

**Sentiment Analysis of News Articles for Stock Price Prediction**

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# Abstract

Over the past few decades, many theories that describe the behaviour of the stock market have been proposed. These theories put forward ideas ranging from those claiming that the stock market cannot be predicted and to those claiming those that with the right assumptions, the stock market can be predicted. Regardless of this, many stock market prediction models (based on technical indicators or non-technical indicators) have been put forward. In this dissertation we aim to consider those non-technical factors that affect stock prices. These non-technical factors come in form of news articles. In the digital age of rapid response to ongoing situations, news articles about events tend to be released as soon as they occur and the assumption is that if we can track news sources, monitor them for the release of relevant news articles, we can use the sentiment orientation of the article (whether positive, negative or neutral) to predict the price of the stock market before the market has a chance to react to the article. This of course poses an important question on how the sentiment orientation of articles. There are several approaches that can be taken towards determining the class of articles but for the purposes of this dissertation, we will focus on the use of Support Vector Machines to perform classification of news articles. The output of classification will then be fed into a hybrid Support Vector Machines – Hidden Markov Model classifier to perform the price prediction.

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To my parents, sisters and friends, I would like to say a massive thanks for all these years of supporting me through my education. A lot of time has passed since I started school 18 years ago and this dissertation is a representation of all the knowledge I have gained in that time. I truly appreciate all the support you’ve all expressed for me and this project.

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# Introduction

One can arguably say that state of the world economy has been built with the stock market serving as a base. Hence, while there are other means of evaluating a country’s economy, the state of the stock market is perhaps one of the more important means of doing so. Predicting the general direction of stock prices therefore is very important in order to make decisions regarding where and what kind of investment takes place. This work attempts to predict the direction of movement of the (close) stock price of the next working day given information up to and including the current day. We propose a prediction system which incorporates news articles other technical indicators such as the stochastic, stochastic (see section 3.6.) .

The advent of the Internet brought with it improvements in many fields ranging from technologies that influence our daily lives to those that may one day take humans to other planets. One of the more mundane improvements is access to news articles – completely changing the way we now make decisions. We no longer have to wait until the following day to find out about events that took place today. Stock market traders are one group of people who rely heavily on this improvement on access to news. Often times, trades are executed using information from the news either consciously and unconsciously. Unconscious decisions can be made because news articles need not necessarily carry extremely significant news in order to be usable to traders – news articles will often bear information about annual earnings, acquisitions and mergers, changes in administration and management as well as stock splits – and thus, news need not bear extremely catastrophic nor positive information, in order to be useful.

Traders will often base their trades on information from news articles regardless of how seemingly important it is. We therefore argue that the key to predicting the stock market is by monitoring extensive sources of news articles and extracting valuable information from the articles which can then be used to predict the stock market. The process of extracting information relating to a person’s opinion or emotions automatically from textual data is referred to as sentiment analysis. This work therefore is an interdisciplinary work that ties together sentiment analysis, machine learning and finance for the prediction of the stock market.

The next section details the motivation for this project. We then carry on describing our objectives, the assumptions we make and structure of this work.

## Motivation

A lot of stock price work has been done using technical and fundamental indicators such as the current investment, general economy, recessional periods, currency and industry – this is known as fundamental analysis. However, very few articles have attempted to go beyond that and while some of these methods perform reasonably well, very few articles in the literature have attempted to go beyond historical data. Even still, within the set of articles that attempt to use recent (external) information such as news articles, very few articles attempt to incorporate historical technical data. In this work, we aim to further fill in this gap by utilising both historical data (section 3.6.) that provide us with an indication of how well the stock price has done in the past as well as current news that provides us with a sense of what the general sentiment regarding a certain stock is. This is primarily because it stands to reason that we will make much higher profits with making optimal use of both (largely independent) sources of information. A few related works have attempted to use both methods to predict the stock market such as Deng et al. (2011) who use technical analysis and sentiment analysis modelled as a regression problem in a Multiple Kernel Learning framework; however, the backbone of the current proposed model uses a Support Vector Machine and Hidden Markov Model (SVM-HMM) hybrid model for the predictions – which to our knowledge hasn’t been used previously.

## Objectives

The primary goals is to propose a system by which the stock price can be predicted as well as perform experiments that test the performance of the system. We also explore the effectiveness of the hybrid system in predicting stock prices.

Furthermore, we aim to extensively and conclusively review related, previous work on the prediction of the stock market using both technical indicators and sentiment-based indicators. Although our discussion of sentiment analysis is heavily favoured towards machine learning based techniques, we aim to give a well-rounded discussion by also taking non-machine learning based techniques into consideration.

## Assumptions

There are several schools of thought regarding whether the stock market can at all be predicted and in order to continue, we must first discuss the current hypotheses and highlight which hypotheses we have based the project on. The current hypotheses being considered comes in the form of the three levels of the Efficient Market Hypothesis.

The weak-form efficient market hypothesis assumes that the market is efficient. In addition, it also assumes that the rates of return are independent, meaning that past return has no bearing on future return. A different way of putting this is that *new* information is different or distinct from *old* information; hence, new movements in the stock price cannot be predicted from old movements – this is referred to as the random walk. Following from this, traders, both algorithmic and human, make invalid assumptions when trading.

The semi-strong form efficient market hypothesis assumes that the market at all times reflects all publicly available information. The stock market hence responds very quickly to new information. Conclusively, this implies that potential investors cannot profit above the stock market as investors can only trade based on new information, after the market has adjusted to it.

The strong form efficient market hypothesis assumes that the market, at all moments reflects both publicly and privately available information. This incorporates both the weak and semi-strong form of the efficient market hypothesis and following this hypothesis, no one can make money above the market.

Hence, it’s quite clear that one of the first decisions to be made is whether or not the efficient market hypothesis is one of our assumptions and if it is, which level. It’s quite clear that to assume any form of the Efficient Market Hypothesis would invalidate this work; hence, we do not assume the efficient market hypothesis. The Efficient Market Hypothesis assumes that all investors are rational and that there exists a perfect flow of information which clearly is invalid. Instead, we assume that at the end of each working day, the stock price reflects the available information. It’s safe to make this assumption as should an important piece of news be released that alters the stock price significantly, the price at the end of the day will reflect this. Should a company be, say, downgraded by standard and poor, the stock price will reflect this downgrade until the rating is increased once more. That is to say that the *shockwave* of a downgrade isn’t just absorbed by the market – the stock price trend line of such a company will continuously, visibly be a *symptom* of the downgrade.

We assume a much simpler model of the stock market – predicting the direction of movement of the close price of the stock market rather than the intra-day price. It’s important to note at this point that predicting the stock market needn’t necessarily involve predicting the exact values – predicting simply the direction of movement is enough (Elkan, 1999; Lavrenko, Schmill, Lawrie, Ogilvie, Jensen, & Allan, 2000; Thomas & Sycara, 2000).

We also assume that the effect of information extends into multiple working days. Hence, an Hidden Markov Model can identify patterns based on the trend of the past several working days.

Finally, we make the assumption that important trends that change the rate of return of a stock price in any significant way can be extracted from news articles.

## Organisation of Document

In the succeeding chapter, we provide an in-depth review of the literature both on sentiment analysis and on stock price prediction. In Chapter 3, as we assume that the average reader is unfamiliar with the techniques used for the project, we provide preliminary background knowledge. Chapter 4 details the scientific method used for the project. Chapter 5 details the results of the experiments run. To conclude, chapter 6 details the closing remarks.

# A Brief Review of the Literature

The current chapter is split into three sections. The first section reviews the recent work on sentiment analysis. The second section reviews the work on, specifically, the domain of stock market prediction with sentiment analysis. We note that there are several means by which sentiment analysis can be applied for use in stock price prediction and we aim to at least touch on the more interesting and relevant methods in the literature. Finally, we provide concluding remarks on the review.

## Sentiment Analysis

Bing Liu (2012) highlights three levels of sentiment analysis: document based, sentence based and aspect-entity based. Document-based sentiment analysis pertains to the classification of an entire document and the key assumption is that the entire document focuses on a single entity. Sentence-based analysis is more in-depth analysis of individual sentences. Aspect-entity based analysis focuses on determining the subject of discussion as well as the sentiment. Even further, opinions are split into regular and comparative opinions – regular opinion express opinion on a single entity while comparative opinion expresses opinion on two or more entities.

Bing Liu highlights that the most important indicator of sentiment are sentiment words such as *poor, happy, sad, brilliant* or *excellent.* Of course, one glaring issue with simply analysing based on sentimental words is the use of sarcasm in language. This, in addition with the fact that sentimental words can change orientation (e.g. ‘not happy’ vs ‘very happy’) depending on the context means that sentiment analysis can’t be reduced simply to a keyword search. It should be noted at this point that financial news articles use sentimental words, making classification harder than with other domains such as movies. Liu discusses extensively sentiment analysis using varying techniques but since we are simply interested in only document-based classification, we focus on articles related to such classification. It is recommended that any reader who wishes to gain a more complete and up-to-date overview of the current sentiment analysis methods should refer to Bing Liu’s work on the subject.

One of the more important aspects of document-based classification is the determination of features. Popular ones include terms and their frequency (which is the selected features for this current projected), parts of speech (POS) – introduced by Turney (2002) – and their tags such as sentiment words and sentiment flippers (words that change the orientation of sentiment words such as *not*). Bing Liu also comments that some domains are easier than others, for example movie reviews tend to be easier to analyse than car reviews – this is due to the multi-entity nature of car reviews. Compare:

**S1***:* The movie is utterly captivating

**S2**: While I like the leather seats, the gear is a bit hard to manipulate

In the literature, there are two main approaches to feature generation: a lexicon-based approach and a bag-of-words approach. The lexicon-based approach as used in Whitelaw et al. (2005) typically involves a set of example words which are then used as a seed for building a larger lexicon through the identification of synonyms in a semi-automatic manner. Bag of words approach typically involves the representation of words as a numerical value indicating their presence, frequency or term frequency-inverse document frequency (TF-IDF) score (Yong, Xu, & Ren, 2011). Please refer to section 3.1.1 for our discussion of TF-IDF. One of the more often cited criticisms of the bag-of-words approach is the loss of semantic association between terms, as the order of words has been lost in the bagging procedure.

Work has been done to improve on the TF-IDF by introducing the delta TF-IDF (Martineau & Finin, 2009 ). Delta TF-IDF improves the importance placed on words that are unevenly distributed in the corpus and discounts those that are evenly distributed – the rationale being that the less unevenly a feature is represented, the higher the chances that it’s relevant for its classification. Delta TF-IDF is formulated mathematically as:

|  |  |  |
| --- | --- | --- |
|  |  | (2.1) |

where is the number of times term appears in document , is the number of positively labelled documents containing term t, is the number of positively labelled documents, is the number of negatively labelled documents with term , is the number of negatively labelled documents and is the value for term in document . Using feature values derived by delta TF-IDF on movie review classification, a SVM achieved an accuracy of 88.1% compared to traditional TF-IDF based classification accuracy of 82.85% on the classification of movie reviews.

Feature selection is critical in sentiment analysis as corpuses tend to be polluted with noise, reducing the performance of any developed system. Core techniques involved in feature selection are stop-word removal and stemming. Furthermore, statistical methods such as the point-wise mutual information (Turney & Littman, 2003; Wilson, Wiebe, & Hoffmann, 2005) and chi-square ( are used in the feature selection process.

The point-wise mutual information measures the correlation between a term and the class . Assuming mutual independence, PMI can be calculated using the joint distribution and the individual distributions. This is formulated mathematically by Aggarwal and Zhai (2012) as:

|  |  |  |
| --- | --- | --- |
|  |  | (2.2) |

where the expected co-occurrence of and is and the actual co-occurrence is . A PMI of greater than 0 means a positive correlation between and and the inverse is the case for a PMI less than 0. We delegate to section 3.1.3 our explanation of .

Sentiment classification techniques are split into two broad ranges of techniques: machine learning techniques (Yong, Xu, & Ren, 2011; Pang, Lee, & Vaithyanathan, 2002; Kang, Yoo, & Han, 2012; Kaufmann, 2012; Moraes, Valiati, & Neto, 2013), lexicon-based approaches – which is further split into dictionary-based approaches (Guang, Xiaofei, Feng, Yuan, Jiajun, & Chun, 2010; Minging & Bing, 2004; Kim & Hovy, 2004) and corpus-based approaches (Deerwester, Dumais, Landauer, Furnas, & Harshman, 1990). We will focus on the machine learning techniques.

Pang et al. (Pang, Lee, & Vaithyanathan, 2002) used a corpus of reviews that were classified according to the number of stars associated with the text reviews and predicted these ratings using naïve bayes, maximum entropy and Support Vector Machines. They compared the performance of unigrams, unigrams + bigrams, bigrams, unigrams + POS, adjectives, top unigrams and unigrams + positions using three-fold cross-validation. The performance of each variation in features depended heavily on the type of machine learning technique used. SVMs on average performed better than both naïve bayes and maximum entropy. It’s important to note that the classifiers performed best when the terms were represented simply as a presence as opposed to frequency. Unigrams performed best in their experiments using the Support Vector Machine-based model with an accuracy of 82.9%.

Yong et al. (2011) propose a method of sentiment analysis similar to the approach this work has taken, pre-processing the words by removing stop words and tokenisation. Words are then sorted based on calculated mutual information and a number of words are selected as the feature items and classified using an SVM. They neglect to specify the domain and source of the corpus, making comparison with this work difficult. However, they achieve very high classification rates with total precision of 81.11%, recall of 81.42% and F-value of 81.25 in a closed test.

## Stock Price Prediction Using Sentiment Analysis

Often, it is the case that a useable corpus of financial news isn’t available hence authors are forced to generate their own data (Zhan, Cohen, & Atreya, 2011) either by manually classifying or automatically generating data (Fung, Yu, & Lu, 2005; Zhan, Cohen, & Atreya, 2011). Zhan et al. (Zhan, Cohen, & Atreya, 2011) in their comparison of manual and automatically generated data highlight that the key to classifying news articles manually is the general information that is being conveyed by the articles. Mergers, lower interest rates are general considered *good news* while corruption, lawsuits, wars are considered *bad news.* They perform classification by working with automatically generated data based on simply the stock price movement (the log of today’s close divided by log of yesterday’s close). The classifier developed has F1-scores of 0.26, 0.38 and 0.36 for positive, neutral and negative articles respectively. They attributed the poor performance to the lack of data and poor article selection whilst also suggesting that news articles are better suited to long-term prediction as opposed to day-to-day prediction. It’s quite clear that while there are issues with automatic generation of data (section 5.3.2.), the method employed by Zhan et al. can be said to be too naïve.

Regardless of the criticisms of automatically labelling news article based on the direction of movement of the next day’s price movement, Kaya et al (2010) had a 60% accuracy using a similar method (price differences between the daily close price) as well as -based feature selection. Fung et al. (2005) utilise piecewise linear segmentation to automatically classify news articles – a method that has been employed in the current work and will be explained in the next chapter.

Gidofalvi (2001), derive a unique method of automatically assigning labels to news articles by aligning news articles to the intraday stock data and although it doesn’t perform very well, we spend some time on it due to its contribution to the literature. A window of influence is defined which is used to evaluate the possible effect of a news article. The author defines the window of influence of an article with the timestamp as the lower boundary offset and the upper boundary offset from t. An offset if negative is is prior to. In addition, news articles that aren’t published within the opening and closing market times are filtered out as these are said to be ambiguous.

To establish how stable/volatile a stock is, a β-value is calculated using the linear regression on data-points (Δ index-price, Δ stock-price). Hence, a β-value of 1 means that whenever the index price changes by δ, the stock price is expected to change by δ as well. A β-value of 2 means that whenever the index price changes by δ, the stock price is expected to change by 2δ as well. A β-value of greater than 1 are relatively volatile and the inverse is the case for stocks less than 1.

In order to remove the effects of the exponential change in price, the formula is:

|  |  |  |
| --- | --- | --- |
|  |  | (2.3) |

The movement of a stock within a time interval is:

|  |  |  |
| --- | --- | --- |
|  |  | (2.4) |

where is the change in the stock price and is the change in index price during the time interval A news article with timestamp can then be measured with offsets to receive a score of .

Movement classes can then be defined from these equations:

|  |  |  |
| --- | --- | --- |
|  |  | (2.5) |

Where and are threshold values. Naïve Bayesian can then be used to predict the probability of a document belonging to a class.

The predictive power of the classification system discussed is low with the system performing worse than random. On analysis, low values show that the movement measure model is poor-fitting to the stock price.

On evaluating the labelling of the news articles, Gidovalvi and Elkan discover that the highest statistically significant settings are and . The authors also find that the most statistically significant settings for alignments are [-20, 0] and [0, 20], that is 20 minutes before and 20 minutes after the release of the news article.

The predictive capability of the classifier was very low and the apparent reasoning for this is that the do not accurately model the relative movement of the stock correctly. Regardless of the accuracy, they concluded by acknowledging that their results contradict the efficient market hypothesis.

