Reputation and Dispute Settlement in International Investment Agreements*

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Abstract

Does reputation matter in international relations? This study explores this question by looking at Foreign Direct Investment (FDI). The dilemma: FDI drives economic growth, but governments of low-income countries also face a temptation to expropriate foreign investors (i.e. by nationalizing assets) to redistribute wealth. As scholars noted, when countries expropriate they may suffer damage to their reputation as safe investment locales, especially when investors lodge complaints with international arbitration institutions, discouraging future FDI. This project examines how international arbitrations shape host states' reputations and FDI flows. Current studies assume that any dispute is harmful for the host country involved: the government's trustworthiness is diminished, regardless of the outcome. This study proposes a new reputational mechanism in which the outcome of a dispute matters. When countries lose a dispute, their reputation takes a hit; but when they win or settle a dispute, their reputation in fact improves. The study highlights governments' incentives to increase transparency in dealing with investors and the impact of transparency on capital flows.

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Does reputation matter in international relations? Does reputation matter when international investment is involved? This study explores this fundamental question by looking at Foreign Direct Investment (FDI).

Foreign direct investment (FDI) is the largest source of capital inflow in the developing world (Singer 2010). It is resilient with respect to crises and its impact is significant and increasing (Loungani and Razin 2001; Büthe and Milner 2014): the nominal amount of total FDI flows in the world is more than tripled since 1997. Dealing with foreign investment is one of the most problematic issues in global governance and in the negotiation of some economic and trade agreements, such as the Canada-EU CETA (Pelc 2017).

FDI presents a dilemma, however: while it drives economic growth and technology transfer to host countries, governments of low-income countries also face a temptation to expropriate foreign investors, whether directly (i.e. by nationalizing assets) or indirectly (e.g. by changing regulations), to redistribute wealth.

Governments uphold their commitments with foreign investors most of the time – yet not always. In 2006 newly-elected president Morales of Bolivia nationalized the entire natural gas industry two days into office; president Chavez in Venezuela expropriated two oil fields from French and Italian companies that same year. Li (2009) finds over 500 acts of direct expropriation between 1960 and 1990. Expropriation is not a thing of the past.

At the same time, when they expropriate, host countries may suffer damage to their reputations as safe investment locales, discouraging future FDI. To assuage investors' concerns, governments of low-income countries signed many bilateral treaties meant as a credible commitment to investors, because the treaties allowed foreign investors to unilaterally initiate an international arbitration process against the host state (i.e. in case of breach of contract). As Figure - shows, in the past thirty years we have seen a remarkable increase in the number of these Bilateral Investment Treaties (BITs), as well as an almost exponential increase in the total number of disputes. It is worth noting that before BITs only another state could file a claim against a state (Simmons 2014).

There is consensus in the current literature that when a government is involved in a dispute its reputation is tarnished. If that is so, why have we been observing increasing levels of FDI over the years, with the nominal amount of global FDI flows more than tripling since 1997? Does reputation, as affected by investment disputes, play a more nuanced role in FDI allocation?

