# Application of Machine Learning Techniques in Credit Card Fraud Detection

#### **Logistic Regression**

This model along with the other selected models is used for binary classification, where the output prediction can only take one of two possible values for example 1 or 0, true or false and in this case fraudulent or no fraud. It is one of the most popular algorithms, and uses a logistic function also called the sigmoid function. Inputted values (x) are combined linearly using weights or coefficient values to predict an output value (y).

```
In [11]:
           import numpy as np
           import pandas as pd
           import matplotlib.pyplot as plt
           import seaborn as sns
           %matplotlib inline
           from sklearn.datasets import load_iris
           import warnings
           warnings.filterwarnings('ignore')
           from collections import Counter
           print('All libraries imported')
          All libraries imported
In [12]:
           from pandas_profiling import ProfileReport
In [13]:
           data = pd.read_csv('creditcard.csv')
In [14]:
           #ProfileReport(data, title="Pandas Profiling Report")
In [15]:
           data.shape
Out[15]:
          (284807, 31)
In [16]:
           data.head()
             Time
                         V1
                                  V2
                                            V3
                                                     V4
                                                               V5
                                                                        V6
                                                                                  V7
                                                                                            V8
                                                                                                      V9
Out[16]:
          0
                   -1.359807
                            -0.072781 2.536347
                                                                                                             -0.0
               0.0
                                                1.378155
                                                         -0.338321
                                                                   0.462388
                                                                             0.239599
                                                                                       0.098698
                                                                                                0.363787
          1
                   1.191857
                             0.266151 0.166480
               0.0
                                                0.448154
                                                          0.060018
                                                                   -0.082361
                                                                            -0.078803
                                                                                       0.085102
                                                                                               -0.255425
                                                                                                             -0.2
          2
                  -1.358354
                            -1.340163 1.773209
                                                0.379780
                                                         -0.503198
                                                                   1.800499
                                                                             0.791461
                                                                                      0.247676
                                                                                               -1.514654
                                                                                                             0.2
          3
                  -0.966272 -0.185226 1.792993
                                               -0.863291 -0.010309
                                                                   1.247203
                                                                             0.237609
                                                                                      0.377436 -1.387024 ...
                                                                                                             -0.1
               1.0
               2.0 -1.158233
                            0.877737 1.548718
                                                0.403034 -0.407193
                                                                   0.095921
                                                                             0.592941 -0.270533
                                                                                                0.817739 ...
                                                                                                             -0.0
```

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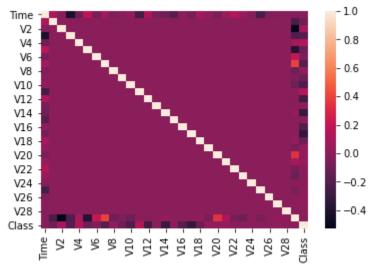
In [17]:

5 rows × 31 columns

data.isnull().sum()

```
Out[17]: V1
          V2
                      0
                      0
          V3
                      0
          V4
          V5
                      0
          V6
                      0
          V7
                      0
          V8
                      0
          V9
                      0
          V10
                      0
          V11
                      0
          V12
                      0
          V13
                      0
          V14
                      0
          V15
                      0
          V16
                      0
          V17
          V18
                      0
                      0
          V19
          V20
          V21
                      0
          V22
                      0
          V23
                      0
          V24
                      0
          V25
                      0
          V26
                      0
                      0
          V27
          V28
          Amount
                      0
          Class
                      0
          dtype: int64
In [18]:
           g = sns.countplot(data['Class'])
           g.set_xticklabels(['Not Fraud', 'Fraud'])
           plt.show()
             250000
             200000
          ig 150000
             100000
              50000
                 0
                            Not Fraud
                                                      Fraud
                                          Class
In [19]:
           data.Class.value_counts()
Out[19]:
                284315
                    492
          Name: Class, dtype: int64
          Out of 284807 cases, there are 492 cases of fruad in this data set Which is 0.17%
In [20]:
           sns.heatmap(data.corr(), annot = False)
           plt.show()
```

