

## Anonymous Reader

### Comments on “Political Risk Guarantees and Capital Flows: The Role of Bilateral Investment Treaties”

The author examines the influence of political risk guarantees of bilateral investment treaties on foreign investments, and more specifically, on debt and equity flows. By using panel data, the author performs a very detailed econometric analysis. I write below a number of comments that might help to improve the current version of the paper. The section of literature review distinguishes papers focusing on the role for capital flows of political risk, financial liberalization, institutions, opacity and capital controls. A table summarising the main contribution and the main results of the papers mentioned would be very helpful for the reader to follow what is the argument to which the author wants to arrive. At the end, it seems to me, that the author wants to find the main determinants of foreign investments. So, a list with each of the papers associated to one (or several) of the determinants would motivate easier the transition to the next section: the empirical model and data.

#### Response:

Thank you for the suggestion. A table summarizing studies of capital flows determinants is now included in Appendix A.

The section of empirical issues and estimation methodology is very well explained. Nonetheless, the author points out in footnote 16 “Though it is interesting to compare estimation results under (non-collapsed instruments) system and difference GMM, we have decided for paper brevity not to include estimation results in this paper.” But maybe a brief comparison in the section of results could still be desirable.

#### Response:

Because of the serious concern about the system estimation methodology and upon review of the different estimation methodologies adopted in the literature, I have decided to follow the LSDV approach of Binici et al. (2010).

The sub-section of Empirical Results, in my opinion, could be presented in a different way as it is a bit difficult to follow. As suggested in the section of Literature Survey, a summary table might help. The author could display a table stating the expected effect of the parameter associated to each variable, and which is the obtained sign of the coefficient.

#### Response:

Thanks for the suggestion. I have improved the presentation of the estimation results while controlling for country, region and time effects.

According to the author, there are, at least, three “surprising” obtained results: In page 21: “Table 5A shows in specifications 2-9 that an improvement in expropriation risk has a surprisingly direct negative influence on portfolio equity flows”... “The results of tables 6B are surprising and do not match the recent evidence of statistically significant positive relationship between bilateral investment treaties and FDI flows. The results of table 6A are yet more surprising.” Why are these results so surprising? Is not any previous research in the literature that found such results? Are the hypotheses that the author supported going into the other direction? Might some parameters associated to these variables present an ambiguous sign? Maybe some heterogeneity by geographical region might be important here.

#### Response:

Please have a look at the LSDV estimation results and the robustness checks.

In Appendix A, the author lists the “Dependent and Explanatory Variable Means”. However, these means are not presented separately for Asia, Africa, Latin America and Caribbean, MENA countries and Europe. Adding five-six rows to the table with this information could give an idea about whether

regional dummies should be considered in the empirical analysis, or on the convenience of running regressions with some interactions.

**Response:**

Table 3 now presents descriptive statistics focusing on the composition of capital flows in middle and low income countries. Middle income countries use FDI and private debt, while low income countries use FDI and public debt.

Finally, I have the intuition that, even without being following the “Bolivarian Revolution”, countries such as Colombia, bordering Venezuela, and Chile, bordering Argentina, might be affected in terms of capital flows, either positively or negatively, that is: might expropriations in Argentina and Venezuela have affected foreign investments in other countries in the region? Is there any role for (spatial) spillovers? The author could think about other situations and specific examples in MENA countries.

**Response:**

This comment is quite an inspiration for adopting the unobserved region effects. The estimation results have interesting interpretations.