

## 6. Predictions and Machine Learning

- We have seen in chapter 2 that regressions are a powerful tool to approximate the Conditional Expectation Function  $E[Y_i|X_i]$
- But: In a regression we impose assumptions on the functional form of the CEF
- For instance: When we estimate a model

$$Y_i = \alpha + \beta_1 \cdot X_{i1} + \beta_2 \cdot X_{i2} + \varepsilon_i$$

we approximate the CEF with a linear function

- We can estimate much more complex functions and can for instance add interaction terms, quadratic terms etc...
  - ... but this will always be assumptions that we impose
  - ... & we cannot be sure about the true functional form of the CEF
- Here: Use more general machine learning techniques to estimate the CEF relaxing assumptions about its functional form

# Regression and Classification

- In „machine learning speak“ people distinguish between regression and classification
- In this terminology:
  - Regression means solving a prediction problem where the dependent variable is a continuous variable (a quantity like age, income, job satisfaction,...)
  - Classification means solving a prediction problem where the dependent variable is a discrete variable (a “label“ or a “class“ such as employee turnover (yes/no), , ...)
- Here we will only cover regression problems
- Classification methods are often very similar (and sometimes you can also apply a regression method for binary classification problems)

## Recall: Basic Properties of the CEF

### Result: CEF Prediction Property

Let  $m(X_i)$  be any function of  $X_i$ . The CEF solves

$$E[Y_i|X_i] = \arg \min_{m(X_i)} E[(Y_i - m(X_i))^2]$$

so it is the best predictor of  $Y_i$  given  $X_i$  in the sense that it solves the minimum mean square error (MMSE) prediction problem.

### Result: CEF Decomposition Property

We can decompose  $Y_i$  such that  $Y_i = E[Y_i|X_i] + \varepsilon_i$

(i) where  $\varepsilon_i$  is mean independent of  $X_i$  that is  $E[\varepsilon_i|X_i] = 0$

(ii) and therefore  $\varepsilon_i$  is uncorrelated with any function of  $X_i$

# Supervised Learning

- The part of ML we are interested in is **supervised learning** as the task of learning a function  $\hat{f}(X)$  (“training an algorithm”) that maps an input  $X$  to an output  $Y$  based on a sample
- The learning method learns from a training sample consisting of a set of input-output observations
- Hence, we have (as before) a data set  $D$  with  $N$  observations and  $M$  explanatory variables

$$(y_1, x_{11}, x_{12}, x_{13}, \dots, x_{1M}), \\ (y_2, x_{21}, x_{22}, x_{23}, \dots, x_{2M}), \dots$$

- In ML the vector  $x_i$  of explanatory variables is called the **feature vector** and the matrix  $X$  of the feature vectors of all observations the **feature matrix**
- We want to estimate a function  $\hat{f}_D(X)$  that approximates the CEF

# Parametric and Non-Parametric Approaches

- An OLS Regression is a specific **parametric** ML algorithm
  - Easy to fit as only few parameters need to be estimated
  - Easy to interpret
- But:
  - Makes strong assumptions on functional form
  - May perform poorly in prediction task when underlying CEF is non-linear and when the number of independent variables is large
- Other **non-parametric** Algorithms may then be more flexible:
  - Do not assume a specific functional form
  - Are thus more flexible to adapt to complex forms of the CEF
  - But are harder to interpret and may perform worse on small data sets

# k-Nearest Neighbor Regression

## Key idea:

- For a given value  $x_i$  we could approximate the CEF  $E[Y_i|X_i = x_i]$  by computing the average of  $Y_i$  across observations with  $X_i = x_i$

**Problem:** We might have very few or no other observations with  $X_i = x_i$

- Instead, use the average value of  $Y_i$  of the  $k$  nearest neighbors of  $x_i$ :