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```
In [21]:
          correlations = data.corr()['Class'].sort_values()
          print('Most Positive Correlations: \n', correlations.tail(6))
          print('\nMost Negative Correlations: \n', correlations.head(6))
         Most Positive Correlations:
          V19
                   0.034783
                  0.040413
         V21
         V2
                  0.091289
         V4
                  0.133447
         V11
                  0.154876
         Class
                  1.000000
         Name: Class, dtype: float64
         Most Negative Correlations:
          V17 -0.326481
         V14
               -0.302544
               -0.260593
         V12
               -0.216883
         V16
               -0.196539
         V3
               -0.192961
         Name: Class, dtype: float64
```

## Data Pre-processing

## **Data Standardization**

Standardizing the features refers to rescaling the features so that they will have the properties of a standard normal distribution with a mean of 0 and standard deviation of 1. I performed standardization on the 'Amount' feature using StandardScalar in the scikit-learn library.

#### Before standardization

```
In [22]:
              data['Amount']
                         149.62
 Out[22]:
                           2.69
             1
             2
                         378.66
             3
                        123.50
                          69.99
             284802
                           0.77
                          24.79
             284803
             284804
                         67 88
Loading [MathJax]/extensions/Safe.js 00
```

```
284806
                   217.00
         Name: Amount, Length: 284807, dtype: float64
In [23]:
          from sklearn.preprocessing import StandardScaler
          data[['Amount']] = StandardScaler().fit_transform(data[['Amount']])
        After standardization
In [24]:
          data['Amount']
                   0.244964
Out[24]:
                  -0.342475
                   1.160686
                   0.140534
                  -0.073403
         284802
                  -0.350151
         284803
                  -0.254117
         284804
                  -0.081839
         284805
                  -0.313249
         284806
                   0.514355
         Name: Amount, Length: 284807, dtype: float64
         Data Splittig using Random seed
        A random seed is used to ensure the same data split each time the code is excecuted.
In [25]:
          from sklearn.model_selection import train_test_split
In [26]:
          x = data.drop("Class", axis =1)
          y = data[["Class"]]
In [27]:
          x.shape
```

```
(284807, 30)
 Out[27]:
 In [28]:
            y.shape
            (284807, 1)
 Out[28]:
 In [29]:
            x_train, x_test, y_train, y_test = train_test_split(x, y, test_size = 0.30, random_state =
 In [30]:
            x_train.shape
            (199364, 30)
 Out[30]:
 In [31]:
            x_test.shape
           (85443, 30)
 Out[31]:
 In [32]:
            y_train.shape
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```

```
Out[32]: (199364, 1)

In [33]: y_test.shape

Out[33]: (85443, 1)
```

## **Data Resampling**

The dataset is highly unbalanced. To tackle this problem, I used resampling techniques such as:

- · Random Undersampling
- Random Oversampling .
- SMOTE
- · Under-Sampling: Tomek Links Removal
- Combination of SMOTE and undersampling

Implemented these on the training data separately to make it balanced

However as a control we will run the model first with no resmapling techniques and analyze the results, this will be done with the other algorithms.

## 1. Linear Regresssion with no Resampling

## Hyper parameter search for Logistic Regression

Hyperparameter is a configuration that is external to the model whose value cannot be estimated from the training data. It should not be confused with the model parameter as a model parameter is a configuration that is internal to the model, and its value can be estimated during the training process.

In the logistic regression model, the regularization parameter 'C' is an important hyperparameter that needs to be tuned carefully. The value of C directly affects the generalization ability of the model. For instance, for large values of C, the model tends to overfit the data, and for small values of C, the model tends to underfit the data. Given an initial list of C values, we performed GridSearchCV technique on the resampled training data to find the best C parameter for the logistic regression model.

```
In [34]:     from sklearn.linear_model import LogisticRegression
     from sklearn.model_selection import GridSearchCV
     from sklearn import metrics
     from sklearn.svm import SVC

In [35]:  ##clf = GridSearchCV(estimator, param_grid, 10, scoring) #(estimator, param_grid, cv(cross))
In [36]:  lg = LogisticRegression(max_iter= 600)
In [37]:  logistic_params = {'C':[x / 10.0 for x in range(0, 15, 1)]}
In [33]:  clf = GridSearchCV(lg, logistic_params, cv = 10, scoring ='accuracy')
```

From the gridsearch 10 fold cross validation, the best C parameter is 0.2. With this value, we can then proceed to build and evaluate the regression model.

