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Domesticating the International: The Uneven Enforcement of Investors' Preferences and its Unintended Consequences

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Doctor of Philosophy in Political Science

by

Monica Widmann

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ABSTRACT OF THE DISSERTATION

Domesticating the International: The Uneven Enforcement of Investors' Preferences and its Unintended Consequences

by

Monica Widmann

Doctor of Philosophy in Political Science

University of California, Los Angeles, 2023

Professor Barbara Geddes, Co-Chair

Professor Aaron Tornell, Co-Chair

This dissertation focuses on the dynamics of sovereign debt politics and the development and usage of the Foreign Sovereign Immunities Act (FSIA). What actions can creditors take against a sovereign country that fails to repay its debts? Can legislation passed in one country to regulate international transactions have economic consequences in other countries? The chapters in this dissertation attempt to answer these questions. Previous research has focused on the role of reputation in influencing the decision of a country to repay their debt and the perception of investors. I argue, however, that US courts are a critical tool in managing sovereign debt markets and in influencing investors' decision to invest. To understand why US courts have the power to adjudicate disputes between investors and foreign states, Chapter 2 examines the era before the advent of the FSIA. In the pre-FSIA period, two branches of government—the Executive (the State Department) and Judicial—were responsible for deciding whether a state could be sued in courts or if the traditional norms of sovereignty would be respected. As

such, a primary reason why the FSIA was passed was to minimize the role of the State Department in the decision-making of the judiciary. Chapter 3 examines how judges in the United States District Court for the Southern District of New York apply the FSIA. When applying the FSIA to sovereign debt cases, liberal and conservative judges rule differently. Conservative judges are more likely to rule against defendants who are democracies than their liberal counterparts. Chapter 4 delves into the economic consequences of court judgments against the debtor nation and their impact on its economy. I argue and find that judicial decisions by US courts can affect the market because a ruling against the defendant debtor increases investor confidence to reinvest in a country, creating positive unintended consequences for the debtor state. To examine the development and role of US courts in disputes involving sovereign states, I collected and utilized three new data sets covering a time frame from 1811 until March 2022 that provide detailed information on sovereign litigation cases.

The dissertation of Monica Widmann is approved.

Jeffrey B. Lewis

Ronald L. Rogowski

Aaron Tornell, Committee Co-Chair

Barbara Geddes, Committee Co-Chair

University of California, Los Angeles

2023

To my family, friends, and loved ones, whose unwavering support made this dissertation possible.

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During my time at UCLA, I have been fortunate to meet numerous people that have made my life easier and my time as a graduate student pleasant. In particular, however, I am grateful for the stability, assistance, and kindness offered by my dissertation committee, as without their invaluable support, this dissertation would not have been possible. My dissertation co-chairs — Barbara Geddes and Aaron Tornell — have been the best co-chairs I could have ever asked for. Barbara has read more drafts of this dissertation than is humanly possible and my work is much improved because of it. I have no doubt that without her support I would not be where I am today. In a department as large as UCLA, where students frequently slip through the cracks due to its culture, Barbara ensured that I did not face such a fate. I will forever be grateful.

During my first year and half at UCLA, I felt fairly lost and misplaced being the only political economy student in the Political Science department. Thankfully, Aaron Tornell was open minded enough to let a Political Science student in his International Finance course where I found my footing. Aaron provided so much financial stability during my PhD studies, which I will always be grateful for because it permitted me to fully pay attention to my studies. Aaron also permitted me to become involved in the Master of Quantitative Economics (MQE) program. Through my involvement in the MQE program, I gained valuable insights into effective teaching of quantitative methods and gained an insider's understanding of program operations. An invaluable experience.

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Since my second year of grad school, I held a lovely cubicle in the California Center

for Population Research (CCPR) office. With this cubicle, came fantastic colleagues. However, it is the last group of office regulars that have been with me during the writing phase of the dissertation that are particularly spectacular. David Henning, Andrew Hess, Jonathan Kowarski, and Huihuang Zhu were the best colleagues I have ever had. I am confident that if David, the one who has an excellent sense of humor, ever reads this, he will have something smart and amusing to say about it. However, the truth remains. These four were always willing to help and chat. Jonathan always provided a steady stream of cookies (along with a nearly daily reminder that I filed my taxes incorrectly and am a tax fraud). Once you looked beyond the East Coast sarcasm of Andrew, you would find someone who is incredibly humble and kind. Huihuang possesses a remarkable level of empathy and understanding. I was fortunate to share office space with such smart and talented colleagues. Most importantly, however, these four put up with my heckling them for being economists. They probably deserve an award for that.

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Chapter 1

Introduction

> "Because of the rapid growth in trade between the United States and foreign countries, it has become increasingly necessary to provide precise statutory guidance to our courts to adjudicate disputes between domestic commercial interests and foreign states." - James M. Cannon, White House Domestic Affairs Advisor under the Ford Administration

After the 1648 Peace of Westphalia, it was assumed that states would interact with and treat each other as equals. It was believed that, even as economic cooperation increased and interdependence grew, each state would retain the ability to make independent decisions within its own realm. However, with the rise of non-state actors that operate independently of the state and exert control or contribute to the production of goods, states may no longer have the ability to make independent decisions within their own realm (Strange, 1996). The first area of economic cooperation to challenge the traditional norms of sovereignty was international trade. In this economic sphere, numerous rules and institutions have been developed to manage trade between states and the relations involving non-state actors and states. However, unlike the trade arena, which has the World Trade Organization with its Dispute Settlement Body, and its predecessor the General Agreement on Tariffs and Trade (GATT), established in 1948,

there is no equivalent institution in the realm of finance and, in particular, for sovereign debt.

Institutions, such as the Paris Club and the London Club, that facilitate debt reduction negotiations for countries burdened by unsustainable debt exist. The Paris Club, formed in 1956, focuses on rescheduling and reducing the debts of developing countries. It operates on a case-by-case basis, negotiating debt repayment terms and offering debt relief measures. The London Club, established in 1976, primarily deals with the restructuring of commercial bank debt. It represents the interests of private banks and financial institutions in negotiations with debtor countries. However, these clubs meet irregularly, do not have a clearly defined set of guidelines, nor do they provide a forum for other types of creditors, such as bondholders. As a result, sovereign debt default resolution has often relied on gunboat diplomacy, banking houses such as the Rothschild's, and/or the role of reputation.

The informal approach to resolving debt crises throughout history has frequently placed the burden of protecting the interests of creditors, who are often banks or bondholders, on the willingness of their home state to intervene. Due to the political nature of sovereign debt default resolution, the extent of intervention on behalf of creditors has varied greatly. With the expanding international economic influence of the United States, the United States itself emerged as the primary home base for numerous individual investors, hedge funds, and banks. Therefore, the United States government found itself needing to create a dispute settlement mechanism for investors. On October 19th 1976, President Ford announced his signing of the Foreign Sovereign Immunities Act (FSIA), which provides the legal framework for determining when a foreign sovereign state can be subject to lawsuits in US courts. In his signing statement he explained that the FSIA "…continues the longstanding commitment of the United States to seek a stable international order under law….private citizens increasingly come into contact

with foreign government activities, it is important to know when the courts are available to redress legal grievances." (Ford, 1976). Undoubtedly, the reference to a stable international order under the rule of law highlights the essential requirement of political and economic stability for facilitating international transactions.

This is of particular importance in the event of a sovereign debt default. Sovereign debt crises pose a significant threat to the stability and well-being of an economy. When a country's government accumulates excessive levels of debt that it is unable to repay, it triggers a cascade of destructive consequences. Firstly, the confidence of lenders and investors is eroded, leading to higher borrowing costs and limited access to credit. Of course, a sovereign debt crisis in one country can lead to a loss of investor confidence and contagion, spreading financial instability to other countries in the region or even globally. This can result in a broader financial crisis and increased borrowing costs for other nations. Secondly, governments are forced to implement austerity measures, such as cutting public spending and increasing taxes, to meet their debt obligations. These measures, while intended to restore fiscal balance, often exacerbate the economic downturn, leading to job losses, reduced consumer spending, and social unrest. Additionally, a sovereign debt crisis can lead to a depreciation of the national currency, causing inflationary pressures and further eroding the purchasing power of citizens. Lastly, a sovereign debt crisis can affect international trade flows. Reduced access to financing, currency devaluation, or economic downturns can hinder a country's ability to import goods and services, impacting trading partners and global supply chains. The destructive impact of sovereign debt crises extends beyond the immediate financial realm, as it undermines investor confidence, impairs long-term development, and harms a country's reputation in the global market. Furthermore, these debt crises have the capacity to extend beyond their initial boundaries and impact other sectors of the economy and nations, leading to widespread complications and challenges.

Given the potential harm that a sovereign default can cause, it is important to understand whether the FSIA can play a role in alleviating investor fears in the event of a default. This dissertation focuses on the dynamics of sovereign debt politics and the evolution and application of the FSIA. It attempts to address the following questions: What actions can creditors take against a sovereign country that fails to repay its debts? Is the judiciary impartial? Can the presence of a property protection regime stimulate economic growth? Can legislation passed in one country to regulate international transactions have economic consequences in other countries? What are the costs of a sovereign default? Linking these topics, my dissertation examines the role of US courts via the application of the FSIA in (1) expanding private property rights protection overseas and (2) settling disputes between creditors and debtor states, which in turn may impact the economy of the debtor state.

In the first empirical chapter of the book, I examine the era before the advent of the FSIA. As a response to the international economic environment after WWII and to aid US investors, the State Department issued the Tate Letter in 1952. The adoption of the Tate Letter resulted in a formal shift in the United States' official foreign policy. The policy changed from one that upheld absolute sovereignty, as per the Act of State doctrine,[1] which prevented external courts from examining actions carried out within a sovereign's borders, to a policy of restrictive sovereignty. Under restrictive immunity, states are unable to claim sovereignty over their commercial activities, which theoretically makes it easier for investors to seek legal recourse. However, the State Department retained the ability to grant absolute sovereign immunity requests from countries being sued in a US court. They did this because deciding which definition

[1]The Act of State doctrine originated from the decision in Underhill v. Hernandez, 168 U.S. 250 (1897). In this case, a United States citizen sued for illegal detention by a Venezuelan revolutionary leader. The court's response was that the acts of another government carried out within its own territory could not be judged by the courts of one country, emphasizing the need for diplomatic channels to address such matters.

of sovereignty to use is ultimately a political act. Nevertheless, as an independent branch, the judiciary did not have to follow suggestions from the State Department. Consequently, during the period from 1952 until the implementation of the FSIA in 1977, two branches took on the responsibility of shaping foreign policy. Under what circumstances was a particular definition of sovereignty employed given the coexistence of two branches of government and two definitions of sovereignty?

Although the Tate Letter formally signaled a switch to restrictive immunity, it also introduced uncertainty in the legal environment such that a judge could choose between applying the Tate Letter (restrictive sovereignty) or the Act of State doctrine (absolute sovereignty). I argue that due to the unclear policy environment, if the defendant country in question was a democracy or if the dispute pertained to a sovereign default, the judiciary tended to rely on the Act of State doctrine, resulting in a more favorable outcome for the defendant. Within the Act of State doctrine, international comity is enshrined, which is the deference to the laws and decisions of another country. Democracies were more likely to be awarded absolute sovereignty because judges were more willing to defer to the decisions made by a country with similar institutions to the US than autocracies. Moreover, cases involving sovereign debt were perceived as a strictly domestic issue since it exclusively concerned a nation's financing. As such, a judge would be reluctant to apply restrictive immunity because doing so would amount to guiding and determining a country's economic policy. I quantitatively support my argument by utilizing two original data sets: a data set of sovereign immunity requests to the State Department and an additional data set of pre-1977 US court cases involving commercial suits brought against an independent country. A case study of Cuba is used to illustrate my argument.

The second empirical chapter of my dissertation examines how judges in the United States District Court for the Southern District of New York (SDNY) apply the FSIA.

The FSIA was passed in 1976 and addressed many of the weaknesses of the Tate Letter. For example, it provides a definition of "commercial," removed the State Department from the litigation process, and increased the enforcement mechanism. With the strengthening of the FSIA, investors gained an ideal dispute settlement mechanism, which, if adhered to without deviating from its provisions, makes it likely for an investor to win when they bring a commercial dispute to court. However, despite the depoliticization of sovereign litigation, politics remained in the process via judicial ideology. Liberals and conservatives have different preferences regarding management of the economy with conservatives being more pro-business and less interventionist than liberals. These preferences lead to a difference in ruling propensities between liberal and conservative judges when the defendant is a democracy. As democracies participate in intra-industry trade to a greater extent than autocracies, conservative judges will practice judicial restraint and rule against them to protect business interests, but liberal judges are likely to be judicial activists and rule in favor of a democratic defendant.

To test this theory, I focused on sovereign debt litigation and collected data that covers the period between 1977 and 2022 from a web scrape of the Public Access to Court Electronic Records website for cases taken to the SDNY, which is where sovereign debt cases are taken. As US dollar denominated sovereign bonds are issued under New York law, lawsuits are seen in the SDNY. Of course, not all sovereign debt suits involve bonds issued in US dollars. There are also bank loans and trade credits that comprise sovereign debt lawsuits, but these are highly likely to end up in the SDNY as contracts typically include clauses that indicate disputes should be taken to New York. If a sovereign debt case is brought before a court other than the SDNY, it is common for the receiving court to transfer the case to the SDNY since it is considered the suitable jurisdiction.[2] Overall, forum shopping is highly unlikely due to various factors, such

[2]Confirmed in interviews with lawyers who have worked these cases.

as the sovereign debt being in the form of a bond, contractual provisions stipulating New York as the designated forum, or cases being transferred to the SDNY due to its recognized suitability as the appropriate jurisdiction.

By utilizing this representative data set, I exploit the quasi-random assignment of judges to cases through the application of causal machine learning, specifically Virtual Twins, in conjunction with Bayesian hierarchical modeling. Through this approach, I find support for my argument. Under the Tate Letter regime, judges would nearly always grant defendants absolute sovereignty when the dispute was over sovereign debt because it was viewed as an internal sovereign matter, but as sovereign debt would be considered a commercial activity under the FSIA, the expectation is that plaintiffs should always win. They should always win not only because of the strengthened FSIA, but also because the evidence that a state defaulted is clear. Nevertheless, despite expectations, plaintiffs do not regularly win. Plaintiffs do not win when the defendant is a democracy and the case is assigned to a liberal judge.

The third empirical chapter examines the implications of court rulings under the FSIA. As US courts now make decisions on issues involving the economic policies of other sovereign states, particularly regarding debt, it is important to consider their impact. What impact, if any, does a court ruling have on the debt market and the economy of a debtor state? I argue that judicial decisions by US courts can affect the market because a ruling against the defendant debtor increases investor confidence to reinvest in a country, creating positive unintended consequences for the debtor state. The judge sends the following information to investors by ruling in favor of the lender-plaintiff: (1) the action of the debtor state was illegitimate, (2) claims made by the creditor are valid, (3) actions to enforce the ruling are acceptable, and (4) given (1) - (3) it may be possible to recoup losses after a default. As a result, investors may be more willing to return to a country shortly after default when a judge rules in favor of the lender.

While a country's leader will want to win a case as it provides short-term benefits that are beneficial for political survival, such as the ability to allocate financial resources at their discretion rather than setting aside a large amount to repay investors, a win in the courtroom may come at the cost of future investment because it will not provide international investors the confidence needed to reinvest in a country after a contract is breached. In fact, losing a case may lead to unintended positive benefits for the country in the medium term. If a ruling in favor of the lender lowers perceived risk for investors, then there are three possible implications.

First, the cost of borrowing should decrease for the debtor country. By ruling in favor of the plaintiff, a judge not only creates the expectation of full repayment for investors holding defaulted bonds, but also boosts investor confidence in bonds that are not in default, as the FSIA becomes a viable tool for investors if needed. Second, the import of intermediate goods should increase. Firms that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and closely monitor the economic climate. Although these firms typically have multiple venues to choose from to settle a dispute, a plaintiff receiving a favorable court ruling from a US judge during a sovereign default episode reassures firms that (a) the economy may turn around and (b) US courts may be a viable option if needed. Third, a debtor state that defaults and receives an unfavorable court ruling is more likely to experience economic growth afterward. Lower borrowing costs can enable a country to service its current debt and invest in public infrastructure that attracts foreign direct investment. Furthermore, an increase in the importation of intermediate goods can have a multiplier effect on the economy, creating jobs and contributing to further growth. These implications are quantitatively tested using structural nested means models, ordinary least squares, and original data on FSIA sovereign debt court rulings.

This dissertation provides several contributions to better understand sovereign debt politics and political economy more broadly. First, it traces the development and usage of restrictive immunity. To the best of my knowledge, the International Relations literature on sovereignty has not addressed the change from absolute to restrictive immunity. Second, as scholars have historically focused on reputation, the role of courts in settling sovereign disputes has been minimal. Therefore, this project is the first book-length exploration of this issue. Third, it provides three new data sets to better understand the dispute settlement process over time. One data set covers all immunity requests sent to the State Department between 1952 and 1977. The second data set comprises all sovereign litigation cases to arrive in US courts from 1811 until 1976. Lastly, the third data set covers all sovereign debt cases brought to the SDNY from 1976 until March 2022.

Chapter 2

Sovereignty Restructured: The Foreign Policy of Absolute Sovereignty

Abstract: To aid investors in the post-WWII economic environment, the State Department issued the Tate Letter in 1952. The adoption of the Tate Letter resulted in a formal shift in the United States' official foreign policy. The policy changed from one that upheld absolute sovereignty, as per the Act of State doctrine, which prevented external courts from examining actions carried out within a sovereign's borders, to a policy of restrictive sovereignty. Under restrictive sovereignty, countries were no longer entitled to assert absolute sovereign immunity in commercial transactions. However, under the Tate Letter regime (1952-1977), the State Department had the ability to grant absolute sovereign immunity requests from countries being sued in a US court. Under what circumstances was a particular definition of sovereignty employed, given the coexistence of two branches of government and two definitions of sovereignty? Although the Tate Letter formally signaled a switch to restrictive immunity, it also introduced uncertainty in the legal environment such that a judge could choose between applying the Tate Letter (restrictive sovereignty) or the Act of State doctrine (absolute sovereignty). I argue that due to the unclear policy environment, if the defendant country was a democracy or if the dispute pertained to a sovereign default, the judiciary tended to rely on the Act of State doctrine, resulting in a more favorable outcome for the defendant. Within the Act of State doctrine, international comity is enshrined, which is the deference to the laws and decisions of another country. Democracies were more likely to be awarded absolute sovereignty because judges were more willing to defer to the decisions made by a country with similar institutions to the US than autocracies. Moreover, cases involving sovereign debt were perceived as a strictly domestic issue since it exclusively concerned a nation's financing. As such, a judge would be reluctant to apply restrictive immunity because doing so would amount to guiding and determining a country's economic policy. I quantitatively support my argument by utilizing two original data sets: a data set of sovereign immunity requests from 1952 until January 1977 to the State Department and an additional data set of pre-1977 US court cases involving commercial suits brought against an independent country. A case study of Cuba is used to illustrate

my argument.

> "This new doctrine applies precisely to Cuba which has taken over many former commercial activities…which are still sold in the United States. If Cuba is to be permitted to collect dollars on its commercial activities it must respond in our courts on its commercial contracts." - Judge Markowitz, Supreme Court of New York

2.1 Introduction

In the spring of 1952, the State Department announced in the Tate Letter that the US would no longer follow the theory of absolute sovereignty, but a restrictive theory of sovereignty. Under absolute sovereign immunity, a foreign state can only be sued in a US court (or any court outside the country being sued) if the foreign state consented to being sued. In contrast, under restrictive sovereignty, a foreign state does not need to give its consent to being sued when the issue involves a commercial activity (acta jure gestionis). If restrictive immunity is applied to lawsuits involving commercial issues, defendant states cannot use the immunity defense, which makes it easier for an investor to have their case heard. Moreover, with the switch to restrictive immunity, there is an expectation that US courts would consistently implement the Tate Letter. However, this was not the case. There were two obstacles in the implementation of the Tate Letter. First, the State Department gave itself the ability to grant requests of absolute sovereignty by a state being sued. Second, in the Tate Letter, the State Department did not provide a definition of "commercial." These two impediments led to frustration by investors because it seemed that the State Department was making decisions based on political circumstances rather than commercial issues, even after formally transitioning to a sovereignty-based restrictive approach.

Investors views of the State Department were not unwarranted. For example, in the case of Weilamann v. The Chase Manhattan Bank where Mrs. Weilamann — a holder of defaulted Soviet Union bonds — was suing Chase Bank in order to obtain funds within

the bank held by the Soviet Union, the State Department did not uphold the Tate Letter. On March 9, 1959, the State Department granted the Soviet Union immunity in this case on the grounds that an attachment cannot be made against the assets of a sovereign state. A few months later, the court, following the immunity suggestion of the State Department, ruled in favor of Chase Bank. In this case, the Soviet Union had issued bonds to pay for machinery, which is an act that any company is capable of doing and, as such, is a clear commercial act. Despite this, restrictive immunity was not applied. In contrast, in the case of Flota Maritima Browning de Cuba v. The Ciudad de la Habana where Cuba had expropriated vessels, the State Department did not grant the immunity request of Cuba and permitted attachment by the plaintiff. US courts, just as before, followed the lead of the State Department and ruled against Cuba in this case.

However, it is not always the case that a court will follow the lead of the State Department. In Chemical Natural Resources, Inc. v. Republic of Venezuela, Venezuela was granted absolute sovereign immunity by the State Department, but the court in this case chose to ignore the State Department and ruled against Venezuela. Furthermore, approximately half of suits involving commercial activities lacked State Department involvement as the State Department will not get involved in a dispute absent a request from a country.[1] As such, it is important to ask – How did the judiciary choose which type of sovereignty to utilize? Were countries with certain characteristics more likely to be awarded absolute sovereignty than another?

Although investors viewed the State Department as influencing the judicial process in such a way that the application of the Tate Letter became inconsistent, the judiciary would continue to apply restrictive immunity even when the State Department was not

[1]Of the 119 disputes that resulted in litigation, the State Department was only involved in 53 of them.

involved in the decision-making process. I argue that even though restrictive immunity was supposed to be applied to all commercial cases during the Tate Letter era, absolute sovereignty was more likely to be applied when the defendant country was a democracy or if the dispute involved sovereign debt. The switch to restrictive sovereign immunity from absolute was formally announced via the Tate Letter, but in practice absolute sovereignty was often applied. This is because absolute sovereignty was already codified in the Act of State doctrine. According to this doctrine, US courts cannot rule on the legitimacy of the sovereign acts of another government and should be deferential to the laws and decisions of another country. Due to lack of clarity in the Tate Letter over what is or is not a commercial activity, guidance for the judiciary on when to apply the Tate Letter rather than the Act of State doctrine was missing. For this reason, in this uncertain legal environment, judges could pick and choose whether to apply restrictive immunity (the Tate Letter) or absolute sovereignty (Act of State doctrine).

Due to the legal environment's uncertainty, courts were inclined to rule in favor of a democratic nation, regardless of the nature of the lawsuit, and in cases of commercial disputes involving sovereign defaults, irrespective of the type of regime. First, given that judges had the ability to pick and choose between absolute and restrictive immunity, democracies were more likely to be awarded absolute sovereignty because judges were more likely to defer to the decisions made by a country with similar institutions to the US than autocracies. Second, since sovereign debt is commonly utilized for domestic financing purposes, it remained perceived as an internal sovereign matter. As a result, the judiciary was unwilling to assume the responsibility of prescribing economic policy to an independent state.

I test my argument using two original data sets: (1) a data set on sovereign immunity requests to the State Department from 1952 to 1977 and (2) a data set covering commercial suits brought to US courts until 1977. I find that the State Department and

the judiciary did not apply the Tate Letter consistently even in commercial disputes. Even when the State Department remained not involved in a dispute, the judiciary would apply absolute sovereignty when the Tate Letter called for restrictive immunity. The judiciary were more likely to grant absolute sovereignty to more democratic countries irrespective of what the dispute was over. However, even the more authoritarian countries would be granted absolute sovereignty if the dispute was over bonds.

2.2 Literature Review

At face value, it is assumed that different branches of government have different responsibilities and generally make decisions independent of each other. Despite this common belief, in practice this does not often occur. Even in countries where the constitution outlines the separation of powers, various branches of government and agencies frequently exert influence over one another. In US domestic politics, the possibility of a veto by the President may prompt Congress to include the President's preferences in the legislation (Kiewiet & McCubbins, 1988). However, it is not only the influence of different branches on each other that is important, but also how they are structured. For example, parties will often act as a legislative carted and organize the House of Representatives in such a way to address their collective dilemmas of passing party-defined policies and reducing member defection. By resolving these dilemmas, individual members of the party can forego some of their personal preferences to achieve common benefits (Cox & McCubbins, 2007). When acting as a cartel, a party can control the agenda by obtaining control over special committee chairs, the Speakership, and other positions and offices. Therefore, this means that the vote matters less and the opposing party's legislation is not considered (Cox & McCubbins, 2005). The significance of the interplay between different branches and the potential for cartel-like conduct in the

legislative branch lies in its impact on economic policy.

Different political institutions and internal arrangements within a branch of government can lead to different economic policy even among democracies. Cox & McCubbins (2001) argue that the diversity of principal-agent relationships across institutions is responsible for the differing economic policies and outcomes observed across democracies. They describe the variation in principal-agent relationships across institutions as veto players. The largest number of veto players will exist where power is divided, and the purpose of each domestic institution is divided (Cox & McCubbins, 2001). To minimize the issue of veto players wherein branches may influence each other or parties may create cartel-like environment out of self-interest, a branch of government or agency may delegate a task to another agency. Of course, delegation may come at the cost for principal as once a task is delegated to another agent, they lose control. The agent may either follow the directions of the principal or an agent may act against the preferences of the principal. However, as Kiewiet & McCubbins (1991) argue in the context of delegation by Congress, it is not so much whether an entity chooses to delegate, but how it does so. Specifically, when delegating, to prevent an agent from shirking, the principal can create monitoring requirements and institutional checks (Kiewiet & McCubbins, 1991). Of course, while delegating tasks may serve the interests of the principal institution, but depending on the nature of the contract's terms, it may not align with the interests of third parties involved. This was the case with the Tate Letter as the State Department maintained some role in decision-making despite the delegation of authority to the courts.

While it is apparent that different branches of government may influence each other and that internal politics within these institutions can impact outcomes, the role of government bureaucracies in international affairs is often overlooked in the analysis of international policy making. In the US, the involvement of departments and bureau-

cracies that have a primarily domestic mandate in foreign economic policy making has grown because (a) their domestic policy goals impacts those outside of the US and (b) they have specialized skills and knowledge that is not only a tool that can be used to support US foreign policy, but may be of use to those outside of the US (Hopkins, 1976). Due to the position of the United States in the international system, its departments and bureaucracies that have these specialized skills often perform roles that would be performed by an international organization. While domestic institutions of the United States may be the most likely to be able to extend their reach overseas, this does not mean that bureaucracies in other countries cannot influence economic policy within their own country. Encarnation & Wells (1985) find that as competition between countries have increased to attract foreign investment, they have developed decision-making structures to handle negotiations with foreign companies that specialize in specific sectors.

In general, countries entrust specific domestic agencies with responsibilities because of their specialized skills and knowledge. However, as argued by Legro (1996), each bureaucracy has its own culture that could influence international outcomes. While Legro (1996) focused on the military as a bureaucracy in different countries, culture also matters in other issue areas as well. For instance, in many countries, Central Banks were delegated authority because they are considered experts in monetary matters and, consequently, are expected to make decisions free from political influence. Nonetheless, the independence of a Central Bank does not imply that it operates without an organizational culture. The theoretical results of Rogoff (1985) suggest that the appointment of a conservative central banker is more likely to lead to low inflation. Utilizing data, Simmons (1996) finds that independent central banks often enacted monetary policy actions that were far more conservative than those taken by governments. Moreover, Cukierman (2003) also finds that having a highly independent Central Bank is corre-

lated with low-inflation. Even though independent Central Banks are separate from politics, they have an organizational culture that influences their policy decisions.