This study deals with how international reputation is built and affects

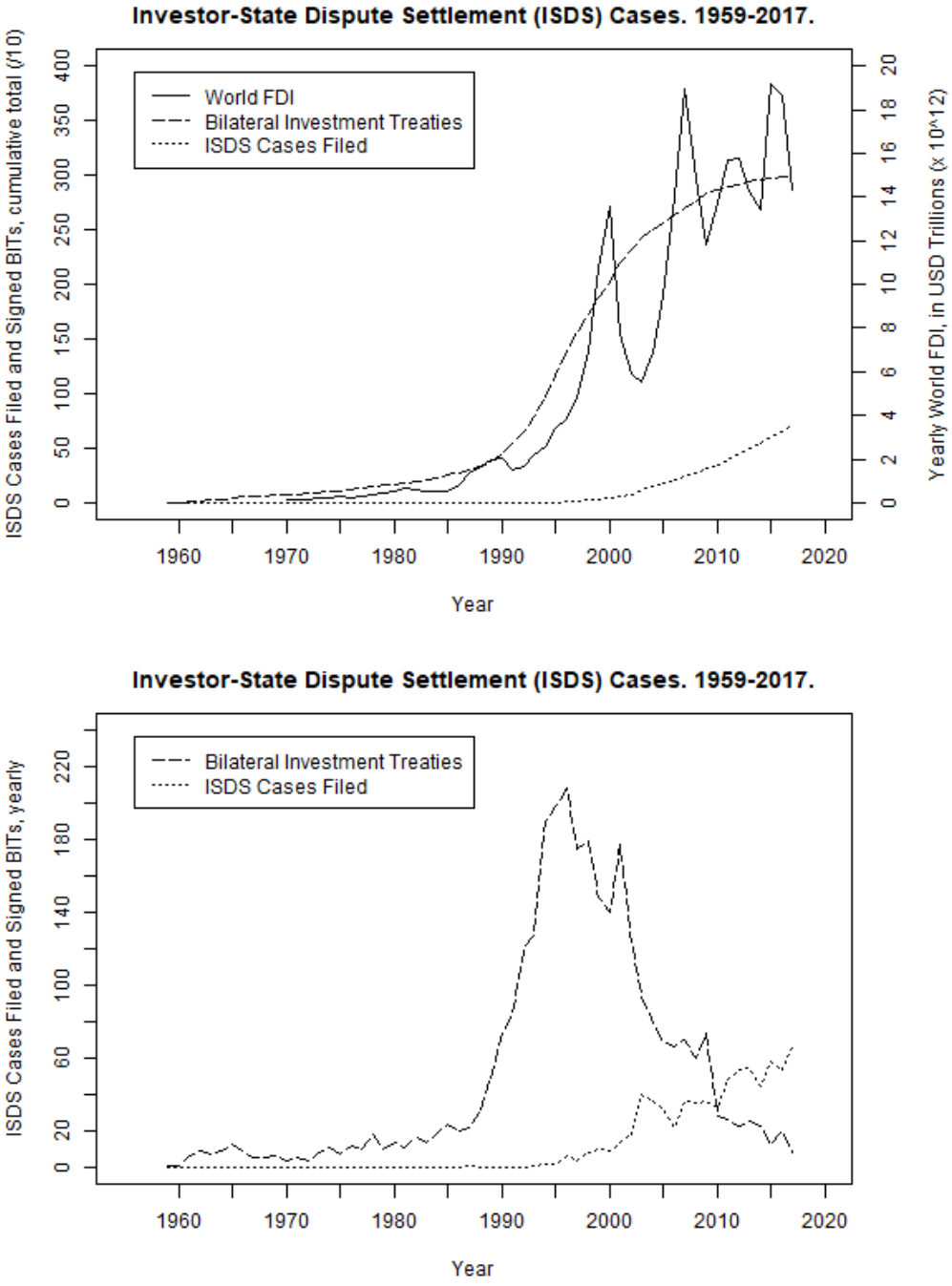

Figure 1: BITs and ISDS Cases – Cumulative (top) and Yearly (bottom)

cooperation on investment, by looking at the effects of dispute settlement institutions on FDI flows. The process under study focuses on what happens after an investor files a case against a host country. How does the FDI of the host country change in response to the new information now available to current and potential investors?

Current studies assume that any dispute process is harmful for the host country involved: the government's trustworthiness is diminished for current and potential investors, regardless of the outcome of the dispute, which results in decreased investments. This study proposes a new reputational mechanism in which the outcome of a dispute matters. When countries lose a dispute, their reputation takes a hit; but when they win a dispute, their reputation may in fact be strengthened – leading to increased investments.

Section 1 introduces the research question. Section 2 discusses in some detail three articles that directly speak to the research question. Section 3 introduces a new reputational theory of FDI, with a discussion of its causal mechanism. Section 4 articulates observable implications of the theory tests the expectations on an original dataset I assembled from a selection of investor-state disputes. Section 5 concludes.

1 Bilateral Investment Treaties and Dispute Settlement

An investor of a capital-exporting country – i.e. the *home* country – usually can file an investor-state dispute only if the home country has signed a Bilateral Investment Treaty (BIT) with the *host* country. A BIT establishes the terms and conditions for private international investment between two countries.

There is no definite consensus in the literature as to whether BITs have a positive impact on FDI. Some say BITs are only effective when the domestic institutions of the host country are already trustworthy (Jensen 2003; Jensen 2008; Tobin and Rose-Ackerman 2011), while others find BITs are most effective for states who lack credibility (Rosendorff and Shin 2012). Some say BITs have a positive impact on FDI because they have repercussions if breached (Allee and Peinhardt 2011), while others are more skeptic (Tobin and Rose-Ackerman 2011; Büthe and Milner 2014). This hints to the potential costs of BITs (Jandhyala et al. 2011), which may not always

be taken into account by the signatories due to competitive pressures with other potential host countries (Elkins et al. 2006). Simply put, there seem to be no definitive agreement as to whether BITs increase FDI flows (Sauvant and Sachs 2009).

