example 12 — Seemingly unrelated regression

Description

sem can be used to estimate seemingly unrelated regression. We will use `auto.dta`, which surely needs no introduction:

```
. sysuse auto
   (1978 Automobile Data)
```


Remarks and examples

Remarks are presented under the following headings:

- Fitting the seemingly unrelated regression model
- Fitting the model with the Builder

Fitting the seemingly unrelated regression model

We fit the following model:

\[
\begin{align*}
\text{mpg} & \leftarrow \text{foreign} \quad \text{displacement} \\
\text{price} & \leftarrow \text{foreign} \quad \text{mpg} \\
\text{weight} & \leftarrow \text{foreign} \quad \text{length}
\end{align*}
\]

```
. sem (price <- foreign mpg displacement) > (weight <- foreign length), cov(e.price*e.weight)
```

Endogenous variables
- price
- weight

Exogenous variables
- foreign
- mpg
- displacement
- length

Fitting target model:

- Iteration 0: log likelihood = -2150.9983
- Iteration 1: log likelihood = -2138.5739
- Iteration 2: log likelihood = -2133.3461
- Iteration 3: log likelihood = -2133.1979
- Iteration 4: log likelihood = -2133.1956
- Iteration 5: log likelihood = -2133.1956
### Example 12 — Seemingly unrelated regression

**Structural equation model**

- **Number of obs** = 74
- **Estimation method** = ml
- **Log likelihood** = -2133.1956

| OIM | Coef. | Std. Err. | z | P>|z| | [95% Conf. Interval] |
|-----|-------|-----------|---|-----|-----------------|
| **Structural** |       |           |   |     |                 |
| price <- foreign | 2940.929 | 724.7311 | 4.06 | 0.000 | 1520.482 - 4361.376 |
| mpg | -105.0163 | 57.93461 | -1.81 | 0.070 | -218.566 - 8.53347 |
| displace-t | 17.22083 | 4.5941 | 3.75 | 0.000 | 8.216558 - 26.2251 |
| _cons | 4129.866 | 1984.253 | 2.08 | 0.037 | 240.8022 - 8018.931 |
| weight <- foreign | -153.2515 | 76.21732 | -2.01 | 0.044 | -302.6347 - -3.868275 |
| length | 30.73507 | 1.584743 | 19.39 | 0.000 | 27.62903 - 33.84111 |
| _cons | -2711.096 | 312.6813 | -8.67 | 0.000 | -3323.94 - -2098.252 |
| var(e.price) | 4732491 | 801783.1 | 3395302 | 6596312 |
| var(e.weight) | 60253.09 | 9933.316 | 43616.45 | 83235.44 |
| cov(e.price, e.weight) | 209268 | 73909.54 | 2.83 | 0.005 | 64407.92 - 354128 |

**LR test of model vs. saturated**: $\text{chi2}(3) = 38.86$, Prob $> \text{chi2} = 0.0000$

**Notes:**

1. Point estimates are the same as reported by

   `. sureg (price foreign mpg displ) (weight foreign length), isure`

   `sureg`’s `isure` option is required to make `sureg` iterate to the maximum likelihood estimate.

2. If you wish to compare the estimated variances and covariances after estimation by `sureg`, type

   `. matrix list e(Sigma)`

   `sureg` does not estimate standard errors on variances and covariances.

3. Standard errors will be different between `sem` and `sureg`. In this case, there is no reason to prefer one set of standard errors over the other, and standard errors are asymptotically equivalent.

   This is a case of exogenous variables only on the right-hand side. When the model being fit is recursive, standard errors produced by `sem` are better than those from `sureg`, both asymptotically and in finite samples.

4. One reason you might want to use `sem` is that `sem` will provide robust standard errors whereas `sureg` does not.

5. Multivariate regression can be viewed as seemingly unrelated regression. You just need to specify the same regressors for each equation. In that case, standard errors reported by `sem` will be the same as those reported by `mvreg` if one applies the multiplicative $\sqrt{\frac{(N - p - 1)}{N}}$ degree-of-freedom adjustment.
Fitting the model with the Builder

Use the diagram above for reference.

1. Open the dataset.
   In the Command window, type
   
   . use http://www.stata-press.com/data/r13/auto

2. Open a new Builder diagram.
   Select menu item Statistics > SEM (structural equation modeling) > Model building and estimation.

3. Change the size of the observed variables’ rectangles.
   From the SEM Builder menu, select Settings > Variables > All Observed....
   In the resulting dialog box, change the first size to .85 and click on OK.

4. Create the four independent variables.
   Select the Add Observed Variables Set tool, , and then click in the diagram about one-fourth of the way in from the left and one-fourth of the way up from the bottom.
   In the resulting dialog box,
   a. select the Select variables radio button (it may already be selected);
   b. use the Variables control to select the four variables in this order: mpg, displacement, foreign, and length;
   c. select Vertical in the Orientation control;
   d. click on OK.
   If you wish, move the set of variables by clicking on any variable and dragging it.

5. Create the two dependent variables.
   Select the Add Observed Variables Set tool, , and then click about two-thirds of the way in from the left and vertically aligned with the top of the length rectangle.
   In the resulting dialog box,
   a. select the Select variables radio button (it may already be selected);
   b. use the Variables control to select the variables price and weight;
   c. select Vertical in the Orientation control;
   d. select the Distances tab;
   e. select .5 (inch) from the Distance between variables control;
   f. click on OK.
   If you wish, move the set of variables by clicking on any variable and dragging it.

6. Create paths from the independent variables to the dependent variables.
   a. Select the Add Path tool, .
   b. Click in the right side of the mpg rectangle (it will highlight when you hover over it), and drag a path to the left side of the price rectangle (it will highlight when you can release to connect the path).
c. Continuing with the tool, create the following paths by clicking first in the right side of the rectangle for the independent variable and dragging it to the left side of the rectangle for the dependent variable:

\[
\begin{align*}
\text{displacement} & \rightarrow \text{price} \\
\text{foreign} & \rightarrow \text{price} \\
\text{foreign} & \rightarrow \text{weight} \\
\text{length} & \rightarrow \text{weight}
\end{align*}
\]

7. Correlate the error terms.
   a. Select the Add Covariance tool, .
   b. Click in the $\epsilon_1$ circle (it will highlight when you hover over it), and drag a covariance to the $\epsilon_2$ circle (it will highlight when you can release to connect the covariance).

8. Clean up.
   If you do not like where a path has been connected to its variables, use the Select tool, , to click on the path, and then simply click on where it connects to a rectangle and drag the endpoint. Similarly, you can change where the covariance connects to the error terms by clicking on the covariance and dragging the endpoint. You can also change the bow of the covariance by clicking on the covariance and dragging the control point that extends from one end of the selected covariance.

   Click on the Estimate button, , in the Standard Toolbar, and then click on OK in the resulting SEM estimation options dialog box.

   You can open a completed diagram in the Builder by typing .

Also see

[SEM] example 13 — Equation-level Wald test
[SEM] sem — Structural equation model estimation command