

Programming with Data

Session 7: Forecasting with Logistic Regressions Dr. Wang Jiwei Master of Professional Accounting

Binary outcomes

What are binary outcomes?



- Thus far we have talked about events with continuous outcomes
 - Revenue, earnings, ROA, etc
- Binary outcomes only have two possible outcomes
 - Did something happen, *yes* or *no*?
 - Is a statement *true* or *false*?
- Financial accounting:
 - Will the company's earnings meet analysts' expectations?
 - Will the company have positive earnings?
- Managerial accounting:
 - Will we have problem with our supply chain?
 - Will our customer go bankrupt?
- Audit:
 - Is the company committing fraud?
- Taxation:
 - Is the company too aggressive in their tax positions?
- Management and strategy
 - Does the business model change?

We can assign a probability to any of these

Binary classficiation algos



- Popular algorithms that can be used for binary classification include:
 - Logistic Regression (today's session)
 - Decision Trees (to be covered)
 - k-Nearest Neighbors
 - Support Vector Machine
 - Naive Bayes

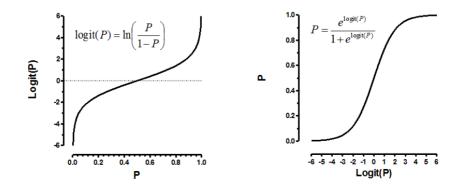
Logistic regression



- When modeling a binary outcome, we use logistic regression
 - A.k.a. logit model
- The *logit* function is $logit(p) = log\left(\frac{p}{1-p}\right)$
 - Also called *log odds*, see next slide

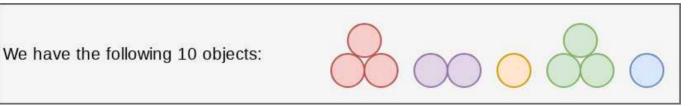
$$\log\left(rac{\mathrm{Prob}(y=1|X)}{1-\mathrm{Prob}(y=1|X)}
ight)=lpha+eta_1x_1+eta_2x_2+\ldots+arepsilon$$

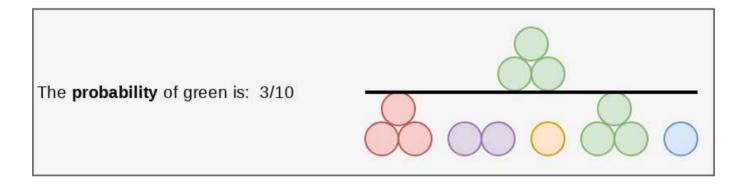
- The sign of the coefficients means the same as before
 - +: *increases* the likelihood of y occurring
 - -: decreases the likelihood of y occurring

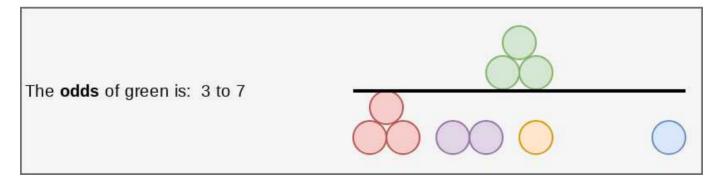


Odds vs probability









Logistic regression interpretation

Interpreting logit values



- The level of the coefficient is different
 - The relationship isn't linear between x_i and y now
 - Instead, coefficient is in *log odds*
 - Thus, $e^{X\beta}$ gives you the *odds*, $o = \frac{p}{1-p}$
 - To get probability, p, we can calculate $p = \frac{o}{1+o}$
- Interpretation: for a one-unit increase in x_i
 - the *log odds* for y = 1 increase by β (same as the OLS), holding others at a fixed value
 - the *odds* for y = 1 increase by (e^β 1) times of baseline odds (ie, odds before the change), holding others at a fixed value
 - $log(o2) log(o1) = \beta$
 - $log(o2/o1) = \beta$
 - $o2/o1 = e^{\beta}$
 - $o2 o1 = (e^{\beta} 1) * o1$
 - you need to sum all relevant log odds before converting to probability
 - Click here for a review

Implement logit regression



• The logistic model is related to our previous linear models as such:

Both linear and logit models are under the class of General Linear Models (GLMs)

- To regress a GLM, we use the glm() command.
- To run a logit regression:

mod <- $glm(y \sim x1 + x2 + x3 + ..., data = df, family = binomial)$

summary(mod)

family = binomial is what sets the model to be a logit

In fact, the lm() we have been using is actually glm() when you specify the
option family = gaussian

Example logit regression



Do holidays increase the likelihood that a department more than doubles its store's average weekly sales across departments?

```
# Create the binary variable from Walmart sales data
df$double <- ifelse(df$Weekly_Sales > df$store_avg * 2, 1, 0)
model1 <- glm(double ~ IsHoliday, data = df, family = binomial)
tidy(model1)</pre>
```

Holidays increase the odds... but by how much?