There is instead a wide consensus that the single most important aspect of a BIT consists in its investor-state dispute settlement clauses (Franck 2006). This "normative breakthrough" in investment law (Tarcisio Grazzini, cited in Simmons 2014) endows private investors with the right to sue a government for damage and to choose the forum in which to do so. Before BITs, only states were allowed to initiate a dispute, as it is the case for the World Trade Organization (Simmons 2014). By far the most used venue for investor-state dispute settlement (ISDS) is the International Court for the Settlement of Investment Disputes (henceforth ICSID, or 'the Court'), followed by the *United Nations Commission on International Trade Law* (UNCITRAL).

Allee and Peinhardt (2010) find systematic variation in legal delegation to the ICSID across BITs: home governments generally prefer ICSID clauses while host governments are generally hostile towards them (but more likely to consent when constrained by their dependence on the global economy). The variation across BITs seems to be driven by capital-exporting countries (Manger and Peinhardt 2017), which can tailor BITs to their needs.

Some argue that after countries experience even a single ISDS case, they are likely to stop signing international investment agreements – including BITs (Poulsen and Aisbett 2013). Yet, not all countries have stopped signing them (Manger and Peinhardt 2017) and, in any case, BITs are usually in force for ten or fifteen years after their termination. Hence, in the short and medium term the relevance of BITs for FDI is hard to question. Furthermore, while some interpret the explosion of the number of filings as a breakdown in the legitimacy of BITs (Simmons 2014), other see that as a consequence of increased trust in the regime (Wellhausen 2015). The key issue hinges on whether investors actually heed to the outcomes of arbitrations in making their investment decisions.

2 Current Theories of the Effects of Dispute Settlement on Foreign Direct Investment

There are only three works, to my knowledge, that deal explicitly with the relationship between FDI inflow and ISDS outcomes (Allee and Peinhardt 2011; Wellhausen 2015; Aisbett et al. 2018). In this section I take them up in turn, pointing out their causal mechanisms and empirical strategies. Previous studies either look at aggregate measures, without taking into account how bilateral relations may affect reputation; or focus only on the negative consequences of a worsened reputation, without even considering the potential positive impact of an improved reputation. This section clarifies these two issues in context, while my proposed way to deal with them is presented in the next section.

Allee and Peinhardt (2011) find that a positive relationship between BITs and FDI holds conditional on good behavior on the part of states. In their interpretation, this means that, on average:

AP1: An additional BIT leads to more FDI.

AP2: An additional ISDS filed against a host state leads to less FDI.

AP3: An additional ISDS lost by a host state leads to less FDI.

They look at ICSID cases only, and only at those cases in which BITs are a legal instrument invoked. Their paper seems to suggest that any ISDS activity would be a negative signal to current and potential investors. They use aggregate measures of BITs (total BITs active in a given year for a given country) and aggregate measures of FDI (total FDI inflow in a given year for a given country). The analysis focuses on the years 1984-2006 (the first ICSID case involving BITs was filed in 1987).

However, aggregate measures may not reveal the whole story, because firms of a same nationality may respond only to cases that affect them or their conationals directly. Wellhausen (2015) points out that arbitration may only matter within a specific home-host relationship and that at the aggregate level of analysis much information would be lost. Hence, she focuses on bilateral FDI flows after a case is filed within a host-home dyad. She looks ISDS cases in general, and finds that:

W1: A host state is likely to see its FDI inflow from a given home state decrease once it breaches a contract with an investor from that home state.

W1b: When the host country breaches a contract against an investor from a given home state, the breach only affects the behavior of investors

from that home state, not others.

W2: For a given host country: the larger its set of home states, the more likely the host country will be to breach its contracts with some of them, *because* the impact of each breach is limited to one host country.

Wellhausen's 'breach of contract' is based on whether there are cases filed against a host country in any given year. This concerns a *perceived* breach of contract by an investor who believes she has a case worth filing[1].

Hence, Wellhausen (2015) makes no distinction as to whether a case is eventually won by the investor or by the home state. A filing does not give us enough information by itself to determine whether a contract has *actually* been breached, unless we are willing to entirely discount the work and the output of the arbitration tribunals (i.e. every filing is unambiguous evidence of wrongdoing on the part of the state). Were it so, it is not clear to me that the tribunals would have any independent effect at all, or that they would be of much use to investors or states alike.

