Differential institutions, differential flows: Do PTAs always lead to increased FDI?

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Motivation

- There is much work on PTAs and FDI (Milner & Büthe 2008, 2014, Blonigen and Piger 2011, Kenyon and Margalit 2013, among others)...
- … and on FDI and institutions (Li and Resnick 2003, Jensen 2003, Daude and Stein 2007, Dreher and Voigt 2011, among others).

- Several studies have considered the heterogeneity of PTAs, particularly with regard to labor and investment provisions

- But the literature does not differentiate between different types of FDI

Theory

- Existing work suggests that PTAs lure investment (Milner & Büthe)
- We hypothesize that PTAs should be more relevant for FDI that is *tradable*
- Mechanism: The core function of PTAs (market liberalization) is most helpful to firms interested in *export-oriented* investment
- We thus expect strongest effects of PTA on FDI in tradable sectors/industries
    - Yes, PTAs have non-trade liberalization provisions, but we'll get to that...

What about PTA heterogeneity?

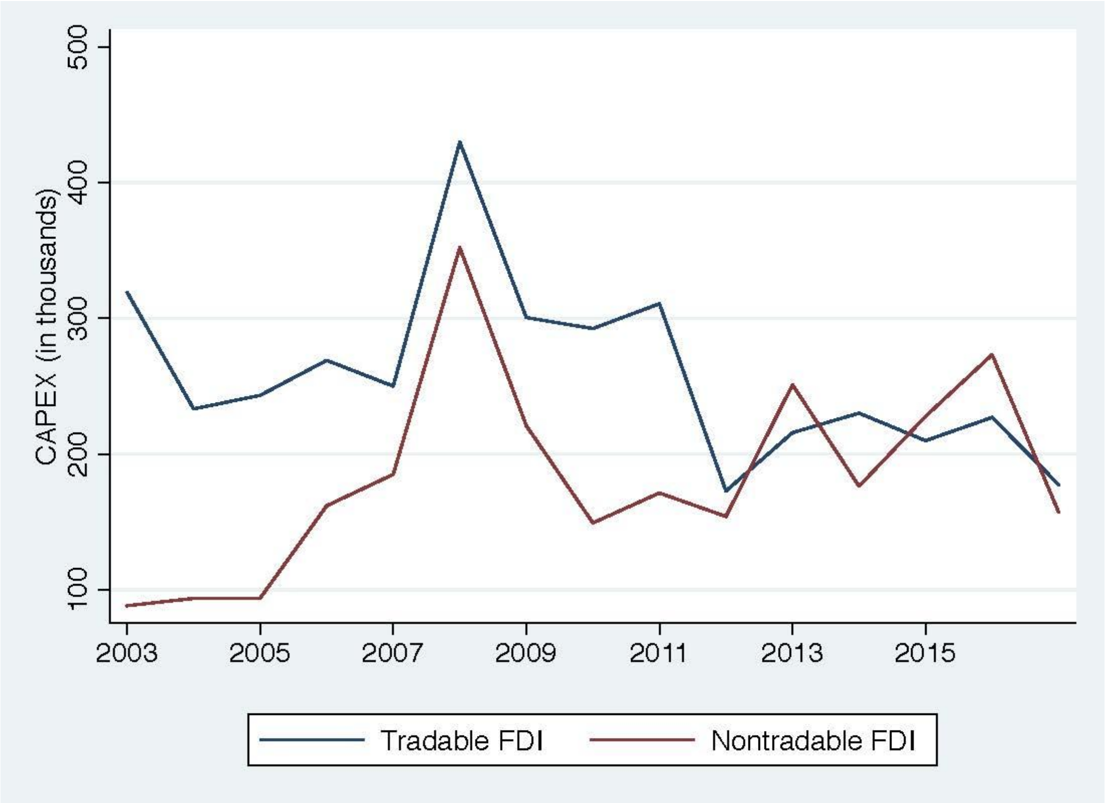
- Labor protection
  - If the firms care about PTAs for export/supply chain, they may be hesitant to invest where developing country PTAs have strong labor rights provisions…

- Investment protection
  - Existing arguments focus on investment protection claims/credible commitment logic. I.e., PTAs as a guard against expropriation.
  - But expropriation fear is likely higher in service/nontradables.

