Minnesota BART

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An helicopter view on VARs

- Vector autoregressive (VAR) models are the main workhorse in empirical macroeconomics: forecasting, impulse response and policy analysis.

- For m-dimensional y_t and p lags, the standard Gaussian VAR model is defined as

$$y_t = \mu + \sum_{l=1}^{p} \Phi_l y_{t-l} + \epsilon_t, \quad \epsilon_t \ \text{iid} \ N(0, \Sigma_t),$$

  for $t = 1, \ldots, T$.

- Intercept $+ np$ regressors per equation.

- $n(1 + np)$ parameters in $(\mu, \Phi_1, \ldots, \Phi_p)$.

Evolution of Bayesian VAR models

- Small/medium size VAR
  - Doan, Litterman and Sims (1984/1986) - Minnesota prior
  - Kadiyala and Karlsson (1993/1997) - MC + MCMC
  - Lopes, Moreira and Schmidt (1999) - VAR + TVP via SIR
  - Primiceri (2005) - Structural VAR + TVP + SV
- Large/huge size VAR
  - Bańbura et al. (2010) - Large VAR
  - Koop and Korobilis (2013) - Large VAR + TVP
  - Carriero et al. (2019) - Large VAR + SV
  - Kastner and Huber (2020) - Huge VAR (sparsity)
- Nonparametric VAR
  - Huber and Rossini (2022) - BART
  - Clark et al. (2023) - BART
  - Huber and Koop (2024) - Dirichlet process mixture (DPM)
  - Hauzenberger et al. (2024) - Gaussian processes (GP)

Minnesota Prior

Let us focus on the 1st equation of the VAR(p) model

$$y_{t1} = \mu_1 + \sum_{l=1}^{p} \sum_{j=1}^{m} \phi_{l,1j} y_{t-l,j} + \epsilon_{t1}$$

The Minnesota prior induces an random walk behavior for y_{t1}:

$$E(\phi_{1,11}) = 1 \quad \text{and} \quad E(\phi_{l,1j}) = 0 \ \ \forall l, j \neq 1$$

and

$$V(\phi_{l,1j}) = \begin{cases} \frac{\lambda_1}{l^{\lambda_3}} & j = 1 \\ \frac{\lambda_2}{l^{\lambda_3}} & j \neq 1 \end{cases}$$

Doan, Litterman and Sims (1984) Forecasting and conditional projection using realistic prior distributions. *Econometric reviews*, 3(1),1-100. Litterman (1986) Forecasting with Bayesian vector autoregressions - five years of experience. *JBES*, 4(1), 25-38.

Modeling Σ_t

Recall the VAR(p) structure

$$y_t = \mu + \sum_{l=1}^{p} \Phi_l y_{t-l} + \epsilon_t, \quad \epsilon_t \text{ iid } N(0, \Sigma_t),$$

Stochastic volatility specifications are crucial for producing accurate density forecasts, Chan (2023).

We model Σ_t via a factor analysis approach:

$$\Sigma_t = \Lambda \Omega_t \Lambda_t + H_t$$

where

- Λ is an $n \times r$ factor loadings matrix ($r \ll n$),
- $H_t = \text{diag}(h_{t1}, \ldots, h_{tn})$, and
- $\Omega_t = \text{diag}(\omega_{t,n+1}, \ldots, \omega_{t,n+r})$.

Our contribution: Minnesota BART

Two-fold extension of Huber and Rossini (2022) and Clark et al. (2023):

- Allowing for high-dimensional data and variable selection via the approach by Linero (2018), and
- Introducing a Minnesota-type shrinkage specification into the BART node splitting selection.