In a similar fashion, Aisbett et al. (2018) look at host-home dyads to test different mechanisms through which BITs may have an effect on FDI allocations. They also look at all available ISDS and find evidence supporting the hypothesis that BITs are best understood as 'deterrents'. Namely:

ABN1: A BIT increases bilateral FDI only if the host country has never taken part in an investment arbitration.

ABN1b: A single arbitration (i.e. filing of a case) causes a significant reputational damage to the host country which leads to a significant decrease in FDI to the host country from the home country of the dissatisfied investor.

They focus on the period 1990—2008. They find that deeper integration leads to more breaches of contract, as host countries with FDI coming from a greater number of home countries expect less FDI decrease than, say, a host whose entire FDI comes from one or two home countries.

None of these articles looks at the different consequences different case outcomes may have[2]. When an investor files a case, she can win, lose or settle – does that matter?

[1] An investor may even file a case for other reasons, without even the perception of a breach of contract. The other possible option, in which there is a breach and no perception of a breach, is immaterial to this discussion, as it involves no arbitration and no reputational consequences

[2] A possible exception can be Aisbett et al. (2018, Table 6). Even then, however, the issue is not theorized or discussed in depth.

3 A Reputational Theory of Foreign Direct Investment

This section develops a reputational theory of FDI where the unit of analysis is the international investor (Investor) and the decisions she makes in the allocation her FDI. Investor is based in the home country and invests in a host country. The hypothesis is that international investors are boundedly-rational decision makers that update their beliefs about the trustworthiness of potential host countries based on publicly available information on investment arbitrations. I follow Tomz (2007, in the context of sovereign debt) in relaxing the assumption of complete information and allowing preferences of host states to change over time. Let us expand on these two points.

Allowing the preferences of states to change over time is different from stating that the incentives of states may change over time. The obsolescing bargaining literature makes it clear that investors have the upper hand before an investment is sunk, because of benefits to a potential host; after an investment is sunk, the host country has the upper hand and a potential incentive to renege on the agreement (Kobrin 1987). This time-inconsistency problem is due to a structural change of the relationship between the parties. What I refer to here, with Tomz (2007), is the possibility that a host state may change its mind after an investment is sunk not because of the structural change in the relationship with the investor, but because of a political development (i.e. a turnover of the executive) or another reason that is distinct from the time-inconsistency structural problem.

The second point is that investors do not have complete information over the preferences of states – they do not observe their true 'type'. They do not know beforehand whether a state is the 'lemon' type or the 'fair-weather' type or the 'stalwart' type in upholding its commitments with foreign investors (from Tomz 2007). A stalwart is a host state that abides by its agreements during good times and bad. A fair-weather is a host that may breach its agreements during bad times (i.e. an economic or currency crisis). A lemon is a country that may breach its agreements during good times and bad. Investors can only infer a host country's type from the its past behavior.

Reputation is sticky and fragile at the same time. Ceteris paribus, investors are likely to have the same trust in a host country tomorrow than they have today – but new relevant information can have a large impact.

The theory relies on two assumptions.

One, reputation is entropic, or asymmetrical. With new information, while it is easy to fall from grace, it is much harder to get back on an investor's good side. There is evidence that individuals may be more supportive of punishing negative reciprocity than rewarding positive reciprocity (Chilton et al. 2017), consistently with evidence from psychology and economics (Fehr and Gächter 2000).
Corollary: reputation offers possibilities of redemption. Hence, and contrarily to the current literature, it may not be the case that every investment arbitration has *only* a negative effect on the reputation of a host country[3].

Two, reputation has an horizon. I do not expect that every information that could potentially be known by an investor be actually known. Reputation only travels so far: investors look at other investors from the same home country, or that deal in the same investment sector, or in the same host country.

It is so for two reasons: relevance/attention and networks. First, each bilateral relationship involves one BIT, and BITs may have different rules; hence investors may learn more relevant information if they look at cases that were disputed under the same BIT (i.e. same home-host dyad), which makes it more likely that they pay attention to them. As far as networks are concerned, information is more likely to be shared and trusted among firms from the same home country.

These two points, taken together, are the innovative contribution of this project.

The null hypothesis is that investors pay no heed to information produced by investment arbitrations when deciding where to invest. I.e., reputation (based on the publicly available data on investment arbitrations) has no role.

An alternative hypothesis, which is the current state of the literature as I understand it, is that investment arbitrations only produce negative signals by suggesting investors where not to invest (Allee and Peinhardt 2011; Wellhausen 2015; Aisbett et al. 2018).

My hypothesis is that the effect of ISDS case depends also on its outcome and need not always be a negative signal to investors (i.e. if the host country wins or settles the arbitration).

