9-19-2018

Commercial Interests in American Foreign Policy, from Dollar Diplomacy to the Trump Administration

Geoffrey Gertz
The Brookings Institution

Follow this and additional works at: https://digitalscholarship.unlv.edu/brookings_lectures_events
Part of the International Relations Commons, and the Public Affairs, Public Policy and Public Administration Commons

Repository Citation
Gertz, G. (2018). Commercial Interests in American Foreign Policy, from Dollar Diplomacy to the Trump Administration. Available at: https://digitalscholarship.unlv.edu/brookings_lectures_events/131

This Lecture is brought to you for free and open access by the Brookings Mountain West at Digital Scholarship@UNLV. It has been accepted for inclusion in Lectures/Events (BMW) by an authorized administrator of Digital Scholarship@UNLV. For more information, please contact digitalscholarship@unlv.edu.
Commercial Interests in American Foreign Policy:

*From Dollar Diplomacy to the Trump Administration*

Geoffrey Gertz
Fellow, Brookings Institution
UNLV Brookings Mountain West
September 2018
"The [intervention] raises serious conflict of interest questions that could impinge on the United States’ ability to conduct effective foreign policy.” – Senator Bob Menendez, letter to US State Department, May 2018
Should we be surprised if the US embassy assisted the Trump Organization in its dispute in Panama?

More generally, when, how, and why does the US State Department intervene to help American companies abroad? And what effects does this have on broader American foreign policy?
Why do investors want diplomats’ help?

• Foreign investment is risky! Once you’ve invested overseas, you’re beholden to the whims of a foreign government

• What recourse do you have?
  » Direct negotiation?
  » Local courts?
An Early Example: “Dollar Diplomacy” in Nicaragua

• La Luz y Los Angeles mining company threatened by Nicaraguan government

• Write to then-Secretary of State Philander Knox requesting help

• US marines ultimately invade Nicaragua, help oust President Zelaya in 1910

• Quote from US consul: La Luz dispute was “the cause of the desire to eliminate Zelaya”
Winners and Losers from “Dollar Diplomacy”

- While businesses gained from their close relationship with political officials, diplomats increasingly questioned such interventions.

- "the whole revolution is inspired and financed by Americans who have wildcat investments down here .... [They hope]" to force the United States to intervene and by so doing make their investments good."
Defending American Sugar in Cuba

- 1959: Fidel Castro’s new “land reform” policy will expropriate many US-owned sugar plantations
- US investors push for aggressive American policy response

But State Department wary:
“… our point of departure must be that keeping Cuba out of the Sino-Soviet orbit, and returning it to the Inter-American system, is more important than the salvaging of the US investment in Cuba to the complete satisfaction of the US business community”
The Diplomats’ Dilemma

- Private companies continued to seek diplomatic assistance, but this commercial work increasingly conflicted with Cold War grand strategy.
- Diplomats were incentivized to focus on the ‘high politics’ of containing communism, not lowly commercial work.
An inside assessment

[The State Department] placed no priority on the commercial function, and those Foreign Service officers who liked commercial work were doomed not to advance in the system. And, let's face it, some officers who were not of the highest caliber ended up getting stuck doing commercial work.

So you had this odd mix of people who were real good at what they did and ended up not getting rewarded, and people who just weren't good at what they did. None of them were judged on the basis of how they did commercial work.”

- Susan Schwab
The Post Cold War Era

- End of Cold War a major shock to the State Department – suddenly need to cultivate a new constituency of supporters
- At same time, markets opening overseas, globalization accelerating
The Post Cold War Era

- State Department pivots to support commercial work
  - Host major conference on commercial diplomacy
  - Strong political backing (especially Warren Christopher and Hillary Clinton)
  - Reforms to training programs, staff incentives
Enron’s Dabhol Plant in India

- Pricing dispute between Enron and Indian government in early 2000s
- US ambassador to India, Secretary of State, and Vice President all raise dispute with Indian officials
- A “Dabhol Working Group” is formed at NSC
- Initially on the agenda for heads of state meeting; Enron scandal emerges that same week
Occidental in Ecuador

- Ecuador government threatens to cancel Oxy’s contract
- Immediate US diplomatic response in Quito and Washington
- US eventually cancels free trade agreement negotiations
How Common are these Cases?