#### Fitting the model

```
In [698...
          classifier1 = LogisticRegression(C = 0.2, max_iter = 600)
          model1 = classifier1.fit(x_train, y_train)
          params = model1.get_params()
          params
Out[698... {'C': 0.2,
           'class_weight': None,
           'dual': False,
           'fit_intercept': True,
           'intercept_scaling': 1,
           'l1_ratio': None,
           'max_iter': 600,
           'multi_class': 'auto',
           'n_jobs': None,
           'penalty': '12'
           'random_state': None,
           'solver': 'lbfgs',
           'tol': 0.0001,
           'verbose': 0,
           'warm_start': False}
```

Prints out all the tunable parameters (values above are the default values), the value of C directly affects the generalization ability of the model. For instance, for large values of C, the model tends to overfit the data, and for small values of C, the model tends to underfit the data. Therefore, the value of C needs to carefully selected by using GridSearchCV.

For this instance, the model exceeded the max iter reached so a new value will have to be specified.

## **Evaluation**

```
In [39]: from sklearn.metrics import accuracy_score
    from sklearn.metrics import plot_roc_curve, plot_precision_recall_curve, roc_curve

In [700... prediction1 = model1.predict(x_test)
    print ('Accuracy Score: ', accuracy_score(y_test, prediction1))

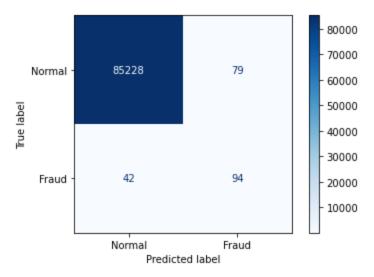
Accuracy Score: 0.9985838512224524
```

#### **Confusion Matrix**

```
In [40]: from ckloars metrics import plot_confusion_matrix, confusion_matrix Loading [MathJax]/extensions/Safe.js
```

```
In [702...
          plot_confusion_matrix(model1, x_test, y_test, cmap = 'Blues', display_labels = ['Normal',
```

<sklearn.metrics.\_plot.confusion\_matrix.ConfusionMatrixDisplay at 0x1e634438310>

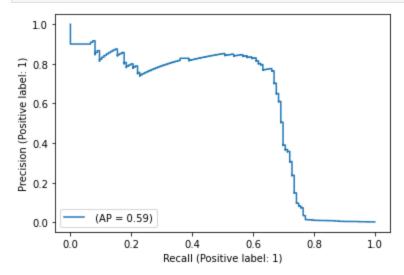


## Classification Report

```
In [703...
          from sklearn.metrics import classification_report
          print(classification_report(y_test, prediction1, digits=4))
                        precision
                                      recall f1-score
                                                          support
                     0
                           0.9995
                                      0.9991
                                                0.9993
                                                            85307
                     1
                           0.5434
                                      0.6912
                                                0.6084
                                                              136
                                                0.9986
                                                            85443
              accuracy
             macro avg
                           0.7714
                                      0.8451
                                                0.8039
                                                            85443
         weighted avg
                           0.9988
                                      0.9986
                                                0.9987
                                                            85443
```

```
In [782...
           from sklearn.metrics import precision_recall_curve, plot_precision_recall_curve
In [783...
           precision, recall, thresholds = precision_recall_curve(y_test, prediction1)
In [784...
           precision
          array([0.0015917, 0.5433526, 1.
                                                   ])
Out[784...
In [785...
           recall
          array([1.
                            , 0.69117647, 0.
                                                      ])
Out[785...
In [786...
           thresholds
Out[786... array([0, 1], dtype=int64)
```

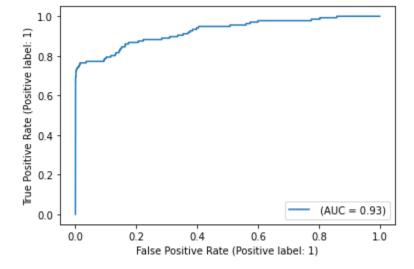
```
plot_precision_recall_curve(model1, x_test, y_test, name = '')
plt.show()
```



