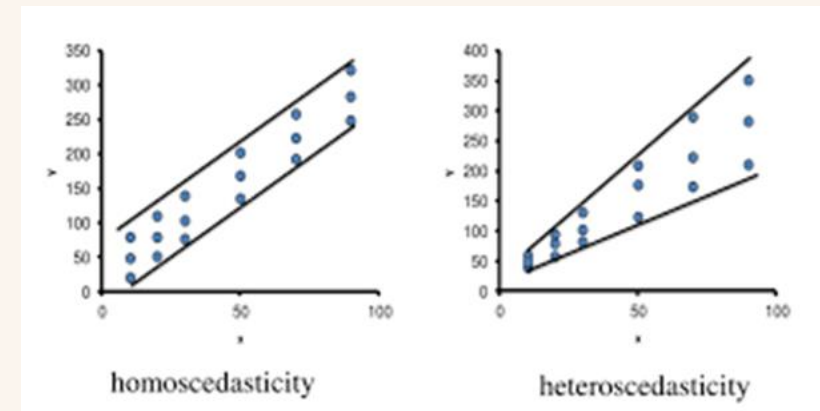


# CFA® Exam Tips – LEVEL II

## Study Tips

### Quantitative Methods

#### Model Misspecification – 3 Violations of Regression Assumptions



Violation	1. (Conditional) Heteroskedasticity	2. Serial Correlation	3. Multicollinearity
Consequences	underestimation of the S.E. of regression coefficients → <i>t</i> -stat inflated → Type I errors increased	inconsistent coefficient estimates, underestimates S.E. → <i>t</i> -stat inflated	inflated S.E. reduced <i>t</i> -stat (so <i>t</i> -tests have little power to reject wrong null)
Testing / Detecting	Breusch-Pagan (BP) test	Durbin-Watson (DW) test, Breusch-Godfrey (BG) test	variance inflation factor (VIF)
Correcting	computing robust standard errors (S.E.)	using robust standard errors (S.E.)	dropping some variables, using a different proxy for some variable, increasing sample size



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