The BAVART model

We replace the linear autoregressive structure by a nonlinear one:

$$y_t \quad = \quad G(x_t) + \epsilon_t, \quad \epsilon_t \sim \quad \text{iid} \;\; N(0, \Sigma_t)$$

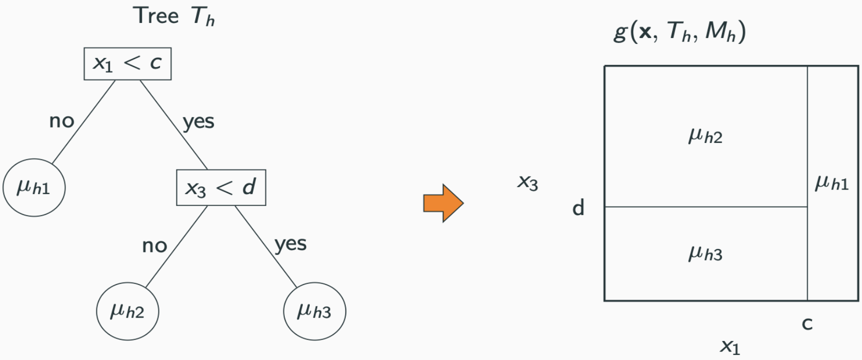
- $y_t = (y_{t1}, \ldots, y_{tn})'$.
- $x_t = (y'_{t-1}, \ldots, y'_{t-p})$.
- $G(x_t) = (g_1(x_t), \ldots, g_n(x_t))'$ is a n-dimensional vector BART mean fucntions.

The full (hierarchical) model

$$
\begin{aligned}
y_t &= G(x_t) + \epsilon_t \\
\epsilon_t &= \Lambda f_t + \eta_t \\
f_t &\sim N(0, \Omega_t) \\
\eta_t &\sim N(0, H_t),
\end{aligned}
$$

The components of H_t and Ω_t follow standard stochastic volatility (SV) models.

A brief introduction to a tree model



Leaf/End node parameters
$M_h = (\mu_{h1}, \mu_{h2}, \mu_{h3})$

Partition $\mathcal{A}_h = \{\mathcal{A}_{h1}, \mathcal{A}_{h2}, \mathcal{A}_{h3}\}$

$g(\mathbf{x}, T_h, M_h) = \mu_{ht}$ if $\mathbf{x} \in \mathcal{A}_{ht}$ (for $1 \leq t \leq b_h$).

The vector of mean functions, $G(x_t)$

Each component of $G(x_t)$ is modeled as a decision tree ensemble:

$$g(x_t) = \sum_{m=1}^{M} g_m\left(x_t; \mathcal{T}_m, \mathcal{M}_m\right),$$

where

- $\mathcal{T}_m$ denotes a *decision tree* shape,
- $\mathcal{M}_m$ denotes a collection of *leaf node parameters*, and
- $g_m(x_t; \mathcal{T}_m, \mathcal{M}_m)$ is a *regression tree function* that returns the prediction associated to x_t for the pair $(\mathcal{T}_m, \mathcal{M}_m)$.

Prior specification:

$$\pi(\mathcal{T}_r, \mathcal{M}_r) \sim \pi_{\mathcal{T}}(\mathcal{T}_r)\, \pi_{\mathcal{M}}(\mathcal{M}_r \mid \mathcal{T}_r)$$

BART prior

BART proceeds by placing a prior on the regression trees.

Prior independence, given the model hyperparameters θ:

$$\pi\left((\mathcal{T}_1, \mathcal{M}_1), \ldots, (\mathcal{T}_M, \mathcal{M}_M) \mid \theta\right) = \prod_{m=1}^{M} \pi_{\mathcal{T}}(\mathcal{T}_m \mid \theta)\pi_{\mathcal{M}}(\mathcal{M}_m \mid \mathcal{T}_m).$$

The prior distribution for the trees $\pi_{\mathcal{T}}$ consists of three steps:

1. A prior on the shape of the tree $\mathcal{T}$;
2. A prior for the splitting rules that first selects a predictor by sampling $k_b \sim \text{Categorical}(s)$ where $s = (s_1, \ldots, s_k)^\top$ is a probability vector.
3. A prior on the splitting rules $[x_{k_b} \leq C_b]$ for each branch node of the tree, given k_b

BART splitting rule

- Select a predictor by sampling $k_b \sim \text{Categorical}(s)$, where

$$s = (1/k, \ldots, 1/k).$$

- What if $m = 100$ and $p = 5$?
  Linero (2018): break down in the presence of larger number of potentially irrelevant features.