[3]It could still have a negative *net* effect.

3.1 Step-by-Step: Itinerary of an ICSID Case and Causal Mechanism

This subsection details the process of an ICSID case from the point of view of an international investor. It then discusses in detail the causal mechanism of the reputational theory.

Either the Investor *believes* Host (state) has breached an agreement, or Investor *does not believe* Host has breached an agreement.

If Investor believes Host has breached an agreement. Investor can resolve the issue promptly with Host, if they both agree to a solution. If they do not, Investor can file a complaint at the ICSID[4]. The ICSID will constitute a tribunal to evaluate the dispute and then render its award. The Court will decide on the justiciability of the dispute (whether the tribunal has jurisdiction) and on the claims made by Investor. If the claims are upheld in part or in full, then Host loses the case. If those claims are found without legal merit or are dismissed in their entirety, Investor loses the case.

On the other hand, if Investor does not believe Host has breached an agreement, it can (i) do nothing or (ii) file a case for other strategic reasons, such as strengthening its bargaining position for contract renegotiations (Pelc 2017; Calvert 2017).

Three remarks on this process. First, the entire case develops conditional on non-settlement by the parties both before and after the filing (since they have the faculty to discontinue the proceedings at any moment before the award is produced). Second, the possibility for Investor to file a case even when Investor believes there has been no wrongdoing showcases the fundamental asymmetry of the investor-state arbitration regime (Simmons 2014). Third, this asymmetry itself makes it all the more important to look at the output of the tribunal to evaluate the potentially very 'noisy' information produced by the filing of a dispute.

In general, it bears keeping in mind that cases are costly for investors: on average, legal fees for each party in 2011-2015 were over 5 million U.S. dollars (the median was 3 million). Additional 900,000 U.S. dollars on average are spent for tribunal costs, often split equally between the parties (Commission 2016). Besides, cases often take years and may generate some additional economic or political difficulties with the host country (Wellhausen 2015).

What can an observer infer from witnessing this process? What follows

[4]There are other venues for investor-state arbitrations, but I focus on ICSID for now.

details the causal mechanism of the theory.

Given that filing a case is costly, it tells an observer it is likely Investor believes Host broke its promises. I would expect the observer to invest less in Host, ceteris paribus.

If a case is lost by Host, the observer will be even more likely to think that Host breached an agreement. Hence, I would expect a further diminution of investment in Host.

If a case is won by Host, the observer may not diminish its investment in Host. This is because Host is not likely to win a case if it did breach its agreement[5].

If a case is settled, and since the terms of settlements are usually not public, an observer has no way of knowing whether they favor Investor or Host. Pelc (2017) suggests that settlements are equivalent to a loss by Host, but this cannot be clear to the observer without prior beliefs or information beyond ICSID proceedings. I propose that a settlement may suggest to an observer that: (i) Investor settled because she did not believe her case to be strong enough after all; or that (ii) Host settled because it decided to appease Investor somehow. In either case, this would confirm that Host indeed does nurture a favorable investment climate. Note that with a settlement both parties also save money on the costs of the proceedings.

This discussion assumes there is an active BIT between host and home, otherwise the case could not be filed. Besides, these multiple effects (filing, settling, losing, winning) are all different in principle and can be combined, which makes them more difficult to identify. I.e., Host can see its aggregate FDI diminish even after winning a case, due to the effect of filing (had it lost the case, the diminution would have been much greater counterfactually).

[5]The investor-observer may conclude that Investor filed a case for other reasons (i.e. Investor does not believe Host violated the BIT). An alternative hypothesis is that if Host wins an arbitration then it can not only breach an agreement, but even get away with it (against the theory proposed here). There is currently little empirical support that this is the case, especially considering that investors can choose the venue of arbitration. Besides, this is not an information that would come to the observer based on the Court proceedings, and can in principle be tested with interviews and survey experiments, as I discuss below.

4 Methodology

The question the statistical analysis aims to answer is how FDI flows vary in response to investment arbitrations. Using multivariate regression, I estimate the effects of different ISDS outcomes on FDI flows. To my knowledge, no previously published research has looked at the effect of arbitrations won by the host state – these effects have been generally assumed away.

4.1 Hypotheses

The statistical analysis looks at bilateral FDI flows as a proxy for the reputation of a host country in the eyes of investors. It is assumed that investors from the same nationality behave similarly and have access to similar information[6]. Two are the hypotheses to be tested:

HP1: Reputation has an horizon. Investors are more likely to be influenced by ISDS cases relevant to *their* investments. i.e., involving the host country in which they are investing. While this effect may be lost in the aggregate, it should be evident by looking at bilateral flows.