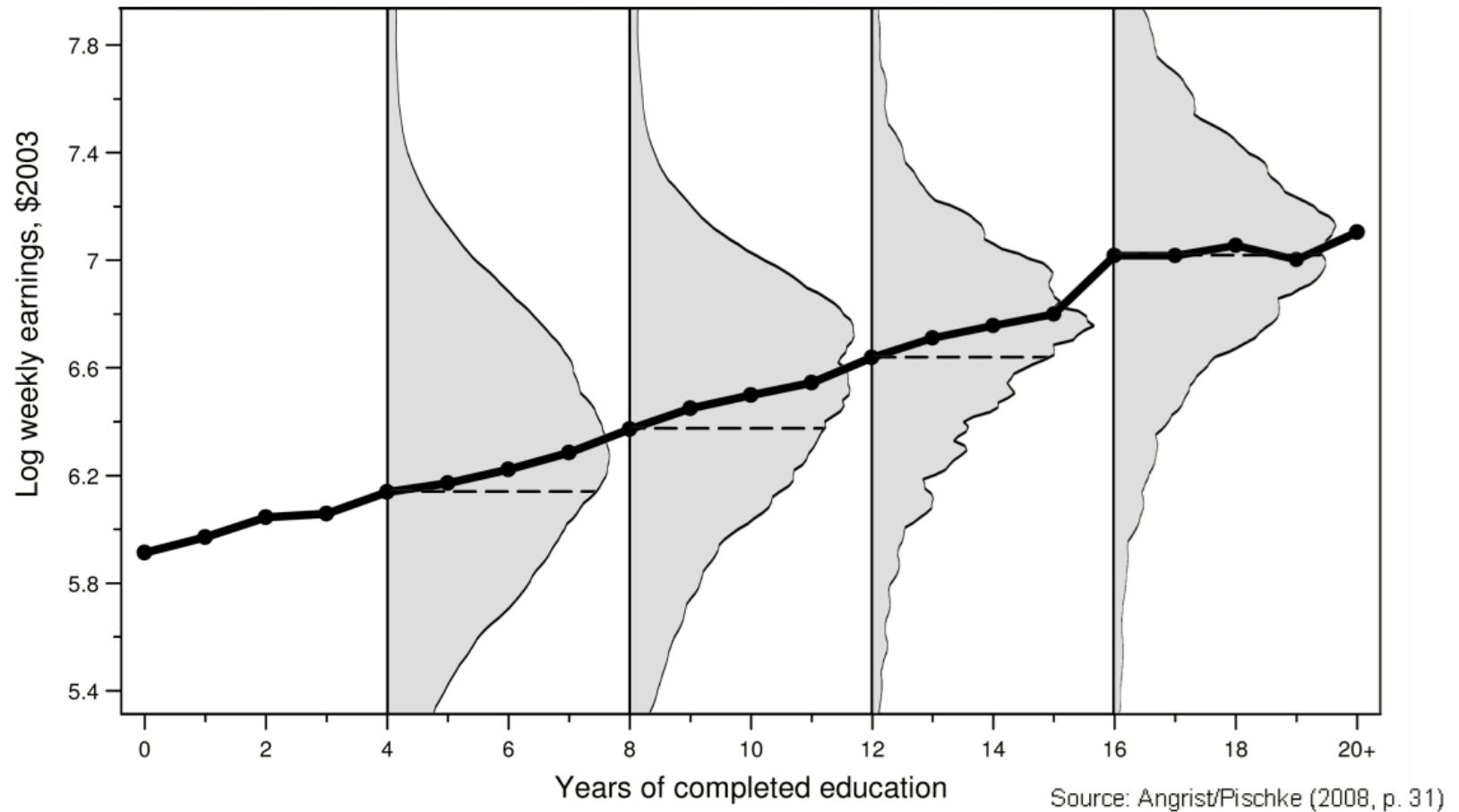
$$\hat{f}_D(x_0) = \frac{1}{K} \sum_{j \in N_k(x_0)} y_j$$

where  $N_k(x)$  is a neighborhood containing the indices of the  $K$  closest  $x$  values in the training data

- Closest neighbors for instance those with smallest Euclidean distance

$$\sqrt{\sum_{j=1}^M (x_{0j} - x_{1j})^2}$$

## Recall: The CEF of earnings as a function of years of education



# k-Nearest Neighbor Regression: Standardization

## Note:

- When the  $x_i$  vector consists of multiple variables measured in different units the measured distance will depend on the unit of measurement
  - If there is, for instance, a wage variable the chosen currency unit will affect the assignment of neighbors
  - Or, if there is a tenure variable measuring the time an employee has been with a firm it will matter whether it is measured in months or years
  - In other words: variables where there are large nominal distances will have stronger effects on “who is an observation’s neighbor”

## Hence:

- When the  $x_i$  vector consists of multiple variables measured in different units, then it is useful to standardize all independent variables/features

$$x_{ij}^{std} = \frac{x_{ij} - \bar{x}_j}{std(x_j)}$$

where  $\bar{x}_j$  is the mean of the variable and  $std(x_j)$  its standard deviation



# The Loss Function and Mean Squared Error

An important concept in ML is the **loss function**

$$L(Y_i, \hat{f}_D(X_i))$$

- The loss function measures the “loss” of approximating  $Y_i$  by  $\hat{f}(X_i, D)$
- Common choice: Squared error

$$L(Y_i, \hat{f}_D(X_i)) = (Y_i - \hat{f}_D(X_i))^2$$

## Central Goal:

Find an algorithm  $\hat{f}_D(X_i)$  that minimizes the expected loss

## Recall:

- When estimating a linear regression we did exactly that, being restricted to the class of linear functions
- In ML more general and flexible functional forms are often considered (sometimes at the expense of interpretability)

# The Loss Function and Mean Squared Error

**Hence:**

- When assessing the predictive performance of an algorithm for a regression problem (i.e. one with a continuous outcome variable), we often use the **mean squared error (MSE)**
- That is, we use the data set (or part of it) to compute the squared deviation between actual values of  $y$  and predicted values  $\hat{y}$

$$MSE = \frac{1}{N} \sum_{i=1}^N \left( y_i - \hat{f}_D(x_i) \right)^2$$

- This can, for instance, be used to compare the performance of different algorithms

# Mean Squared Error and $R^2$

**Note: The Mean Squared Error is directly connected to  $R^2$**

- The coefficient of determination  $R^2$  is the proportion of the variance in the dependent variable that is predictable from the independent variables
- It is given by

$$R^2 = 1 - \frac{\frac{1}{N} \sum_{i=1}^N (y_i - \hat{f}_D(x_i))^2}{\frac{1}{N} \sum_{i=1}^N (y_i - \bar{y})^2}$$

where  $\bar{y} = \frac{1}{N} \sum_{i=1}^N y_i$  is the mean of the  $y_i$

- Hence

$$R^2 = 1 - \frac{MSE}{V[y_i]}$$

- As the variance of the dependent variable  $V[y_i]$  is given, minimizing the MSE corresponds to maximizing the  $R^2$