#### Area Under Precision Recall Curve = 0.59

## Reciever Operating Characteristic Curve (ROC)

```
In [713... from sklearn.metrics import plot_roc_curve, roc_curve
In [789... plot_roc_curve(model1, x_test, y_test, name = '')
plt.show()
```



Area under ROC (AUROC) = 0.93

# 2. Linear Regression with Random Under Sampling

Undersampling can be defined as removing some observations of the majority class. This is done until the majority and minority class is balanced out.

Undersampling can be a good choice when you have a ton of data -think millions of rows. But a drawback to undersampling is that we are removing information that may be valuable

```
In [37]:
          from imblearn import under_sampling
In [38]:
          from imblearn.under_sampling import RandomUnderSampler
In [39]:
          rus = RandomUnderSampler(random_state = 0)
          x_under, y_under = rus.fit_resample(x_train, y_train)
In [40]:
          x_under.shape
          (712, 30)
Out[40]:
In [41]:
          y_under.shape
         (712, 1)
Out[41]:
In [42]:
          y_under.Class.value_counts()
               356
Out[42]:
               356
         Name: Class, dtype: int64
In [43]:
          g = sns.countplot(y_under['Class'])
          g.set_xticklabels(['Not Fraud', 'Fraud'])
          plt.show()
```



Both majority and minority samples are now equal with 356 instances

#### Parameter search

Using the already created GridSearchCV, we will fit it with the new under sampled feature and target variables and find the best C values from the initial list above

From the gridsearch 10 fold cross validation, the best C parameter is 0.6 for the under sampled data. With this value, we can then proceed to build and evaluate the regression model.

## Fitting the Model

```
classifier2 = LogisticRegression(C = 0.6, max_iter = 600)
model2 = classifier2.fit(x_under, y_under)
```

#### **Evaluation**

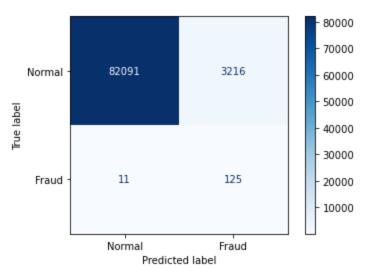
```
prediction2 = model2.predict(x_test)
print ('Accuracy Score: ', accuracy_score(y_test, prediction2))
```

Accuracy Score: 0.9622321313624288

#### **Confusion Matrix**

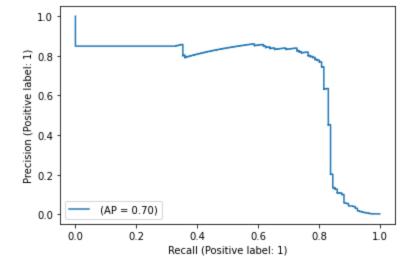
Loading [MathJax]/extensions/Safe.js  $n_{\text{matrix}}(\text{model2}, x_{\text{test}}, y_{\text{test}}, \text{cmap} = 'Blues', display_labels = ['Normal', was also be a constant of the constan$ 

Out[54]: <sklearn.metrics.\_plot.confusion\_matrix.ConfusionMatrixDisplay at 0x11e16190a00>

