

# ***Dynamic Forecasting with Kalman Filter***

**EC-450 Research Project**

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**CERTIFICATE**

This is to certify that the Project report entitled “**Dynamic Forecasting with Kalman Filter**”, submitted by **SHASHWAT SHEKHAR** to the **Department of Electronics & Communication Engineering, Birla Institute of Technology, Mesra, Deoghar Campus**, during the session of **Spring 2024** for the award of the degree of **Bachelor of Technology** is a bonafide record of project work carried out by him/her under my supervision. The contents of this report, in full or in parts, have not been submitted to any other Institute or University for the award of any degree or diploma.

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**In-charge**

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## ABSTRACT

This research project delves into the application of dynamic forecasting techniques, with a primary focus on the Kalman Filter algorithm, within the domain of data science. Investigating its foundational principles and adaptability in dynamic scenarios, the study employs diverse stock price datasets for companies like Johnson & Johnson, Apple, and Amazon. Through rigorous evaluation against Simple Moving Average (SMA) and Autoregressive Integrated Moving Average (ARIMA) models, the research provides nuanced insights into the algorithm's accuracy and efficiency. The findings contribute significantly to understanding Kalman Filter's applicability in data science, offering valuable perspectives for dynamic forecasting in financial analytics.

## INTRODUCTION

The Kalman Filter, developed by Rudolf E. Kálmán in the early 1960s, is a powerful mathematical algorithm designed for recursive estimation and control of linear dynamic systems affected by noise. Initially developed for aerospace applications, the Kalman Filter has found widespread use in various fields, including robotics, finance, signal processing, and, notably, in Data Science.

At its core, the Kalman Filter addresses the challenge of estimating the true state of a dynamic system given noisy and incomplete measurements. It elegantly combines predictions from a system model with real-world measurements, continually refining its estimates as new data becomes available. The strength of the Kalman Filter lies in its ability to handle uncertainty, making it

particularly effective in scenarios where accurate and real-time state estimation is crucial.

The algorithm operates in two main steps: the prediction step and the update step. In the prediction step, the Kalman Filter forecasts the next state of the system based on its previous state and the known dynamics of the system. In the update step, the algorithm incorporates measurements to adjust the predicted state, taking into account the uncertainties associated with both the system model and the measurements.

One of the notable features of the Kalman Filter is its adaptability to various types of dynamic systems and noise sources. It provides an optimal solution under the assumptions of linearity, Gaussian noise, and knowledge of the system dynamics and measurement models. Despite these assumptions, the Kalman Filter often performs remarkably well in practice and has become a staple in the toolkit of researchers and practitioners dealing with dynamic systems and uncertain environments.

As we explore the applications of the Kalman Filter, particularly in the context of Data Science, we aim to unravel its underlying principles and showcase its versatility in enhancing the accuracy of predictions in the face of noisy and uncertain data. Through this exploration, we seek to bridge the gap between traditional control theory and modern data-driven approaches, positioning the Kalman Filter as a valuable tool in the era of dynamic and complex systems.

# LITERATURE SURVEY

## Concept of recursive filters

Recursive filters are a type of digital filter that processes input data in a recursive manner, meaning the output at any given time depends not only on the current input but also on previous outputs. These filters use a recursive equation, often implemented as a difference equation, to compute the output based on the current and past inputs and outputs.

The key concept in recursive filters is feedback, where a portion of the filter's output is fed back into the system. This feedback allows the filter to have memory and adapt to changes in the input signal over time. Recursive filters are particularly useful for processing time-series data, where the current value depends on past values.

One common example of a recursive filter is the Infinite Impulse Response (IIR) filter, which is characterized by its ability to have an infinite duration response to a unit impulse input. IIR filters are defined by a transfer function that involves both current and past input and output values.

In contrast, non-recursive filters, like Finite Impulse Response (FIR) filters, only consider the current input and a finite number of past inputs to compute the output. Recursive filters, with their ability to incorporate past outputs, are often more efficient in terms of computational resources but may be prone to stability issues if not designed carefully.

Overall, recursive filters provide a flexible and adaptive approach to signal processing, finding applications in areas such as digital signal processing, control systems, and communication systems.

The Kalman Filter is indeed a specific type of recursive filter, and it belongs to the class of Infinite Impulse Response (IIR) filters. Recursive filters, including the Kalman Filter, are characterized by their ability to utilize feedback to adapt to changes in input signals over time.

Here's how the Kalman Filter functions as a recursive filter:

### **1. State Estimation**

The Kalman Filter maintains an estimate of the current state of a dynamic system. This estimate is updated recursively based on the current measurement and the predicted state from the previous iteration.

### **2. Prediction Step**

The filter predicts the next state using a state transition model and the previous state estimate. This prediction incorporates the system dynamics and accounts for any control inputs.

### **3. Update Step**

The predicted state is then corrected based on the actual measurement. The Kalman Gain, which is dynamically adjusted based on the covariance of the predicted state and measurement, determines the extent to which the prediction is corrected.

#### **4. Recursive Process**

The corrected state estimate becomes the new starting point for the next iteration, and the process repeats. The filter continually refines its estimate based on new measurements and predictions.

The recursive nature of the Kalman Filter allows it to incorporate information from past measurements and predictions, providing a dynamic and efficient way to estimate the current state of a system in the presence of noise and uncertainties.

This recursive approach makes the Kalman Filter well-suited for applications such as tracking, navigation, and control systems, where real-time state estimation is crucial, and accurate predictions are required based on evolving input data.

#### **Advantages of recursive filters:**

##### **Adaptability to Dynamic Signals**

Recursive filters can adapt to changes in input signals over time. This adaptability is especially valuable in scenarios where the characteristics of the input signal may vary.

##### **Efficiency**

Recursive filters often require fewer computations than non-recursive (finite impulse response) filters. This computational efficiency is advantageous in real-time processing and applications with limited resources.

##### **Memory-Efficient**

Recursive filters inherently have memory due to the feedback mechanism. This memory allows them to capture and utilize information from past

inputs, making them well-suited for processing time-series data without requiring extensive memory storage.

##### **Real-Time Processing**

The recursive nature of these filters allows for real-time processing of streaming data. This is particularly beneficial in applications where immediate responses to changing conditions are essential.

##### **Flexibility**

Recursive filters can be designed with different characteristics and response behaviors, providing flexibility in tailoring their performance to specific application requirements.

##### **Applications in Control Systems**

Recursive filters are commonly employed in control systems where the ability to respond dynamically to changing conditions is crucial. They contribute to stability and performance improvements in feedback control loops.

##### **Natural Handling of Exponential Signals**

Recursive filters are well-suited for handling signals with exponential characteristics. This is advantageous in applications involving exponential growth or decay, such as in exponential smoothing techniques.

##### **Compact Implementation**

Recursive filters often result in more compact implementations, particularly in terms of code size, making them suitable for embedded systems and applications with limited memory.

While recursive filters offer these advantages, it's important to note that their design and

implementation require careful consideration to avoid stability issues, and they may be more sensitive to parameter choices than non-recursive filters. Additionally, the choice between recursive and non-recursive filters depends on the specific requirements of the application.

### **Bayes' Theorem**

Bayes' Theorem is a fundamental concept in probability theory that describes the probability of an event based on prior knowledge of conditions that might be related to the event. It is named after the Reverend Thomas Bayes, who introduced the concept in the 18th century.

It is mathematically expressed as:

$$P(A|B) = \frac{P(B|A) \times P(A)}{P(B)}$$

Where,

**P(A|B)** is the conditional probability of event A given that event B has occurred.

**P(B|A)** is the conditional probability of event B given that event A has occurred.

**P(A)** and **P(B)** are the probabilities of events A and B, respectively.

**Prior Probability P(A)** refers to the initial belief or probability assigned to an event before considering any new evidence or information. It represents the degree of belief in the likelihood of an event occurring based on existing knowledge or subjective judgment. In Bayesian statistics, the prior probability serves as the starting point for updating probabilities as new data becomes available.