- There are two ways to interpret this:
 - 1. Coefficient by coefficient
 - 2. In total

Interpretting specific coefficients



 $logodds(Double\ sales) = -3.45 + 0.54 IsHoliday$

- Interpreting specific coefficients is easiest done manually
- Odds for the *IsHoliday* coefficient are exp(0.54) = 1.72
 - This means that having a holiday modifies the baseline (i.e., non-Holiday) odds by 1.72 to 1
 - Where 1 to 1 is considered no change (exp(0) = 1)
 - Baseline exp(-3.45) is 0.032 to 1

Automating the above: exp(coef(model1))

(Intercept) IsHolidayTRUE
0.03184725 1.71367497

Interpretting in total



- It is important to note that log odds are additive
 - So, calculate a new log odd by plugging in values for variables and adding it all up
 - Holiday: -3.45 + 0.54 * 1 = -2.91
 - No holiday: -3.45 + 0.54 * 0 = -3.45
- Then calculate odds and log odds like before
 - With holiday: exp(-2.91) = 0.055
 - Without holiday: exp(-3.45) = 0.032
 - Ratio of holiday to without: 1.72!
 - This is the individual log odds for holiday

We need to specify values to calculate log odds in total

Converting to probabilities



• We can calculate a probability at any given point using the log odds

$$Probability = rac{odds}{odds+1}$$

- Probability of double sales...
 - With a holiday: 0.055 / (0.055 + 1) = 0.052
 - Without a holiday: 0.032 / (0.032 + 1) = 0.031

These are easier to interpret, but require specifying values

Using predict() to simplify it



- predict() can calculate log odds and probabilities for us with minimal effort
 - Specify type = "response" to get probabilities

```
IsHoliday <- c(FALSE, TRUE)
test_data <- as.data.frame(IsHoliday)
predict(model1, test_data) # Log odds if no type = "response"
## 1 2
## -3.446804 -2.908164</pre>
```

predict(model1, test_data, type = "response") #probabilities

1 2 ## 0.03086431 0.05175146

- Here, we see the baseline probability is 3.1%
- The probability of doubling sales on a holiday is higher, at 5.2%

R practice: Logit



- A continuation of last session's practices answering:
 - Is Walmart more likely to see a year over year decrease in quarterly revenue during a recession?
- Practice using mutate() and glm()
- Do exercises 1 and 2 in the practice file
 - R Practice

What about more complex model?



##	#	A tibble: 4 x	5			
##		term	estimate	<pre>std.error</pre>	statistic	p.value
##		<chr></chr>	<dbl></dbl>	<dbl></dbl>	<dbl></dbl>	<dbl></dbl>
##	1	(Intercept)	-1.78	0.0673	-26.4	1.93e-153
##	2	IsHolidayTRUE	0.370	0.0284	13.0	8.80e- 39
##	3	Temperature	-0.0108	0.000470	-23.0	1.70e-117
##	4	Fuel_Price	-0.309	0.0196	-15.8	6.20e- 56

Odds
exp(coef(model2))

##	(Intercept)	IsHolidayTRUE	Temperature	Fuel_Price
##	0.1692308	1.4483570	0.9892316	0.7340376

We need to specify values for all inputs to determine probabilities, ie, the impact of each input depends on the values of the others!