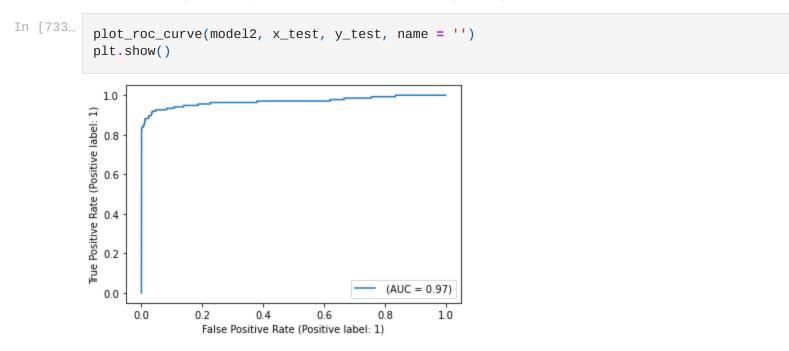


### **Classification Report**

```
In [728...
          print(classification_report(y_test, prediction2, digits = 4))
                        precision
                                      recall f1-score
                                                          support
                     0
                           0.9999
                                      0.9623
                                                            85307
                                                0.9807
                     1
                           0.0374
                                      0.9191
                                                0.0719
                                                              136
                                                0.9622
              accuracy
                                                            85443
                                      0.9407
             macro avg
                           0.5186
                                                0.5263
                                                            85443
         weighted avg
                           0.9983
                                      0.9622
                                                0.9793
                                                            85443
```



## Reciever Operating Characteristic Curve (ROC)



Area under ROC (AUROC) = 0.97

## 3. Linear Regression with Random Over Sampling

```
y_over.Class.value_counts()
In [738...
                199008
Out[738...
                199008
          Name: Class, dtype: int64
In [739...
           y_train.Class.value_counts()
                199008
Out[739... 0
                   356
          Name: Class, dtype: int64
In [740...
           g = sns.countplot(y_over['Class'])
           g.set_xticklabels(['Not Fraud', 'Fraud'])
           plt.show()
            200000
            175000
            150000
            125000
            100000
             75000
             50000
              25000
                            Not Fraud
                                                      Fraud
                                         Class
```

#### Parameter Search

## Fitting the model

```
classifier3 = LogisticRegression(C = 0.1, max_iter = 600)
model3 = classifier3.fit(x_over, y_over)
```

#### **Evaluation**

```
prediction3 = model3.predict(x_test)
print ('Accuracy Score: ', accuracy_score(y_test, prediction3))

Accuracy Score: 0.0611553001431363
```

Accuracy Score: 0.9611553901431363

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#### **Confusion Matrix**

```
In [745...
           confusion_matrix(y_test, prediction3)
Out[745...
          array([[81999,
                            3308],
                             125]], dtype=int64)
                       11,
In [746...
           plot_confusion_matrix(model3, x_test, y_test, cmap = 'Blues', display_labels = ['Normal',
          <sklearn.metrics._plot.confusion_matrix.ConfusionMatrixDisplay at 0x1e633a3e430>
                                                        80000
                                                        70000
                        81999
                                         3308
            Normal
                                                        60000
                                                        50000
          Frue label
                                                        40000
                                                        30000
                                         125
                          11
              Fraud
                                                        20000
                                                        10000
```

### Classification report

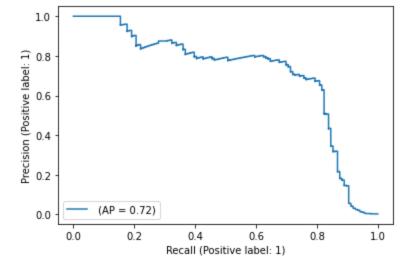
Normal

Predicted label

```
In [747...
          print(classification_report(y_test, prediction3, digits = 4))
                        precision
                                      recall f1-score
                                                          support
                     0
                            0.9999
                                      0.9612
                                                 0.9802
                                                            85307
                     1
                            0.0364
                                      0.9191
                                                 0.0700
                                                              136
                                                 0.9612
                                                            85443
              accuracy
                            0.5181
                                      0.9402
                                                            85443
             macro avg
                                                 0.5251
         weighted avg
                           0.9983
                                      0.9612
                                                 0.9787
                                                            85443
```

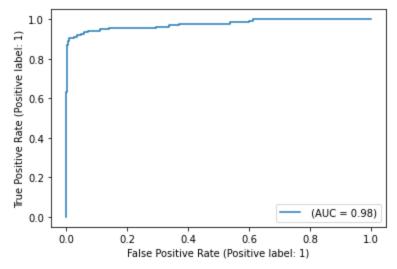
Fraud

```
In [748... precision, recall, thresholds = precision_recall_curve(y_test, prediction3)
In [749... plot_precision_recall_curve(model3, x_test, y_test, name = '')
plt.show()
```



## Reciever Operating Characteristic Curve (ROC)

plot\_roc\_curve(model3, x\_test, y\_test, name = '')
plt.show()



# 4. Linear Regression with Synthetic Minority Oversampling Technique SMOTE

This technique generates synthetic data for the minority class.

