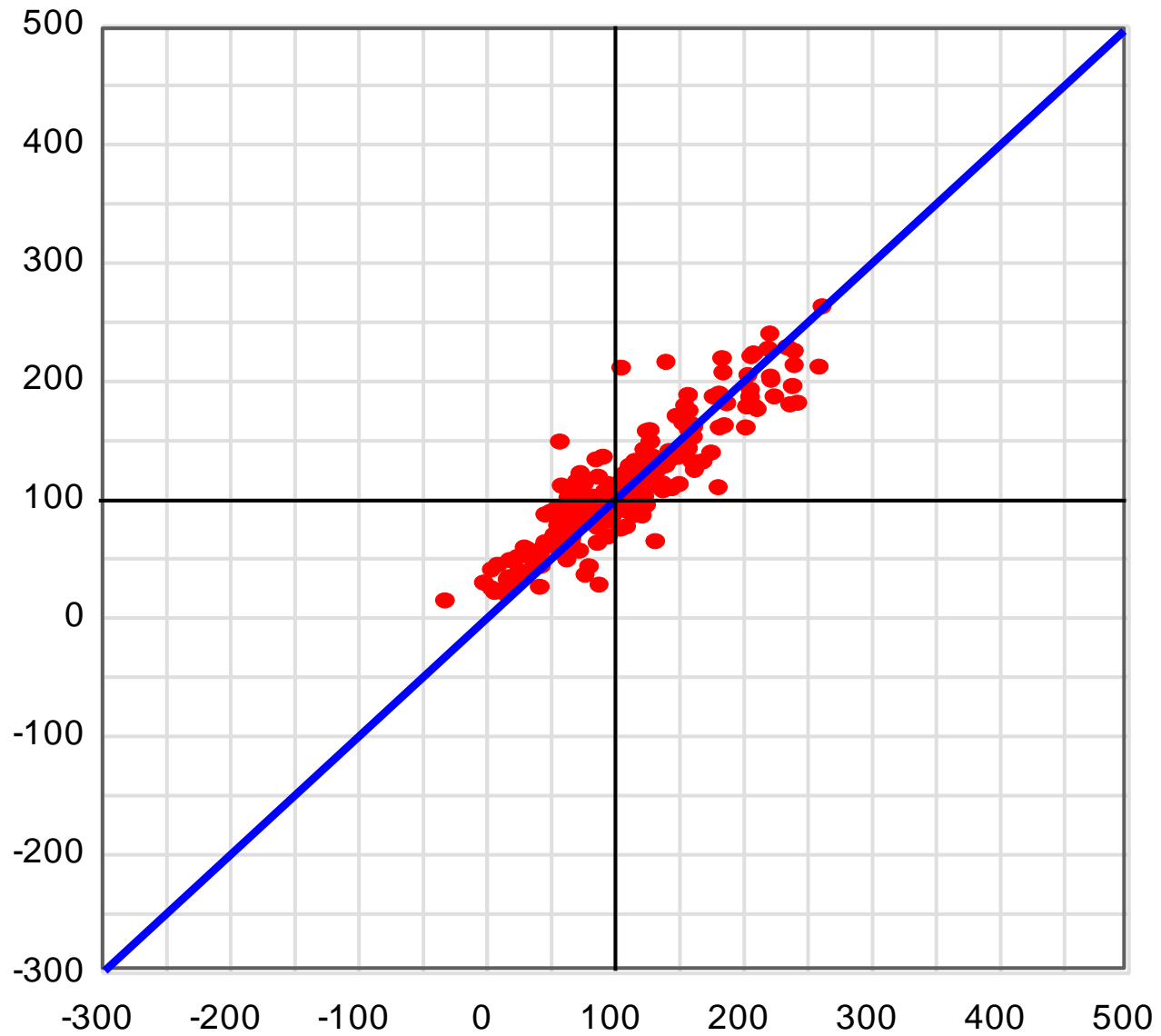
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**DEFENSE**



# December 2002



**“The prime mover in a financial market is not value or price, but price *differences*; not averaging, but arbitraging.”**

Benoit Mandelbrot, The (Mis) Behavior of Markets

**Structure, Entropy  
and  
Traders' Confidence**

- 1. Ace of Spades**
- 2. King of Spades**
- 3. Queen of Spades**
- 4. Jack of Spades**
- 5. Ten of Spades**
- 6. Nine of Spades**

- 1. King of Spades**
- 2. Three of Diamonds**
- 3. Jack of Diamonds**
- 4. Ten of Hearts**
- 5. Two of Clubs**
- 6. Seven of Hearts**

**Positive Feedback structures the market by increasing the relative strength difference between winners and losers.**

**The emergence of structure  
is the trend.**

**Negative Feedback collapses  
structures built up during  
periods of positive feedback.**



**The collapse of RS structure  
“re-shuffles” the market.**

# En·tro·py

**The tendency for all matter and energy in the universe to evolve toward a state of inert uniformity; deterioration of [the structure of] a system or society.**

**Webster's**

**Two distinct market  
environments**

**driven by two opposed  
trading paradigms.**

**“In some seasons  
trend following is good.”**

“Trading strategies that buy past winners and sell past losers realized significant abnormal returns over the 1965 to 1989 period.”

Jegadeesh and Titiman, “Returns to Buying Winners and Selling Losers: Implications for Stock Market Efficiency”, 1993

“The historically strongest stocks produced the best future results and the historically weakest stocks produced the worst.”

Robert Levy, *The Relative Strength Concept of Common Stock Price Forecasting*, 1968.

(Study based on data from October 1960 to October 1965)

**“In others, reversing is good.”**

Harold M. Gartley, who had pioneered relative strength to study stock groups, abandoned its use in the 1930s and 1940s because it did not work.