Probabilities



Month	IsHoliday	Probability		
9	FALSE	0.0266789		
9	TRUE	0.0374761		
12	FALSE	0.0398377		
12	TRUE	0.0586483		

A bit easier: Marginal effects



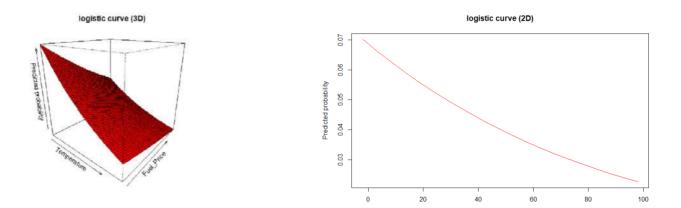
Marginal effects tell us the change in our output for a change of 1 unit to an input

- Marginal effects are partial derivatives (slope of the tangent line) of a regression equation with respect to each variable in the model for each unit in the data
 - In OLS regression with no interactions or higher-order term (such as polynomial functions with quadratic terms x^2), the estimated coefficients are marginal effects
- Using package:margins, we can calculate marginal effects
- There are a few types that we could calculate:
 - An *Average Marginal Effect* tells us what the average effect of an input is across all values in our data
 - This is the default method in the package
 - We can also specify a specific value to calculate marginal effects at

Logistic 2D/3D curve



Marginal effect means the partial derivative of any given point on the surface



Temperature

Marginal effects in action



```
# Calculate Average Marginal Effects (AME)
# It will take a while
library(margins)
m <- margins(model2)
m</pre>
```

Temperature Fuel_Price IsHoliday
-0.0003377 -0.009644 0.01334

- By default, the margins() returns the Average Marginal Effect (AME)
- A holiday increases the probability of doubling by a flat 1.33%
 - Not too bad when you consider that the probability of doubling is 3.23%
- If the temperature goes up by 1°F (0.55°C), the probability of doubling changes by -0.03%
- If the fuel price increases by 1 USD for 1 gallon of gas, the probability of doubling changes by -0.96%

package:margins niceties



We can get some extra information about our marginal effects through summary():

summary(m) %>%
 html_df()

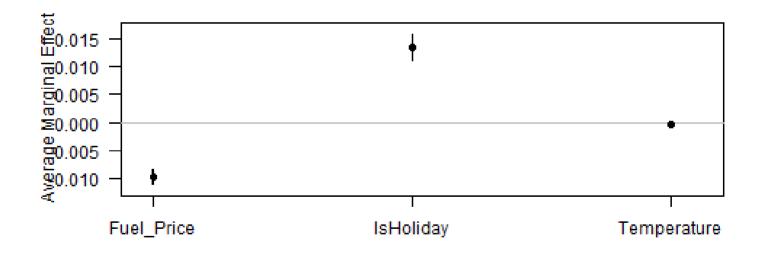
factor	AME	SE	Z	р	lower	upper
Fuel_Price	-0.0096438	0.0006163	-15.64800	0	-0.0108517	-0.0084359
IsHoliday	0.0133450	0.0011754	11.35372	0	0.0110413	0.0156487
Temperature	-0.0003377	0.0000149	-22.71255	0	-0.0003668	-0.0003085

- Those p-values work just like with our linear models
- We also get a confidence interval

Plotting marginal effects



Note: The `which...` part is absolutely necessary at the moment # due to a bug in the package (mismatch of factors and AME values # you may try to remove `which...` to see what happened plot(m, which = summary(m)\$factor)



Marginal effects at a specified value

```
margins(model2, at = list(IsHoliday = c(TRUE, FALSE)),
            variables = c("Temperature", "Fuel_Price")) %>%
    summary() %>%
    html_df()
```

factor	IsHoliday	AME	SE	Z	р	lower	upper
Fuel_Price	FALSE	-0.0093401	0.0005989	-15.59617	0	-0.0105139	-0.0081664
Fuel_Price	TRUE	-0.0131335	0.0008717	-15.06650	0	-0.0148420	-0.0114250
Temperature	FALSE	-0.0003271	0.0000146	-22.46024	0	-0.0003556	-0.0002985
Temperature	TRUE	-0.0004599	0.0000210	-21.92927	0	-0.0005010	-0.0004188

- specify the values through *at* argument, *variables* for the features of changes
 - On a holiday, if fuel price changes by 1 unit, the probability of doubling changes by -1.31%

Marginal effects at a specified value

```
margins(model2, at = list(Temperature = c(0, 20, 40, 60, 80)),
            variables = c("IsHoliday")) %>%
    summary() %>%
    html_df()
```

factor	Temperature	AME	SE	Z	р	lower	upper
IsHoliday	0	0.0234484	0.0020168	11.62643	0	0.0194955	0.0274012
IsHoliday	20	0.0194072	0.0016710	11.61387	0	0.0161320	0.0226824
IsHoliday	40	0.0159819	0.0013885	11.51001	0	0.0132604	0.0187033
IsHoliday	60	0.0131066	0.0011592	11.30623	0	0.0108345	0.0153786
IsHoliday	80	0.0107120	0.0009732	11.00749	0	0.0088046	0.0126193

At 0 temperature, a holiday will result in 2.34% increase of probability of doubling.