SMOTE (Synthetic Minority Oversampling Technique) works by randomly picking a point from the minority class and computing the k-nearest neighbors for this point. The synthetic points are added between the chosen point and its neighbors.

- · Choose a minority class as the input vector
- Find its k nearest neighbors (k neighbors is specified as an argument in the SMOTE() function)
- Choose one of these neighbors and place a synthetic point anywhere on the line joining the point under consideration and its chosen neighbor
- Repeat the steps until data is balanced

SMOTE (Synthetic Minority Over-sampling Technique) is a type of over-sampling procedure that is used to correct the imbalances in the groups. This technique creates new data instances of the minority groups by

copying existing minority instances and making small changes to them. This makes SMOTE great at amplifying signals that already exist in the minority groups, but won't create new signals for those groups.

```
In [41]: from imblearn.over_sampling import SMOTE
```

Now, when dealing with synthetic data, the first rule is: Don't put synthetic data in your testing data! We want to implement our model on live data, so we want to see how our model will perform on real data and not the synthetic data that we have created. This means that we can only add the synthetic data to the training set. We can do that with the following code:

```
In [42]:
          smt = SMOTE(random_state = 0)
          # fit predictor and target variable
          x_train_SMOTE, y_train_SMOTE = smt.fit_resample(x_train, y_train)
          print('Original dataset shape for y \n', y.Class.value_counts())
          print('Resample dataset shape for y \n', y_train_SMOTE.Class.value_counts())
         Original dataset shape for y
                284315
          0
          1
                  492
         Name: Class, dtype: int64
         Resample dataset shape for y
                199008
         1
               199008
         Name: Class, dtype: int64
In [753...
          g = sns.countplot(y_train_SMOTE['Class'])
          g.set_xticklabels(['Not Fraud', 'Fraud'])
          plt.show()
            200000
            175000
            150000
            125000
            100000
             75000
             50000
             25000
                0
                          Not Fraud
                                                  Fraud
```

From here we can train our model on the training data with SMOTE included. Note that we are using the same logistic regression model created earlier, just fitting it with the new training data.

Class

#### Parameter search

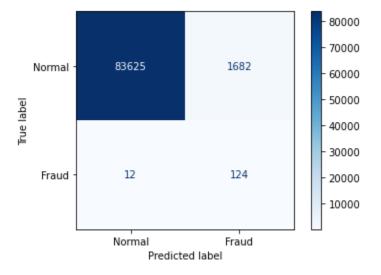
#### **Evaluation**

```
prediction4 = model4.predict(x_test)
print ('Accuracy Score: ', accuracy_score(y_test, prediction4))
```

Accuracy Score: 0.9801739171143335

#### **Confusion Matrix**

Out[47]: <sklearn.metrics.\_plot.confusion\_matrix.ConfusionMatrixDisplay at 0x2608673b1f0>



## **Classification Report**

```
In [758...
          print(classification_report(y_test, prediction4, digits = 4))
                        precision
                                      recall f1-score
                                                          support
                     0
                           0.9999
                                      0.9803
                                                0.9900
                                                            85307
                     1
                           0.0687
                                      0.9118
                                                0.1277
                                                              136
                                                0.9802
                                                            85443
              accuracy
                                      0.9460
             macro avg
                           0.5343
                                                0.5588
                                                            85443
                                                0.9886
         weighted avg
                           0.9984
                                      0.9802
                                                            85443
```

```
1.0 - (AP = 0.73)
```

plot\_precision\_recall\_curve(model4, x\_test, y\_test, name = '')

In [760...

plt.show()

0.0

0.2

## Reciever Operating Characteristic Curve (ROC)

Recall (Positive label: 1)

0.4

0.6

0.8

1.0

```
In [761...
                plot_roc_curve(model4, x_test, y_test, name = '')
                plt.show()
                  1.0
               Frue Positive Rate (Positive label: 1)
                  0.8
                  0.6
                  0.4
                  0.2
                                                                              (AUC = 0.97)
                  0.0
                         0.0
                                      0.2
                                                                            0.8
                                                  0.4
                                                               0.6
                                                                                         1.0
                                       False Positive Rate (Positive label: 1)
```

# 5. Linear Regression Tomek links removal

Tomek links are pairs of very close instances but of opposite classes. Removing the instances of the majority class of each pair increases the space between the two classes, facilitating the classification process.

