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# PROCEEDING

**THE 3RD INTERNATIONAL CONFERENCE  
ON MATHEMATICS AND STATISTICS**

**BOGOR, 5 - 6 AUGUST 2008**

*Mathematics and Statistics: bridge for academia, business,  
and government in the entrepreneurial era*

3rd  
**ICOMS** 2008  
INTERNATIONAL CONFERENCE ON MATHEMATICS AND STATISTICS



Department of Statistics  
Faculty of Mathematics  
Institut Teknologi Sepuluh Nopember



INDONESIAN  
MATHEMATICAL SOCIETY  
(Indonesian Mathematical Society)  
P.O. Box 1000 1000



Department of Mathematics  
University of Indonesia

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## THE 3<sup>RD</sup> INTERNATIONAL CONFERENCE ON MATHEMATICS AND STATISTICS

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**Mathematics and Statistics: bridge for academia, business,  
and government in the entrepreneurial era**

organized by



MSMSSEA (Moslems Statisticians and  
Mathematicians Society in South East Asia)



Department of Statistics  
Department of Mathematics  
Institut Pertanian Bogor



Department of Mathematics  
Universiti Malaysia Terengganu,  
Malaysia

## PREFACE

Assalaamu'alaikum warahmatullaahi wabarakaatuh

Welcome all participants of ICoMS 2008 to Bogor – Indonesia. This event is organized by MSMSSEA in collaboration with Institut Pertanian Bogor (Indonesia) and Universiti Malaysia Terenganu (Malaysia).

We, the organizing committee, are very glad having this international conference due to many reasons.

1. ICoMS is a good avenue for mathematicians, statisticians, and other scientist to communicate.
2. ICoMS 2008 has a theme related to entrepreneurial era which is very important for mathematicians and statisticians, and scientist in general.
3. The event is important venue for business group, government, and academia to communicate and share knowledge as well.
4. Bogor is beautiful place in Indonesia surrounded by many research centers, IPB, Botanical garden, an other point of interest related to research institution.

We are also happy that the Vice President of Republic of Indonesia, Ministry of National Education, Ministry of Energy and Mineral Resources, and Ministry of Communication and Information Technology are supporting to the ICoMS 2008.

This event held on two days, August 5-6, and consist of several parts. We invite 17 outstanding professors to share and discuss topics in mathematics and statistics, including application. As many as 170 paper and 30 posters presented during this two-day conference. We appreciate to all of contributor from various countries who are motivated to participate in this event.

High appreciation is also awarded to companies and agencies which facilitate so that the even could run well.

We really hope all participants can benefit many things from this international event. May God bless you.

Wa'alaikumsalam warahmatullaahi wabarakaatuh.

The Committee of ICoMS 2008

## CONTENTS

Preface		ii
Contents		iii
Speech of Director General of Higher Education: Dr. Fasli Jalal		xiii
<b>SESSION A</b>		
Vector-Borne Disease Transmission Model: The Case of Filariasis Transmission in Jati Sampurna	A.K. Supriatna a; H. Serviana b E. Soewono	1
Optimization of Dining Table Placement in Restaurant Using Genetic Algorithm	Monika, Arnold Aribowo, Samuel Lukas	11
The Influence of Islamic Mathematics In The Malay World: A Study of Classical Astronomical Tables	Baharrudin Zainal and Mat Rofa Ismail	16
Problem-Based Learning Strategy To Improve Mathematics Skills Among Students	Ismail Abdullah	24
Linear Time Invariant Versus Linear Parameter Varying Reduced Order Controller Design For Aircraft Model	Widowati	31
Scientific Computing Research In The Faculty of Information Science And Technology Universiti Kebangsaan Malaysia	Mohammad Khatim Hasan, Muriati Mokhtar, Riza Sulaiman and Jumat Sulaiman	39
The Functions of Contextual Problems On A Mathematics Instruction Implementing The Realistic Approach	Rini Setianingsih	47
Further Results On The Ramsey Numbers For Star Union Cycle Versus Wheel On Seven Vertices	I Wayan Sudarsana, Edy Tri Baskoro, and Hilda Assiyatun	54
Characteristics of Lecturer That Influences Effective Teaching In Quality Education Based On Tqm Concepts	Khairul Anuar Mohd Ali, Zainol Mustafa, Fazli Idris & Siau Yee	58
Feynman Diagrams And The Tau Function	Zainal Abdul Aziz	66
An Evaluation Of The Efficiency Wage Model: Evidence From Bangladesh Food Industry	Masud Rana, Md. Azizul Baten and Mezbahur Rahman	74
Modeling Self-Potential (Sp) Distribution Groundwater Flow Using Boundary Element Method (BEM)	Muhammad Hamzah, S., Santoso, D., Parnadi, W.W., Sulistijo, B	83
Nonlinear Dynamic Plant Identification Of Waste Heat Boiler Unit Using Adaptive Wavelet - Neural Network (Wavenet) Method	Yuliati	91
A Group Mutual Exclusion Algorithm For Ad Hoc Mobile Networks	Armin Lawi	100
On The Measurement Of Credit Risk: A New Geometric Approach	Alireza Bahiraie, Noor Akma Ibrahim, Ismail bin Mohd, Azhar A.K.M	105