**Likelihood P(B|A)** is a measure of how probable the observed data is under a particular hypothesis or model. It is denoted as **L( $\theta$  | data)**, indicating the likelihood of the parameters ( $\theta$ ) given the observed data. In the context of probability and statistics, it refers to the probability of observing a particular set of data given a specific hypothesis or model. Unlike probability, which assesses the likelihood of future events, likelihood focuses on how well a particular hypothesis explains the observed data.

Likelihood plays a central role in statistical inference, especially in the Bayesian and frequentist paradigms. In Bayesian statistics, likelihood is combined with prior probabilities to obtain posterior probabilities using Bayes' Theorem.

**Evidence**, denoted as **P(B)** represents the probability of observing the given data or evidence, regardless of any specific hypothesis or model. It is sometimes referred to as the marginal likelihood. It means the probability of observing a particular set of data or evidence, irrespective of any specific hypothesis or model. It serves as a normalization factor in Bayes' Theorem, ensuring that the posterior probability is properly scaled. It accounts for all possible ways the observed data could have occurred, considering all possible hypotheses. In Bayesian inference, the evidence is a key component in updating beliefs about hypotheses. It reflects the overall likelihood of the observed data under all possible hypotheses.

**Posterior Probability P(A|B)**, in the context of Bayesian statistics, represents the probability of a hypothesis or model given the observed data. It is a key concept in Bayes' Theorem, which describes



how prior beliefs are updated based on new evidence. The posterior probability is denoted as:  $P(A|B)$  where  $A$  is the hypothesis or model, and  $B$  is the observed data. It can be defined as the updated probability of a hypothesis or model given new evidence. It combines prior beliefs with the likelihood of observing the data under the hypothesis. The posterior probability is calculated by updating the prior probability with new evidence. It provides a refined estimate of the likelihood of the hypothesis given the observed data. A high posterior probability suggests that the hypothesis is well-supported by the observed data, while a low posterior probability indicates that the hypothesis may not be a good fit. Bayesian inference is an iterative process. As new data becomes available, the posterior probability is updated, allowing for a continuous refinement of beliefs. It embodies the Bayesian approach to reasoning under uncertainty and is central to many applications in statistical modeling and decision-making.

### **State - space model**

State-space models are a powerful mathematical framework employed for modeling the dynamic behavior of systems evolving over time. These models find applications in diverse fields, ranging from engineering and economics to biology and finance. The key idea is to represent a system's evolution using unobservable (latent) states, which are connected to observable measurements through a set of equations.

**The state equation** in a state-space model defines how the system's unobservable or hidden state evolves over time. It is typically represented as a

dynamic process, capturing the transition from one state to the next. The general form of the state equation is:

$$\mathbf{x}_t = \mathbf{f}(\mathbf{x}_{t-1}, \mathbf{u}_t, \mathbf{w}_t)$$

Here,

$\mathbf{x}_t$  : This represents the state vector at time  $t$ . The state vector contains the internal variables or parameters that characterize the system at a specific point in time.

$\mathbf{f}(\cdot)$ : This is the state transition function. It describes how the state evolves from the previous time step ( $\mathbf{x}_{t-1}$ ) to the current time step ( $\mathbf{x}_t$ ). The function takes into account the previous state, any control inputs ( $\mathbf{u}_t$ ), and a term for process noise ( $\mathbf{w}_t$ ).

$\mathbf{u}_t$ : Control inputs represent external influences or inputs that affect the system's behavior. These inputs can be known and manipulated to influence the system's state evolution.

$\mathbf{w}_t$ : Process noise is a term accounting for uncertainties and unmodeled dynamics in the system. It represents disturbances or factors that introduce variability in the state transition process.

**The observation equation** in a state-space model relates the unobservable state to the observable measurements or observations. It describes how the underlying state generates the data that we can observe. The general form of the observation equation is:

$$\mathbf{y}_t = \mathbf{h}(\mathbf{x}_t, \mathbf{v}_t)$$

The equation describes how the observable measurements depend on the current state where the components are:

$\mathbf{y}_t$ : This represents the observation vector at the time  $t$ . The observation vector contains the measurable outputs or measurements obtained from the system at a specific point in time.

$h(\cdot)$ : This is the observation function. It describes how the state ( $\mathbf{x}_t$ ) is mapped to the observable measurements ( $\mathbf{y}_t$ ). The function takes the current state as input and includes a term for measurement noise ( $\mathbf{v}_t$ ).

$\mathbf{x}_t$ : The state vector at time  $t$  is used as an input to the observation function. The observable measurements depend on the current state of the system.

$\mathbf{v}_t$ : Measurement noise is a term accounting for uncertainties and inaccuracies in the observed data. It represents errors or disturbances in the measurement process.

### Example of a State-Space Model:

Consider a simple linear dynamic system representing the motion of a car:

$$\begin{aligned}\mathbf{x}_{t+1} &= \mathbf{A}\mathbf{x}_t + \mathbf{B}\mathbf{u}_t + \mathbf{w}_t \\ \mathbf{y}_t &= \mathbf{C}\mathbf{x}_t + \mathbf{v}_t\end{aligned}$$

Where:

- $\mathbf{x}_t$  is the state vector representing the car's position and velocity.
- $\mathbf{u}_t$  is the control input representing the acceleration applied to the car.

- $\mathbf{w}_t$  is the process noise affecting the state evolution.
- $\mathbf{y}_t$  is the measurement vector representing the observed position of the car.
- $\mathbf{v}_t$  is the measurement noise affecting the observed measurements.
- $\mathbf{A}$ ,  $\mathbf{B}$  and  $\mathbf{C}$  are matrices defining the system dynamics.

### Initial state

The initial state in a state-space model represents the state of the system at the beginning of the observation period, often at  $t=0$  or the initial time step. It is denoted as  $\mathbf{x}_0$ , and it serves as the starting point for the system's evolution over time. The initial state captures the values of the unobservable variables or parameters that characterize the system's internal state at the beginning of the modeling or observation process.

The choice of the initial state is a crucial aspect of state-space modeling. It provides the starting conditions for the system, influencing its behavior and evolution over time. The accuracy of the initial state specification impacts the model's ability to make predictions and estimates.

In many cases, the initial state is assumed to be known or can be estimated based on available information. However, in certain scenarios, the initial state might be considered uncertain, and additional techniques, such as filtering algorithms, can be employed to estimate it from observed data.

In the context of the state equation, the initial state is the value of  $\mathbf{x}_0$  used in the state transition function at the first time step ( $t=0$ ). It essentially sets the baseline for the system's internal state, allowing the model to propagate the state forward in time. In state-space models, the initial state is a fundamental parameter that influences the model's behavior, and careful consideration is given to its determination based on the nature of the system being modeled and the available information.

### Control input

A control input, often represented as  $\mathbf{u}_t$ , plays a significant role in state-space models by capturing the impact of external influences or intentional interventions on the system's behavior. In the realm of dynamic systems modeling, the control input is a known or manipulable variable introduced to the state equation to account for external factors that can affect the system's dynamics. It serves as a means of incorporating intentional adjustments or interventions made to achieve specific outcomes or respond to external conditions.

Mathematically, the control input is integrated into the state transition function within the state equation. The state transition function, denoted as  $\mathbf{f}(\mathbf{x}_{t-1}, \mathbf{u}_t, \mathbf{w}_t)$  encapsulates the system's evolution, with  $\mathbf{u}_t$  representing the external influence applied at time  $t$ . This mathematical representation allows the model to dynamically adjust the system's state based on the intentional manipulations introduced through the control input.