- Typically, you start a project by inspecting the data, cleaning it, and preparing it for the analysis
- To do so you first pick two subsets of the variables in your data frame:
  - A (one dimensional) array containing the dependent variable to be predicted, which you typically name  $y$
  - A two dimensional array or data frame containing the explanatory variables (features) of each observation, which you typically name  $X$
- For instance, you can define `y=df['JobSatis']`
- To define the feature matrix  $X$ , for instance
  - include all other variables: `X=df.drop(columns='JobSatis')`
  - or include a subset of the variables: `X=df[['age','wage']]`
- Sometimes there are missing values shown in a data frame as NaN
  - Rows with NaN can be dropped using `df = df.dropna()`

- Key ML methods are implemented in package scikit-learn
- Starting point: we can also run a linear regression
- Import:

```
from sklearn.linear_model import LinearRegression
```

- Then we can perform a regression with the following code:

```
lreg = LinearRegression().fit(X, y)
```

- $X$  is a (two dimensional) array containing the explanatory variables (features) of each observation
  - $y$  is a (one dimensional) array containing the dependent variable to be predicted
- We can then use the results to make predictions  

```
lreg.predict([[50]])
```

 predicts the  $y$  for  $X = 50$
- Note: As Sci-kit Learn rather aims at making predictions, we do not easily get nice regression tables. To obtain these rather use `statsmodels`

- To fit a k-Nearest Neighbor Regression import:

```
from sklearn.neighbors import KNeighborsRegressor
```

- Then we can perform a knn regression with the following code:

```
knn=KNeighborsRegressor(n_neighbors=8).fit(X, y)
```

- where  $X$  is again the feature matrix and  $y$  the variable to be predicted
- `n_neighbors` specifies the number of neighbors considered

- The method `mean_squared_error` computes the MSE:

```
from sklearn.metrics import mean_squared_error
```

```
y_pred = knn.predict(X)
```

```
print(mean_squared_error(y, y_pred))
```

- The method `r2_score` computes the  $R^2$ :

```
from sklearn.metrics import r2_score
```

```
print(r2_score(y, y_pred))
```

## Your Task

## Predicting performance

- The dataset `data_performance.csv` contain data on employees in a call center of a Chinese travel agency (taken from Bloom et al. (2015))
- Your task is to train an algorithm to predict the performance of these call center workers
- The variable `z_performance` is a standardized performance measure, which is based on employee performance on their main task (e.g. phone calls answered, calls answered per minute, weekly minutes on the phone)
- Import the data from  
`https://raw.githubusercontent.com/dsliwka/EEMP2022/main/datasets/data\_performance.csv`
- Please first inspect the data and look at the variables (`df.columns`)
- Plot a histogram of the performance variable with `sns.histplot`

- Then prepare the data:
  - Drop all rows with missing values
  - Define your  $y$  vector `y = . .`
  - Define your feature matrix `X = . .` omitting the dependent variable as well as the variable `personid`
- Then perform a k-Nearest Neighbor Regression to predict `z_performance` with  $k = 5$  neighbors
- Compute the mean squared error and the  $R^2$  of this prediction
- Note: You can also compute the  $R^2$  “manually” by computing the variance of the dependent variable `y` with `y.var()`
- Save the notebook as `PerformancePrediction`



# Hyperparameters

- **Parameters** are learned by the algorithm during training (like regression coefficients)
- **Hyperparameters** refers to something that is passed to the algorithm, i.e. is set by the user and determines how the algorithm works
  - The number of neighbors to inspect in a KNN model is a hyperparameter that we have to specify when we create the model
- We can compare the prediction accuracy of a model to determine the best values for the hyperparameters
- In order to understand this further we will consider:
  - The problem of overfitting
  - The importance of separating training and test data
  - The bias-variance trade-off

# Overfitting, Training Error, and Test Error

**Recall:** Quality of the prediction often assessed by *mean squared error* (MSE):

$$MSE = \frac{1}{N} \sum_{i=1}^N \left( y_i - \hat{f}_D(x_i) \right)^2$$

**A key problem:**

- When the estimated functional form is very flexible, we will overestimate the predictive power of our algorithm when computing the MSE on the **same data** which we used to train the algorithm

**This is due to *Overfitting*:**

- The function  $\hat{f}_D(X)$  estimated on a sample  $D$  will tend to follow patterns too closely that by chance occur in  $D$  rather than the whole population!
- When overfitting plays a big role, then  $\hat{f}_D(X)$  will be a bad predictor for observations that are not part of the training sample  $D$

# Overfitting, Training Error, and Test Error

## Key element of ML:

- Assess the prediction quality **out-of-sample!**
- In order to do so: Use only a subset of the data to train the algorithm
- Use the remainder to assess the quality of the prediction

## Important distinction: Training error and test error

- *Training error*: Average of loss function over the *training data*  $D_{train}$

$$\overline{err}_{train} = \frac{1}{|D_{train}|} \sum_{j \in D_{train}} L(y_j, \hat{f}_{D_{train}}(x_j))$$