Slide By Slide Method In Solving General Global Optimization Problems	Goh Khang Wen, Ismail bin Mohd, and Yosza bin Dasril	111
The Infinite Divisibility Of Geometric Distribution	Dodi Devianto and Katsuo Takano	120
Tight Immersions And Transnormal Embeddings	B.A.Saleemi	126
Hydromagnetic Flow Over An Impermeable Linearly Stretching Sheet Immersed In A Non-Darcian Porous Medium	Noor Fadiya Mohd Noor and Ishak Hashim	131
Wavelet Analysis Of Solar Mass Ejection During Active And Quiet Sun	Saifuddin Ahmed Jilani and M.Ayub Khan YousfZai	138
Modeling A Determination Of Expected Commercial Value Of A Project In Producing Innovative Products In Smes	Nursafarizah Abd Aziz, Nor Ratna Masrom, Yosza Bin Dasril, and Adi Saptari	144
Modelling Nurse Rostering Using A 0-1 Goal Programming: A Case Study In Hukm	Ruzzakiah Jenal, Wan Rosmanira Ismail, Liong Choong Yeun And Masri Binti Ayob	151
<b>SESSION B</b>		
Enhancing Students' Mathematical Learning through Teacher Professional Development	Yaya S. Kusumah	159
Around Prime And Maximal Ideals Of A Skew Polynomial Ring Over A Dedekind Domain	A. K. Amir, P. Astuti, and I. Muchtadi-Alamsyah	169
The Fuzzy Version Of The Fundamental Theorem Of Semigroup Homomorphism	<u>Karyati</u> , Indah Emilia W, Sri Wahyuni, Budi Surodjo, Setiadji	173
Solving Fourth-Order Parabolic Equations By Red-Black Quarter-Sweep Sor Iterative Methods	J. Sulaiman, M. Othman, and M.K. Hasan	180
25 Years Development Of Knowledge Graph Theory: The Results And The Challenge	Sri Nurdianti and Cornelis Hoede	187
Eigenvalues And Eigenvectors Of Matrices Over Fuzzy Number Max-Plus Algebra	M. Andy Rudhito, Sri Wahyuni, Ari Suparwanto, and F. Susilo	195
The Partition Dimension Of Windmill Graph	Darmaji, Novian Syah, Saladin Uttunggadewa, Edy Tri Baskoro	203
Sorting Process Of Two Sets Of Non-Quantitative Data: Mathematical Method And Analysis	Edi Cahyono, David Taniar, La Ode Saidi, Arman and Natalis Ransi	206
On The Metric Dimension Of $P_2[P_n]$	S. Widosaputro, E.T. Baskoro, A.N.M. Salman, and D. Suprijanto	215
IS-LM In Slow-Fast System	Joice Ruth Juliana, Endah Asmawati	219

A Four-Stage Fifth-Order Runge-Kutta-Nystrom Methods With Dispersion Of High Order	Norazak Senu, Mohamed Suleiman' Fudziah Ismail, Mohamed Othman, and Norfifah Bachok@Lati	224
Logic In Recurrent Hopfield Network	Saratha Sathasivam	232
The Generalization Of Incidence Algebra	Ema Carnia, Sri Wahyuni, Irawati and Setiadji	238
Representation Of Sm-Operators On Product Spaces Of $r$ - Lebesgue Spaces $L_p(E, \Sigma, m), 1 < p < \infty$	Muslim Ansori ,Soeparna Darmawijaya and Supama	242
Benard-Marangoni Instability In A Rotating Fluid Layer With Feedback Control Strategy	Zailan Siri and Ishak Hashim	252
Interior Point Methods For Solving Linear Programing	Iwan Tri Riyadi Yanto,Julan Hernadi, and Yudi Ari Adi	259
Endo-Prime N-Group	Indah Emilia Wijayanti	266
Modelling Of Budget Allocation For University Library	Engku Muhammad Nazri Bin Engku Abu Bakar, Syariza Abdul Rahman, Noorezatty Mohd Yusop	271
A Novel Natural Approach To Euclidean TSP	Nur Azman Abu, Shahrin Sahib And Nanna Suryana	278
R-Linear Independent Generalization	Suprpto, Sri Wahyuni, Indah Emilia W., Irawati	287
A Study For Hyperbolic Decline Exponent Bound	S. Wahyuningsih, S. Darwis, A.Y. Gunawan, and A.K. Permadi	291
The $F$ -Coloring Of The Corona Product Of Complete Graph With Cycle Graph	Adiwijaya, A.N.M. Salman, E.T. Baskoro, and D. Suprijanto	298
A Modified Explicit Group Iterative Algorithm With Accelerated Over-Relaxation For Solving Poisson Equation	Shukhrat I. Rakhimov, Mohamed Othman	302
Asymptotic Behavior Of Linear Delay Differential Systems	Eti Dwi Wiraningsih, Widodo, Lina Aryati, Syamsuddin Toaha	307
On total vertex-irregular labellings of $tP_n$ a forest constructed from a disjoint union of paths	Nurdin I, E.T. Baskoro, A.N.M. Salman, N.N. Gaos	311