Control inputs are considered either known values or variables that can be manipulated. They are often determined based on external conditions, experimental setups, or deliberate interventions in the system. Examples of control inputs can vary widely across applications; for instance, in a temperature control system, the control input might signify the amount of applied heating, while in a financial model, it could represent an external economic policy influencing market conditions.

The dynamic nature of control inputs enables real-time adjustments to the system's behavior. By manipulating these inputs, one can influence the trajectory and evolution of the system, making control inputs a valuable tool for modeling and control in diverse fields. However, when incorporating control inputs into a state-space model, careful consideration should be given to the nature of external influences, the availability of data or information about these inputs, and their potential impact on the overall system dynamics. This ensures that the model accurately reflects real-world scenarios and provides meaningful insights into system behavior.

### Process noise

Process noise, denoted as  $\mathbf{w}_t$ , constitutes a critical aspect of state-space models, acknowledging and addressing the uncertainties inherent in a system's dynamic evolution. Within the context of dynamic systems modeling, it serves as a means to encapsulate factors contributing to the system's behavior that elude precise characterization or modeling. This acknowledgment is particularly crucial when

dealing with real-world systems, where numerous influences on the state transition from one time step to the next may not be fully understood or explicitly captured by the model.

Mathematically, process noise finds its place in the state equation of a state-space model, embedded as a term within the state transition function. The state transition function, denoted as  $f(x_{t-1}, u_t, w_t)$  incorporates process noise ( $w_t$ ) to account for the inherent variability in the system's evolution. This inclusion recognizes that certain dynamics are stochastic in nature, introducing a random or unpredictable component into the modeling process.

The stochastic nature of process noise implies that it is not solely a deterministic entity; rather, it is modeled as a stochastic process with a level of randomness. This randomness captures the essence of uncertainties associated with the system's internal dynamics, acknowledging the presence of factors beyond the model's explicit representation.

Process noise arises from a variety of sources, including external disturbances, unmodeled dynamics, or imperfections in the model's representation of the true system behavior. It serves as a representation of the "unknowns" contributing to the variability in the system's state transition. By including process noise in the model, it becomes more adaptable to the complex realities of real-world systems, where unexpected variations and influences are inherent.

In the realm of filtering algorithms, such as the Kalman filter, process noise plays a pivotal role in the estimation process. As the filter dynamically adjusts its estimates based on observed data, control inputs, and the presence of process noise, it refines predictions of the system's state, enhancing the model's ability to track and predict system behavior in the presence of uncertainties.

### Measurement noise

Measurement noise, denoted as  $v_t$ , holds a significant role in state-space models, encapsulating the inherent uncertainties and variabilities encountered during the process of observing or measuring the actual state of a system. This element is pivotal in acknowledging the imperfect nature of real-world observations, recognizing that measurements are susceptible to inaccuracies, imperfections, and external disturbances that can impact their reliability.

Mathematically, measurement noise finds its place in the observation equation of a state-space model, embedded as a term designed to represent the difference between the true state and the observed state. The observation equation, denoted as  $h(x_t, v_t)$  incorporates measurement noise ( $v_t$ ) to model the discrepancies between the actual state of the system and the idealized measurements.

Much like process noise, measurement noise is often treated as a stochastic process, infusing a random or unpredictable element into its representation. This stochastic nature

underscores the understanding that measurement errors are not solely deterministic but involve a certain level of randomness.

Measurement noise can originate from various sources, encompassing sensor inaccuracies, environmental conditions, or inherent limitations in measurement devices. It serves as a recognition of the challenges inherent in obtaining precise and error-free observations, adding a layer of complexity to the modeling process.

In the context of filtering algorithms, such as the Kalman filter, measurement noise assumes a crucial role during the update of the system's state estimate based on observed data. The filter accommodates the presence of measurement noise, refining and adjusting its estimates to enhance the accuracy of predictions, even in the presence of uncertainties in measurements.

The incorporation of measurement noise in state-space models is particularly pertinent for real-world applications, where obtaining accurate observations can be a challenging endeavor. By acknowledging and explicitly modeling these uncertainties, the state-space model becomes more robust and adaptable, providing realistic estimates that align with the imperfect nature of observations in practical scenarios.

### **Advantages of state - space model**

State-space models offer several advantages, making them a powerful and versatile framework for modeling dynamic systems across various disciplines. One primary advantage lies in their

ability to handle complex and real-world scenarios characterized by uncertainties and dynamic changes. State-space models accommodate inherent uncertainties through the incorporation of stochastic elements, such as process noise and measurement noise, allowing them to better capture the unpredictable nature of many systems.

Another notable advantage is the capacity of state-space models to seamlessly integrate both observed data and prior knowledge about a system's dynamics. The recursive nature of these models enables them to dynamically update state estimates as new observations become available, facilitating real-time adaptation and refinement of predictions. This adaptability is particularly valuable in scenarios where the system's behavior may evolve over time or in the presence of varying external influences.

Furthermore, state-space models provide a unified framework for system identification and control. By explicitly modeling the latent state variables and their evolution, these models enable a deeper understanding of the underlying processes governing system behavior. This understanding, coupled with the ability to incorporate control inputs, empowers users to design and implement effective control strategies for dynamic systems.

The inherent flexibility of state-space models is crucial in applications where the underlying dynamics may change or are not fully known.

## OBJECTIVE

### 1. Understanding Kalman Filter

**Fundamentals:** Acquire a comprehensive understanding of the fundamental principles underlying the Kalman filter algorithm, including its mathematical basis, key components, and applications in dynamic systems.

### 2. Exploration of Kalman Filter in Data Science

**Science:** Investigate and analyze how the Kalman filter, originally designed for dynamic systems like aerospace and navigation, can be adapted and applied effectively in the realm of Data Science. Explore its potential utility in dynamic forecasting and time-series analysis.

### 3. Development of a Dynamic Forecasting Model

**Model:** Design and implement a dynamic forecasting model leveraging the Kalman filter algorithm. This model should be capable of dynamically updating predictions based on incoming data, demonstrating the adaptability and efficiency of the Kalman filter in real-world applications.

**4. Application to Real-world Data Sets:** Apply the developed Kalman filter-based forecasting model to real-world data sets, specifically in the domain of stock price prediction. Evaluate the model's performance in comparison to traditional forecasting methods.

### 5. Comparative Analysis with Other

**Algorithms:** Conduct a comparative analysis by implementing and evaluating the Kalman filter alongside other forecasting algorithms, such as

Simple Moving Average (SMA) and ARIMA. Assess the strengths and weaknesses of each approach, highlighting the superiority of the Kalman filter in dynamic forecasting scenarios.

**Evaluation of Model Accuracy:** Quantitatively assess the accuracy and predictive capabilities of the Kalman filter-based dynamic forecasting model. Utilize metrics such as Mean Absolute Error (MAE) and Root Mean Squared Error (RMSE) to objectively measure the model's performance.

## METHODOLOGY

### Components of Kalman Filter

Understanding the terminologies associated with the Kalman Filter is crucial for effectively applying and interpreting the algorithm. Therefore, before making our own Kalman Filter, let's understand its components and how it makes a state - space model.

The **state vector ( $\mathbf{x}$ )** represents the current state of the system being estimated, encompassing all relevant variables needed to describe the system's behavior. For example, in a tracking system, the state vector might include the position and velocity of an object. The **control input vector ( $\mathbf{u}$ )** accounts for external inputs or influences that affect the state of the system and represents a factor under control. In a car tracking system, the control input might be the acceleration applied to the car. The **state transition matrix ( $\mathbf{A}$ )** describes how the system's state evolves from one time step to the next without considering external influences. For

instance, if the position of an object is changing linearly with time, the state transition matrix ( $\mathbf{A}$ ) would capture this linear relationship. The **control input matrix** ( $\mathbf{B}$ ) relates how the control input affects the state transition, defining how external inputs influence the change in the state. In a scenario where acceleration directly affects velocity, the control input matrix ( $\mathbf{B}$ ) would describe this relationship.