The literature provides several significant insights that can be drawn from it. First, even in the presence of separation of powers and delegation to another agency, different branches and bureaucracies often influence each other. Second, domestic departments and bureaucracies may be delegated tasks even if it may have international ramifications due to their expertise in an area. As such, not all issues related to international affairs is decided by the President or Congress. Third, these departments and bureaucracies possess a distinct organizational cultures. This implies that despite the government's belief that they are delegating authority to an impartial institution, these bureaucracies may have their own preferences and biases, which impacts the extent to which legislation or a contract is followed.

2.3 Tracing Legal & Political Developments to the Tate Letter

Sovereignty, globalization, and democracy are features of world politics, but the presence of each feature has ebbed and flowed over time. While the focus on how these features interact has often been discussed in relation to major world events like conflict and intervention, it is often minor actors and less visible events that define sovereignty. The Tate Letter is no exception. The Tate Letter changed the official US foreign policy of granting absolute sovereignty to restrictive sovereignty, which meant that a country could no longer claim sovereign immunity over commercial transactions. This change in US foreign policy came after a study in the State Department determined that (a) countries that claimed to be following absolute sovereignty had signed onto the 1926 Brussels Convention on Maritime Liens and Mortgages, which waived sovereign immunity over vessels and (b) the United States had stopped claiming immunity on

its own merchant vessels within foreign jurisdictions and in its own. Most importantly, however, the State Department felt that "...the widespread and increasing practice on the part of governments of engaging in commercial activities makes necessary a practice which will enable persons doing business with them to have their rights determined in the courts" (State Department, 1952). With an increase in economic globalization following WWII, the State Department felt pressured to protect investor interests.

The State Department becoming involved in the relations between individual investors and sovereign states is nothing new. Beginning with President Theodore Roosevelt and extending until the start of the Great Depression, the United States utilized dollar diplomacy.[2] This often took the form of controlled or supervisory loans, which generally meant that a country had to submit itself to US financial advisers to implement various reforms, and in return, the country would have access to bank loans from US-based banks. Bankers benefited from these loans as it decreased risk and often came along with a high interest rate. When a country was under a supervisory loan, bond prices and investments to the country would often rise (Rosenberg, 1999). For example, bond prices and investments into Colombia soared after the involvement of US financial advisers in 1923.[3] As investors acquired protections from the State Department, they were more willing to invest in otherwise risky countries.

However, State Department involvement began to wane as the Great Depression drew near. While a factor in growing hesitancy by the State Department to act as a broker between bankers and countries was partly due to growing criticism of financial imperialism, the main factors were questions over US military interventions in countries under dollar diplomacy[4] and the its economic impact as not all countries were

[2]See Rosenberg (1999) for more information on dollar diplomacy.

[3]By the early 1920s, these US financial advising was referred to as Kemmerer missions, which entailed going into a country and often changing their financial institutions.

[4]Most prominently, Nicaragua.

as successful as Colombia.[5] With countries not becoming economically successful, the State Department no longer wanted to be involved in default negotiations. As such, the State Department began to minimize its role in managing relations between investors and countries. Bankers could ask for comments from the State Department before lending to a country in regards to its political risk and, in the event of a default, form a bondholder organization[6] (Adamson, 2002), but the direct involvement ended.

Even though the State Department was engaged with dollar diplomacy, it was not heavily involved in sovereign suits as the majority of cases did not start appearing until the 1920s. The US judiciary in this time period were determining for themselves how suits against foreign states should be handled. The general position was that when a United States individual or corporation conducts business with a foreign government, they should be entitled to the same level of judicial protection as they currently have when dealing with their own government.[7] Formally, the United States government permitted its citizens to sue them with the passing of the Tucker Act of March 3, 1887. This act permitted individuals to sue the US government over contractual claims or any situation where a plaintiff believes they are entitled to payment by the government. While this act did formally establish the right of a US citizen to sue the US government, it should be noted that citizens had filed lawsuits against the US government prior to its enactment. Nevertheless, the prevailing view was that if US citizens were granted the ability to sue their own government, they should also have the same right when it comes to foreign governments.

From the onset, however, there were tensions between the State Department and the US judiciary. An instance of this occurred in the case of Berizzi Brothers Co. v. S.S.

[5]Most countries, even those that were successful, followed a boom bust cycle.

[6]After default, it is in the interest of bondholders to form an organization, so that they can more effectively negotiate with a sovereign state over repayment.

[7]This is reflected by statements made by Chief Justice Marshall in Schooner Exchange v. McFaddon, 11 U.S. (7 Cranch) 116, 136 (1812).

Pesaro in 1921 when the Supreme Court disregarded the State Department's advice to not grant vessels absolute immunity due to their commercial nature, and instead maintained the established practice of applying absolute sovereignty. The judiciary here disregarded the State Department because at this point in time the norm was for courts to grant sovereign states absolute immunity in cases involving vessels. This case further demonstrates that even though the US judiciary supported the right of US citizens to sue foreign governments in US courts, this did not necessarily ensure that US citizens would prevail in such cases. It was not until the 1940s, in the cases of Ex Parte Peru, 318 U.S. 578 (1943) and Mexico v. Hoffman, 324 U.S. 30 (1945), that the Supreme Court stated that sovereign immunity decisions will be decided by the State Department on a case-by-case basis or, in its absence, general State Department policy. The latter, of course, requires court interpretation of general State Department policy.

2.4 Theory and Hypotheses

Nevertheless, following WWII, the State Department wanted to aid investors and faced some pressure to do so, but the State Department did not want a return to dollar diplomacy that existed prior to WWII. The development of the Tate Letter was a compromise between providing investors protections and minimizing their role by having courts become the intermediary between investors and countries. Given that US courts have already handled cases involving US business interests and foreign states, and in some cases have upheld the idea that American citizens should have the right to sue foreign states over business matters, making the transition to a legal environment where restrictive immunity was the status quo would not be a difficult one. However, although the State Department stated that they wanted those doing business abroad to have their rights—mainly being private property rights as used in the United States—protected

via courts, they tried to limit the ability of the court to act independently by allowing a country to petition the State Department for absolute immunity in the event of a suit.

However, even though the State Department had the capability to mediate in a dispute, it did not engage in or become involved in every instance. For the State Department to become involved, a formal diplomatic request had to be sent to the State Department from the country being sued or a court can ask the State Department to step in and offer its view. The latter, however, happened very rarely.[8] Once a request was made, the State Department would either look over the court transcripts or have the plaintiff and defendant present memoranda or an oral argument to the State Departments Office of the Legal Adviser. Once a decision was made, if a decision was made, the Attorney General and relevant embassy would be informed.

A request to the State Department did not guarantee a suggestion of absolute sovereign immunity to the Attorney General nor did it guarantee that the State Department would make decisions based on their definition of restrictive immunity as laid out in the Tate Letter. The Tate Letter was formulated in an attempt to give investors a dispute settlement mechanism, but investors became disenchanted with this mechanism for multiple reasons including State Department involvement in the process. For investors, the State Department was a source of bias because they believed that the State Department would grant a country absolute sovereign immunity when a request was made even when the dispute was over a commercial issue. Moreover, these absolute sovereign immunity requests could arrive before a suit begins, during a judicial proceeding, or even after a case has been settled. As such, the State Department could potentially prevent an investor from having their day in court or over turn a ruling made by a judge. It is unsurprising that investors would view the State Department as

[8] Out of 113 requests, 4 requests for State Department input was directly made from a court/judge and 1 request came from the Department of Justice.

negative influence.

Of course, since the State Department functions as an extension of the executive branch and is tasked with advancing its interests, its decisions may be influenced by political sensitivities or executive bias, rather than solely based on evidence of contractual compliance. Moreover, adhering strictly to the Tate Letter may contradict other undisclosed rules and preferences of the State Department and, as a result, enforcing the Tate Letter may not have been a priority. For the State Department, it did not matter whether a country was a democracy or autocracy or if the country was a close ally of the United States. What mattered was political sensitivity and current foreign relations as curtailing the sovereignty of a state is ultimately a political issue. For example, the tense relations with Cuba during the Tate Letter regime often meant that the State Department was inconsistent in their application of restrictive immunity by granting absolute sovereignty in some commercial disputes and not others.

As a remedy, investors sought to address the State Department's inconsistent application of restrictive immunity by calling for its removal, which would leave disputes to be resolved exclusively by the courts. While it is unsurprising that the State Department would be described as biased because of the purpose of this institution and that investors would want their removal from the decision-making process, this call, however, implicitly assumes that the judiciary strictly follows the law as written or the arrangements of a contractual agreement. Were the judiciary more likely to apply restrictive immunity during this time period?

While ensuring their is separation between the branches of government and creating an environment in which judicial decision-making is free of political inference are worthy goals, I argue that it is not the case that the judiciary would consistently apply restrictive immunity in commercial disputes. Although the judiciary may not be subject to the same political pressures as the State Department, which can lead to decisions being

made based on political circumstances, it is important to note that the judiciary's interpretation of the law may not always align with the expectations of investors. This is because in addition to the issue of the State Department formalizing the process in which they become involved in suits during the Tate Letter period, the Tate Letter did not delineate how to determine whether an act is governmental (a public act) or commercial (a private act). Hence, even though the theory of restrictive sovereignty immunity specifies that countries will not have immunity over commercial issues, there are some gray areas. For example, in the event that a country defaults on its bonds and/or bank loans, it is unclear under the Tate Letter whether this is a governmental or private (commercial) act as the decision to default is one made by a government for internal reasons, but the act of borrowing and defaulting is also one that any private actor could make. It is in these gray areas where there is uncertainty over whether restrictive or absolute sovereignty should be applied.

For this reason, courts could choose when to apply restrictive sovereign immunity or absolute sovereign immunity. Aiding in their ability to choose is the principle of international comity. International comity is deference to the laws and decisions of another country. It is not a formal international law, but a principle that has manifested gradually into various domestic doctrines that US courts follow such as the Act of State doctrine. International comity is not simply about recognizing the laws and choices of another country, but also restraining the reach of US courts. The application of comity comes in many forms. For example, there is comity to courts, which is when a US court believes that the more appropriate venue for a case is within the country where the event took place.[9] Another form is comity to legislatures or as Justice Scalia named, prescriptive comity. This form of comity can be defined as "...the respect sovereign

[9]This is referred to as forum non conveniens. This type of comity did not become prevalent until the 2000's where the 7th and 9th circuit began to use this for expropriation cases.

nations afford each other by limiting the reach of their laws" (Scalia 1993).[10] The point being that it is important to avoid conflict with the laws of other nations. At the Federal level, prescriptive comity has manifested itself as the Act of State doctrine. This doctrine states that the actions taken within the borders of a sovereign cannot be questioned by a court outside of that country. When deciding whether to apply restrictive immunity or not, the judiciary is choosing to either apply the Tate Letter or the Act of State doctrine.

Finally, there is comity to a sovereign party. This form of comity typically refers to the ability of a foreign state to bring a suit, as plaintiff, to a US court, which is only permitted if the country is not at war with the United States and if it is a country that the US has recognized as sovereign. Most importantly, comity to a sovereign party also includes protecting foreign officials and states from the reach of US courts by limiting the types of issues they can be sued over. It is this aspect of comity that the Tate Letter attempted to introduce, but ultimately struggled to take hold among the judiciary. It struggled to take hold because the rules were unclear. Within the Tate Letter, a definition of "commercial" is lacking. In this context, the Tate Letter was effectively pitted against the Act of State doctrine, which upheld prescriptive comity by advocating deference to the laws and decisions of foreign nations. Lacking clarity from the Tate Letter, the judiciary were likely to rule in favor of the defendant in commercial cases by relying on prescriptive international comity and applying the Act of State doctrine. The concept of absolute sovereignty came before the development of restrictive immunity. For this reason, restrictive immunity needed to compete with the already established norm of absolute sovereignty. In sum, the norm of absolute sovereignty was difficult to change.

Of course, this does not suggest that absolute sovereignty would always be applied

[10]Hartford Fire Ins. Co.v.California, 509 U.S.764, 817 (1993) (Scalia, J., dissenting).

by the judiciary. As discussed, even prior to the development of the Tate Letter, the judiciary were open to the notion that American businesses should be granted the same standing to sue foreign governments as they have to sue the US government. Given the ability of the judiciary to choose between absolute and restrictive immunity, however, the judiciary looked at other factors when making decisions. One of these factors is the institutions of the defendant state. Whereas the State Department made decisions based on the foreign policy needs of the executive branch, the judiciary relied on information about the defendant state's domestic institutions.

When presented with a case that involved a foreign state, courts would often consider whether a particular country was a "friendly" state. For example, in the 1920 case against the Ottoman Empire, Judge Knox stated that "In recognition of that comity which, under the law of nations, exists between friendly states, this court…has from time to time released from arrest the property of foreign governments… When, however, a foreign government has seen fit to sever diplomatic relations with the United States…it is not the function of the court to [grant immunity]."[11] Moreover, a court taking into consideration whether a state is friendly or not is not an artifact of the pre-Tate Letter period. For instance, Chief Justice Stone stated, in relation to a case against South Korea, that "Courts may not so exercise their jurisdiction, by the seizure and detention of the property of a friendly sovereign, as to embarrass the executive arm of the government in conducting foreign relations."[12] But what is a "friendly" state according to the judiciary?

The judiciary does not live in a black box unaware of international events. When Judge Knox argued that it would be inappropriate to grant the Ottoman Empire international comity, he would have known that the Ottomans supported the Central Powers

[11] 1920 U.S. Dist. LEXIS 1345, THE GUL DJEMAL
[12] New York & Mail S.S. Co. v. Republic of Korea, July 13, 1955, 132 F. Supp. 684

during WWI. Nevertheless, the majority of suits brought to US courts were not major players in WWI, WWII, or the Cold War. As such, courts could not make comity decisions based on political climate alone. Instead, the regime characteristics of the country involved in the suit would help inform the choices of the judiciary. As noted, prescriptive comity is about respecting the laws and choices of another country. The laws and rules of another country that is most likely to be respected are those that are most similar to those of the United States. However, this preference towards awarding absolute sovereignty to more democratic countries became more pronounced after the introduction of the Tate Letter. Although the Tate Letter was not clear enough to influence judges to consistently apply restrictive immunity in lieu of absolute sovereignty when a suit involved commercial issues, it did introduce uncertainty in a process that even before the Tate Letter was largely guided by the beliefs of judges. With confusion over when to apply restrictive immunity, Judges were more likely to consider the institutional features of a country in the Tate Letter period than they were before. As such, the more democratic institutional features a country had, the more likely they were to be awarded absolute sovereignty after the Tate Letter was announced.

> H1: After the Tate Letter, the more democratic the country is, the more likely it is to be awarded absolute sovereignty.

In addition to institutional characteristics of a country, the type of commercial issue that the suit is over also influences judicial outcomes. Due to the tension between the Tate Letter and the Act of State doctrine, it is unclear as to how a judge should rule on issues that take place within a country such as sovereign default. When a country defaults on its debts, it is not always clear whether this should be considered a

governmental or private (commercial) action, as the decision to default may be made by the government for internal reasons, but borrowing and defaulting could also be done by a private entity. These ambiguities give rise to uncertainty as to whether restrictive or absolute sovereignty should apply. Due to the ambiguity in the Tate Letter, certain judges devised their own interpretation of what constitutes a governmental act. Judge Smith in the case of Victory Transport v. Spain defined government acts as being "…limited to the following categories: (1) internal administrative acts, such as expulsion of an alien; (2) legislative acts, such as nationalization; (3) acts concerning the armed forces; (4) acts concerning diplomatic activity; and (5) public loans." Although a default often negatively impacts international investors who own the debt, it is considered an internal issue as defaults regularly come with high costs for the domestic economy such that the decision by a government to default is often considered one that is only made when a government must do it. Courts, with unclear directions from the Tate Letter, did not want to dictate the economic policy of a foreign country and often would define debt as a governmental activity.

> H2: US courts are more likely to rule in favor of a country if the suit involves a commercial issue that is viewed as an internal decision.

With the advent of the Tate Letter, the separation of power between the judicial and executive branch decreased as the roles between the two branches were more clearly delineated. That said, the State Department still at times played a role in commercial disputes between a US investor and a foreign state. Were the judiciary likely to follow the decision of the State Department in the event that they became involved in a lawsuit? When making a decision absent the State Department, the judiciary is influenced by

different factors than the State Department and have different preferences. These factors and preferences do not disappear upon the presence of the State Department. However, it is not the case that the courts did not think about State Department preferences or at least what they thought would be State Department preferences. For example, in the 1964 appellate court case of Victory Transport v. Spain, Judge Smith declared that from the Tate Letter, "… the State Department has made it clear that its policy is to decline immunity to friendly foreign sovereigns in suits arising from private or commercial activity." While this statement from Judge Smith is incorrect, as there is nothing in the text of the Tate Letter that mentions declining absolute immunity for friendly states, it demonstrates that State Department preferences were at least considered in the decision-making process. Following this statement, Judge Smith then says, "But the 'Tate letter' offers no guidelines or criteria for differentiating between a sovereign's private and public acts." Given the lack of guidance in the Tate Letter and the factors that influence judicial decision-making absent the State Department, when the State Department is involved in a case that is being reviewed by a court, it is unlikely that the State Department sovereignty suggestions will always be followed by the court. Therefore, the amount of interference and influence that the State Department was perceived to be having on the judicial system by investors, is much smaller than what may have been expected.

H3: US courts were unlikely to consistently follow State Department immunity suggestions.

2.5 Data

2.5.1 Original Data Collection

To test these hypotheses and examine sovereign litigation more generally, two original data sets were collected. First, there is a data set on requests made to the State Department. This data set is collected by using the State Department's Digest of U.S. Practice of International Law.[13] This source provides the most comprehensive list of requests and is the only known source of such information. As such, it is possible that this data set is missing some requests. There are 113 observations in this data set and covers the time period from May 1952 (enactment of the Tate Letter) to January 1977 when the Foreign Sovereign Immunities Act (FSIA) came into force. From the information available in the the State Department's Digest of U.S. Practice of International Law, I gathered several pieces of information to form the data set, including the names of the plaintiff and defendant, case name, when the request was made, when the State Department responded, if the request came after a court ruling, whether the request came from the country being sued or a court, if immunity was granted, and if they made any comments about attachment requests.

Most importantly, as it is necessary to understand whether the issue area of a suit influences outcomes, I code the type of economic issue for which the immunity was requested. This variable — Type Economic — contains eight categories. These categories are the following: Other - Not Commercial, Debt - Bond, Debt - Trade, Debt - Other, Expropriation - Payments, Expropriation - Physical, Other, and Unknown. "Other - Not Commercial" contains a variety of suits, such as work injuries by personnel at an embassy or on a vessel. While these cases involve a contract between employee and employer, it is not a contract that is concerned with commerce. "Debt - Bond" cases

[13] see State Department (1977)

are disputes involving a sovereign default on bonds. "Debt - Trade" includes items such as trade credits, which is an agreement between a sovereign state and supplier to send goods prior to payment. "Debt - Other" includes items like dividend certificates and rent agreements for embassies. Cases that fall under the "Expropriation - Payments" are those where the foreign state expropriate payments, which encompasses scenarios such as when a bank that has been newly nationalized declines to release funds to a customer or denies a bank account owner access to their own money. "Expropriation - Physical" includes suits where a country expropriate the physical assets of a US investor. For example, if a country expropriates a factory or a hotel the case is labeled as one involving the a physical expropriation. "Other" includes all other items that are commercial in nature such as damaged vessels, but do not fit into the other categories. To code the Type Economic variable, I relied on the information presented in the digest and, where applicable and available, information from the court case. Nevertheless, in a few cases, information was so sparse it is impossible to identify the type of issue the request was for, so these were coded as "Unknown". Of course, it is possible to divide the cases into further categories, but the categories would become excessively niche and specialized that not much information would be gained from doing so. In addition to Type Economic, the variable "Diplomatic Request Granted?" is also used in the statistical analysis. This variable is coded as "1" if the state was granted immunity and "0" otherwise. However, in addition to this, information on whether the State Department ignored a request is also collected and used for summary statistics.

Second, I collected an original data set of all commercial suits involving sovereign states in the United States prior to the enactment of the FSIA. The resulting data set includes 119 cases concluded between 1811 to November 1976.[14] To collect this

[14]Commercial cases between November 1976 and the enforcement of the FSIA are lacking.

information, I relied on NexisUni.[15] I first performed a broad search in this data base by searching for all cases that contain the words "sovereign", "immunity", and/or "sovereign immunity" before December 31, 1977. Next, I went through the resulting list of cases and kept all commercial suits involving a sovereign state. Nations with dubious degree of sovereignty, like Puerto Rico, were not included in the data set. Commercial for data collection purposes is defined as anything involving the transaction or an agreement to a transaction of goods, services, and money. This data set contains cases from multiple courts including from both the federal and state level. Additionally, it also includes appeals of a case. For example, in the case of Lillian Hannes v. Kingdom of Roumania Monopolies Institute, both the case brought to the "Supreme Court of New York, Special Term, New York County" and the "Supreme Court of New York, Appellate Division, First Department" are coded as separate observations. This decision was made because different courts, with different judges, sometimes rule differently even though the case is the same. Moreover, in some cases, the State Department did not get involved until a case was moved to an appellate court.

Similar to the State Department immunity requests data set, the pre-FSIA court data set includes information such as defendant, plaintiff, case name, the court the suit was taken to, the start and end dates of a case, the docket or reporter number, the judges assigned, and whether the case was seen in a state court ("State Judge?").[16] Additionally, it includes a binary variable for whether the case is one that was appealed ("Appeal?"), a "Type Economic" variable that has all the same categories as the one in the State Department data set except for the "Unknown" and "Other - Not Commercial" category, and a binary variable for whether the State Department was involved in the case. Moreover, there is an indicator variable for whether an attachment request was

[15] Formerly LexisNexus.
[16] This information was web scraped.

made ("Attachment Attempt") and an indicator variable for whether the court granted the request for an attachment ("Awarded Attachment"). There is a categorical plaintiff type variable ("Plaintiff Type") indicating whether the suit was brought by individuals, a company, or a bank.

When the State Department immunity request data set is merged with the data set on court litigation, suits with no immunity requests to the State Department are coded as "0" for the "Diplomatic Request Granted?" variable, which is also included in the pre-FSIA court data set. It is important to note that not all observations in the State Department data set are also included the data set covering court cases because either (1) an immunity request was made before litigation began and the dispute was not taken to court, (2) the request was over a non-commercial issue, which is not included in the pre-FSIA court data set, and (3) information on the case is unavailable. Information on a case is often unavailable if the suit was brought to a *state* court, which has either not digitized cases prior to the late 1980s or at some point lost the details of the case.

2.5.2 Additional Data

In addition to the original data sets, three additional variable are included in the analysis. First, there is a "Latin America" indicator variable that is coded as "1" if the defendant is a Latin American country and "0" otherwise. I include this variable because it is possible that, due to its proximity to the US, Latin American countries may be treated differently in lawsuits or by the State Department. Second, I create an indicator variable—"World War—that is coded as"1" if the case took place during WWI or WWII. This variable is included because politics towards sovereignty may have differed during periods of fighting. Lastly, I use the the measure of liberal democracy from the V-dem data set (Coppedge et al., 2022). The Liberal Democracy index covers the years from 1789-2021 and ranges from 0 to 1 with zero being the least democratic. This measure

of democracy was chosen because it focuses on the rule of law, the independence of the judiciary, and the extent of checks and balances in a country. This variable aids in differentiating between countries that have institutional features most similar to the US (i.e., those that are more democratic) and those that are most dissimilar (i.e., more authoritarian).

2.6 Methods & Results

2.6.1 State Department

The United States would eventually enact the FSIA due to complaints from investors that the process under the Tate Letter was biased against them. How did the State Letter respond to requests of absolute immunity? Examining the raw data, as presented in Table 1 below, it is apparent that there is no clear pattern of State Department decisions. This is expected as the State Department is the agent of the executive branch. 37% of requests for immunity are denied and 41% are granted. Among the commercial requests, 32 were denied immunity, 27 were granted immunity, and 6 requests were ignored. It is clear that restrictive immunity was not applied consistently as evidenced by the number of immunity requests granted for disputes concerning commercial issues. Hypothetically, if the State Department were adhering to the Tate Letter, we would expect close to all requests involving non-commercial issues to be granted immunity, but instead only 11 out of 21[17] of these requests were granted immunity. Additionally, there does not appear to be a clear issue area where the State Department was more or less like to grant or deny an immunity request.

[17] Where the outcome is known. Otherwise, a total of 22 cases.

Table 1: State Department Responses by Type Economic

	Diplomatic Request Granted?				
Immunity	Denied	Granted	Ignored	Unknown	**Total**
Type Economic					
Debt-Bond	1 (33%)	2 (67%)	0 (0%)	0 (0%)	3 (100%)
Debt-Other	1 (100%)	0 (0%)	0 (0%)	0 (0%)	1 (100%)
Debt-Trade	11 (55%)	8 (40%)	1 (5.0%)	0 (0%)	20 (100%)
Expropriation-Payments	3 (75%)	1 (25%)	0 (0%)	0 (0%)	4 (100%)
Expropriation-Physical	2 (25%)	5 (62%)	1 (12%)	0 (0%)	8 (100%)
Other	14 (47%)	11 (37%)	4 (13%)	1 (3.3%)	30 (100%)
Other-Not Commercial	8 (36%)	11 (50%)	2 (9.1%)	1 (4.5%)	22 (100%)
Unknown	2 (8.0%)	8 (32%)	14 (56%)	1 (4.0%)	25 (100%)
Total	42 (37%)	46 (41%)	22 (19%)	3 (2.7%)	113 (100%)

Of course, the Tate Letter was not meant to be applied to non-commercial cases. To examine State Department decision-making only among immunity requests that would fall under the purview of the Tate Letter, the non-commercial cases,including those that fell under the "Unknown" category, are removed from the data and presented in Table 2 below. As before, a clear trend of State Department decision-making is lacking. While the small sample size makes inferences difficult, it is important to note that defendant states involved in lawsuits over defaults on sovereign bonds or the expropriation of physical assets are most likely to be awarded an absolute sovereign immunity request. 42% of requests for absolute sovereign immunity requests were granted when the case involved a commercial dispute. If the Tate Letter was being upheld, the percentage of cases should be 0.

Table 2: State Department Responses by Type Economic - Only Commercial Cases

	Diplomatic Request Granted?			
Immunity	Denied	Granted	Ignored	**Total**
Type Economic				
Debt-Bond	1 (33%)	2 (67%)	0 (0%)	3 (100%)
Debt-Other	1 (100%)	0 (0%)	0 (0%)	1 (100%)
Debt-Trade	11 (55%)	8 (40%)	1 (5.0%)	20 (100%)
Expropriation-Payments	3 (75%)	1 (25%)	0 (0%)	4 (100%)
Expropriation-Physical	2 (25%)	5 (62%)	1 (12%)	8 (100%)
Other	14 (48%)	11 (38%)	4 (14%)	29 (100%)
Total	32 (49%)	27 (42%)	6 (9.2%)	65 (100%)

While examining the raw data provides useful insights, it does not take into account political factors that may influence State Department decisions. To examine this more closely, I first utilize binomial elastic net regression as it is useful when the data is sparse and the N is small, which is the case here. This method, as described by Zou & Hastie (2005), involves modifying the criterion function of the regression coefficients (such as the sum of squared errors and likelihood) by adding two penalties. These penalties penalize both the absolute magnitude (known as "lasso" penalty) and squared value (known as "ridge" penalty) of the regression coefficients. In elastic net regression, the tuning parameters are the weights assigned to the two penalties used in the regression. The lasso penalty pushes variables that are not relevant to the model's accuracy to exactly zero. In contrast, the ridge penalty will shrink coefficients that do not contribute enough to the fit of the model towards zero, but not exactly to zero. The elastic net approach merges the selection feature of lasso regularization with the shrinkage capability of ridge regression regularization. Using lasso by itself is not ideal here as lasso underperforms when the independent variables may be correlated with each other. In a scenario where variables are highly correlated, lasso may select a variable and push the other correlated variables to zero.