Perhaps more unconventionally, is the use of tweets from twitter to predict the stock market (Bollen, Mao, & Zeng, 2011). They determine the correlation between the mood of the twitter feeds and the Dow Jones Industrial Average. The moods are determined using OpinionFinder (classifies into positive and negative) and Google-Profile of Mood States (GPOMS). A Granger Causality Analysis and Self-organising Fuzzy Neural Network are then used to determine the validity of the hypotheses that moods predict the stock market. The orientation provided by OpinionFinder is discovered to be less predictive than the GPOMS dimension *Calm*. They also claim that there exists a (3-4 days) time lag between the mood expressed on twitter and the changes in the DJIA values – hence stock price movements can be predicted in advance.

Bar-Haim et al. (2011) propose a method of identifying expert investors from twitter feeds, which can then act as a basis for predicting the increase in stock prices. They compare two extreme methods: focusing on tweets that explicitly state transaction details as well as learning the correlation between the stock price and the tweet’s contents. The second approach removes restrictions on the applicable tweets but with the caveat that a lot of noise is likely to be introduced into the training process. They show that making the process user-sensitive improves the prediction accuracy. The algorithm involves a classifier which classifies a time-annotated set of tweets by each user and classifies each as bullish, bearish or neutral. Each tweet can then be evaluated for correctness by determining that the stock market behaves in accordance with the classification of the tweet. Tweets finally are ranked according to correctness. Another method utilised is unsupervised learning based on the timestamp of the tweet. They compare performance using several methods: joint-all model (a single SVM model trained on all tweets), transaction model (finds expert users based on the correlation of their tweets to the movement of the stock price), per-user model (removes noise by unsupervised learning for each potential expert), joint-experts model (using the per-user model, train a single SVM model). They conclude that the most accurate models are the per-user and the joint-experts perform the best.

Zhang and Skiena (2010) compare blogs and news as a basis for prediction, perform a large-scale analysis of the stock market and propose a trading strategy based on sentiment data. Data from Dailies (an aggregator of news), twitter, Spinn3r RSS feeds and LiveJournal was processed by Lydia (a text processing system), resulting in time series consisting of a time series of words and their orientation. They discovered that the media exposure correlates more to the stock market of certain industries (Aerospace and Defence) and less so for others (Software and Computer Services).

AZFinText (Schumaker & Chen, 2005) works with the assumption that 20 minutes after a news article is released, the stock price reflects the effect of the news. As opposed to labelling with a polarity (up or down), it labels using the stock price 20 minutes after the news article is published. The system uses proper nouns as the features and filters the selected features by only further selecting proper nouns that occur three or more times. It uses Support Vector Regression to try to predict the price of the stock in 20 minutes. For a period of 23 trading day, using 2809 articles and predicting for the S&P 500 Index, they achieved a 8.50% return on investment while the S&P 500 Index achieved only a 5.62%.

NewsCATS (Mittermayer & Knolmayer, 2006) categorises news articles into “good”, “bad” and “no movers”. Using a thesaurus as a curator, they classify press releases as good if the maximum gain in 15 minutes after its release is large () and the maximum loss is (). The inverse is the case for “bad” news. Neutral news articles are classified as those whose gain and loss do not exceed 3%. NewsCATS achieved an average of 0.29% over 2602 trades while a simulated random trader achieved a profit of 0.07% over 2599 trades. Mittermayer and Knolmayer conclude by cautioning that the results do not factor transaction cost and hence do not accurately reflect the potential profit.

## Concluding Remarks

Sentiment analysis has been identified to have a broad range of applications from determining the public sentiment of films to the current application of stock price prediction. It’s quite clear that the problem of sentiment analysis faces different challenges depending on the domain or the dataset source. Our review of the literature has been heavily biased towards techniques that are specifically relevant to this project and readers are encouraged to read the survey by Medha et al. (2014) for more complete overview of the domain. In addition, another reasonable conclusion from the literature review is that sentiment analysis is not only a reasonable, quick method of text mining but also can be applied as a step in more complex processes such as stock price prediction.

Having seen the variety of techniques used in the literature, we point out that the main differences between our approach and previous work are that we use a hybrid SVM-HMM model to both improve our chances of predicting correctly and to emphasis the recent data as well as the use of historical technical data and recent sentiment data. We believe that this novel approach makes an important contribution to the literature and makes headway in leaving room for further exploration of effective stock price prediction.

This concludes our review of the literature on sentiment analysis for stock price prediction.

# **Background Knowledge**

In the previous chapter, we introduced in passing several key concepts, especially in the context of sentiment analysis. In this chapter, we aim to arm the reader with the key knowledge required to gain an understanding of the rest of this document. In addition, some concepts that were mentioned in the previous chapter are fully explained here. Hence, this chapter (especially section 3.1.) is also a good precursor to chapter 2.

## Sentiment Analysis

Sentiment analysis, according to Wikipedia[[1]](#footnote-2), is defined as “*the use of natural language processing, text analysis and computational linguistics to identify and extract subjective information in source materials*.” We have seen in chapter 2 that the possibilities in terms of approaches to the general problem of sentiment analysis are extremely varied; hence, once more we focus on the steps required to a machine learning-based solution. We split our discussion into clear steps that one would expect when performing a machine learning task.

### Feature Generation

Regardless of whether the chosen approach to acquiring labels is manual or automatic, feature generation from the corpus[[2]](#footnote-3) has to occur. Tokenising is the preferred approach to feature generation. Tokenisation refers to the splitting of a document into single words, phrases, nouns or other parts of speech which are called tokens. Tokens often disregard any form of punctuation. These tokens usually come in form of unigrams, bigrams, trigrams and (more generally) n-grams.

Unigrams are n-grams that are of size one. For illustrative purposes, we show the feature generation from a document consisting of only one sentence.

**D1**: The fat cat sat on the fat dog.

**:** The, fat, cat, sat, on, the, dog

Higher-order n-grams were introduced to solve the issue of complete disintegration of any semantic relationship between the terms; however, unigrams perform quite well, despite this criticism (Pang, Lee, & Vaithyanathan, 2002).

Bigrams are n-grams that are of size two. Bigrams introduce a relationship between the individual words:

**D2**: Standard and Poor changes Goldman recommendation from A to BBB

**:** Standard and, and Poor, Poor changes, changes Goldman, Goldman recommendation, recommendation from, from A, A to, to BBB.

In the case of the D2, we can see why bigrams can be beneficial: a classifier might be able to identify the negative orientation of the document due to the bigrams *from A* and *to BBB*. Conversely a classifier might be able to detect the positivity should the bigrams be *from BBB* and *to A*. As far as unigram-based classifiers are concerned, there isn’t any difference. While one might think that the higher the order of the n-gram, the better a classifier would be, this isn’t the case. Higher-order n-grams bear more similarity to the source document than an overall pattern; in short, higher-order n-grams become less useful in determining sentiment orientation.

N-grams are not the only means of generating features. Features can also consist of noun phrases or pronouns. These are usually accompanied by other parts of speech like adjectives. In order to extract nouns, documents have to be processed by a part of speech tagger such as the one provided by Stanford[[3]](#footnote-4). Even more specific parts of speech such as Proper Nouns or Name Entities[[4]](#footnote-5) can act as features (Liu, 2012).

A key part of feature extraction are is stop-word removal and stemming. Stop-words are words in the document that occur very frequently across the corpus and often bear no weight in the orientation. Examples of such words in the English language are *a*, *the*, *rather*, *but*, *also*. Textfixer provides a full list of such words[[5]](#footnote-6). Removal of these words is key to reduction of noise across the corpus. In some cases, stop words are key to the determining the orientation of sentences (often relevant at sentence-level classification). For illustrative purposes, the following sentence shows the case in which stop words are useful:

**D3:** If only Mr Tim was a decent actor.

The removal of the stop-words *if* and *only* completely alter the sentiment orientation of the sentence.

Stemming refers to the linguistic normalisation of words from their inflected form to a common form. Words needn’t be mapped to its exact morphological stem, a relation is usually all that’s needed. The example below shows the effect of stemming.

Cooperation, Cooperating, Cooperative, Cooperates ↦ Cooperate

Popular stemming algorithms are the Porter Stemmer and the Snowball Stemming Algorithms. Like stop-word removal, stemming reduces the noise in the features and results in better performance.

### Feature Representation

In order to make the documents useful to numeric classifiers such as artificial neural networks or Support Vector Machines, the terms need to be transformed into their weighted forms. The weighting of the terms is shown to be at least as important as their selection (Strzalkowski, 1994).

The vector space model introduced by Salton et al. (1975) is the preferred algebraic method of representing textual documents. The document is represented as a single vector where each dimension in the vector is a single feature. Features that do not exist in a particular document are simply given a value of 0. The weights are usually calculated using either simply their presence (binary), counts (integer), frequency(float) or their term frequency inverse document frequency (TF-IDF) score (float). Hence we can say that in a corpus of documents and features, a document is represented as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.1) |

where . We described an improvement on TF-IDF in chapter 2 and now, we provide the mathematics behind the traditional TF-IDF (Salton, Wong, & Yang, 1975). Given, the document, the weight is calculated as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.2) |

where is the number of documents that contain the term . 1 is added to prevent divide-by-zero errors. is the term frequency and is given by the formula:

|  |  |  |
| --- | --- | --- |
|  |  | (3.3) |

where is the number of times feature occurs in document and is the total number of terms in the document . The higher the value assigned to a feature, the importance, it is given.

### Feature Reduction

Due to the incredibly large number of features generated by tokenisation, it’s necessary for feature reduction to take place; the preferred methods for this are and singular value decomposition (Golug & Kahan, 1965), although we only discuss based feature reduction.

is used to test the level of independence or correlation between the features and the classes. A value of 0 indicates a lack of dependence while a large value implies a large dependence. Features with a value greater than a set threshold are selected. is formulated mathematically by Aggarwal and Zhai (2012)as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.4) |

where is the number of documents in the corpus, is the conditional probability of documents being assigned to label , given that they contain token , is the number of documents assigned label c. and is the number of documents which contain .

## T-Test Based Split-and-Merge Piecewise Linear Approximation

In their paper ‘The Predicting Power of Textual Information on Financial Markets’, Fung et al, (2005) present a means of generating labelled data by detecting trends in a time series and aligning news with the trends; we present their algorithm here.

### The Splitting Phase

The split-phase of the algorithm handles discovering the trends in a time series while the merge phase helps avoid over-segmentation. Each time series can be represented as a list of tuples – each tuple containing the price and time:

|  |  |  |
| --- | --- | --- |
|  |  | (3.5) |

where is the price at for and the time series has a length .

The process starts by representing the trend with a line defined by the first and last points (a segment). In order to decide if the line is enough to represent , a one-tail t-test is defined:

|  |  |  |
| --- | --- | --- |
|  |  | (3.6) |

where is defined as the expected mean square error:

|  |  |  |
| --- | --- | --- |
|  |  | (3.7) |

where is the number of points in the segment. is the projected price (derived from the line ) at time. The t-statistic is defined by:

|  |  |  |
| --- | --- | --- |
|  |  | (3.8) |

Where is the variance. The t-statistic is compared with the t-distribution using a degrees of freedom and . Hence, there is a 0.05 probability of the null hypothesis being accepted given that is incorrect. If is accepted, then the mean-squared error is low and the projected trend line is very similar to the actual time series . If is accepted then, the line is not enough to represent . If is accepted, then the line is split where the error norm is maximum – – resulting in two segments. The process iterates by repeating the process on the two segments. The algorithm is represented in algorithm 3.1, as produced by Fung et al.

### The Merging Phase

Over-segmentation is the existence of two adjacent segments whose slopes bear enough similarity to not warrant two separate segments. To fix this issue, the merging phase merges these segments into one large one. The merging phase aims at combining adjacent segment whose merging would not result in being rejected.

Consider a time series (where ), the result of splitting time series . is a segment in . Should potential merge of the segments and not result in being rejected then they are regarded as candidates for merging. Let the list contain all such pairs of candidates. The selected candidates are the pairs that would result in the smallest increase in . This process is repeated until the -test is rejected. Hence . The merge algorithm is provided in figure 3.2.

|  |
| --- |
| split(]) – split a time series of of length  from time to time where |
| 1:  2:  3:  4: **for**  to **do**  5:  6: **if**  **then**  7:  8:  9: **end if**  10:  11: **end for**  12:  13: **if** -test.reject **then**  14:  15:  16: **end if**  17: **return** |

Algorithm 3.1 – The Split Algorithm

|  |
| --- |
| merge() – merge two adjacent segments on time series T |
| 1: **while** *true* **do**  2:  3: **repeat**  4:  5:  6: **if**  **then**  7:  8:  9: **end if**  10: **until** end of time series  11:  **if -**test.accept() **then**  12: drop  13: **else**  14: break  15: **end if**  16: **end while**  17: **return** |

Algorithm 3.2 – The Merge Algorithm

## Support Vector Machines

Techniques in machine learning generally are classified into two main divisions: supervised and non-supervised learning. Support Vector Machines (SVMs) are classified under the former. This means that the process by which SVMs solve tasks is by first undergoing a training phase in which input data (referred to as a set of examples or instances) are used to learn a model that can then be used to classify new instances into a category or a set of categories. SVMs typically solve binary classification[[6]](#footnote-7) problems.

SVMs work by projecting and mapping (by using a kernel function) training data instances into a high-dimensional feature space, such that the gap between the two categories is maximised. Hence, new instances can be classified by side of the gap the point falls on. *Gap* is a vague term and is difficult to define. Instead, SVMs work by constructing a hyperplane that separates the two categories – this is referred to as the maximum margin hyperplane. The maximum margin hyperplane is sought after theoretically, as such an hyperplane should lead to the lowest generalisation error.

A hyperplane which defines the decision boundary of the classes is in turn defined in terms of a set of points whose set of points satisfy the equation.

where is the weight vector of the hyperplane, is the kernel method that maps the data points to a (hopefully)linearly feature space and is the bias.

For linearly separable data, two hyperplanes can be defined which completely separate the data such that there are no points between them. The area in space that is bordered by the two hyperplanes is called a margin. The two hyperplanes are defined by the following equations:

In order to define and , vectors must be selected which just touch the margins – these vectors are referred to as support vectors as these are the only data instances required to represent the model. The margin can also be defined more formally in terms of and which are the shortest distance between the maximum margin hyperplane and the closest positive support vector and the shortest distance between the and the closest negative support vector, respectively.

In figure 3.1., is defined as the offset between the maximum margin hyperplane and the origin. We can thus say that is the width between and . Given that the distance between and is , the total distance is then . We therefore need to minimise in order to maximise the margin, . This problem can thus be formulated mathematically as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.9) |

Figure 3.1. – Maximum margin hyperplane and margins of a binary classification SVM-based model

where is an example, is the target class. Minimising can be reduced to minimising

Having formulated the linearly separable case, we note that not all SVM-applicable problems are linearly-separable; in fact, most of them are not, even in kernel or feature space. For this, we introduce a slack variable which acts as a penalty term for misclassified examples. is thus formulated mathematically as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.10) |

Hence, can be rewritten as . This new formulation is referred to as a soft margin and the modified optimisation goal is:

|  |  |  |
| --- | --- | --- |
|  |  | (3.11) |

Often, we find that there is more than a single category to classify. There are two main approaches to multiclass classification problems: one-versus-one and one-versus-rest. One-versus-one attempts to differentiate between each two pairs of class while one-versus-many differentiates between a single class and the other classes.

We conclude our discussion of Support Vector Machines with the kernel function, . The resulting feature space is heavily dependent on the exact function mapping and there are a few popular kernel functions, which are simply listed here.

1. Linear kernel is defined as (i.e. no mapping)
2. Polynomial kernel is defined as where c is a constant which accounts for the influence of higher-order terms versus the lower-order terms is the degree
3. Radial basis function kernel where is a hyper-parameter referred to as the kernel bandwidth.
4. Gaussian kernel:

## Hidden Markov Models (HMM)

Hidden Markov Models (written as **,** pictured as figure 3.2.) are simply a set of parameters which explain a pattern for a known class or category. HMMs can be used to classify a test-pattern for which it has the highest posterior probability. Sequences can be considered as a series of states , written as . There are no restrictions on the number of states to be visited or the number of times a state can be visited. In order to define any sequence, transition probabilities –the probability of at ­ given at - must be evaluated. We have included a state transition diagram for an imagined model with only 4 states in figure 3.3 and formulate the transition probabilities mathematically as:

|  |  |  |
| --- | --- | --- |
|  |  | (3.12) |

Figure 3.2 – Hidden Markov Model

Figure 3.3 – A State Transition Model

At each step in the sequence, the state emits a symbol . Symbols are otherwise referred to as observations as they are visible. Hence, we might have a sequence of observations **.** Given the states and observation, we can then make another deduction: the probability of observing a certain symbol given the hidden state at time :

|  |  |  |
| --- | --- | --- |
|  |  | (3.13) |

is thus referred to as the emission probabilities. At each time step, a transition must occur and a symbol must be emitted, resulting in the redundant formulations:

|  |  |  |
| --- | --- | --- |
|  | for all  for all | (3.14) |

There are three main problems that must be addressed with the Hidden Markov Model: The Evaluation problem, the decoding problem and the learning problem.