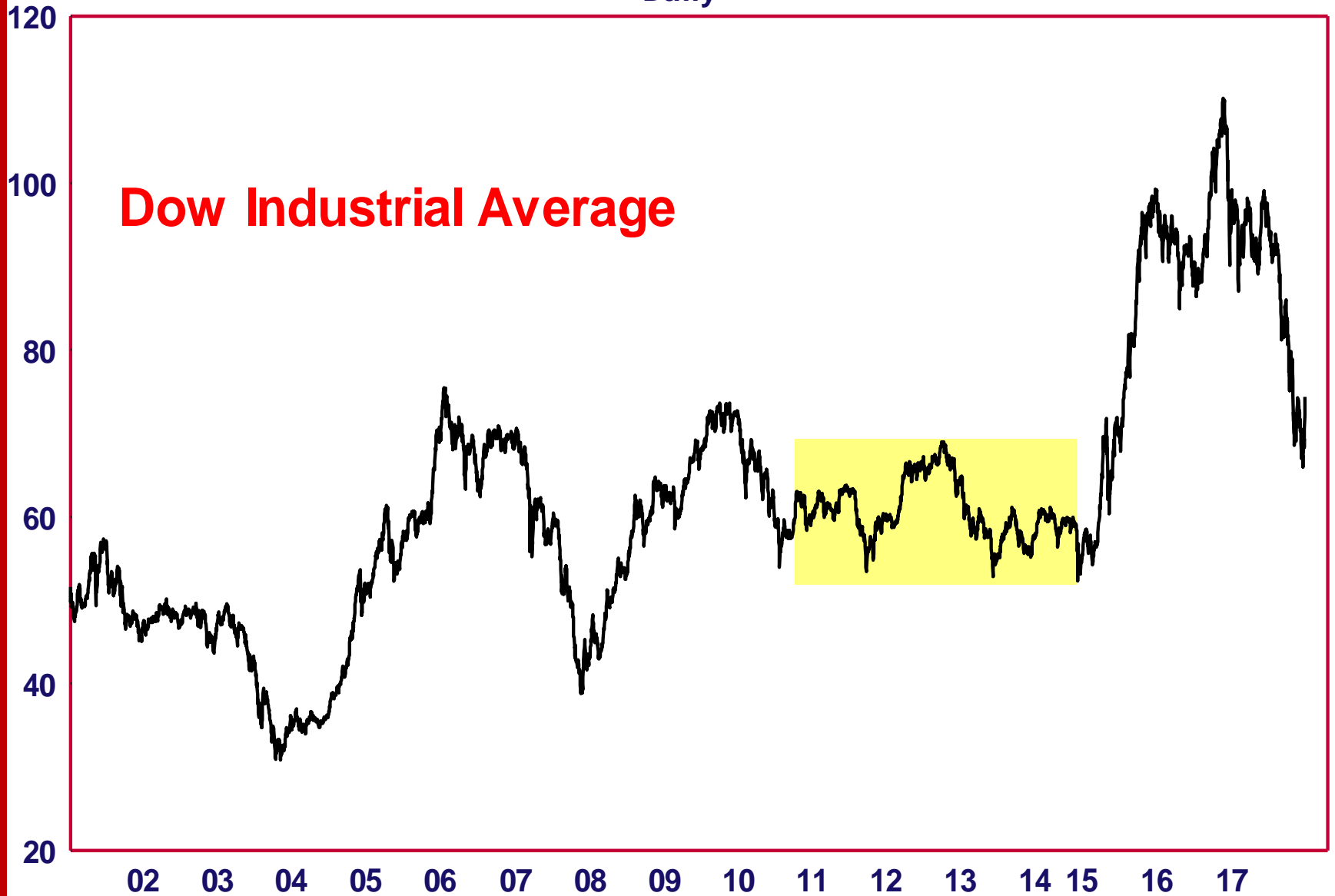
“In a narrow market, when prices are not getting anywhere to speak of but move within a narrow range, there is no sense in trying to anticipate what the next big movement is going to be, up or down. . . .”

Jesse Livermore, Reminiscences of a Stock Operator (*Lefevre*)

“Those were the lean years, 1911-1914. The market flattened out. Things drifted from bad to worse. *I not only lost all I had but got into debt again. There was no money to be made.*”

Jesse Livermore, Reminiscences of a Stock Operator  
(Lefevre)

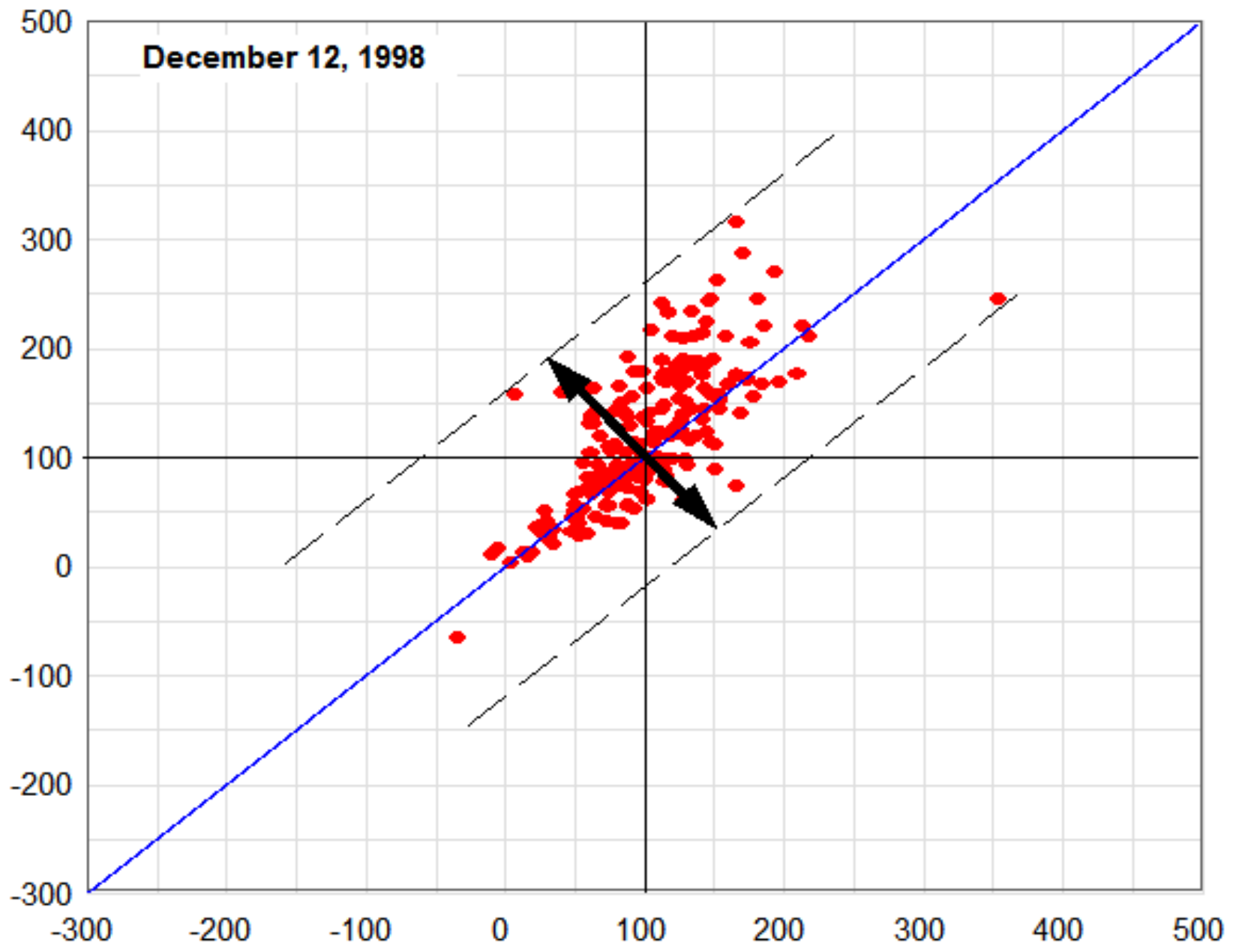
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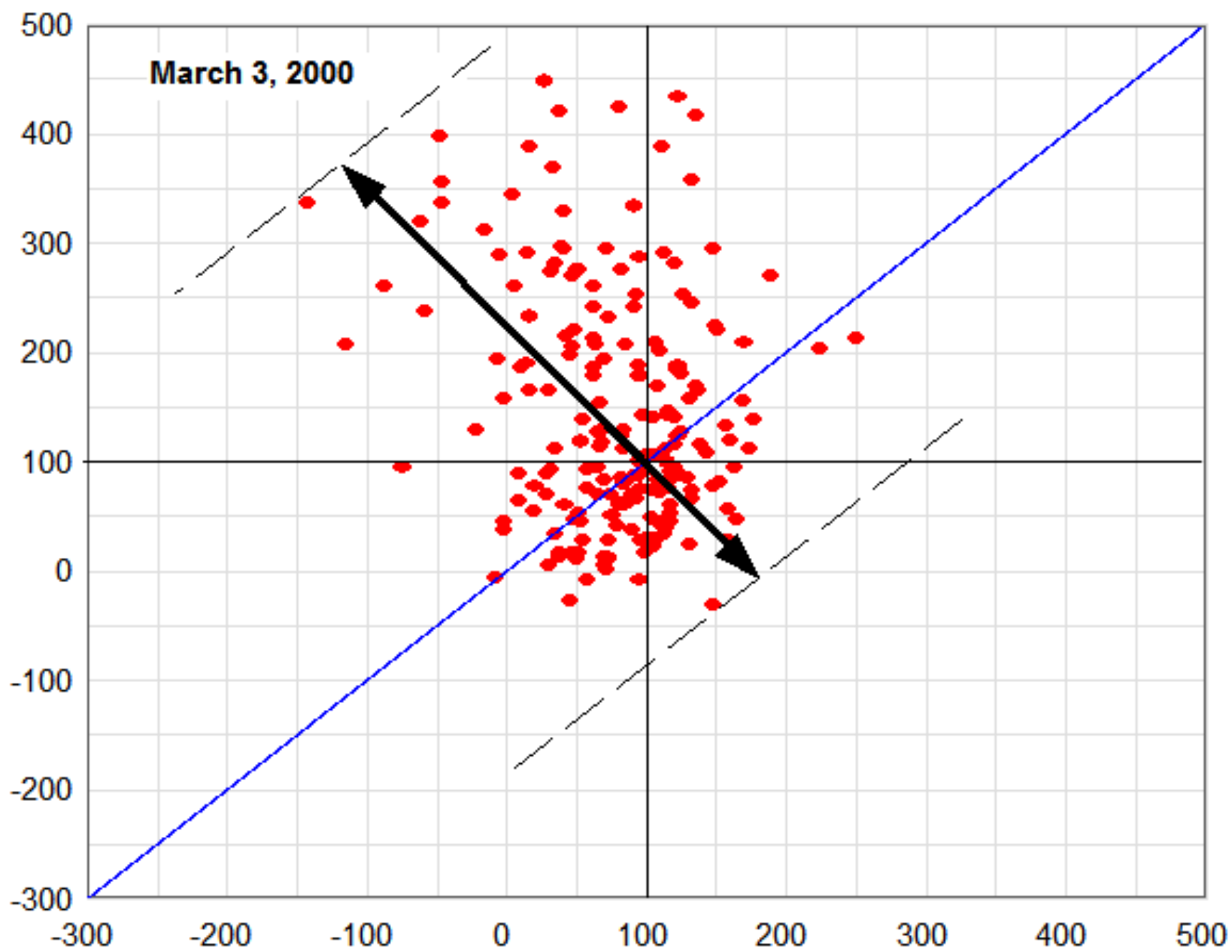