- *Test error/generalization error*: Average loss when applying  $\hat{f}_{D_{train}}(X)$  for observations that are not part of the training data

$$\overline{err}_{test} = \frac{1}{|D_{test}|} \sum_{j \in D_{test}} L(y_j, \hat{f}_{D_{train}}(x_j))$$

- First import:

```
from sklearn.model_selection import train_test_split
```

- The method `train_test_split` conveniently splits the data set into training and test data:

```
X_train, X_test, y_train, y_test  
= train_test_split(X, y, train_size=0.7, random_state=181)
```

### Note:

- The `train_size` parameter determines the share of observations used for the training data set, the remaining observations are the test set
- The method returns four arrays: `X_train` and `X_test` are the feature matrices for the observations in the train and test sets
- `y_train` and `y_test` are the outcome variables in the two data sets
- As the data sets are randomly sampled you will get a different sample each time → fix the sampling with the parameter `random_state=181`

- We can then train the algorithm on our test data:

```
knn = KNeighborsRegressor(n_neighbors=10).fit(X_train,  
                                             y_train)
```

- Recall: The method `mean_squared_error` computes the MSE:

```
from sklearn.metrics import mean_squared_error
```

- Print the training mean squared error:

```
print(mean_squared_error(y_train,  
                         knn.predict(X_train)))
```

- Print the test mean squared error:

```
print(mean_squared_error(y_test, knn.predict(X_test)))
```

## Your Task

### Predicting performance

- Open again your notebook `PerformancePrediction`
- Now split the data in a training and a test set where the test set should comprise 70% of the observations and set the `random_state=181`
- Train the knn Algorithm on the training set
- Compute the mean squared error and  $R^2$ 
  - on the training set and
  - on the test set
- Interpret your findings. Did we obtain a good prediction?
- Save the notebook

- We have seen in section 1 of the course how to “manually” standardize variables (subtracting the mean and dividing by the standard deviation)
- Scikit-Learn provides a convenient way to standardize all variables in  $X$   

```
from sklearn.preprocessing import StandardScaler  
scaler=StandardScaler()  
scaler.fit(X_train)  
X_trainS=scaler.transform(X_train)  
X_testS=scaler.transform(X_test)
```
- Then  $X\_trainS$  and  $X\_testS$  are standardized versions of  $X\_train$  and  $X\_test$
- The standardization is done with the mean and standard deviation of the respective variables in the training set

## Your Task

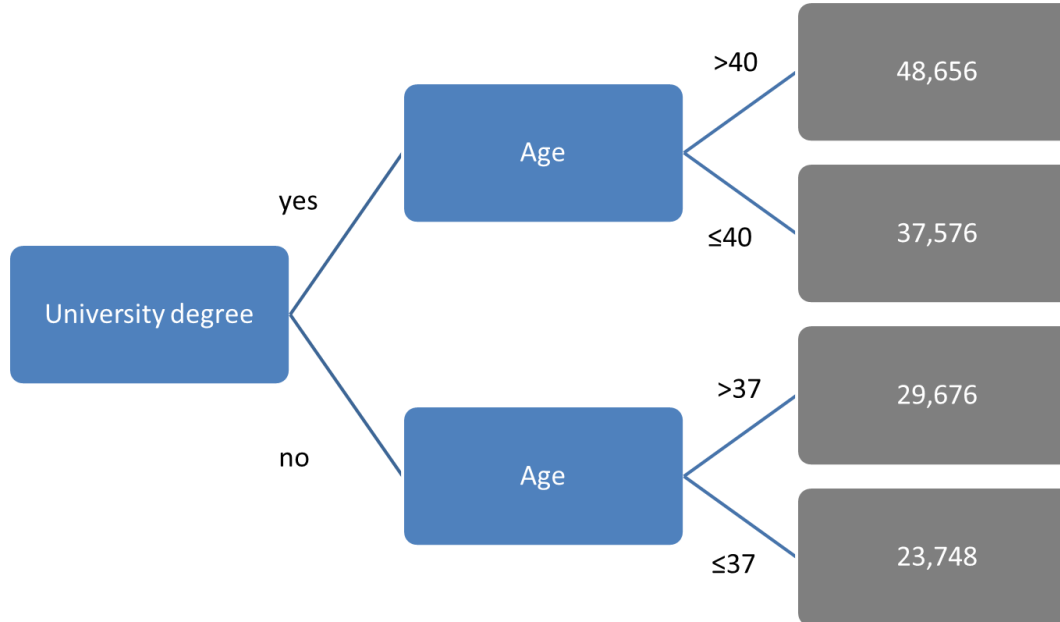
### Predicting performance

- Open the `PerformancePrediction` notebook
- Now standardize the variables in the feature matrix  $X$  with the `StandardScaler`
- Then perform a k-Nearest Neighbor Regression to predict `z_performance` with  $k = 5$  neighbors training the algorithm on the standardized data
- Again, compute the test mean squared error and the  $R^2$  of this prediction
- Save the notebook



# Decision Trees

- Decision trees are the building block of powerful ML algorithms
- The key idea of a decision tree is simple:
  - Sequentially partition the data
  - At each step generate two subsets
  - Base the split in each step on a specific condition on one variable
  - Choose the splits by minimizing the expected loss (MSE)



# Decision Trees: How it works

## Top-down, greedy approach known as *recursive binary splitting*

(Compare James/Witten/Hastie/Tibshirani (2022, pp. 327)

- Begin at the top of the tree & successively split the predictor space
- Each split generates two new branches
- Called “greedy” because at each step, the best split is made at that particular step (rather than looking ahead)
- To perform recursive binary splitting,
  - select a feature  $j$  and cutpoint  $s$  such that splitting the predictor space into the “regions”  $\{X|X_j < s\}$  and  $\{X|X_j \geq s\}$  leads to the smallest loss
  - repeat the process, looking within each region generated in the previous step for the best predictor and cutpoint minimizing the loss within the respective region
  - ...