HP2: An investment arbitration can have different effects on FDI inflows of the host country depending on the outcome. Specifically: (i) a case won by the host country has a positive effect on FDI; (ii) a case lost by the host country has a negative effect on FDI; (iii) the filing of a case has a negative effect; (iv) a case settled has a positive effect on FDI.

Table 1: Expectation of ISDS Activity Effects on Host FDI Inflow

ISDS Activity	Current Literature	Hypothesized Effect
Case Filed against Host	$-$	$-$
Host Loses a Case	$-$	$-$
Case is Settled	$(-)$	$+$
Host Wins the Case	n/a	$+$

The sign indicates the expected direction of co-variation for the corresponding ISDS-related event. The current literature is not too clear on what expect when a case is settled; partial exceptions are Allee and Peinhardt (2011) and Pelc (2017). The literature is silent on what to expect when a host country wins a case.

[6]This assumption is necessary for the data I use here. Nothing prevents this assumption from being relaxed and the theory tested on firm-level data.

I focus only on ISDS cases for which a BIT is a legal instrument invoked in the dispute.

4.2 Data and Variables

The dataset is time-series cross-sectional with directed dyads (home country → host country). The dataset includes 236 host countries and the years 2001–2012.

The dependent variable is FDI flow (in US dollars), as disseminated by UNCTAD[7]. The dyads included in the dataset are all those dyads for which there is at least one available observation of FDI flow within the indicated time window. For the analysis FDI flows have been transformed using the Inverse Hyperbolic Sine (IHS), which allows us to interpret the results more or less as if the transformation had been logarithmic. The IHS has the added advantage to work with negative values (i.e. negative FDI flows) and zero values, unlike a logarithmic tranformation.

The main predictors of interest are variables connected with the existence of Bilateral investment treaties in a dyad, as well as the filing and outcomes of ISDS cases. For BITs, the datasets includes dummies that record the dyad-years when a BIT was active in the dyad (signed or in force). For ISDS data, the datasets aggregates each ISDS case ever filed where BITs are a legal instrument invoked in the case. For BITs and ISDS data the main source is UNCTAD[8].

To control for the potential effects BITs outside of the dyad may have, I include a count of all of the BITs signed by the host country until that time. To control for the variation of available FDI across years, I include the total FDI received by that host in a given year.

Note that the percentage frequency distribution of the data in the table, which includes only ISDS cases where at least a BIT is a legal instrument, mirrors almost perfectly the total distribution of ISDS cases in general[9]

Furthermore, note that – due to the limited availability of other variables, most notably FDI bilateral data – the analyses below mostly rely on ISDS data within 2001–2012.

[7]UNCTAD's FDI Statistics: https://unctad.org/en/Pages/DIAE/FDI%20Statistics/FDI-Statistics-Bilateral.aspx.

[8]UNCTAD's Investment Policy Hub: https://investmentpolicyhubold.unctad.org/.

[9]UNCTAD's Investment Policy Hub: https://investmentpolicyhubold.unctad.org/ISDS.

Table 2: Frequency Distribution of ISDS Cases Where a BIT Is Involved. 1987–2018

ISDS Case Status	%	Count
Won by investor(s)	31.1	140
Won by host state	36.0	162
Settled or discontinued	30.6	138
Tied	2.2	10
Total ISDS Concluded Cases	100	450
Additional Pending Cases	–	275
Total ISDS Cases Filed (BIT)	–	725

As of December 31, 2018. Table based on dataset put together by the author. Source for ISDS data: UNCTAD Investment Policy Hub.

The control variables included are those established in the literature (for example, Allee and Peinhardt 2011; Wellhausen 2015). I include GDP per capita (ln) and GDP growth of host and home (World Bank data). Also included is a measure of bilateral trade from the Correlates of War Trade Statistics when available (Barbieri Katherine and Pollins 2009; Katherine and Keshk 2016), otherwise from the IMF Direction of Trade.

A measure of political constraints (as constructed by Henisz 2002) is added because evidence suggests that democratic countries are more likely to include ISDS clauses in their BITs (Simmons 2014). Lastly, I include host country population and a measure of capital account openness (Chinn and Ito 2006).

4.3 Results

Table 3 shows the models estimated. The coefficients of the variables of interest can be compared, as they have been run on the same set of data. In each case, each predictor is lagged one period to somewhat limit the possibility of reverse causation.