- Bias will increase as k increases (VAR: $k = mp$).

- Credible intervals will widen as well.

Exercise: BART in a high dimensional setting

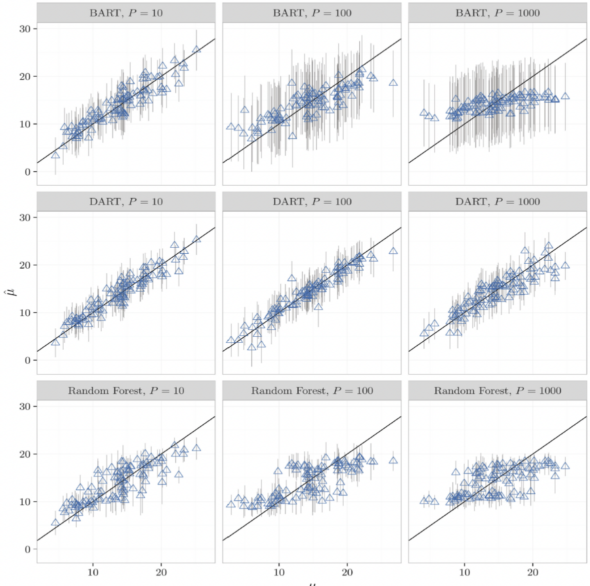
Consider the following nonlinear regression

$$\begin{aligned} y_i &= g(x_i) + \epsilon_t, \\ g(x_i) &= 10 sin(\pi x_{i1} x_{i2}) + 20(x_{i3} - 0.5)^2 + 10 x_{i4} + 5 x_{i5}, \end{aligned}$$

where

- $\epsilon_t \sim \mathcal{N}(0,1)$,
- $T = 100$ observations,
- 5 relevant predictors,
- $k - 5$ irrelevant predictors,
- $k = \{10, 100, 1000\}$.

Predictions degrade as k increases, Linero (2018)



DART prior

If many predictor are potentially irrelevant, why should s_k constant over k?

Linero (2018) propose a solution when k is close or much larger than T:

$$s \sim \text{Dirichlet}(\alpha/k, \dots, \alpha/k)$$

Full Bayesian variable selection:

$$\frac{\alpha}{\alpha + k} \sim \text{Beta}(0.5, 1).$$

Minnesota BART

Rule 1: The past values of a specific variable play a more significant role in predicting its current value compared to the past values of other variables.

Rule 2: The most recent past is considered more influential in predicting current values than events further in the past.

Therefore, for equation n, the prior for the splits probability is defined::

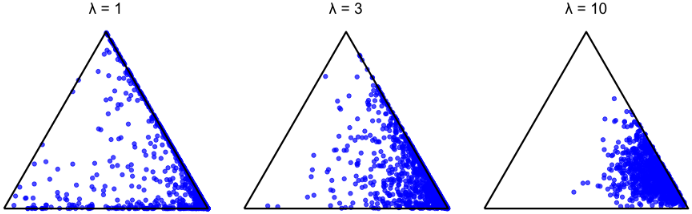
$$(s_{1n}, \dots, s_{kn}) \sim \text{Dirichlet}(\phi_{1n}, \dots, \phi_{kn}) \tag{1}$$

The scale parameters of the Dirichlet distribution are defined are defined as follows:

$$\phi_{in} = \begin{cases} \frac{\lambda_1}{l^2}, & \text{for the scale on the } l\text{-th lag of variable } i, \\ \frac{\lambda_2 \cdot \rho}{l^2}, & \text{for the coefficient on the } l\text{-th lag of variable } j,\ j \neq i, \end{cases}$$

Minnesota BART

Draws from $Dirichlet\left(\lambda, \frac{\lambda}{4}, \frac{\lambda}{9}\right)$. This figure illustrates the effect of varying λ on the concentration parameters of the *Dirichlet* prior on the simplex for $\lambda = (1, 3, 10)$. The vertices of the simplex correspond to one-sparse probability vectors, the edges represent two-sparse vectors, and the interior points indicate denser probability distributions.