### Evaluation

Given an HMM, the transition and emission probabilities, evaluate the probability of a sequence being generated by the model:

|  |  |  |
| --- | --- | --- |
|  |  | (3.15) |

The problem can be solved by sum of all possible sequences of the conditional probability of the transitions multiplied by the emission probability the sequence. However, this is a computational intensive procedure. Instead the forward algorithm (Algorithm 3.3) is used to solve the problem. For the forward algorithm, we define , which defines the probability that an HMM is in state at step having already generated the first elements of the sequence .

|  |  |  |
| --- | --- | --- |
|  |  | (3.16) |

The time-inverse algorithm, referred to as the backward algorithm (Algorithm 3.4) can also be used to solve the evaluation problem, and it’s necessary to define :

|  |  |  |
| --- | --- | --- |
|  |  | (3.17) |

|  |
| --- |
| forward() – calculate recursively |
| 1: **initialise** , visible sequence,  2: **for**  3:  4: **until**  5: **return**  for the final state  6: **end** |

Algorithm 3.3 – The Forward Algorithm

|  |
| --- |
| backward() – calculate recursively |
| 1: **initialise**, visible sequence  2: **for**  3:  4: **until**  5: **return**  for the known initial state  6: **end** |

Algorithm 3.4 – The Backward Algorithm

### Decoding

Suppose we have a sequence of observations and a model **,** the task of decoding is to determine the most likely sequence of hidden states that generated the observations as illustrated in figure 3.4. The Viterbi algorithm is used to solve this problem (Algorithm 3.5.)

Figure 3.4 – Viterbi Algorithm

|  |
| --- |
| decoding() – determine the most likely |
| 1: begin **initialise**  2: **for**  3:  4: **for**  *j*  5:  6: **until**  7:  8: Append to Path  9: **until**  10: **return** Path  11: **end** |

Algorithm 3.5 – Viterbi Algorithm

### Learning

Given the number of states and the number of visible states and a set of training observations, determine the emission and transition probabilities. Starting with estimates of and , we can improve our estimates by first calculating the probability of transition from to given by :

|  |  |  |
| --- | --- | --- |
|  |  | (3.18) |

where defines the probability that the model generated . The improved estimates and can then be used in the forward-backward algorithm (also known as the Baum-welch algorithm):

|  |  |  |
| --- | --- | --- |
|  |  | (3.19) |

and:

|  |  |  |
| --- | --- | --- |
|  |  | (3.20) |

|  |
| --- |
| Forward-backward() – determine and |
| 1: begin **initialise** , , training sequence , convergence criterion ,  2: **do**  3: compute from and by equation 3.19  4: compute from and by equation 3.20  5:  6:  7: **until**  8: **return**  9: **end** |

Algorithm 3.6 – The Forward-Backward Algorithm

## Hybrid HMM-SVM Model

The variation in hidden markov models comes in the form of which the emission probabilities are calculated; hence, HMMs can be based on the Poisson distributions, Gaussian distributions or Gaussian mixture models and in this case SVMs. For continuous data, Gaussian mixture models are typically the preferred method for deriving the emission probabilities; however, they are often criticised for their poor discriminatory capabilities. Conversely, SVMs are popular for their great discriminatory capabilities (Valstar & Pantic, 2012).

SVMs do not directly output probabilities, instead they output the measured distance between the example data and the hyperplane: . In order to create a link between the posterior probability of a instance having a class : and the result of the SVM, we need to utilise Platt’s (1999) proposal for generating pseudo-probabilities by the use of a sigmoid function:

|  |  |  |
| --- | --- | --- |
|  |  | (3.21) |

where and are derived by using maximum likelihood estimation fron a training set. And is the unthresholded output of the SVM defined by:

|  |  |  |
| --- | --- | --- |
|  |  | (3.22) |

In the binary case, we can thus compute the posterior conditional probabilities and of classes and given the symbol . Finally using Bayes’ rule, we can compute the emission probabilities from the outputs of the SVM using the prior probability calculated from the frequency of the class in the training data:

|  |  |  |
| --- | --- | --- |
|  |  | (3.23) |

## Technical Indicators: A Description.

Our selection of technical features is based on the work of Kim and Han (2000) who in turn, base their selection on the review of financial experts. The list of technical features and the formulas for how they are derived is provided in figure 3.2.

The Stochastic Oscillator developed by George Lane (1998), compares the closing price with the price range over the previous period. ’s sensitivity can be altered by changing the length of the period or by introducing a momentum. The stochastic oscillator is therefore used to identify bullish[[7]](#footnote-8) or bearish[[8]](#footnote-9) deviations in a time series – which can then be used to predict reversals in trend line directions. The moving average of the stochastic (referred to as the stochastic ) is used for less sensitive comparisons to the market. For even less sensitivity, the Stochastic Slow is used.

The momentum is used to determine by how much the closing price has changed over a period. Williams is an indicator of the price momentum which serves to compare the close price with the highest high price over a certain period. Correcting for inversion, the Williams multiply the value by -100, which results in values within the range of 0 to -100. reflects whether a stock has been oversold ( values of less than -80) or overbought ( values of higher than -20).

Another technical indicator that can be used to define overbought or oversold stock is the Rate of Change (ROC). The ROC is defined by calculating the difference in the current close price and the close price days ago and is typically used by analysing for positive and negative divergence in the ROC values.

The Accumulation/Distribution (A/D) oscillator measures whether investors are buying or selling a stock and is also a measure of momentum. The A/D Oscillator works by associating changes in price which is in other words, identifying trends.

The 5 and 10-day disparity measures give a value to the difference between the current closing price and the moving average over the past 5 or 10 days, respectively.

The price oscillator measures the difference between two moving averages. A positive value for this technical indicator reflects an upward price trend and the reverse is the case for a negative value. In addition, the price oscillator often acts as a normaliser so that the price oscillator values of one stock can be compared with that of another stock.

The variation between the close price and the statistical mean of a stock is referred to as the commodity channel index (CCI). The CCI was introduced by Donald Lambert (1980) to identify new trends and serves as a warning for extreme conditions in the commodities market but is also applied to the stock market. A high CCI indicates that prices are unusually high above their average while a low CCI price reflects that stock prices are extremely low below their average. As with some other indicators, the CCI can be utilised in identifying overbought or oversold stocks.

The relative stock index (RSI) developed by Welles Wilder measures the speed at which price changes and hence is another momentum indicator. RSI values fall within the range of 0 to 100 and also indicate the overbought (RSI above 70) or oversold (below 30) status of a stock.

In this work, we will use all the technical features listed in Figure 3.5, in addition to the sentiment analysis features extracted from news articles.

|  |  |
| --- | --- |
| Technical Indicator | Formula |
| Stochastic |  |
| Stochastic |  |
| Slow Stochastic |  |
| Momentum |  |
| Rate of Change |  |
| William’s %R |  |
| A/D Oscillator |  |
| Disparity5 |  |
| Disparity10 |  |
| Price Oscillator |  |
| Commodity Channel Index |  |
| Relative Strength Index |  |
|  |  |

|  |
| --- |
| where is the close price, is the highest high and is the lowest low for the last days, is the high price at time , is the low price at time t, is the 5 day moving average, is the 10 day moving average, , , , the upward price change at time and is the downward price change at time . |

Figure 3.5 – Technical Indicators and their formulas

# Scientific Method

## Method Overview

The proposed system is comprised of two main parts: sentiment-based news classification and price prediction. Any developed system cannot completely rely on news as news is sporadic and there’s no guarantee that news regarding a certain entity will be released for every single trading day and thus, there needs to be a means by which prediction can still take place. This comes in the form of technical data (section 3.6.). In addition, combining news information and technical features improves performance. Hence, there are two phases of classification – the classification of pure news articles and the classification of technical data. Figure 4.1 shows the system overview, ignoring news labelling.

## Sentiment Classification

As emphasised in previous sections, the first task to be performed is the classification of news articles. As with classification of other types of data, the following steps need to be performed: data acquisition, data labelling, data pre-processing, data analysis and then finally classification. The range of human sentiment is very wide and includes sentiment such as happiness, sadness, calmness, anger and anxiousness. This range is much too wide for the application at hand. In fact, we have taken a much simpler approach and simply classified the sentiment of the news articles into three categories: happy, sad and ambivalent.

Unlike sentiment classification for domains such as films, cars or music, happiness, sadness and ambivalent news articles may not bear much information about the progress of the entity. While the sentiment of the article is what we aim to extract, a cursory look at any news article that bears financial information will show that news articles aren’t very sentimental. This indicates that classification based simply on human sentiment while perhaps being accurate, might not be as useful given that we aim to predict the stock market. Therefore, to supplement classification based on sentiment, we also classify based on the progression of the company. This means that the articles are classified into an additional set of categories (positive, negative and neutral).The aim with the progress classification is that articles get classified based on what the news article’s evaluator expects will happen as regards to whether the entity’s stock price will go up, down or simply stay the same as a result of the article.

This new direction of evaluation however raises the question of how to gauge the effect of a news article. For illustrative purposes, if the price of a specific stock has been on the rise for the past three days and then a news article is released and it’s classified as “positive”, how do we factor that in? Does it simply not matter as we have a direction of progress or could we instead watch for the rate of the change of the stock price? We aim to answer some of these questions in the following sections and over the next chapter.

### Data Acquisition

#### News Articles Acquisition

It’s clear that the very first task to be performed is the acquisition of news articles either labelled or non-labelled. Although a fair bit of work have been done using this particular approach to stock price prediction, we were unable to find any publicly available datasets that met all the constraints of this dissertation. Hence, a dataset of about 2250 news articles was generated from online news sources.

**Data Acquisition**

**Price Prediction**

News Articles Storage

Stock Price Data

External News Sources

External Stock Price Data

**Feature Generation and Selection**

Chi-square feature selection

Generate vector space model with TF-IDF as weights

SVM-based classifier

**Pre-processing**

Normalisation

Feature generation from stock price data and SVM-classification of news

HMM-SVM-based classifier

Down Price Direction

Up Price Direction

News Classification into positive, Neutral or Negative

Figure 4.1 - Process Overview

**Sentiment Classification**

**Pre-processing**

Stemming

Tokenisation (into unigrams, bigrams)

Stop-word removal

Although selecting news sources may appear to be a trivial task, it requires careful consideration as news sources have to be able to satisfy the following requirements:

1. It has to be popularly read, especially by traders. This is particularly important because a high level of trust needs to be placed in the news source, enough to determine that significant changes in stock price trend will be reflected in the news articles.
2. The news sources should have decent (frequent) coverage of news– to ensure that we gather as much data as possible.

Given these requirements, investors on online forums (as well as individuals with knowledge of finance) were asked which news sources were read and the following sources were given: Reuters, Bloomberg, Financial Times, Market Watch, Yahoo Finance. Our survey was responded to by about 20 active traders.

The next step is to scrape selected websites (Bloomberg, Reuters) for news articles. We do not discuss the exact process of scraping websites as these technical details are not of interest to this project. However, scraping can involve interesting problems such as logging in to websites via a program (in this case, python) and extracting data.

Prior to the scraping of news articles, we must first determine what it is we hope to find – in this case, we want to scrape enough news articles in order to perform classification on the news articles. Hence the gathering of news articles has to be targeted so that we have enough data for each of the companies we aim to classify

Finally, the news data is extracted and put in the following xml format:

<?xml version='1.0' encoding='us-ascii'?>

<news>

<entry author=''…'' datetime=''…'' url=''…''>

<headline>

…

</headline>

<body>

…

</body>

</entry>

</news>

Figure 4.2 – XML Format for Scraped News Articles

#### Stock Price Data Acquisition

The acquisition of the numerical stock data simply involves selecting the companies which are of interest and extracting the data from Yahoo Finance. In this case, the API (ystockquote) was used to extract the data for relevant companies. The data collected for each company includes the following: Date, Adjusted Close, Close, High, Low, Open, and Volume.

### Data Labelling

At the start of the project, the intention was to crowd source the labelling of the articles. This would be done by asking individuals with knowledge of economics and finance to evaluate the news articles. This involved uploading the corpus to a website for easier classification. (sentimentanalysis.bolanleonifade.me). However, the rate at which the articles were being classified was very slow so the alternative approach taken was to use prior knowledge (of the current author) to label the article. This of course meant that experiments might suffer due to lack of enough financial knowledge. Therefore, in order to provide a baseline or at the very least, a means of evaluating the manually labelled data, a set of automatically labelled data was created as well.

* + - 1. **Manual Labelling**

Manual labelling of data is simply reading each news article and labelling them by hand. The evaluators are asked to estimate the company’s progression based on the news article. Their estimates can fall into the following categories: (up, down, neutral). The evaluators are also asked to provide the sentiment of the article (happy, sad, neutral). From henceforth, for clarity purposes, we shall refer to the former as “progress sentiment” and the latter as “emotion sentiment”

One might think that there is a perfect correlation between the two sets of categories. However, there can be differences between the two. For illustrative purposes, we will examine a couple of cases in which there are differences:

The headline “Exxon Mobil reports Fire, oil spill at Nigerian terminal”, evokes a feeling of sadness but due to the established nature of Exxon, it’s unlikely that this event is going to lead to a massive dent in the stock price, we give the article a progress sentiment of neutral (because the article doesn’t go on to indicate that Exxon will suffer from this incident). Another article that wouldn’t be expected to change the stock price much is “JP Morgan employee falls to death from building roof in Hong Kong”. It’s however clear that the article is “sad”, but the effect on JP Morgan’s progress would virtually be nil.

If the previous two examples give the impression that from headlines, we can always tell the emotion sentiment of an article, it would be wrong. In fact, a seemingly neutral headline such as ”Coca-cola names Walter Finance Chief as Fayard Retires” goes on to discuss the recent struggles of Coca-cola, therefore giving it an emotion sentiment of sad and a progress sentiment of neutral. In the same strain, we discovered articles can both be up for progress sentiment and emotion sentiment; this would be the case for articles that discuss an entity’s growing business.

* + - 1. **Automatic Labelling**

In order to perform automatic labelling of news articles, we need to generate projected trends, this gives us an idea of the overall outlook of the stock price – that is, for example, we can safely say that the overall projected trend of the stock price is an upwards movement if the price over a period of time has changed positively, ignoring every minor dip in the price trend. We can perform automatic labelling by using piecewise linear approximation. This allows us to align news articles with the projected stock price and simply label the articles based on the projected stock price.

There are obvious inaccuracies that can occur from the use of such a method – in fact, as shown in the literature review, classification based purely on price differences, tends not to be very accurate – this is because one cannot say for sure that all articles released during periods of overall upwards positive price movement are positive and vice versa. However, we are operating under the assumption that news articles strongly reflect the direction of movement of the stock market. We expect the price to move up when news articles discuss increases in sales, innovation, positive restructuring and we expect the price to move downwards when news articles discuss fines, bankruptcy, litigation, sanctions etc.

Automatic labelling, therefore, provides us with a baseline. The higher the similarity between the results of automatic labelling and that of manual labelling, the more *trust*, we can place in the results of manual labelling.

* + - 1. **Evaluating Labelled News Articles**

Sentiment labelling generated via automatic categorisation is a reflection of the price movements, not a reflection of the articles themselves. However, since the articles themselves are manually labelled to reflect precisely the sentiment which they carry, we can conclude that if there exists a high similarity the results of manual labelling and the results of automatic labelling, then we can say confidently that the labelled articles can lead to positive results in later classification.

We note that news articles labelled automatically cannot be classified based on emotion sentiment. Emotion sentiment by definition requires a human evaluator to label articles based on what feelings are evoked by reading the article. However, since the method by which we automatically label stock data is based on the progression of the stock price, we can automatically label articles based on progress sentiment.

How therefore do we evaluate the results of labelling? An easy method of doing this is by calculating the Pearson’s product-moment correlation coefficient. We comprehensively discuss the results of the calculations and other considerations (specific to calculating the correlation) when discussing the evaluations in chapter 5). We finish off this section by pointing out that the more similar the correlation values are between the projected trend line (generated via piecewise linear approximation) and the actual stock price trend line, the higher the similarity is between the two trends.

### Data Pre-processing

Retrieved news articles are in HTML format. The news articles therefore need to be converted into plain text, tokenised (into unigrams and bigrams), stemmed and have stop words removed (discussed in chapter 3) before classification can take place.

### Document Representation

After the completion of all pre-processing steps, the documents are now ready to be transformed into vectors. The library Scikit-learn provides the TfidfVectorizer that converts the news articles into a TF-IDF-weighted document-term matrix. TF-IDF has been discussed in (chapter 3).

### Feature Selection or Reduction

In the literature, the chi-squared method for feature selection and the SVD method are popular. We decided to use as SVD is a very computationally expensive method.

### Classification

The final step is to train the SVM to predict the news article. In order to properly evaluate the SVM, cross validation over the data set was performed. 10-fold cross validation ensured we got the performance of the hyper-parameters of the SVM. The results of each fold were evaluated using the following metrics: confusion matrix, recall, precision and f-measure. These results can then be averaged over the number of folds to determine the overall performance of the hyper-parameters.

## Price Prediction

Price prediction is the actual step that combines the results of sentiment classification into a single result. We have introduced all the techniques relevant for price prediction in chapter 3, thus we will dive into the method of prediction.