Data

- Sample: all developing countries from 2003–2016
- Dependent variables: Tradable and non-tradable FDI
  - Novel sector and sub-sector level data from FDImarkets (capital expenditure)
  - We divided 1,118 subsectors into tradable and non-tradable FDI (intercoder reliability = 97%)
  - For example, insurance, investment management and legal services were considered non-tradable, whereas automobiles, footwear and electrical equipment were considered tradable
  - We considered 692 sub-sectors to be tradable and 426 to be non-tradable
  - We treat the tradability of a sub-sector as time and country invariant

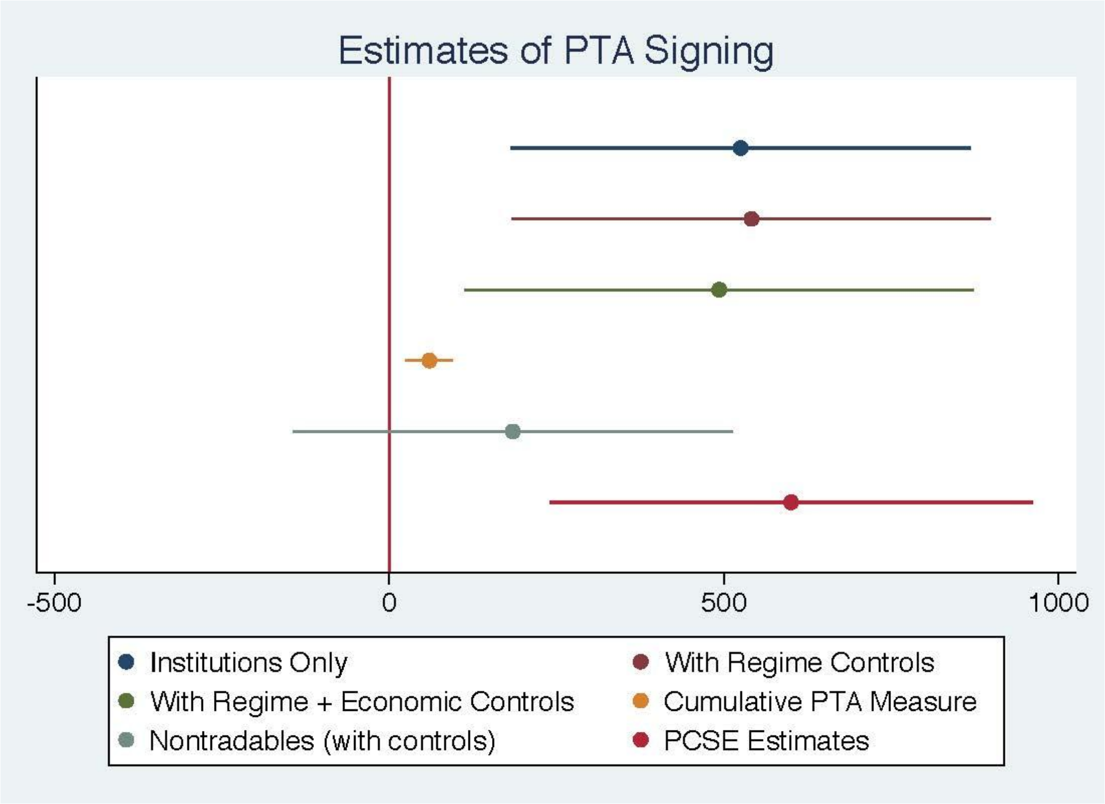
Tradable vs. Nontradable FDI: 2003-2018



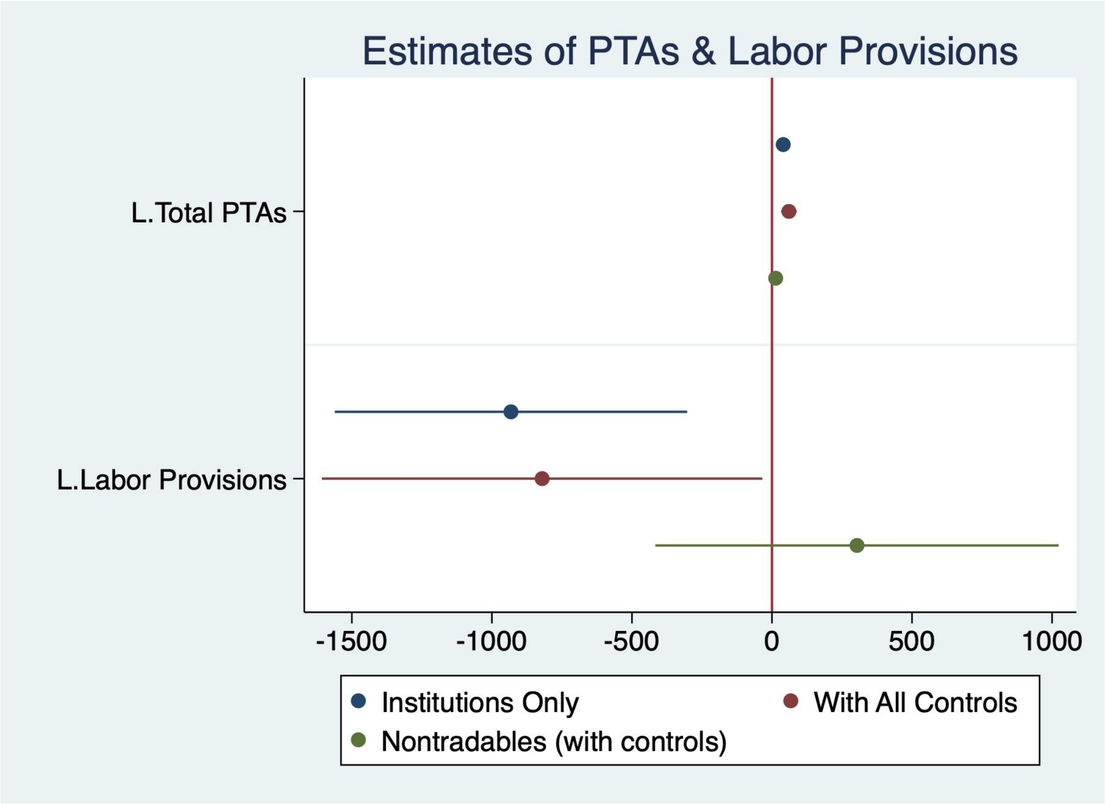
Empirical Model

- Independent variables
  - PTAs (cumulative)
  - PTA labor provisions
  - PTA investment provisions
- Possible confounds
  - Other institutions: BITs, WTO*
  - Regime characteristics: polity, regime durability, regime constraints*
  - Economic factors: GDP per capita, capital openness, lagged endogenous variable (tradable/non-tradable FDI), year FEs
- Estimation
  - Fixed-effects regression
  - PCSE [with panel-specific AR(1)]

