Political risk guarantees and capital flows: the role of bilateral investment treaties

The paper examines the impact of political risk, political risk guarantees and their impact on capital flows. In particular, the article decomposes capital flows into debt and equity and analyses the role played by political risk in these flows for the period 1984 to 2011. Using data for a panel of 66 middle income countries via a GMM the results suggests that non-guaranteed debt and equity flows tend to gravitate toward countries/or regions that have ratified bilateral investment treaties with the originating countries. In effect, bilateral investment treaties serve to dampen, if not eliminate the inherent perceived political risk of recipients of these capital flows. A number of suggestions for boosting capital flows to middle income countries, including but not limited to reform of financial markets are addressed in the article.

The article is well written. The arguments are well presented and defended and I have no problems with the empirical techniques employed. I therefore recommend this article for publication subject to some minor corrections.

1. The author probably needs to justify more the selection of middle as opposed to high or low income countries for the analysis. A quick glance through the data held by the World Bank indicates more flows to some low income economies and of course the high income developing countries. If political risk guarantees is anything to go by then certainly there must be something missing that we are not picking up.
2. Section 3 is too long and should be compressed with focus on the key variables under consideration. The specifications can also be condensed. And please align all equations from section 3 onwards.
3. The entire manuscript requires very careful editing and proof reading. For instance in the introduction, page 3 line 7, there is need for full stop after footnote 5 and 6. Many more of these and other errors occur through most pages and these should be corrected.