# Decision Trees: How it works

## More formally, at each step:

- For each branch look at the set of observations in this branch
- Within this set, define two subsets for feature  $j$  and cutpoint  $s$

$$R_1(j, s) = \{X | X_j < s\} \text{ and } R_2(j, s) = \{X | X_j \geq s\}$$

- Let  $\hat{y}_{R_k}$  be the average value of  $y_i$  across all observations in  $R_k(j, s)$

Note: This  $\hat{y}_{R_k}$  is the *predicted value* for this region

- Seek the values of  $j$  and  $s$  that minimize

$$\sum_{i:i \in R_1(j,s)} (y_i - \hat{y}_{R_1})^2 + \sum_{i:i \in R_2(j,s)} (y_i - \hat{y}_{R_2})^2$$

- Repeat the steps until a certain (predetermined) depth of the tree is attained
- The depth of the tree is a hyperparameter to be tuned

- To fit a decision tree import:

```
from sklearn.tree import DecisionTreeRegressor
```

- Then we can fit the tree with:

```
dtree = DecisionTreeRegressor(max_depth=3) .  
      fit(X_train, y_train)
```

- where `max_depth` is a hyperparameter that gives the maximal depth of the tree (the number of layers)
  - Note: Restricting `max_depth` prevents overfitting as a tree without a maximum depth will simply map out the whole data set
- Another hyperparameter is `min_samples_leaf` specifying a minimal number of observation that have to be in each leaf

- For a (not too large) tree it is convenient to plot the tree

```
from sklearn.tree import plot_tree
```

- To set the plot size

```
plt.figure(figsize=(20, 10))
```

- Plot the tree and show it

```
plot_tree(dtree, feature_names=X.columns,  
          fontsize =10)  
plt.show()
```

- Note:

- `feature_names` is a parameter with which you specify the names of the features to be displayed
- `X.columns` gives back a list of the variable names in the dataframe containing the features

## Your Task

## Predicting performance

- Open again your notebook `PerformancePrediction` and save it under a different name `PerformancePredictionTree`
- Now instead of the Knn regression train a decision tree with a maximum depth of 3 (note: here you do not need to standardize the X matrix)
- Plot the tree and interpret your findings
- Compute the mean squared error and  $R^2$ 
  - on the training set and
  - on the test set
- Save the notebook

# Optimizing Prediction Quality

- But one can go beyond merely assessing the quality of an algorithm by measuring the accuracy of the prediction out-of-sample
- We should aim at finding a specification (i.e. a version of the algorithm) that yields the best out-of-sample prediction
- That is, for instance, find the specification that yields the lowest MSE when applied to new data
- To do so, it is useful to consider **different splits of the data** into training and test data
- An algorithm performs well when it consistently produces good out-of-sample predictions across different splits
- This can be done using so-called *cross validation*

# Cross-Validation

**K-fold Cross Validation:** Split multiple times and compute the average test error

- First split data into K roughly equal-sized folds (subsets)  $D_1, D_2, \dots, D_K$
- Repeat for  $k = 1, 2, \dots, K$ :
  - For k-th fold, train the model on data from all other folds, i.e.  $D \setminus D_k$
  - Calculate prediction error on  $D_k$  to obtain  $MSE_k$

$$MSE_k = \frac{1}{|D_k|} \sum_{j \in D_k} L(y_j, \hat{f}_{D \setminus D_k}(x_j))$$

- Compute the average prediction error

$$MSE^{K-fold} = \frac{1}{K} \sum_{k=1}^K MSE_k$$

- Then again pick the specification of an algorithm that minimizes  $MSE^{K-fold}$
- It is common to use k=5 or k=10



# Tuning Hyperparameters

- Often, we consider models with hyperparameters  $\alpha$  such as the number of neighbors in KNN regression or the depth of a tree
- We train an algorithm for a specific hyperparameter  $\alpha$  (or vector of hyperparameters if there are more than one)
- Key question: But what are the “best” values for the hyperparameters?

