

Table of Contents

Acknowledgments vii

Chapter 1 Introduction

- 1.1 Introduction* 1
- 1.2 What Is a Monte Carlo Study?* 2
 - 1.2.1 Simulating the Rolling of a Die Twice* 2
- 1.3 Why Is Monte Carlo Simulation Often Necessary?* 4
- 1.4 What Are Some Typical Situations Where a Monte Carlo Study Is Needed?* 5
 - 1.4.1 Assessing the Consequences of Assumption Violations* 5
 - 1.4.2 Determining the Sampling Distribution of a Statistic That Has No Theoretical Distribution* 6
- 1.5 Why Use the SAS System for Conducting Monte Carlo Studies?* 7
- 1.6 About the Organization of This Book* 8
- 1.7 References* 9

Chapter 2 Basic Procedures for Monte Carlo Simulation

- 2.1 Introduction* 11
- 2.2 Asking Questions Suitable for a Monte Carlo Study* 12
- 2.3 Designing a Monte Carlo Study* 13
 - 2.3.1 Simulating Pearson Correlation Coefficient Distributions* 13
- 2.4 Generating Sample Data* 16
 - 2.4.1 Generating Data from a Distribution with Known Characteristics* 16
 - 2.4.2 Transforming Data to Desired Shapes* 17
 - 2.4.3 Transforming Data to Simulate a Specified Population Inter-variable Relationship Pattern* 17
- 2.5 Implementing the Statistical Technique in Question* 17
- 2.6 Obtaining and Accumulating the Statistic of Interest* 18
- 2.7 Analyzing the Accumulated Statistic of Interest* 19
- 2.8 Drawing Conclusions Based on the MC Study Results* 22
- 2.9 Summary* 23

Chapter 3 Generating Univariate Random Numbers in SAS

- 3.1 Introduction* 25
- 3.2 RANUNI, the Uniform Random Number Generator* 26
- 3.3 Uniformity (the EQUIDST Macro)* 27
- 3.4 Randomness (the CORRTEST Macro)* 30

- 3.5 *Generating Random Numbers with Functions versus CALL Routines* 34**
- 3.6 *Generating Seed Values (the SEEDGEN Macro)* 38**
- 3.7 *List of All Random Number Generators Available in SAS* 39**
- 3.8 *Examples for Normal and Lognormal Distributions* 45**
 - 3.8.1 *Random Sample of Population Height (Normal Distribution)* 45
 - 3.8.2 *Random Sample of Stock Prices (Lognormal Distribution)* 46
- 3.9 *The RANTBL Function* 51**
- 3.10 *Examples Using the RANTBL Function* 52**
 - 3.10.1 *Random Sample of Bonds with Bond Ratings* 52
 - 3.10.2 *Generating Random Stock Prices Using the RANTBL Function* 54
- 3.10 *Summary* 57**
- 3.12 *References* 58**

Chapter 4 *Generating Data in Monte Carlo Studies*

- 4.1 *Introduction* 59**
- 4.2 *Generating Sample Data for One Variable* 60**
 - 4.2.1 *Generating Sample Data from a Normal Distribution with the Desired Mean and Standard Deviation* 60
 - 4.2.2 *Generating Data from Non-Normal Distributions* 62
 - 4.2.2.1 *Using the Generalized Lambda Distribution (GLD) System* 62
 - 4.2.2.2 *Using Fleishman's Power Transformation Method* 66
- 4.3 *Generating Sample Data from a Multivariate Normal Distribution* 71**
- 4.4 *Generating Sample Data from a Multivariate Non-Normal Distribution* 79**
 - 4.4.1 *Examining the Effect of Data Non-normality on Inter-variable Correlations* 80
 - 4.4.2 *Deriving Intermediate Correlations* 82
- 4.5 *Converting between Correlation and Covariance Matrices* 87**
- 4.6 *Generating Data That Mirror Your Sample Characteristics* 90**
- 4.7 *Summary* 91**
- 4.8 *References* 91**