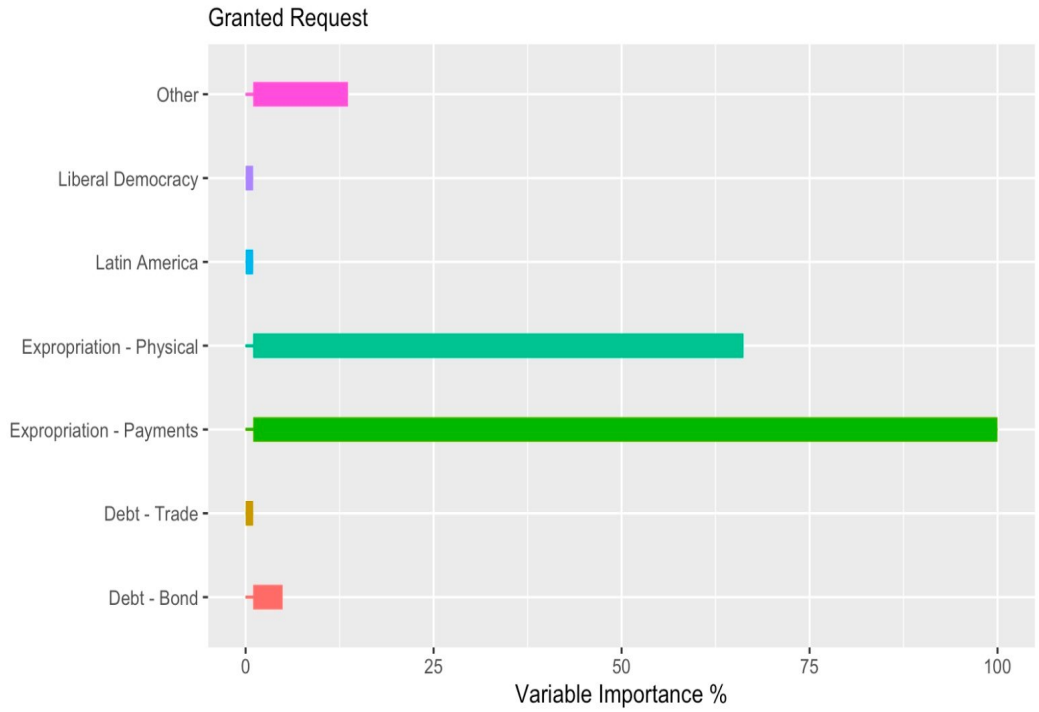
Lasso in such a scenario may not necessarily be the optimal predictor among all correlated variables (Zou & Hastie, 2005). To address this issue, the Elastic Net method averages the highly correlated variables.

The dependent variable here is the categorical variable "Diplomatic Request Granted?", which indicates whether the request was granted. Dummies for each category in Type Economic are included with the reference group being the "Other - Not Commercial" category.[18] An indicator variable for Latin America is included along with the Liberal Democracy variable. The cases that were labeled as "Unknown" for Type Economic were removed for this analysis along with missing data for Liberal Democracy. In this particular setting, after using cross validation, a value of .921 was selected for α. The α sets how much mixing there is between lasso and ridge regression. When $\alpha = 0$ ridge is utilize and when $\alpha = 0$ lasso is used. The λ parameter selected after cross validation was .047. The λ parameter determines how much shrinkage occurs. When $\lambda = 0$, no shrinkage occurs. The λ value is set independently of α.

Figure 2.1 presents the results from the elastic net regression. Feature selection assigns a score to variables based on their effect at predicting the outcome variable. As the score increases, so does the magnitude of the effect. Among requests that were granted, the model found the four features that have an effect and marked all other features with a zero coefficient, essentially removing them from the model. With the reference category being "Other - Not Commercial", the model selected "Expropriation - Payments", "Expropriation - Physical", "Other", and "Debt - Bond" as categories that are most likely to lead to the granting of absolute sovereignty. This suggests that the Tate Letter was not being followed by the State Department as cases involving commercial disputes were being granted absolute sovereignty. As such, the claims of interference by investors were not unwarranted.

[18] Due to the single observation for "Debt - Other" it was collapsed into the "Expropriation - Payments" category as it is most substantively similar to this category.

Figure 2.1: State Department Decisions - Elastic Net



To further test if there is a relationship between Liberal Democracy, Latin America, or Type Economic and the sovereign immunity request outcomes, I estimate an OLS regression with robust standard errors clustered by Country. As before, the reference group for Type Economic is "Other - Not Commercial". The results are presented in Table 3 below. All independent variables are insignificant. Latin America was not treated any differently than other countries in other regions. Furthermore, the domestic institutions of a defendant state did not influence State Department decisions. The insignificance of Liberal Democracy and Latin American aligns with the results from the elastic net model. All of the categories for Type Economic were insignificant for the OLS result, which differs from the elastic net model. This difference, however, may be due to the fact that elastic net, unlike OLS, does not compute coefficients by minimizing the residual sum of squares, but minimizes the "penalized" residual sum of squares.[19] Overall,

[19]Moreover, due to the small sample size—only 84 observations—the results from OLS may be unreliable and the results from the elastic net may also be biased.

however, the results confirm that the State Department made decisions that were not in line with the Tate Letter. While this is unsurprising as the State Department is the agent of the executive branch, it also suggests that the State Department could potentially be a negative presence for investors as they could intervene in such a way that prevented an investor from having their day in court or change the outcome of a lawsuit. From the results, it is evident that the State Department did not follow the Tate Letter and apply restrictive immunity for commercial disputes, but potentially made decisions on a case-by-case basis. The case of Cuba will be used to illustrate this point.

Table 3: State Department Decisions - OLS Regression

	Dependent variable: Diplomatic Request Granted?
Liberal Democracy	−0.02
	(0.29)
Latin America	0.02
	(0.15)
Debt-Bond	0.14
	(0.32)
Debt-Trade	−0.13
	(0.14)
Expropriation-Payments	−0.33
	(0.28)
Expropriation-Physical	0.09
	(0.18)
Other	−0.15
	(0.14)
Constant	1.52***
	(0.14)
Note:	*p<0.1; **p<0.05; ***p<0.01

OLS Regression with Robust Standard Errors clustered by Country. Dependent variable is "Diplomatic Request Granted?" that is coded as "1" if the State Department grants the absolute immunity request of a defendant state. The "Unknown" observations were removed from the sample.

The Case of Cuba

During the Cold War period, which covers the entirety of the Tate Letter period, the United States had tense relations with Cuba after Fidel Castro overthrew Batista in January 1959. By 1960, Castro began to nationalize foreign property and companies largely belonging to US citizens. In response to the nationalization, the Eisenhower administration imposed import quotas for Cuban sugar and nearly cutoff all trade with Cuba. It was not until the Kennedy Administration that trade with Cuba would be completely cutoff. A total of 16 immunity requests were made by Cuba during the Tate Letter period. 15 of the 16 requests involved a commercial dispute. Of the 16 requests, Cuba was denied immunity only 5 times – all connected to a commercial dispute. The 16 immunity requests from Cuba are presented in Table 4 below. The eleventh case—Benton v. Cuban Air Force—is the only dispute that would not clearly fall under the Tate Letter and Cuba was granted immunity in that case.

Given that nearly all of these are requests made in relation to a commercial dispute and the US had cut ties with Cuba, why was Cuba denied immunity only five times? As argued, the State Department did not make immunity request decisions based on characteristics like regime type, but on the current political environment. The majority of requests from Cuba came in 1961 and 1962 following the change in economic policy from Castro. Due to the political situation, awarding Cuba absolute sovereign immunity was the preferred outcome for US foreign policy politics as denying the absolute sovereignty of Cuba could potentially be viewed as an action against the Soviet Union. Hence, Cuba was not denied immunity the majority of the time.

In cases such as the Naviera Vacuba that gained much public attention as crewmen hijacked a ship and sailed to the US to gain asylum when its original destination was the Soviet Union, it would not have been possible to decline immunity without straining relations. As stated by Secretary of State Dean Rusk "…it has been determined that the release of this vessel would avoid further disturbance to our international relations in the premises" (197 F. Supp. 710, 1961). As a result, the State Department granted Cuba immunity and it was ordered for the ship to be returned to Cuba. This decision by the State Department came shortly after Cuba released the plane from the Eastern Air Lines Flight 202 hijacking.[20] In fact, following a note

[20] A flight hijacked from Miami and flown to Cuba when its original destination was Tampa, Florida.

submitted to the UN Security Council by the United States, the Cuban government stated that "…if the Government of the United States guarantees the right of immunity and sovereignty of the boats and airplanes belonging to the Cuban people that are seized in our country and taken to United States territory…the Government of Cuba will accord reciprocal treatment to American boats and airplanes…" (State Department, 1961, pp. 407–8). As such, the decision made in this case by the State Department had little to do with guidelines as laid out in the Tate Letter.

Table 4: Immunity Requests by Cuba

Date	Type Economic	Case Name	Request Granted?
1952-08-15	Other	O'Brien v. Republic of Cuba	1
1961-04-25	Exprop.-Physical	Dixie Paint & Varnish Co. v. Republic of Cuba	1
1961-06-19	Other	Arcade Bldg. of Savanna v. Republic of Cuba	1
1961-08-21	Other	Naviera Vacuba	1
1961-10-25	Exprop.-Payments	French v. Banco Nacional de Cuba	0
1961-12-08	Exprop.- Payments	Gonzalez v. Industrial Bank of Cuba	0
1961-12-13	Exprop.-Physical	Kane v. National Institute of Agrarian Reform	1
1961-12-13	Exprop.-Physical	National Institute of Agrarian Reform v. Dekle	1
1961-12-28	Other	Bergstresser v. Cuban Air Force F.A.R.	1
1962-02-14	Exprop.-Payments	Ritter v. Republic of Cuba	0
1962-02-23	Not Commercial	Benton v. Cuban Air Force	1
1962-03-22	Debt-Trade	Berlanti Construction Co. v. Republic of Cuba	0
1962-04-24	Debt-Trade	Harris & Company Advertising Inc. v. Republic of Cuba	1
1962-06-26	Exprop.-Physical	Flota Maritima Browning v. Motor Vessel Ciudad Habana	0
1965-07-28	Debt-Trade	Mayan Lines v. Republic of Cuba	1
1973-10-25	Debt-Trade	Industria Azucarera Vacioal v.Empresa Navegacion	1

Of course, although cases like these are commercial in nature because often the hijacked ship carries trade goods, the cases labeled "Other", such as Naviera Vacuba, may be more

political in nature than other commercial cases. If the "Other" category and non-commercial requests are ignored, then 6 of the 11 immunity requests by Cuba were granted. While it is the case that the State Department appeared to be granting immunity requests in situations that had a lot of attention, particularly as it pertained to the return of ships and planes, the State Department was also more inclined to grant Cuba sovereignty when the contested assets were located within its borders, such as in disputes over the expropriation of physical assets. Flota Maritima Browning v. Motor Vessel Ciudad de la Habana is an outlier among requests regarding the expropriation of physical assets as the ship was already in the US and the State Department said it would not grant immunity as the ownership of the vessel was ambiguous. The remaining four instances of immunity denials cover disputes that fall under either Expropriation - Payments or Debt - Trade. In the three Expropriation - Payments disputes, the assets were located within the borders of the United States. The case of Ritter v. Republic of Cuba involved assets located in the Florida branch of Banco Nacional de Cuba. Even though Banco Nacional de Cuba was nationalized in 1960, Florida law contended that assets of the bank did not belong to Cuba and that Cuba was obliged to pay Ritter.

The case of French v. Banco Nacional de Cuba concerned the payments of dividends, which were supposed to be in American dollars, but the Cubans after nationalization, wanted to pay in pesos. In Gonzalez v. Industrial Bank of Cuba, the Cuban bank would not cash a check in US dollars to Cuban refugees based in the US, but offered to pay in Cuban pesos. In the latter two cases, the State Department deemed it to be a clear commercial issue, but it is important to note that it also was not a commercial act that required the taking back of a physical asset from Cuba. The only Debt - Trade case, Berlanti Construction Co. v. Republic of Cuba, was over a construction contract for low cost housing in Cuba. The plaintiffs had already started construction when the Cuban government halted construction, so Berlanti Construction sued for financial losses. The State Department considered this case to be "…regarded as of a private nature, jure gestiovis, for which sovereign immunity from suit cannot be recognized" (State Department, 1977). Hence, it appears that the State Department was willing to apply restrictive immunity, but only when it would not cause further strain on its foreign relations.

This leads to the question: Would outcomes in immunity requests from Cuba be different

if the request was over a different issue area? To examine this, I use machine learning (ML) classifiers through diverse counter factual explanations as developed by Mothilal, Sharma, & Tan (2020). It creates a counterfactual by utilizing an ML model and changes the value of an independent variable to generate a different outcome.[21] Essentially this method is implemented via four steps. First, the data is split into a testing and training set.[22] Second, a model is fitted on the training data using a random forest classifier. Next, the counterfactuals are generated using randomized sampling.[23] Lastly, to examine the validity of the results, local and global feature importance scores are estimated using the generated counterfactuals.[24] Hence, an importance score is the fraction of counterfactuals that have a modified value of a specific feature.[25] A local importance score is the score for a specific observation one is interested in. The global importance score is for the entire sample.

For this method, the dependent variable continues to be "Diplomatic Request Denied?", but all cases that were ignored by the State Department are dropped for this analysis as this method, in its current iteration, works best with binary dependent variables. The only features included are Type Economic, Year, and Country name. All remaining cases, after dropping observations that were ignored, are included in the analysis. However, as my focus is on Cuba, I will be generating counterfactuals for Cuban cases only. Focusing just on counterfactuals for Cuba helps validate the results as it can be verified by contextual knowledge. After splitting the data into training and test sets, only four Cuban cases are available to generate a counterfactual on. As the interest here is in Type Economic, it will be this feature that is permitted to vary. I limit the max number of counterfactuals to produce to four due to the small number of observations. Results are presented in Tables 5-8 below.

[21] See Appendix 6.1 for more information.

[22] In this analysis, it is split, 60/40.

[23] Other options include genetic algorithm search and kd-tree based generation, but due to sample size, I chose the simplest option.

[24] The importance scores are calculated by averaging c = arg min yloss$(f(c), y) + \lambda_1 dist(c, x)$ See Appendix 6.1 for more information.

[25] see Mothilal, Mahajan, Tan, & Sharma (2021)

Table 5: Mayan Lines v. Republic of Cuba

Year	Country	Type Economic	Denied?
1965	Cuba	Debt - Trade	Yes

Counterfactual Set	
Debt - Bond	No
Other	No
Exprop. - Physical	No
Unknown	No

Local Importance
Country - 0.7, Type Economic - 0.6, Year - 0.4

Table 6: O'Brien v. Republic of Cuba

Year	Country	Type Economic	Denied?
1952	Cuba	Other	No

Counterfactual Set	
Exprop. - Payments	Yes
Debt - Trade	Yes

Local Importance
Country - 0.75, Type Economic - 0.6, Year - 0.6

Table 7: Flota Maritima Browning

Year	Country	Type Economic	Denied?
1962	Cuba	Exprop. - Physical	No

Counterfactual Set	
Exprop. - Payments	Yes
Debt - Trade	Yes

Local Importance
Country - 0.7, Type Economic - 0.55, Year - 0.6

Table 8: Naviera Vacuba

Year	Country	Type Economic	Denied?
1961	Cuba	Other	No

Counterfactual Set	
Exprop. - Payments	Yes
Debt - Trade	Yes

Local Importance
Country - 0.75, Type Economic - 0.55, Year - 0.55

The results above confirm that in the case of Cuba, the State Department was making decisions that were based on what was most politically safe and not based on the guidelines as outlined in the Tate Letter. According to the local importance scores, Type Economic is important in determining outcomes. Country was regularly of greater importance, but due to theoretical interest and ease of interpretation, I chose to control for it. The global importance calculation confirmed the local importance results (Global Importance - Country 0.86, Type Economic 0.57, Year 0.45). Table 5 presented a case where the immunity request was denied. In this case, the model suggested that to change the outcome to where the immunity request would be granted, Type Economic would need to be changed to Debt - Bond, Other, Expropriation

- Physical, or Unknown. Debt - Bond and Expropriation - Physical are both categories that denying immunity would be particularly intrusive and, as such, less likely to occur in a politically sensitive situation. Tables 5-8 all involve cases over a physical asset where immunity was granted, but to change the outcome the model predicted that Type Economic would need to be changed to either Expropriation - Payments or Debt - Trade, which are two categories that are less intrusive. Overall, while it is evident that the State Department was not consistently biased against investors, it is also the case that the State Department was not following the Tate Letter. For this reason, investors wanted an environment in which the State Department had no role in deciding sovereign immunity in disputes with sovereign states.

2.6.2 The Courts

Were investors correct that the US judiciary would be better at applying the Tate Letter? What criteria did the judiciary use to determine whether to apply absolute or restrictive sovereign immunity? To better understand judicial decision-making, I first examine the raw data. Table 9 presents the outcomes of lawsuits where the State Department was not involved. What is prominent is that out of the 11 cases involving bonds, 10 were won by the defendant (the country that defaulted). Despite this being a commercial issue, US courts rarely ruled in favor of the plaintiff. This lends support to Hypothesis 2. As sovereign debt was viewed as an internal sovereign issue, the judiciary were less likely to rule in favor of the plaintiff. In addition to sovereign bonds, the judiciary appeared to be willing to grant absolute sovereign immunity over Debt - Trade issues as well. Of the 15 Debt - Trade cases, the judiciary ruled in favor of the defendant 11 times. In contrast, with Expropriation - Payments, out of the 7 cases, courts ruled in favor of the plaintiff 6 times. For Expropriation - Physical, ruling propensity was nearly split evenly between the two outcomes. If the court was indeed applying the Tate Letter, then nearly all outcomes in the suits included in Table 9 should be in favor of the plaintiff as these are commercial issues. However, this is not the case. At face value, the expectation is that the judiciary would apply the Tate Letter. Nonetheless, since the Tate Letter lacked clarity, the judiciary had the discretion to select between absolute and restrictive immunity with ease. Absent State Department involvement, it is evident that the judiciary favored awarding absolute sovereignty

when the lawsuit involved issues that were deemed domestic problems, such as soveriegn debt.

Table 9: Court Outcomes - No State Department Involvement

	Type Economic					
	Debt-Bond	Debt-Other	Debt-Trade	Exprop.-Payments	Exprop-Physical	Other
Winner						
Defendant	10 (27%)	0 (0%)	11 (30%)	1 (2.7%)	7 (19%)	8 (22%)
Plaintiff	1 (2.6%)	2 (5.1%)	4 (10%)	6 (15%)	6 (15%)	20 (51%)
Total	11 (14%)	2 (2.6%)	15 (20%)	7 (9.2%)	13 (17%)	28 (37%)

While the lack of the clarity in the Tate Letter led to it not being applied in certain issue areas by the judiciary, the degree to which the State Department influenced the judiciary remains a question. To examine this, the lawsuits where the State Department either denied or granted immunity are presented in Table 10 and 11, respectively. When the State Department denied an immunity request, this suggests that the State Department stance on the issue was that absolute immunity should not be applied. If the judiciary simply went along with the State Department, two trends in the data should be present. First, in cases where the State Department denied absolute sovereign immunity, the judiciary should be ruling in favor of the plaintiff. Second, in cases where the State Department granted absolute immunity, the judiciary should be more likely to rule in favor of the defendant.

Table 10: Court Outcomes - State Department Denied Immunity

	Type Economic					
	Debt-Bond	Debt-Other	Debt-Trade	Exprop.-Payments	Exprop.-Physical	Other
Winner						
Defendant	0 (0%)	0 (0%)	4 (50%)	1 (12%)	1 (12%)	2 (25%)
Plaintiff	1 (11%)	0 (0%)	2 (22%)	3 (33%)	1 (11%)	2 (22%)
Total	1 (5.9%)	0 (0%)	6 (35%)	4 (24%)	2 (12%)	4 (24%)

However, as seen in Table 10 above, it is not the case that the judiciary follows along with State Department suggestions. When the State Department denies an absolute immunity request, it does not guarantee that the plaintiff will automatically win a case. Moreover, as presented in Table 11 below, the granting of an absolute immunity request by the State Department, also does not guarantee that the judiciary will rule in favor of the defendant. Regardless of any suggestion from the State Department, there was no assurance that the courts would issue rulings in a specific direction. Hypothesis 3 is supported by the data. It is not the case that the a clear immunity decision issued by the State Department guarantees that the judiciary will make a decision that is aligned with the State Department. Overall, it does not appear to be the case that removal of the State Department will lead to greater application of the Tate Letter. While the State Department is an agent of the executive branch, the judiciary has inherent biases of its own.

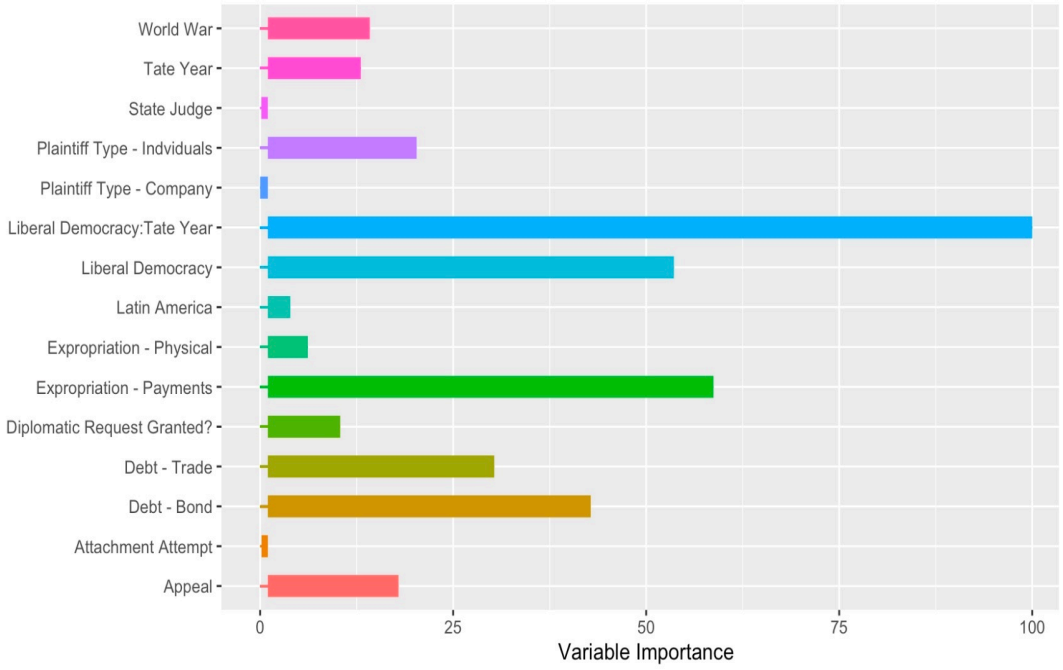
Table 11: Court Outcomes - State Department Granted Immunity

	Type Economic					
	Debt-Bond	Debt-Other	Debt Trade	Exprop.-Payments	Exprop.-Physical	Other
Winner						
Defendant	2 (14%)	0 (0%)	2 (14%)	0 (0%)	4 (29%)	6 (43%)
Plaintiff	0 (0%)	0 (0%)	3 (43%)	2 (29%)	1 (14%)	1 (14%)
Total	2 (9.5%)	0 (0%)	5 (24%)	2 (9.5%)	5 (24%)	7 (33%)

From the tables above, it is evident that the US judiciary were not always applying restrictive immunity in commercial cases. Given that US courts were inconsistent in applying the Tate Letter, how did the judiciary make decision in these cases? As a first cut at understanding what factors influenced judicial outcomes, I estimate a binomial elastic net model. The dependent variable here is "Defendant Win", which is a binary variable that takes on a value of "1" if the court outcome is in favor of the defendant and "0" otherwise. The variable "Tate Year" is assigned a value of "1" if a case took place while the Tate Letter was in effect, and "0" if not. To test Hypothesis 1, "Liberal Democracy" is included along with its interaction with "Tate Year" to examine whether after the Tate Letter, the more democratic the country is, the more likely it is to be awarded absolute sovereignty. The variable "Type Economic" is included, with the reference category being the "Other" group.[26] As noted, the data set on litigation in US courts only includes commercial cases. As a result, "Other - Not Commercial" was not an available category to be used as the reference category as it was with the analysis of the State Department granting of immunity requests. The inclusion of Type Economic will permit the testing of Hypothesis 2. Also included are "World War", "Appeal?", "Attachment Attempt","Latin America", and "State Judge?". "State Judge?" is included because it may be possible that judges who are elected rather than appointed may rule differently. "Plaintiff Type" is included with bank as a reference category. The "Diplomatic Request Granted?" variable is also included. The results are presented in Figure 2.2.

[26]With Machine Learning techniques, categorical variables must be transformed into indicator variables for each category.

Figure 2.2: Court Decision - Elastic Net



The results above overwhelmingly demonstrate that the economic issue area of a dispute and the interaction between Liberal Democracy and Tate Year are useful in understanding case outcomes. "State Judge", "Plaintiff Type - Company", and "Attachment Attempt" were given a zero coefficient. The variable that appears to be able to explain whether a defendant won a case to a great degree is the interaction of Liberal Democracy and Tate Year, which lends support to Hypothesis 1. Of the categories that comprise Type Economic, "Expropriation - Payments", "Debt - Bond" and "Debt -Trade" that influence the outcome variable, which lends support to Hypothesis 2. The "Diplomatic Request Granted?" variable is near 0, which indicates that it is not a major determinant of court outcomes. As a result, this supports Hypothesis 3. To validate this result and examine which direction these variables are in, I estimate an ordinary least squares regression for ease of interpretation and the fewer assumptions that it requires. The results are presented in Table 12. For Model 1, robust standard errors clustered by country

are utilized and for Model 2 the robust standard errors are clustered by court. Clustering by country and court was chosen to ensure that a particular group of observations are not driving results.

The results in Table 12 support the results from the elastic net estimation. The interaction between Liberal Democracy and Tate Year is statistically significant at the 1% level for Model 1 and 2. Moreover, Liberal Democracy is significantly different from zero for both models. In the pre-Tate Letter period, as democracy increased, the probability of a defendant winning decreases by .62. During the Tate Letter years, the probability of a defendant winning a case increases by 1.09 for every one unit increase in Liberal Democracy. This supports Hypothesis 1. After the Tate Letter, the more democratic the country is, the more likely it is to be awarded absolute sovereignty. Tate Year is insignificant in both models. This is expected as the Tate Letter did not delineate a clear definition of what is commercial and how it interacts with other doctrines. Debt - Bond is in the positive direction and statistically significant. When a dispute is over defaulted sovereign bonds, the defendant state is most likely to win a case. This lends support Hypothesis 2 that US courts are more likely to rule in favor of a country (the defendant) if the suit involves a commercial issue that is viewed as an internal decision. The decision to default on a bond is more likely than the other types of economic issues to be viewed as a sovereign internal matter. Debt - Trade is only statistically significant and in the positive direction in Model 2. Expropriation - Payments is in the negative direction and statistically significant, which suggests that for issues that are least likely to occur within the borders of a sovereign state, restrictive immunity is more likely to be applied. "Diplomatic Request Granted?" is insignificant in both models. This lends support to Hypothesis 3 that the State Department did not have great influence over the judicial decision-making even when they were involved.

Table 12: OLS Regressions of Court Outcomes

	Dependent variable: Defendant Win	
	(1)	(2)
Liberal Democracy	-0.62^{**}	-0.62^{***}
	(0.28)	(0.20)
Tate Year	-0.17	-0.17
	(0.20)	(0.13)
Diplomatic Request Granted?	0.10	0.10
	(0.13)	(0.13)
Attachment Attempt	-0.01	-0.01
	(0.12)	(0.13)
Plaintiff Type - Company	0.04	0.04
	(0.17)	(0.38)
Plaintiff Type - Individuals	0.23	0.23
	(0.14)	(0.36)
Debt-Bond	0.36^{**}	0.36^{*}
	(0.15)	(0.21)
Debt-Trade	0.31	0.31^{***}
	(0.19)	(0.11)
Expropriation-Payments	-0.44^{**}	-0.44^{***}
	(0.17)	(0.17)
Expropriation-Physical	0.08	0.08
	(0.18)	(0.21)
Appeal?	0.15^{*}	0.15^{**}
	(0.08)	(0.06)
Latin America	0.04	0.04
	(0.11)	(0.10)
World War	-0.15	-0.15
	(0.24)	(0.12)
State Judge?	-0.03	-0.03
	(0.10)	(0.10)
Liberal Democracy:Tate Year	1.09^{***}	1.09^{***}
	(0.32)	(0.39)
Constant	0.36	0.36
	(0.26)	(0.38)
Note:		*p<0.1; **p<0.05; ***p<0.01

Model 1 has Robust Standard Errors clustered by Country. Model 2 has Robust Standard Errors clustered by Court. Dependent variable is "Defendant Win" that is coded as "1" if the defendant won the lawsuit and "0" otherwise.