## SESSION C

The Effectiveness Of The Contextual Video As A Teaching Tool In The Teaching And Learning Statistics At The Universiti Tun Hussein Onn Malaysia (Uthm)	<u>Nafisah Kamariah Md Kamaruddin</u> , Zulkarnain Md Amin, Norfadzilah Ishak, Wan Mohd Rashid Wan Ahmad, And Maizam Alias	316
The Nonlinear Mechanism Of Tsunami Wave Generation	Nazeeruddin Yaacob And Zainal Abdul Aziz	323
Open Economy Macroeconomics: A Linear Rational Expectations Model	Iman Sugema and Toni Bakhtiar	332
The Range Of Mathematical Capability Of University Math Lecturers In Jakarta Indonesia	Ramir Santos Austria	340
An Application Wavelet Based Preconditioner For The Solution Of Ordinary Differential Equation	Ismail Bin Mohd and Farikhin	347
Research And Statistic Studying Model At Junior High School By Realistic Mathematics Education Application	Yani Ramdani	352
Using The Algebra Of Hypergraph For Reconstruction Phylogenetic Trees	Mulia Astuti, Irawati, Intan Muchtadi-Alamsyah, Ahmad Muchlis, Achirul Akbar Dan Muliana. A. Halim	366
Interval Linear Programming	Herry Suprajitno, Ismail Bin Mohd	374
What Happen With Numbers At Our Primary School?	Mohini Mohamed, Zulkifli, Jasmaniah	382
Determination Of GPS Signal Path Using The Runge-Kutta Method	Mardina Abdullah, Siti Sarah Nik Zulkifli, Mahamod Ismail, Ahmad Mahir Razali And Azami Zaharim	387
A Novel Linguistic Aggregation Method For Group Decision Making	Zamali Tarmudi, Mohd Lazim Abdullah And Abu Osman Md Tap	392
A Series Of Element Shape Functions For Infinite Elements	Sri Mardiyati	399
Promoting Creativity In Learning Mathematics Using Open-Ended Problems	Tatag Yuli Eko Siswono	406
Modeling Traffic Lights In Intersection Using Petri Nets	Dieky Adzkiya And Subiono	412
An Alternative Formulation For Electromagnetic Wave Propagations In Source Free Region	Noraini Md Nusi And Mohamed Othman	418
On The Number Of Families Of Branching Processes With Immigration With Family Sizes	Husna Hasan	424

Marangoni Convection In A Fluid Layer With Non-Uniform Temperature Gradient	Norihan Md. Arifin, Siti Suzilliana Putri Mohamed Isa, Roslinda Mohd Nazar, and Mohd Noor Saad	429
Dubrovin Valuation Rings Of Skew Ploynomial Rings	Intan Muchtadi Alamsyah	435
<b>SESSION D</b>		
The Roles Of Numerical Method And Optimal Control Theory In Cancer Immunotherapy	Ismail Bin Mohd, Arif Bin Mandangan	438
The Development of Applied Statistical Analysis	H. Ahmad Ansori Mattjik	450
Risk Factors For Water Fowl Infection With Avian Influenza H5n1, West Java Province, Indonesia	Etih Sudarnika, Asep Saefuddin, Abdul Zahid And Chaerul Basri	459
Trend Of The Import And Export Of Cocoa In Malaysia	H. J. Zainodin, G. Khuneswari & S.C. Albert Ling	463
Performance Analysis Of Reactive Mobile Ad Hoc Networks Routing Protocols Based On Taguchi Technique	Hazura Mohamed, Muhammad Hisyam Lee, Mazalan Sarahintu, Shaharuddin Salleh, And Bahrom Sanugi	472
Optimum Designs Of Multiresponse Surface Models For The First Order Lattice Simplex Designs	Ruslan , Susanti L, Purhadi, Sony S	479
Bayesian Approach For Choice-Conjoint Model In Consumer Preferences	Zulhanif, Ismail Bin Mohd, Noor Akma Ibrahim, Mustafa Bin Mamat	484
Simultan Equation Models Of Gross Domestic Product By Exchange Rate And Money Supply Scenario Analysis For Indonesian Economy	Bagus Sumargo	492
On Designing Algorithm For Sample Selection	L. Muhamad Safiih And Yaya Sudarya Triana	501
Generating Claim Data Of General Insurance Based On Collective Risk Model And Claim Process	Aceng K. Mutaqin, Dumaria R. Tampubolon, Sutawanir Darwis	506
An Application On Multiple-Correspondence Analysis On The Survey For Implementation Of The Profit-Loss Sharing Concept	Novriana Sumarti, Nurdinintya Athari S., And M. Rizka Fadhli	509
GIS Spatial Data Visualization Tools For Artificial Reefs Distribution	Mustafa Man, Md Yazid Mohd Saman, Noor Maizura M. Noor Khalid Samo And W.Aezwani W.A.Bakar	514