Tomek's link exists if the two samples are the nearest neighbors of each other

In the code below, we'll use ratio='majority' to resample the majority class.

```
In [762... # import library from imblearn.under_sampling import TomekLinks

In [763... #TomekLinks?

Loading [MathJax]/extensions/Safe.js
```

```
# fit predictor and target variable
          x_{t1}, y_{t1} = t1.fit_{resample}(x_{train}, y_{train})
           print('Original dataset shape for y \n', y.Class.value_counts())
           print('Resample dataset shape for y \n', y_t1.Class.value_counts())
          Original dataset shape for y
                284315
          1
                  492
          Name: Class, dtype: int64
          Resample dataset shape for y
                198995
          1
                  356
          Name: Class, dtype: int64
In [765...
           g = sns.countplot(y_t1['Class'])
           g.set_xticklabels(['Not Fraud', 'Fraud'])
           plt.show()
            200000
            175000
            150000
            125000
          100000
             75000
             50000
             25000
                           Not Fraud
                                                   Fraud
                                        Class
```

t1 = TomekLinks(sampling\_strategy='majority')

In [764...

#### Parameter Search

## Evaluation

In [768...

```
In [769... prediction5 = model5.predict(x_test)

Loading [MathJax]/extensions/Safe.js
```

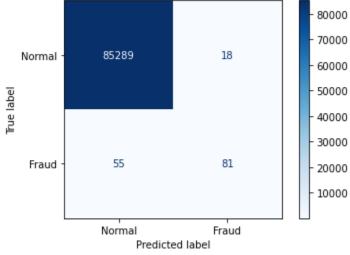
classifier5 = LogisticRegression(C = 0.1, max\_iter = 600)

 $model5 = classifier5.fit(x_t1, y_t1)$ 

```
print ('Accuracy Score: ', accuracy_score(y_test, prediction5))
```

Accuracy Score: 0.9991456292499094

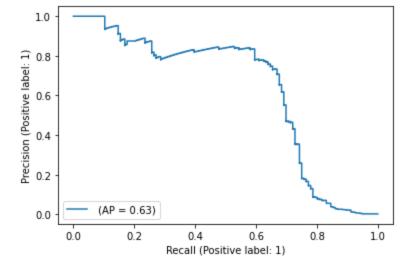
#### **Confusion Matrix**



## **Classification Report**

```
In [772...
          print(classification_report(y_test, prediction5, digits = 4))
                        precision
                                      recall f1-score
                                                          support
                     0
                           0.9994
                                      0.9998
                                                0.9996
                                                            85307
                     1
                           0.8182
                                      0.5956
                                                0.6894
                                                              136
                                                0.9991
                                                            85443
              accuracy
                           0.9088
                                      0.7977
                                                0.8445
                                                            85443
             macro avg
         weighted avg
                           0.9991
                                      0.9991
                                                0.9991
                                                            85443
```

```
plot_precision_recall_curve(model5, x_test, y_test, name = '')
plt.show()
```



## Reciever Operating Characteristic Curve

```
In [774...
             from sklearn.metrics import plot_roc_curve, plot_precision_recall_curve, roc_curve
In [775...
             plot_roc_curve(model5, x_test, y_test, name = '')
             plt.show()
             #plt.plot([0,1], [0,1], c='b')
               1.0
            True Positive Rate (Positive label: 1)
               0.8
               0.6
               0.4
              0.2
                                                               (AUC = 0.95)
               0.0
                    0.0
                              0.2
                                        0.4
                                                   0.6
                                                             0.8
                                                                       1.0
                               False Positive Rate (Positive label: 1)
 In [ ]:
```