Today's Application: Shipping delays

The question



Can we leverage global weather data to predict shipping delays?



A bit about shipping data



- WRDS doesn't have shipping data
- There are, however, vendors for shipping data, such as:

MarineTraffic

- They pretty much have any data you could need:
 - Over 650,000 ships tracked using ground and satellite based AIS
 - AIS: Automatic Identification System
 - Live mapping
 - Weather data
 - Fleet tracking
 - Port congestion
 - Inmarsat support for ship operators

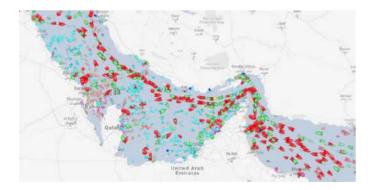
What can we see from naval data?



Cruise: Quantum of the Seas

state and a second seco	JANTUM OF THE SEAS	ADD 10 FLET	CREATE NOTIFICATIONS
Vbyage Information		Latest Polition	
MYY PKG Intel - Loose And Structure - Al Artin 2000 And Antonia Antonia - VARY 1104(20)	MY PEN O ETA 2010-Inite data (7 anti-ria V Russing Educations	Poplian Records 2000-01-02 98:11 VTC 14 minutes ago virtualist Local Tome 2020-01-29 54:11 LT (VTC +8) Area 1800 - Malaista Strait Current Pirt Picell 44:AMG Latitude / Longitude 2.30:1117 - (181-2339)	Kasta Europai Anality Josa Burtelane Europaine Materica Liter Mark
regional (14: 2020-01-20 60:00 L1:UTC + Calculated ETA:	0.	Blance: Movered Speed/Counter 6 km / 312 * Am Source 211 6 40064 NECARRY VETERLE	***

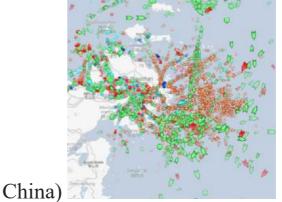
Oil tankers in the Persian gulf



Busiest port for transshipment (Singapore)



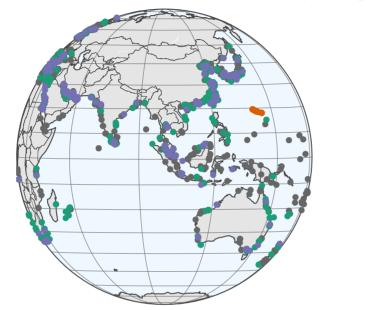
Busiest ports by containers and tons (Shanghai & Ningbo-Zhoushan,



28 / 52

Singaporean owned container and tanker ships, August 31, 2018







- Cargo
- Tanker
- **TYPHOON**
- Port
- Cargo
- Tanker
- TYPHOON

Code for last slide's map

```
SINGAPORE MANAGEMENT
```

```
library(plotly) # for plotting
library(RColorBrewer) # for colors
# plot with boats, ports, and typhoons
# Note: geo is defined in the code file -- it controls layout
palette = brewer.pal(8, "Dark2")[c(1, 8, 3, 2)]
p <- plot_geo(colors = palette) %>%
add_markers(data = df_ports, x = ~port_lon, y = ~port_lat, color = "Port") %>%
add_markers(data = df_Aug31, x = ~lon, y = ~lat, color = ~ship_type,
text = ~paste('Ship name', shipname)) %>%
add_markers(data = typhoon_Aug31, x = ~lon, y = ~lat, color="TYPHOON",
text = ~paste("Name", typhoon_name)) %>%
layout(showlegend = TRUE, geo = geo,
title = 'Singaporean owned container and tanker ships, August 31, 2018')
p
```

- plot_geo() is from package:plotly
- add_markers() adds points to the map
- layout() adjusts the layout
- Within geo, a list, the following makes the map a globe
 - projection = list(type = "orthographic")

What might matter for shipping?