We use a linear SVM model rather than a non-linear for this particular task. The reason being that solving for C is easier for solving for and ; thus, making the applicability of the proposed model more feasible. We have not tested the effectiveness of a Gaussian SVM, however, we have reason to believe that we would gain even better results with a Gaussian SVM (Keerthi & Lin, 2003), should we have the time and resources to compute for the optimal values of C and ;

In order to make price predictions for each individual company, the news data have to be re-split into categories defined by the company the news is relevant to. Thus, we have 14 features for training the SVM-HMM model: 12 technical indicators and 2 news-based features (progress and feeling). For each company, 120 days of news classified by the SVM in section 4.2.6, combined with 120 days of technical data served as the test period while a definable and changeable number of days served as the training period. We say definable as we use a sliding window of training data to train the hybrid SVM-HMM model. This ensures that the model is as sensitive as permissible to the market as possible.

Manual analysis of the piecewise linear approximation-based trend line, gives an indication of how long the trends last for and thus the number of days for the training window. Once determined, we used a fixed training window width. Defining an appropriate window width has significant bearing on price prediction; a longer window width during times of stability is likely to lead to better results than shorter widths. Correspondingly, a shorter window width during times of rapid swings in the price might lead to better prediction. Keeping this in mind, it has to be noted that the SVM, in order to compute usable probability has to be trained on enough data, hence there is a trade-off between the number of training data that can be used for SVM training and the sensitivity to the market in the short-term. Having defined the window, the SVM is trained with data within the bounds of the window. The SVM can then provide the emission probabilities as explained in section 3.6.

Our definition of the HMM is almost complete as we have the number of states (two, each representing the upwards and downwards movement of the stock price) and the emission probabilities. The transition probability however, is still unknown so we learn this using the Baum-Welch algorithm for the transition probability. Finally, we can then run the Viterbi algorithm on the past days of data to predict the sequence of states for each of the past days. As we are only interested in predicting the next day’s price, we simply take the hidden state for the day as the prediction of the next day.

Figure 4.2 and figure 4.3 provides a visual illustration of the process, for a single day’s prediction for time .

Figure 4.3 – Timeline visualisation of sequence and window

Data from window

Data from window

Baum-Welch

Emission Probabilities

SVM - training

Transition Probabilities

Emission Probabilities

Viterbi

Data from sequence

Figure 4.4 – Process visualisation for prediction. Pink boxes represent data from time series, Blue boxes represent processes, Green boxes represent intermediate results from processes, orange boxes represent final result being sought after

We formalise the process of making a prediction in algorithm 4.1.

|  |
| --- |
| price prediction |
| 1: **for** each trading day  2: select training window of length  3: using cross-validation and grid-search determine parameters for SVM  4: train SVM for emission probabilities using , using parameters  5: train HMM for transition probabilities using and emission probabilities  6: state of viterbi algorithm using sequence  7: **yield** state of as prediction for |

Algorithm 4.1 – Price Prediction Algorithm

# Evaluation and Results

## Method Overview

In this section, we detail the results of each of the main activities that have been discussed in section 4. The format of this section is the same as that of section 4, this is for easy referencing and comprehension.

## Data Acquisition

### News Article Acquisition

We do not use all of the acquired data because of time constraints – there’s no way for a single person to manually label the 12000 articles in the available time frame of 4 weeks. Hence, we had to discard a lot of the news articles and aim for classifying a fraction of the news articles (about 2250 articles). There is a need to determine which companies we aim to classify. The companies selected were chosen from the Dow Jones Industrial Average (DJIA) because the companies listed on the index are major American companies which tend to get a lot of attention from the media.

The table below shows the number of articles that were gathered for each company.

|  |  |  |
| --- | --- | --- |
| Company Name | Number of Articles | |
| Chevron | | 88 |
| Cocacola | | 52 |
| Disney | | 108 |
| Exxon | | 120 |
| Goldman | | 731 |
| IBM | | 118 |
| JP Morgan | | 613 |
| Microsoft | | 259 |
| Pfizer | | 115 |
| Visa | | 48 |

Figure 5.1 – Number of articles collected for each company

### Stock Data Acquisition

The price daily values were collected for the period from the 1st of January, 2013 to the 30th of September, 2014. Of course, the stock price data is only released for working days so this accounts for only 440 working days.

## Labelling

### Manual Labelling

We show the results of manual labelling in this section. Principally, this comes in the form of the Pearson’s correlation coefficient carried out between the stock price and the aggregate sentiment. The aggregate sentiment is calculated simply by adding the sentiment for every previous day in the time series. In order to do this, we need to calculate the aggregate sentiment for each working day.

Supposing therefore that we have 4 articles released on any day labelled as such: (please refer to the appendix – section 7.1 – for how this is derived from the sentiment labels) using progress sentiment. The aggregate sentiment would be given as by taking the sum of all the sentiments together. In addition to this, supposing we have any set of 8 days for which the aggregate sentiment for each day is given, we have aggregate sentiments for each day to be the sum of previous sentiments:

We’ve aggregated the sentiments to better show the rise and fall of the overall sentiment. With this transformed sentiment, we calculate the correlation between the stock price closing values and the sentiment. The table below shows the correlation values between each company’s stock data and the aggregated sentiments.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Company Name | Correlation of Progress Sentiment (Actual) | | Correlation of Emotion Sentiment (Actual) | Correlation of Progress Sentiment (Projected) | Correlation of Emotion Sentiment (Projected) |
| Chevron | | 51.7 | 51.8 | 49.7 | 50.1 |
| Cocacola | | 32.8 | 32.6 | 32.99 | 32.84 |
| Disney | | 97.6 | 97.6 | 97.10 | 97.13 |
| Exxon | | 79.0 | 78.8 | 79.7 | 79.6 |
| Goldman | | 76.74 | 77.42 | 71.98 | 72.5 |
| IBM | | 53.2 | 53.3 | 51.7 | 51.8 |
| JP Morgan | | 84.2 | 84.4 | 84.5 | 84.7 |
| Microsoft | | 95.8 | 95.8 | 95.8 | 95.8 |
| Pfizer | | 51.1 | 51.6 | 50.9 | 51.3 |
| Visa | | 89.14 | 89.20 | 88.80 | 88.86 |

Figure 5.2 – Table of correlation between sentiment and stock price using manually labelled data

Looking at the table above as well as Figure 5.1, there are several points raised regarding the values shown. We attempt to discuss some of them here but leave others until we show the results of automatic labelling. In addition, we also generate correlation coefficients between the projected trend lines (from piecewise linear approximation) and the sentiment – for purposes of comparison with the results of automatic labelling.

We see that in almost all cases, the values of the correlation projected values are almost always lower than the correlation between the actual stock prices. It is expected that there would be a difference between the correlation between the two pairs of values but assuming that piecewise linear approximation generates trends as accurately as possible, the difference between the correlation values should never be large enough to raise questions. Exxon as we can see has correlation coefficients that are larger in the projected trend line than in the actual trend line, although probably not significantly so.

In addition, we can see that although emotion sentiment and progress sentiment are intended to be different measures of labelling articles, they lead in all cases to similar correlation coefficients. However, we note that in almost all cases, actual progress sentiment has a higher correlation value than projected progress sentiment.

Finally, we address the fact that something must be done for those days in which news articles are not released (this applies as well when calculating the correlation for automatically labelled data). There are three assumptions we can make when classifying based on progress:

1. There is an underlying feeling of positivity – that is, these cases, the stock price is assumed to go up meaning that the progress sentiment is always positive
2. There is an underlying feeling of neutrality – the stock price will stay the same when there’s no news.
3. An underlying feeling of negativity – the stock price will go down when there’s no news

While it might seem that an underlying feeling of neutrality is the most appropriate, this is not true. The underlying feeling depends on the company being discussed. Prices of most companies change positively when there’s no news hence we assume an underlying feeling of positivity. However, for companies such as IBM, there’s an underlying feeling of negativity. This is determined by simply looking at the overall projected trend line. IBM over the course of the time period has shown a gradual decrease in price. This is sentiment is well reflected in articles as IBM over the course of the time period had trouble keeping up with other technology firms who have incorporated cloud computing into the services offered, which IBM had yet to do.

The term *underlying feeling* is vague and thus, explaining what is meant by it is important. Prices rise when traders feel that a stock is undervalued (hence, their demand for it increases), conversely prices fall when traders believe that a stock is overvalued (hence, demand falls). The belief that a stock is overvalued or undervalued changes with events – that are hopefully reported in the news. In the absence of news, we need to still capture this belief or feeling that traders have towards a certain stock. While technical indicators *imply* this feeling, we can explicitly state this feeling as sentiment for those days that news articles aren’t released. This basic assumption for days in which there is no news isn’t perfect – thus, there is a bit of noise introduced into the system. We address how this can be improved in future work in section 6.1.

News articles aren’t released solely during weekdays; however stock markets are closed over the weekend. This doesn’t mean that trading does not occur over the weekend – extended hours trading does – however price changes aren’t released for the weekend. Hence, in order to calculate the correlation, we have to eliminate news articles that are released on days that fall on weekends. This of course is detrimental to our calculations but despite this we see that there still is a high correlation between stock prices and news articles.

### Automatic Labelling

The first few steps that need to be carried out for automatic labelling are similar to the steps carried out for manual labelling – summarily, calculating the aggregate sentiment of the news articles over the time period. As previously mentioned in section 4.2.2.2, we only calculate the progress sentiment of the news articles. The sentiment is then correlated both with the projected trend and the actual price trend. Figure 5.3 - 5.12 show generated projected trend lines as well as the actual stock price movements for the companies.

Using the Exxon trend line as a sample case, we show how news articles are classified based on where they fall in the projected trend line – Figure 5.13

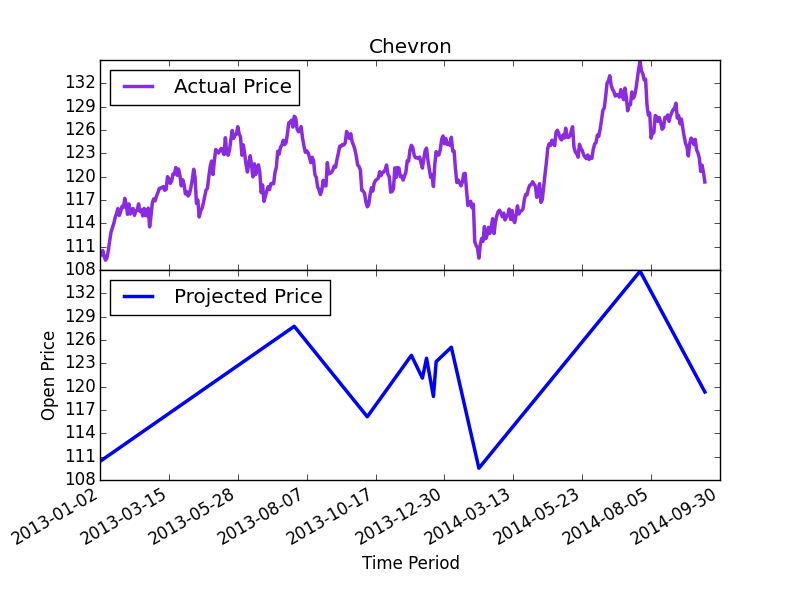


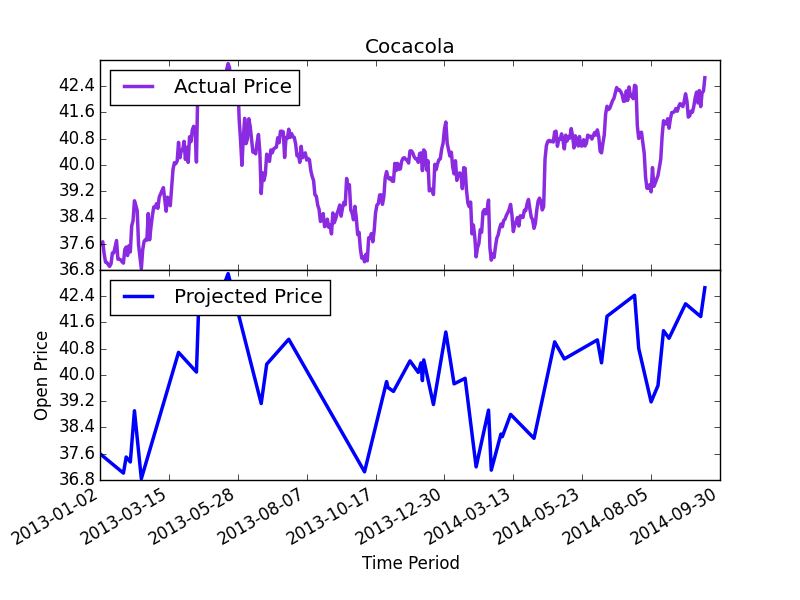
Figure 5.3 - Actual Stock Price and Projected Price of Chevron