An Alternative Approach In Getting A Representative Model In A Mutiple Regression Analysis	G. Khuneswari, H. J. Zainodin, G. Darmesah & S. H. Sim	522
Wireless Internet Usage Among Students In Universiti Malaysia Sabah	Sathissan Ragavan, Darmesah Gabda, Amran Ahmed	531
An evaluation of a software for circular variables: ORIANA	Siti Fatimah Hassan, Abdul Ghapor Hussin and Yong Zulina Zubairi	539
Evaluation Of Some Methods For Estimating Parameters Of Regression Model With Various Zero Observations By Monte Carlo Simulation	Fitria Virgantari, Tjut Awaliyah, I Wayan Mangku, and Siswadi	545
Stability Model's By "Eberhart-Russel's" And Biplot Of Qpm (Quality Protein Maize) Under Central Maize In Indonesia	M Yasin Hg., Sigit Budi Santoso., And Sri Sunarti	553
Increasing Power Of Robust Test Through Pre-Testing In Multivariate Simple Regression Model	Rossita M. Yunus And Shahjahan Khan	559
Application Of Buhlmann-Straub Model On Tectonic Earthquake Insurance Problem	Hasih Pratiwi, Subanar, Danardono, And J.A.M. Van Der Weide	567
Evaluating The Cox-Aalen Model	Danardono	574
Estimation Of Distributed Lag Model With Adaptive Ekspectation And Partial Adjustment On The Distribution Of Fmcd-Based Robust Mahalanobis Distance	Aidawayati Rangkuti	579
Organizational Commitment Of Public Sector Employees In Pakistan: A Statistical Evidence	<u>Hazlina Hj Ali</u> , Maman A. Djauhari, and Sharipah S.S. Yahaya	587
Carbon Based Material Processing Method Using Statistical Application Technique	<u>Dr. M. Rashid Salahria</u> and Qasim Zafar	595
	N. Hashim, A.N. Zainal Abidin, M. Deraman, W. R. Wan Abdullah, A. Mohd Ramli, 6R.M. Yunus	600
<b>SESSION E</b>		
Continuous Time Model For Portfolio Problem Using Dynamic Programming Approach	Sugiyarto, Ismail Mohd., Mustafa Mamat And Yosza Dasril	607
A Comparison of MLE and GEE On Modeling Binary Panel Response	Jaka Nugraha, Suryo Guritno, Sri Haryatmi	612
Bayesian Scan Statistic For Spatial Cluster Detection	Setia Gunawan Wijaya, Dian Lestari, And Yekti Widyaningsih	619
Correlation Coefficient Estimation From Grouped Data	Teti Sofia Yanti	626
The Performance Of Exponential Weighted Moving Average (Ewma) Control Chart Between Classical, Robust And Bootstrap Method	Khalida Binti Oseman, Nazaruddin Omar And Habshah Midi	634

Inventory Model With Gamma Distribution	Hadi Sumadibrata, Ismail Bin Mohd	642
Accuracy Analysis Of Naive Bayesian Anti-Spam Filter	Ruslam, Armin Lawi, And Sri Astuti Thamrin	649
A New Method For Generating Fuzzy Rules From Training Data And Its Application In Financial Problems	Agus Maman Abadi, Subanar, Widodo, Samsubar Saleh	655
The Application Of Laws Of Large Numbers In Convergence Concept In Probability And Distribution	Georgina M. Tinungki	662
An Empirical Bayes Approach for Binary Response Data in Small Area Estimation	Dian Handayani, Noor Akma Ibrahim, Khairil A. Notodiputro, MOhd. Bakri Adam	669
Statistical Models For Small Area Estimation	Khairil A Notodiputro, Anang Kurnia, and Kusman Sadik	677
Maximum Likelihood Estimation For The Non-Separable Spatial Unilateral Autoregressive Model	Norhashidah Awang, Mahendran Shitan	685
Small Area Estimation Using Natural Exponential Families With Quadratic Variance Function (Nef-Qvf) For Binary Data	Kismiantini	691
Using An Extended And Ensemble Kalman Filter Algorithm For The Training Of Feedforward Neural Network In Time Series Forecasting	Zaقياتud Darojah, M. Isa Irawan, And Erna Apriliani	696
Estimation Of Outstanding Claims Liability And Sensitivity Analysis: Probabilistic Trend Family (PTF) Model	Arif Herlambang, Dumaria R Tampubolon	704
Expected Value Of Shot Noise Processes	Suyono	711
Modelling Malaysian Wind Speed Data Via Two Paramaters Weibull	Nur Arina Basilah Kamisan, Yong Zulina Zubairi, Abdul Ghapor Hussin, Mohd. Sahar Yahya	718
Application Of Latin Hypercube Sampling And Monte Carlo Simulation Methods: Case Study The Reliability Of Stress Intensity Factor And Energy Release Rate Of Indonesian Hardwoods	<u>Yosafat Aji Pranata</u> And Pricillia Sofyan Tanuwijaya	726
The Development Of Markov Chain Monte Carlo (Mcmc) Algorithm For Autologistic Regression Parameters Estimation	Suci Astutik, Rahma Fitriani, Umu Sa'adah, And Agustin Iskandar	734
A Note About Dh-Fever Estimation With ARIMAX Models	Elly Ana, Dwi Atmono Agus W	741
Evaluation Of Additive-Innovational Outlier Identification Procedure For Some Bilinear Models	Ismail, M.I., Mohamed, I.B., Yahya, M.S.	745