Again: Find the hyperparameters that minimize expected loss **out-of-sample**

- Let  $\hat{f}_D(X, \alpha)$  be the algorithm trained with hyperparameters  $\alpha$
- We can now estimate the K-Fold cross validation (CV) mean squared error

$$MSE^{K-fold}(\hat{f}, \alpha)$$

- And then choose the value of  $\alpha$  that minimizes this
- Note: Some also advocate the random standard error rule: Pick the least complex model that is in a range of one standard error from the best model

- Scikit-Learn provides a convenient tool to perform cross validation:

```
from sklearn.model_selection import cross_val_score
```

- Then perform K-fold cross-validation:

```
cv = cross_val_score(knn, X_train, y_train, cv=5,  
                     scoring='neg_mean_squared_error')
```

- Returns an array of  $k$  (here 5) estimates for the generalization error (one for each of the  $k$  folds)
- We can just look at the mean of these with `cv.mean()`
- To find (near) optimal values of the hyperparameters:
  - We can write a python loop to vary  $k$  and look for the value of  $k$  that minimizes the CV mean squared error
  - But Scikit-Learn can also do that automatically with grid search

- Scikit-Learn also provides a class for automatic hyperparameter tuning  
`from sklearn.model_selection import GridSearchCV`
- You only have to specify the model that you want to apply it to and the range of parameter values which you want to check
- To define the set of parameter values (here 1 to 5) to be checked define a python dictionary (can also be multiple parameters)

```
param_grid = {'n_neighbors' : [1,2,3,4,5]}
```

- Then create a grid search object

```
knn_grid= GridSearchCV(KNeighborsRegressor(),  
                        param_grid, cv=5, scoring='neg_mean_squared_error')
```

- Now run the fit method of this object like you did before on knn:

```
knn_grid.fit(X_train, y_train)
```

- And then for instance get the value of  $k$  that maximizes accuracy

```
print(knn_grid.best_params_)
```

- The grid search object also has a method to make predictions based on the optimized set of parameters:

```
knn_grid.predict(X_test)
```

- You can use this to compute the test error and the test  $R^2$

```
mean_squared_error(y_test, knn_grid.predict(X_test))
```

```
r2_score(y_test, knn_grid.predict(X_test))
```

Note furthermore:

- The `GridSearchCV` object has an attribute `cv_results_` which allows to access the evaluation metrics in more detail
- For instance, `knn_grid.cv_results_['mean_test_score']` is an array containing the mean squared error (when this is the specified scoring method) for all parameter combinations that were checked

## Your Task

## Predicting performance

- Open again your notebook `PerformancePrediction`
- Now try to find the optimal number of neighbors in the Knn regression (note: again use the standardized X matrix)
- Perform a grid search defining a parameter grid  

```
param_grid={'n_neighbors': np.arange(2, 20)}
```

  - Note: `np.arange(3, 20)` returns an array of values between 3 and 20 with steps of 1
  - (You could also specify larger steps with a third parameter such as `np.arange(2, 20, 2)`)
- What is the optimal number of neighbors?
- Compute the test mean squared error and  $R^2$
- Save the notebook

# Model Complexity/Flexibility

A model/algorithm is said to be more **complex** or **flexible** when it has more parameters and thus can more easily adapt to patterns in the data

- A multiple linear regression is, for instance, more complex
  - when it has more explanatory variables and more interaction terms
  - or when it includes polynomial terms
- A knn-regression is more flexible when the number of neighbors is smaller
  - it then can adapt more flexibly to patterns in the near neighborhood
- A decision tree is more flexible when it has higher depth...

## Note:

- A more flexible model is more likely to be able to come close to the true CEF
- But: A more flexible model is also more likely to pick up patterns in the data that are simply due to the specific sampling of the training data
- This consideration leads to an important trade-off between **bias** and **variance**

# Bias

- Recall: When  $f(X_0)$  is the true CEF then  $Y_0 = f(X_0) + \epsilon$
- Define: An algorithm  $\hat{f}$ 's **bias** at a specific vector of feature values  $X_0$

$$\text{bias}(\hat{f}(X_0)) = E_D[\hat{f}_D(X_0)] - f(X_0)$$

- Key idea:
  - Suppose we have different training data sets  $D$
  - For each training data set we train a specific algorithm to obtain  $\hat{f}_D(X_0)$
  - The bias is the difference between the average prediction made by the algorithm across different samples and the true CEF  $f(X_0)$
- It is preferable to have a low bias!
  - Then there is no systematic difference between our predictions based on certain training data sets and the true CEF

# Variance

- Consider again the use of different training data sets  $D$
- Again each training data set yields (in general) a different prediction  $\hat{f}_D(X_0)$
- Key question: How much do these estimates vary?
- This estimation **variance** at  $X_0$  is

$$variance\left(\hat{f}(X_0)\right) = E\left[\left(\hat{f}_D(X_0) - E[\hat{f}_D(X_0)]\right)^2\right]$$

- It is the mean squared deviation between predictions made by the same algorithm when trained with different training data sets  $D$
- It is preferable to have a low variance!
  - Then the predictions are rather consistent. That is, if the algorithm is trained on different training data sets, it makes similar predictions for the same feature vector  $X_0$



# The Bias-Variance Decomposition

- Suppose now that we draw an observation  $(Y_0, X_0)$  from the *test data set*
- Expected mean squared error

$$E \left[ \left( Y_0 - \hat{f}_D(X_0) \right)^2 \right] = E \left[ \left( f(X_0) + \epsilon - \hat{f}_D(X_0) \right)^2 \right]$$