Figure 5.4 - Actual Stock Price and Projected Price of Cocacola

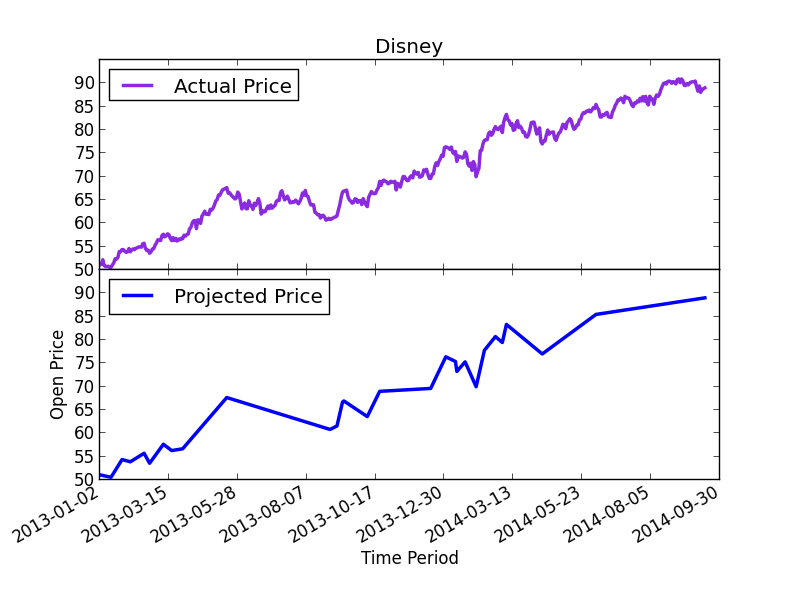


Figure 5.5 – Actual Stock Price and Projected Price of Disney

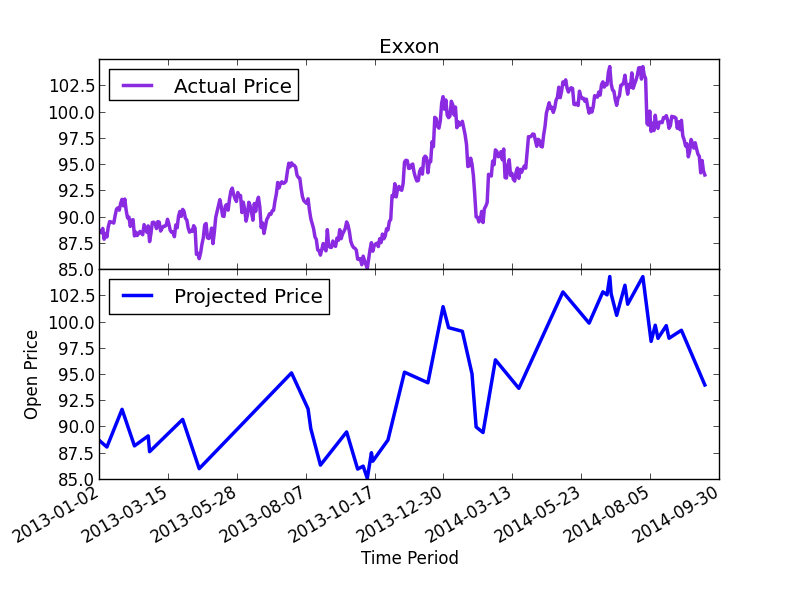


Figure 5.6 – Actual Stock Price and Projected Stock Price of Exxon

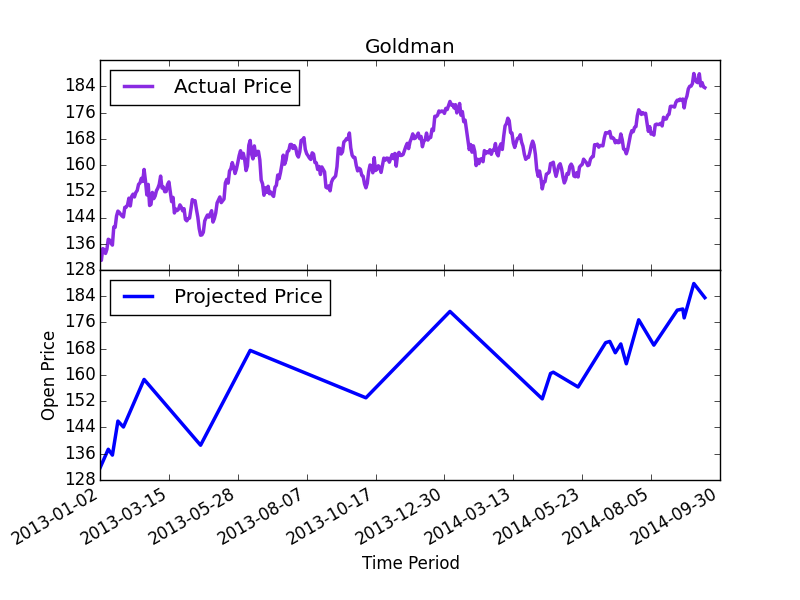


Figure 5.7 - Actual Stock Price and Projected Price of Goldman

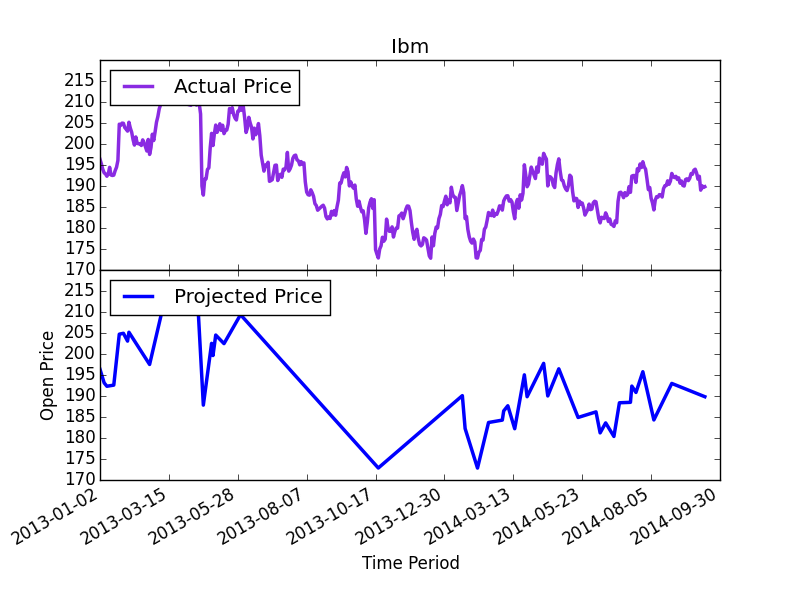


Figure 5.8 - Actual Stock Price and Projected Price of IBM

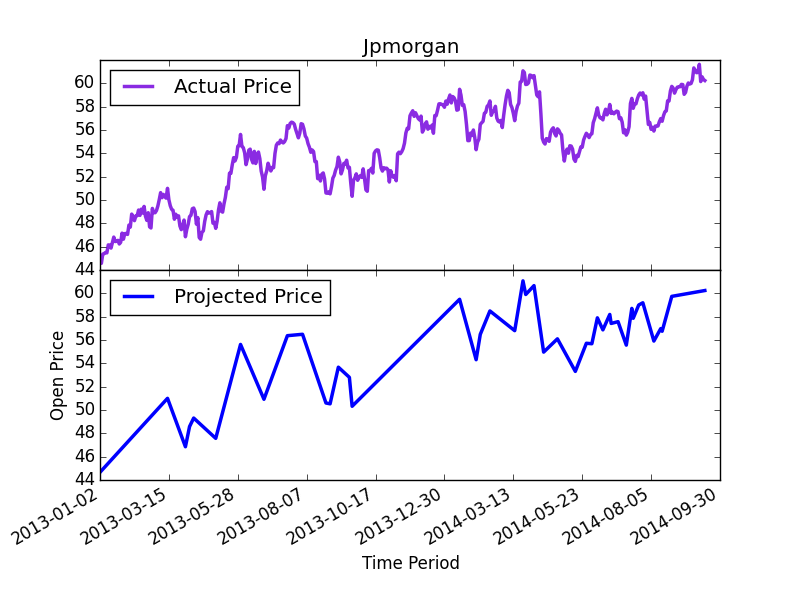


Figure 5.9 - Actual Stock Price and Projected Price of JPMorgan

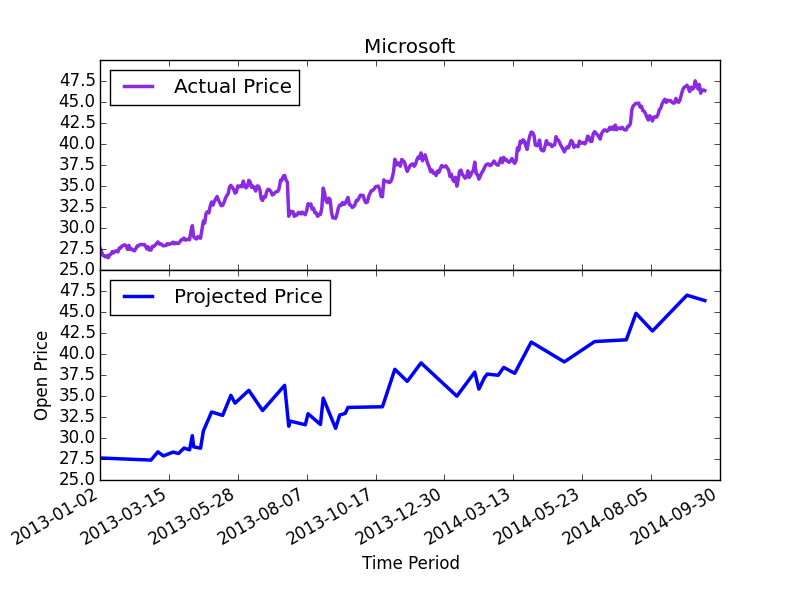


Figure 5.10 - Actual Stock Price and Projected Price of Microsoft

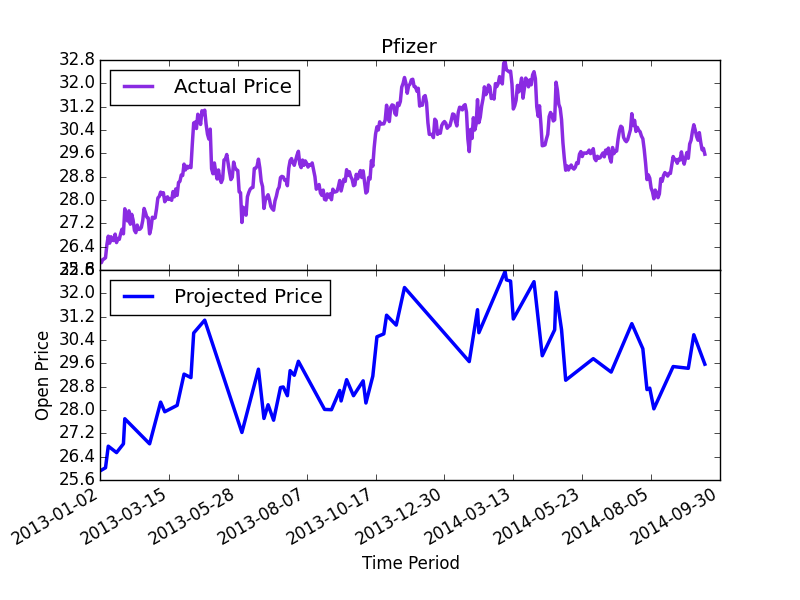


Figure 5.11 - Actual Stock Price and Projected Price of Pfizer

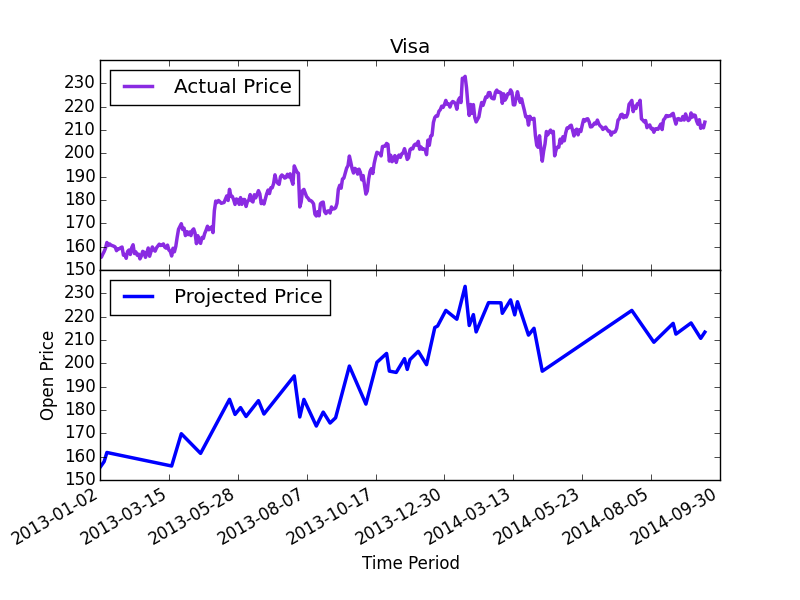


Figure 5.12 - Actual Stock Price and Projected Price of Visa

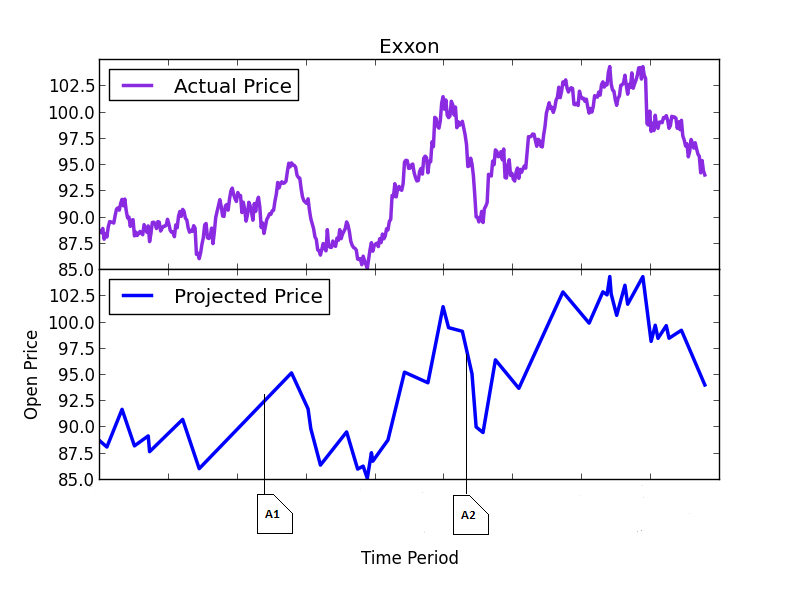
****

Figure 5.13 – Aligned News Articles with Trends

Using Figure 5.13 as a sample case, we would classify article A1 as “up” or positive while A2 would be classified as “down” or negative. After achieving this step, we can then proceed to calculate the correlation between the automatically calculated prices and the labelling. The table below shows the correlation results.

|  |  |  |  |
| --- | --- | --- | --- |
| Company Name | Correlation of Progress Sentiment (Actual) | | Correlation of Progress Sentiment (Projected) |
| Chevron | | 50.2 | 51.8 |
| Cocacola | | 32.1 | 32.0 |
| Disney | | 97.0 | 97.5 |
| Exxon | | 80.4 | 79.7 |
| Goldman | | 50.0 | 52.60 |
| IBM | | 52.12 | 53.41 |
| JP Morgan | | 85.37 | 85.14 |
| Microsoft | | 94.99 | 94.99 |
| Pfizer | | 53.08 | 53.33 |
| Visa | | 89.27 | 89.62 |

Figure 5.14 – Correlation between emotion sentiment and stock price using automatically generated data

Looking at the data above and comparing them, we see that the correlation values are quite similar to that of the manual data except for the correlation values of Goldman Sachs which is vastly different from the result of manual classification. The reason for this is that Goldman Sachs often is the source of the news (for example, Goldman Sachs often advises on buying and selling other companies) and the news is not about Goldman Sachs. This means that automatic labelling is blind to these issues as it labels both news *by* Goldman as well as news *about* Goldman without using any filter. However, when manually labelling, we ensure to label those articles are “neutral” in terms of progress of the entity and the relevant emotion sentiment.

### Labelling Discussion

We see that our results aren’t perfect – we believe that this is more indicative of the small dataset than a general inability of sentiment to correlate with the stock price.

As this is an exploratory project, the results of labelling is in general very positive – providing a reason to go on with classification of the news articles – preferably using the manually labelled data. The high similarities between the progress coefficient of the automatic and manual data also is a form of validation for the manually labelled data and idea that news articles correlate with the stock price. However, the results also make harder to overlook the issues with automatic labelling.

## Data Pre-processing

Using the method described in section 4.2.3, the dataset was pre-processed. However, there’s a decision to be made about which method of tokenisation is best. In our experiments, we performed only 3 types – unigrams, bigrams and combination of both. These types are the most popular in the literature. Unigrams, also known as bag of words are criticised often for not bearing enough information but we see that in all areas, they perform quite well. Bigrams, as we will see also perform comparatively to unigrams. The combination seems to perform the best of all three. In addition, when tokenising, we only select words that have greater than three characters.

The table below shows the number of features that are extracted and the number pre-selected (based on term frequency) before feature extraction or selection.

|  |  |  |  |
| --- | --- | --- | --- |
|  | Unigram | Bigram | Unigram + Bigram |
| Initial number of features | 26322 | 310660 | 336982 |
| Selected amount of features | 11000 | 16000 | 16000 |

Figure 5.15 – Initial features and pre-selected features

## Feature Selection or Feature Reduction

During the experimentation phase, we compared the results of SVD with based feature reduction. The results are very similar with no distinct advantage provided by SVD (rather, it’s disadvantageous as it took up to 2 hours to compute for bigrams), we decided to opt for feature selection based on , hence the classification results in the succeeding section detail the results based on feature selection and not feature reduction simply because the results are virtually the same. Even furthering our decision to use is the fact that the computational intensive process of SVD will be even more pronounced with a live system.

In addition to the benefits provided by , there are also benefits in terms of ability to examine the features selected more closely. In figure 5.9 and 5.10, we show 10 tokens selected for both the progress and emotion sentiment (please note that these aren’t in any particular order – instead the table is as a result of words selected across all folds during cross-validation).

|  |  |  |
| --- | --- | --- |
| Unigram | Bigram | Unigram + Bigram |
| aaa | accord announced | aaa |
| surplus | zero percent | abnormal |
| illegal | capital declined | analysts predict |
| destroy | company profit | exciting |
| asian | stock buyback | growing market |
| litigation | Creditworthiness decreased | Largest technology |
| embezzlement | stock gained | Lawsuit jpmorgan |
| examination | wall street | laundering |
| fine | volatility index | straight year |
| value | legal claims | breach contract |

Figure 5.16 - Words selected for progress classification (manually labelled data)

|  |  |  |
| --- | --- | --- |
| Unigram | Bigram | Unigram + Bigram |
| acceptable | aaa credit | abandon |
| grossing | aaa rated | billion asset |
| questionable | abc network | cash flow |
| rallied | income drop | government bond |
| suppress | percent called | shrank percent |
| disagree | seek boost | trading stock |
| distort | later acquire | state law |
| expense | gain ground | jpmorgan led |
| investigation | dollar bond | Exclusive |
| policy | compliance action | development |

Figure 5.17 – Words selected for feeling classification (manually labelled data)

We have neglected to include the corresponding tables for the automatically labelled data as automatically labelled data had lower overall accuracy than manually labelled data and was not further used in price prediction. In addition, it should be noted that the words shown in either table are not necessarily exclusive to the table. For example, “jpmorgan led” which appears in the 8 row of the Unigram + Bigram column also appears as a bigram feature when classifying based on progress sentiment.

## Document Classification

### Manual Classification

In this section, we detail the results of classification of manually labelled data and the settings used to achieve the results. As we use an SVM linear classifier, the parameters that need to be set are the class weights and the cost. Other parameters to be set are default parameters by the classifier. First, we discuss the classification of progress sentiment and show the results, followed by the classification of emotion sentiment.

#### Progress Sentiment Classification

In order to set the weights, we need to look at the support for each class. Figure 5.18 shows the number of articles supporting each class. The hyper-parameters used for configuring the SVM are as follows:

LinearSVC (the class used for classification) implements the one-versus-rest classifier for multiclass problems. We use a *C* value of 2.9, discovered by cross-validation and grid search. We use automatically set class weights (which modifies the C-values for each class) for the SVM as Figure 5.18 shows, the classes are not represented equally in the training sets. Using a StratifiedKFold cross validator, we can preserve the percentage of representation for each sample.