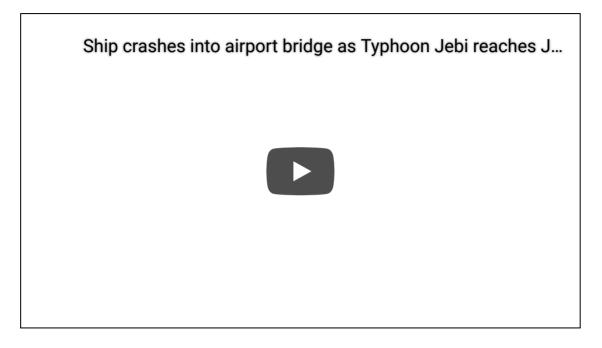


What observable events or data might provide insight as to whether a naval shipment will be delayed or not?

1. Typhoons



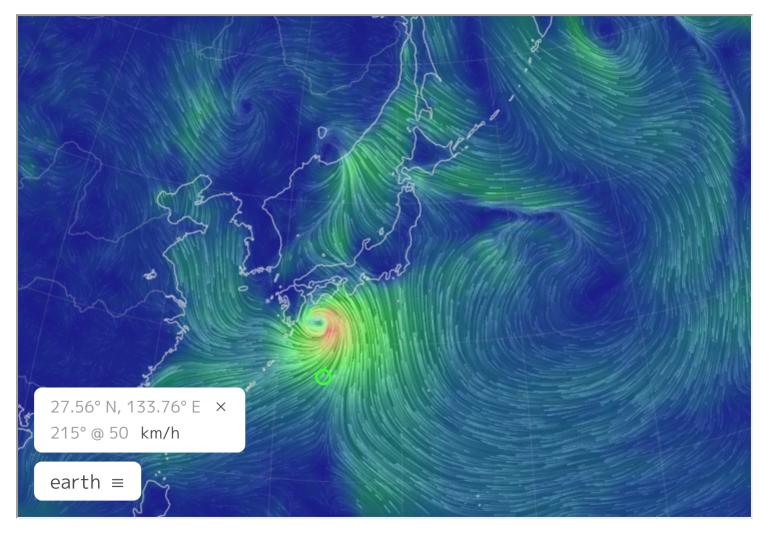




click to play on youtube

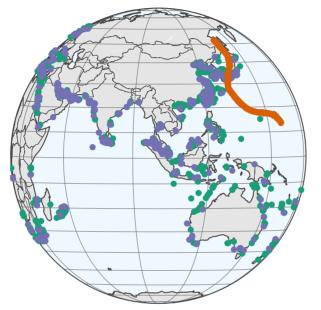






Typhoons in the data Singaporean container/tanker ships, September 4, 2018, evening

SMU GAPORE MANAGEMEN School of Accountancy



- Cargo
- Tanker
- Typhoon Jebi
- Cargo
- Tanker
- Typhoon Jebi

Code for last slide's map



• This map is made the same way as the first map

R Practice on mapping



- Practice interactive mapping using typhoon data
 - 1 map using package:plotly
- Bonus practice
 - 1 map using package:leaflet
- There is another interactive mapping package:sf but its installation is not friendly on a Mac
- Do exercises 3 and 4 in the practice file
 - R Practice

Predicting delays due to typhoons

Data



- If the ship will report a delay of at least 3 hours some time in the next 12-24 hours
- What we have:
 - Ship location
 - Typhoon location
 - Typhoon wind speed

We need to calculate distance between ships and typhoons

Distance for geo



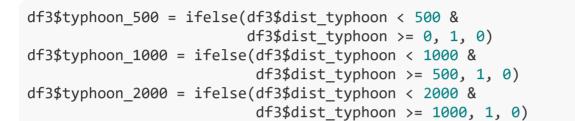
- There are a number of formulas for this
 - *Haversine* for a simple calculation
 - Vincenty's formulae for a complex, incredibly accurate calculation
 - Accurate within **0.5mm**
- Use distVincentyEllipsoid() from package:geosphere to get a reasonably quick and accurate calculation
 - Calculates distance between two sets of points, x and y, structured as matrices
 - Matrices must have longitude in the first column and latitude in the second column
 - Provides distance in meters by default

