

Forecast Adjustment Under Shocks: A Unification

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Abstract

This work systematizes and unifies the rich landscape of model adjustment and model correction methods, with a special focus on forecast adjustment under the presence of shocks.

1 Introduction

Forecasting amid anticipated shocks raises unavoidable questions: should the forecast model be abandoned in favor of a discretionary or ad-hoc or one-off adjustment? Does the discretion of a forecaster rule out a quantitative method for making the adjustment? What is the ultimate purpose of the adjustment, and how it is to be used? For how long is the adjustment necessary or reliable?

This work aims to systematize and unify a range of conceptual approaches and tools that have developed across the broad ecosystem of the econometric and forecasting literatures.

difference between discretionary and automated

Setting the model back on track

what we are talking about here is not forecast combination, but there may be, nevertheless, a role for forecast combination: combining the forecasts generated by small differences in covariate and/or donor choice

The role and meaning of similarity

How important is a shared DGP?

The forecast horizon — does it matter? If so, how so? [Lin and Eck \[2021\]](#) has a one-period horizon. [Clements and Hendry \[1998\]](#) p. 203 discuss how long to keep the forecast adjustment in place. For a corrected “slope parameter”, the effect of h is not so clear.

1.1 Literature Review

Three Clements and Hendry books

- 1994

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- 1998
- 1999

Quinton-Guerrera and Zhong

1.2 Model Adjustment Using Similarity-Based Parameter Correction: A Global Overview

1. a random object to forecast that depends on a linear specification
2. a parametric model family shared by donors
3. a correction term for the model family shared by donors
4. a parametric specification for the correction term
5. a reliable estimation procedure for the shared model
 - (a) This should be straightforward
6. a reliable estimation procedure for the correction term
 - (a) This might not be straightforward. Some models like GARCH, for example, might deliver very noisy estimates for indicator variables that occur just once.
7. a correction function that aggregates (i.e. maps) donor correction terms based on some notion of similarity

2 Setting

3 Model-Specific Considerations

3.1 ARIMA

3.2 GARCH

3.3 HAR

3.4 VAR

4 Real Data Examples

5 Discussion

- Binary Outcome Forecasts
- Density Forecasts
- Quantile Forecasts

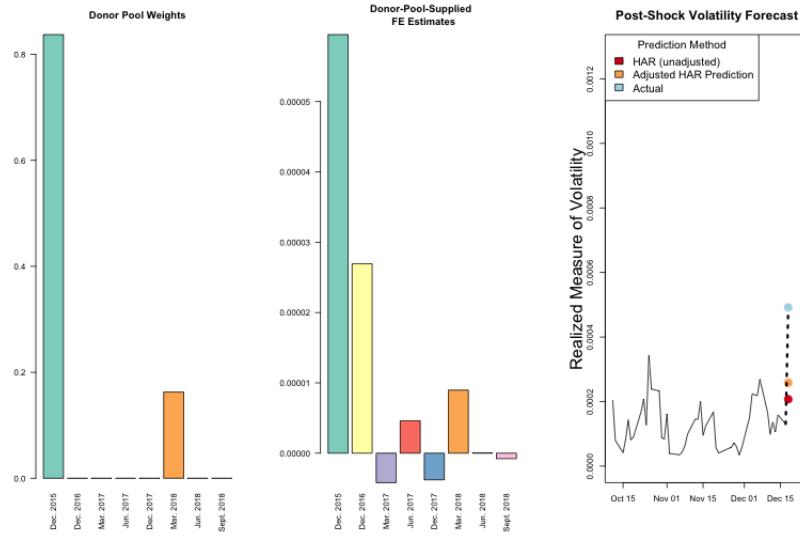


Figure 1: Volatility series of six i.i.d. GARCH processes, each of which experiences a volatility shock, indicated with a red vertical line, at a uniformly distributed point in the set $\{756, \dots, 2520\}$ of trading days, corresponding to between 3 and 10 years of daily trading data.

References

- Michael Clements and David F Hendry. *Forecasting economic time series*. Cambridge University Press, 1998.
- Jilei Lin and Daniel J Eck. Minimizing post-shock forecasting error through aggregation of outside information. *International Journal of Forecasting*, 2021.