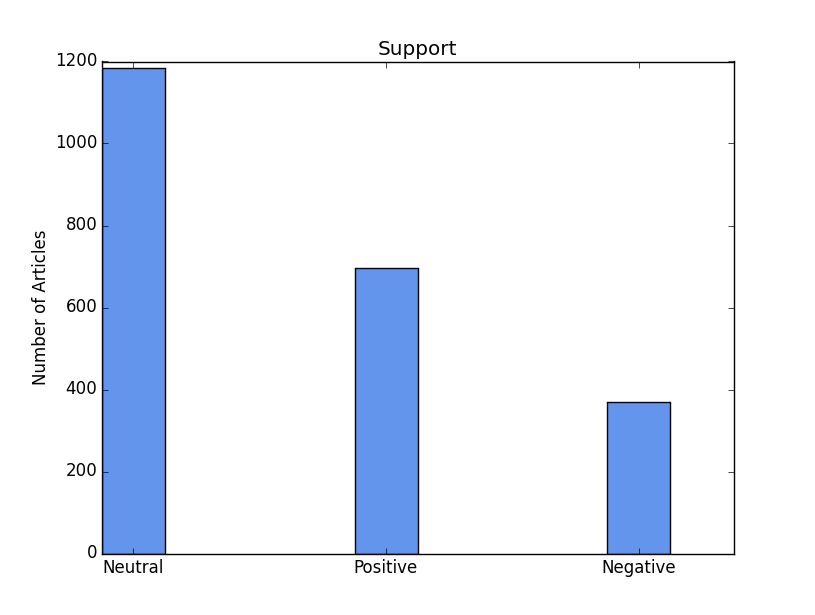
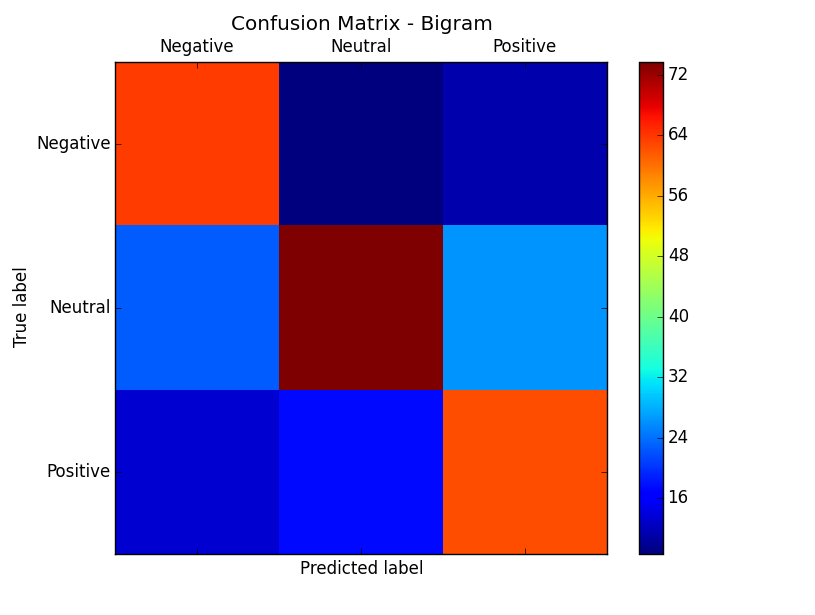
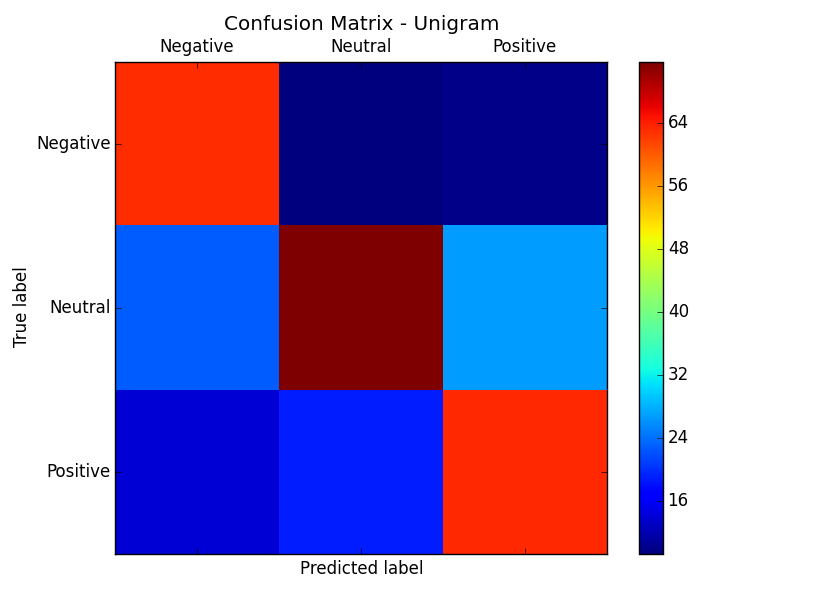


Figure 5.18 – support for the various classes (manual/progress)

Similar settings were used for bigrams, unigrams and combination experiments. In order to determine accuracy, we use cross validation and the following metrics: f-measure, recall, precision and confusion matrix. We compute the average of the scores of all the folds. The confusion matrices for unigram, bigram and combination (Figure 5.19) show an overview of the accuracy for the three classes.

The confusion matrices show that there aren’t very big differences in the performances of the three methods of tokenisation (except when classifying positive articles). It’s very difficult to explain why this is the case except that all three methods carry similar levels of information for this problem.



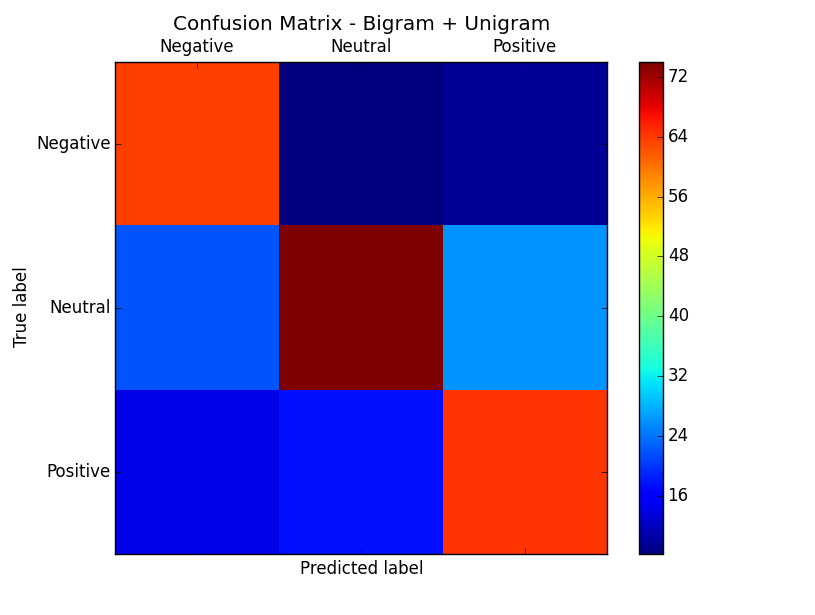


Figure 5.19 – Confusion matrices (Manual/Progress). Top left – Unigram, Top Right – Bigram, Bottom – Unigram + Bigram in percentages

|  |  |  |  |
| --- | --- | --- | --- |
|  | Unigram | Bigram | Unigram + Bigram |
| F-measure | 68.62 | 69.82 | 70.51 |
| Recall | 68.68 | 69.97 | 70.58 |
| Precision | 69.04 | 70.17 | 70.62 |

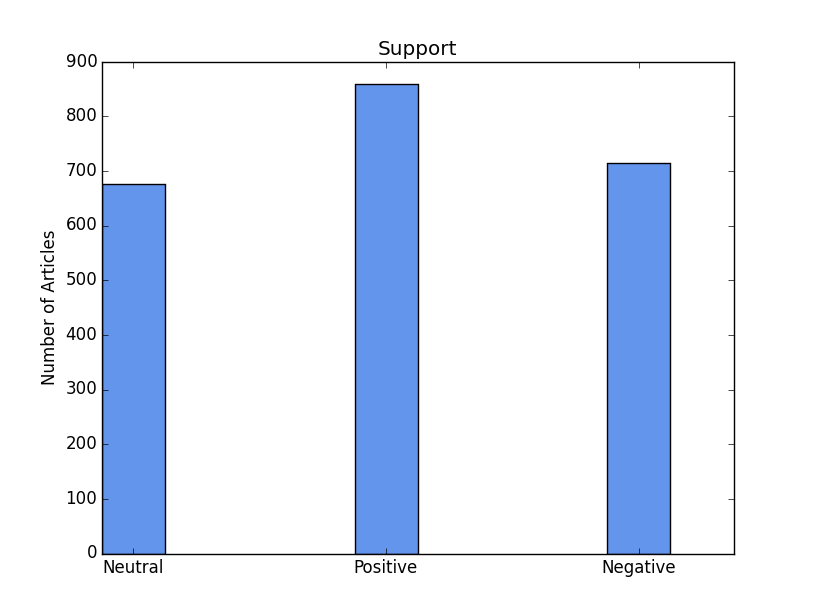
Figure 5.20 – Table of performance of linear SVM measured by cross validation (manual/progress)

Delving into the actual numbers, we see that overall, the bigram does better than the unigram and the combination of both does better than either of them singularly. Combining this information with the confusion matrix, we see that bigrams and the combination perform better due to being able to slightly classify positive news articles better.

Given the similarities in the values, T-tests were performed (with an alpha of 0.05 and degrees of freedom where is the number of articles) to determine there are any significant differences between the results attained with the features. The t-tests confirmed that there are no statistically significant differences between the results.

#### Emotion Sentiment Classification

Poorer results were achieved for the classification of emotion sentiment in general. This is contradictory to the initial belief that emotion sentiment would be easier than progress sentiment to classify – however, it’s now clear that given that the articles bear little obvious sentiment, the results are not entirely surprising. We performed classification using a linear SVM as before. The settings for emotion sentiment were quite different. In addition, classification performance for the emotion sentiment was quite poor overall. As per the previous section, we start by introducing the frequencies for the classes (Figure 5.21)

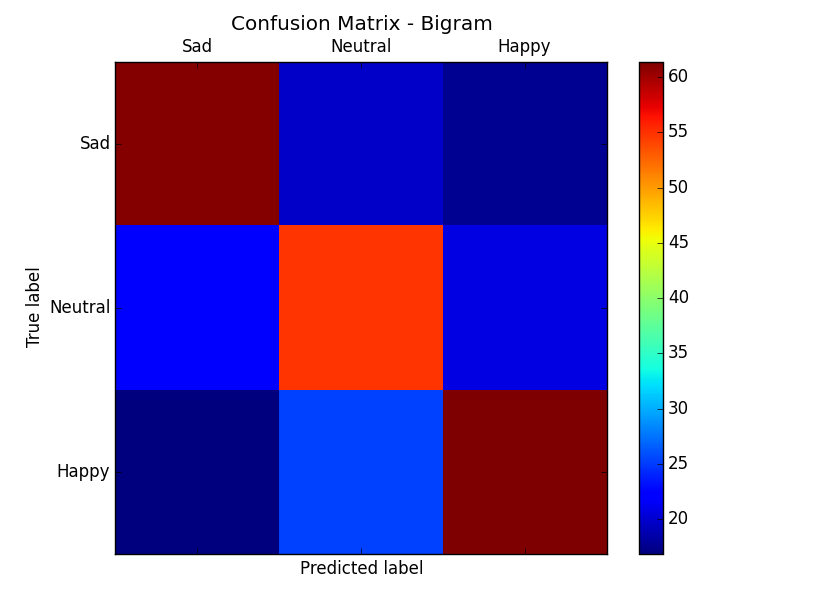
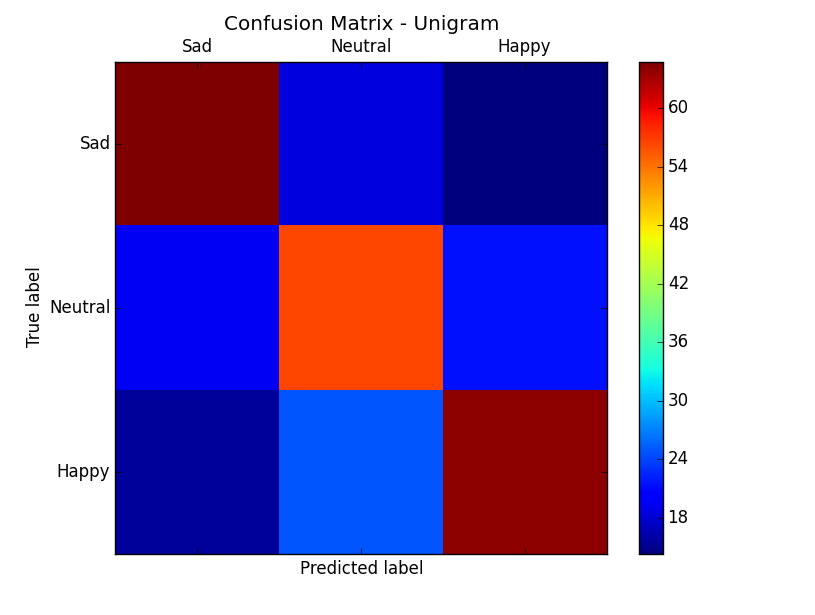


Neutral Happy Sad

Figure 5.21 – Support for the classes (Manual/Emotion)

Different hyper-parameter settings were used for classification. The parameter was set to higher levels with a value of. The other parameters, such as the class weight were also set automatically based on the class.

Considering the confusion matrices (Figure 5.15), we see that all three methods of tokenising perform very similarly as before. A possible reason for this is that news articles often bear mixed feelings. On the surface, it may seem that news articles bear emotion sentiment orientations that lean towards one way or the other but this isn’t so. News articles often carry information that lean to both sides. A classic example of such news articles is articles that discuss “happy” sentiment. In a few of these articles, there’s also discussion of past “sad” sentiment that led to perhaps structural changes that result in improvement. Hence, while progress sentiment might be relatively clear, emotion sentiment can often be ambiguous when it comes to classifying neutral articles.



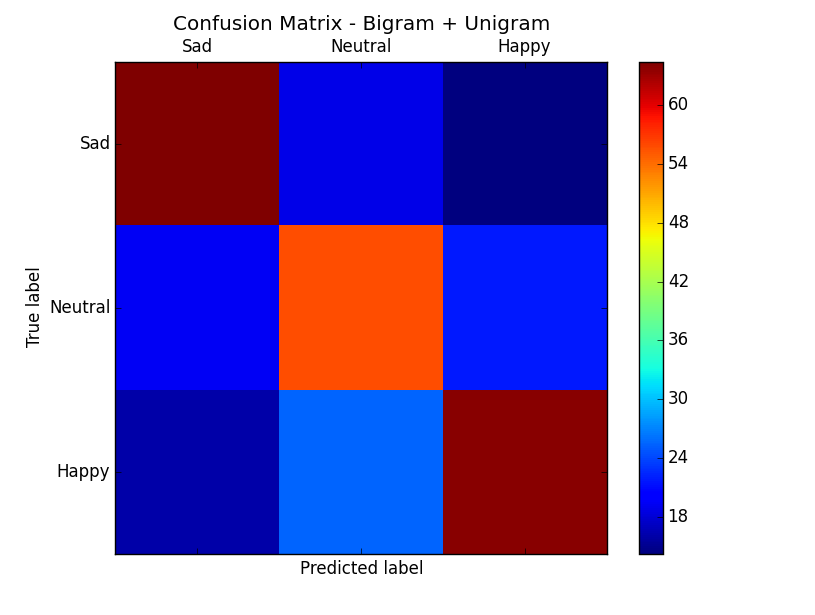


Figure 5.22 – Confusion matrices (Manual/ Emotion). Top left – Unigram, Top Right – Bigram, Bottom – Unigram + Bigram in percentages

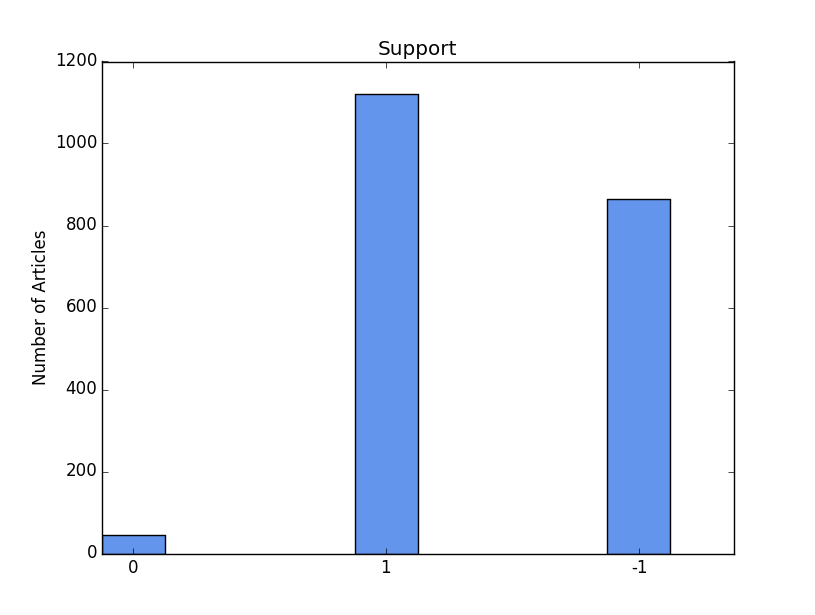
|  |  |  |  |
| --- | --- | --- | --- |
|  | Unigram | Bigram | Unigram + Bigram |
| F-measure | 62.00 | 60.87 | 63.68 |
| Recall | 62.48 | 61.06 | 63.92 |
| Precision | 62.23 | 61.15 | 63.99 |

Figure 5.23 - Table of performance of linear SVM measured by cross validation (Manual/ Emotion)

Bigrams are typically expected to do better than unigrams due to the fact they retain sentence structure but clearly, bigrams doesn’t do very well for this problem looking at the performance measures in Figure 5.16. However, combination of both performs better than either but not by much.

### Automatic Classification

In this section, we follow the same pattern as in section 5.6.1, with the exception that we only discuss progress sentiment. We use a value of 3.5. For automatic classification, neutral movements are severely underrepresented (only about 46 news articles were classified neutral); hence, we only consider positive and negative movements.



