Report on Bachelor / Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

Student:	**MARTIN HNATH**
Advisor:	**Doc. PhDr. Adam Geršl, Ph.D.**
Title of the thesis:	**Linkage between Exchange Rate and Foreign Direct Investments: Empirical Evidence from Developing Countries**

OVERALL ASSESSMENT *(provided in English, Czech, or Slovak):*

The thesis is aiming at high objectives: to enrich the world literature on the linkage between FDI and exchange rate (ER), and to innovate the methodology of assessing the currency regimes. Author also applies highly advanced techniques of estimation for testing the relevance of these objectives.

For that, I consider the chapter on FDI theoretical backgrounds, and especially its section 2.3 on determinants of FDI, of crucial importance. It could prepare the propper theoretical guidelines for further balanced research. To my disappointment the section 2.3 covers mere 2 ½ pages, contains rather obsolete references (Blonigen & Piger, 2011, being the only more recent title) and misses some seminal papers on FDI determining factors [1]. Author then rushes in the next section (2.4) to very narrow ER considerations, omitting so the other (and quite probably more robust) factors determining FDI. In the chapter 3 the text focusses thoroughly on the ER as the determinant of FDI. That would be fully acceptable provided a similar stress were provided to other important factors.

Another methodological problem arises in ch. 4 („Sample Description") where the choice and the quality of data are discussed. It is the choice between FDI flows and FDI stocks where the problem of their cointegration/colinearity with exchange rate could enter the stage. I would welcome a more extensive assessment of methodology of FDI statistics since the FDI values can be stricken by a systemic statistical measurement bias (value illusion) since the methodology of reporting FDI changes in time and between countries can differ significantly – see e.g. Duce, M. (2003), Definitions of foreign direct investment: a methodological note. Banco de España, Madrid. The FDI data can be therefore too heterogenous.

Chapter 4 is otherwise highly focused on the analysis of some specific factors required for the future analysis of ER, leaving other factors aside.

The specification of the basic model comes straight on the first page of chapter 5, discarding some more fundamental model building backed by theory and related to countries´ supply side. So an intuitive empirical model is proposed instead. However, such a model can be grossly misspecified due to omitted variable bias leading to the risk that the importance of included variables will be inconsistent with reality. This approach was to a large extent compensated by including into the „baseline model" (see table 6.2) 11 variables used in gravity models, unfortunately without much concern for their theoretical relevance.

Additional bias could be added to regressions by transforming negative FDI to zero, see e.g. Martinez-Zarzoso, I. (2013). The Log of Gravity Revisited. *Applied Economincs 45(3)*, 311-327.

---

[1] E.g. papers by Baltagi B. H, P. Egger, M. Pfaffermayr, 2007; Alfaro L. et al., 2008 and 2009; Guerin S., Manzocchi S., 2009; Seyoum B. (2011). Remark: Bruce Blonigen is misspelled in the text as Bloningen (which actually is quite a common misspelling by other authors, too).

Report on **Bachelor / Master Thesis**

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

Student:	**MARTIN HNATH**
Advisor:	**Doc. PhDr. Adam Geršl, Ph.D.**
Title of the thesis:	**Linkage between Exchange Rate and Foreign Direct Investments: Empirical Evidence from Developing Countries**

The econometrics commencing on p. 33 up to 39 are highly expert in their details to technicalities. The first estimation results are, however, rather less convincing where the only robust coefficients are those of economic growth in both partner countries, financial development and language. All ER-related variables are insignificant. Their separation and estimate by IV is again rejecting the hypothesis of ER importance for FDI, which is also a sort of a positive finding for pragmatic policy conclusions.
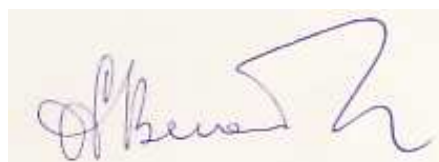
The author admitted in the introductory text that the literature about the interaction between exchange rate regimes and volatility, and FDI is rather scarce and that literature which is available leads to mixed (or directly inconclusive) results. The author´s results confirm that the previous experiences remain valid, not pulling the weil of ignorance much. He used a highly sophisticated set of instruments for that.

My conclusions: The author deserves a praise for showing his ability to digest and apply a vast quantity of important and technically demanding research papers. His econometric skills are undisputed. What I lacked there was his ability to form hypotheses which would be relevant for explaining real data due to their theoretical relevance too, so that testing blind alleys would be avoided.
My proposed grade for this thesis is 2 („very good").

SUMMARY OF POINTS AWARDED (for details, see below):

CATEGORY		POINTS
Literature	*(max. 20 points)*	18
Methods	*(max. 30 points)*	27
Contribution	*(max. 30 points)*	14
Manuscript Form	*(max. 20 points)*	18
TOTAL POINTS	*(max. 100 points)*	**77**
GRADE	**(1 – 2 – 3 – 4)**	**2**

NAME OF THE REFEREE: Vladimír Benáček

DATE OF EVALUATION:　　11.6.2014

_____
Referee Signature

EXPLANATION OF CATEGORIES AND SCALE:

LITERATURE REVIEW: *The thesis demonstrates author's full understanding and command of recent literature. The author quotes relevant literature in a proper way.*

Strong	*Average*	*Weak*
20	*10*	*0*

METHODS: *The tools used are relevant to the research question being investigated, and adequate to the author's level of studies. The thesis topic is comprehensively analyzed.*

Strong	*Average*	*Weak*
30	*15*	*0*

CONTRIBUTION: *The author presents original ideas on the topic demonstrating critical thinking and ability to draw conclusions based on the knowledge of relevant theory and empirics. There is a distinct value added of the thesis.*

Strong	*Average*	*Weak*
30	*15*	*0*

MANUSCRIPT FORM: *The thesis is well structured. The student uses appropriate language and style, including academic format for graphs and tables. The text effectively refers to graphs and tables and disposes with a complete bibliography.*

Strong	*Average*	*Weak*
20	*10*	*0*

Overall grading:

TOTAL POINTS	GRADE		
81 – 100	1	= excellent	= výborně
61 – 80	2	= good	= velmi dobře
41 – 60	3	= satisfactory	= dobře
0 – 40	4	= fail	= nedoporučuji k obhajobě