Backtesting

PRO PRACTICE WORKSHEET

Work through these by hand or with a spreadsheet. There's no wrong answer, the goal is just practice.

Section 1 - Audit for Lookahead Bias

Pick a hypothetical trading rule (e.g. 'buy when quarterly earnings beat estimates'). What data would need to be timestamped carefully to avoid lookahead bias?

Section 2 - Calculate Cost Drag

A strategy trades 100 times a year at an estimated 0.08% cost per trade. Calculate the annual cost drag and the net return if gross return is 14%.

Section 3 - Design an Out-of-Sample Split

If you had 10 years of historical data, how would you split it into a 'training' period for tuning and a 'test' period for judging the result?

Section 4 - Spot Survivorship Bias

Think of a backtest using 'today's S&P 500 constituents' over the past 20 years. What companies would be missing, and how might that skew the result?

Section 5 - Reflection

Think of a strategy you've heard claimed 'great backtested returns.' What questions from this lesson would you ask before trusting that number?