Neutral Positive Negative

Figure 5.24 – Support for the classes (Automatic / Progress)

Here, we only present the numerical results (Figure 5.25) to restrict repetitiveness as well as the fact that the manually labelled data will be used. It would of course be interesting to consider how well automatically labelled data performs when used subsequently for price prediction, however time constraints prevent this. In addition, the intention was not to use automatic labelling for classification; instead, it provided an adequate benchmark for comparison with the results of manual labelling. We have extensively discussed the pitfalls with automatic labelling (section 5.3.) we believe that the results here can be explained by these.

|  |  |  |  |
| --- | --- | --- | --- |
|  | Unigram | Bigram | Unigram + Bigram |
| F-measure | 64.50 | 66.30 | 64.49 |
| Recall | 67.97 | 72.55 | 61.36 |
| Precision | 61.43 | 61.12 | 68.05 |

Figure 5.25 - Table of performance of linear SVM measured by cross validation (Automatic/ Progress)

## Price Prediction Results

We present summary statistics of the features in the appendix (excluding statistics) for each of the companies analysed in section 7.2.

An important aspect of the price prediction is setting the window width. For companies that show less frequent swings in their trends (Chevron, Disney, Microsoft, Visa, J.P. Morgan, Pfizer, Goldman), we used the entire dataset available to us: That is, we train on 320 days, while predicting for 120 days. For companies that show slightly more rapid swings, we train on 120 days (6 months of data), predicting on 120 (Exxon), and finally, for the most unstable companies over the period we train on 60 days (Cocacola, IBM).

As with sentiment classification, we have opted to use a linear SVM. This again reduces the problem of setting parameters to finding the optimal value. We employ a grid-search with cross-validation in finding the C-values. The process of finding the C value has to be repeated for every trading day. It’s easy to see how the process can be expensive during the experimental phase but daily predictions would be much faster as we’d be searching for one C-value – the value for the current day.

In order to present the results, we normalise the close prices to a base of 1 (at the start of the 120-day period). The (financial times series) line is a reflection of the market price – or the close price, except normalised. The simple return is calculated using the formula:

|  |  |  |
| --- | --- | --- |
|  |  | (5.1) |

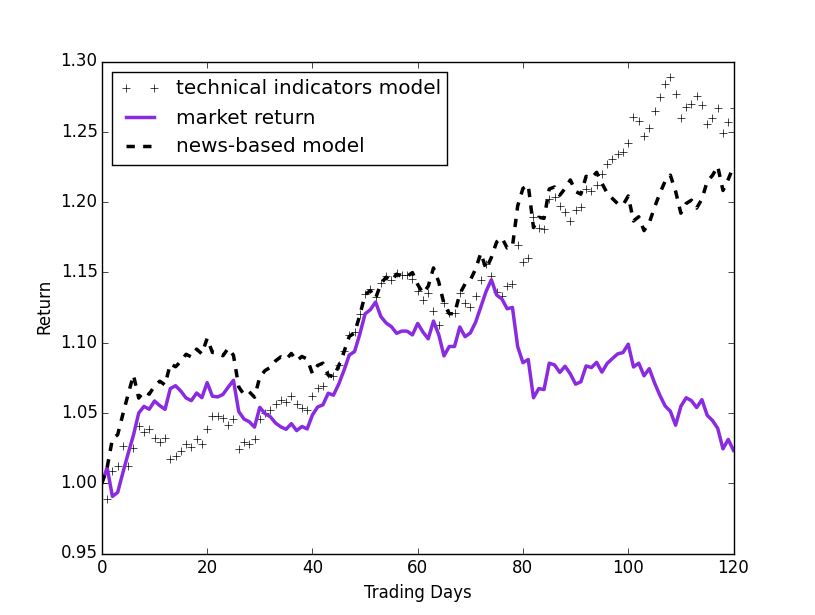
Where is the price at time . The cumulative return over a period of -days is thus calculated as:

|  |  |  |
| --- | --- | --- |
|  |  | (5.2) |

For clarification purposes, we provide the following illustration: Supposing at the start of the 120 day period, we buy stocks at a certain price, as the closing price changes, the return we’d make by selling the stock changes. This is exactly what the market return trend line signifies. Thus, a buyer at the start of the period loses money should the stock price fall and vice versa, should the price rise.

In order to determine the return of a prediction system, we assume that trades are made based on the prediction. Should the prediction system make a false prediction, trades made based on that prediction result a negative return; however, should it make a correct prediction, trades made based on that prediction result in a positive return. We can thus use the cumulative return formula to generate the return over a period of -days. If the model predicts a rise in price, a trader can simply hang on to the stock or buy new stocks and wait for the stock to gain in value. Should the model predict a fall in price, the trader can borrow shares from a broker, sell the stocks at the high price, wait until the price drops then buy shares at the lower price and return the borrowed shares back – the trader profits on the difference between the higher price and the lower price. This is referred to as shorting stocks. Either way, money can only be made depending on what assumptions the trader makes about the future.

Our experiment consists of two phases: using the SVM-HMM model inclusive of the sentiment data and without – this is in order to make a reasonable evaluation of the effect of sentiment data. Figures 5.26 to 5.35 show the results of both experiments.



**Chevron – Comparison Chart**

Figure 5.26 – Chevron return based on technical indicators only model, market return and news-based model

**Cocacola – Comparison Chart**

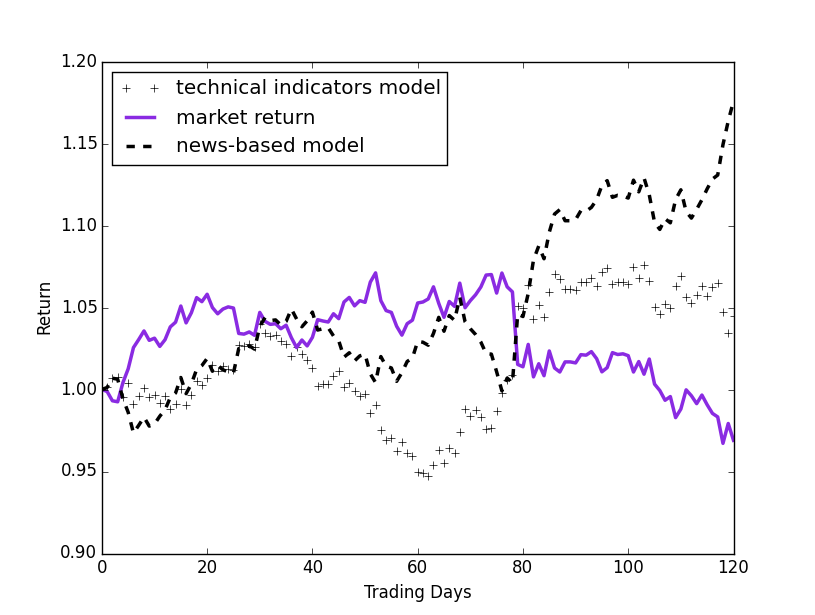


Figure 5.27 - Cocacola return based on technical indicators only model, market return and news-based model



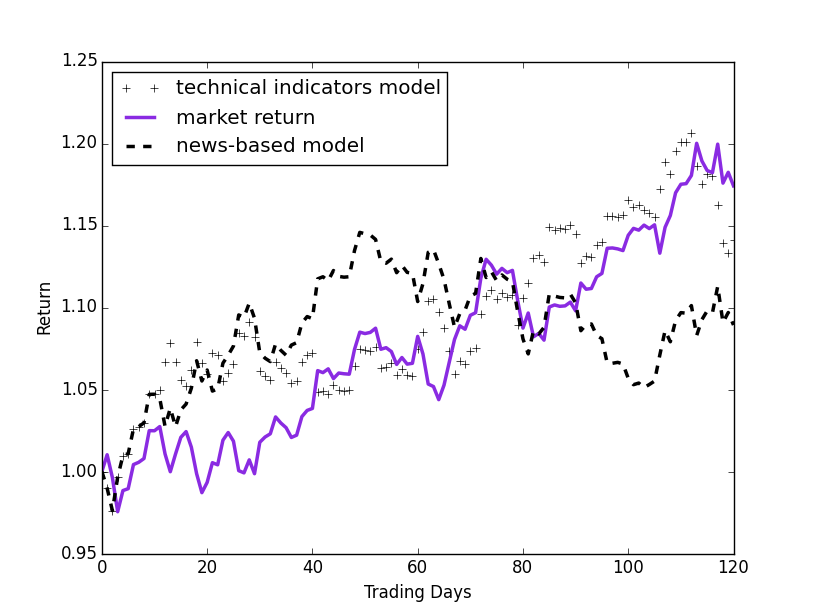
**Disney – Comparison Chart**

Figure 5.28 - Disney return based on technical indicators only model, market return and news-based model



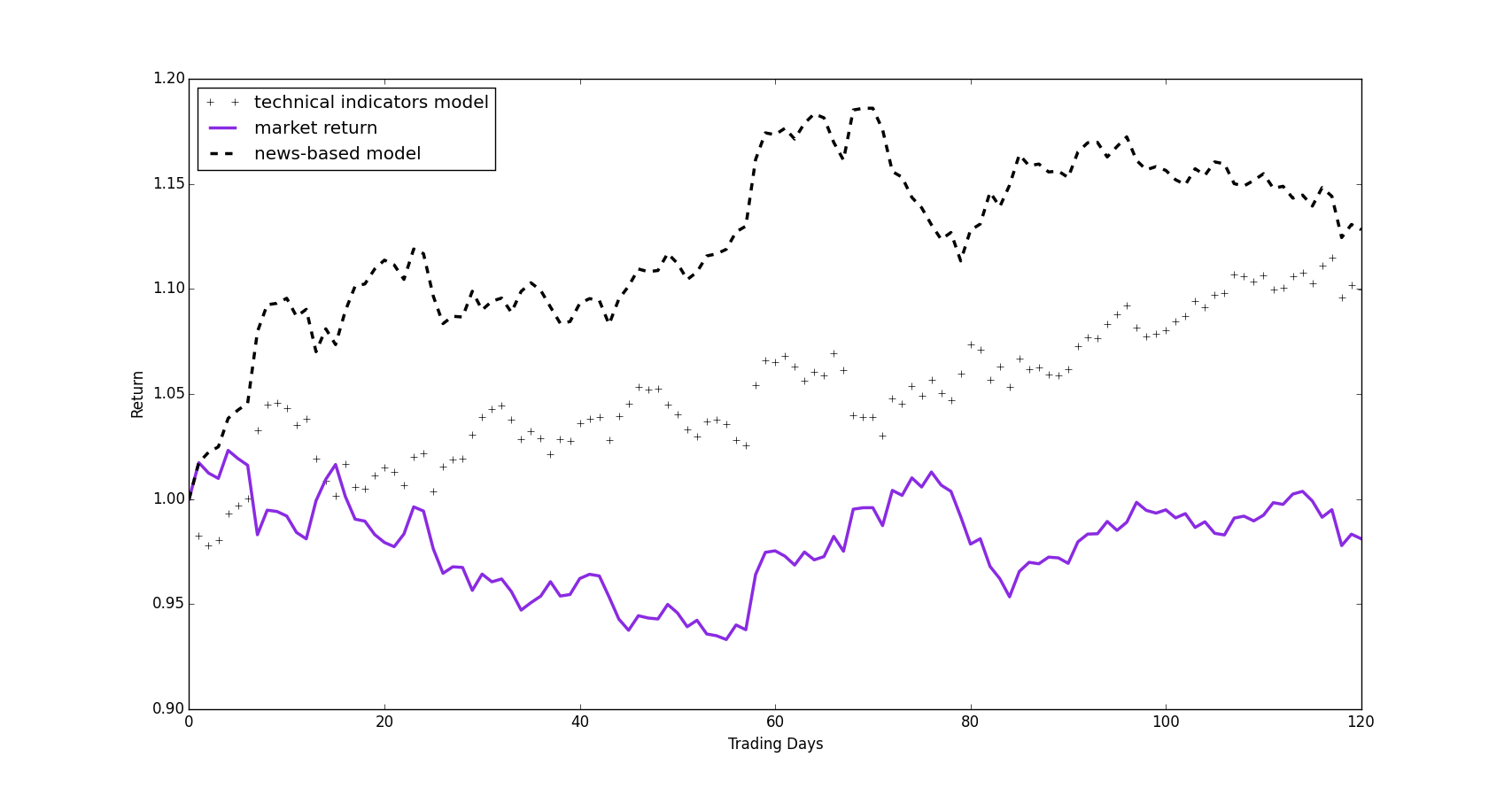
**Exxon – Comparison Chart**

Figure 5.29 - Exxon return based on technical indicators only model, market return and news-based model



**Goldman Sachs– Comparison Chart**

Figure 5.30 – Goldman Sachs return based on technical indicators only model, market return and news-based model



**IBM – Comparison Chart**

Figure 5.31 - IBM return based on technical indicators only model, market return and news-based model



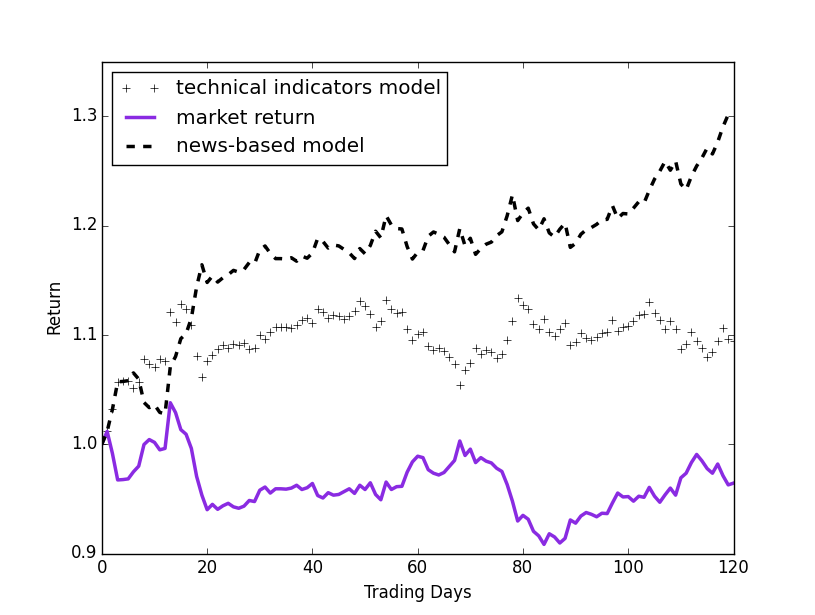
**J.P. Morgan – Comparison Chart**

Figure 5.32 – J.P. Morgan return based on technical indicators only model, market return and news-based model



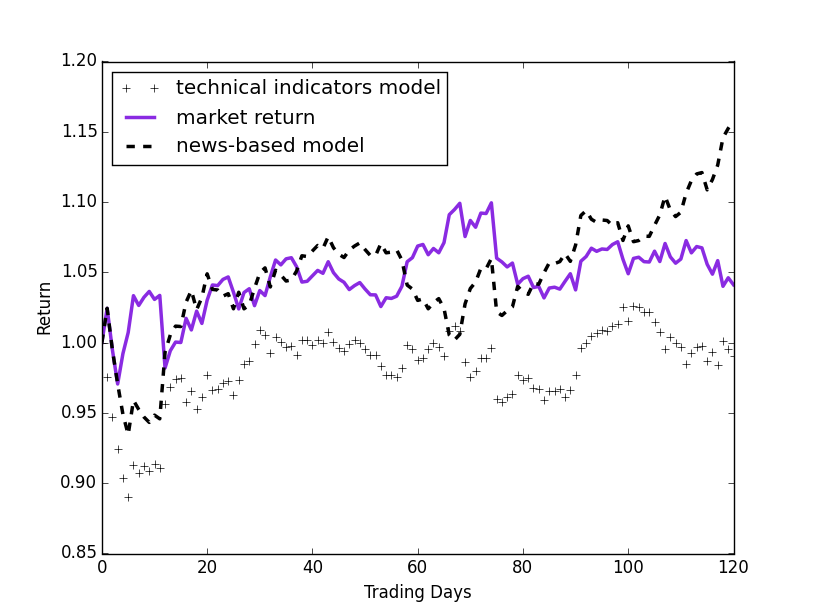
**Microsoft – Comparison Chart**

Figure 5.33 - Microsoft return based on technical indicators only model, market return and news-based model



**Pfizer – Comparison Chart**

Figure 5.34 - Pfizer return based on technical indicators only model, market return and news-based model



**Visa – Comparison Chart**

Figure 5.35 - Visa return based on predictions vs return of time series (inclusive of news-based features)

Examining all the preceding images, it’s quite clear that the addition of news-based features has a real and tangible effect on the overall prediction accuracy of the model. We attempt at this juncture to provide reasons and possible justification for our results. It’s important to note that each trend line is different and we have treated each company differently, and thus each of the models have different results.

Chevron and Goldman’s news based models, experienced poorer performance than the technical based models. We also highlight Microsoft whose news-based model performs poorly in comparison to the market, although better than the technical-only indicator. We propose that the reason for this is the less than perfect classification of sentiment as the other news based models experienced a better performance both than the market and the technical-only models.

We highlight Cocacola which seems to be a special case of (relative) positivity given that the very little news over the period. We also note that it performs better than the technical indicators only model.