Although these results lend support to Hypothesis 1, 2, and 3, to examine this further, I apply generalized random forests (GRF) (Athey, Tibshirani, & Wager, 2019) to the data via a doubly robust empirical welfare maximization over the produced trees (Athey & Wager, 2021). This method is used to figure out where a treatment would be most beneficial[27] and will be used to understand whether the enactment of the Tate Letter was beneficial for any particular group of countries. The regression results already seem to indicate that how democracies were treated pre and post Tate Letter differed with democracies more likely to benefit during the Tate Letter era. While the implementation of the Tate Letter will be used as the treatment variable in this analysis, I am not claiming causality. As discussed, the Tate Letter added noise to the decision-making environment, but was not a doctrine that required a judge to make a change as guidelines were unclear and it was not a piece of legislation that was passed by Congress or a Supreme Court ruling.

To implement this method, I first fit a causal forest via GRF. GRF differs from a classical random forest, an ensemble model composed of a group of decision trees, by maximizing heterogeneity among the last nodes of a tree (Athey et al., 2019).[28] After fitting the causal forest, doubly robust scores are computed. Doubly robust scores produce an unbiased average treatment effect by combining regression and propensity score methods.[29] Next, the doubly robust scores are then used to fit a policy tree.[30] A policy tree depth needs to be shallow, so that the results are meaningful. I set the depth to 2, which means that from the origin node on the tree there will be only 2 branches.

When using a GRF, to assess fit, a calibration test can be estimated and this is presented in Table 13. As a rule of thumb, for the mean forest prediction, a coefficient as close to 1 as possible is ideal as it suggests that the resulting predictions are correct. The "differential forest

[27]For example, if there is a limited amount of drugs available to treat a particular disease, this method would help aid in determining whom to treat.

[28]Typically, you would split the data into a training and testing set. However, I chose not to here because the data set is small and the Type Economic variable is detailed, so upon a random splitting, there would not be enough observations in each category to obtain results that are most reflective of the substantive situation and not just mathematically correct.

[29]See Chernozhukov, Escanciano, Ichimura, Newey, & Robins (2020) for more details.

[30]A policy tree is estimated via $\hat{\pi} = argmax \frac{1}{n} \sum_{i=1}^{n} (2\pi(X_i) - 1)\hat{\Gamma}_i : \pi \in \Pi$ where $\hat{\pi}$ is the resulting policy, Π is the depth of a tree, X_i are the covariates, and Γ_i the doubly robust scores.

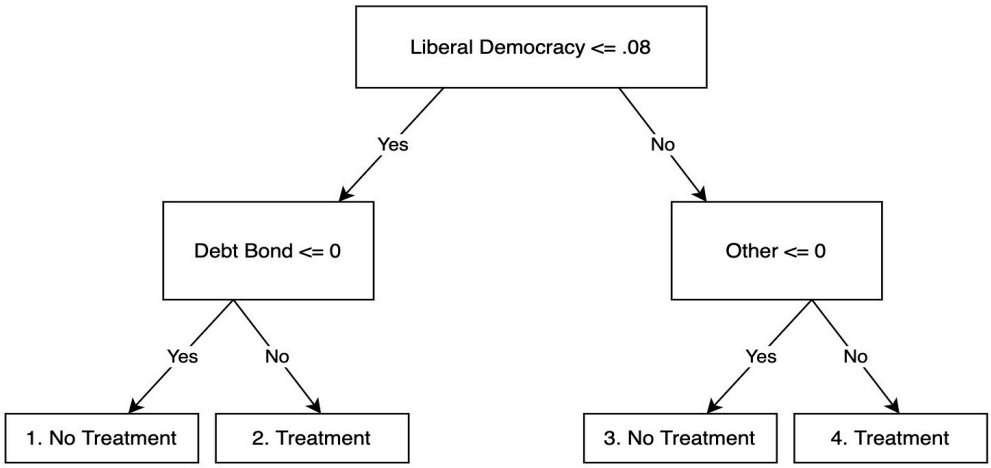
prediction" coefficient signals whether there is any heterogeneity in the estimated model. In order to estimate a model that is useful for evaluating policy responses, heterogeneity needs to present. If the differential forest prediction coefficient is significant, then the null of no heterogeneity can be rejected. An additional rule of thumb is that the closer to 1 the coefficient of the differential forest prediction is the more likely there is to be heterogeneity. While the results in Table 13 are imperfect, overall they suggest that the GRF estimation is usable.

Table 13: GRF Model Efficacy

Mean Forest Prediction	0.837*
	(0.629)
Differential Forest Prediction	0.584**
	(0.326)
Note:	*p<0.1; **p<0.05; ***p<0.01

The resulting policy tree is presented in Figure 2.3. This tree presents information on what subsets of the population *should* receive a treatment as it would prove to be the most beneficial among this group. In the context being studied here, the group identified as benefiting from a treatment means that it is this particular that benefited most from being seen after the Tate Letter was implemented. According to this tree, a non-democratic country is less likely to be ruled against if the suit is over bond than if it was over any other issue. The more democratic countries are most likely to benefit if the suit involves any issue that does not fall under the "Other" category. As a reminder, the "Other" category includes items such as a vessel crashing into a port and violating the Securities Exchange Act of 1934. Essentially, the group of activities that should, theoretically, lead a country to be ruled against during the Tate Letter era, is less likely to occur as the level of democracy in a country increases.

Figure 2.3: Policy Tree



The results from the policy tree supports the OLS results and the hypotheses, but are these results significant? Table 14 and 15 presents the subgroup treatment effects among the treated and untreated, respectively. Of particular importance are nodes 2 and 4, which are significant and the treated have a higher mean value than the untreated, which suggests that in the Tate Letter Years, disputes over sovereign bonds and democracies were likely to have court outcomes in their favor. Overall, autocracies who are in a dispute over sovereign bonds increases the probability of winning a court case during the Tate Letter period than prior to the Tate Letter. Moreover, the probability of a democracy winning a dispute increases by .77 during the Tate Letter period.

Table 14: Treatment Effect - Treated

Node	Mean	SE	Lower CI	Upper CI	p-value
1	0.42	0.08	0.26	0.58	0.00
2	0.85	0.11	0.64	1.07	0.00
3	0.29	0.15	-0.01	0.58	0.06
4	0.77	0.06	0.66	0.88	0.00

Table 15: Treatment Effect - Untreated

Node	Mean	SE	Lower CI	Upper CI	p-value
1	0.97	0.06	0.86	1.08	0.00
2	0.76	0.13	0.50	1.02	0.05
3	0.87	0.08	0.70	1.03	0.09
4	0.16	0.10	-0.04	0.36	0.12

2.7 Discussion

How did the judiciary choose which type of sovereignty to utilize? Did the formal establishment of the Tate Letter have an impact on decision-making? The State Department may have issued the Tate Letter, which instituted restrictive immunity, but they did not apply it consistently. It was inconsistent in its application of restrictive immunity because it did not want to increase tensions with a country where a difficult relationship already existed or risk any foreign policy aims they may have by infringing on state sovereignty. Under the Tate Letter regime, a country had an option to make a request for absolute sovereignty to the State Department to avoid being ruled against and, therefore, having restrictive immunity applied. However, the State Department did not always grant a country absolute sovereignty, but they also did not always apply restrictive immunity to commercial cases. The raw data, as presented in Table 1, demonstrates that the State Department was inconsistent in its application of the Tate Letter. 37% of immunity requests were denied and only 41% were granted. Most importantly, as presented in Table 2, among the commercial requests, 32 were denied immunity and 27 were granted immunity.

The statistical results also support the conclusions drawn from examining the raw data that the State Department did not apply restrictive immunity consistently and that their decisions lacked a clear pattern based on the type of economic issue the dispute was over. However, the results from the elastic net model suggest “Expropriation - Payments”, “Expropriation-Physical”, “Other”, and “Debt - Bond” are issue areas that are most likely to lead to the granting of absolute sovereignty. This result suggests that the Tate Letter was not being followed by the State Department as cases involving commercial disputes were being granted absolute

sovereignty. To further test if there is a relationship between Liberal Democracy, Latin America, or Type Economic, I utilized OLS regression with robust standard errors as presented in Table 3. The results generally suggest that geographic location of a country and regime type do not influence the State Department. Furthermore, all of the Type Economic categories were insignificant as well. The raw data, the elastic net estimation, and the OLS results combined suggest that (1) other factors than the Tate Letter impacted State Department decision-making and (2) restrictive immunity was not being applied as laid out in the Tate Letter.

It is evident that restrictive immunity was not applied when it, theoretically, should have been by the State Department if the Tate Letter was followed. Moreover, a clear pattern is missing in the data. To investigate this further, the case of Cuba was examined. By examining requests made by Cuba, it became evident that the State Department did not apply restrictive immunity when it was politically difficult to do so. From the counterfactual exercise, it appears that the State Department was less likely to deny immunity for commercial issues when the dispute was over assets within the borders of Cuba. Given this, it may seem that the judges involved in the Victory Transport case were correct in their belief that friendly states were more likely to be declined immunity by the State Department. However, for the State Department, it was less about the dichotomy between friendly and unfriendly, but political feasibility. The State Department did decline immunity requests from Cuba when the request was over an economic issue that made it easy to do so. These economic issues tend to be those where the asset was not physically located within Cuba's borders and those that involved planes and vessels. Moreover, not all requests made by friendly states were denied. For example, Israel, Mexico, and India have all had immunity requests granted.

Overall, the State Department made decisions regarding immunity on a case-by-case basis that took into account the current political environment. The State Department did not apply restrictive immunity as laid out in the Tate Letter and, therefore, investors want for change was not misplaced as the interests of investors were not safeguarded. However, would the judiciary be better at applying restrictive immunity? How did they make decisions during the same period?

To examine the decision-making of the judiciary, Table 9 presented the court cases where the defendant did not make an immunity request. From this, it is apparent that the judiciary

did not always apply restrictive immunity. It is possible that a court could apply restrictive immunity and still rule in favor of the defendant, but in cases involving the default of bonds or trade credits, it is difficult to fathom a situation where restrictive immunity is applied and the plaintiff does not win as it is a clear violation of any commercial contract. The results demonstrated that the judiciary was also unlikely to rule in favor of the plaintiff when a dispute was over bonds. This is because the decision to default is viewed as a strictly internal decision. With the Tate Letter being unclear about what is or is not a commercial act, courts were left to define this boundary for themselves. What is considered a commercial act may vary by court, but it is clear both from the statement made in the Victory Transport case and the data that the decision to default was viewed as a uniquely sovereign and internal choice that should not be challenged in courts. The data lend support to Hypothesis 1.

Tables 10 and 11 presented the court cases where the State Department was involved in deciding sovereign immunity. From these tables, it is apparent that the judiciary does not always follow along with suggestions from the State Department. If it did follow the State Department, then when the State Department denied immunity, plaintiffs should always win and when the State Department granted immunity, the plaintiff should always lose. However, this is not what occurred. Despite the role of the State Department in these cases, US courts were still an independent body able to decide when it wanted to follow along with the State Department. Table 16 below presents all the court cases against Cuba that the State Department was also involved in. To reiterate, when the State Department declines immunity, if the court just follows along, then in these cases, the defendant should always lose the case. When immunity is granted, the defendant should win. Among the sample of Cuba cases, there are 4 cases whose outcomes do not match expectations following a State Department decision.[31] While Cuba is a hard test to assess judicial independence from the State Department as Cuba was politically prominent during the Cold War, even in this case, the courts were not guaranteed to follow State Department suggestions. Hypothesis 3 is supported with the data.

[31] In particular, French v. Cuba is interesting as when the case was appealed, the court, comprised of different judges from the original court, switched their position.

Table 16: Cuba Court Cases - State Department Involved

Date	Type Economic	Case Name	Request Denied?	Defendant Winner?
1961-03-24	Debt-Trade	Harris & Co. Advertising, Inc. v. Republic of Cuba	0	No
1961-05-15	Exprop.-Payments	Republic of Cuba v. Ritter	1	No
1961-08-29	Other	Rich v. Naviera Vacuba, S.A.	0	Yes
1961-09-22	Other	Republic of Cuba v. Arcade Bldg. of Savannah	0	Yes
1961-11-17	Exprop.-Physical	Republic of Cuba v. Dixie Paint & Varnish Co.	0	Yes
1961-12-21	Other	Cuban Air Force, F.A.R. v. Bergstresser	0	No
1961-12-26	Exprop.-Payments	Gonzalez v. Industrial Bank	1	No
1962-02-06	Exprop.-Physical	National Institute of Agrarian Reform v. Dekle	0	Yes
1962-09-04	Debt-Trade	Republic of Cuba v. Mayan Lines, S.A.	0	Yes
1962-10-09	Debt-Trade	Berlanti Construction Co. v. Republic of Cuba	1	Yes
1963-05-14	Exprop.-Physical	National Institute of Agrarian Reform v. Kane	0	Yes
1964-07-14	Exprop.-Physical	Flota Maritima Browning de Cuba v. Ciudad Habana	1	No
1966-12-20	Exprop.-Payments	French v. Banco Nacional De Cuba	1	No
1968-10-15	Exprop.-Payments	French v. Banco Nacional De Cuba	1	Yes
1974-02-13	Debt-Trade	Spacil v. Crowe	0	Yes

Given that the judiciary does not appear to be heavily influenced by the State Department in cases where they are involved, how do US courts decide cases? After 1952, the judiciary were put in a position to choose between following the Tate Letter and the Act of State doctrine. The Tate Letter increased uncertainty in the decision-making environment because it left key terms undefined drawing it into direct conflict with the Act of State doctrine, which states that the actions taken within the borders of a sovereign cannot be questioned by a court outside of that country. Due to this uncertain legal environment, judiciary would consider the regime characteristics of the defendant country and the issue area that the dispute was over prior to coming to a decision. As such, the judiciary is likely to rule in favor of the defendant when the commercial dispute is over issues that take place within the borders of the defendant country such as default on sovereign bonds or if the country is a democracy. The Act of State doctrine states that the laws and choices of a country should be deferred to, but in an environment where the Tate Letter exists concurrently, the judiciary needed to decide when to apply the Act of State doctrine vs. the Tate Letter. As democracies are most similar to the United States, I

argued that democracies were the most likely group of countries to have their laws and decisions respected.

To examine the judicial preferences towards countries with more democratic features during the Tate Letter era and the tendency to rule in favor of a country if the suit involves a commercial issue that is viewed as an internal decision, I first estimate an elastic net model that is presented in Figure 2.2. The results showed that State Department decisions mattered very little as the "Diplomatic Request Granted?" was not a main variable that explained the outcome the most, which supports Hypothesis 3. The variable that appears to be able to explain whether a defendant won a case to a great degree is the interaction of Liberal Democracy and Tate Year, which lends support to Hypothesis 1. Of the categories that comprise Type Economic, "Expropriation - Payments", "Debt - Bond" and "Debt -Trade" that influence the outcome variable, which lends support to Hypothesis 2. This finding was then further probed with OLS and robust standard errors, which are presented in Table 12.

The OLS results confirm that defendants with more democratic features are likely to win cases during the Tate Letter period. Moreover, it was found that defendants were also more likely to win when the dispute was over defaulted bonds supporting the theory that judges were unwilling to apply restrictive immunity for issues that they viewed as inherently internal. The finding that Debt - Trade was also significant and in the positive direction in Model 2 also supports Hypothesis 2 as trade credits have similar characteristics to that of bonds. The physical expropriation of assets is a difficult issue area as it usually takes place within the borders of a country, but, depending on the context of the situation, it may be against customary international law. Under customary international law, expropriation is permissible when it is accompanied by compensation and is taken for a public purpose as regulated by domestic law.[32] Hence, in some expropriation cases, the application of restrictive immunity would have judges intruding upon internal decisions by a government. Its insignificance in the OLS model is reflective of its position between being within the borders of a country and against international law. Expropriation - Payments is in the negative direction and significant, however. This

[32]Over time, international law towards expropriation would change, but during the time period under investigation here, there was more tolerance for expropriation and fewer outlets for investor grievances.

suggests that for issues that are least likely to occur within the borders of a sovereign state, restrictive immunity is more likely to be applied. "Diplomatic Request Granted?" is insignificant in both models. This lends support to Hypothesis 3 that the State Department did not have great influence over the judicial decision-making even when they were involved.

As a further probe of these results, I estimate a GRF with doubly robust empirical welfare maximization to produce a policy tree. This model is used to predict which subgroup of observations are most likely to benefit from the treatment (the Tate Letter). Benefiting from treatment here means a court ruled in favor of the defendant. The results are presented in Figure 2.3 and Tables 14 and 15. According to this model, democracies where more likely to be ruled in favor of during the Tate Letter period than period prior to the Tate Letter across commercial issue areas. However, even autocracries would receive a ruling in their favor if the issue are of the dispute was over sovereign bonds. Hypothesis 1 and 2 are supported by this analysis.

Overall, the GRF analysis suggests that regime type after the implementation of the Tate Letter influenced judicial outcomes. Its implementation was most beneficial for countries with democratic institutions as it influences judges to rule in favor of the defendant (the country). The judiciary takes into consideration the domestic institutions of the defendant country because the legal environment after 1952 was rife with uncertainty. As judges did not whether they should apply the Tate Letter or the Act of State doctrine, using the principle of prescriptive international comity, they would apply the Act of State doctrine when the defendant country had domestic institutions similar to those of the US. Hence, after the Tate Letter, the more democratic the country is, the more likely it was to be awarded absolute sovereignty. However, it is also the case that defendant countries with more authoritarian institutions were likely to benefit if the suit was over sovereign bonds. A sovereign default was viewed as an internal decision by the government as it was considered an issue area that affected the every day running of a country and, therefore, it was not the place of the courts to make economic policy for a country. While democracies have advantage over in all economic issue areas, US courts are more likely to rule in favor of a defendant irrespective of their regime type if the suit involves a commercial issue that is viewed as an internal decision.

2.8 Conclusion

US investors and banks received protections from the State Department under dollar diplomacy that persuaded them to invest in countries that they would not have otherwise due to decrease in risk. While investors wanted this practice to continue, the State Department was hesitant to provide these protections and wanted to decrease their role in managing relations between investors and the countries they invest in. As the international community began to adopt restrictive immunity, the State Department issued the Tate Letter. Issuing the Tate Letter served two purposes. First, it delegated authority to US courts in order to reduce the involvement of the State Department in commercial disputes. Under the Tate Letter, the State Department would only become involved in a dispute if a request was made by a sovereign state. Second, as other countries were adopting restrictive immunity, the US did not want its investors to be at a disadvantage in the international marketplace. Consequently, the Tate Letter fulfilled these two objectives simultaneously.

However, the delegation of authority to US courts did not lead to the application of the Tate Letter as it was originally formulated nor was it followed by the State Department. As the State Department functions under the authority of the executive branch, it is expected that they would prioritize foreign policy considerations and other internal protocols of the executive branch, which may prevent them from adhering to the guidelines publicly declared in the Tate Letter. Nevertheless, US courts also did not follow the guidelines of the Tate Letter. This is not only because of the irregular involvement of the State Department in the decision-making process, but because the Tate Letter was unclear. The Tate Letter did not provide a definition of what is or is not to be considered commercial. Due to lack of clarity in the Tate Letter over what is or is not a commercial activity, guidance for the judiciary on when to apply the Tate Letter rather than the Act of State doctrine was missing. For this reason, in this uncertain legal environment, judges could pick and choose whether to apply restrictive immunity (the Tate Letter) or absolute sovereign immunity (Act of State doctrine).

In this uncertain legal environment, how did the judiciary decide to apply the Tate Letter rather than the Act of State Doctrine? Were countries with certain characteristics more likely to

be awarded absolute sovereignty than another? I argued that even though restrictive immunity was supposed to be applied to all commercial cases after the enactment of the Tate Letter, absolute sovereignty was more likely to be applied when the defendant country was a democracy and if the dispute involved sovereign debt. When determining which course of action to pursue, the principle of prescriptive international comity, which was codified in the Act of State doctrine, and maintains that a judge should be respectful of the laws and rulings of foreign countries, was more likely to be applied in cases where the defendant state was a democratic government. As a result, democracies were more likely to be awarded absolute sovereignty because judges were more likely to defer to the decisions made by a country with similar institutions to the US than autocracies. Second, since sovereign debt is commonly utilized for domestic financing purposes, it remained perceived as an internal sovereign matter. For this reason, the judiciary was unwilling to assume the responsibility of prescribing economic policy to an independent state. Regime type of the defendant state was not a deciding factor for this issue area.

While the State Department retained the ability to intervene in cases when requested by the defendant state, the State Department at times would ignore requests or even deny a country absolute sovereignty. A state going to the State Department did not guarantee that the State Department would grant them absolute sovereignty. Naturally, with the delegation of authority by the State Department to US courts, there is an anticipation that a US judge may align with the State Department's stance if they were to intervene. However, this was not necessarily the case. In a number of cases, the judiciary would often rule differently than the State Department. The State Department and the US judiciary are separate entities with varying organizational cultures and responsibilities, which meant that their preferences were not always in agreement.

Investors in general, and bondholders even more so, were dissatisfied with the system established by the Tate Letter. Their main concern was to minimize the State Department's involvement in the hope of broadening the application of restrictive immunity. However, during this time, the judiciary was no more likely than the State Department to consistently implement restrictive immunity. Nevertheless, investors wanted the State Department removed from the judicial decision-making process, and their pressure eventually led to the replacement of the Tate Letter with the FSIA. Along with eliminating the State Department, the FSIA addressed the

procedural shortcomings of the Tate Letter, such as the lack of a clear definition of "commercial" and the ability of plaintiffs to seize a sovereign state's assets. Although the FSIA represented a significant improvement on paper for investors, it did not necessarily guarantee impartiality on the part of judges in the FSIA period.

Chapter 3

Violating Impartiality: The United States Judiciary Governing the Market

Abstract: Following pressure from investors, the 1976 Foreign Sovereign Immunities Act (FSIA) was passed by Congress to increase separation between the executive and judicial branch. Most importantly, however, unlike previous guidance provided by the State Department, the FSIA defined what is or is not a commercial act. Sovereign debt under this new legal regime could not be dismissed as a sovereign issue. Thus, it would be reasonable to suppose that the majority of lawsuits involving sovereign debt are won by plaintiffs because the evidence that a state—the defendant—defaulted is clear. This, however, does not occur in practice. What affects the decisions judges make? I argue that a judges' ideological inclination affects their decisions. Conservative judges, unlike their liberal counterparts, practice judicial restraint on economic issues meaning that they are more likely to uphold the FSIA and rule against the defendant because conservatives are pro-business and less interventionist in the economy. Due to spillover effects from a sovereign default into the trade arena, the difference in ruling propensity between conservative and liberal judges is most acute when the defendant is a democracy. Democracies tend to have closer trade ties with the US than other regimes and, therefore, conservative judges will still rule against a democracy to protect business interests. However, as democracies tend to have more veto players than autocracies, the decision to default may appear to be more credible from a democracy as the political consequences from a default are more easily materialized. For this reason, as liberal judges are unlikely to practice judicial restraint on economic issues and are not pro-business like conservatives, they are more likely to rule in favor of democracies because the decision to intervene in the economy through a default is credible. As a result, the greatest difference in ruling propensity is when the defendant is a democracy. I test my argument with an original data set of US sovereign debt litigation cases that covers the period between 1977 and March 2022. Using Bayesian hierarchical modeling and Virtual Twins, I demonstrate that the outcome of a case is influenced by (a) whether the case is assigned to a liberal or conservative judge, (b) the strength of economic ties between the United States and the debtor state, and (c) the level of democracy in the defendant country. Despite expectations, plaintiffs do not regularly win.

3.1 Introduction

In an Opinion issued on July 8th, 1983 in the case of Allied Bank International vs. Costa Rica, Judge Griesa stated that he would not rule in favor of the plaintiff (Allied Bank International) despite the evidence against Costa Rica. According to Judge Griesa, "The essential facts [of the case] are not in dispute…" because the Costa Rican government did stop payments to creditors and did default.[1] Based on the facts, Allied Bank International should have won this case, but yet, they did not. Why did Judge Griesa not rule in favor of the plaintiffs if the facts were clear? What affects the decisions judges make?

Prior to the 1976 Foreign Sovereign Immunities Act (FSIA), the dispute settlement process between a sovereign state and an investor fell under the guidance of the 1952 Tate Letter that was issued by the State Department. The Tate Letter changed the official US foreign policy of granting absolute sovereignty to restrictive sovereignty. This meant that a country could no longer claim sovereign immunity over commercial transactions, which should have made it easier for investors to have their day in court. However, two weaknesses existed under the Tate Letter regime that led to its replacement. First, a sovereign state could file an absolute sovereign immunity request with the State Department. Second, a definition of "commercial" was lacking in the Tate Letter, which gave judges leeway in the application of restrictive immunity. As a result, there was pressure from investors to replace the Tate Letter regime with a dispute settlement process that was free of political interference.

Formally, the FSIA has rectified the issues of the Tate Letter. The US judiciary were given sole oversight in disputes involving a sovereign state. As a result, US judges could now make decisions without the involvement of the State Department. Moreover, the FSIA clarified what acts of a state should be considered a commercial act and how to make this determination. Under the FSIA, to determine whether an act is commercial or not, the "nature of the act" test is used. This means that when evaluating a case to determine whether it falls under the purview of the FSIA, a judge needs to consider the nature and not the purpose of the act. For example, prior to the FSIA, sovereign debt would typically not be considered a commercial act

[1] "Allied Bank International v. Banco Credito Agricola, 566 F. Supp. 1440." (1983)

because of its purpose, which is to fund government activities and goals. However, under the FSIA, the purpose of sovereign debt would be disregarded. Instead, the nature of the act, which is the same as that of a corporation taking out loans or issuing bonds, would be considered. As a result, under the FSIA, sovereign debt is a commercial issue and, for this reason, sovereign states can be sued in US courts in the event of a default.

Due to the FSIA, US judges can make debt default costly by (1) forcing a country to repay all of its creditors and/or (2) by preventing a country from re-entering the market by issuing orders that permits creditors to seize its assets. In many ways, US judges, under the FSIA, play a similar role to that of the Law Merchant (LM) during the Middle Ages (Milgrom, North, & Weingast, 1990). With an LM, one party in a trade deal can accuse the other of cheating and file a claim, which then the LM adjudicates in an honest manner. The purpose of the LM is to settle disputes, impose sanctions, and to provide information. These are also functions that US judges provide in sovereign debt disputes. However, while Milgrom, North, and Weingast (1990) contemplate the possibility of corruption among judges, they do not consider preferences.

Preferences have a role in influencing outcomes. In his explanation for his decision to not rule in favor of Allied Bank International, Judge Griesa stated that he was concerned about US foreign policy because a ruling for the plaintiffs would suggest that the defendants—in this case, three Costa Rican state-owned banks—should have ignored the mandate of their government and pay the creditors. In other words, a ruling would violate the sovereignty of Costa Rica. Griesa specifically says that "Such an act by this court risks embarrassment to the relations between the executive branch of the United States and the government of Costa Rica."[2] While he did not rule in favor of the plaintiffs, he also chose to not rule in favor of the defendants because the sovereignty defense used was inapplicable under these circumstances. Nevertheless, the appeal court would reverse his case dismissal in favor of the plaintiffs. The US executive branch joined this litigation case as amicus curiae and stated that Judge Griesa was mistaken in his beliefs about relations between Costa Rica and the US. The judicial branch was informed that the "…United States has an interest in maintaining New York's status as one of the foremost commercial centers in the world…[creditors] may assume that, except under the

[2] "Allied Bank International v. Banco Credito Agricola, 566 F. Supp. 1440." (1983)

most extraordinary circumstances, their rights will be determined in accordance with recognized principles of contract law."[3] For this reason, the decision by Judge Griesa was changed and Allied Bank International won its case against Costa Rica. This case—one among many—highlights how sovereign debt litigation case outcomes may be influenced by factors that do not include the merits of a case.

While politics has always played a role in sovereign debt from the decision by a country to take on debt to default resolution, the regulation of sovereign debt markets has changed over time. Unlike the trade arena that has the World Trade Organization with its Dispute Settlement Body, there is no equivalent in the finance arena. In fact, international financial markets have historically lacked a formal method of regulation and instead has persisted on informal methods that rely on the role of reputation (Tomz, 2007a), banking houses such as the Rothschild's (Polanyi, 1944), or the Tate Letter. However, arguments that rely on the role of reputation or banking houses for regulation apply to a period where banks were the main actors involved in the bond market or when the US judiciary played a small role in adjudicating disputes between creditors and debtors.