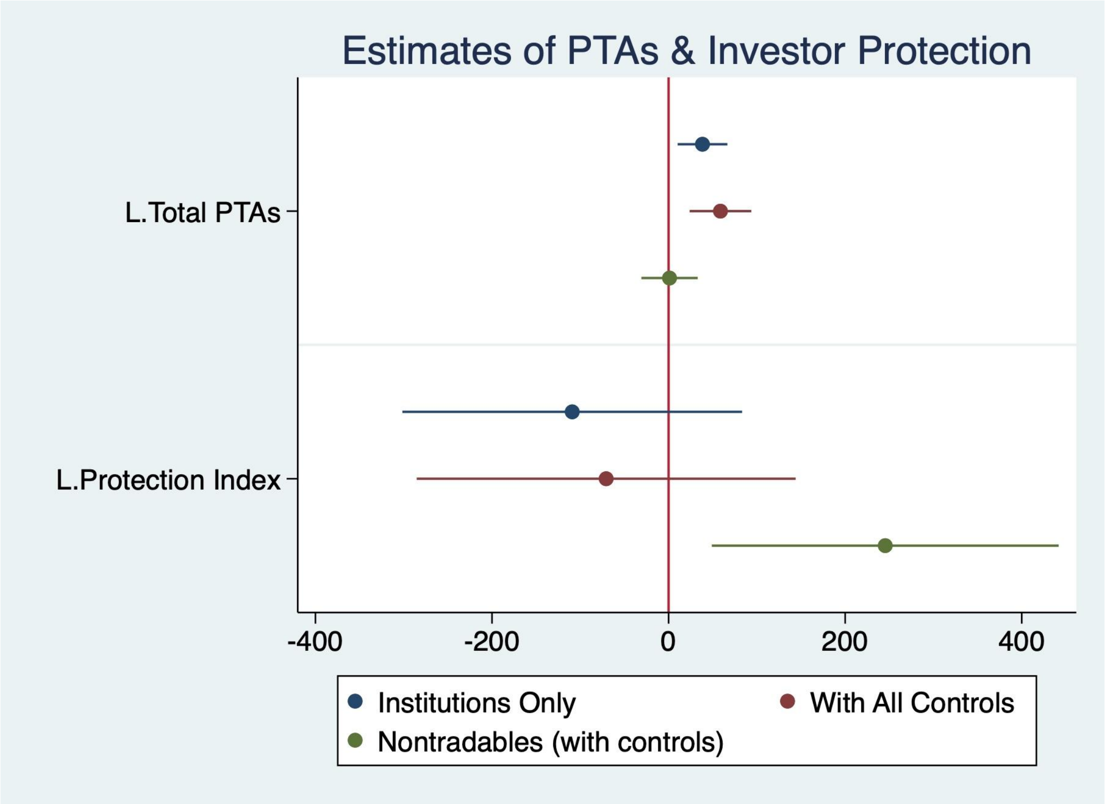
Baseline results



Relaxing PTA homogeneity assumption: Labor



Relaxing PTA homogeneity assumption: Investment



Main findings

- Overall, PTAs only have a significant impact on FDI when the FDI is tradable
- These results hold with institutional, regime type and economic controls
- PTAs with stringent labor provisions (i.e. that are most protective of workers) deter FDI
- Investment provisions have a positive and significant effect on non-tradable FDI but no effect on tradable FDI