Interval Estimation For Quantile On One Parameter Exponential Distribution Under Multiple Type-Ii Censoring On Complex Case	Akhmad Fauzy	754
A Detection Measure Of Influential Observation Based On Forward Search Approach For Cox-Regression	Mohamed, I. B., Noh, N. A. M., Taib, N. A. M.	760
Gee-Smoothing Spline For Longitudinal Data	Suliadi, Noor Akma Ibrahim, Isthrinayagy S. Krishnarajah, and Isa Daud	768
<b>SESSION F</b>		
On Some Theory And Applications Of Bayesian Hierarchical Modeling	Kamarulzaman Ibrahim	776
Simultaneous Estimation After Selection And Ranking And Other Procedures :	Suryo Guritno	782
The Negative Exponential Case		
Survival Probabilities Of Genes In Partial Selfing Populations	Muhamad Sabran	789
The Probability Difference Indices And Empirical Sampling Distribution For Dif Indices For Identifying Item Bias In Multidimensional Item Response Theory	Badrun Kartowagiran And Heri Retnawati	799
Volumetric Stem Biomass: A Comparative Study Using Multiple Regression Models	Noraini Abdullah, Zainodin Hj. Jubok And Amran Ahmed	806
An Innovative Approach In Analysing Wind Data Via Graphical Display	Fakhrulrozi Hussain, Yong Zulina Zubairi, And Abdul Ghapor Hussin	815
Denoising Time Series Data Using Daubechies Wavelet Packet Transformation	Samsul Ariffin Abdul Karim, Mohd Tahir Ismail	823
Detection Of Outliers In Circular Regression Model Via Row Deletion Approach	Abuzaid, A. H., Mohamed, I. B., And Hussin, A.G.	828
Implementation Of Classification Predictive Association Rule ( CPAR) Algorithm To Diabetes Diagnose	Herwanto, Imas S. Sitanggang	835
Bayesian Survival Analysis Of Acute Leukemia Patients Using Multivariate Adaptive Regression Spline Model	Nurhayati Ulath, Sri Astuti Thamrin, And Armin Lawi	842
Combining Individual Learning And Group Discussion In Calculus Course	Endah Asmawati, And Joice Ruth Juliana	847
PBSTAT: A Web-Based Statistical Analysis Software For Participatory Plant Breeding	Willy Bayuardi Suwarno, Sobir, Hajrial Aswidinnoor, And Muhamad Syukur	852
Reliability Of The Specific Gravity (Sg) Value Of Three Indonesian Hardwoods Using Experimental Test And Monte Carlo Simulation	Yosafat Aji Pranata And Pricillia Sofyan Tanuwijaya	859
Comparison Of Differencing Parameter Estimation From Arfima	Gumgum Darmawan, Nur	866

Model By Spectral Regression Methods	Iriawan, Suhartono	
Application Of Cluster Analysis To Developing Core Collection In Plant Genetic Resources	Sutoro	875
Small Area Estimation With Time And Area Effects Using A Dynamic Linear Model	Kusman Sadik And Khairil Anwar Notodiputro	880
Statistical Analysis Of Wind Direction Data	Ahmad Mahir Razali, Arfah Ahmad, Azami Zaharim And Kamaruzzaman Sopian	886
Generalized Additive Mixed Models in Small Area Estimation	Anang Kurnia, Khairil A. Notodiputro, Asep Saefuddin, I Wayan Mangku	891
Kernel Principal Component Analysis In Data Visualization	Ismail Djakaria, Suryo Guritno, Sri Haryatmi	898
GARCH Models And The Simulations	Nelson Nainggolan, Budi Nurani Ruchjana And Sutawanir Darwis	906
Rainfall Prediction Using Bayesian Network	Hera Faizal Rachmat, Aji Hamim Wigena, and Erfiani	911
Identifying Item Bias Using The Simple Volume Indices And Multidimensional Item Response Theory Likelihood Ratio (Irt-Lr) Test	Heri Retnawati	916
Ordinary Kriging And Inverse Distance Weighting For Mapping Soil Phosphorus In Paddy Field	Mohammad Masjkur, Muhammad Nuraidi and Chichi Noviant	924
K-Means Clustering Visualization On Agriculture Potential Data For Villages In Bogor Using Mapserver	Imas S. Sitanggang, Henri Harianja, and Lailan Syaufina	932
Some Methods To Estimate The Number Of Components In A Mixture	M. A. Satyawan, A. H. Wigena, Erfiani	941
A Probabilistic Model For Finding A Repeat Triplet Region In DNA Sequence	Tigor Nauli	947
Application Of Spherical Harmonics In Determination Of Tec Using Gps Observable	Mardina Abdullah, Siti Aminah Bahari, Baharudin Yatim, Azami Zaharim, Ahmad Mahir Razali	954
Testing Structure Correlation Of Global Market By Statistic Vvsv	Erna Tri Herdiani, and Maman A. Djauhari	961
Exploring the MAUP from a spatial perspective	Gandhi Pawitan	967
Estimation of RCA(1) Model using EF: A new procedure and its robustness	1Norli Anida Abdullah, 2Ibrahim Mohamed, 3Shelton Peiris	996
Second Order Linear Elliptic Operators In The Unit Square	Abdul Rouf Alghofari	1008