- One can show that this is equal to

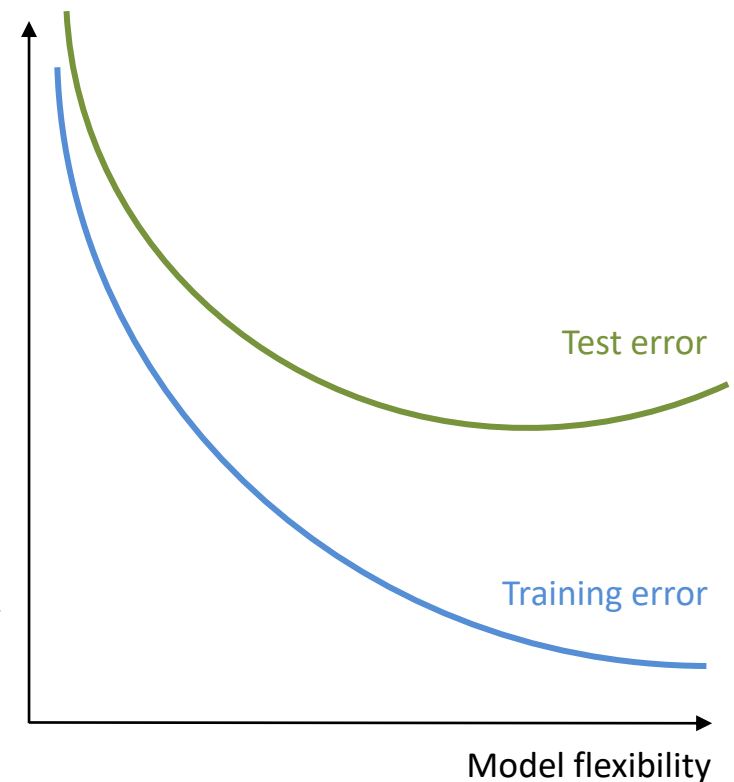
$$V[\epsilon] + \left( E[\hat{f}_D(X_0)] - f(X_0) \right)^2 + E \left[ \left( \hat{f}_D(X_0) - E[\hat{f}_D(X_0)] \right)^2 \right]$$

where

- $V[\epsilon]$  is the *irreducible error*
- $E[\hat{f}_D(X_0)] - f(X_0)$  is the *bias* of the algorithm
- $E \left[ \hat{f}_D(X_0) - E[\hat{f}_D(X_0)] \right]$  is the *variance* of the algorithm

# The Bias-Variance Trade-off

- When increasing the flexibility of a model the training error is reduced  
→ a more flexible model can pick up more detailed patterns
- Initially the test/validation error tends to fall as well
  - as otherwise the model is too simple/inflexible
  - here the **bias** is reduced when adding complexity
- But when the complexity increases further, the test error will tend to increase again
  - Here the **variance** increases
  - Model becomes so flexible that it will map random patterns in training data
  - A very complex model will “memorize” the training data & thus **overfit**



# Ensemble Learning and Random Forests

- Decision trees are relatively easy to understand and interpret
- But they tend to suffer from high variance (in particular with high depth):
  - When splitting the training data into two parts & fitting a decision tree to both halves, the results could be quite different
  - In other words, deep trees tend to overfit the data
- But it has turned out that training different trees on the same data set and averaging their predictions improves prediction accuracy
- This is the broader idea of **ensemble** methods in ML: Use multiple learning algorithms and average their predictions to obtain a higher accuracy
- An important and powerful such ensemble method is a **Random Forest**:
  - Train many decision trees & use the average prediction
  - Each single tree will have a high variance, but allows for low bias
  - Averaging across trees will reduce variance

# Ensemble Learning and Random Forests

## Important:

- If the different trees are very similar, the improvement will be small as they will make similar predictions
- Hence a random forest introduces intentional randomness in the construction of each tree (therefore the name!)

## Random forests introduce two forms of randomness:

1. For each tree use a different random sample of the data
  - Apply so-called **bootstrap aggregation (bagging)**
  - That is, for each tree draw a sample of the same size as the original data set (with replacement such that an observation can be drawn twice)
  - Train the tree on this sample
2. For each node in a tree consider only a **randomly chosen subset of the features** as candidates to use for the next split

## Bootstrap: Example

Original Sample:			Bootstrap Sample:	
1	Anna		3	Peter
2	Mehmet		10	Rosa
3	Peter		9	Herbert
4	Chloé		4	Chloé
5	Marie		1	Anna
6	Huan		8	Pedro
7	Robert		1	Anna
8	Pedro		3	Peter
9	Herbert		6	Huan
10	Rosa		5	Marie

# Random Forests: Bagging

## Bagging:

(James/Witten/Hastie/Tibshirani (2022, pp. 340))

- Draw  $b = 1, \dots, B$  different “bootstrap samples” of the same size  $N$  as the original sample
  - That is, for each sample draw  $N$  times an observation from the original sample (with replacement – an observation in the original sample can show up several times in the bootstrap sample!)
  - For each sample  $b$  train your algorithm (here: the decision tree) to obtain a predictor  $\hat{f}_b(x)$
- Key idea: Data sets are different but they are drawn from the same distribution as the original data so share the underlying characteristics
- The bagging prediction is then simply

$$\hat{f}_{bag}(x) = \frac{1}{B} \sum_{b=1}^B \hat{f}_b(x)$$

# Random Forest: Using Subsets of Features at each Split

Underlying reasoning for using only a **subset of the features**:

- Improve the prediction by avoiding that the different trees are too similar
- For instance, when some predictors are very important, the splits at the top of each tree will be very similar (even with bagging)
- But when the trees are similar, their predictions will be highly correlated and then less can be learned from aggregating their results
- Note: splits lower down in the tree have less data and thus are more prone to be affected by noise