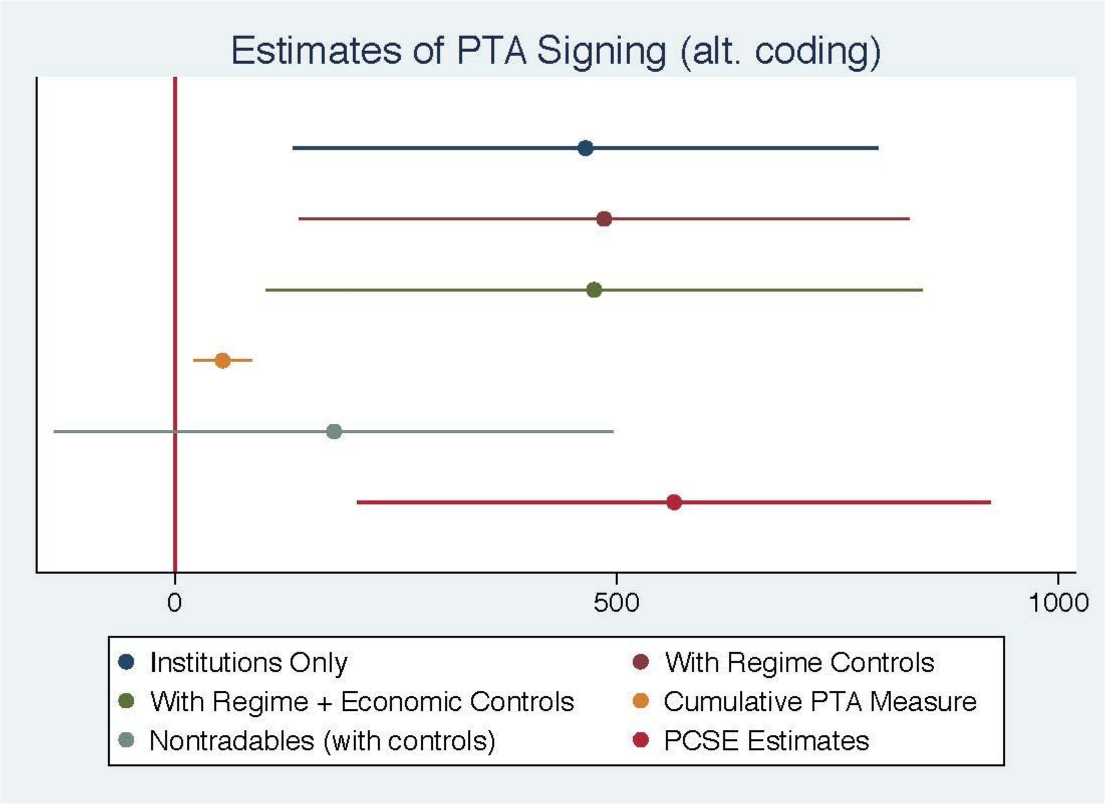
Robustness Checks

- Blackwell/Glynn Sequential-G estimation
- Arellano (1987) fixed-effects regression
- Endogenous institutions: do low values of FDI drive onset of institutions?
- Alternative codings of what is “tradable”
- Domestic constraints (veto players)
- Dispute settlement mechanisms (DSM)

Conclusion & avenues for future research

- Existing explanations of the effect of PTAs on FDI are incomplete
- In addition to accounting for the heterogeneity of PTAs, we must also account for the heterogeneity of FDI
- Future research should address this topic using dyadic data
- This work also calls into question the effect of investment provisions on FDI

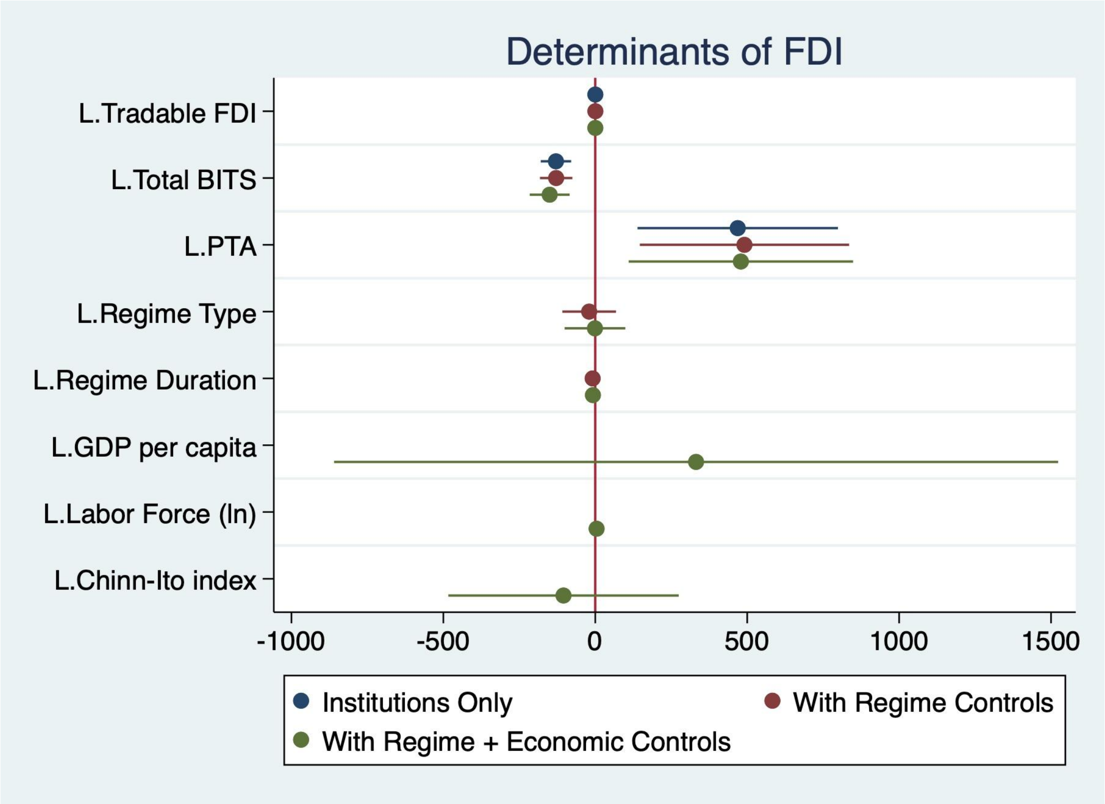
Alternative Coding on “Tradable”