- Enron and Oxy unique cases, reported in public domain
- But most commercial diplomacy occurs behind closed doors >> difficult to study
- New data source: leaked State Department cables
A New Dataset

• We search the online database of internal State Department cables publicly released by Wikileaks.

• Identify 440 individual investment disputes involving American companies and foreign governments
## Evidence from Diplomatic Cables

<table>
<thead>
<tr>
<th>Category</th>
<th>Level of Engagement</th>
<th>Type of engagement</th>
<th># disputes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Explicit Issue Linkage</td>
<td>5</td>
<td>USG official explicitly links investment dispute to aid, trade or other host state government priority.</td>
<td>9</td>
</tr>
<tr>
<td>High-Level Diplomatic Agenda</td>
<td>4</td>
<td>Embassy raises dispute with host country head-of-state or USG officials raise dispute during an official visit.</td>
<td>66</td>
</tr>
<tr>
<td>Mid-Level Diplomatic Agenda</td>
<td>3</td>
<td>Embassy raises dispute with host state minister or legislator; Washington-based USG official or legislator raises issue with host state embassy in US.</td>
<td>56</td>
</tr>
<tr>
<td>Technocratic Intervention</td>
<td>2</td>
<td>Embassy raises dispute with low ranking host state official (including disputes in which it was impossible to discern at what level the embassy raised the issue with the host state).</td>
<td>117</td>
</tr>
<tr>
<td>No intervention</td>
<td>1</td>
<td>Cables specifically mention that the company did not approach the USG for assistance or that the USG did not intervene in the dispute.</td>
<td>42</td>
</tr>
<tr>
<td>Insufficient Data</td>
<td>NA</td>
<td>No evidence in the cables that the embassy discussed dispute with host state officials.</td>
<td>150</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>440</td>
</tr>
</tbody>
</table>
What do the cables reveal?

- Diplomatic interventions are common.
- But Enron and Oxy examples are outliers: aggressive engagement is rare, more likely to see lower level, day-to-day diplomatic work.
Gerald Metals in Tajikistan

- Contract dispute between commodity trader and Tajik state-owned company
- No aggressive pressure, but US continually raises dispute during bilateral meetings
- Ultimately resolved through informal talks at dinner banquet
How valuable is diplomacy for American firms?

- Looking at individual cases we see some evidence of how diplomacy helps resolve disputes. But how to test more systematically?
Exploiting Ambassador Vacancies

- Ambassadors often play a crucial role in resolving disputes. But ambassadors rotate in and out of countries.
- Do companies suffer when there’s no ambassador present?

» Yes!
Ambassador Vacancies and Investment Arbitration Claims

• Overall, likelihood of an American investor filing an investment arbitration claim about 25 percent higher during ambassador vacancies.

• If ambassador is vacant for a year in a country with weak rule of law, expected number of arbitration claims is twice as high.
How does today’s diplomacy compare to earlier eras?

- Commercial interests are again an important component of US foreign policy
  - But we’re not sending in the marines anymore
- Diplomats aren’t bowing to private pressure; they’re more likely to take the initiative themselves
- Commercial diplomacy supports, rather than conflicts with, other diplomatic goals
  - Supporting capitalism and market-based economic models in developing countries
Conclusions and Implications

• A strong, well-resourced diplomatic corps provides benefits to American companies

• With growing nationalist economic competition, commercial diplomatic likely to expand

• Academics pay lots of attention to formal rules and institutions governing the global economy; but informal interactions matter too!
Thank You!