In general, we see that both technical indicator only models and news-based model tend to suffer a loss in performance at the same time, however, the news based model tends to suffer less and recover faster. We believe that the results aren’t only dependent on news, but also on explicitly stating the sentiment for days that there isn’t any news – thus identifying the underlying predisposition of the market towards a stock is very important (as discussed in section 5.3.1.)

To finish up, we provide a table of exact figures of the return at the end of the 120 day period of the three trend-lines, in order to also provide a numerical evaluation (Figure 5.36.) Again, we point out that should a number shown be less than 1, that signifies a loss. For Exxon, market return for example, an intuitive way of interpreting the result is that an investor puts in £1 at the start of the period and gets £0.97 back. Total Returns represent the amount of money made at the end of the 120 day period.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Company Name | Market Return | | News-Based Model Return | Technical Indicators Only Model Return |
| Chevron | | 1.03 | 1.23 | 1.26 |
| Cocacola | | 1.085 | 1.123 | 1.04 |
| Disney | | 1.11 | 1.26 | 1.14 |
| Exxon | | 0.97 | 1.16 | 1.045 |
| Goldman | | 1.17 | 1.10 | 1.15 |
| IBM | | 0.975 | 1.135 | 1.08 |
| JP Morgan | | 1.03 | 1.24 | 1.16 |
| Microsoft | | 1.15 | 1.10 | 0.97 |
| Pfizer | | 0.965 | 1.3 | 1.09 |
| Visa | | 1.045 | 1.15 | 0.94 |
| **Total Returns** | | **0.53** | **0.798** | **0.605** |

Figure 5.36 – Numerical Representation of return over 120 day period

Looking into figure 5.36, we see that most companies experience a gain in the value of their share price over the period, hence shareholders over this period would have gained a significant return. We however see that our news-based model performed even better over the same period with the technical-only model performing second best. Given, our significantly encouraging results, we can say that our results correlate with the results of the literature review: in general news can be a reasonable basis for stock price prediction. We can also confidently say based on our results that there is significant merit to using technical indicators but even more merit when news is incorporated.

# Conclusion

We hope it’s say that the project is overall a success as both phases (sentiment analysis and price prediction) were completed successfully. One important result to point out is that one needn’t necessarily achieve sentiment classification accuracy of nearly 100% in order to base predictions based on automatic classification. We however, spend some time discussing what could be improved in order to make the system more reliable

## Future Work

One of the first obstacles to work around, as is the case in many projects is time restrictions. This severely restricted the amount of time we could spend manually classifying and the results of Goldman (section 5.3.3.) show us that automatic labelling while they can perform well, have to be used on a perfectly curated data set – which again requires a lot of manual work. The manual data was also classified primarily by an amateur despite the relative lack of knowledge compared to an expert, it has shown good results. Regardless it is recommended that further work utilise financial experts to manually classify the dataset. It’s further recommended that any manually classified data set is further reviewed by a separate team of experts. Given only this recommendation, it’s easy to see how this recommendation could make the process of developing a more advanced system could be significantly more expensive than the cost of this project in monetary terms (which was the cost of a 6-month Financial Times subscription).

Another point to note is the assumptions that have to be made for those days in which there is no news – in this work, we evaluated the trend-lines over the period and assigned a value for each day there wasn’t any news based on general the stock price movement over the period. We can improve this by performing a more in-depth analysis of the trend-line and assigning a more bespoke underlying sentiment to those days.

Another issue that was the repercussion of having little time is the dataset. Our meagre ~2250-article dataset proved to be useful enough but an even better dataset would contain articles upwards of 30000. This can easily be achieved by pooling news articles from several news sources. Another benefit of having such a large dataset is customisation of sentiment classification on a per-organisation or at least per-industry scale. We hope that the expected improvement to the sentiment classification accuracy is by this point obvious to the user. As a test, we decided to cross-validate the Goldman Sachs news dataset ((unigrams + bigrams) feature set and progress-sentiment classification) and we achieved an f-measure of 75.09%, significantly better than the 70.51% of the pooled data set.

We mentioned in section 4.3. that the means by which the window width is decided is by evaluating the linear approximation trends manually, which of which the result was a rigid window width; however, upon reflection, a fixed training window is too rigid, it’s better to integrate piecewise linear approximation into the overall process in order that training occurs with a customised sliding window. Hence, for the prediction based for test data at current time the training window of length , would only include training data in a segment defined by piecewise linear approximation. With the constraint that is the last known point in the time series defined by .

## External Aspect

A research paper accompanying this dissertation was written titled “Sentiment Analysis for Stock Price Prediction”. The paper was co-authored with Michel Valstar. The paper was written successfully for the fulfilment of the external aspect of the current work.

## Personal Reflection

The current dissertation has been less bumpy of a ride than I thought it’d be. It’s been a great learning experience on my end because I was given as much elasticity as possible intellectually by my supervisor. I started out with knowing nothing about the current field – it’s safe to say that the only aspects of the current work that I had any prior knowledge of were Support Vector Machines and Hidden Markov Models – everything else has been learnt as I went along.

The hardest part of the project was initially attempting to recruit financial experts. An important lesson learnt is that financial experts are very unlikely to work for free – especially not work that hopes to put them out of work in the future. Regardless of every obstacle and delay, I believe that the project was a success in every sense of the word.

# Appendix

## Keys for Transforming Sentiments to Numbers

### Progress Sentiment

|  |  |
| --- | --- |
| Sentiment | Numerical Value |
| Up | -1 |
| Neutral | 0 |
| Down | 1 |

### Emotion Sentiment

|  |  |
| --- | --- |
| Sentiment | Numerical Value |
| Sad | -1 |
| Neutral | 0 |
| Happy | 1 |

## Summary Statistics for Each Company

### Chevron

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0.00 | 100.00 | 56.92 | 31.62 |
| Stochastic | 2.59 | 98.95 | 56.94 | 29.57 |
| Slow Stochastic | 3.94 | 98.40 | 56.98 | 28.74 |
| Momentum | -9.31 | 10.63 | 0.43 | 4.04 |
| Rate of Change | 92.17 | 108.69 | 100.42 | 3.34 |
| William’s %R | 0 | -100 | -43.07 | 31.62 |
| A/D Oscillator | -1.12 | 1.82 | 0.52 | 0.50 |
| Disparity5 | 96.67 | 102.80 | 100.05 | 0.95 |
| Disparity10 | 95.24 | 103.82 | 100.12 | 1.53 |
| Price Oscillator | -0.02 | 0.02 | 0.0008 | 0.008 |
| Commodity Channel Index | -236.24 | 276.01 | 19.70 | 112.89 |
| Relative Strength Index | 82.83 | 82.83 | 52.86 | 11.71 |

Figure 7.1 – Descriptive Statistics for Technical Indicators (Chevron)

### Cocacola

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0.00 | 100.00 | 57.82 | 30.34 |
| Stochastic | 0.51 | 99.88 | 57.66 | 27.88 |
| Slow Stochastic | 1.51 | 99.15 | 57.51 | 27.06 |
| Momentum | -3.09 | 2.66 | 0.14 | 1.14 |
| Rate of Change | 92.71 | 106.99 | 100.41 | 2.28 |
| William’s %R | 0.00 | -100 | -42.17 | 30.34 |
| A/D Oscillator | -1.49 | 1.98 | 0.50 | 0.48 |
| Disparity5 | 96..62 | 103.01 | 100.07 | 0.94 |
| Disparity10 | 95.48 | 104.12 | 100.15 | 1.38 |
| Price Oscillator | -0.02 | 0.02 | 0.0006 | 0.007 |
| Commodity Channel Index | -358.84 | 347.35 | 20.60 | 112.41 |
| Relative Strength Index | 23.00 | 75.98 | 52.66 | 11.14 |

Figure 7.2 - – Descriptive Statistics for Technical Indicators (Cocacola)

### Disney

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0.00 | 100 | 62.48 | 29.93 |
| Stochastic | 2.05 | 99.32 | 62.49 | 27.31 |
| Slow Stochastic | 3.66 | 98.3 | 62.53 | 26.30 |
| Momentum | -5.37 | 10.14 | 1.17 | 2.51 |
| Rate of Change | 91.93 | 114.49 | 101.82 | 3.74 |
| William’s %R | -100.00 | 0.00 | -37.51 | 29.93 |
| A/D Oscillator | -0.89 | 2.55 | 0.58 | 0.449 |
| Disparity5 | 104.66 | 104.66 | 100.26 | 1.19 |
| Disparity10 | 95.94 | 106.52 | 100.60 | 1.80 |
| Price Oscillator | -0.02 | 0.03 | 0.003 | 0.01 |
| Commodity Channel Index | -248.09 | 298 | 48.03 | 102.73 |
| Relative Strength Index | 30.85 | 82.93 | 58.08 | 10.01 |

Figure 7.3 – Descriptive Statistics for Technical Indicators (Disney)

### Exxon

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0.17 | 100 | 54.16 | 31.11 |
| Stochastic | 1.02 | 97.37 | 54.16 | 29.04 |
| Slow Stochastic | 1.83 | 95.97 | 54.15 | 28.31 |
| Momentum | -9.36 | 6.94 | 0.24 | 2.98 |
| Rate of Change | 90.54 | 107.54 | 100.31 | 3.17 |
| William’s %R | -99.83 | 0 | -45.83 | 31.11 |
| A/D Oscillator | -0.69 | 1.64 | 0.49 | 0.48 |
| Disparity5 | 96.38 | 102.97 | 100.04 | 0.91 |
| Disparity10 | 94.78 | 103.76 | 100.10 | 1.43 |
| Price Oscillator | -003 | 0.02 | 0.0004 | 0.008 |
| Commodity Channel Index | -292.76 | 269.53 | 12.08 | 109.58 |
| Relative Strength Index | 18.88 | 77.38 | 51.88 | 11.48 |

Figure 7.4 – Descriptive Statistics for Technical Indicators (Exxon)

### Goldman

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0 | 100 | 58.95 | 31.28 |
| Stochastic | 2.66 | 97.83 | 59.00 | 29.43 |
| Slow Stochastic | 3.91 | 96.93 | 59.02 | 28.66 |
| Momentum | -16.99 | 17.06 | 1.76 | 7.19 |
| Rate of Change | 90.50 | 113.24 | 101.26 | 4.63 |
| William’s %R | -100 | 0 | -41.04 | 31.28 |
| A/D Oscillator | -0.95 | 2.32 | 0.54 | 0.50 |
| Disparity5 | 95.90 | 104.10 | 100.17 | 1.35 |
| Disparity10 | 93.99 | 105.86 | 100.39 | 2.06 |
| Price Oscillator | -0.03 | 0.03 | 0.0019 | 0.01 |
| Commodity Channel Index | -279.82 | 281.85 | 30.23 | 108.09 |
| Relative Strength Index | 29.11 | 80.11 | 55.30 | 11.83 |

Figure 7.5 – Descriptive Statistics for Technical Indicators (Goldman)

### IBM

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0 | 100 | 50.57 | 31.11 |
| Stochastic | 0.8 | 98.74 | 50.58 | 29.05 |
| Slow Stochastic | 2.88 | 97.78 | 50.60 | 28.19 |
| Momentum | -24.83 | 18.29 | -0.03 | 7.00 |
| Rate of Change | 88.32 | 109.26 | 100.05 | 3.63 |
| William’s %R | -100 | 0 | -49.42 | 31.11 |
| A/D Oscillator | -2.2 | 2.39 | 0.50 | 0.56 |
| Disparity5 | 92.41 | 104.29 | 99.99 | 1.19 |
| Disparity10 | 91.12 | 105.19 | 100.00 | 1.78 |
| Price Oscillator | -0.05 | 0.03 | 7e-20 | 0.01 |
| Commodity Channel Index | -497.3 | 430.24 | 1.64 | 114.40 |
| Relative Strength Index | 22.88 | 76.67 | 50.30 | 10.76 |

Figure 7.6 – Descriptive Statistics for Technical Indicators (IBM)

### JP Morgan

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0 | 100 | 60.30 | 30.73 |
| Stochastic | 4.76 | 98.15 | 60.33 | 28.54 |
| Slow Stochastic | 6.39 | 96.9 | 60.35 | 27.62 |
| Momentum | -5.64 | 6.66 | 0.50 | 2.22 |
| Rate of Change | 90.7 | 113.6 | 101.06 | 4.13 |
| William’s %R | -100 | 0 | -39.69 | 30.73 |
| A/D Oscillator | -0.9 | 2.58 | 0.54 | 0.50 |
| Disparity5 | 95.4 | 103.34 | 100.12 | 1.26 |
| Disparity10 | 93.39 | 104.91 | 100.34 | 1.94 |
| Price Oscillator | -0.04 | 0.03 | 0.001 | 0.01 |
| Commodity Channel Index | -328.71 | 246.43 | 29.14 | 106.92 |
| Relative Strength Index | 26.61 | 80.07 | 54.81 | 11.51 |

Figure 7.7 – Descriptive Statistics for Technical Indicators (JPMorgan)

### Microsoft

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 2.22 | 100 | 63.27 | 26.16 |
| Stochastic | 6.51 | 98.78 | 63.23 | 23.56 |
| Slow Stochastic | 8.12 | 97.56 | 63.22 | 22.49 |
| Momentum | -4.5 | 4.92 | 0.57 | 1.37 |
| Rate of Change | 87.56 | 117.07 | 101.70 | 3.99 |
| William’s %R | -97.78 | 0 | -36.72 | 26.16 |
| A/D Oscillator | -2.3 | 3.13 | 0.50 | 0.54 |
| Disparity5 | 89.7 | 107.41 | 100.25 | 1.51 |
| Disparity10 | 89.78 | 107.65 | 100.57 | 2.11 |
| Price Oscillator | -0.07 | 0.04 | 0.003 | 0.012 |
| Commodity Channel Index | -265.14 | 450.17 | 52.86 | 99.14 |
| Relative Strength Index | 29.47 | 79.85 | 56.80 | 9.67 |

Figure 7.8 – Descriptive Statistics for Technical Indicators (Microsoft)

### Pfizer

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0 | 100 | 56.64 | 30.10 |
| Stochastic | 4.01 | 97 | 56.62 | 27.97 |
| Slow Stochastic | 4.96 | 95.86 | 56.57 | 27.22 |
| Momentum | -2.98 | 2.51 | 0.14 | 1.04 |
| Rate of Change | 90.7 | 108.91 | 100.57 | 30.10 |
| William’s %R | -100 | 0 | -43.35 | 3.50 |
| A/D Oscillator | -1.14 | 1.9 | 0.53 | 0.46 |
| Disparity5 | 96.01 | 103.56 | 100.08 | 1.11 |
| Disparity10 | 94.57 | 104.59 | 100.18 | 1.72 |
| Price Oscillator | -0.04 | 0.02 | 0.0006 | 0.009 |
| Commodity Channel Index | -307.87 | 310.55 | 27.52 | 110.72 |
| Relative Strength Index | 25.32 | 80.83 | 52.88 | 10.90 |

Figure 7.9 – Descriptive Statistics for Technical Indicators (Pfizer)

### Visa

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Technical Indicator | Min | Max | Mean | Standard Deviation |
| Stochastic | 0 | 100 | 57.95 | 29.14 |
| Stochastic | 4.62 | 97.92 | 58.06 | 26.30 |
| Slow Stochastic | 5.59 | 96.41 | 58.15 | 25.28 |
| Momentum | -21.81 | 21.81 | 1.91 | 7.57 |
| Rate of Change | 112.32 | 112.32 | 101.14 | 3.97 |
| William’s %R | -100 | 0 | -42.04 | 29.14 |
| A/D Oscillator | 2.17 | 2.17 | 0.55 | 0.50 |
| Disparity5 | 104.71 | 104.71 | 100.15 | 1.30 |
| Disparity10 | 106.26 | 106.26 | 100.36 | 1.91 |
| Price Oscillator | -0.03 | 0.03 | 0.0017 | 0.01 |
| Commodity Channel Index | -300.54 | 334.46 | 30.89 | 108.34 |
| Relative Strength Index | 26.45 | 77.62 | 54.74 | 9.84 |

Figure 7.10 – Descriptive Statistics for Technical Indicators (Visa)

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1. Definition acquired from: *en.wikipedia.org/wiki/Sentiment\_analysis* [↑](#footnote-ref-2)
2. Wikipedia (*en.wikipedia.org/wiki/Text\_corpus*) defines a corpus as a large and structured set of texts. [↑](#footnote-ref-3)
3. The Stanford Natural Language Processing Group provide a copy of their tagger at nlp.standford.edu/softwaretagger.shtml [↑](#footnote-ref-4)
4. Name entities are similar to proper nouns but refer to specific entities. Dates, organisations, places or numerical data can serve as name entities. [↑](#footnote-ref-5)
5. Common stop words in the English Language at www.textfixer.com/resources/common-english-words.txt [↑](#footnote-ref-6)
6. Binary classification involves the training of a model to differentiate between only two classes. [↑](#footnote-ref-7)
7. Bullish market periods are periods in a financial time series in which prices are on the rise. [↑](#footnote-ref-8)
8. Bearish market periods are periods in a financial time series in which prices are on the fall. [↑](#footnote-ref-9)