## POSTER

Study Of Fractional Factorial Split-Plot Experiment	Sri Winarni, Budi Susetyo, and Bagus Sartono	1012
Improving Model Performance For Predicting Poverty Village Category Using Neighborhood Information In Bogor	Bagus Sartono, Bagus Sartono, and Zulhelmi Thaib	1019
Ammi Models On Count Data: Log-Bilinear Models	Alfian Futuhul Hadi H. Ahmad Ansori Mattjik I Made Sumertajaya Halimatus Sa'diyah	1026
Prediction Of Oil Production Using Non Linear Regression By Sdpro Software (Special Program Package) <sup>*)</sup>	Budi Nurani R , and Kartlos J. Kachiashvili	1038
An Implementation Of Spatial Data Mining Using Spatial Autoregressive (Sar) Model For Education Quality Mapping At West Java <sup>*)</sup>	Atje Setiawan A. , Retantyo Wardoyo , Sri Hartati , and Agus Harjoko	1045
Validation Of Training Model For Robust Tests Of Spread	Teh Sin Yin, and Abdul Rahman Othman	1056
Spectral Approach For Time Series Analysis	Kusman Sadik	1063
The ACE Algorithm for Optimal Transformations in Multiple Regression	Kusman Sadik	1066
The Relation Between The Students' Interaction And The Construction Of Mathematical Knowledge	Rini Setianingsih	1069
Application of Auto Logistic Regression Spatial Model using Variogram Based Weighting Matrix to Predict Poverty Village Category	Utami Dyah Syafitri, Bagus Sartono, Vinda Pratama	1075

**Speech of Director General of Higher Education at ICoMS 2008  
At Novotel Corralia, Bogor, 5 August 2008**

Dr. Fasli Jalal  
The Director General of Higher Education  
Ministry of National Education, Republic of Indonesia

Bismillahirrahmanirrahim  
Assalamu'alaikum Warrahmatullahiwabaraktuh

Good morning ladies and gentlemen

It is a great honor for me to provide a speech in this important scientific event, the Third International Conference on Mathematics and Statistics of MSMSEA (Muslim Statistician and Mathematician Society in South East Asia). I can see from here that the audiences are of from various countries. So, let me welcome you to Indonesia, a country of great diversity in unity. I think it likes mathematics and statistics that we always find diversities and similarities. As far as I know that these two terms that make science and technology develop rapidly.

Someday a Germany great scientist, who found the Normal Distribution, Carl Fredric Gauss (1777-1855), had mentioned that mathematics, is the queen and servant of science. It is very reasonable statement, becuase mathematics plays an important role in developing science and technology and in the same time it must be reconed in all aspects of science production, preservation and dissemination. Hence, it is a servant of science. In the other hand, all scientists, irrespective their domains have to understand mathematics (including statistics) in order to analyze the problems properly. Thus, it is a queen of science. With its two functions, mathematics with its derivatives has narrowed the gap between the so called hard science and soft science. Hence, there is no exact distinctin between soft and hard sciences. Whatever the sciences, they need mathematics and statistics in order to clarify and simplify the issues. In mathematics and statistics, simplicity is the clarity of mind. However, mathematics and statistics can analyze complex issues. The modelling itself is the simplication of complicated real world.

Ladies and gentlemen

Let me talk about about sscience, mathematics and technology which are well-known as the tripod in an unknown area. All scientists who have achieved high standing positions in science reputation always have strong mathematical background. Hence, they can see the things that the other people can't see, also they can predict that the other people can't predict. Their deductive as well as inductive thinking are both adequate. These two ways of thinking are essential in research and science development. Deductive reasoning is considered mathematical way of thinking, while inductive is statistical way of thinking. Both type of reasoning are the key factors of scientific circle, without them the science development is stagnant. The Kuhnian model of scientific revolution occures when the deductive and inductive thinking are accomodated well in a society. Hence, education has to provide great room for student to flourish their reasoning. Their brain for deductive and inductive thinking can develop if the school gives enough space for student creativity. Hence, they can think freely and try to find facts, which are called data in the statistical term, to proof their ideas. A great Indonesian statistician, Prof. Nasoetion (1932-2002), someday mentioned 'In God we trust, all other bring data'.

The challenges are to find the ways in order to facilitate the students to love science and mathematics. After they love and understand the important of science and mathematics as well as stimulated by realities, finally they can develop technologies. Hence, the three point of the tripod are interconnected and progress well in a conducive ecosystem. Many technological problems influence the mathematical and science development, and at the end have made the society developed and their income increased. However, the conducive academic atmosphere is needed in order the tripod of science, mathematics, and technologies can develop well. For example, the problems of communication and information have made topology, number theory, and graph theory which are needed in developing information technology. This phenomenon has created big market for the mathematicians and statisticians. Finally, without strong mathematics (including statistics) the technologies as well as the economy are stuck. In other word, there is no great economy without great mathematics and science. Hence the economic development is termed as knowledge-based economy or K-economy. There is no K-economy in society with poor knowledge. In other words, K-economy can only develop well in the society, who understand knowledge. This society is called knowledge-based society or K-society. I am sure that all scientists in this room agree with me that the developing countries have to be the K-society in order to lead the world. Otherwise, we are only the followers.

Ladies and gentlemen.

I understand that one of the clusters in this conference is 'mathematics in education processes. I believe this is very important for scientist and professors of higher education to pay enough attention to the basic and secondary education, especially in cultivating the important of mathematics and science for emerging technologies. Students with poor comprehension of mathematics can be predicted will have difficulties in facing complex subjects. Therefore, the universities have obligations to make the basic and secondary education understand well the fundamental principles of mathematics including their mathematical skills. Since the pupils are the main sources of the future scientists and technologists, their foundation in basic science and mathematics is greatly important. Hence, interesting method of subject delivery is key factor for the pupils to comprehend mathematics. So, one of important services of higher education to society is to train the teacher of lower education in order to follow new frontier of science. They need to be updated. This service has direct and indirect positive effect to the universities. The direct effect is to obtain high quality of student intake, while the indirect one is to share knowledge to the society.