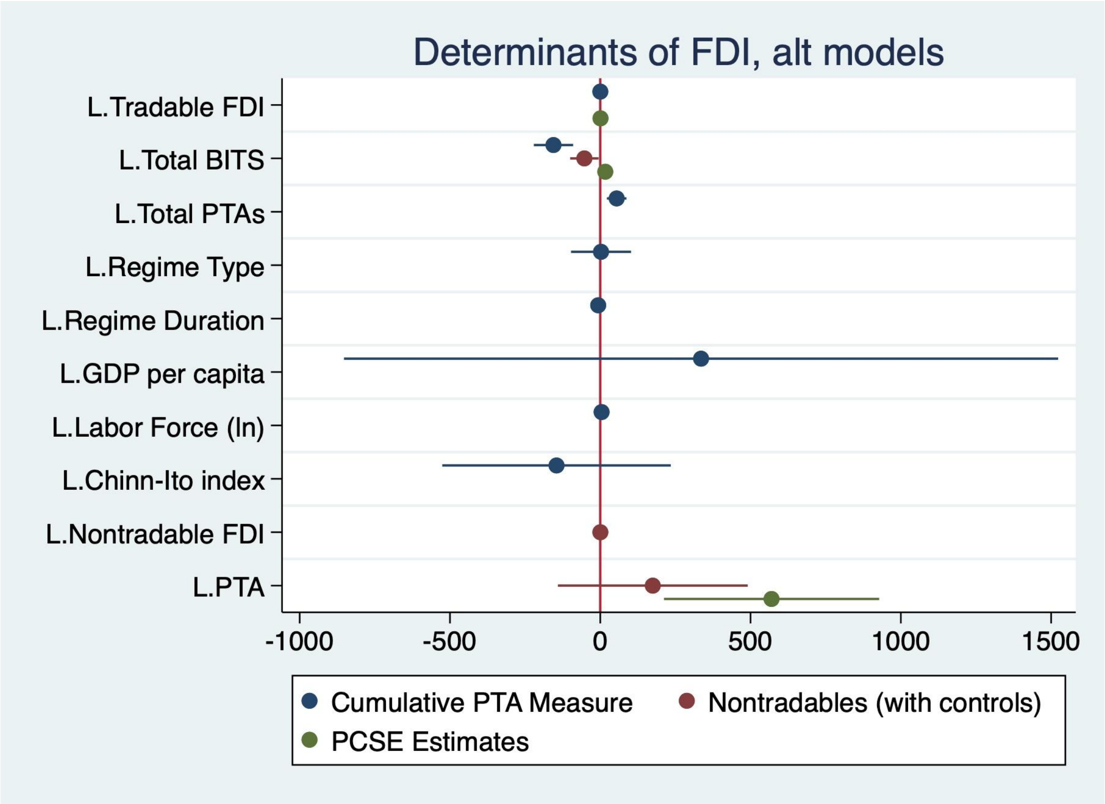
Examples of sub-sectors

Tradable	**Non-tradable**
Automobiles	Truck transportation
Coffee & tea	Warehousing and storage
Electric lighting equipment	Courier services
Plastic bottles	Postal service
Ships and boats	Specialty hospitals
Soft drinks	Retail banking
Wood products	Scenic and sightseeing transport
Video games	Solar electric power

Full model estimates, pt. 1



Full Model Estimates, pt. 2



Relaxing PTA homogeneity assumption: Services