Model (1) includes only the ISDS variables of interest. The results show that, at the .05 significance level, we cannot reject the hypotheses that a filing of a case and a case won by the investor are associated with diminished

FDI inflows. Furthermore, we cannot reject the hypothesis that a settled case is associated with an increase in FDI inflow – as discussed in theory section. To my knowledge, this is a novel result.

Model (2) includes dyad and year fixed effects; model (3) adds variables pertaining to BITs; model (4) further adds a series of controls. The results remain basically the same across all models, even when we include dyad and fixed effects which, as known, bias coefficients towards zero and make it less likely to obtain statistical significance, making estimates more conservative. This seems to support our second hypothesis, HP2.

Regarding our first hypothesis, HP1, notice how whether or not there is a signed BIT in the dyad has a positive and significant effect that is an order of magnitude larger than the effect of another BIT. This is consistent with the idea that investors pay more attention to BITs that affect a specific FDI flow directly.

The same models were also run using cumulative values for the previous two years and five years (i.e. the total number of ISDS cases filed in the past two years and in the past five). The results are shown in Table 4, for both the previous two years and the previous five years, with and without controls.

The negative coefficients of a case filed are smaller in magnitude and not statistically significant when we look at the last two years – but they are still significant when we look at the last five years.

The negative coefficients of the cases lost by the host state in the past two years are statistically significant and of smaller magnitude as the effect of cases lost in the previous year, which makes sense as investors tend to react quickly to new information – especially if it is negative information about the host state.

The positive coefficient of a settlement is smaller and statistically significant if we look at the past two years, and it peters out even more if we look at the past five years.

We can also observe a positive and statistically significant effect (to the .05 significance level) associated with the cases won by the host state in the past two years. This is consistent with what we would expect given our hypotheses. Remarkably, the positive effect of a case won by the host state is about half the size of the effect of a case lost by the host state, which suggests that awards and punishments by investors are given out asymmetrically (as discussed in Section 3).

As they have not been documented before, positive effects associated with

Table 3: Previous Year Effects of ISDS Cases on Bilateral FDI Flows. 2001–2012.

	(1)	(2)	(3)	(4)
BIT signed, dyad (dummy)			0.428**	0.307*
			(0.170)	(0.165)
Tot. BITs signed, host (count)			0.034**	0.026**
			(0.007)	(0.007)
Pending cases, dyad	0.499**	0.070	0.060	0.024
	(0.126)	(0.197)	(0.197)	(0.189)
Total FDI host				0.055**
				(0.018)
Filed, count	-0.657**	-0.455*	-0.443*	-0.397*
	(0.222)	(0.233)	(0.228)	(0.223)
To Investor, count	-1.675**	-1.795**	-1.777**	-1.751**
	(0.392)	(0.826)	(0.824)	(0.814)
To State, count	0.252	-0.106	-0.085	0.036
	(0.473)	(0.473)	(0.458)	(0.468)
Settled, count	1.565**	1.514**	1.549**	1.599**
	(0.477)	(0.662)	(0.675)	(0.672)
Tied, count	-0.306	-0.798**	-0.681**	-0.909**
	(2.287)	(0.107)	(0.106)	(0.123)
Trade, dyad				0.064**
				(0.025)
Pol. Constraints, host				0.255
				(0.196)
GDPpc (ln), host				1.386**
				(0.313)
GDP Growth, host				0.012*
				(0.007)
Pop. (ln), host				4.594**
				(0.719)
Capital Openness				-0.490**
				(0.218)
GDPpc (ln), home				0.168
				(0.294)
GDP Growth, home				0.008
				(0.007)
Constant	1.872**	1.197**	-0.144	-89.687**
	(0.055)	(0.057)	(0.240)	(13.799)
N	14459	14459	14459	14459
Dyad Fixed Effects	No	Yes	Yes	Yes
Year Fixed Effects	No	Yes	Yes	Yes

p<.1, ** p<.05, *** p<.01. The dependent variable is always a the Inverse Hyperbolic Sine (IHN) of a host country's bilateral FDI inflow. The label "To Investor" refers to cases awarded in favor of the investor (i.e. cases lost by the host state).

Table 4: 2-Year and 5-Year Cumulative Effects of ISDS Cases on Bilateral FDI Flows. 2001–2012.