These conditions no longer hold. Beginning in the late 1970s, the role of banks in sovereign lending began to steadily decline and hedge funds, through the purchasing of bonds, have since replaced them as the primary creditor. In their role as primary creditor, these non-state actors have been taking sovereign states to court. Furthermore, due to the changed international environment, some of these hedge funds are referred to as "vulture funds" because they purposely purchase bonds after a default to sue a country in a US court for the pre-default price of the bond. Most importantly, with the passing of the FSIA, the US judiciary provides a more formal method of regulating debt markets than was available in the past. For this reason, it is necessary to consider how decisions are being made. What influences who wins? Are the rules as they are laid out in the FSIA being followed?

Although the FSIA was implemented to depoliticize sovereign litigation, I argue that politics remained in the process via judicial ideology. Judicial ideology, however, acts as a moderator to the characteristics of a sovereign state. Specifically, there are two characteristics of a defendant

[3] "Allied Bank International v. Banco Credito Agricola, 757 F.2d 516." (1985)

country that influences outcomes—close economic ties with the US and a democratic form of government. First, economic ties between the defendant and the US in the trade arena make it more likely for a judge to rule against the defendant. If the US is in a trade competition relationship—the degree to which two countries trade the same products—with the defendant country, a judge is more likely to rule against the defendant out of concern that a broken contract in the sovereign debt arena will spillover into the trade arena, which, in turn, will lead to increased tariffs and expropriation. Second, democracies are less likely to be ruled against. This is due to international comity—a discretionary doctrine that permits a judge to dismiss a case out of respect for the sovereign state defendant—and the presence of checks and balances. The presence of multiple veto players lends credibility to the decision of the defendant to default as there may have been veto players against the decision to default such that political costs are likely to materialize. As it appears that a default in a democracy will only occur when it absolutely must, a judge is likely to utilize international comity to dismiss the case and permit the default decision to remain a domestic issue.

Judicial ideology acts as a moderator to these two defendant characteristics and, as a result, the difference in ruling propensity between conservative and liberal judges is most acute when the defendant country has close economic ties with the US and a democratic form of government. Conservative judges are more likely to rule against the debtor state (the defendant) because they exercise judicial restraint, defined as not departing from a doctrine or law, in relation to economic issues. Conservative judges have more judicial restraint in regards to economic issues than liberal judges because of the institutional persistence of protecting business interests. Countries that are in trade competition with the US are those who engage in intra-industry trade and these are typically democracies. Although democracies have better property rights and rule of law, these factors do not mitigate the importance of protecting business interests and practicing judicial restraint in relation to economic issues for conservative judges.

While upholding the FSIA outweighs the regime characteristics of the defendant country for conservative judges, liberal judges will extend international comity to democratic regimes even if the defendant is in a trade competition with the US. This is because liberal judges are least likely to practice judicial restraint on economic issues as they are not pro-business like conservatives,

so they are more likely to be judicial activists and deviate from the FSIA. For this reason, the greatest difference in ruling propensity between conservative and liberal judges should be seen among defendants who are democracies as democracies engage in the most intra-industry trade. Between conservative and liberal judges, it is conservative judges who would feel most strongly about protecting the interests of US investors. As a result, conservative judges are more likely to rule in favor of the plaintiff to protect business interests than liberal judges.

I support this argument with two quantitative approaches. First, as the data is hierarchical in nature with defendant, plaintiff, and judge level variables, I use Bayesian hierarchical modeling to examine what influences the outcome of a case. Second, I exploit the quasi-random assignment of judges to cases to attain the overall and subgroup treatment effect of a case being assigned to a conservative or liberal judge. I do this by utilizing Virtual Twins, which is a predictive method that combines machine learning and causal inference.

Using these approaches, I find that conservative judges are more likely to rule in favor of the plaintiff when the defendant is a democracy than liberal judges. From the Bayesian model, it is evident that the higher the trade competition a defendant country has with the United States, the more likely it is for the plaintiff to win. It is also the case that a plaintiff is less likely to win as the level of democracy in a country increases. Moreover, it also suggests that liberal and conservative judges may rule differently if the defendant is a democracy. The Virtual Twins estimation confirmed that ideology influences outcomes when the defendant is a democracy. It detected a group of democratic countries that are more likely to be ruled against if a conservative judge instead of a liberal judge oversees the case. In sum, although one would expect plaintiffs to win regularly, as the facts surrounding a sovereign debt default are hard to dispute, plaintiffs do not always win. In particular, they do not win when the defendant is a democracy and the case is assigned to a liberal judge.

3.2 The Importance of Sovereign Debt Litigation

Scholars of sovereign debt have long grappled with the question of why countries repay their debt. A prominent explanation rests on the notion of reputation. Eaton and Gersovitz (1981) put forth the argument that those who default at time t may be excluded from the debt market

in the future at $t+1$. With the assumption that exclusion from the market is permanent, the amount of credit a country can attain depends on the lenders' perception of a country's desire to not be excluded from the market. For this reason, reputation is important. Tomz (2007a) expands on Eaton and Gersovitz (1981) by examining three types of states—those who either (1) service debt in good and bad times (stalwarts), (2) service only in good times (fairweathers), or (3) default regularly when times are bad and sometimes in good times (lemons)—and how lenders use the information about these three types of states as it accumulates over time to determine borrowing rates. Lenders will lend to reliable states, so governments want to have a good reputation for repayment. Building on this reputational theory, Jerome Roos (2019) argues that there are three actors who can prevent default, but they are reliant on reputation. To prevent default there must be creditors who will sanction a defaulting country by withholding future credit and investment, conditional lending by the IMF, and political and business elites within the debtor state who advocate for debt repayment. Although reputation is critical to understanding the politics of sovereign debt, the role of US courts has been absent from this line of work.

Diverging from the reputation-based theory, Bulow and Rogoff (1989b) argue that it is not reputation, but direct sanctions via domestic courts that are the primary motivation for countries to repay their debt. This is because of the link with trade. In their theory, when a country defaults on foreign loans, conducting trade becomes difficult because (1) a country risks having assets seized by creditors awaiting payment on the defaulted bonds and (2) they will be prevented from taking on more debt—that helps fund trade and investment—until the current debt crisis is dealt with. Hence, trade will decline rapidly if there is a default that leads to a direct sanction via domestic courts. Bulow and Rogoff (1989a) qualify this argument when discussing US interests. If the debtor is a state with close trade ties to the US, then that state will not experience the negative consequences of default. Instead, it will be US citizens footing the bill for a default in a state that the US trades heavily with.

Following Bulow and Rogoff (1989a), much of the recent literature attempts to estimate the effect of sovereign debt litigation on trade. Using the legal saga of the Argentine crisis, Hébert and Schreger (2017) examine the relationship between default probability and the legal

rulings in the case of the Republic of Argentina vs. NML Capital on various trade channels. They argue that legal rulings in the case gives information to those participating in the market, which, in turn, affects the probability of default. In fact, they find that a 10% increase in default probability leads to a 6% decline in Argentine equity value. Hébert and Schreger (2017) then attempt to determine whether it is exporting firms, importing firms, or foreign-owned firms that are most negatively impacted by an increase in default probability. Their evidence suggests that foreign-owned firms, exporters, banks, and large firms are hurt more by an increase in default probability than small importing firms.

From the literature it is evident that sovereign debt may have a large impact on the economic management of a country which, in turn, affects the domestic politics of a country.[4] Yet, the politics of sovereign debt litigation is often missing from discussion, which is problematic as it reveals problems with applying the standard reputation model to understand sovereign debt politics today. Unlike in the past where creditors were large entities that coordinated with each other in the event of a default, today creditors are largely dispersed, which makes collective action to sanction a debtor state more difficult.

After the 2001 Argentine default, several hedge funds—like NML Capital—purchased the defaulted bonds and did not join the other bondholders in the 2005 and 2010 restructurings. Instead of participating in the restructurings, these hedge funds—often referred to as "Vulture Funds"[5]—sued Argentina in US courts.[6] In response to this suit, Judge Griesa issued a ruling that prevented Argentina from paying the creditors' involved in the 2005 and 2010 restructurings until the holdout creditors began to receive payments from Argentina as well. The Argentine government, headed by Cristina Fernández de Kirchner, refused to make payments to the holdout creditors despite the fact that the payments were small relative to the Argentine economy as a whole.[7] As a result of the refusal to settle with the holdout creditors, Argentina did not and

[4]See Tomz (2007a); Stasavage (2003); Van Rijckeghem and Weder (2009); Saiegh (2009); and Kohlscheen (2010) for a discussion about the domestic politics of sovereign debt in democracies and for the authoritarian case, see Ballard-Rosa (2016).

[5]Vulture funds are hedge funds that buy bonds or bank loans that a country already defaulted on and then take that country to court in hopes of gaining a large profit from the default. Vulture funds are often based in the British Virgin Islands and other tax havens.

[6]They were able to sue in US courts because the debt was denominated in US dollars and issued under New York law.

[7]This is why Hébert and Schreger (2017) believe that rulings in favor of the creditor (NML) would

could not re-enter capital markets. If Argentina attempted to re-enter the market, they ran the risk of having assets seized as Judge Griesa granted hedge funds their attachment order requests.[8]

Ongoing court cases can prevent a country from entering the market.[9] In the case of Argentina, even though they settled with creditors in two restructurings, they did not re-enter the market until 2016 when the new government—voted in on a policy platform aimed at settling with creditors and ending the legal saga—agreed to settle with all creditors. In fact, weeks after settling with creditors, Argentina issued a 16.5 billion dollar bond, which was Argentina's first issuance since the 2001 default. It was US courts that prevented Argentina from re-entering the market after its 2010 restructuring. For this reason, judicial decision-making should be examined in the sovereign debt context.

3.2.1 The US Judiciary as International Regulator and the Ensuing Puzzle

Before the 1976 FSIA, a strong enforcement device for creditors against governments was lacking.[10] The Tate Letter era was imperfect as restrictive immunity was not applied consistently by the judiciary and the State Department could become involved when requested by the defendant. Even prior to the Tate Letter, the only choice creditors had was to either accept the loss from a default, enter restructuring negotiations, or to pressure their home governments to get involved[11] because a country is not a corporation. When a government defaults it cannot be sold off to help investors recoup some of their loses. There is no liquidation. For this reason, the FSIA is a demarcation point for investors in terms of the choices they have available to them in the event a dispute arises.

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increase the likelihood of default and rulings in favor of Argentina lowered the likelihood of default.

[8] Attachment orders permits hedge funds to seize the assets of a sovereign to recoup losses.

[9] Studies have found that countries do not enter the debt market while a case is going through the court system. See Schumacher, Trebesch, and Enderlein (2021) for an excellent description of how sovereign debt litigation prevents countries from re-entering the market.

[10] The United States was the first country to codify sovereign immunity into a statute via the FSIA.

[11] Creditors could pressure their home governments—usually through lobbying—to put in place trade sanctions, initiate diplomatic negotiations, or intervene militarily. This primarily occurred in the 19th and 20th centuries. See Waibel (2011) for an explanation on how and when creditors requested their home government to intervene. Also, see Tomz (2007a) and Mitchener and Weidenmier (2010) for a discussion on the uses of gunboat diplomacy in relation to sovereign debt repayment.

However, as the FSIA is domestic legislation and not international law, US courts are not available as a dispute settlement mechanism to every investor. The FSIA permits agents to sue a foreign entity in US courts if the dispute involves any commercial activity, such as expropriations, defaults, enforcement of arbitral agreements, and maritime liens, that has substantial connection to the US. For example, a hedge fund based in any country that purchased Argentine bonds denominated in US dollars can then sue Argentina at the United States District Court for the Southern District of New York[12] if Argentina does not pay them in the event of a default. For a sovereign debt litigation case to be seen under the FSIA, the bonds must be denominated in US Dollars.

While the FSIA places limits on who can utilize US courts and under what circumstances, the FSIA does not make a distinction between the "state" and its "government". This means that a current government can be held accountable for debt issued by previous governments even if there was a transition from autocracy to democracy. Additionally, a suit against a state-owned or operated entity—such as an oil company or central bank—is considered the "state" in suits. Given that the FSIA has a broad definition of the "state" and considers sovereign debt to be a commercial issue, sovereign debt litigation cases should be straightforward. A country defaults and is then taken to court by those who own the debt and is seen by a judge. The judge must either rule in favor of the plaintiff (against the defendant), rule in favor of the defendant (against the plaintiff), or dismiss the case (rule in no one's favor). However, sovereign debt litigation cases are not murder mysteries. There is no question over whether a country stopped payments and it is easy to confirm that the debt holders are indeed debt holders. In fact, governments have never attempted to dispute the occurrence of a default.[13] For this reason, states (defendants) should be losing all cases.

Shortly after its enactment, the first sovereign debt litigation cases arrived from the 1980s Latin American debt crisis. One case that came out of this crisis was CIBC vs. Banco Central

[12] As bonds are issued under New York Law it is the First Circuit Southern District of New York that hears these cases.

[13] They have tried to close suits by disputing (a) whether they are the originators of the debt, (b) whether they truly own the state operated oil company, or (c) by attempting to activate the Odious Debt Doctrine—a legal theory that a state should not be held accountable for debt taken on by an illegitimate or despotic regime—in their defense. See Gelpern (2005) for a discussion on attempts to implement the Odious Debt Doctrine.

do Brasil, which was brought to the court in 1995. This was the first case brought by a vulture fund. A vulture fund is a hedge fund that purposely purchases debt after a default when the debt is the cheapest to then take a country to court to sue them for its original worth.[14] CIBC had purchased $1.4 billion of Brazil's debt on the secondary market. Instead of participating in the restructurings, this hedge fund chose to take Brazil to court. Ultimately, Judge Barbara S. Jones chose to dismiss the case. A dismissed case is not necessarily a negative event for a country because it means that there is no court order to pay the creditor in the dispute, but if they wish to, that option is still available for the country. In the case of CIBC vs. Banco Central do Brasil, Brazil chose to settle with CIBC out-of-court despite the dismissal.

In a similar vein to that of the emergence of vulture funds, hedge funds have developed a new courtroom strategy beginning in the late 1990s. Hedge funds have attempted to utilize pari passu clauses that are often included in bond contracts to establish that all creditors will be treated equally in the event of a default. However, pari passu is often applied in corporate debt default cases because when corporations default there is often a liquidation and, therefore, the creditors involved want the goods divided in a manner they deem appropriate. As discussed, liquidation does not occur when a government defaults, which is why the application and interpretation of pari passu when applied to sovereign debt litigation has been highly contested.

The first sovereign debt litigation case to use pari passu is Elliot Associates vs. Republic of Peru in 1996. In this case, Elliot Associates argued that Peru cannot legally pay the creditors they settled with through restructuring negotiations due to the principle of pari passu. Judge Robert Sweet agreed with this interpretation of pari passu. In response to this court ruling, Peru chose to immediately settle with Elliot Associates—paid approximately $56 million—rather than default on all of their bonds. Although several other hedge funds after Elliot Associates have attempted to use pari passu, all were unsuccessful until the recent case of Argentina.

These case anecdotes highlight a puzzling occurrence—plaintiffs do not always win. In CIBC vs. Banco Central do Brasil, it was clear that Brazil did default, and that CIBC did own

[14]CIBC was a hedge fund that the Dart family was involved in. The Dart family owns the Dart Container Corporation, which is the largest producer of foam products such as cups and plates. They also own Dart Management, which is a vulture fund— that has made a considerable profit from the financial crises in Argentina and Greece.

Brazilian debt, yet the judge dismissed the case. After the strategic and successful use of pari passu by Elliot Associates in its case against Peru, the majority of those who came after using the same strategy failed. Despite the expectation for plaintiffs to win these straightforward cases, they are, in fact, not regularly winning.

3.3 The Argument and Hypotheses

What affects the decisions judges make? I argue that the ideological inclinations of judges affect their decisions. However, judicial ideology acts as a moderator to two defendant characteristics that influence outcomes. Similar to other issue areas (e.g., Alesina & La Ferrara (2014); Choi, Harris, & Shen-Bayh (2022)), the characteristics of the defendant can influence the outcome of a case. When the defendant is a sovereign state being sued over an economic event in US courts, one important characteristic is the economic relations the defendant has with the US. Economic ties between the defendant and the US in the trade arena increases the probability that the plaintiff creditor will win. This is due to the concern that a broken contract in one area of the economy will lead to broken contracts in other areas. Cole and Kehoe (1998) argue that the reputation of a government in the sovereign debt arena will affect other areas where interaction is dependent on trust. The potential for a negative spillover is particularly acute between the finance and trade arenas as trade is an area that is dependent on trust.[15] Hence, if a debtor state breaks their contract with creditors by defaulting, that government would be viewed as untrustworthy. This, in turn, would cause concern that the debtor state will then break contracts in the trade arena by implementing tariffs, non-tariff barriers, and expropriating.[16] Most simply put, a broken contract signals that a country has unstable economic policy.

The concern over a potential spillover from a broken contract in the sovereign debt arena into the trade arena should be more pronounced in countries where there is already existing

[15] In fact, Mansfield and Reinhardt (2008) have found that agreements can help reduce volatility in trade policy and trade flows.

[16] Tomz and Wright (2008) examine the link between the different types of sovereign theft—debt default and expropriation—and conclude that more research needs to be done on how the honoring of contracts in one arena will lessen the occurrence of another form of theft.

trade competition. Trade competition here is defined as "…the extent to which two countries trade similar products with the same partners" (Kim, Liao, & Imai, 2020). Trade competition is not just about exports, but imports as well because with the growth of global supply chains, countries must also compete for inputs that permit them to produce the final product (e.g., raw materials, machinery parts, etc.). Due to the growth and characteristics of intra-industry trade, a country's greatest trade competitor is often the country that it also exports a significant amount to. Some of these exports being intermediate goods that are later used to produced final goods. For this reason, economic policy stability in these countries is important for the US. As similar products are being imported and exported, and firms are becoming increasingly reliant on global value chains, the importance of trade liberalization and policy stability has grown for the US government.[17]

To prevent spillover and send a signal that broken contracts will not be tolerated, I expect US judges to be more likely to rule in favor of the plaintiff in sovereign debt litigation cases where the US is in a trade competition with the defendant. This is because the US wants to ensure that the country it has economic ties with maintains a favorable investment climate. A ruling in favor of the plaintiff sends a signal to the defendant that a contract breach will not be ignored even in the adjacent sovereign debt arena.[18] The higher the trade competition is with the US, the more likely for the defendant to lose a sovereign debt litigation case because the impact of spillover in these countries would be more severe.

> H1: On average, the higher the trade competition with the United States, the more likely it is for a judge to rule in favor of the plaintiff.

While the extent of trade ties with the US is one important defendant characteristic, another

[17] In Song Kim (2017) finds that most political lobbying by firms for trade liberalization in the US is within industry.

[18] My theory argues the opposite from the theory put forth by Bulow and Rogoff (1989a) who argue that in countries where US trade interests are most acute, court sanctions against a defaulting government does not occur, and, therefore, it is US citizens who would be footing the bill for a default rather than the defaulter. In my theory, that takes intra-industry instead of inter-industry trade into account, the debtor state must pay back its debt because it would hurt US investors.

characteristic of significance is the regime type of the defendant. Democratic regimes have an advantage in sovereign debt litigation cases just as they have advantages when entering the sovereign bond market. The idea that democracies have an advantage in the sovereign debt arena began with North and Weingast (1989). They argued that due to the checks and balances, democracies are less likely to repudiate debt and, for this reason, sovereign bonds issued by democracies are desirable and come with lower interest rates. Since North and Weingast (1989), scholars have found that democracies have better access to the bond market and receive better bond ratings than comparable authoritarian regimes (Beaulieu, Cox, & Saiegh, 2012). Furthermore, Biglaiser and Staats (2012) find that the regime characteristics that influence credit ratings positively is the presence of strong courts, the rule of law, and property rights.[19]

The institutional features of democracy work alongside the doctrine of international comity, which helps democracies gain an advantage in court. International comity[20] is a discretionary doctrine that permits a judge to dismiss a case out of respect for foreign sovereigns.[21] While the FSIA has clearly defined terms and guidelines regarding its application, there is nothing preventing a judge from utilizing an international norm.[22] If international comity is applied to a sovereign debt litigation case, it is saying that the US judiciary respects the decision of that particular debtor state to default. Comity is typically applied unless it violates "…some fundamental principal of justice, some prevalent conception of morals, [or] some deep-rooted tradition of the common weal."[23] In other words, comity should be applied in all cases except where it hurts the common good or public policy. However, as this is a norm and not legislation, there are no guidelines as to how to determine what is in the common good, so judges will use international comity when they see fit.

A US judge will be more likely to defer to the decisions of a democracy more so than an

[19] Also see Biglaiser and Staats (2010) for information on why firms are attracted to democracies with strong courts and adherence to rule of law.

[20] As defined by the Supreme Court, international comity is "the recognition which one nation allows within its territory to the legislative, executive, or judicial acts of another nation…" ("Hilton v. Guyot, 159 U.S. 113, 164," 1895)

[21] See Estreicher and Lee (2020)

[22] The Act of State doctrine itself is not utilized as it is actual law, but due to the clarity of the FSIA, a judge knows when each should be applied.

[23] "Fannie F. Loucks et al., as Administrators of the Estate of Everetta, 224 N.Y. 99" (1918)

authoritarian regime. This is due to the presence of checks and balances. The presence of multiple veto players should curb the ability of an executive to pass statutes (Tsebelis, 1995) that veer far from principles of justice. Utilizing international comity to dismiss a case when the defendant is a democracy occurs because the motives for default appear to be more legitimate than when it occurs within an authoritarian regime. A default damages both current and future financial opportunities, so there is likely to be veto players within a democracy that oppose it, which means that a default may lead to negative political consequences. Regimes with fewer veto players tend to default more frequently than those with a greater number (Borensztein & Panizza, 2009; Saiegh, 2009; Van Rijckeghem & Weder, 2009). Due to the nature of authoritarian regimes, the presence of checks and balances is difficult to discern. Hence, from the perspective of a judge, a default in a democracy will only occur when it absolutely must, which is why they are likely to dismiss the case and permit the default decision to remain a domestic issue by using international comity. The more democratic a country is, the less likely it is for a judge to rule against them.

> H2: On average, the more democratic a country is, the less likely for a judge to rule in favor of the plaintiff.

Judicial ideology acts as a moderator to these two defendant characteristics and, as a result, the difference in ruling propensity between conservative and liberal judges is most acute when the defendant country has close economic ties with the US and a democratic form of government. This is because democracies tend to attract the most intra-industry trade (Madeira, 2014) due to their ability to enforce written contracts (Nunn, 2007).[24] Therefore, there is a group of countries that are in a trade competition relationship with the United States that are also democracies. As such, there is a tension between protecting business interests and ruling in favor of democracies. For this reason, ideological inclinations matter most in these cases as judges are not mechanical decision-makers, but often decide cases based on their ideology. Studies have

[24]See Nunn (2007) for an explanation of why contract enforcement is a comparative advantage in trade relationships.

found judicial decision-making to be influenced by ideology (Epstein, Landes, & Posner, 2013; Segal & Spaeth, 2002; Sunstein, Schkade, Ellman, & Sawicki, 2006) and it can outweigh other factors (Martin, Quinn, Ruger, & Kim, 2004). Ideology is important because US presidents are likely to nominate individuals that they believe are like themselves and, as such, vacant seats in the judiciary is an opportunity for a president to have a lasting effect on the judicial branch. The political affiliation of the president who nominated a judge is often a strong indicator of how that judge will rule (Cohen & Yang, 2019; Pinello, 1999). With Republican presidents nominating conservative judges and presidents affiliated with the Democratic party nominating liberal judges. As presidents nominate judges that they believe have similar beliefs to their own, a left-right divide on sovereign debt is likely.[25] A liberal position on economic issues among the judiciary would be pro-union, anti-business, or pro-consumer (Bonica & Sen, 2021) and the conservative one anti-union, pro-business, or anti-consumer.

Conservative judges are more likely to exercise judicial restraint when a suit is over commercial issues. When a judge practices judicial restraint, it means that they do not deviate from a written doctrine or law. Conservative judges are more likely than liberal judges to practice judicial restraint because of institutional persistence. From 1875-1891, the Republican Party increased the power and jurisdiction of federal courts by giving them dominance over interstate commerce. The purpose of doing so was to aid businesses as federal courts were in a position to monitor regulation attempts by state and national authorities. The expansion of the purview of the federal court meant that neither the state nor the national government could in the future overstep its reach (Gillman, 2002). Following the expansion of the federal court to protect business interests, Republicans have continued passing various acts to support their constituency.[26] For example, the Taft-Hartley Act of 1947, which restricts the power of labor

[25]Left-right divides have been found in advanced industrial countries on issues such as free-trade with left-wing parties advocating for more protectionist policies than right-wing parties (Milner & Judkins, 2004). For example, in the United States, after 1970, Republicans increasingly became for free trade due to support from export-oriented business and agricultural interests and Democrats more protectionist as unions gained strength (Karol, 2000). In fact, most of the votes Clinton received for the passing of NAFTA in 1993 came from Republicans.

[26]Even when the Republican and Democratic parties switched platforms with Democrats becoming the party of big government and the Republican party one favoring the curbing of federal power, the expanded power of the court remained, and conservative judges continued to be the most likely to practice judicial restraint to aid business interests.

unions, was passed by a Republican dominated Congress over the veto of President Harry S. Truman. The Republican party is a pro-business party and the judges nominated by Republican presidents are likely to be pro-business as well. By expanding the power of the federal courts over commerce and appointing conservative judges, the Republican party created institutional persistence of judicial restraint among conservative judges on issues relating to the economy. As such, in relation to economic issues, conservative judges are most likely to practice judicial restraint. As a result, although democracies have better property rights and rule of law, these factors do not mitigate the importance of free trade and stable economic policy for conservative judges or make them any less likely to practice judicial restraint.

Conservative judges are more likely to rule against a defendant (in favor of the plaintiff) irrelevant of regime type. By ruling against a country, the conservative judge is upholding the FSIA, supporting businesses who export and import from abroad, and sends a signal that bonds issued in US dollars have value for investors because they will get paid even in the event of a default. As many countries issue bonds in and fix their currency to the US dollar, the United States has an interest in the stability of the global financial market and in the financial stability of countries that its domestic constituents make investments in and trade with. This is why in the case of Allied Bank International vs. Costa Rica, the US government stated concern over maintaining the status of New York as the commercial capital of the world. With rulings in favor of the plaintiff, conservative judges are practicing judicial restraint, protecting the reputation of the US as a leader of the financial system, and supporting economic openness as investors have confidence that their investments have some protection.

Liberal judges, unlike conservatives, do not practice judicial restraint on economic issues, but in fact can be labeled judicial activists. A judicial activist is one that deviates from a baseline that is deemed to be correct (Kmiec, 2004, p. 1475). Although what is considered judicial activism can be subjective, in some cases, as it is under the FSIA, judicial activism occurs when clear rules are defied. Conservatives are more willing to stick closely to the guidelines provided by the FSIA to aid business interests. However, liberals do not prioritize business interests to the same extent. Liberals will intervene in the economy to create and aid social welfare programs. Whereas republicans are likely to pass acts that aid businesses, democrats focus more on health

policy, the environment, and consumer protection (Farhang, 2008). Upholding the FSIA is not a priority for liberal judges. As a result, liberal judges are more likely to defer to the decisions of a democracy to default and keep the default choice a domestic issue due to their propensity to be judicial activists. Subsequently, liberal and conservative judges rule differently when the defendant is a democracy, but similarly when the defendant is an autocracy.

> H3: Conservative judges are more likely to rule against a defendant that is a democracy than liberal judges.

