

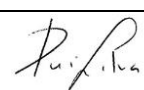
# IMESS DISSERTATION

**Note: Please email the completed mark sheet to Year 2 coordinator (cc Chiara Amini [chiara.amini@ucl.ac.uk](mailto:chiara.amini@ucl.ac.uk) and [ssees-imess@ucl.ac.uk](mailto:ssees-imess@ucl.ac.uk))**

Please note that IMESS students are not required to use a particular set of methods (e.g. qualitative, quantitative, or comparative) in their dissertation.

<b>Student:</b>	Jiamin Cheng
<b>Dissertation title:</b>	The impact of the macroeconomic and the parent bank on the credit risk of the subsidiaries of foreign banks: evidence from CEE countries.

	70+	69-65	64-60	59-55	54-50	<50
	A	B	C	D	E	F
<b>Knowledge</b> <i>Knowledge of problems involved, e.g. historical and social context, specialist literature on the topic. Evidence of capacity to gather information through a wide and appropriate range of reading, and to digest and process knowledge.</i>					X	
<b>Analysis &amp; Interpretation</b> <i>Demonstrates a clear grasp of concepts. Application of appropriate methodology and understanding; willingness to apply an independent approach or interpretation recognition of alternative interpretations; Use of precise terminology and avoidance of ambiguity; avoidance of excessive generalisations or gross oversimplifications.</i>					X	
<b>Structure &amp; Argument</b> <i>Demonstrates ability to structure work with clarity, relevance and coherence. Ability to argue a case; clear evidence of analysis and logical thought; recognition of an argument limitation or alternative views; Ability to use other evidence to support arguments and structure appropriately.</i>						x
<b>Presentation &amp; Documentation</b> <i>Accurate and consistently presented footnotes and bibliographic references; accuracy of grammar and spelling; correct and clear presentation of charts/graphs/tables or other data. Appropriate and correct referencing throughout. Correct and contextually correct handling of quotations.</i>						x
<b>Methodology</b> <i>Understanding of techniques applicable to the chosen field of research, showing an ability to engage in sustained independent research.</i>					X	

<b>ECTS Mark:</b>	E	<b>UCL Mark:</b>	52	<b>Marker:</b>	Rui Silva
<i>Deducted for late submission:</i>				<b>Signed:</b>	
<i>Deducted for inadequate referencing:</i>				<b>Date:</b>	11/09/2021

## MARKING GUIDELINES

**A (UCL mark 70+):** Note: marks of over 80 are given rarely and only for truly exceptional pieces of work.

Distinctively sophisticated and focused analysis, critical use of sources and insightful interpretation. Comprehensive understanding of techniques applicable to the chosen field of research, showing an ability to engage in sustained independent research.

**B(UCL mark 65-69):**

A high level of analysis, critical use of sources and insightful interpretation. Good understanding of techniques applicable to the chosen field of research, showing an ability to engage in sustained independent research.

**C (UCL mark 60-61):**

Some evidence of critical analysis, knowledgeable interpretation. Wide range of sources used to develop a logic and coherent argument. Good understanding of techniques applicable to the chosen field of research, the extent of independent research could have improved.

**D (UCL mark 59-55):**

Employ relevant sources and show ability to engage in systematic inquiry. Little critical analysis of the material. It demonstrate methodological awareness but the standard and rigor of the analysis can improve.

**E (UCL mark 54-50):**

Mostly descriptive argument. Employ relevant but limited sources. The structure, logic and overall quality of the argument needs improvement.

**F (UCL mark less than 50):**

Demonstrates failure to use sources and an inadequate ability to engage in systematic inquiry. Inadequate evidence of ability to engage in sustained research work and poor understanding of appropriate research techniques.

### **Comments, explaining strengths and weaknesses (at least 300 words):**

The topic of this thesis is interesting and attempts to explore one risk transmission channel in the banking sector – namely, the relationship between a parent and its subsidiary/branch. The validity of this topic is even more relevant considering the markets that the author proposes to explore (CEE). However, this work has many problems which make it very hard to properly understand what was done in the literature, which are the dominant paradigms, the authors' methodology, and his conclusions. The very poor structure of the narrative, confusing and vague terminology, and the numerous grammatical mistakes made that task even more complicated. In that sense, I go point-by-point.

The introduction is confusing, especially because the author follows a narrative style with a vague and often continuous tense. In that sense, statements such as "In that context, multinational banks began to expand rapidly in CEE countries..." is an example. When did it began?

The overview of foreign banks is quite problematic, especially because it mostly resembles a log diary. A large number of statements lack sources or data. For example: "Poland and Hungary were first established secondary system in CEE countries. In the 1990s, some countries in the CEE region experienced high inflation and sovereign crisis due to macroeconomic imbalances and policy dilemmas. The reform has led to many corporate bankruptcies, non-performing loans have overwhelmed commercial banks and the government...". That is also especially noticeable when reviewing the impact of the 2008 financial crisis on the banking systems of those countries. More importantly, the author devotes most of the attention to the banks in Hungary and Czech Republic considering the average NPLs in those countries. However, countries such as Lithuania have even highest NLP and they are barely mentioned.