**The approach:**

- At each node of the tree allow only a subset of the features to be used for the next split
- This subset is determined by a random draw
- The idea is to “decorrelate” the trees or to force them to learn where it is more difficult to learn

# Random Forest: Using Subsets of Features at each Split

- Subset of features that may be used for a split randomly drawn at each node
- The size of this subset has to be set as a hyperparameter
- If there are  $M$  features and this maximal number of features is set to  $P$ :
  - At each node the random forest algorithm randomly randomly picks  $P$  out of the  $M$  features
  - The algorithm then seeks the best split (as usual when estimating a decision tree) but only within this subset of features
- Note:
  - When  $P = N$  then each split can look at all features in the data set and randomness only comes from bootstrapping (“bagging estimator”)
  - When  $P = 1$  then each split could only use one randomly picked feature
- Recommendation: When there are  $M$  features, allow  $P = \sqrt{M}$  features (randomly picked at each node) to be used for the next split




- To fit a decision tree import:

```
from sklearn.ensemble import RandomForestRegressor
```

- Then we can fit the random forest with:

```
forest = RandomForestRegressor(n_estimators=10) .  
        fit(X_train, y_train)
```

where `n_estimators` sets the number of trees to be estimated

- Another hyperparameter is `max_features` specifying the number of features randomly drawn at each split that can be used for this split, where
  - you can either set a specific number such as `max_features=4`, or
  - do a grid search with `GridSearchCV`, or 
  - follow the convention to use the square root of  $M$  by specifying `max_features='sqrt'`
- You may also set (& tune) the tree hyperparameters such as `max_depth`

## Your Task

## Predicting performance

- Open again your notebook `PerformancePredictionTree`
- Now train a random forest
  - Set `max_features="sqrt"`
  - Set the number of estimators to 500 and the random state to 181
- Compute the test mean squared error and test  $R^2$
- Save the notebook as `PerformancePredictionForest`

# Feature Importance

- We use ML methods to make predictions but often we also want to understand how these predictions work
- For some methods like linear regressions or (shallow) decision trees that is quite easy
- For others (in particular when there are many features) it is more difficult and the algorithm remains a “black box”
- One important tool to open the black box to some extent: Approaches to estimate the importance of the different features for the prediction
- Different ML algorithms have different methods to assess feature importance
- Here: Show one method that work across all algorithms:  
**Permutation feature importance**

# Permutation Feature Importance

- Estimate the mean squared error of your prediction  $MSE(\hat{f}_D, X_{test})$
- For each feature  $j$ : Repeat  $K$  times
  1. Generate feature matrix  $X_{testPerm,jk}$  by randomly permuting feature  $j$ 
    - That is: just randomly shuffle the values, for instance by splitting the data set in pairs and exchanging the values of the pairs
    - Then this feature is completely uninformative
  2. Estimate the error based on the predictions of the permuted data, i.e.  $MSE(\hat{f}_D, X_{testPerm,jk})$
- Calculate permutation feature importance of feature  $j$  as

$$i_j = \frac{1}{K} \sum_{k=1}^K MSE(\hat{f}_D, X_{testPerm,jk}) - MSE(\hat{f}_D, X_{test})$$

- That is: How much does the error increase when I make the feature completely uninformative

- Import feature importance class:

```
from sklearn.inspection import permutation_importance
```

- Then perform estimation of feature importance

```
perm_importance = permutation_importance(model,  
                                         X_test, y_test, n_repeats=30, random_state=0)
```

- For `model` insert the name of the fitted estimator
- `n_repeats` specifies the number of permutations performed

- We obtain the feature importances from

```
perm_importance.importances_mean
```

- We can plot the feature importances in a bar chart:

```
pd.Series(perm_importance.importances_mean,  
          index=X_train.columns).plot(kind='barh')
```

- `index=X_train.columns` determines that the bars get the names of the columns in the DataFrame `X_train`

# Partial Dependence Plots

- From the feature importance we learn about the importance for the feature for the prediction
- But we do not learn **how** a feature matters, for instance
  - is there a positive, negative, or non-monotonic association?
  - what is the magnitude of the respective slope of the CEF?
- To inspect this, we can use **partial dependence plots**
  - Pick a feature to be inspected
  - For different potential values of the feature make a prediction for  $y$  holding all other features constant
  - Plot these predictions
- Note: The plots only has a clean ceteris paribus interpretation if the feature in question is uncorrelated with all other features

- Import feature importance class:

```
from sklearn.inspection import PartialDependenceDisplay
```

- Then plot the partial dependence

```
PartialDependenceDisplay.from_estimator(model,  
                                       X, ['X_1', 'X_2'])
```

where

- `model` is the fitted estimator
- `X` is the feature matrix
- `['X_1', 'X_2']` is a list of the features for which you want to plot the partial dependence

# Conclusion

## Aim of the course:

- Familiarize you with different empirical methods
- Let you apply these methods to gain practical skills in using Python to work with data

## Key messages:

- Linear regressions are a powerful tool to approximate conditional expectations with easily interpretable linear functions
- Other machine learning methods may provide more flexible functional forms but sometimes at the expense of interpretability
- Important to distinguish between the different key objectives (i) to make predictions and (ii) to estimate causal effects
- For the former: Importance to test prediction quality *out-of-sample*
- For the latter: Importance to understand the role of *identifying assumptions* and their plausibility in different contexts