I fully agree with the theme of the third ICoMS "mathematics and statistics as a bridge for academia, government and business in the entrepreneurial era". This theme implies some consequences, such as: mathematics and statistics are not just passive subject to be learned or memorized, they must be considered as active materials to be understand creatively and hence finally the scientists can produce mathematics and statistics. In other words, students have to learn mathematics and statistics actively including the basic theory and their application. It is understood that inside the airplane there exist complex mathematics and statistics. Without strong mathematics and statistics, the airplane cannot fly appropriately. This example can be extended into many areas of life and technologies, including medicine, social sciences, economy, business, politics, public health, biotechnology, manufacturing, civil engineering, energy, and so on. However, to produce mathematics and statistics needs entrepreneurial soul. Hence collaboration among stakeholder from various institutions is needed in approaching the complex issues in the entrepreneurial era.

For our fellows from the private sectors, one easy way to help mathematicians and statisticians is to provide education programs on CSR (Corporate Social Responsibility). For example we can build a

mathematics fellowship program, mathematics and statistics entrepreneurial award, entrepreneurial research competition, and many other things. For implementing these ideas, we are more than happy to collaborate with the private sectors.

Ladies and gentlemen

At the present time, almost all countries are shifting their concept of development from centralism to decentralism. The paradigm shift is also recognized by international bodies, like The World Bank. Hence, the role of scientists including mathematicians and statisticians are getting crucial. Why? Because regional development without strong human resource is difficult. The local governments certainly need knowledge for their regional planning. Mathematicians and statisticians can collaborate with the local government in creating and measuring some tangible indicators for government strategic planning and road mapping. Otherwise, the plan is too normative and uneasy to measure. As a result, the progress of development cannot be evaluated objectively. Number is not everything in lives, but lives without number is nothing. Hence, cooperative action among academia, government and business is 'a must'.

To optimize the opportunity, let me provide you some assignment to formulate what is the role of mathematicians and statisticians in the economic holistic development. While you are presenting your research papers, maximize your present here to have such discussion on mathematics related to regional development, entrepreneurship, environment, food and energy resources including the process of education and research. It looks simple but needs a well trained mathematicians and statistician like you all. I believe you can produce innovative approaches which are useful for the Indonesian government, universities, research centers, private sectors, and other community. Your thought is surely needed by other participants coming from various countries.

Finally, I convey my deep gratitude while hoping you enjoy this conference and other activities organized by MSMSSEA. I hope you are always fresh and healthy with full enthusiasm in participating the important event.

Selamat berkonferensi dan terima kasih.

Billahittaufig wal hidayah

Wassalamu'alaikum warahmatullahi wabarakatuh

Dr. Fasli Jalal



# GENERATING CLAIM DATA OF GENERAL INSURANCE BASED ON COLLECTIVE RISK MODEL AND CLAIM PROCESS

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**Abstract:** Meyers and Schenker (1984) presented algorithms to generate claim data of general insurance based on collective risk model. The components that generated are claim frequency and claim severity. In this paper, we propose two algorithms to generate claim data of general insurance based on collective risk model and claim process. The algorithm not only generating claim frequency and claim severity, but also time of claim events and time of claim payments. The first algorithm is particularly useful in short-tail insurance business. The second algorithm is particularly useful in long-tail insurance business. In this paper, the algorithms illustrated by generating claim data of general insurance using MATLAB program.

**Keywords:** general insurance, collective risk model, claim process, claim frequency, claim severity, long-tail insurance business, MATLAB program

## 1. Introduction

In business of general insurance, claim data are very important for pricing and reserving. Taylor and McGuire (2004) reported that claim data usually containing date of injury; date of notification; finalized/unfinalized status, including dates of changes of status; paid losses; case estimates; and various other claim characteristics (e.g. injury type, injury severity, etc.).

Meyers and Schenker (1984) presented algorithms to generate claim data of general insurance based on collective risk model. The components that generated are claim frequency and claim severity. In this paper, we propose a new algorithm to generate claim data of general insurance based on collective risk model and claim process. The algorithm not only generating claim frequency and claim severity, but also time of claim events and time of claim payments. The algorithm is particularly useful in long-tail insurance business for testing or comparing performance of one or more methods of pricing and reserving. In this paper, claim process means claim payment process. The algorithm is illustrated by generating claim data of general insurance using MATLAB program.

The remainder of the paper is structured as follows. Section 2 presents the Meyer-Schenker's algorithm. The proposed algorithm is discussed in Section 3. Section 4 provides an example to illustrate the proposed algorithm in MATLAB program.

## 2. Meyers-Schenker's algorithms

Meyers and Schenker (1984) presented three algorithms to generate claim data of general insurance based on collective risk model. Let  $N$  be a random variable denoting the claim frequency,  $\lambda$  be the expected claim frequency, and  $\chi$  be a random variable with  $E[\chi] = 1$  and  $\text{Var}[\chi] = c$ . The claim frequency distribution can be modeled by the following algorithm.

**Algorithm 1**

1. Select  $\chi$  at random from the assumed distribution.
2. Select the claim frequency,  $N$ , at random from a Poisson distribution with parameter  $\chi \cdot \lambda$ .

If  $\chi$  has a Gamma distribution, the claim frequency distribution described by Algorithm 1 is the negative binomial distribution (Klugman *et al.*, (2004)). Meyers and Schenker (1984) called the parameter  $c$  is the contagion parameter for the claim frequency distribution. If  $c = 0$ , **Algorithm 1** yields the Poisson distribution.