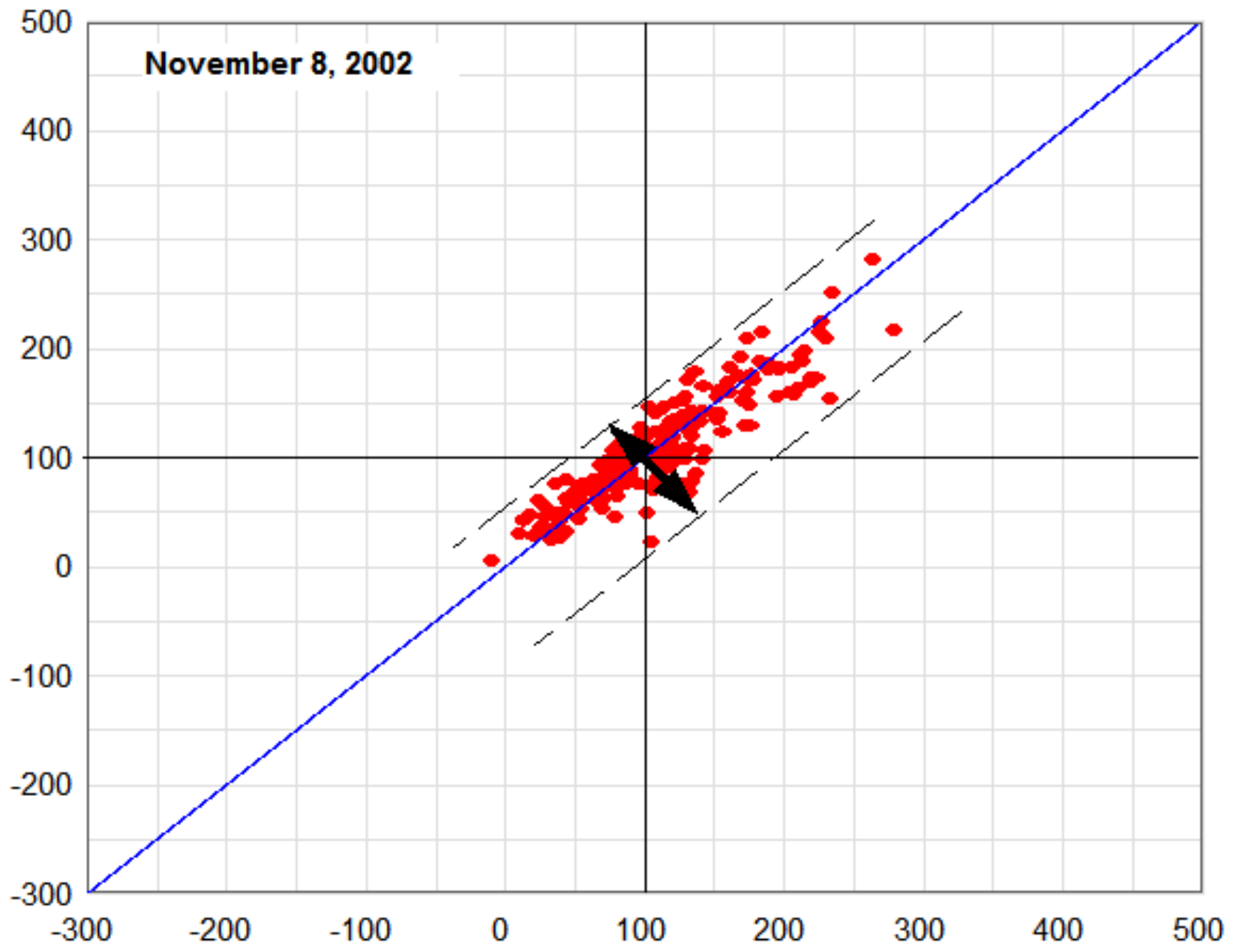
# Key Indicators

# **The Relative Strength Spread**

**Is feedback positive or negative?**

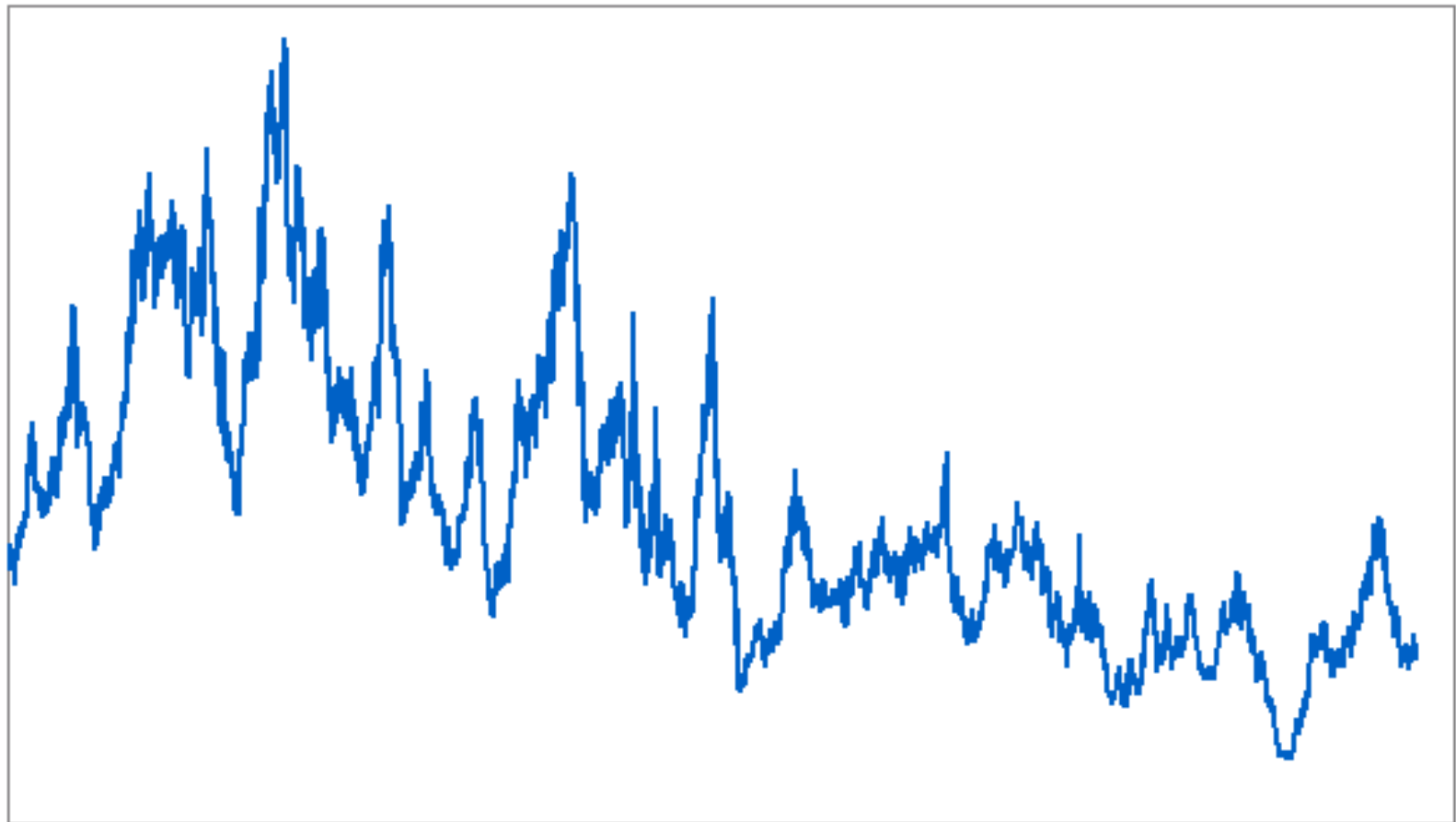








# The Spread



91 92 93 94 95 96 97 