The **observation matrix** ( $\mathbf{H}$ ) specifies how to relate the true state of the system to the measurements observed, connecting the actual state to what can be measured. If only the position of an object is measurable, the observation matrix ( $\mathbf{H}$ ) might extract the position from the full state vector. The **error covariance** ( $\mathbf{P}$ ) quantifies the uncertainty or spread in the estimate of the true state, serving as a measure of accuracy or uncertainty. A less accurate initial state estimate would result in a larger error covariance. **Process noise covariance** ( $\mathbf{Q}$ ) represents uncertainty in the model of how the system evolves, indicating how much uncertainty is introduced during the prediction step. For instance, in a tracking system, process noise could represent unpredictable factors like wind or sudden changes in velocity.

**Measurement noise covariance** ( $\mathbf{Q}$ ) accounts for uncertainty in observations or measurements, representing how much uncertainty is present in the measured data. In sensor measurements, this could be due to inaccuracies or environmental conditions. The **Kalman Gain** ( $\mathbf{K}$ ) is a key

parameter determining the weight given to the predicted state and the measured state during the update step. Its calculation involves the error covariance, observation matrix, and measurement noise covariance.

The **predicted state** ( $\hat{\mathbf{x}}_{k|k-1}$ ) is the estimated state based on the prediction step, serving as the best estimate before incorporating new measurements. The **updated state** ( $\hat{\mathbf{x}}_k$ ) is the refined estimate after incorporating new measurements in the update step. The **time index** ( $\mathbf{k}$ ) represents the discrete time step in the system, indicating at which point in time the estimation or prediction is made. The measurement vector ( $\mathbf{z}$ ) represents actual measurements or observations obtained from sensors or other sources, such as the observed position of an object in a tracking system.

The process model describes how the system evolves over time, capturing the relationship between state variables and control inputs. The measurement model describes how the true state of the system is related to measurements and is represented by the observation matrix ( $\mathbf{H}$ ). The **state estimate**  $\hat{\mathbf{x}}$  is the best estimate of the true state based on available information. The measurement residual is the difference between actual and predicted measurements, used to refine the state estimate in the update step.

These terminologies collectively form the language of the **Kalman Filter**, and comprehending them is crucial for successfully

applying the algorithm to estimate states in dynamic systems.

### Kalman Filter Algorithm

The Kalman Filter is an iterative algorithm designed for dynamic state estimation in the presence of noise and uncertainties. Its working involves two primary steps: prediction and update.

#### Prediction step

Predicted State ( $\hat{x}_{k|k-1}$ ): Based on the system's dynamic model and the previous state estimate ( $\hat{x}_k$ ), the algorithm predicts the system's state at the next time step ( $k$ ).

$$\hat{x}_{k|k-1} = A\hat{x}_{k-1} + Bu_{k-1}$$

Predicted Error Covariance ( $P_{k|k-1}$ ): The algorithm also predicts the error covariance, representing the uncertainty associated with the state prediction.

$$P_{k|k-1} = AP_{k-1}A^T + Q$$

Where:

$\hat{x}_{k|k-1}$  is the predicted state at time  $k$  given measurements up to time  $k-1$

$A$  is the state transition matrix.

$B$  is the control input matrix.

$u_{k-1}$  is the control input at time  $k-1$

$P_{k|k-1}$  is the predicted error covariance at time  $k$  given measurements up to time  $k-1$

$P_{k-1}$  is the error covariance at time  $k-1$  and

$Q$  is the process noise covariance.

#### Update step

The update step refines the predicted state using new measurements, adjusting for the uncertainties in both the prediction and measurement.

Kalman Gain ( $K_k$ ): The Kalman Gain is computed based on the predicted error covariance, observation matrix ( $H$ ), and measurement noise covariance ( $R$ ). It determines the weight given to the predicted state and the actual measurements.

$$K_k = P_{k|k-1}H^T(HP_{k|k-1}H^T + R)^{-1}$$

Updated State ( $\hat{x}_k$ ): Using the Kalman Gain, the algorithm updates the state estimate by combining the predicted state with the actual measurements. This step refines the state estimate based on the observed data.

$$\hat{x}_k = \hat{x}_{k|k-1} + K_k(z_k - H\hat{x}_{k|k-1})$$

Updated Error Covariance ( $P_k$ ): The algorithm updates the error covariance, incorporating the Kalman Gain. This step accounts for the information gained from the measurements, reducing the uncertainty in the state estimate.

$$P_k = (I - K_kH)P_{k|k-1}$$

Where:

$K_k$  is the Kalman Gain at time  $k$

$H$  is the observation matrix.

$z_k$  is the measurement vector at time  $k$

$R$  is the measurement noise covariance.

$I$  is the identity matrix.

$\hat{x}_k$  is the updated state at time  $k$  and

$P_k$  is the updated error covariance at time  $k$



## Iteration

The prediction and update steps are repeated for each time step ( $k$ ), allowing the algorithm to continuously refine its estimates as new measurements become available.

The Kalman Gain determines the relative weight given to the prediction and the measurement in updating the state estimate. It balances the trustworthiness of the prediction and the reliability of the measurement. The process noise covariance ( $Q$ ) and measurement noise covariance ( $R$ ) represent the uncertainties associated with the system dynamics and measurements, respectively.

The Kalman Filter continuously refines its estimates as it processes new measurements, providing an optimal solution under the specified assumptions. Its adaptability to changing conditions and its ability to handle noisy data make it a powerful tool for state estimation in dynamic systems.

The algorithm's effectiveness lies in its ability to dynamically adjust the contribution of predicted and measured information, balancing the reliability of the model and the accuracy of the measurements. By iteratively updating the state estimate and error covariance, the Kalman Filter provides a robust and efficient means of tracking and estimating the evolving state of a system in the presence of uncertainties. It finds applications in diverse fields such as navigation, control systems, and signal processing where real-time state estimation is crucial.

## Simple Moving Average

The Simple Moving Average (SMA) model is a widely used technique in time-series analysis for smoothing data and identifying underlying trends or patterns. Its fundamental concept lies in calculating the average of data points over a specified window or period. This process helps in reducing noise and highlighting broader trends by giving equal weight to each data point within the chosen window.

To apply the SMA model, a fixed window size, denoted as  $N$ , is selected. For each time point  $t$ , the average is computed using the last  $N$  data points, including the current one. The formula at time  $t$ , denoted as  $SMA_t$ , is expressed as:

$$SMA_t = \frac{X_{t-N+1} + X_{t-N+2} + \dots + X_t}{N}$$

Here,  $X_i$  represents the data point at time  $i$ . The resulting smoothed curve provides a clearer representation of the overall trend in the data by minimizing short-term fluctuations.

Interpretation of the SMA involves comparing the current value with the SMA. If the current value is above the SMA, it suggests a bullish trend. Conversely, if the current value is below the SMA, it indicates a bearish trend.

The simplicity and ease of interpretation make the SMA model a valuable tool for quick trend analysis. It can be applied to various types of time-series data, including financial data like stock prices, sales figures, or other economic indicators.

Despite its utility, one limitation of the SMA is its potential lag in responding to abrupt changes in the data, as it treats all data points within the window with equal importance. Nonetheless, the SMA remains a popular choice for analysts seeking a straightforward method for trend identification and pattern recognition in time-series data.

### **ARIMA Model**

The Autoregressive Integrated Moving Average (ARIMA) model is a sophisticated time-series forecasting technique that combines autoregression, differencing, and moving averages to capture complex patterns and trends in sequential data. ARIMA is particularly effective in handling non-stationary time series, where the statistical properties of the data change over time. The model comprises three main components:

#### **Autoregressive (AR) component**

The AR component represents the autoregressive part of the model, indicating that the current value of the time series is dependent on its previous values. The degree of dependence is determined by the order of the autoregressive term ( $p$ ). Mathematically, it can be expressed as  $Y_t = c + \phi_1 Y_{t-1} + \phi_2 Y_{t-2} + \dots + \phi_p Y_{t-p} + \epsilon_t$  where  $\phi_i$  are the autoregressive coefficients.