Let  $Z$  be a random variable denoting claim severity,  $S(z)$  be the cumulative distribution function for the claim severity,  $z$ , and  $X$  be a random variable denoting the aggregate loss for an insured. Aggregate losses can then be generated by the following algorithm.

**Algorithm 2**

1. Select the claim frequency,  $N$ , at random from the assumed claim frequency distribution.
2. Do the following  $N$  times.
  - 2.1. Select the claim severity,  $Z$ , at random from the assumed claim severity distribution.
3. The aggregate loss amount for an insured,  $X$ , is the sum of all claim severity,  $Z$ , selected in Step 2.1.

Implicit in the use of **Algorithm 2** is the assumption that the claim severity distribution,  $S(z)$ , is known. In practice, this distribution must be estimated from historical observations, or it must be simply assumed. Under such conditions, errors in selecting the parameters of the claim severity are inevitable. To model parameter uncertainty in the claim severity distribution, Meyers and Schenker (1984) made the simplifying assumption that the shape of the distribution is known, but there is uncertainty in the scale of the distribution.

Let  $\beta$  be a random variable satisfying the conditions  $E[1/\beta] = 1$  and  $\text{Var}[1/\beta] = b$ , then the aggregate losses amount for an insured modeled by the following algorithm.

**Algorithm 3**

1. Select the claim frequency,  $N$ , at random from the assumed claim frequency distribution.
2. Select the scaling parameter,  $\beta$ , at random from the assumed distribution.
3. Do the following  $N$  times.
  - 3.1. Select the claim severity,  $Z$ , at random from the assumed claim severity distribution.
4. The aggregate loss amount for an insured,  $X$ , is the sum of all claim severity,  $Z$ , divided by the scaling parameter,  $\beta$ .

Meyers and Schenker (1984) called  $\beta$  is the mixing parameter. The mixing parameter is a measure of parameter uncertainty for the claim severity distribution.

**3. The proposed algorithms**

In this section, we propose two algorithms to generate claim data. The first algorithm is extension of **Algorithm 3** by adding time of claim events. Let  $T1$  be a random variable denoting the time between claims, then the algorithm to generate claim frequency, claim severity, and time of claim events is as follows.

**Algorithm 4**

1. Select the claim frequency,  $N$ , at random from the assumed claim frequency distribution.
2. Select the scaling parameter,  $\beta$ , at random from the assumed distribution.
3. Do the following  $N$  times.
  - 3.1. Select the time between claims,  $T1$ , at random from the assumed time between claims distribution.
  - 3.2. Select the claim severity,  $Z$ , at random from the assumed claim severity distribution.
4. The aggregate loss amount for an insured,  $X$ , is the sum of all claim severity,  $Z$ , divided by the scaling parameter,  $\beta$ .

The **Algorithm 4** assume that a claim is finished by one payment. This algorithm is particularly useful in short-tail insurance business.

In long-tail business insurance, it is common that a claim is finished by more than one payment. The second algorithm is particularly useful in long-tail insurance business. Let  $T2$  be a random variable

denoting the time between payments, and  $M$  be a random variable denoting the number of payments, then the algorithm to generate claim frequency, claim severity, time of claim events, and time of claim payments is as follows.

**Algorithm 5**

1. Select the number of claims,  $N$ , at random from the assumed claim frequency distribution.
2. Do the following  $N$  times.
  - 2.1. Select the scaling parameter,  $\beta$ , at random from the assumed distribution.
  - 2.2. Select the time between claims,  $T1$ , at random from the assumed time between claims distribution.
  - 2.3. Select the number of payments,  $M$ , at random from the assumed distribution of the number of payments, then do the following  $M$  times.
    - 2.3.1. Select the time between payments,  $T1$ , at random from the assumed distribution of the time between claims.
    - 2.3.2. Select the claim severity,  $Z$ , at random from the assumed claim severity distribution.
  - 2.4. The aggregate loss amount for an insured,  $X$ , is the sum of all claim severity,  $Z$ , divided by the scaling parameter,  $\beta$ .

The **Algorithm 5** assume that the payments for a claim are independent.

### 3. Example

Two algorithms in Section 3 illustrated by generating claim data of general insurance using MATLAB program. Figure 1 display MATLAB program for **Algorithm 4**. The execution result of Figure 1 for  $\lambda = 3$ ,  $b = 0.1$ , and  $c = 0.1$  shown in Table 1.

```
function [OUT,X] = ALGOR4(lambda,b,c)
chi = GAMRND(1/c,c);
N = POISSRND(chi*lambda);
beta = GAMRND(1/b+2,b/(1+b));
time = 0;
if N > 0
    for i=1:N
        T1 = EXPRND(50);
        time = time + T1;
        Z(i) = GAMRND(5,1000)/beta;
        OUT(i,1) = time;
        OUT(i,2) = Z(i);
    end
else
    Z = 0;
    OUT = 0;
end
X = sum(Z);
```

Figure 1. MATLAB Program for Algorithm 4

Table 1. Result for Figure 1

Time of Claim Event	Claim Severity
43.866	5143.4
110.79	6396.8
147.98	6700.9
TOTAL	18241.0

MATLAB program for **Algorithm 5** is available from the first author.

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