98 99 00 01 02 03 04 05 06 07 08 09 10 11 12 13 14

# **Rising Spread**

- result of positive feedback  
(momentum)**

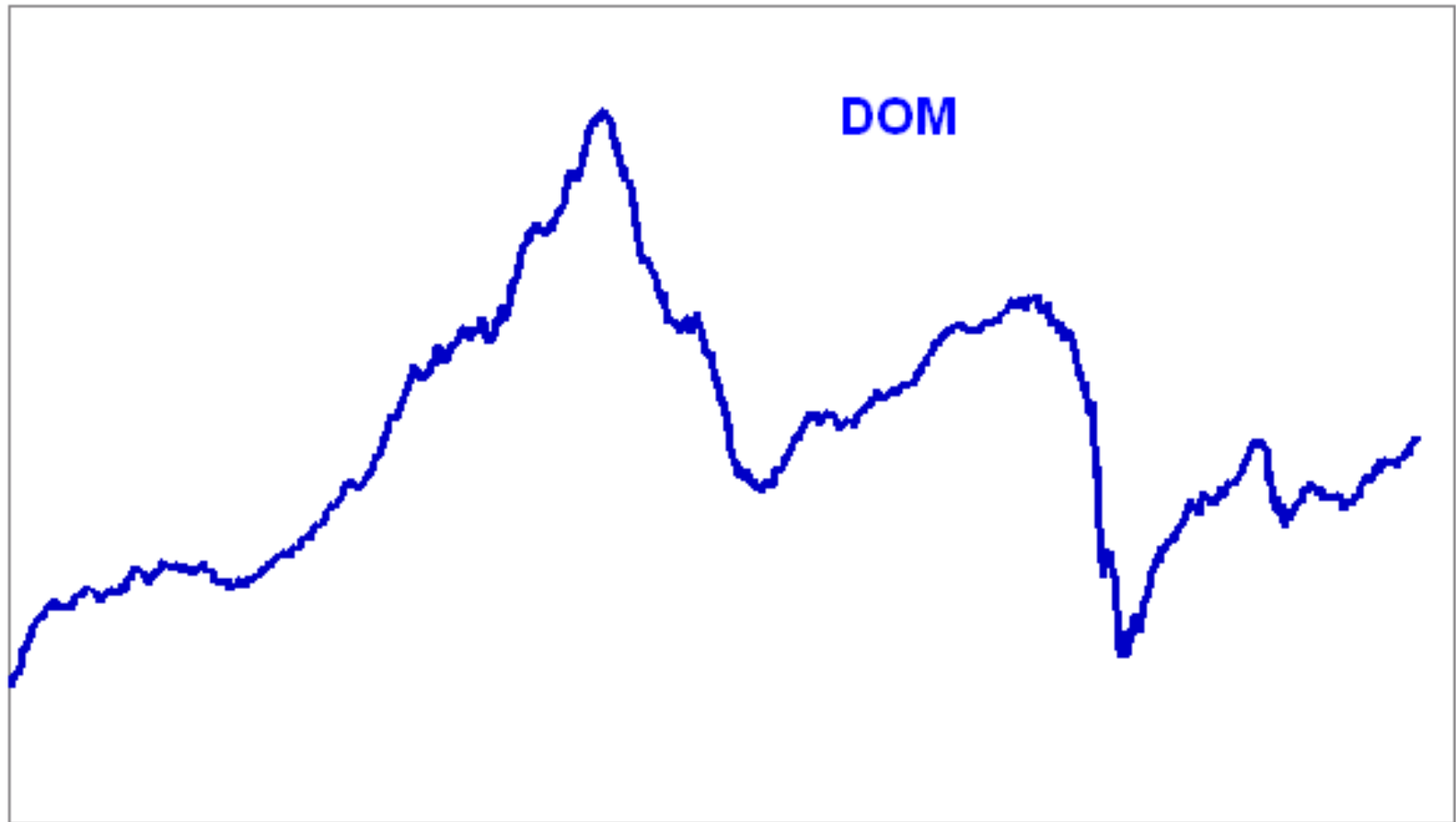
# Falling Spread

- result of negative feedback  
(entropy)