3.4 A New Data Set on Judicial Decision-Making

To assess the history of sovereign debt litigation since the enactment of the FSIA in 1976, I have constructed a new data set that covers the period from when the FSIA was put into force to March 2022. In order to obtain a representative sample of sovereign debt litigation, cases are collected from the United States District Court for the Southern District of New York (SDNY). As US dollar denominated sovereign bonds are issued under New York law, lawsuits are seen in the SDNY. Sovereign states choose to issue bonds under New York law rather than under their own domestic law because investors are unlikely to buy those bonds because the country is deemed untrustworthy.[27] As bonds issued in US dollars provide some protection, investors are more willing to purchase these bonds. Of course, not all sovereign debt suits involve bonds issued in US dollars. There are also bank loans and trade credits that comprise sovereign debt lawsuits, but these are highly likely to end up in the SDNY as contracts typically include clauses that indicate disputes should be taken to New York. In the event that a sovereign debt case is taken to a court other than the SDNY, the court that received the suit typically has the case moved to the SDNY. Although there is no formal regulation requiring judges outside of the SDNY to move a sovereign debt case to the SDNY, this is the norm.[28] As a result, there is no room for forum shopping within the US judicial system as either the sovereign debt is in the form of a bond, the contract includes a clause that it be seen in New York, or a case is moved

[27] This is typically referred to as "Original Sin" in the sovereign debt literature.
[28] Confirmed in interviews with lawyers who have worked these cases.

to the SDNY as it is seen as the appropriate forum. Hence, by focusing on the SDNY, the data set collected is representative. Moreover, trade credits make up an exceptionally small portion of the debt portfolio of a sovereign state and sovereign bank lending decreased drastically after the 1980s debt crises, so the majority of sovereign debt is in bonds.[29]

This data set was acquired by performing a web-scrape of the Public Access to Court Electronic Records (PACER) website, which was then double checked by running a search for cases in NexisUni.[30] Once the relevant cases were acquired, the documents were scraped for information such as the Docket Number, case name, the plaintiffs involved (i.e., bank, hedge fund, individual), the judge assigned, amount of money demanded by the plaintiffs, amount of money awarded by the judge, start and end date of a case, the nature of the case, and the judge's decision. I added information on attachment requests, the granting of an attachment, the type of debt the lawsuit is over, and who nominated each judge and their party affiliation after the scrape.

The resulting data set is at the docket[31] unit level. This means that there are multiple observations per country-year for some countries. I identify 405 sovereign debt litigation cases brought to the SDNY. Of these 405 cases, 74 are bank loans, 279 are bonds, and 52 are over trade credits. This is the most comprehensive and up-to-date data set on this issue. Table 1 provides an overview of the data on judges in the data set and Table 2 provides an overview of the case and plaintiff information.

[29] This of course excludes debt where the creditor is the IMF, World Bank, etc.
[30] Please see the Appendix 6.2 for the steps taken to collect the data.
[31] A docket number is the number assigned to each individual case in US courts.

Table 1: The Data By Judicial Characteristics - A Selection of Cases

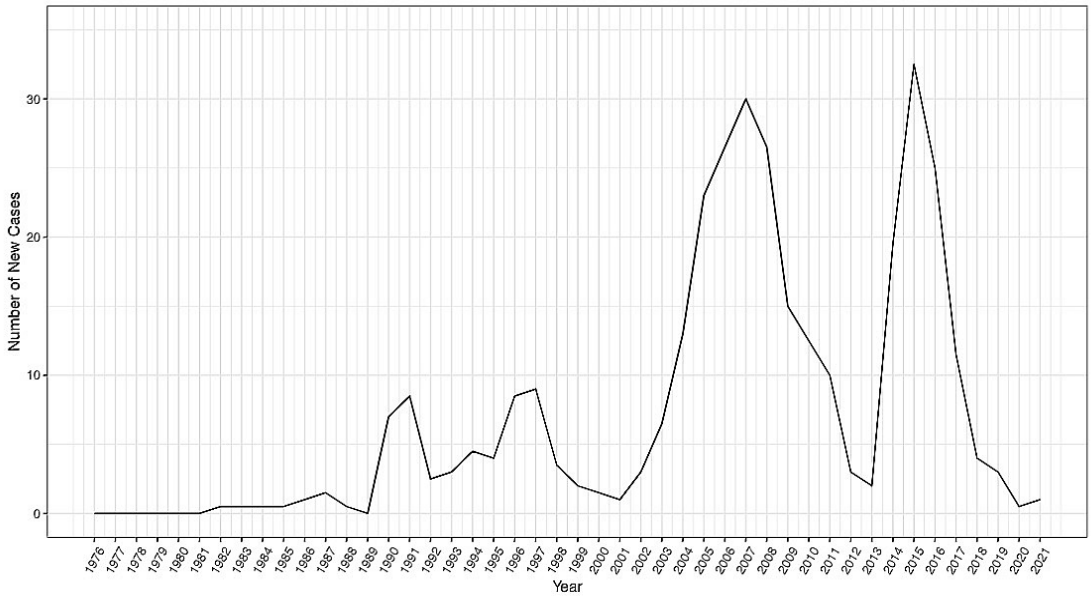
Docket Number	Country	Start Year	Judge	Party	President
1:84-cv-08101-JSM	Nigeria	1984	John S. Martin	Republican	George H.W. Bush
1:90-cv-06639-DNE	Liberia	1990	David N. Edelstein	Democrat	Harry Truman
1:86-cv-09935-MJL	Bolivia	1986	Mary Johnson Lowe	Democrat	Jimmy Carter
1:90-cv-03651-RPP	Peru	1990	Robert P. Patterson	Republican	Herbert Hoover
1:94-cv-04733-BSJ	Brazil	1994	Barbara S. Jones	Democrat	Bill Clinton
1:96-cv-06360-JFK-RLE	Nicaragua	1996	John F. Keenan	Republican	Ronald Reagan
1:96-cv-06586-MGC	Iraq	1996	Miriam Goldman Cedarbaum	Republican	Ronald Reagan
1:14-cv-09844-KBF	Ecuador	2014	Katherine B. Forrest	Democrat	Barack Obama
1:15-cv-00725-RJS	Ecuador	2015	Richard J. Sullivan	Republican	George W. Bush
1:08-cv-00164-LAP	Argentina	2008	Thomas P. Griesa	Republican	Richard Nixon
1:15-cv-05551-DAB	Peru	2015	Deborah A. Batts	Democrat	Bill Clinton
1:14-cv-08242-LAP	Argentina	2014	Loretta A. Preska	Republican	George H.W. Bush

Table 2: The Data By Plaintiff Characteristics - A Selection of Cases

Docket Number	Country	End Year	Plaintiff	Plaintiff Type
1:91-cv-06500-LBS	Iraq	1992	The Commercial Bank of Kuwait	Bank
1:96-cv-07034-SS	Zambia	1997	Camdex International, Ltd.	Hedge Fund
1:96-cv-05849-KMW	Iraq	1998	Commodity Credit Corporation	Hedge Fund
1:02-cv-01246-JSM	Liberia	2002	FH International Financial Services, Inc.; SIFIDA Investment Company, S.A.; Wall Capital, Ltd.; Hamsah Investments, Ltd.	Hedge Fund
1:06-cv-03976-LAP	Argentina	2007	Andres Jacinto Alzugaray; Maria Cristina Aste	Individual
1:15-cv-00725-RJS	Ecuador	2016	Daniel Penades	Individual
1:15-cv-09630-KPF	Central African Republic	2017	The Export-Import Bank of The Republic of China	Bank

As with any sanctioning device, there is a question about how often it is used. Figure 3.1 plots the number of new cases brought to court since 1976. Of course, how much US courts are used for sovereign debt litigation is driven by the number of defaults per year and the size of a default.[32] Hence, there are peaks and valleys in the number of *new* cases brought each year. Nevertheless, as presented in Figure 3.1 below, it appears that US courts are being used in an attempt to sanction debtor states.

Figure 3.1: New Case Initiation by Year



After bringing a suit to court, whether and the extent to which a country is sanctioned is dependent on the ruling by the judge appointed to the case. District court judges are initially randomly assigned to a case. Currently, the SDNY has forty-two judges, which means that if a new case were brought to the court today, random selection would occur among these forty-two individual judges. However, judges are only initially randomly assigned, which means that if there are multiple cases against the same defendant, it is likely, but not guaranteed that it

[32]See Schumacher, Trebesch, and Enderlein (2021) for an examination of the factors that drive creditors to court.

will be assigned to the same judge. For example, Judge Griesa was initially randomly assigned to an Argentine sovereign debt litigation case in 2002. As more Argentine cases were brought forward, they were all assigned to Judge Griesa until his death in 2017. Hence, in the data set, Griesa is listed as the deciding judge in all cases brought against Argentina in the 2002-2017 period. There is, however, no guarantee of this, so plaintiffs cannot act strategically by bringing cases after they have seen a similar case won by a plaintiff. Moreover, there is still randomization between countries and default episodes. Sovereign debt cases are not the sole responsibility of one judge. Given the potential influence of a judge on the outcome of a case,

Table 3: Number of Judges involved in Sovereign Debt Litigation by President

President	Number of Judges
Barack Obama	5
Bill Clinton	19
George H.W. Bush	3
George W. Bush	4
Gerald Ford	2
Harry Truman	2
Herbert Hoover	1
Jimmy Carter	3
John F. Kennedy	2
Lyndon B. Johnson	1
Richard Nixon	8
Ronald Reagan	8

how diverse is the population of judges that have been involved in past sovereign debt litigation cases? Table 3 above presents the number of unique judges involved in sovereign debt litigation by President. There are a total of 58 different judges nominated by 12 US Presidents that were involved in the 405 cases present in the data set. As can be expected, there are very few judges nominated from the Gerald Ford (1974-77), Lyndon B. Johnson (1963 – 1969), Harry Truman (1945-53), and Herbert Hoover (1929-33) presidencies in the data set because of factors such as (a) when the president held office and (b) the number of judicial vacancies during a president's term. For instance, 52 district court judges were nominated and appointed during the Ford presidency which is much lower than the 305 district court judges nominated and appointed

during the Clinton presidency. Moreover, in addition to presidential opportunity to nominate a judge, when a president held office can contribute to the number of overall judges by president involved in sovereign debt litigation cases. Many of the judges nominated by President Hoover or Truman would either have retired or died by the time the first cases under the FSIA would have made it to the court. Nevertheless, judges that have presided over sovereign debt suits have been nominated by a variety of presidents.

Most importantly, however, is how these cases are concluded. With sovereign debt litigation cases, there are multiple ways in which a case may be closed. The primary division is between cases decided by a judge and those closed by other actors. There are three ways in which a judge can close a case: (1) they can rule in favor of the Plaintiff, (2) they can rule in favor of the Defendant, or (3) they may dismiss the case without having to rule in anyone's favor. Outside of a judge's control, there are four other methods of case closure: (a) the US put a freeze on all cases that involve assets of a country,[33] (b) the case is closed administratively Pursuant to Memorandum From the Administrative Office of the United States Courts,[34] (c) the case closed before reaching a judge, and (d) out-of-court settlement. Out-of-court settlement is the most common reason for case closure outside of a judge's purview. A case is coded as being closed due to an out-of-court settlement when the court document states that there is an "order of dismissal on consent" or that it was dismissed Pursuant to Rule 41(a). For example, in Greylock Global Distressed Debt Master Fund Ltd. et al v. The Republic of Argentina where the outcome was a voluntary out-of-court settlement, the document states the following:

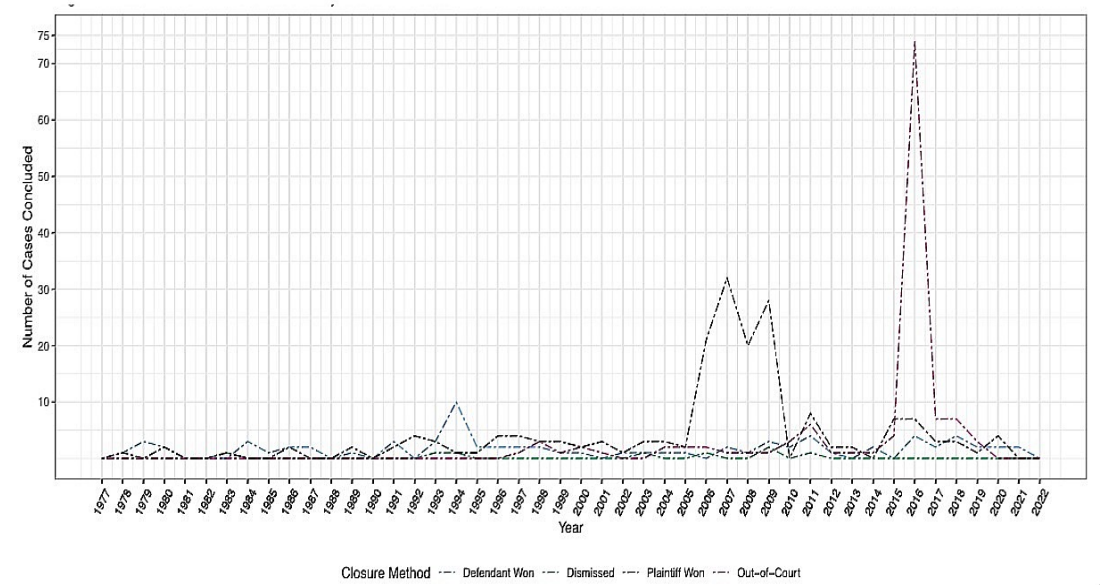
[33]This happened with Iraq for a very brief time period.
[34]This effectively means putting a case on hold.

> STIPULATION AND ORDER OF DISMISSAL: Pursuant to Rule 41(a) of the Federal Rules of Civil Procedure, Plaintiffs Greylock Global Distressed Debt Master Fund, Ltd. and Greylock Global Opportunity Master Fund, Ltd. (together, "Plaintiffs") and Defendant The Republic of Argentina, by and through their respective undersigned counsel of record, hereby stipulate that all claims of the Plaintiffs in this proceeding are hereby dismissed with prejudice, with each party to bear its own attorneys' fees and costs. The Republic of Argentina terminated. (Signed by Judge Thomas P. Griesa on 12/5/2016)

How are most cases concluded? Figure 3.2 below presents the number of cases closed by method and year. Only the most common closure methods are presented, which are the three options available to a judge and out-of-court settlement. The other case closure methods occur irregularly and rarely, so they are not represented in the figure below.[35] In Figure 3.2, there are two large peaks in the data. The first peak is that of plaintiffs winning cases brought against Argentina under Judge Griesa. The second peak occurs in 2016 after Mauricio Macri—who ran on a platform that prioritized ending the legal saga with creditors—was elected President of Argentina. Once Macri was elected, creditors settled out-of-court as the Argentine government was now more willing to negotiate. Excluding these two peaks, there does not appear to be any case closure option that occurs more regularly than all others.

[35] Only 11 cases were closed by other means. The cited 405 observations already excluded these 11.

Figure 3.2: Total Number of Closed Cases by Method and Year



Data and Empirical Analysis

Variables

Sovereign debt litigation involves the choices and decisions of three actors: the Judge, the Plaintiff, and the Defendant. Variables for each actor are used in the statistical analysis. Theoretically, I expect conservative and liberal judges to rule differently. As a proxy for the ideology of a judge, I use the partisan affiliation of the president who nominated them with Republicans considered as conservative and Democrats as liberals. While a simple measure, multiple studies have shown that it is a robust proxy indicator (Cohen & Yang, 2019; Pinello, 1999). REPUBLICAN NOMINATED is a binary variable that takes on a value of "1" if the judge was nominated by a Republican and "0" if by a Democrat.

For the plaintiff level variables, I use an indicator variable for whether an attachment request was made or not. Attachments requests are important because if granted by the judge, it means that the creditor in that case can legally seize the defendant's property to recoup their losses from

the default. Most importantly, however, a plaintiff that requests an attachment may be more aggressive than one that did not, which may sway the outcome of a case. If a plaintiff requests an attachment, ATTACHMENT ATTEMPT is coded as "1" and "0" otherwise. Another plaintiff level variable I use is a binary variable for whether a plaintiff is a hedge fund or not.[36] HEDGE FUND takes on the value of "1" if plaintiff is a hedge fund and "0" otherwise. This variable is included because hedge funds are known for using tactics to win suits that other plaintiffs are not known for implementing, which may influence outcomes.

For the defendant level variables, I include REGIME TYPE$_{-1}$, which is lagged variable obtained from the Varieties of Democracy (V-dem) data set. I use the liberal democracy index from V-dem because this measure focuses on the strength of the rule of law, the independence of the judiciary, and the constraints on the executive (Coppedge et al., 2022). The liberal democracy index is constructed such that the values range from 0 to 1 with 1 being the most democratic. Additionally, IMF PROGRAM$_{-1}$ is included as an indicator of the general economic climate in the country and is coded as "1" if the defendant was participating in an IMF program the year before or during a case and "0" otherwise. In addition to the other defendant level variables I include INVESTMENT PROFILE$_{-1}$ that is obtained from the PRS group ICRG database and is lagged by a year in the analysis. The measure is based on a survey of investors about how concerned they are about the risk for contract viability/expropriation, profits repatriation, and payment delays. Values range from 0 to 12 with 12 being low risk and 0 high risk. This variable needs to be included because the investment policies of individual countries may a) increase or decrease the amount invested in a country and b) determine the behavior of defendants during a trial. Also included is TYPE ECONOMIC, which is a variable that indicates the type of sovereign debt—either Bank, Bond, or Trade Credit—the suit is over. Moreover, an additional lagged control variable included is DEFAULT AMOUNT$_{-1}$. This variable covers all types of sovereign debt, and it is a continuous variable as it takes into account how much of the debt was defaulted on. It is included because the extent of a country's default may affect its willingness

[36] In the raw data set, plaintiffs come in many forms which include individuals, banks, hedge funds, mixed coalition (For some cases, individuals, banks, and hedge funds, may jointly bring a suit.), and a city. Note that there is only one city (City of New Rochelle in New York) that has brought a case against a country (Liberia).

to settle with creditors during restructuring negotiations before being taken to court, and it may also impact the number of cases that end up in court. To construct this variable, I downloaded public and publicly guaranteed external debt data on arrears and debt serviced from the World Bank's Debtor Reporting System. The DEFAULT AMOUNT$_{-1}$ variable is calculated as $\frac{Arrears}{Debt\ Due}$. While it is possible that there is under reporting in the Word Bank data, it is more comprehensive than a binary variable that indicates the start and end of a default.

The key variable of interest at the defendant level is TRADE COMPETITION$_{-1}$, which is lagged by a year. This measure was attained from Kim, Liao, and Imai (2020) who use a dynamic clustering method to measure the degree of competition between two countries. Kim, Liao, and Imai (2020) provide measures of trade competition from a 3, 7, and 15-cluster model. The more clusters there are, the more refined the data is.[37] Due to my theory, I chose to use the data resulting from the 15-cluster model because it is most representative of intra-industry trade. Trade competition is a proxy for US economic interests towards the defendant country. Of course, this measure does not reveal whether the executive branch is representing a coalition of interests that may or may not include investors that engage in intra-industry trade with that particular defendant or simply an agent of a particular set of actors. This is simply a measure of economic relations between the United States and the defendant country.

As I am interested in the outcomes of these cases, my dependent variable—CREDITOR WIN—is a binary measure that takes on a value of "1" if the plaintiff won and "0" otherwise.[38] This dependent variable is appropriate for several reasons. First, a case that was dismissed by a judge is a positive outcome for the defendant because they are not *legally* responsible for paying creditors back. Case dismissal rarely occurs due to lack of evidence or questions relating to the merit of the case. Second, out-of-court settlements occur once the debtor is willing to negotiate.[39] A judge has no say in the outcome of those negotiations just as a judge has no control over whether a defendant chooses to settle with a creditor after they win. Therefore,

[37] For example, with a 15-cluster model the data would be clustered by whether it is a fuji or gala apple, but with fewer clusters trade competition is between apples and bananas.

[38] This means that cases that were dismissed and out-of-court settlements are coded as "0".

[39] A debtor state could become willing to negotiate either because of a change in government and/or repetitive losses. For example, out-of-court settlements in the Argentine case occurred after Judge Griesa made multiple decisions against Argentina and a new Argentine president who was less hostile towards the idea of settling with creditors was elected.

out-of-court settlements are most substantively similar to a case dismissal.

3.5 Empirical Analysis

To answer the question of what affects the decisions judges make, I use two empirical tests. For the first test, I use probit Bayesian hierarchical modeling to attain an overall picture of what influences sovereign debt litigation outcomes. The second test applies Virtual Twins, which is a method that first creates a counterfactual where the judge is a liberal rather than a conservative (or vice versa) and then identifies a subgroup of observations where being assigned to a conservative judge has an impact. Nevertheless, the primary problem with analyzing sovereign debt litigation is self-selection into the arbitration process. That is, plaintiffs are likely to bring a case to court if they believe they can win and make a profit. Although I am interested in what happens after the selection process, the selection process itself may influence outcomes. If plaintiffs are only bringing cases that they believe they can win, then, in conjunction with the expectation that most cases should be won by plaintiffs because the facts are difficult to dispute, plaintiffs should not be losing any case. In other words, this self-selection is biased against the theory that variation exists in the outcome due to various economic and political factors. However, despite the potential for self-selection into arbitration and the indisputable facts of a sovereign default, the data suggest, as presented in Figure 3.2, that plaintiffs do not always win. Therefore, this implies that politics has a role to play in sovereign debt litigation cases.

3.5.1 Bayesian Hierarchical Model: Evaluating the Landscape

The nature of the data—repeated measures from the same country, nominating president, and judge—lends itself to hierarchical modeling. For this analysis, I use a probit hierarchical model with country, nominating president, and judge random effects. The priors used in this analysis are vague.[40] In addition to using Bayesian hierarchical modeling, I also manage the missing data by imputing the data using MCMC. There is missing data because the sovereign

[40]Specifically, I used (.01, .01) for the precision and (0, .01) for the mean. This allows the model to rely on the data for estimation.

debt litigation data is available until 2022, but the independent variables from other sources in this analysis, such as TRADE COMPETITION$_{-1}$ and INVESTMENT PROFILE$_{-1}$, are unavailable through 2022. For this reason, I consider the missingness in this situation as missing completely at random (MCAR). As the missing data is continuous, I draw from the normal distribution.

The table below presents the results, which, in addition to the mean and SD, includes the lower and upper bound of the 95% credible interval.[41] Furthermore, the Monte Carlo standard error of the mean (MCerr) is included and is an indicator of how much error is in the estimate from using the MCMC method. The closer the MCerr is to zero the better and this typically occurs as number of iterations in the analysis increases. Also included is the the potential scale-reduction factor of the Gelman-Rubin statistic (psrf) also known as the R-hat. The Gelman-Rubin statistic examines whether the between variance and within chain variances are equal. The rule of thumb is that everything below 1.1 is acceptable and the closer to 1 the value is the better. Larger values means that there is a large difference between the chains. Lastly, I include Bayesian p-value's (P>0), which is a test of the direction of the effect.[42]

The main variables of interest in this analysis are TRADE COMPETITION$_{-1}$, REGIME TYPE$_{-1}$, and the interaction between REPUBLICAN NOMINATED and REGIME TYPE$_{-1}$. From my theory, I expect TRADE COMPETITION$_{-1}$ to be in the positive direction, REGIME TYPE$_{-1}$ to be in the negative direction, and the interaction between REPUBLICAN NOMINATED and REGIME TYPE$_{-1}$ to be in the positive direction. The results from a probit hierarchical model with country, president, and judge random effects are presented in Table 4.

The mean of the TRADE COMPETITION$_{-1}$ variable is in the positive direction and the probability that it is in the positive direction is near 1.0, which supports Hypothesis 1. The higher the trade competition is with the United States, the more likely it is for the defendant to lose the case. The REGIME TYPE$_{-1}$ variable is in the negative direction and the probability of this coefficient being in the positive direction is close to 0. This means that the plaintiff is less likely to win as the level of democracy increases in the defendant country, which supports

[41] Calculated using the highest posterior density interval.

[42] The closer to 1 this value is, the more likely it is for the direction of the coefficient to be positive.

Table 4: Bayesian Hierarchical Model: Factors Influencing Litigation Outcome

	Dependent variable: Creditor Win						
	Mean	SD	Lower95	Upper95	P>0	MCerr	psrf
Intercept	-3.43	1.36	-6.12	-0.81	0.01	0.03	1.00
Trade Competition$_{-1}$	0.14	0.07	0.01	0.26	0.98	0.00	1.00
Republican Nominated	-0.83	1.47	-3.73	2.02	0.29	0.03	1.00
Regime Type$_{-1}$	-3.83	1.84	-7.46	-0.27	0.01	0.03	1.00
Republican Nominated*Regime Type$_{-1}$	1.77	2.12	-2.51	5.88	0.80	0.04	1.00
Hedge Fund	-0.59	0.20	-0.98	-0.19	0.00	0.00	1.00
Attachment Attempt	2.39	0.53	1.39	3.44	1.00	0.00	1.00
IMF Program$_{-1}$	-1.32	0.59	-2.46	-0.16	0.01	0.00	1.00
Investment Profile$_{-1}$	0.44	0.13	0.19	0.69	1.00	0.00	1.00
Type Economic	-0.94	0.34	-1.63	-0.30	0.00	0.00	1.00
Default Amount$_{-1}$	4.57	0.56	3.47	5.68	1.00	0.00	1.00

Note:

Presented are the results from a Bayesian probit hierarchical model with country, president, and judge random effects. The dependent variable is Creditor Win.

Hypothesis 2. REPUBLICAN NOMINATED*REGIME TYPE$_{-1}$ is in the positive direction and the probability that it is in the positive direction is .80. While the probability that it is in the positive direction is not 1.0, it does lend support to Hypothesis 3 as there does appear to be some division between liberal and conservative judges. The MCerr is near zero for all the independent variables. For all variables, the Gelman-Rubin statistic (psrf) is near 1.

Overall, the results from this model lend support to Hypothesis 1, 2, and 3.[43] To further examine the relationship between judge assignment and litigation outcome, I use a method that identifies subgroups[44] to examine whether there would be a difference in outcome if a case was assigned to a judge with a different ideological leaning.

[43]However, there are limitations to using Bayesian hierarchical modeling. Due to the size of the data set, it is unfeasible to include additional and more complex interactions into the analysis to further examine Hypothesis 3.

[44]It should be noted that subgroup identification and interactions are not perfect substitutes for each other.

3.5.2 Virtual Twins

Virtual Twins (VT)[45] combines machine learning and causal inference by utilizing Random Forests (RF) and Regression Trees. The main purpose of this method is to identify subgroups that have an enhanced treatment effect. In other words, some subgroups may benefit (or be harmed) more from a treatment than other groups. It is particularly useful in cases where the overall treatment effect is small or insignificant, but there may be a subgroup where the treatment is particularly harmful or beneficial. The VT method uses the same concepts from counter-factual models and can be easily applied to studies that have a binary or continuous dependent variable.

The first step in implementing VT is to utilize RF, which is a method that outputs average predictions. Under VT with a binary dependent variable, for each observation, there are two potential outcomes with only one of these outcomes observed in the data. VT implements a random forest to predict the probability of an outcome occurring for each individual observation and, therefore, creates a counter-factual. This is done by first by utilizing RF to regress Y_i on the pre-treatment covariates of interest (X_i) and the observed treatment (T_i) and then re-estimating RF where the treatment is changed to $1 - T_i$. Hence, for each observation, VT outputs two predicted probabilities—the treatment ($\hat{P}_{1i}$) and control "twins" ($\hat{P}_{0i}$)—that each individual observation will have an outcome of "1". To obtain the individual treatment effects, which is the difference between an individual observation, outcome when receiving a treatment versus not, the difference between the treatment and control "twins" is taken for each observation i. This is defined as $Z_i = \hat{P}_{1i} - \hat{P}_{0i}$.