Geoffrey Gertz
Fellow, Brookings Institution
gtgertz@brookings.edu
### DV: Investment arbitration claims

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Count model</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ambassador vacancies</td>
<td>0.793***</td>
<td>2.886***</td>
<td></td>
</tr>
<tr>
<td>(0.392)</td>
<td>(1.042)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ambassador vacancies × rule of law</td>
<td>-1.219*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(0.628)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Extended ambassador vacancy</td>
<td></td>
<td>1.911**</td>
<td></td>
</tr>
<tr>
<td>(0.764)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Extended ambassador vacancy × rule of law</td>
<td>-0.824*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(0.469)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Rule of law</strong></td>
<td>-0.059</td>
<td>-0.21</td>
<td></td>
</tr>
<tr>
<td>(0.403)</td>
<td>(0.388)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Investment climate</strong></td>
<td>-0.212***</td>
<td>-0.172**</td>
<td>-0.188**</td>
</tr>
<tr>
<td>(0.072)</td>
<td>(0.077)</td>
<td>(0.075)</td>
<td></td>
</tr>
<tr>
<td><strong>Arbitration claims (lagged)</strong></td>
<td>0.148</td>
<td>0.137</td>
<td>0.133</td>
</tr>
<tr>
<td>(0.128)</td>
<td>(0.123)</td>
<td>(0.120)</td>
<td></td>
</tr>
<tr>
<td><strong>Democracy</strong></td>
<td>0.047*</td>
<td>0.059**</td>
<td>0.052*</td>
</tr>
<tr>
<td>(0.026)</td>
<td>(0.027)</td>
<td>(0.027)</td>
<td></td>
</tr>
<tr>
<td><strong>Natural resource rents</strong></td>
<td>0.314**</td>
<td>0.274**</td>
<td>0.255*</td>
</tr>
<tr>
<td>(0.134)</td>
<td>(0.140)</td>
<td>(0.141)</td>
<td></td>
</tr>
<tr>
<td><strong>GDP PC (log)</strong></td>
<td>7.617**</td>
<td>7.665**</td>
<td>7.331*</td>
</tr>
<tr>
<td>(3.598)</td>
<td>(3.834)</td>
<td>(3.765)</td>
<td></td>
</tr>
<tr>
<td><strong>GDP PC(^2) (log)</strong></td>
<td>-0.456**</td>
<td>-0.459*</td>
<td>-0.435*</td>
</tr>
<tr>
<td>(0.222)</td>
<td>(0.235)</td>
<td>(0.230)</td>
<td></td>
</tr>
<tr>
<td><strong>Constant</strong></td>
<td>-39.035**</td>
<td>-38.487**</td>
<td>-36.460**</td>
</tr>
<tr>
<td>(16.095)</td>
<td>(16.899)</td>
<td>(16.524)</td>
<td></td>
</tr>
</tbody>
</table>

### Inflation model

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ratified BIT</strong></td>
<td>-3.612***</td>
<td>-3.615***</td>
<td>-3.534***</td>
</tr>
<tr>
<td>(0.707)</td>
<td>(0.738)</td>
<td>(0.748)</td>
<td></td>
</tr>
<tr>
<td><strong>US FDI stock (log)</strong></td>
<td>-0.438**</td>
<td>-0.488**</td>
<td>-0.482**</td>
</tr>
<tr>
<td>(0.206)</td>
<td>(0.235)</td>
<td>(0.234)</td>
<td></td>
</tr>
<tr>
<td><strong>Constant</strong></td>
<td>11.887***</td>
<td>12.936***</td>
<td>12.784***</td>
</tr>
<tr>
<td>(4.273)</td>
<td>(4.939)</td>
<td>(4.927)</td>
<td></td>
</tr>
</tbody>
</table>

---

**Note:** Standard errors in parentheses. Statistical significance: *p < 0.1, **p < 0.05, ***p < 0.01.
Figure 1. Ambassador vacancies, investment arbitrations, and the rule of law

Note: Weak rule of law defined as the tenth percentile among developing countries in the World Bank’s World Governance Indicators rule-of-law index, while strong rule of law is the ninetieth percentile among developing countries. The figure is based on results of Model 2. Shaded areas show 90 percent confidence intervals.