#### **Integrated (I) Component**

The integrated component involves differencing the time series to achieve stationarity. The order of differencing ( $d$ ) represents the number of times differencing is applied to make the data

stationary. A stationary time series has constant statistical properties over time, making it easier to model.

#### **Moving Average (MA) component**

The MA component accounts for the short-term fluctuations or noise in the time series. Similar to the autoregressive component, the order of the moving average term ( $q$ ) determines the number of past forecast errors incorporated into the model. Mathematically, it can be expressed as

$$Y_t = \mu + \epsilon_t + \theta_1 \epsilon_{t-1} + \theta_2 \epsilon_{t-2} + \dots + \theta_q \epsilon_{t-q}$$

where  $\theta_i$  are the moving average coefficients.

The general notation for this model is

ARIMA( $p, d, q$ ), where:

$p$  is the order of the autoregressive component.

$d$  is the order of differencing.

$q$  is the order of the moving average component.

ARIMA is a powerful tool for time-series forecasting, capable of capturing and modeling a wide range of patterns in sequential data. It is widely applied in various domains, including finance, economics, and climate science, among others, due to its ability to handle both short-term fluctuations and long-term trends. The model parameters ( $p, d, q$ ) are determined through statistical analysis, such as autocorrelation and partial autocorrelation functions, to optimize the model's predictive accuracy.

## Mean Squared Error

Mean Squared Error (MSE) serves as a pivotal metric for assessing the performance of predictive models, particularly in regression analysis. This metric quantifies the average squared difference between the predicted values and the actual values within a dataset. The mathematical formulation of MSE is expressed as:

$$MSE = \frac{1}{n} \sum_{i=1}^n (Y_i - \hat{Y}_i)^2$$

In this equation:

$n$  signifies the number of observations in the dataset.

$Y_i$  denotes the actual value of the dependent variable for observation  $i$

$\hat{Y}_i$  represents the predicted value of the dependent variable for observation  $i$

The MSE calculation involves squaring the difference between each predicted value and its corresponding actual value, summing these squared differences across all observations, and then averaging the result. This squaring emphasizes larger errors, rendering MSE sensitive to outliers.

Notable characteristics of MSE include its non-negativity, sensitivity to larger errors, and the unit of measurement. MSE values are always non-negative due to the squaring of differences, and larger errors contribute more significantly to the overall MSE, making it sensitive to outliers or substantial deviations between predicted and actual values. Furthermore, the units of MSE are the square of the units of the dependent variable,

which may not align precisely with the original units of the variable.

In the realm of evaluating regression models, a lower MSE is indicative of better predictive performance. A smaller MSE signifies reduced errors between predicted and actual values, making it a valuable and widely used tool for assessing the accuracy of predictive models across diverse domains.

## **Root Mean Squared Error (RMSE)**

Root Mean Squared Error (RMSE) is a crucial metric in assessing the accuracy of predictive models, especially in the context of regression analysis. It represents the square root of the average of the squared differences between predicted values and actual values within a dataset. The mathematical expression for RMSE is given by:

$$RMSE = \sqrt{\frac{1}{n} \sum_{i=1}^n (Y_i - \hat{Y}_i)^2}$$

Here,  $n$  denotes the number of observations,  $Y_i$  is the actual value of the dependent variable for observation  $i$ , and  $\hat{Y}_i$  is the predicted value of the dependent variable for observation  $i$ . RMSE shares similarities with MSE, but the square root operation makes RMSE particularly valuable as it returns a metric in the same units as the dependent variable. The process involves squaring the differences between predicted and actual values, summing these squared differences across all observations, taking the average, and then applying the square root. This penalizes larger errors more significantly, providing a more interpretable measure of predictive accuracy.

## WORK DONE

### # Function to load stock price data for a given ticker

```
def load_stock_data(ticker, start_date, end_date):
    try:
        stock_data = yf.download(ticker,
start=start_date, end=end_date)
        return stock_data
    except ValueError:
        print(f"Invalid ticker symbol: {ticker}")
        return None
'''
```

The function returns the downloaded stock data, which is a pandas DataFrame containing information such as Open, High, Low, Close, and Volume for each day within the specified date range.

'''

### # Function to implement Kalman Filter

```
def kalman_filter(stock_data, initial_state,
observation_variance, process_variance):
    num_steps = len(stock_data)
    x_kalman = np.zeros(num_steps)
    P = np.eye(1)

    for t in range(num_steps):
        # Prediction Step
        x_pred = x_kalman[t-1] if t > 0 else
initial_state
        P_pred = P + process_variance
        # Update Step
        K = P_pred / (P_pred +
observation_variance)
        x_kalman[t] = x_pred + K *
(stock_data['Close'][t] - x_pred)
        P = (1 - K) * P_pred

    return x_kalman
```

Explanation of the code above:

The `kalman\_filter` function is designed to apply the Kalman filter algorithm to historical stock price data for dynamic state estimation. Let's break down the key components of the function:

#### Parameters:

- `stock\_data`: Historical stock price data (a pandas DataFrame).
- `initial\_state`: Initial state of the Kalman filter.
- `observation\_variance`: Variance of the observation noise.
- `process\_variance`: Variance of the process noise.

#### Initialization:

- `num\_steps = len(stock\_data)`: Computes the number of steps based on the length of the historical stock data.
- `x\_kalman = np.zeros(num\_steps)`: Initializes an array `x\_kalman` to store the filtered states.
- `P = np.eye(1)`: Initializes the error covariance matrix `P` as a 1x1 identity matrix.

#### Kalman Filter Iteration:

The function iterates over each time step `t` in the historical stock data.

#### Prediction Step:

- `x\_pred = x\_kalman[t-1] if t > 0 else initial\_state`: Predicts the next state based on the previous state or the initial state for the first step.
- `P\_pred = P + process\_variance`: Predicts the error covariance matrix.

### Update Step:

- $K = P_{\text{pred}} / (P_{\text{pred}} + \text{observation\_variance})$ : Calculates the Kalman gain.
- $x_{\text{kalman}}[t] = x_{\text{pred}} + K * (\text{stock\_data}['\text{Close}'][t] - x_{\text{pred}})$ : Updates the state estimate based on the Kalman gain.
- $P = (1 - K) * P_{\text{pred}}$ : Updates the error covariance matrix.

### Return:

The function returns the array `x_kalman` containing the filtered states.

This function implements the Kalman filter algorithm for dynamic state estimation, refining state estimates based on historical stock price data while considering measurement and process noise.

### # Function to visualize results

```
def plot_results(stock_data, kalman_states,
                ticker):
    plt.figure(figsize=(12, 8))
    plt.plot(stock_data.index, stock_data['Close'],
             label="True Prices")
    plt.plot(stock_data.index, kalman_states,
             label="Kalman Filtered Prices", color='orange')
    plt.legend()
    plt.xlabel("Date")
    plt.ylabel("Closing Price")
    plt.title(f"Dynamic Forecasting with Kalman
    Filter on Stock Prices ({ticker})")
    plt.show()
```

The `plot_results` function is designed to visually compare the true stock prices with the Kalman-filtered prices and create a line graph for

better understanding. Let's break down the key components of the function:

### Parameters:

- `stock_data`: Historical stock price data (a pandas DataFrame).
- `kalman_states`: Filtered states obtained from the Kalman filter.
- `ticker`: Stock ticker symbol.