After Z_i is obtained, the second step is to create a regression tree with Z.[46] With a regression tree, the data is split based on the independent variable that reduces the heterogeneity in the dependent variable—here being Z—the most. In this manner, the most important independent variables are selected. The goal is to obtain covariates that are strongly correlated with Z, which are then used to define a region A that contains the observations where the treatment effect is greater than the average effect for the whole sample. When applying the regression

[45] For more information on VT, see Foster, Taylor, & Ruberg (2011)

[46] A classification tree could also be used.

tree, Z becomes the dependent variable and covariates X.[47] From the regression tree, values of Z_i is predicted for each observation. Then, using a pre-defined threshold c, the predicted values of Z_i are used to define a region $\hat{A}$. The observations that are greater than c are included in $\hat{A}$. The formula below is used to obtain a measure of the enhanced treatment effect in the subgroup region $\hat{A}$. It is important to note that $\hat{Q}\hat{A}$ is the difference between the estimated treatment effect within the subgroup and the estimated overall treatment effect.

$$Q(A) = (P(Y = 1|T = 1, X\epsilon A) - P(Y = 1|T = 0, X\epsilon A)) - (P(Y = 1|T = 1) - P(Y = 1|T = 0))$$

In this analysis, I define threshold c as $\delta + 0.1$ where δ is the overall mean treatment effect. Subgroups that have an enhanced treatment effect are those that are 10% greater than the overall mean. To obtain an estimate of $\hat{Q}(\hat{A})$, I use the re-substitution method (RM), which uses the original data, and the simulate new data (bootstrapping) approach. With RM, $P(Y = 1|T = 1\ , X\epsilon\hat{A})$, $P(Y = 1|T = 0\ , X\epsilon\hat{A})$, $P(Y = 1|T = 1)$, and $P(Y = 1|T = 0)$ are estimated from the data and substituted into the equation for $Q(A)$. RM is likely to suffer from bias and over-fitting. To mitigate this, I use parametric bootstrapping. Bootstrapping will lead to less bias and over-fitting of the model.

When applying VT, I continue to use CREDITOR WIN as the dependent variable. For the pre-treatment variables, the same independent variables from the Bayesian analysis are used. I use REPUBLICAN NOMINATED as the treatment. This means that a conservative judge presiding over a case is the treatment. As discussed, US judges are initially randomly selected to preside over a case. However, when there are repeated cases brought against the same plaintiff, often, but not always, the same judge will be assigned to all the cases (Macfarlane, 2014). Judge assignment may be quasi-random. This is not only the case with sovereign debt litigation, but with all issue areas. It is not, however, a guarantee that the same judge will preside over cases brought against the same plaintiff. A potential plaintiff cannot be certain that they will receive the same judge as a plaintiff who just won a case against the same defendant. As a result, a plaintiff initiating a suit because they are certain they will receive a particular judge is unlikely.

[47] With the Classification Tree a binary variable from Z must be created. Any value greater than threshold c is coded as "1" and "0" otherwise.

Unlike other methods, with VT it is not possible to use random effects or easily take into account that there are repeated observations by country or judge. This is an issue because there may be some concern that Argentina is driving results as Argentina's 2001 default was the largest in history and, for this reason, it received an unprecedented amount of suits brought against it. Not only are there repeated observations for Argentina, but Judge Griesa was assigned to the majority of these cases. I address the potential of the Argentine cases driving the results by collapsing the repeated Argentina observations into fewer observations based on the year a case ended and who won the case. This means, for example, the 19 cases against Argentina that ended in 2008 and where the plaintiff won the case, was collapsed into a single observation.[48] While this is an imperfect solution, it does minimize the likelihood that Argentina is driving results either due to the characteristics of the country or judge assignment. As a result, the concern that there is selection into a suit by a plaintiff in expectation that they will receive a particular judge is also minimized as in the data set this possibility is only of concern in the case of Argentina.[49]

For this analysis, I dealt with the missing data by using Multivariate Imputation by Chained Equations[50] and to obtain the standard errors, VT with 2000 bootstraps was applied. The complexity parameter (CP) for the regression trees is set to .10. This number was chosen after allowing the trees to fully grow and then choosing a CP where the 10-fold cross-validated error flattens out, which is the smallest tree size that is within one standard error of the minimum.[51] The treatment effects and regression tree are presented in Table 5 and Figure 3.3 below, respec-

[48] In Appendix 6.2, I estimate the model on the full data set with the inclusion of a binary variable—ARGENTINA—that takes on a value of "1" if Argentina was the defendant and another estimation where Argentina is completely removed. The results hold across samples. Of course, in the sample where Argentina is removed, significance is lost because the analysis is under powered.

[49] In future iterations of this project, VT will be extended to account for repeat observations that is typically seen in the social sciences.

[50] I used the MICE package in R. After creating the multiple data sets, I combined all of them by taking the mean. While it is recommended to pool results from an estimation after using MICE rather than combining all of the data sets, I chose to do the latter as there is currently no method to combine results from multiple regression forests. This is an aspect that will be addressed in the extension of VT. However, I do not believe this impacts the results as I take the mean from a large sample of imputed data sets.

[51] Also, when using multiple imputation with VT, it is best to be conservative and not let the tree grow out too much. Saying less is more in this case. This is another issue that will be addressed in the extension of VT for the social sciences.

tively. As presented in Table 5, the difference between conservative and liberal judges, across

Table 5: Virtual Twins Results

	Estimate	SE	Lower CI	Upper CI	P-Value
Subgroup Treatment - RM	0.201	0.098	0.009	0.392	0.040
Subgroup Treatment - Bootstrapped	0.136	0.065	0.010	0.263	0.035
Overall Treatment	0.087	0.072	-0.053	0.227	0.222

Note: Presented are the treatment effects from the Virtual Twins estimation. With the re-substitution method (RM), probabilities are estimated from the data and substituted into the equation for Q(A). In contrast, for Subgroup Treatment - Bootstrapped a parametric bootstrap approach is used. The dependant variable is Creditor Win. The treatment variable is the Republican Nominated variable. 'Overall' is the treatment effect for the entire population. The RM and bootstrapped subgroup treatment effects are for the identified subgroup, which are located on the right hand side of Figure 3.3.

the whole sample, is small and insignificant in the VT model. The overall treatment effect is .087 and the p-value is .22. While the overall treatment effect is insignificant, Hypothesis 3 is supported by this model[52] because there is a subgroup that is more greatly affected by being assigned a conservative judge. The RM subgroup estimate is .20 and it is statistically significant at the 5% level of significance. The bootstrapped subgroup estimate is .14 and it is statistically significant with a p-value of .035. These results suggests that for a subgroup of defendants, as shown in Figure 3.3 this subgroup is more democratic countries, conservative judges are more likely to rule in favor of a plaintiff than a liberal judge.

The regression tree visually confirms the results from Table 5 that there is a subgroup of countries where judge assignment is important (Hypothesis 3). To detect heterogeneous treatment effects, a regression tree selects independent variables that cause the greatest decrease in heterogeneity in the dependent variable. The data here are split into subgroups by the REGIME TYPE$_{-1}$ variable.[53] REGIME TYPE$_{-1}$ is the variable that explains the outcome in sovereign debt litigation the most according to this model as it is the root node. This does not mean that the other variables are irrelevant. The infliction point is at .407. For context, within this sample, REGIME TYPE$_{-1}$ has a minimum of .0260, a mean of .3768, and a maximum of .8050. The split is between countries that have some form of checks and balances, an independent

[52]Hypotheses 1 and 2 are not tested in this analysis.

[53]The regression trees in Appendix 6.2 are nearly identical to this one and identifies the same subgroup.

judiciary, and the presence of the rule of law, and those that do not.

In the regression tree, the rectangles present the final subgroups and in each rectangle the

Figure 3.3: Regression Tree Results from Virtual Twins

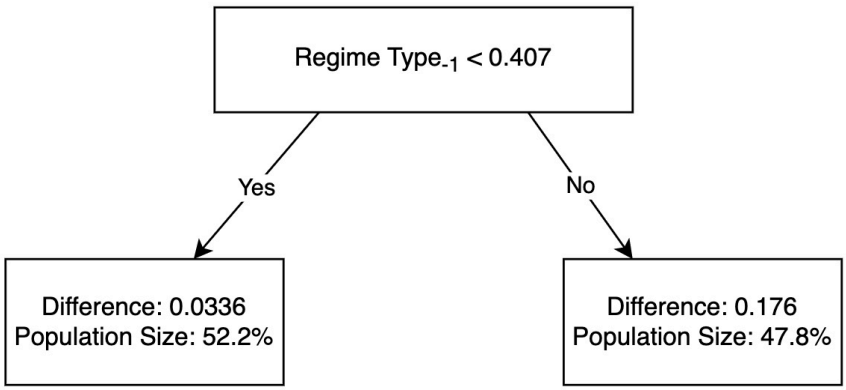


Figure 3.3 presents the estimated regression tree from VT. Each box contains the population size of each category and the mean estimated *individual* differential treatment effect, which is the difference for an individual observation between being assigned a liberal vs. conservative judge. This is not the overall subgroup differential treatment effect, which is presented in Table 5. However, the overall subgroup differential treatment effect is estimated from the right hand side outcome (the "no" branch). This figure says that the difference in case outcome is greatest when a conservative rather than a liberal judge is assigned to country that has at least some democratic features (i.e., has a score of .407 or greater from the V-dem measure).

percentage of the sample size of the corresponding subgroup and the mean estimated individual differential treatment effect, which is the difference between an individual's outcome when receiving a treatment versus not, are included. The individual differential treatment effect is not $\hat{Q}(\hat{A})$. $\hat{Q}(\hat{A})$ is the overall subgroup differential treatment effect, which is presented in Table 5. The subgroup that $\hat{Q}(\hat{A})$ estimates is the farthest to the right. The branch that is placed by VT farthest to the right is the one that is determined to be most impacted by treatment.

In the terminal node defined by REGIME TYPE$_{-1} < .407$, on the right-hand side, the mean estimated individual differential treatment effect[54] is 0.176. This node accounts for 47.8% of the whole study population. The subgroup that is most affected by being assigned to a conservative

[54]i.e., the difference in probabilities of the treatment and control "twins".

judge are those who have a value of REGIME TYPE$_{-1}$ above .407, which are the more democratic regimes. In contrast, the more authoritarian regimes are unlikely to be affected by judge assignment. In the terminal node defined by REGIME TYPE$_{-1} < .407$ on the left-hand side, which are the more authoritarian countries, the mean estimated individual differential treatment effect is 0.0336. This node accounts for 52.2% of the whole study population. Overall, this analysis suggests that liberal and conservative rule similarly when the defendant is autocratic, but ruling propensity diverges when the defendant is a democracy.

3.6 Discussion

Despite the expectation for plaintiffs to win regularly, they do not. What affects the decisions judges make? I argued that the ideological inclinations of judges may influence outcomes. However, the difference in ruling propensity between liberal and conservative judges is most acute when the defendant is a democracy because of their economic ties with the United States. Economic ties with the United States are an important defendant characteristic because of the general concern that if a country violates a debt contract, there is a chance that they will breach contracts in other economic arenas as well. The potential threat of spillover is most acute where there are already existing trade relations between the US and the defendant. To assess the relationship between economic ties and litigation outcome, Hypothesis 1 examined whether higher levels of trade competition with the United States, increased the probability of a judge to rule in favor of the creditor. The results from Table 4 suggest that as TRADE COMPETITION$_{-1}$ increases, the probability of the creditor winning a case also increases. While this finding does not address the ideological inclinations of judges in decision-making, it establishes that there is a link between sovereign debt and the adjacent trade arena.

Another defendant level variable I focus on is regime type. I argued that a US judge will be more likely to defer to the decisions of a democracy more so than an authoritarian regime because of the presence of checks and balances. Defaults are ultimately a decision made by domestic actors and it is often a costly one. Theoretically, the more veto players there are, the less likely it is for default to occur unless it is absolutely needed as there is likely a group of actors who are against defaulting. The decision to default is more credible coming from a regime

with multiple veto players than those with fewer. As such, as democracies tend to have more veto players than autocracies, a judge is more likely to invoke international comity when the defendant is a democracy. While the FSIA is clear enough that a judge knows when to apply the FSIA, legislation cannot prevent a judge from applying an international norm. At the core of international comity is the notion that the judiciary should respect the decisions of a sovereign state regarding internal matters. When that internal matter is the decision to default, whether a judge chooses to utilize international comity is dependent on how legitimate the decision to default appears. Since democracies are more likely to have multiple veto players, the judiciary are more likely to respect the decision to default from democracies than autocracies. For this reason, I expected a judge to utilize international comity and not rule in favor of the plaintiff (creditor) if the defendant is a democracy. In the Bayesian hierarchical model, it was found that as the level of democracy increases, it became less likely for creditors to win, which lends support to Hypothesis 2. Democracies have an advantage in the sovereign debt arena that autocracies do not have.

In conjunction with these two defendant characteristics, judicial ideology influences outcomes. Conservative judges are more likely to rule against the debtor state (the defendant) because they exercise judicial restraint when a suit is over a commercial issue. They practice judicial restraint in their interpretation of the FSIA due to institutional persistence as Republicans specifically expanded the reach of federal courts to regulate commerce such that neither the state nor federal government oversteps boundaries as delineated by law. On economic issues, conservatives have always been pro-business. In contrast, liberal judges do not practice judicial restraint on economic issues because they are not pro-business to the same extent as conservatives and are more likely to intervene in the economy to create and aid social welfare programs. As a result, I expected conservative judges to be more likely than liberals to rule in favor of the creditor as they practice judicial restraint on economic issues and a ruling in favor of the plaintiff protects business interests.

However, as democracies also engage in intra-industry trade, I argued that the difference in ruling propensity between conservative and liberal judges will be among this subgroup of countries. Democracies attract more intra-industry trade because intra-industry trade is reliant

on the ability of the host country to enforce written contracts, which is more likely to occur in a democracy than autocracy. As conservative judges practice judicial constraint on economic issues, they are more likely to rule against a democracy than a liberal judge due to the degree of trade competition with these countries. In turn, liberal judges are less likely to rule against a democracy, even though trade competition is likely to be high with the US, because they are more likely to be judicial activists on economic issues. Ideological inclinations should be more pronounced when the defendant is a democratic country as conservative judges are likely to rule against them and liberal judges in the defendants favor as they are likely to extend international comity to democracies. The interaction between REPUBLICAN NOMINATED and REGIME TYPE$_{-1}$ in Table 4 is in the positive direction. This suggests that when a conservative judge rather than a liberal judge is assigned to a case where the defendant is a democracy, the creditor is more likely to win.

To further examine the role of judicial ideology as a moderator, I used VT with REPUBLICAN NOMINATED as the treatment variable and found that the greatest difference between conservative and liberal judges occurs among defendants who are democracies. This supports the results from the Bayesian model. There is a subgroup of countries where the ideology of a judge who is assigned to a case can change outcomes. Overall, differences along ideological lines are most visible when the defendant is a democracy due to their involvement in international trade and their institutional features. Conservative and liberal judges tend to rule most similarly when the defendant is an autocracy, but are more likely to rule differently when the defendant is a democracy.

3.7 Conclusion

In 1976, the United States enacted the FSIA, which permitted actors to sue a foreign entity in US courts. This marked a milestone in US foreign policy as it removed interference from the State Department and gave judges clarity on when restrictive rather than absolute sovereignty is applied. Since this enactment, hedge funds have increasingly gone to the SDNY to bring cases against countries that have defaulted. These lawsuits can have a debilitating effect on the defendant country by wreaking havoc on the domestic economy through shrinking

employment opportunities and price increases in necessities like food. For this reason, the goal of this paper was to understand who wins and who loses sovereign debt litigation cases. What affects the decisions judges make? At face value, the answer is obvious. Creditors should be regularly winning cases because the evidence is clear—it is not possible to deny the occurrence of a default—and plaintiffs are likely to bring cases that they believe will win in court. However, this is not what occurs in practice. Plaintiffs do not win every case brought to the SDNY.

I demonstrate that the ideological inclinations of judges can explain case outcomes. However, these ideological inclinations work in conjunction with the characteristics of the defendant. One important defendant characteristic is trade competition with the United States. Defendants that have close economic ties with the United States are more likely to be ruled against. With a default, there is the risk that a country will also break contracts in other areas of the economy, which could hurt US investors. Hence, to send a signal that behavior that hurts investors will not go unnoticed, judges will rule against the defendant. Being ruled against by a judge is more likely to happen when a country is in a trade competition relationship with the US as this indicates a country is engaging in intra-industry trade, which is heavily reliant on contracts. A second important characteristic is the regime type of the defendant country. Democracies are less likely to be ruled against than authoritarian regimes because the decision to default appears to be more legitimate due to institutional constraints in democracies.

Furthermore, since it is democracies that attract the most intra-industry trade, it is these group of countries where the difference between conservative and liberal judges are most stark. Liberal judges are more likely to be judicial activists and rule in favor of a democratic defendant despite the FSIA because of their preference for individual rights over business interests. Taking into account the institutions present in a democracy, a liberal judge is more likely to view the decision to default by a democracy as legitimate and, as such, extend international comity and permit the decision to default to remain a domestic issue. Conservative judges, however, practice judicial restraint on economic issues and are more likely to support business interests. As a result, they are more likely to rule in favor of the plaintiff even when the defendant is a democracy because democracies are involved in the most intra-industry trade. Despite expectations, outcomes to sovereign debt litigation cases vary.

There are policy and normative implications for the lack of impartiality in sovereign debt litigation cases. The most glaring issue is that state sovereignty is being infringed upon by US judges. While most countries that are involved in the global economy have lost some sovereignty, that is a choice. A country chooses to go to the IMF in exchange for loans. With the FSIA, it is non-state actors that are dragging a sovereign state to court. Once at court, a judge can enact measures that force the hands of a state to pay all its creditors, including the vulture hedge funds. The concern is that vulture funds will continue to take advantage of a state in distress and make economic crises worse.

What are the implications of these rulings? In the shadow of a looming debt crisis due to COVID-19, the lack of rules or guidelines to manage vulture funds is problematic. When a conservative judge rules in favor of a creditor that is a vulture fund, they are rewarding unscrupulous behavior and, therefore, could encourage such behavior. It is possible that US judges are exacerbating economic conditions within a country. However, in spite of the violation of absolute sovereignty and the predatory behavior of vulture funds, US judges could be potentially good for economic development as well. A ruling against the defendant and for the plaintiff could reassure investors such that they do not flee a country during an economic crisis. As a consequence, countries that are ruled against may experience quicker economic recovery than those that escaped a negative ruling either due to being a democracy or not having strong economic ties with the United States. While a ruling in the favor of the defendant may benefit politicians in the short-term because their hands are not forced, there may be economic benefits for the defendant if they are ruled against.

Chapter 4

Information Clearinghouse: Market Implications of US Judicial Decisions

Abstract: The Foreign Sovereign Immunities Act (FSIA) was created to give US courts the power to decide commercial disputes between a sovereign state and a non-state actor who is typically based outside that state. As US courts now make decisions on issues involving the economic policies of other sovereign states, particularly regarding debt, it is important to consider their impact. What impact, if any, does a court ruling have on the debt market and the economy of a debtor state? I argue that judicial decisions by US courts can affect the market because a ruling against the defendant debtor state increases investor confidence to reinvest in a country, creating positive unintended consequences for the debtor state. The judge sends the following information to investors by ruling in favor of the lender-plaintiff: (1) the action of the debtor state was illegitimate, (2) claims made by the creditor are valid, (3) actions to enforce the ruling are acceptable, and (4) given (1) - (3) it may be possible to recoup losses after a default. As a result, investors may be more willing to return to a country shortly after default when a judge rules in favor of the lender. Although a country's leader would not want to lose a sovereign debt litigation case as it may require them to repay the debt in full, losing a case may lead to unintended positive benefits for the country in the medium term. If a ruling in favor of the lender lowers perceived risk for investors, then there are three possible implications. First, the cost of borrowing should decrease for the debtor country. By ruling in favor of the plaintiff, a judge not only creates the expectation of full repayment for investors holding defaulted bonds but also boosts investor confidence in bonds that are not in default, as the FSIA becomes a viable tool for investors if needed. Second, the import of intermediate goods should increase. Firms that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and closely monitor the economic climate. Although these firms typically have multiple venues to choose from to settle a dispute, receiving a favorable court ruling from a US judge during a sovereign default episode reassures firms that (a) the economy may turn around and (b) US courts may be a viable option if needed. Third, a debtor state that defaults and receives an unfavorable court ruling is more likely to experience economic growth afterward. Lower borrowing costs can enable a country to service its current debt and invest in public infrastructure that attracts foreign direct investment. Furthermore, an increase in the importation of intermediate goods can have a multiplier effect on the economy, creating jobs and contributing to further growth. These implications are tested quantitatively using original data on FSIA sovereign debt court rulings.

> "New York law is so widely utilized in global finance that it is no exaggeration to characterize it as an international public utility. It applies in a large proportion of outstanding stock of foreign law-governed sovereign bonds, followed by English law…The reach of the Court of Appeals' decision is so wide that it may also impact creditors whose bonds are not governed by New York law…This decision may also impact official bilateral loans contracted by a sovereign if it has a mix of bond, bank and official bilateral borrowing—as do many sovereigns." – (Republic of France, 2014) (Amicus Curiae Brief in Support of Argentina)

4.1 Introduction

On the outskirts of Buenos Aires, protesters held up anti US Judge Griesa signs in front of the factory of U.S. automotive supplier Lear Corporation for laying off its workers. Jorge Capitanich - Chief of the Cabinet of Ministers in Argentina - would refer to Judge Griesa as a US imperialist (Otaola & Lough, 2014). This early August layoff and comment from a government official came shortly after Argentina defaulted on their debt in July 2014 following a drawn-out saga with Judge Griesa over the repayment of Argentine sovereign bonds that culminated in a Supreme Court ruling against Argentina. The June 16th 2014 Supreme Court decision sent shockwaves throughout the international financial community by ruling that plaintiffs (creditors) can use a subpoena to gain information from banks about the assets of a country even if those assets are not located within the United States. Dubbed the "Trial of the Century" by financial pundits, this ruling strengthened creditors rights under the Foreign Sovereign Immunities Act (FSIA). Additionally, the Supreme Court also ruled that Argentina must honor the terms to their bond agreements, which include the pari passu clause that requires equal treatment among creditors.[1] For Argentina, this meant that they must pay all creditors or default on all of them. In an act of defiance, Argentina chose to default.

While the Argentine government and its citizens linked US judicial decisions to the lackluster state of the economy, practitioners and academics were divided on the role and impact of US courts. Prior to the 2014 Supreme Court rulings, some scholars argued that a problem with the debt market is that the rights of creditors are too weak, which leads to regular defaults by sovereign states (Shleifer, 2003). As such, US courts may present a potential solution by

[1] Pari Passu clauses are included in nearly all bond agreements issued under New York or English law.

increasing the rights of creditors. However, during the Argentine trial in the Supreme Court, a slew of amicus curiae briefs were received that argued for a ruling in favor of Argentina. For example, Stiglitz (2014) and countries such as France, Mexico, and Brazil, argued that if the Supreme Court ruled against Argentina, it would give creditors too much power and, therefore, it would damage the market and harm developing countries. It would do so by increasing the length of time a country is in default and, at the same time, minimizing the attractiveness of default to the extent that leaders choose to remain in economic distress rather than negotiate with creditors to increase fiscal space (Republic of France, 2014; Stiglitz, 2014). Nevertheless, despite the disagreement about the effects of the FSIA, little is known about when or whether the FSIA has any impact on the market and, in turn, the economies of debtor states.

Courts are recognized for providing two related functions. First, they are responsible for deciding over contentious issues. Second, courts are information providers. In their capacity as information providers, they send signals about the validity of legal claims made by the plaintiff and the legitimacy of the defendants' actions. Viewing courts as information providers is nothing new. For example, Milgrom et al. (1990) discuss how the Law Merchant (LM) during the Middle Ages settled disputes, imposed sanctions, and provided information, which enabled enforcement among a large community of traders. With the establishment of the FSIA, US courts can fill these two roles by deciding over sovereign debt disputes and providing information about whether the plaintiffs claims were valid. Of course, of concern is what happens after a court decides over a contentious issue and provides information because courts themselves cannot enforce a ruling.

In the domestic politics setting, enforcement typically occurs via policy changes where the ruling of a court places constraints on the legislative branch (Stephenson (2004); Rogers & Vanberg (2002)). Courts do not dictate what legislation is passed, but they limit the policy options available. International courts, such as the WTO and the International Criminal Court, may play a similar role. For instance, the WTO has the capability of sending information about the legality of the trade policies of a government to the international community. With such information, other governments can adjust their own policies and various industry groups can lobby their government to change policy (Rosendorff (2005); Mansfield, Milner, & Rosendorff (2002)). Although a court may not have enforcement mechanisms, sharing information can lead

to the development of shared expectations on how actors may informally enforce a ruling from an international institution (Weingast (1997); Milgrom et al. (1990); Keohane (1986)).

This question about the ability to enforce a ruling by a court is complicated under the FSIA. The FSIA was passed to give creditors and investors a rule-based mechanism to express grievances and have them resolved in US courts. As such, domestic courts within the US are responsible for making decisions that have implications for international actors. It is this feature that distinguishes it from domestic courts limiting the domestic policy space of the legislative branch and from international institutions regulating the actions of sovereign states. The FSIA is not an international law, but US domestic legislation that seeks to govern the actions of international actors. However, just like an international institution, by sending information regarding the validity of the plaintiff's claims, it can lead to the development of shared expectations and norms among non-state actors about how to sanction a country after a judge rules in favor of a plaintiff.

Securities laws can be likened to the FSIA in that they are also domestic regulations aimed at governing entities that operate beyond the confines of a single state. Securities legislation requires a company to register with a domestic agency, such as the SEC in the United States, if it wants to sell stocks. The company must provide all information related to the security being sold to an investor. Porta, Lopez-De-Silanes, & Shleifer (2006) examined the effect of securities laws on stock market development and find that the enforcement of securities laws does not matter. What matters is the presence of extensive legislation that requires disclosure by sellers and has rules delineating how investors may recoup losses if a seller is dishonest. Research on securities laws suggests that domestic legislation can change the behavior of investors and permit a country to develop a large market even if enforcement is lacking.

Of importance, however, is the willingness of the domestic court itself to apply existing legislation. Putnam (2009) suggests that US courts are willing to regulate private actors when their actions may damage the efficacy of US domestic legislation. I find that US judges are more likely to implement the FSIA, by ruling in favor of the plaintiff, when the defendant country is a democracy that has trade ties to the United States. Overall, there is reason to believe that a US court will not only utilize existing legislation, but also that their rulings may be enforced by the

plaintiff or even the parties not directly involved in the suit. However, unlike other legislation examined by scholars, the FSIA permits private non-state actors to sue foreign sovereign states and it is this aspect that not only makes it unique, but also potentially increases the difficulty of enforcement of rulings. This is particularly the case when a suit involving a sovereign default is brought to a US court because it has been historically difficult to force a country repay its debt.

What impact, if any, does a court ruling have on the debt market and the economy of a debtor state? I argue that judicial decisions by US courts can impact the market because a ruling against the defendant lowers the perceived risk faced by later investors, which leads to positive unintended consequences for the debtor state. If an investor believes that the FSIA will be there to help them recoup their losses via a judicial ruling against the defendant, they would be more willing to take on riskier investments. While the court itself cannot enforce its judgments, a court ruling can impose costs via third parties that they send information to through their rulings. If judgments against the debtor pursuant to the FSIA lower the perceived level of risk associated with a state that has just defaulted on a debt agreement, then three implications should arise for the defendant state.

First, the cost of borrowing should decrease for the debtor country. By ruling in favor of the plaintiff, a judge not only creates the expectation of full repayment for investors holding defaulted bonds but also boosts investor confidence in bonds that are not in default, as the FSIA becomes a viable tool for investors if needed. Second, the import of intermediate goods should increase. Firms that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and closely monitor the economic climate. Although these firms typically have multiple venues to choose from to settle a dispute, receiving a favorable court ruling from a US judge during a sovereign default episode reassures firms that (a) the economy may turn around and (b) US courts may be a viable option if needed. Third, a debtor state that defaults and receives an unfavorable court ruling is more likely to experience economic growth afterward. Lower borrowing costs can enable a country to service its current debt and invest in public infrastructure that attracts foreign direct investment. Furthermore, an increase in the importation of intermediate goods can have a multiplier effect on the economy,

creating jobs and contributing to further growth. I test these expectations using data I gathered on sovereign debt litigation cases.

4.2 Literature Review

The sovereign debt literature in IPE has long grappled with the issue of what motivates states to repay their debt and the options creditors have to punish debtor states who default. Sovereign debt research is divided between two opposing views. First, there are those that believe that sovereign defaults may create a reputation cost for the debtor. Eaton & Gersovitz (1981) put forth the argument that those who default at time t may be excluded from the debt market in the future at $t + 1$. With the assumption that exclusion from the market is permanent, the amount of credit a country can attain depends on the lenders' perception of a country's desire to not be excluded from the market. For this reason, reputation is important. Tomz (2007b) expands on Eaton & Gersovitz (1981) by examining three types of states—those that either (1) service debt in good and bad times (stalwarts), (2) service only in good times (fairweathers), or (3) default regularly when times are bad and sometimes in good times (lemons)—and how lenders use the information about these three types of states as it accumulates over time to determine borrowing rates. Lenders will lend to reliable states, so governments want to have a good reputation for repayment. It is important to note that in the pure reputational approach there is no need for courts, the IMF, or politics except to help spread information.