	2-Year	5-Year	2-Year	5-Year
BIT signed, dyad (dummy)	0.431**	0.432**	0.309*	0.310*
	(0.170)	(0.170)	(0.165)	(0.165)
Tot. BITs signed, host (count)	0.034**	0.034**	0.026**	0.026**
	(0.007)	(0.007)	(0.007)	(0.007)
Pending cases, dyad	0.221	0.287	0.159	0.208
	(0.265)	(0.197)	(0.262)	(0.189)
Total FDI host			0.057**	0.056**
			(0.018)	(0.018)
Filed(2y), count	-0.276		-0.215	
	(0.173)		(0.169)	
To Investor(2y), count	-1.468*		-1.441*	
	(0.805)		(0.799)	
To State(2y), count	0.710**		0.784**	
	(0.266)		(0.281)	
Settled(2y), count	1.219**		1.271**	
	(0.539)		(0.547)	
Tied (2y),count	0.261**		-0.126	
	(0.103)		(0.126)	
Filed(5y), count		-0.299**		-0.240*
		(0.151)		(0.138)
To Investor(5y), count		-0.287		-0.293
		(0.490)		(0.482)
To State(5y), count		0.507		0.525
		(0.386)		(0.382)
Settled(5y), count		0.799		0.832
		(0.500)		(0.509)
Tied (5y),count		1.079**		0.549**
		(0.115)		(0.143)
Trade, dyad			0.064**	0.064**
			(0.025)	(0.025)
Pol. Constraints, host			0.254	0.261
			(0.196)	(0.196)
GDPpc (ln), host			1.383**	1.394**
			(0.313)	(0.314)
GDP Growth, host			0.012*	0.011*
			(0.007)	(0.007)
Pop. (ln), host			4.596**	4.588**
			(0.723)	(0.723)
Capital Openness			-0.482**	-0.495**
			(0.219)	(0.220)
GDPpc (ln), home			0.177	0.179
			(0.295)	(0.295)
GDP Growth, home			0.008	0.007
			(0.007)	(0.007)
Constant	-0.138	-0.152	-89.797**	-89.759**
	(0.240)	(0.240)	(13.861)	(13.866)
N	14459	14459	14459	14459
Dyad Fixed Effects	Yes	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes	Yes

p<.1, ** p<.05, *** p<.01. The dependent variable is always a the Inverse Hyperbolic Sine (IHN) of a host country's bilateral FDI inflow. The label "To Investor" refers to cases awarded in favor of the investor (i.e. cases lost by the host state).

cases settled (or won) by the host state may be an artifact of the data, due to the sample. Yet, it seems to me we would be very unlikely to observe such an effect were it not occurring, for two reasons.

One, the coefficients and standard errors may be affected by other ISDS cases which may have an impact on FDI (all those cases that did not involve a BIT). If ISDS cases truly only have negative effects on FDI flows, as all of the current literature suggests, it is hard to see how we could explain the positive coefficients.

Two, some argue that arbitrators have incentives to favor the interests of those who have the power to invoke the use of the system (here the private investors, Van Harten 2012). More than 76% of the time tribunals interpreted contested terms as to advantage investors over states (Simmons 2014). This would also suggests we are not likely to observe a potential positive effect associated with cases won by the host state.

5 Final Remarks

This study contributes a new mechanism for the understanding of reputation in the context of foreign direct investment and dispute settlement. The new mechanism offers possibilities of a reward, in terms of increased FDI flows, to those host countries that settle or win an investment arbitration. This point matters because it allows us to partly explain the increase in FDI flows despite the increase in arbitrations. To my knowledge, this mechanism has not been discussed by past studies.

The analysis focuses on disputes where a bilateral investment treaty has been a legal instrument invoked in proceedings, but there is no reason not to think that these results can also apply to non-BIT dispute settlement, for example based on multilateral Treaties with Investment Provisions (TIP) like NAFTA. This is work in progress at the moment.

Similar behavior by conational firms has been assumed here, but it can be more thoroughly tested in the future. Future research may also look at the observable implications of the theory, especially concerning how knowledgeable investors are about these cases and how much of an influence these cases have in their decision-making.

The question of investor rights and protections is the most heated issue in any international agreement with investment provisions (i.e. recently the Trans-Pacific Partnership). Many developing countries have been rescinding

their bilateral treaties lately due to the many cases filed against them, thereby rejecting the regime in which only investors can initiate a dispute. This study contributes a deeper assessment of the effects of treaties and arbitrations on foreign investment.

Furthermore, by improving our understanding of the effects of dispute settlement institutions, this research will contribute to the policy debate about the secrecy of the arbitral awards: do investors prefer countries with a strong tradition of rule of law, or bureaucracies they can bribe to obtain special concessions instead? This study highlights the positive impact of transparency for governments that have not breached their agreements.

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