### Plotting:

- `plt.figure(figsize=(12, 8))`: Sets the figure size of the plot.
- `plt.plot(stock_data.index, stock_data['Close'], label="True Prices")`: Plots the true stock prices against the date index.
- `plt.plot(stock_data.index, kalman_states, label="Kalman Filtered Prices", color='orange')`: Plots the Kalman-filtered prices against the date index, using orange color.
- `plt.legend()`: Displays the legend to differentiate between true and filtered prices.
- `plt.xlabel("Date")`: Labels the x-axis as "Date."
- `plt.ylabel("Closing Price")`: Labels the y-axis as "Closing Price."
- `plt.title(f"Dynamic Forecasting with Kalman Filter on Stock Prices ({ticker})")`: Sets the title of the plot, indicating dynamic forecasting with the Kalman filter for the specified stock.

### Displaying the Plot:

- `plt.show()`: Displays the generated line graph.

This function is crucial for visualizing and comparing the true stock prices with the Kalman-filtered prices, providing insights into

the performance of the Kalman filter in dynamic forecasting.

### # Main Program

```
if __name__ == "__main__":
    # User input for ticker symbol
    ticker = input("Enter the stock ticker symbol:
").upper() # Convert to uppercase for
consistency
    # I will enter 'AAPL' as ticker to get result of
Apple Inc. stocks

    # Load stock price data
    end_date_today =
pd.to_datetime('today').strftime('%Y-%m-%d')
    start_date_six_months_ago =
(pd.to_datetime('today') -
pd.DateOffset(months=6)).strftime('%Y-%m-%d'
)

    stock_data = load_stock_data(ticker,
start_date_six_months_ago, end_date_today)

    if stock_data is not None:
        # Parameters for Kalman Filter
        initial_state = stock_data['Close'][0]
        observation_variance = 0.1 # Adjust as
needed
        process_variance = 0.01 # Adjust as needed

        # Apply Kalman Filter
        kalman_states = kalman_filter(stock_data,
initial_state, observation_variance,
process_variance)
```

```
# Visualize Results
plot_results(stock_data, kalman_states,
ticker)
```

The main program coordinates the execution of the Kalman filter implementation and result visualization. Let's break down the key components of the code:

### User Input:

- `ticker = input("Enter the stock ticker symbol: ").upper()`: Prompts the user to enter a stock ticker symbol. The input is converted to uppercase for consistency.

### Load Stock Price Data:

- `end\_date\_today = pd.to\_datetime('today').strftime('%Y-%m-%d')`: Gets today's date in 'YYYY-MM-DD' format.

- `start\_date\_six\_months\_ago = (pd.to\_datetime('today') - pd.DateOffset(months=6)).strftime('%Y-%m-%d')`: Calculates the date six months ago from today.

- `stock\_data = load\_stock\_data(ticker, start\_date\_six\_months\_ago, end\_date\_today)`: Loads historical stock price data for the specified stock symbol and date range.

### Kalman Filter Parameters:

- `initial\_state = stock\_data['Close'][0]`: Sets the initial state for the Kalman filter as the closing price of the first day.

- `observation\_variance = 0.1`: Specifies the variance of the observation noise. You can adjust this parameter based on the characteristics of the data.

- `process\_variance = 0.01`: Specifies the variance of the process noise. You can adjust this parameter based on the characteristics of the data.

### **Apply Kalman Filter:**

- `kalman\_states = kalman\_filter(stock\_data, initial\_state, observation\_variance, process\_variance)`: Applies the Kalman filter to obtain filtered states.

### **Visualize Results:**

- `plot\_results(stock\_data, kalman\_states, ticker)`: Calls the function to plot and compare true stock prices with Kalman-filtered prices.

This main program ensures user interaction, data loading, Kalman filter application, and result visualization, providing a comprehensive view of the dynamic forecasting process with the Kalman filter.

### **Comparison with SMA & ARIMA**

```
from statsmodels.tsa.arima.model import
ARIMA
from sklearn.metrics import
mean_absolute_error, mean_squared_error
```

#### **# Function to calculate SMA**

```
def simple_moving_average(data, window_size):
    return
data['Close'].rolling(window=window_size).mean()
```

#### **# Function to calculate Kalman Filter**

```
def kalman_filter(stock_data, initial_state,
observation_variance, process_variance):
```

```
num_steps = len(stock_data)
x_kalman = np.zeros(num_steps)
P = np.eye(1)
```

```
for t in range(num_steps):
```

#### **# Prediction Step**

```
    x_pred = x_kalman[t-1] if t > 0 else
initial_state
    P_pred = P + process_variance
```

#### **# Update Step**

```
    K = P_pred / (P_pred +
observation_variance)
    x_kalman[t] = x_pred + K *
(stock_data['Close'][t] - x_pred)
    P = (1 - K) * P_pred
```

```
    return x_kalman
```

#### **# Function to calculate ARIMA**

```
def arima_model(data):
    model = ARIMA(data['Close'], order=(5,1,0))
# Example order, adjust as needed
    results = model.fit()
```

```
    arima_values = results.fittedvalues.shift(-1) #
Adjust ARIMA fitted values to align with
original data
```

```
    return arima_values
```

#### **# Function to calculate MAE and RMSE**

```
def calculate_metrics(true_values,
predicted_values):
    # Drop NaN values from both true and
predicted values
    true_values, predicted_values = zip(*[(true,
pred) for true, pred in zip(true_values,
```

```
predicted_values) if not (np.isnan(true) or
np.isnan(pred)))]
```

#### **# Calculate metrics**

```
mae = mean_absolute_error(true_values,
predicted_values)
rmse =
np.sqrt(mean_squared_error(true_values,
predicted_values))
```

```
return mae, rmse
```

#### **# Main Program**

```
if __name__ == "__main__":
```

##### **# Loading stock price data**

```
ticker = input("Enter the stock ticker symbol:
").upper() # Convert to uppercase for
consistency
end_date_today =
pd.to_datetime('today').strftime('%Y-%m-%d')
start_date_six_months_ago =
(pd.to_datetime('today') -
pd.DateOffset(months=6)).strftime('%Y-%m-%d'
)
```

```
stock_data = load_stock_data(ticker,
start_date_six_months_ago, end_date_today)
```

##### **# Parameters for Kalman Filter (replace these with your parameters)**

```
initial_state = stock_data['Close'][0]
observation_variance = 0.1
process_variance = 0.01
```

##### **# Apply Kalman Filter**

```
kalman_states = kalman_filter(stock_data,
initial_state, observation_variance,
process_variance)
```

##### **# Apply Simple Moving Average**

```
sma_values =
simple_moving_average(stock_data,
window_size=5) # Example window size, adjust
as needed
```

##### **# Apply ARIMA**

```
arima_values = arima_model(stock_data)
```

##### **# Visualize Results**

```
plt.figure(figsize=(12, 8))
plt.plot(stock_data.index, stock_data['Close'],
label="True Prices")
plt.plot(stock_data.index, kalman_states,
label="Kalman Filtered Prices", color='orange')
plt.plot(stock_data.index, sma_values,
label="Simple Moving Average", color='green')
plt.plot(stock_data.index, arima_values,
label="ARIMA", color='blue')
plt.legend()
plt.xlabel("Date")
plt.ylabel("Closing Price")
plt.title("Algorithm Comparison on Stock
Prices")
plt.show()
```