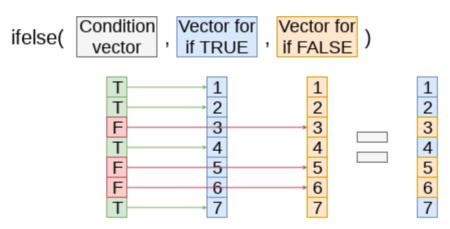
```
library(geosphere)
x <- as.matrix(df3[ , c("lon", "lat")]) # ship location
y <- as.matrix(df3[ , c("ty_lon", "ty_lat")]) # typhoon location
df3$dist_typhoon <- distVincentyEllipsoid(x, y) / 1000 # convert to KM</pre>
```

Clean up



• Some indicators to cleanly capture how far away the typhoon is





Do typhoons delay shipments?



```
##
## Call:
\#\# glm(formula = delayed ~ typhoon 500 + typhoon 1000 + typhoon 2000,
      family = binomial, data = df3)
##
##
## Deviance Residuals:
      Min
                10 Median
                                         Max
##
                                 30
## -0.2502 -0.2261 -0.2261 -0.2261
                                      2.7127
##
## Coefficients:
               Estimate Std. Error z value Pr(>|z|)
##
## (Intercept) -3.65377 0.02934 -124.547 <2e-16 ***
## typhoon 500 0.14073 0.16311
                                  0.863 0.3883
## typhoon 1000 0.20539 0.12575 1.633 0.1024
## typhoon 2000 0.16059 0.07106 2.260 0.0238 *
## ---
## Signif. codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.' 0.1 ' ' 1
##
## (Dispersion parameter for binomial family taken to be 1)
##
##
      Null deviance: 14329 on 59184 degrees of freedom
## Residual deviance: 14322 on 59181 degrees of freedom
##
     (3866 observations deleted due to missingness)
## AIC: 14330
##
```



```
odds1 <- exp(coef(fit1))
odds1</pre>
```

(Intercept) typhoon_500 typhoon_1000 typhoon_2000
0.02589334 1.15111673 1.22800815 1.17420736

 Ships 1,000 to 2,000 km from a typhoon have a 17% increased odds of having a delay

```
m1 <- margins(fit1)
summary(m1)</pre>
```

factor AME SE z p lower upper ## typhoon_1000 0.0052 0.0032 1.6322 0.1026 -0.0010 0.0115 ## typhoon_2000 0.0041 0.0018 2.2570 0.0240 0.0005 0.0076 ## typhoon 500 0.0036 0.0042 0.8626 0.3883 -0.0046 0.0117

Ships 1,000 to 2,000 km from a typhoon have an extra 0.41% chance of having a delay (baseline of 2.5%, ie, all x = 0)



 Alternatively, we may calculate actual probability by summing up all relevant log odds.

(Intercept) typhoon_500 typhoon_1000 typhoon_2000
0.02523980 0.02894356 0.03081733 0.02950702

- Ships 1,000 to 2,000 km from a typhoon have a 3% chance of having a delay (baseline of 2.5%)
- Note the calculation of odds for each scenario:
 - all typhoon = 0: α
 - typhoon_ $500 = 1: \alpha + \beta 1$
 - typhoon_ $1000 = 1: \alpha + \beta 2$
 - typhoon_2000 = 1: $\alpha + \beta 3$

What about typhoon intensity?



- Hong Kong's typhoon classification: Official source
 - 1. 41-62 km/h: Tropical depression
 - 2. 63-87 km/h: Tropical storm
 - 3. 88-117 km/h: Severe tropical storm
 - 4. 118-149 km/h: Typhoon
 - 5. 150-184 km/h: Severe typhoon
 - 6. 185+km/h: Super typhoon

```
table(df3$HK_intensity)
```

##

##	(-1,41]	(41,62]	(62,87]	(87,117]	(117,149]	(149,999]
##	3398	12039	12615	11527	2255	21141

Typhoon intensity and delays



## # A tibble: 10 x 5								
##		term	estimate	<pre>std.error</pre>	statistic	p.value		
##		<chr></chr>	<dbl></dbl>	<dbl></dbl>	<dbl></dbl>	<dbl></dbl>		
##	1	(Intercept)	-3.65	0.0290	-126.	0		
##	2	typhoon_500:Weak	-0.00879	0.213	-0.0413	0.967		
##	3	typhoon_500:Moderate	0.715	0.251	2.86	0.00430		
##	4	typhoon_500:Super	-8.91	123.	-0.0726	0.942		
##	5	typhoon_1000:Weak	0.250	0.161	1.55	0.121		
##	6	<pre>typhoon_1000:Moderate</pre>	0.123	0.273	0.451	0.652		
##	7	typhoon_1000:Super	-0.0269	0.414	-0.0648	0.948		
##	8	typhoon_2000:Weak	0.182	0.101	1.80	0.0723		
##	9	<pre>typhoon_2000:Moderate</pre>	0.0253	0.134	0.189	0.850		
##	10	typhoon_2000:Super	0.311	0.136	2.29	0.0217		