Bayesian inference

- **Prior features (in a nutshell)**
  - Choice of prior and hyperparameters from BART literature.
  - Horseshoe prior used for any linear conditional mean coefficients

- **MCMC features (in a nutshell)**
  - Standard MCMC steps from BVAR and BART.
  - Novel updating step for the split probabilities:

$$s_1, \ldots, s_k | \phi, \text{data} \sim \text{Dirichlet}(\phi_1 + n_1, \ldots, \phi_k + n_k)$$

where n_k are the number of splits on predictor k over the ensemble.

Another simulation exercise

- In order to illustrate the properties of the proposed priors we conduct a simulation study where we aim to assess the efficacy of DART-VAR and Minnesota DART in recovering the sparsity pattern.

- We will be reporting the *posterior inclusion probability* as metric for variable selection.

$$\text{PIP}_k = \Pr(\text{predictor } k \text{ appears in the ensemble} \mid \text{data}).$$

- We will report the results of the **first equation** of the estimated dynamic system.

Experiment A

The data is generated from a linear m dimensional VAR(1) model:

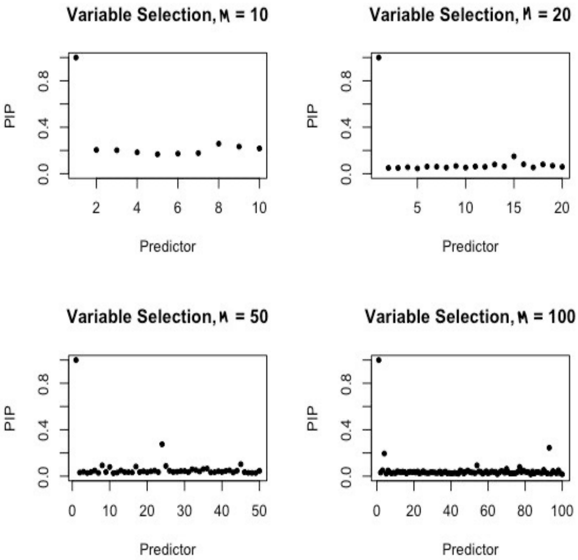
$$\Phi = 0.5I_m$$

and with $m = 10, 20, 50, 100$.

True sparsity: behavior of each variable only depends on its own past.

$m = 100$: Each equation has 99 redundant variables.

Linero's DART prior



Experiment B

The data is generated from a VAR(5) model:

$$\Phi_1 = 0.65 I_m \tag{2}$$

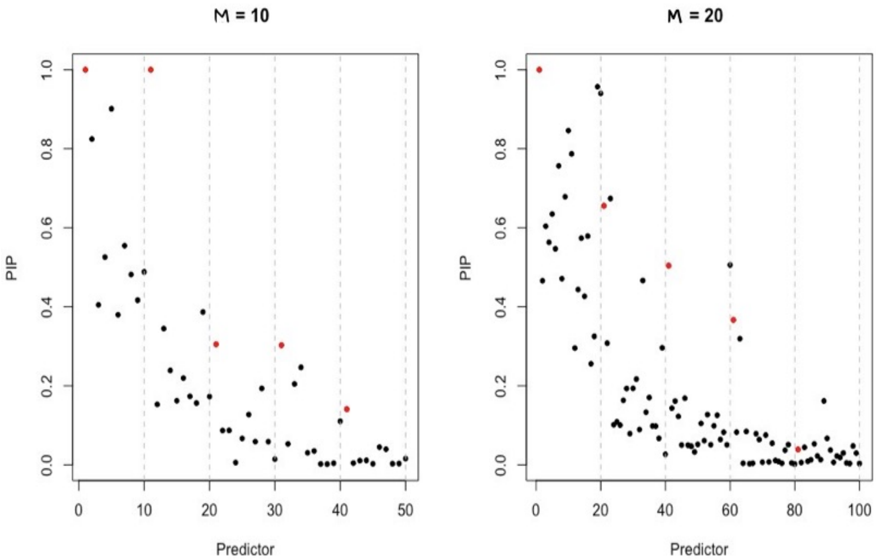
and

$$\Phi_j = (-1)^{j-1}(0.4225) I_m, \quad j = 2, \ldots, 5, \tag{3}$$

for $m = 10$ or $m = 20$.

The coefficients decrease for distant lags, reflecting the conventional wisdom that recent lags hold greater importance than those further in the past.

Minnesota DART prior

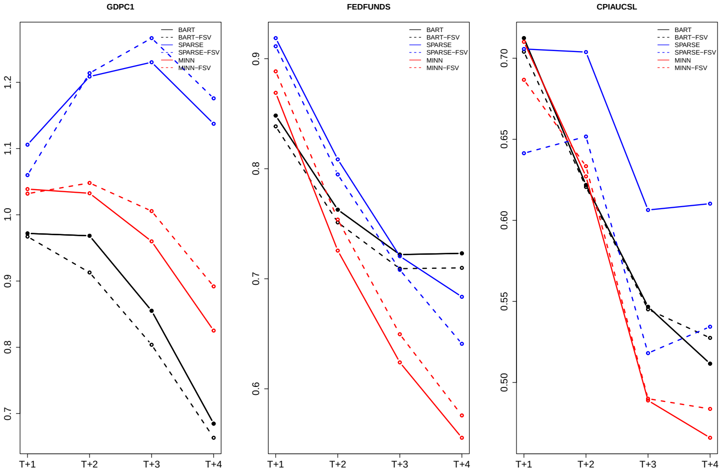


Real data exercise

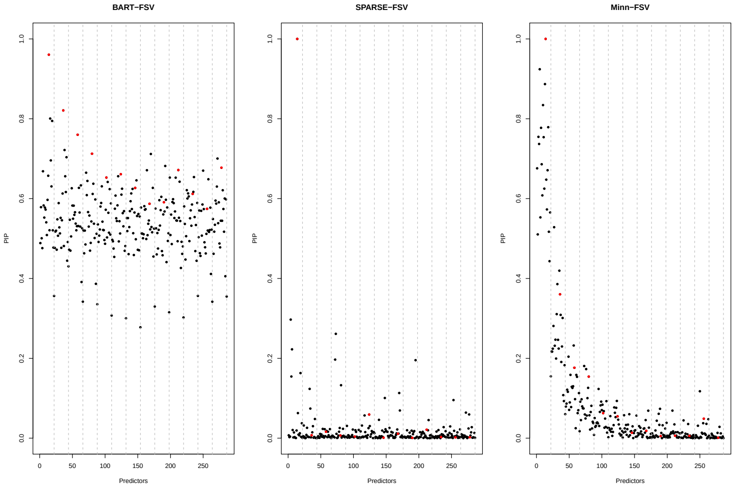
- Data: 22 series from FRED-QD, McCracken and Ng (2016).
- Time span: 1965Q1 - 2019Q4.
- Expanding window: 2005Q1 to 2019Q4.
- Horizons: $h = 1, 2, 3, 4$.
- Evaluation metric: Root mean squared predictive error (RMSPE)
- Baseline model: BVAR-FSV with Minnesota prior