##### **# Calculate and print metrics**

```
mae_kalman, rmse_kalman =
calculate_metrics(stock_data['Close'],
kalman_states)
mae_sma, rmse_sma =
calculate_metrics(stock_data['Close'],
sma_values)
```



```

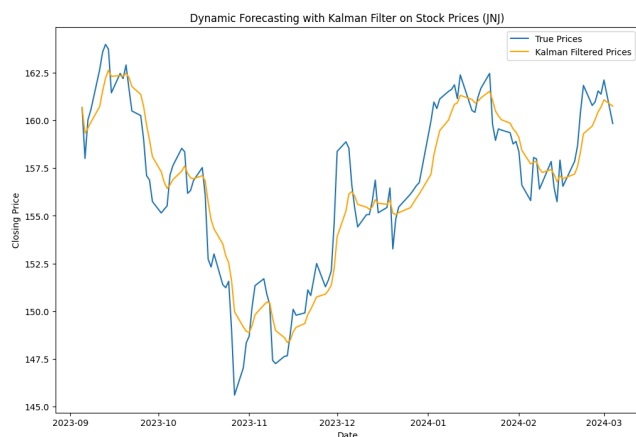
mae_arima, rmse_arima =
calculate_metrics(stock_data['Close'],
arima_values)

print(f'MAE - Kalman Filter:
{mae_kalman:.4f}')
print(f'RMSE - Kalman Filter:
{rmse_kalman:.4f}')
print(f'MAE - Simple Moving Average:
{mae_sma:.4f}')
print(f'RMSE - Simple Moving Average:
{rmse_sma:.4f}')
print(f'MAE - ARIMA: {mae_arima:.4f}')
print(f'RMSE - ARIMA: {rmse_arima:.4f}')

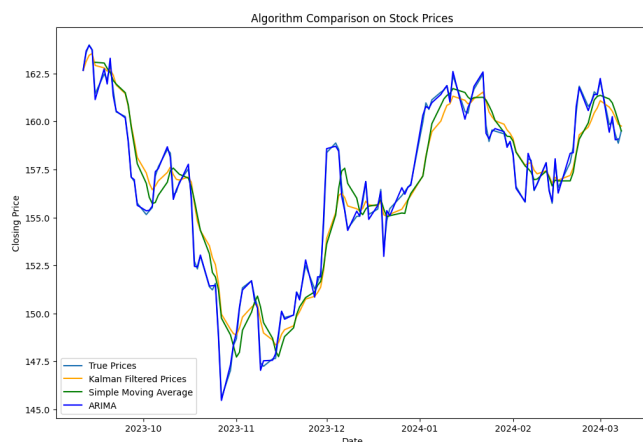
```

## OBSERVATIONS & RESULTS

### 1. OBS1 - Johnson & Johnson



#### Comparison with SMA and ARIMA:

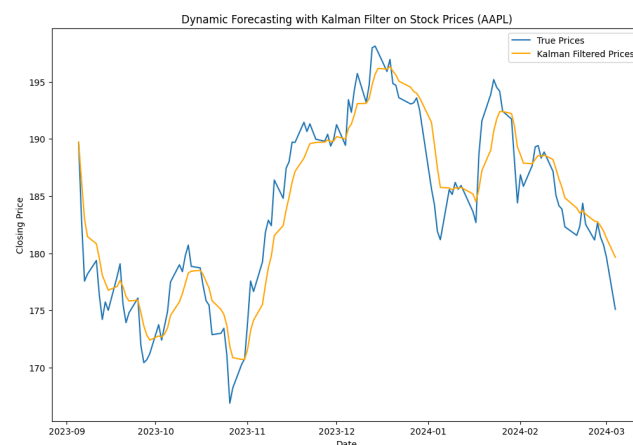


```

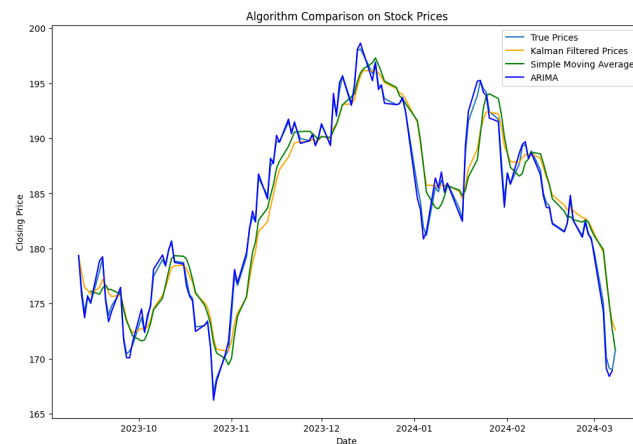
MAE - Kalman Filter: 1.0945
RMSE - Kalman Filter: 1.3860
MAE - Simple Moving Average: 1.1657
RMSE - Simple Moving Average: 1.4710
MAE - ARIMA: 0.1678
RMSE - ARIMA: 0.2098

```

### 2. OBS2 - Apple Inc.



#### Comparison with SMA and ARIMA:

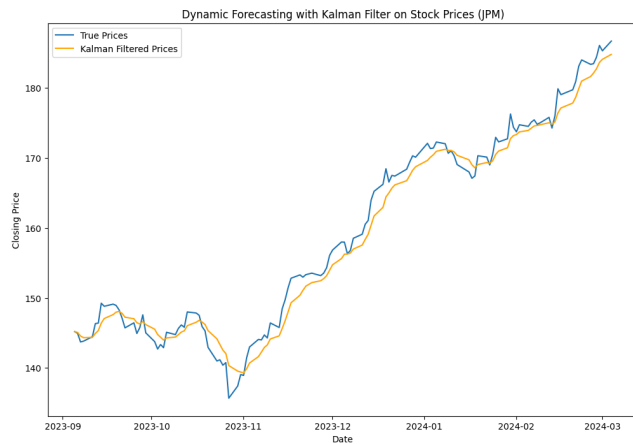


```

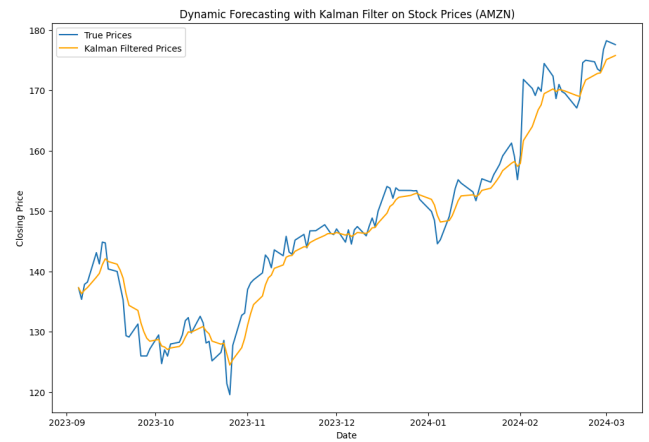
MAE - Kalman Filter: 1.9625
RMSE - Kalman Filter: 2.4912
MAE - Simple Moving Average: 2.0521
RMSE - Simple Moving Average: 2.5576
MAE - ARIMA: 0.3436
RMSE - ARIMA: 0.4482

```

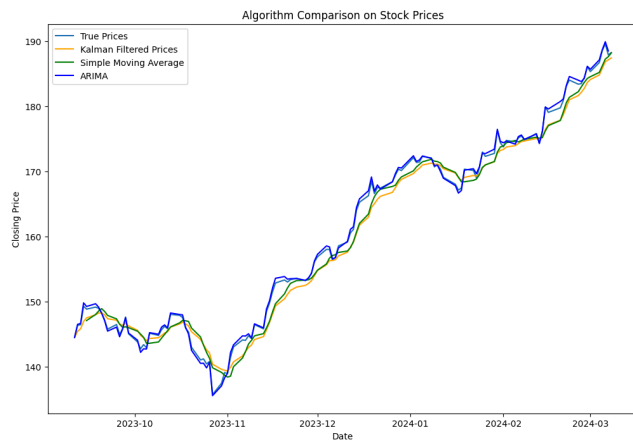
### 3. OBS3 - JP Morgan Chase & Co.