Chapter 5 *Automating Monte Carlo Simulations*

- 5.1 *Introduction* 93**
- 5.2 *Steps in a Monte Carlo Simulation* 94**
- 5.3 *The Problem of Matching Birthdays* 94**
- 5.4 *The Seed Value* 98**
- 5.5 *Monitoring the Execution of a Simulation* 98**
- 5.6 *Portability* 100**
- 5.7 *Automating the Simulation* 100**
- 5.8 *A Macro Solution to the Problem of Matching Birthdays* 101**
- 5.9 *Full-Time Monitoring with Macros* 103**

5.10 Simulation of the Parking Problem (Rényi's Constant) 105

5.11 Summary 116

5.12 References 116

Chapter 6 Conducting Monte Carlo Studies That Involve Univariate Statistical Techniques

6.1 Introduction 117

6.2 Example 1: Assessing the Effect of Unequal Population Variances in a T-Test 118

6.2.1 Computational Aspects of T-Tests 119

6.2.2 Design Considerations 119

6.3.3 Different SAS Programming Approaches 120

6.3.4 T-Test Example: First Approach 121

6.3.5 T-Test Example: Second Approach 125

6.3 Example 2: Assessing the Effect of Data Non-Normality on the Type I Error Rate in ANOVA 129

6.3.1 Design Considerations 130

6.3.2 ANOVA Example Program 130

6.4 Example 3: Comparing Different R^2 Shrinkage Formulas in Regression Analysis 136

6.4.1 Different Formulas for Correcting Sample R^2 Bias 136

6.4.2 Design Considerations 137

6.4.3 Regression Analysis Sample Program 138

6.5 Summary 143

6.6 References 143

Chapter 7 Conducting Monte Carlo Studies for Multivariate Techniques

7.1 Introduction 145

7.2 Example 1: A Structural Equation Modeling Example 146

7.2.1 Descriptive Indices for Assessing Model Fit 146

7.2.2 Design Considerations 147

7.2.3 SEM Fit Indices Studied 148

7.2.4 Design of Monte Carlo Simulation 148

7.2.4.1 Deriving the Population Covariance Matrix 150

7.2.4.2 Dealing with Model Misspecification 151

7.2.5 SEM Example Program 152

7.2.6 Some Explanations of Program 7.2 155

7.2.7 Selected Results from Program 7.2 160

7.3 Example 2: Linear Discriminant Analysis and Logistic Regression for Classification 161

7.3.1 Major Issues Involved 161

7.3.2 Design 162

7.3.3 Data Source and Model Fitting 164

7.3.4 Example Program Simulating Classification Error Rates of PDA and LR 165

7.3.5 Some Explanations of Program 7.3 168

7.3.6 Selected Results from Program 7.3 172

7.4 Summary 173

7.5 References 174

Chapter 8 Examples for Monte Carlo Simulation in Finance: Estimating Default Risk and Value-at-Risk

- 8.1 Introduction 177***
- 8.2 Example 1: Estimation of Default Risk 179***
- 8.3 Example 2: VaR Estimation for Credit Risk 183***
- 8.4 Example 3: VaR Estimation for Portfolio Market Risk 199***
- 8.5 Summary 211***
- 8.6 References 212***

Chapter 9 Modeling Time Series Processes with SAS/ETS Software

- 9.1 Introduction to Time Series Methodology 213***
 - 9.1.1 Box and Jenkins ARIMA Models 213***
 - 9.1.2 Akaike's State Space Models for Multivariate Times Series 216***
 - 9.1.3 Modeling Multiple Regression Data with Serially Correlated Disturbances 216***
- 9.2 Introduction to SAS/ETS Software 216***
- 9.3 Example 1: Generating Univariate Time Series Processes 218***
- 9.4 Example 2: Generating Multivariate Time Series Processes 221***
- 9.5 Example 3: Generating Correlated Variables with Autocorrelated Errors 228***
- 9.6 Example 4: Monte Carlo Study of How Autocorrelation Affects Regression Results 234***
- 9.7 Summary 243***
- 9.8 References 243***

Index 245