RMSPE

real GDP growth, federal funds rate, inflation
BART/SPARSE/MINN = Uniform/Dirichlet/Minnesota splitting



Inclusion probabilities - CPI



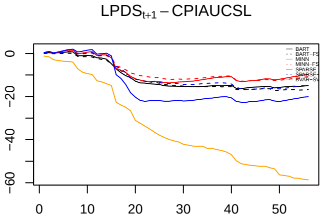
Comparing the priors through log predictive density scores

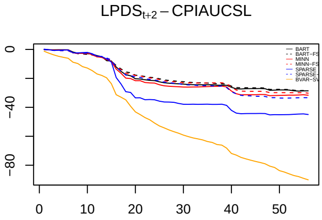
- To obtain a more comprehensive evaluation, we consider a metric that account for for the models ability to predict higher-order moments of the predictive distribution - **Log Predictive Density Score**

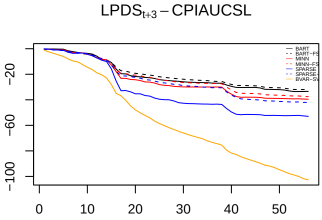
$$\text{LPDS} = \log p(y_{t_0+1}, \ldots, y_T \mid y^{tr}) = \sum_{t=t_0+1}^{T} \log p(y_t \mid y^{t-1})$$

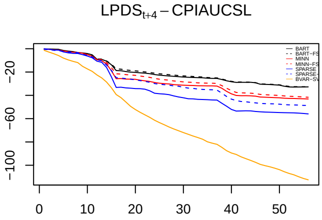
- The first t_0 time series observations, $y^{tr} = (y_1, \ldots, y_{t_0})$, are designated as the "training sample," while the remaining observations, $y_{t_0+1}, \ldots, y_T$, are used for evaluation based on the log predictive density.
- Each probability split prior specification for the mean function is shown under both the homoskedastic and stochastic volatility (SV) settings, where the former is represented by a continuous line and the latter by a dashed line.