Moderate storms predict delays when within 500km

Super typhoons predict delays when 1,000 to 2,000km away



odds2 <- exp(coef(fit2))
odds2[c(1, 3, 10)]</pre>

##	(Intercept)	typhoon_500:Moderate	typhoon_2000:Super
##	0.02589637	2.04505487	1.36507575

- Ships within 500km of a moderately strong storm have 104% higher *odds* of being delayed
- Ships 1,000 to 2,000km from a super typhoon have 36% higher *odds*



##	(Intercept) typ	phoon_500:Moderate	typhoon_2000:Super
##	0.02524268	0.05029586	0.03414352

- Ships within 500km of a moderately strong storm have a 5% chance of being delayed (baseline: 2.5%)
- Ships 1,000 to 2,000km from a super typhoon have a 3.4% chance

Marginal effects



m2 <- margins(fit2)
summary(m2) %>%
html_df()

factor	AME	SE	Z	р	lower	upper
Moderate	0.0007378	0.0006713	1.0990530	0.2717449	-0.0005779	0.0020535
Super	-0.0050241	0.0860163	-0.0584087	0.9534231	-0.1736129	0.1635647
typhoon_1000	0.0035473	0.0036186	0.9802921	0.3269420	-0.0035450	0.0106396
typhoon_2000	0.0039224	0.0017841	2.1985908	0.0279070	0.0004257	0.0074191
typhoon_500	-0.0440484	0.6803640	-0.0647424	0.9483791	-1.3775373	1.2894405
Weak	0.0009975	0.0005154	1.9353011	0.0529534	-0.0000127	0.0020077

- Delays appear to be driven mostly by 2 factors:
 - 1. A typhoon 1,000 to 2,000 km away from the ship
 - 2. Weak typhoons

Summary of Session 7

For next week

Schol of Accountancy

- Try to replicate the code
- Continue your Datacamp career track
- Continue with your project
 - You can start to explore models

R Coding Style Guide



Style is subjective and arbitrary but it is important to follow a generally accepted style if you want to share code with others. I suggest the The tidyverse style guide which is also adopted by Google with some modification

- Highlights of **the tidyverse style guide**:
 - *File names*: end with .R
 - *Identifiers*: variable_name, function_name, try not to use "." as it is reserved by Base R's S3 objects
 - *Line length*: 80 characters
 - *Indentation*: two spaces, no tabs (RStudio by default converts tabs to spaces and you may change under global options)
 - Spacing: x = 0, not x=0, no space before a comma, but always place one after a comma
 - *Curly braces* {}: first on same line, last on own line
 - Assignment: use <-, not = nor ->
 - *Semicolon(;)*: don't use, I used once for the interest of space
 - *return()*: Use explicit returns in functions: default function return is the last evaluated expression
 - *File paths*: use relative file path "../../filename.csv" rather than absolute path "C:/mydata/filename.csv". Backslash needs \\

R packages used in this slide



This slide was prepared on 2021-09-08 from Session_7s.Rmd with R version 4.1.1 (2021-08-10) Kick Things on Windows 10 x64 build 18362 🔯.

The attached packages used in this slide are:

##	geosphere RC	ColorBrewer	plotly	margins	rlang	broom
##	"1.5-10"	"1.1-2"	"4.9.4.1"	"0.3.26"	"0.4.11"	"0.7.9"
##	lubridate	forcats	stringr	dplyr	purrr	readr
##	"1.7.10"	"0.5.1"	"1.4.0"	"1.0.7"	"0.3.4"	"2.0.1"
##	tidyr	tibble	ggplot2	tidyverse	kableExtra	knitr
##	"1.1.3"	"3.1.3"	"3.3.5"	"1.3.1"	"1.3.4"	"1.33"