The literature review shares many of the issues above. Many statements lack data, sources and proper explanation and justification. Several terms are introduced without proper definition. The author frequently (until the end of the thesis) mistakes correlation with causation (in fact, he never speaks of causation). Many sources seem to have been chosen randomly without accounting for the expected differences in banking systems of developed and developing countries. Frequently, the author contradicts himself, and even uses the same source contradictorily (e.g., uses Fofack (2005) to express and idea and then later uses again the same source to contradict the same idea). Frequently, he indicates that the effects of certain variables in the credit risk may have an ambiguous effect. However, he virtually always just cites sources supporting one direction of the effect. Overall, the literature is a patchy collection of sources which frequently is not logical or coherent, and more importantly, contradictory. It is almost impossible to obtain a feeling for what was done in the literature.

The data and methodology are organized in a very naïve manner. To begin, the author describes step-by-step the functions and the process when extracting the data from Orbis Bank. For example: "...the database can use the search function filter to create a specific dataset... the database has the tool function... the tool function tab can be accessed for various analyses...". The sample is restricted to 8 countries without a solid justification. The author claims that he has chosen those countries because they integrated the EU in 2004, and the sample begins in 2009. However, Romania and Bulgaria also became part of the EU prior to 2009, and thus, by the same argument, could and should have been included. The definition of the variables also has several issues.

Using the NPL as the proxy for credit risk is rather naïve, even though it is frequently employed in the literature. Frequently, banks do not allow loans to default unless there is no possible "legal" way of avoiding that. Therefore, what happens is that loans which are getting close to their expiry are restructured, and thus, any potential "risks" are reflected in impairments. Therefore, NPL do not provide a clear picture of the quality and risk of a bank's portfolio. Moreover, the author motivates this variable with the argument that "most of literature uses it" and does not explain and justify why it is reasonable to work with it in the first place. The independent variables also have some issues. There's a log transformation of the bank's assets (which is commonly done in the literature), which the author does not properly justify (it is not just a matter of adjusting magnitude of the expected coefficients in a regression, otherwise, we could just apply an affine transformation to the vector). There's no apparent reason to use the ROAA instead of the ROA. The author frequently predicts contradictory signs for the coefficients of each variable without proper justification; make predictions that do not make too much sense; reveal poor knowledge of certain financial metrics, balance sheet composition, and banking business. Some hypotheses are clearly unreasonable, which is verified in the latter part of the work.

The interpretation of the descriptive statistics is insufficient and, at times, incorrectly made. For example, the author indicates that the average inflation rate in the countries where the subsidiaries operate is of 116%. Not only is that impossible, but it shows that the author failed to understand that he is working with the CPI and not the inflation rate. The author also frequently speaks of "endogenous variables" without considering the meaning of that in econometric terms.

The discussion of the methodology also has several issues. Using a FE is not unreasonable. However, the author indicates that he will control for time effects. However, neither the regression equation nor the regressions that will follow include any time effects. The explanation of the Hausman test is incorrect, and the justification to use a GMM estimator is insufficient.

The regressions in (1) and (2) are not the regressions shown in the outputs. More importantly, there are numerous tests missing. The author does not check the variables for stationarity. There are no tests of autocorrelation, heteroskedasticity and cross-sectional dependence. Even without those tests, it is unreasonable to not cluster the standard errors or, at the very least, work with robust ones. The interpretation of the F test for FE is incorrect. More importantly, the interpretation of the coefficients is incorrect. The author does not interpret the coefficient as the marginal impact of the change in 1 unit of the independent variable. On the contrary, it interprets as the marginal impact of the variation in one unit of the dependent variable. Additionally, he also does not consider the units in which each variable is expressed. The results of the regression, at times, contradict some very unreasonable hypothesis made by the author, and the latter fails to properly recognize that issue. Finally, running a GMM estimation as a "robustness check" does not make too much sense. The justification to use that estimator is not clear. The conditions are not explained (e.g., which variables are taken as being endogenous).

Overall, the work has too many limitations and problems.

**Specific questions you would like addressing at the oral defence (*at least 2 questions*):**

- **Why exactly do you run a GMM estimator? Which where the restrictions adopted? Which variables are endogenous? What may be explaining the change in the sign of certain coefficients (e.g., capital)?**
- **Why would you expect liquidity, inflation and profitability to increase credit risk?**
- **What justifies the fact that an increase in the parent's bank profitability increase the credit risk of the subsidiary or branch?**
- **What explains the different signs of inflation in both at the domestic and the parent's country?**
- **Why don't you control (and even test) for time-effects?**
- **In table 10, do you think we have reasons to believe that the results in the regression for the branch are robust?**