Marginal Log Predictive Density Score - CPI

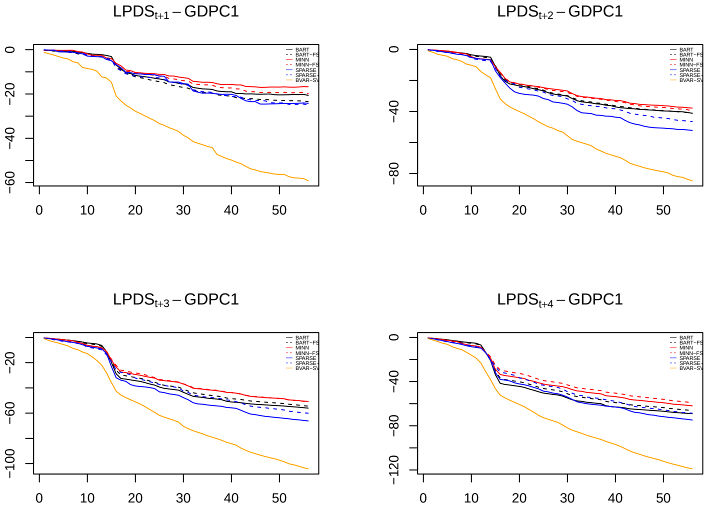




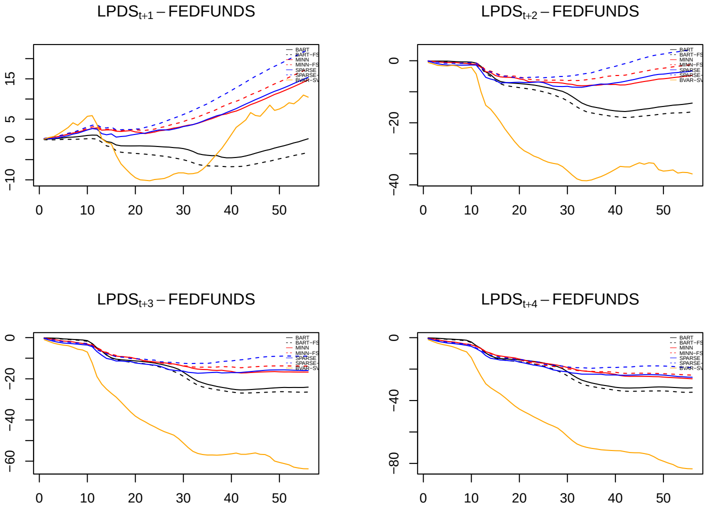




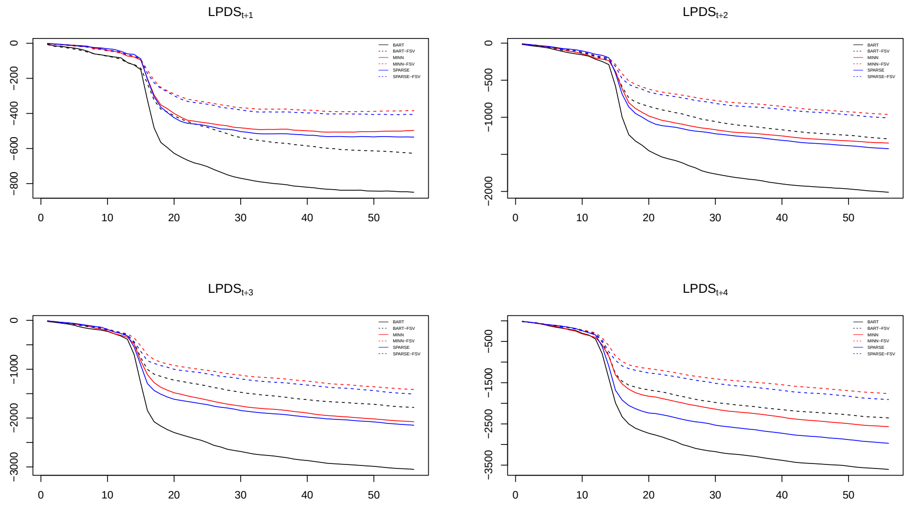
Marginal Log Predictive Density Score - GDPC1



Marginal Log Predictive Density Score - FedFunds



Joint Distribution Log Predictive Density Score



Prior Elicitation

- The choice of λ is of critical importance, as it plays a central role in determining the expected level of shrinkage in the model.
- **Empirical Analysis:** We evaluate different levels of λ using a grid of values ($\lambda_1 = \{1, 3, 5, 10, 20\}$, $\lambda_2 = \{0.5, 1, 1.5, 2.5, 5, 10\}$) and assess their impact on the log-predictive density score relative to the standard BART prior.
- **Impact of λ on Shrinkage Forecasting:** Higher values of λ lead to a more gradual decay in posterior inclusion probabilities, preserving the influence of lags and cross-lags over a longer range. This highlights the importance of carefully selecting λ, as it directly affects variable selection, model interpretability, and forecasting accuracy.

Prior Elicitation : Posterior Inclusion Probability - CPI

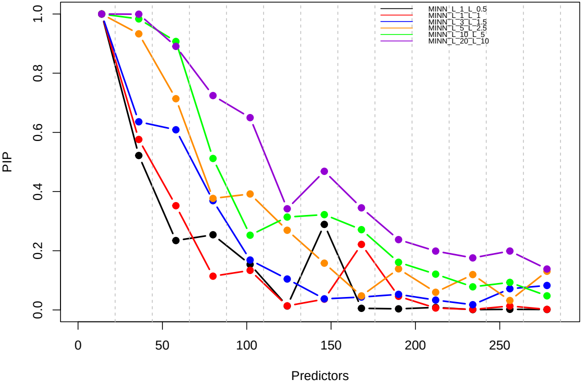


Figure: **Own-Lag Posterior Inclusion Probability**. In-sample Posterior Inclusion Probability (PIP) for the CPI's own lag across different grid values of $\lambda_1 = \{1, 3, 5, 10, 20\}$ and $\lambda_2 = \{0.5, 1, 1.5, 2.5, 5, 10\}$.