# **Direction of Momentum**

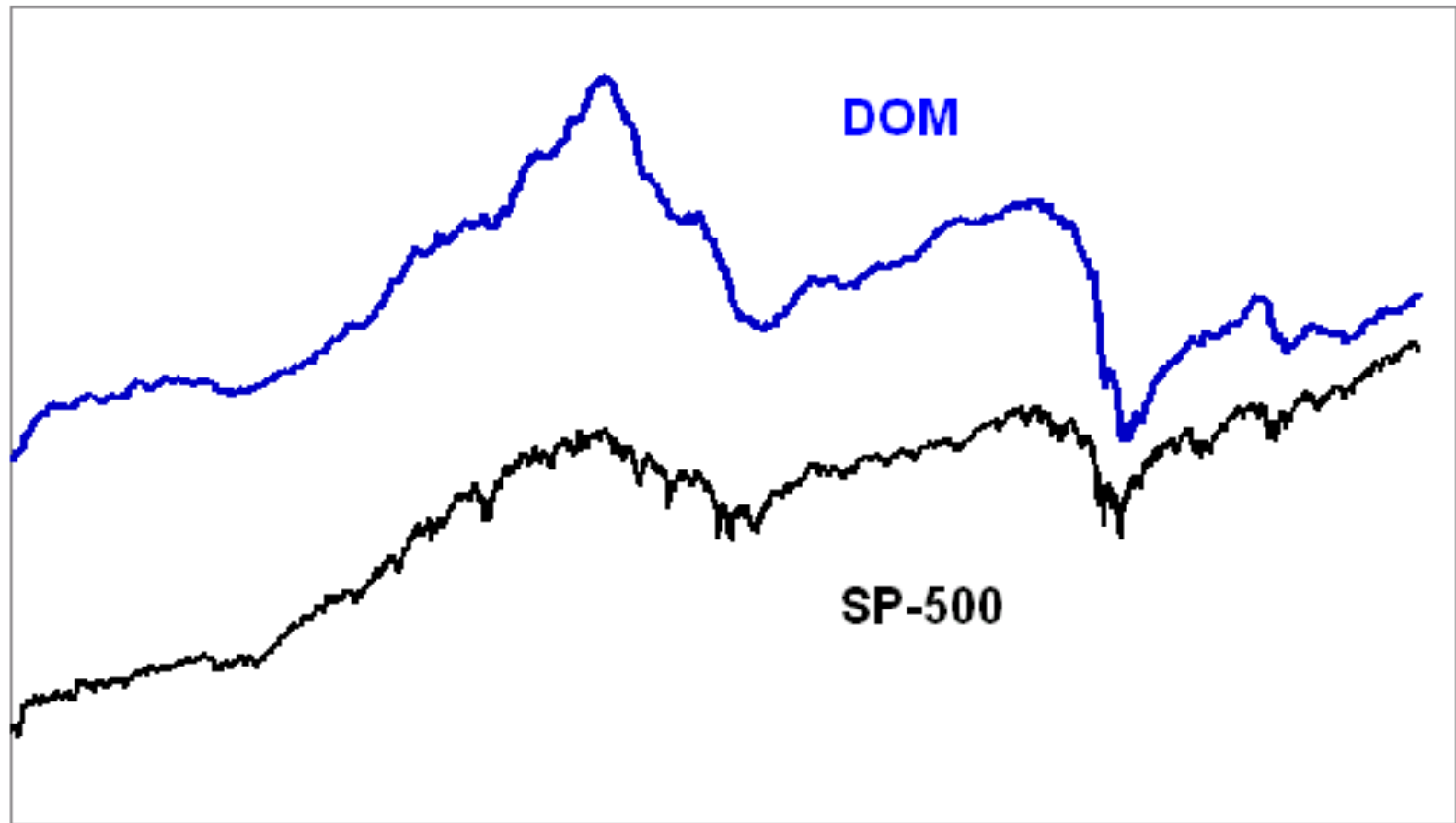
**In what direction is momentum  
(positive feedback) moving the  
market?**

# Direction of Momentum



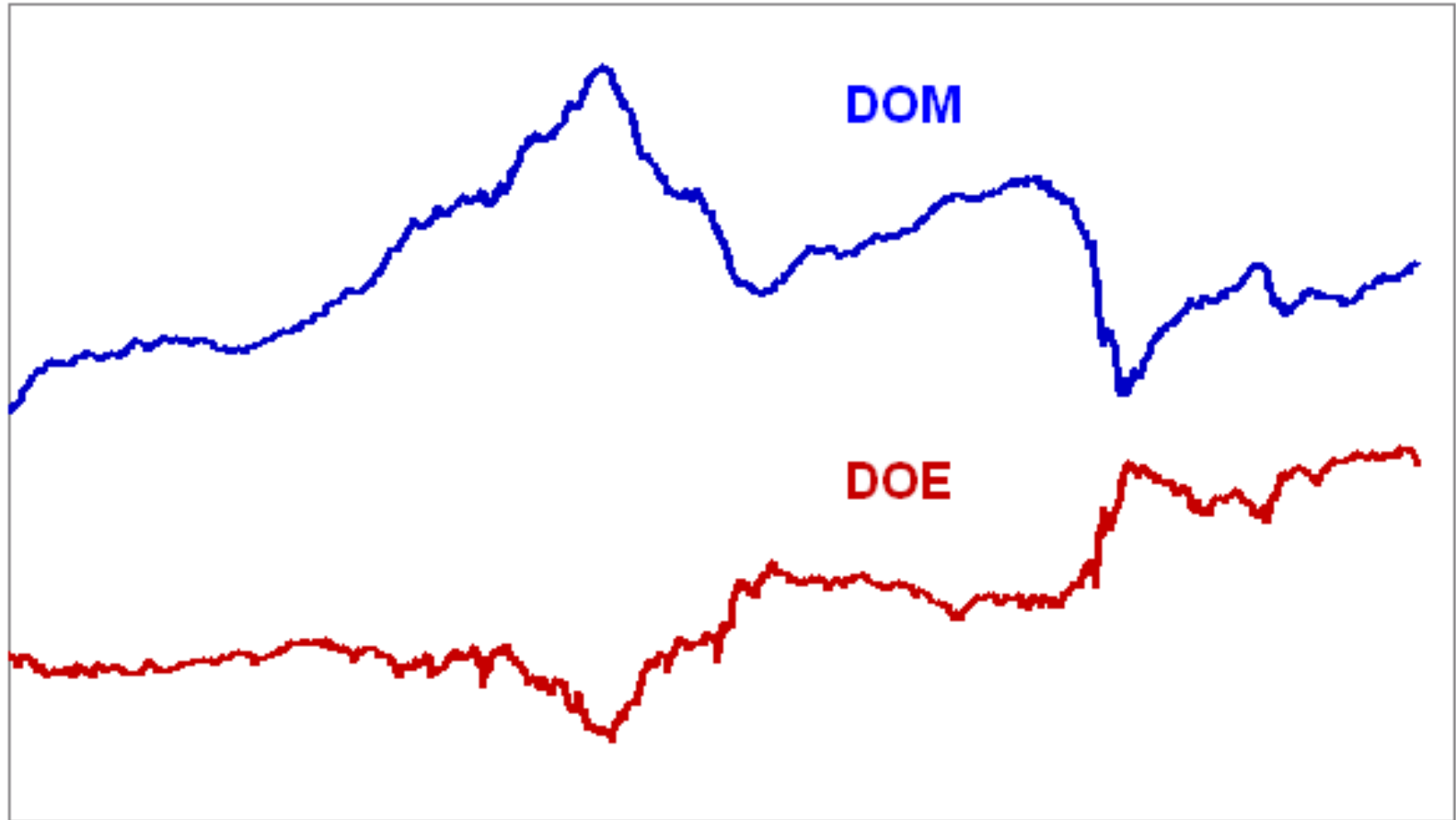
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# Direction of Momentum