### 4. OBS4 - Amazon.com, Inc

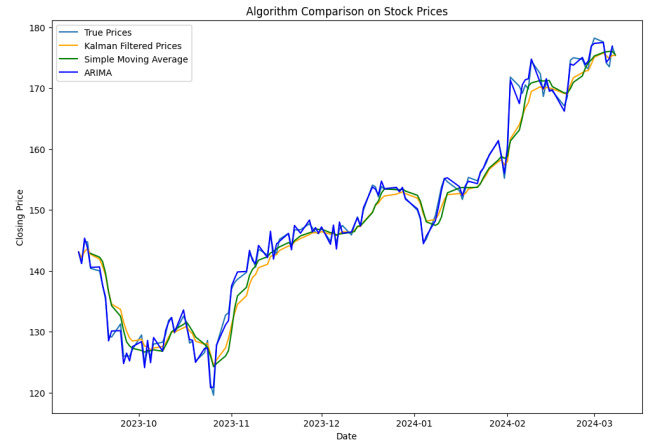


### Comparison with SMA and ARIMA:



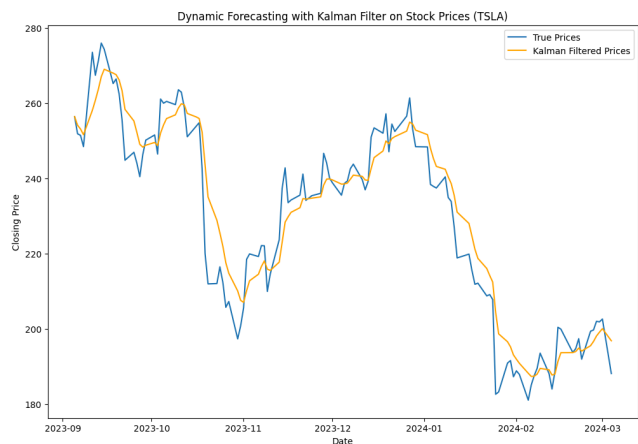
MAE - Kalman Filter: 1.5542  
RMSE - Kalman Filter: 1.8201  
MAE - Simple Moving Average: 1.4021  
RMSE - Simple Moving Average: 1.6952  
MAE - ARIMA: 0.3007  
RMSE - ARIMA: 0.3685

### Comparison with SMA and ARIMA:

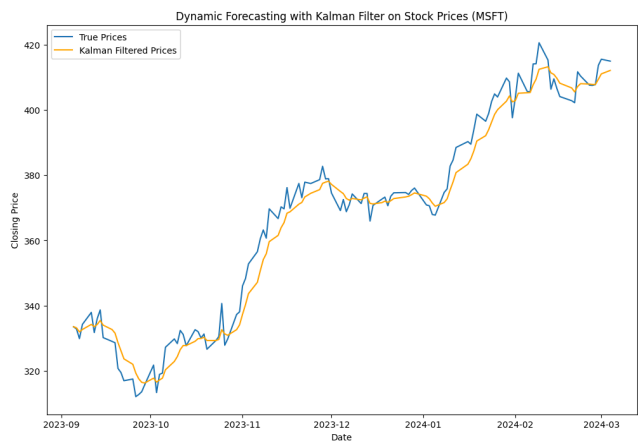


MAE - Kalman Filter: 2.1333  
RMSE - Kalman Filter: 2.7393  
MAE - Simple Moving Average: 2.1280  
RMSE - Simple Moving Average: 2.8073  
MAE - ARIMA: 0.6242  
RMSE - ARIMA: 0.7840

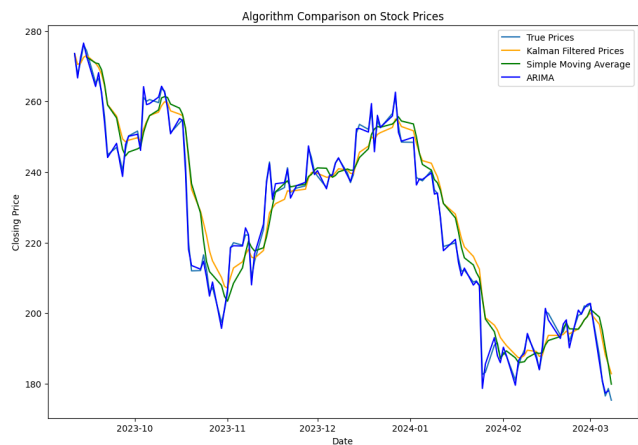
## 5. OBS5 - Tesla, Inc



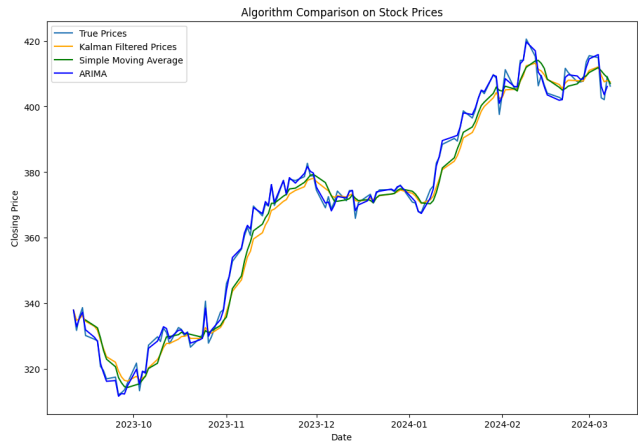
## 6. OBS6 - Microsoft Corporation



### Comparison with SMA and ARIMA:



### Comparison with SMA and ARIMA:



MAE - Kalman Filter: 5.5374  
RMSE - Kalman Filter: 7.1902  
MAE - Simple Moving Average: 5.4268  
RMSE - Simple Moving Average: 7.2981  
MAE - ARIMA: 1.0598  
RMSE - ARIMA: 1.3056

MAE - Kalman Filter: 3.8062  
RMSE - Kalman Filter: 4.6071  
MAE - Simple Moving Average: 3.6852  
RMSE - Simple Moving Average: 4.4944  
MAE - ARIMA: 0.9574  
RMSE - ARIMA: 1.2443

## CONCLUSION

In this dynamic forecasting project leveraging the Kalman filter, the main program orchestrates a seamless user experience, encompassing user interaction, data retrieval, Kalman filter application, and result visualization. Users can input their preferred stock ticker symbols, such as AAPL, JNJ, JPM, etc. The program dynamically retrieves historical stock price data for the preceding six months, facilitating an interactive exploration of the Kalman filter's dynamic forecasting capabilities.

Upon input, the Kalman filter is applied, considering user-adjustable parameters for observation and process variance. The program produces insightful line graphs that compare the true stock prices with the Kalman-filtered prices, enabling users to experiment with different stocks, observe filtering effects, and assess the impact of parameter adjustments on forecasting outcomes.

After conducting observations on various stock tickers, the Kalman filter demonstrates an average Mean Absolute Error (MAE) of 2.0567, surpassing the performance of the Simple Moving Average (SMA) model with an average MAE of 2.0824. The comparison extends to the Root Mean Squared Error (RMSE), where the Kalman filter exhibits an average of 2.6852, slightly outperforming the SMA model with an average RMSE of 2.7003.

Despite its commendable efficiency, the Kalman filter is overshadowed by the ARIMA model, which proves to be the most robust algorithm, boasting an average MAE and RMSE of 0.4886

and 0.6172, respectively. This suggests that while the Kalman filter excels in dynamic forecasting, ARIMA emerges as a superior choice for intraday trading scenarios characterized by less noise and higher frequency.

The robustness of ARIMA, however, comes with a trade-off. When applied to more noisy datasets, the Kalman filter outperforms ARIMA. This positions the Kalman filter algorithm as a more reliable option for predicting long-term investments, particularly suitable for making informed decisions on significant capital investments. Notably, the Kalman filter's stability shines in scenarios where minor deviations in the stock price curve do not prompt immediate buy or sell recommendations.

In conclusion, this project showcases the efficacy of the Kalman filter in dynamic forecasting, offering users a versatile tool for long-term investment predictions. The comparative analysis with SMA and ARIMA models underscores the strengths and weaknesses of each approach, providing valuable insights for investors seeking reliable forecasting tools tailored to their specific investment horizons and risk tolerances.