Prior Elicitation : Posterior Inclusion Probability - CPI

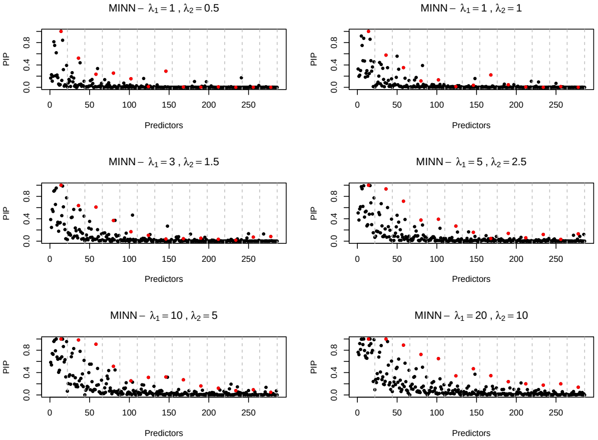


Figure: **Posterior Inclusion Probability for different shrinkage parameters.**

Prior Elicitation

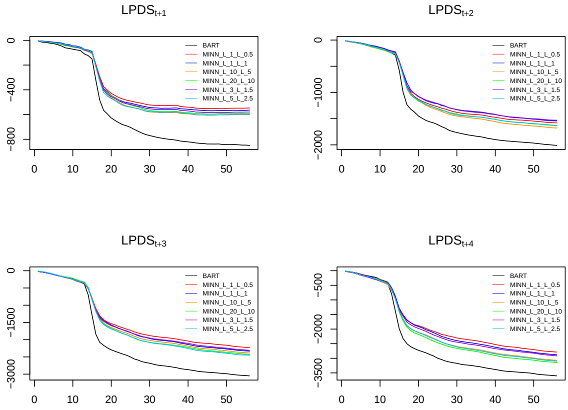


Figure: **Log Predictive Density Score for different shrinkage values.** Cumulative log predictive scores for the last 56 time points (labeled with time index $T - t_0$, where $t_0 = 160$), across different grid values of $\lambda_1 = \{1, 3, 5, 10, 20\}$ and $\lambda_2 = \{0.5, 1, 1.5, 2.5, 5, 10\}$.

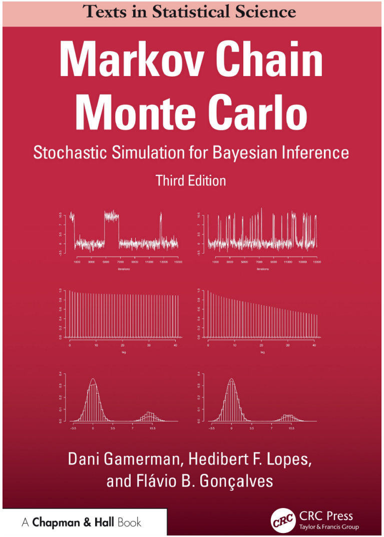
Final Remarks

- **Advancing Multivariate BART for High-Dimensional Analysis:** We introduce a structured prior that enables shrinkage in split probabilities, addressing sparsity and time dependence limitations in high-dimensional VARs.

- **Empirical Validation & Forecasting Gains:** Our priors improve forecast accuracy, particularly for higher-order moments, with the Minnesota specification outperforming the sparse alternative.

- **Broader Applications & Future Directions:** The framework extends to structural analysis (GIRFs, LP) and can be further improved through scalable sampling methods and time-varying parameters.

Gamerman, Lopes and Gonçalves (2026)



Muchísimas gracias por su generosa atención!

Any thoughts?

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