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# Direction of Entropy



91 92 93 94 95 96 97 98 99 00 01 02 03 04 05 06 07 08 09 10 11 12 13 14

The background of the slide is a golden, embossed texture. In the center, there is a faint, embossed image of the Roman god Janus, which has two faces looking in opposite directions. The overall color palette is warm, consisting of various shades of gold, yellow, and brown.

# **The Janus Strategy**

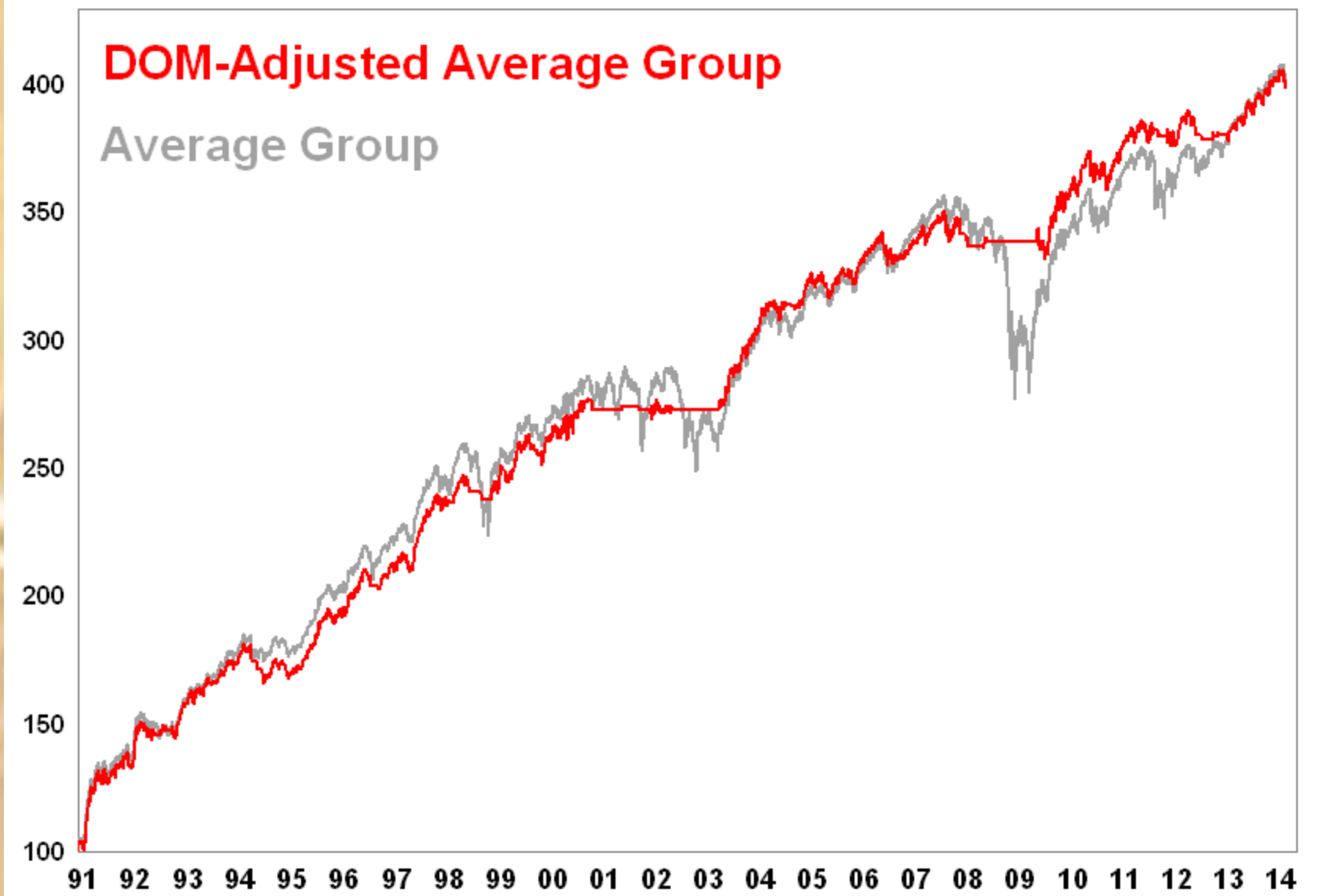


# **Morningstar Sub-Industry Groups**

- **Stocks in each group  
equally balanced**
- **No survival bias**

# Average Group





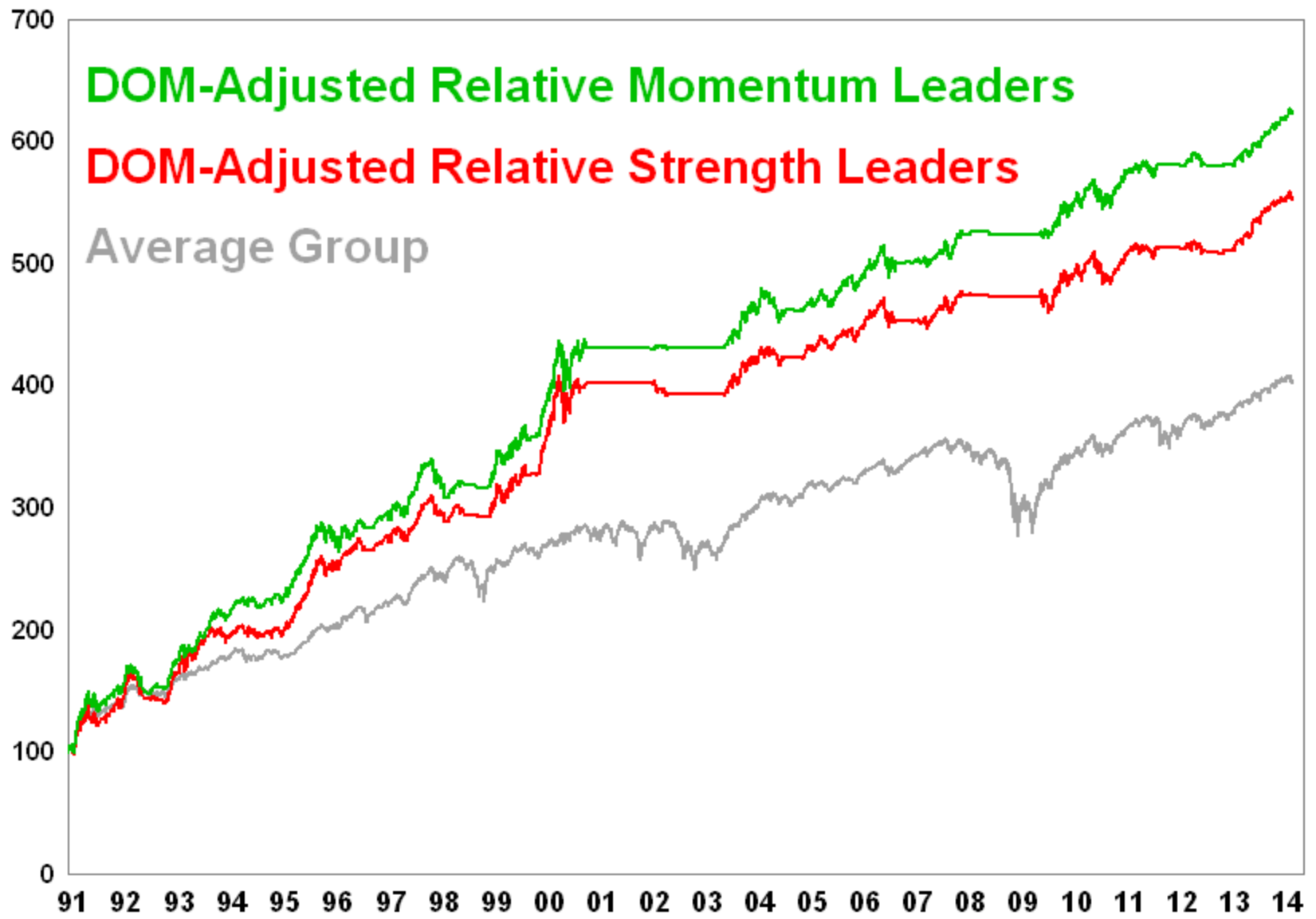
# Relative Strength Leaders

Average Group









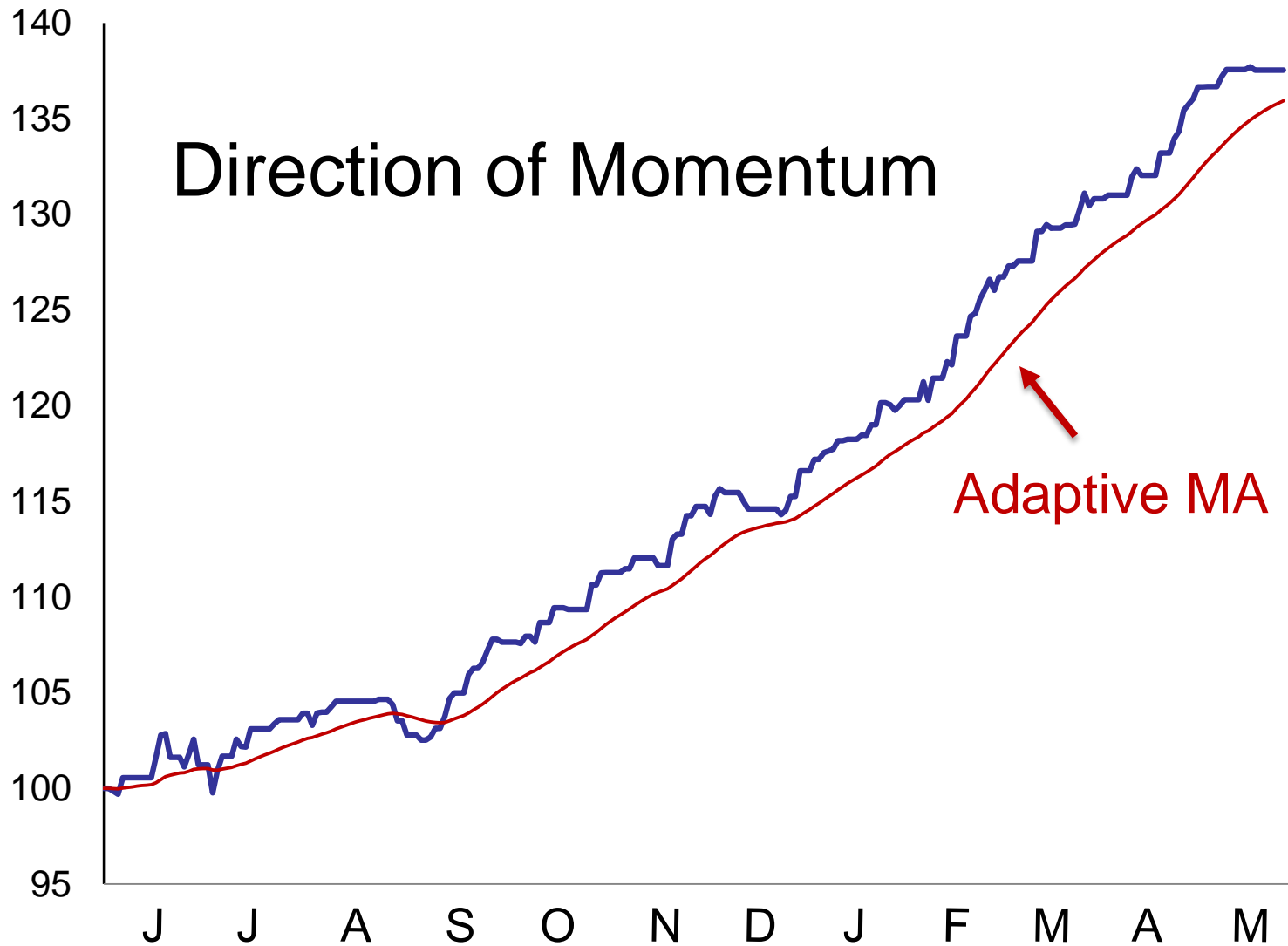
**December 1990 – January 2014**

**Long – 71%**

**Cash – 29%**



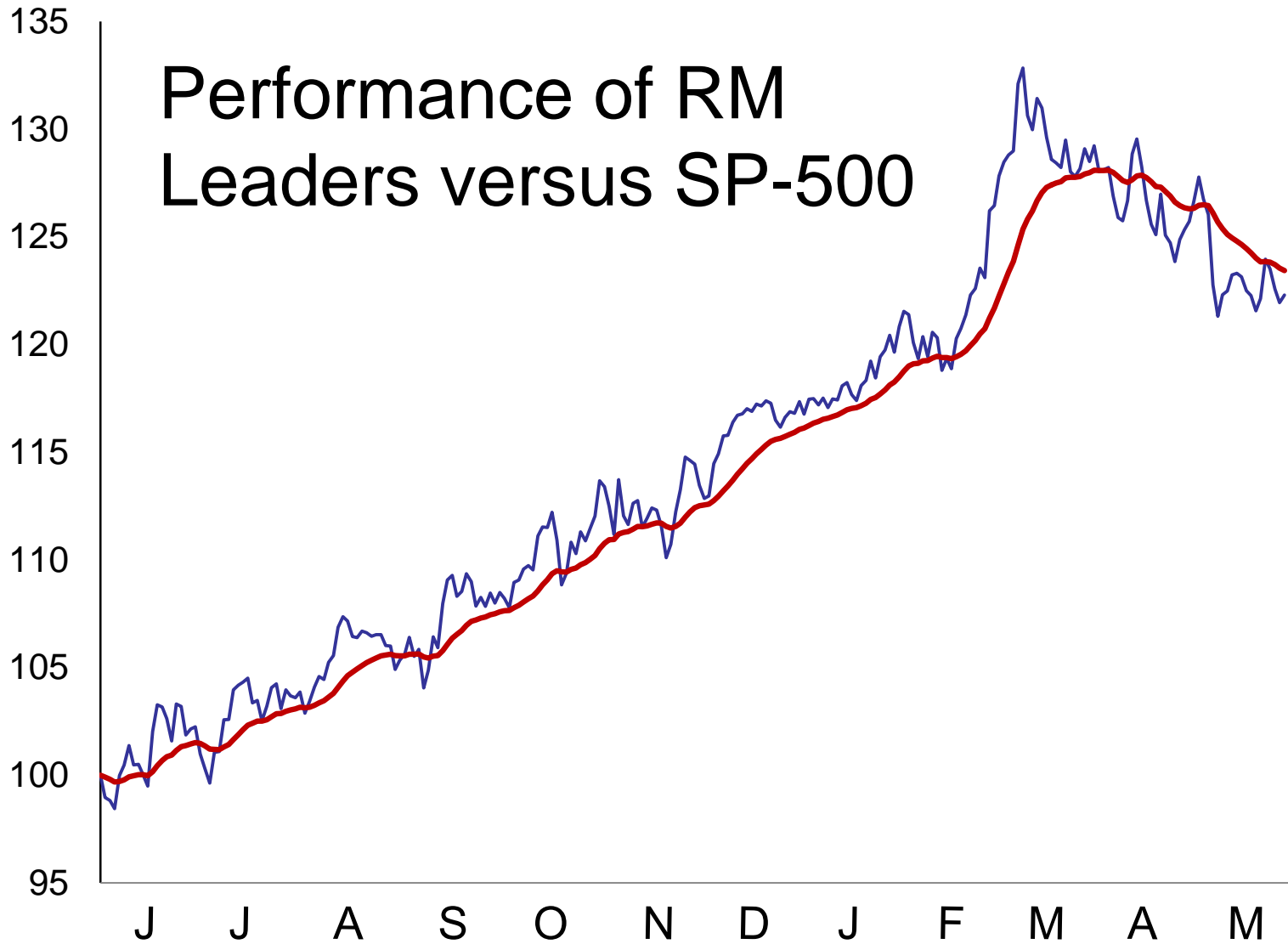
# Direction of Momentum

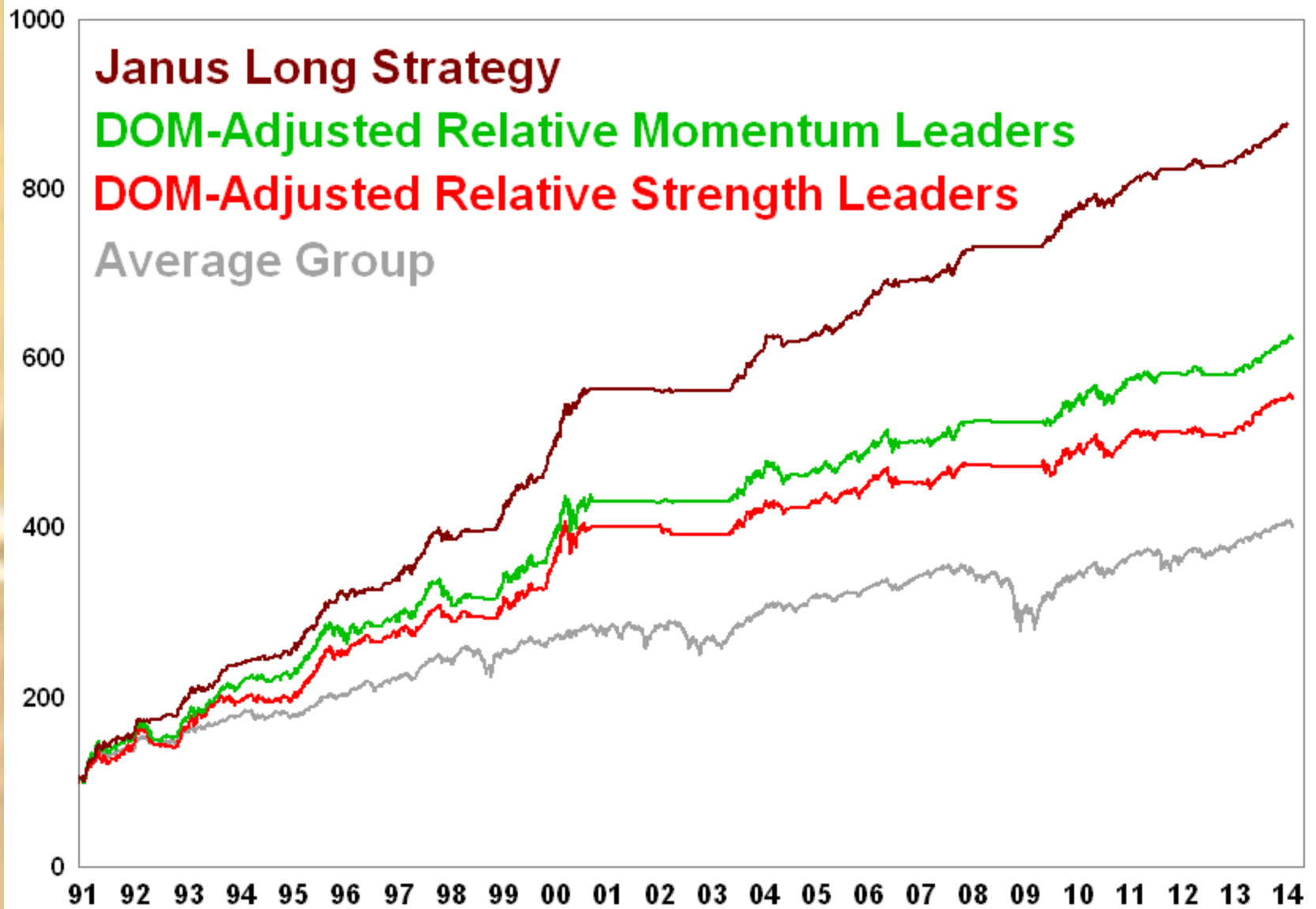


Adaptive MA



# Performance of RM Leaders versus SP-500





**“It is not the strongest of  
the species that survives,  
nor the most intelligent,  
but the one most  
responsive to change.”**

**Charles Darwin, The Origin of Species**

# equityPM

Advisory For The Equity Portfolio Manager

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