The second approach, which differs from the reputational approach, is the direct punishment approach. Bulow & Rogoff (1989b)[2] argue that it is not reputation, but direct sanctions via domestic courts that are the primary motivation for countries to repay their debt. This is because of the link with trade. In their theory, when a country defaults on foreign loans, conducting trade becomes difficult because (1) a country risks having assets seized by creditors awaiting payment on the defaulted bonds and (2) they will be prevented from taking on more debt—that helps fund trade and investment—until the current debt crisis is dealt with. Unlike the reputational approach, the inclusion of institutions whether it be the IMF, the courts, or

[2] Also see Bulow & Rogoff (1989a).

domestic politics becomes necessary as they serve as the means through which sanctions are announced and potentially enforced.

Within the direct punishment approach, the recent literature has attempted to examine the impact of courts. In relation to the debt arena, Schumacher et al. (2021) directly examine whether courts are able to disrupt the access countries have to the debt market. They have found that courts have a negative impact on a debtor state's access to the debt market. Access to the international debt market declines when a country is facing litigation, either because the price of issuing bonds is high or because a country runs the risk of having those bonds seized to pay off existing creditors. But in the absence of the international bond market, governments will utilize domestic credit markets while they are in court (Schumacher et al., 2021). Courts in the US appear to have some power in the international bond market.[3] Ahmed & Alfaro (2017) examine investors reactions to court rulings against Argentina using 2-day cumulative abnormal returns on Latin American sovereign EMBI bonds. They find that on average the filing of a new case increases returns, which, in turn, means that the perceived risk of sovereign default is decreased across Latin America. However, when examining just Argentina, they find that abnormal cumulative returns were negative, but when dropping Argentina from the analysis, the effect of a court filing against Argentina increased returns in other Latin American countries. According to Ahmed & Alfaro (2017), cases brought against Argentina created a positive spillover in other Latin American countries. Suggesting that investor confidence in similar countries may increase even if it decreases in the country being sued.

However, as discussed by Bulow & Rogoff (1989b), the power of the court may reach even farther and spill into other economic arenas. Using the saga of the Argentine crisis, Hébert & Schreger (2017) examine the relationship between default probability and the legal rulings in the case of the Republic of Argentina vs. NML Capital on various trade channels. They find that a 10% increase in default probability leads to a 6% decline in Argentine firm equity value. Hébert & Schreger (2017) then attempt to determine whether it is exporting firms, importing firms,

[3]Not debt specific, but Morse (2019) finds that when global performance indicators of state policy are published via intergovernmental bodies such as the Financial Action Task Force that combat money laundering, international banks will minimize resources to those states that are listed on the noncompliance list.

or foreign-owned firms that are most negatively impacted by an increase in default probability. Their evidence suggests that foreign-owned firms, exporters, banks, and large firms are hurt more by an increase in default probability than small importing firms. This previous research indicates that courts may matter, but the findings either rely on a specific country's experience during the court proceedings or focus solely on a single country, like Argentina, which encountered an exceptionally large default and was uncooperative under Kirchner's leadership.

In sum, it appears that US domestic courts can possibly reach beyond the borders of the US and have an impact on the markets of other countries. Nevertheless, there are a few problems with previous studies on this subject matter. The limitations with some of the studies that examine the impact of a court, however, is that they only examine either (a) the filing of a court case rather than the outcome of a case, (b) the impact only over a short time period, or (c) only utilize cases brought against Argentina. Thus, these studies do not clearly address whether being taken to court poses any costs on the debtor state that is significantly different from the costs of a default without a court sanction.

4.3 Argument and Hypotheses

Defaults typically, but not always, occur during episodes of economic stress because states do not have the capacity to pay either due to an increase in international interest rates or decreased government revenues. The question then becomes how to stabilize and rebuild the economy. Sometimes efforts to rebuild comes in the form of direct government intervention via a change in fiscal policy, the Central Bank intervening in some manner, or IMF involvement. It is typically the case that the stock market and the economy more generally react positively when there is a government or IMF intervention, as it may suggest a potential turnaround in economic forecasting in the future. However, government or IMF intervention are not the only options. US courts may play a similar role to these institutions. The IMF is not an institution designed to settle disputes between holders of sovereign debt and a sovereign state, so if individual debt holders—hedge funds, banks, individuals, or a company—want a formal mechanism of dispute resolution, then they would have to go to a US court. Furthermore, as most developing countries debt is issued in US dollars and/or contract terms require a dispute to be taken to a US court,

it is not in the interest in the debtor state to ignore a ruling by a US judge.

If a country were to default on its debt, what effect, if any, would a ruling made by a US court via the FSIA have on economic actors operating in a debtor state? I argue that the FSIA can reduce the risk perception of investors when a US judge rules in favor of the plaintiff in disputes against sovereign states. By reducing risk perception, it encourages investors to take on risks that they may otherwise may not have. The judge sends the following information to investors by ruling in favor of the plaintiff: (1) the action of the debtor state was illegitimate, (2) claims made by the creditor (the plaintiff) are valid, (3) actions to enforce the ruling are acceptable.

Consequently, an investor may be more inclined to revisit a country shortly after its default if a judge rules in favor of the plaintiff. This is because winning the lawsuit can create an expectation that they will not have to bear the full extent of their losses in case of a problem. While there is variation in the wording and extent of rulings, when a judge rules in favor of the plaintiff, the ruling typically states that the country is obligated to repay their creditors, and if unable or unwilling to do so, the creditors may seize assets equivalent to the amount lost. The US's prominent status in the global economy lends significant credibility to a judicial decision made by a US judge, making it highly influential among investors. As noted by a distressed assets investor, "A ruling against a country does increase confidence, but it is still the job of hedge fund or investor to recoup those losses, which sometimes requires us to seize physical assets and that is not easy to do."[4] Of course, it could be contended that the level of difficulty faced by an individual investor or hedge fund in securing payment from the government or confiscating assets should determine the extent of impact that a judicial decision has on such investors and, as a result, judicial opinions should not matter. However, the ability of an investor or hedge fund to recoup assets post-ruling is an individual level problem. Whether losses are recovered or not does not directly affect other investors.

What is important is that the judge ruled in favor of the plaintiff. A ruling in favor of an individual investor or hedge fund has an effect on all other investors, which is why it is possible for the FSIA to decrease risk perception in investors. It has an effect on investors as a collective

[4]Anonymous interview with distressed assets investor.

group because the majority of bond contracts, along with other economic agreements between a country and an investor, include a governing clause stating which jurisdiction a dispute should be taken to if a dispute arises.[5] Rulings in favor of the plaintiff send a signal that a governing clause in an agreement is more than a mere window dressing. Although an investor may not be directly involved in a particular dispute, simply recognizing that the words on paper can carry weight could help alleviate concerns. Overall, "A contract with the United States…as the jurisdiction is preferred to one without."[6] This is because investors want to keep the option of going to court since it is not a meaningless action.

If the FSIA leads to a decrease in risk perception of investors when a judge rules in favor of the plaintiff, then such rulings should be associated with (a) lower borrowing costs post-judgement for the defendant state, (b) a growth in the import of intermediate goods, and (c) eventual growth in GDP due to lower borrowing costs and increased growth of intermediate goods. First, if a judicial ruling in favor of a plaintiff decreases risk perception in the investor such that they are willing to reinvest in the country, then borrowing costs should be lower. The main cost of borrowing for sovereign states that borrow using bonds is interest rates. As the interest rate increases, so does the associated expense. However, this high interest rate is often needed by developing countries and emerging markets to attract investors because they are considered a risky investment choice. Consequently, developing countries and emerging markets must strike a balance between the desire for low borrowing expenses and the necessity of high interest rates. They achieve this by issuing a variety of bond types that can vary along a number of dimensions, but most importantly by issuing currency and maturity rates.

Typically, bonds issued in US dollars have longer maturities than domestic currency denominated bonds with the latter typically carrying a higher interest rate because of the greater risk that local currencies will lose value over time. Bonds issued in US dollars also have lower interest rates than those issued in local currency as they fall under the guise of the FSIA simply for being in US dollars. Of course, most developing countries suffer from "original sin,"

[5] In the area of sovereign bonds, these contracts are often made in a boilerplate fashion such that all contracts are quite similar to each other. Most variation is in Collective Action Clauses, which states what percentage of bondholders must agree to make a restructuring legally binding on all bondholders.

[6] Anonymous interview with distressed assets investor.

which is the inability of a developing country to issue bonds in their own currency as they are not attractive to investors. Original sin has been always an issue for developing countries and while the extent of original sin may wax and wane for a country over time, it remains an issue (Eichengreen, Hausmann, & Panizza, 2022). Having bonds denominated in a foreign currency can pose a problem for a country as they cannot unilaterally alter the terms of the agreement. This is exactly why investors prefer US dollar denominated debt – it ties the hand of the issuing country.

Although bonds issued in US dollars typically have lower interest rates than any existing corresponding local-currency debt, it does not mean that bonds denominated in US dollars do not experience fluctuations on the secondary market. Similarly to a bond denominated in the local currency or other securities, the value of dollar denominated bonds rise and fall with the economic conditions of the country. Nevertheless, while these bonds may react similarly to debt issued in local currency, it is not necessarily the case that they change to the same degree. Most research on the costs of sovereign default find that sovereign bond yields are higher after default than in tranquil times (Borensztein & Panizza, 2009; Chowdhry, 1991) and that this is even the case after there is a debt restructuring (Sturzenegger & Zettelmeyer, 2007). However, during periods of economic distress, borrowing costs are still lower with bonds issued in a foreign currency than the local currency (Chamon, Schumacher, & Trebesch, 2018). Even though some states may avoid issuing new bonds during an ongoing court case (Schumacher et al., 2021), the benefits to issuing US denominated debt outweigh the costs of autonomy for many states as the borrowing costs for them do not rise to the same extent as bonds issued in domestic currency.

I expect borrowing costs to be lowered in the event that a debtor state is taken to court and losses a case because of the confidence it gives investors. This outcome is different from what would occur if a country defaulted on US denominated bonds and was not ruled against in court. A transgression on a sovereign bond agreement via default impacts the bond market such that interest rates should increase for that debtor state, the price of the bond will decrease, and the yield will increase. However, if the FSIA does decrease the risk perception of investors, when a judge rules against the state that defaulted, then it follows that in expectation, interest rates decrease, the bond price increases, and the yield decreases. Although a single ruling may

only directly impact an individual or small group of investors, a ruling in favor of the plaintiff spills over into the perceptions of others holding bonds of that country or who are considering purchasing the bonds of the defaulted state. As any bond that is denominated in US dollars can be seen in a US court under the FSIA, a ruling in favor of the plaintiff signals that the FSIA is more than just window dressing legislation and an actual tool for investors to use. Not only is this important for investors who are considering purchasing bonds from a state that has recently defaulted but it is also important because not all defaults are complete defaults. A state can choose which creditors to default on and by how much. Meaning that it is possible for states, for example, to only default on 10% of its bondholders and not all of them at the same time. In such a scenario, an investor who is currently holding bonds of a defaulted state would be interested to know how others have fared in court in case they are defaulted on in the future.

> H1: On average, a ruling in favor of the plaintiff is likely to decrease interest rates and the bond yield.

Second, if a judicial ruling in favor of a plaintiff decreases risk perception in the investor such that they are willing to reinvest in the country, then there should be an increase in the amount of intermediate goods imported. Bonds are not the only economic area that relies on contracts. Trade has always been reliant on firm-to-firm and firm-to-country contracts, but with the growth of global value chains (GVCs), its reliance has increased. GVCs are arguably more reliant on contracts compared to more traditional forms of trade. This is because multiple countries are involved in the production of a single item, and any disruption in one location can become quite costly for a firm. In order for GVCs to thrive, an enforceable contract is required (Nunn, 2007) as there is always the concern for expropriation or some type of agreement violation.

Nevertheless, leaders in developing countries, particularly those in emerging markets, often seek to enhance their countries' integration within GVCs, as they recognize the potential for economic growth that it offers. A method that many leaders use to attract foreign direct investment, of which GVCs are one type, is to enact various domestic legislation that either allow a domestic firm or the country itself to be taken to court within the country, or offer

private property rights protections as a guard against expropriation. A country may also sign international agreements, such as bilateral investment treaties, which permit a firm to utilize an international dispute settlement mechanism, such as the International Centre for Settlement of Investment Disputes (ICSID). Between these two options, it is the international investment agreement that is the most likely to increase integration in GVCs as firms are more likely to believe these legal protections are adequate (Malesky & Milner, 2021).

Of course, in addition to the courts within a country and international agreements, there is a third option for firms that the trade literature has overlooked. When a firm signs an agreement with another firm or country, they can insert a governing clause that outlines where a dispute is to be taken given a disagreement or issue arises. In many contracts, firms select the United States, particularly if it is a firm with ties to the United States, or a European country as their jurisdiction of choice. Adding such a clause to a jurisdiction does not prevent the firm from using either ICSID or a court within the state where they are producing or sending goods. As a result, firms often engage in forum shopping. Even after receiving a favorable ruling in an international or host state court, they may seek further compliance by going to a US or European court and obtaining an additional ruling.

Businesses that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and therefore closely monitor the economic climate. This includes sovereign defaults. Trade and finance influence each other and when there is a sovereign default, there are often trade costs for the debtor state. For example, Rose (2005) finds that bilateral trade declines after debt renegotiations are concluded with trade partners and that this decline can last over a decade. Using industry-level data Borensztein & Panizza (2010), find that while defaults may be costly for export-oriented industries, the impact only lasts a brief time. While the extent of damage a sovereign default can have on overall trade is disputable and may vary, there is no doubt that there is an association between debt and trade. Typically, during a default episode, interest rates increase, consumption and output collapses, and there is a decrease in trade.

However, I argue that any spillover into the trade sector is expected to be primarily observed in the domain of imported intermediate goods, given that the cost of a breached or canceled

contract is highest in this category. As such, when a sovereign default occurs, imported intermediate goods will decrease. However, if the FSIA does decrease investor risk perception when a defendant state is ruled against in the sovereign debt arena, the amount of imported intermediate goods should increase in comparison to states that defaulted without being ruled against by a US court or were not taken to court. By ruling against the defendant in a sovereign debt litigation case, a judge is stepping in to enforce a contract. As a result, this may not only increase confidence among investors involved in the sovereign bond market, but there may be spillover into the trade arena. More precisely, it could result in enhanced trust among firms participating in GVCs as it implies that relying on the US legal system to resolve conflicts is an effective dispute resolution mechanism. Even though these firms typically have multiple venues to choose from to settle a dispute, having a US judge rule in favor of the plaintiff during a sovereign default episode reassures firms that (a) the economy may turn around and (b) that US courts may be a viable option if needed.

> H2: On average, a ruling in favor of the plaintiff is likely to increase the import of intermediate goods.

If the ruling favors the plaintiff, this may lead to a decrease in investors' perception of risk towards the debtor state that has just defaulted. Consequently, this could result in lower borrowing costs and an increase in trade, which may contribute to the debtor state experiencing an increase in economic growth. Lower borrowing costs are important for the economic stability of a country and its potential for economic growth, for numerous reasons. For example, they can help finance government projects and infrastructure development, such as road development, which could potentially attract foreign direct investment. Lower borrowing costs are beneficial for a sovereign country not only because it can take on debt at a lower cost but also because it can reduce the burden of existing debt by making it more affordable to service it. This, in turn, can free up resources for other important priorities.

While lower borrowing costs can indirectly contribute to economic growth, it is not the only factor as intermediate goods contribute to economic growth by acting as a multiplier in

the economy due to the linkages it creates between factories and sectors (Jones, 2011) that may generate jobs. Intermediate goods function in a similar manner to capital in the neoclassical growth model, where capital leads to output, which subsequently leads to more capital. Of course, with linkages comes complementarity (Hirschman, 1958). Just as intermediate goods through its linkages can act as a multiplier in the economy, the complement of this is the ability of shortages of intermediate goods to hinder the economy. Supply chain disruptions, for instance, can prevent intermediate goods from fulfilling their role as multipliers and potentially hurt the economy. For example, if a final good requires input "A" and input "B", and input "B" is produced in the country, but due to supply chain issues, input "A" is either not produced in the country or sent to the country where the final product is made, then the final good cannot be produced. In such a scenario, jobs may be lost, which hurts the economy. Supply chain disruptions are exacerbated in the event of a sovereign default because the import of intermediate goods is dependent on contracts.

Nevertheless, as discussed, ruling against a defendant in a sovereign debt case may decrease the perceived risk for an investor or firm in a country that has recently defaulted. Property rights protection has been considered the key to economic growth by social scientists since Montesquieu (1748) and Smith (1776), and democratic institutions are often associated with protecting property rights. Additionally, many believe that, on average, for a country to achieve economic growth, it must have both democratic institutions and active participation in international trade (Barro, 2003; Dollar & Kraay, 2003; Frankel & Romer, 1996). However, it is possible for US courts to either act as a substitute for domestic institutions that support private property rights protection for foreigners or in conjunction with them.

If a ruling against the defendant can potentially lower borrowing costs and increase the volume of trade, then it follows that economic growth may increase. When contract enforceability is not a severe problem, risk taking is encouraged, which leads to greater investment and, in turn, growth (Rancière, Tornell, & Westermann, 2008).[7] By ruling against the defendant country, the judge is sending a signal that it expects the contract to be honored. This gives

[7]See Rancière et al. (2008) for a discussion on how contract enforceability problems impacts borrowing costs and growth.

investors within the debt and trade arena confidence, which permits a faster return to economic normalcy in these countries. As a result, countries that defaulted who are ruled against in the court and, therefore, were held accountable, are more likely to experience economic growth than countries who defaulted but were not ruled against and those never taken to court. Signing a contractual agreement that includes a jurisdictional clause or issuing bonds in US dollars is not enough to elicit economic growth after default because there is still uncertainty over whether a judge will apply the FSIA and rule against the debtor state. By ruling against the defendant, investors perceptions about the country that just defaulted are improved.

> H3: Countries that defaulted and received a judicial ruling against them are more likely to experience higher economic growth post-ruling than those without a negative judicial ruling.

4.4 Data

To examine whether a ruling in favor of the plaintiff in US courts can reduce the risk perception of investors, I use the "Sovereign Debt Litigation in US Courts: post-FSIA" data set. From this data set I create the treatment variable — Creditor Win — that takes on a value of "1" if the plaintiff won the case and "0" otherwise. Of course, to further examine the impact and validity of Creditor Win as the treatment variable, Defendant Win, which takes on a value of "1" if the defendant won the case and "0" otherwise, is used as a placebo treatment variable. In addition to case outcomes, two additional variables are constructed. Start Court takes on a value of "1" the date a court proceeding begins regardless of outcome and "0" otherwise. This variable is employed in some model estimations due to the potential market reaction to the news of a legal proceeding's commencement. Case Ends takes on a value of "1" the date a court proceeding ends regardless of outcome and "0" otherwise. It is incorporated into certain model estimations to analyze if the market's response to the creditor winning a case is similar to the market's response to the case's closure. Information on court litigation is captured on a daily basis, but it is aggregated to the monthly or yearly level when applicable.

Also included is an annual variable measuring whether and how much a country defaulted on

its debt during the previous year— Default Amount. This variable covers all types of sovereign debt, and it is a continuous variable as it takes into account how much of the debt was defaulted on. To construct this variable, I downloaded public and publicly guaranteed external debt data on arrears and debt serviced from the World Bank's Debtor Reporting System. The Default Amount variable is calculated as $\frac{Arrears}{Debt\ Due}$. While it is possible that there is under reporting in the Word Bank data, it is more comprehensive than a binary variable that indicates the start and end of a default. This variable is a more appropriate measure than total debt because it measure how much of the debt is in default. The total amount a country currently has in debt may affect the ability of a country to pay, but it is the amount that is already defaulted on that has the potential to be sued over and the amount that needs to be addressed to assuage investor fears.

The annual liberal democracy index from the Varieties of Democracy (V-dem) dataset is included as the Regime Type variable. The liberal democracy index is used because this measure focuses on the strength of the rule of law, the independence of the judiciary, and the constraints on the executive (Coppedge et al., 2022). This is included because it is possible that investors may react differently when a country with rule of law is ruled against, as opposed to one that lacks such features. Moreover, as many scholars believe that the domestic institutions of a country may influence investment and, in turn, growth, it is necessary to include this variable. Lastly, I include a variable — Restructure — that takes into account whether a debt restructuring has occurred. A debt restructuring is an agreement between the debtor state and its creditors to change the terms of the contract. It could result in changes in the maturity rate, interest rate, and/or a face value haircut to the amount owed. Restructurings can occur either pre or post default. The occurrence of a debt restructuring may impact outcomes in two ways. First, as restructuring negotiations can conclude in a variety of ways, it is possible that a group of creditors are unsatisfied with the terms of the negotiations and, therefore, go to court. Second, it is possible that restructuring a country's debt could provide benefits, such as preventing or at least postponing a possible default, or reaching an agreement with creditors after a default has occurred. Overall, the consequences of a sovereign debt restructuring may impact the debt market either positively or negatively and, therefore, must be taken into account in the statistical

model. Restructure is an indicator variable that takes on a value of "1" if a debt restructuring at time t and "0" otherwise. This variable simply indicates if the debt restructuring concluded with an agreement. It does not indicate what were the terms of the agreement, such as the size of a haircut or changes in maturity. I use the data from Cruces & Trebesch (2013) on sovereign debt restructurings to construct this variable. This data is available at the monthly level, but where appropriate, it is aggregated up to the yearly level. These variables are used in every statistical test.

Different dependent variables are used to test my arguments about the consequences of a ruling against a defendant country. To examine whether a ruling against a country influences investment, I first use data on bonds denominated in US dollars, which is obtained from the JPMorgan Emerging Market Bond Index (EMBI+). The EMBI+ is measured in basis points. A basis point is one-hundredth of a percentage point (0.01%) or, in other words, 100 basis points is 1%. Hence, if an time increases by by 25 basis points, it means the rate has risen by 0.25%. It is measured in basis points because the EMBI+ index provides data on the difference between the return rates of U.S. Treasury bills and government bonds issued in US dollars by other countries. The difference between these items is the spread. Interpreting the EMBI+ index is straightforward. For example, if a country has an EMBI spread of 300, this means that the interest rate for that country is roughly 3 percentage points higher than that of the US treasury's annual interest rate. The EMBI+ index is the most comprehensive data source on emerging market and developing country bond spreads.

The EMBI+ data were downloaded from GFD Finaeon Solutions. The availability of this data varies between daily and monthly intervals. Therefore, to conduct the statistical analysis, this variable is aggregated to the monthly level. As the interest here is the change in bond spread, the dependent variable is the change in Δ EMBI+ Monthly Bond Spread. This variable is available from December 1993 to August 2022. Bond data on 37 countries[8] are available, but China is removed from the analysis due to its difference from the other countries in the sample.[9]

[8] A full list of countries is provided in Appendix 6.3.

[9] China is quite different from other countries in the sample due to its influence in the global economy. It is one of the world's largest trading nations and is deeply integrated into global supply chains making it a severe outlier.

In addition to using the JPMorgan Emerging Market Bond Index to formulate the dependent variable, the 12-month rolling mean of the EMBI+ index — Bond Spread μ_{12} — is used as a control variable to address the potential of a reversion to the mean.

To examine the spillover effects of court rulings into the trade arena, I use annual data on the total imports of intermediate goods from the OECD Bilateral Trade database (BTDIXE) (OECD, 2017). From this data, the dependent variable is formed which is the growth rate in the amount imported. Next, to examine whether a judicial ruling can impact economic growth, I use the GDP per capita data from the Maddison Project (Bolt & Zanden, 2020), which is also yearly, to formulate the economic growth dependent variable. With these dependent variables, I will be able to examine the potential implications, if any, of the FSIA.

4.5 When the Gavel Drops: A State's Journey to the Courtroom

Of course, well before a state is sued in court, they must first abrogate on a contractual agreement. How a state breaks a contract varies and nowhere is this more apparent than when it comes to sovereign debt. While much of the literature typically uses a binary variable to indicate when a default starts and ends, measuring a sovereign debt default in such manner can be misleading as some states may only default on a small portion of their overall debt and others may default on the total amount. For example, from the list of countries in the World Bank's Debtor Reporting System that have defaulted on some form of debt, the minimum default amount was .000000057% out of total debt in a single year, while the maximum was a complete default. The median default was on 41.5% or 0.415 of debt. A state that only defaults on a small amount may not face the same economic problems that typically follow a default as a state that defaults on a large amount.[10] Therefore, it is important to use a continuous variable for the amount defaulted on and not just a binary variable. Besides the economic consequences of default, there could exist a correlation between the amount defaulted on and being taken to court. When examining all countries included in the World Bank's Debtor Reporting System, 122 countries defaulted at least once and among these 122 countries, 29 were taken to court at

[10]For an account of default patterns among creditors, see Schlegl, Trepesch, & Wright (2019).

least once. This suggests that when a country defaults, there is a 24% chance of being taken to court.

To examine the relationship between amount of default and going to court, I employ OLS with robust standard errors and Country and Year fixed effects. In this analysis, the dependent variable is "Go To Court," which is a binary variable that takes on a value of 1 if the country was taken to court in that year and 0 otherwise. I include the Default Amount, Regime Type, and Restructure variable. Additionally, I include a binary variable — Bond Default — that takes on a value of 1 if the default amount included bonds and 0 otherwise. It is possible to use data on default amount that just cover bonds, but these time series are often very short, which makes it difficult to include lags. Typically, but not always, there are restructuring negotiations prior to being taken to court. As such, in some estimations, I include a one year lag of Restructure. An interaction between Default Amount and Restructure is also included as there may be a relationship between the amount defaulted on and the likelihood of entering restructuring negotiations. This factor could influence whether a state is taken to court because in cases of high default, there is often a diverse set of creditors who may not participate in the restructuring negotiations or who may be dissatisfied with the outcome of the negotiations, leading them to file a lawsuit. The results are presented in Table 1 below.

Among the sample that is estimated in Table 1,[11] there are 112 countries that defaulted with 27 being taken to court at least once. From the model estimations in Table 1, it appears that there is a relationship between default amount and going to court. In all specifications, an increase in Default Amount increases the probability of going to court by at least .04. However, while statistically significant, an increase in default amount only increases the probability by a small amount. Restructure_{-1} is statistically significant in Model 4 and in the negative direction. Restructure is statistically significant and in the positive direction in Models 3 and 5. This suggests that a year after a restructuring negotiation is completed, the less likely it is to be a factor in going to court. However, in the year of restructuring, completing a restructuring negotiation increases the probability of utilizing the SDNY to settle disputes by at least .51

[11]The number of countries is reduced due to data availability for Regime Type, which led to the removal of small island nations.

Table 1: OLS Regressions - Factors Influencing Litigation Decison

	Dependent variable: Go To Court				
	(1)	(2)	(3)	(4)	(5)
Default Amount	0.04***	0.04***	0.04***	0.04***	0.04***
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Restructure$_{-1}$		−0.03		−0.22***	
		(0.09)		(0.06)	
Restructure			0.57***		0.51**
			(0.15)		(0.22)
Bond Default	0.01	0.01	0.01	0.01	0.01
	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Regime Type	−0.03	−0.03	−0.03	−0.03	−0.03
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Default Amount:Restructure$_{-1}$				0.69***	
				(0.20)	
Default Amount:Restructure					0.22
					(0.37)
N	3450	3450	3450	3450	3450
Number of Countries	112	112	112	112	112

Note: *p<0.1; **p<0.05; ***p<0.01

Only defaulted countries and years included in sample. Year and Country fixed effects with robust standard errors were utilized. Period under analysis: 1976-2020. This analysis is entirely yearly. In some estimations, Restructure$_{-1}$ is lagged by one year.

when the amount defaulted on is close to zero. Nevertheless, the interaction between Default Amount and Restructure$_{-1}$ is statistically significant and in the positive direction in Model 4, but the interaction between Default Amount and Restructure is statistically insignificant and in the positive direction in Model 5. This suggests that higher creditor diversity that comes with a higher default amount may lead to greater dissatisfaction from restructuring negotiations, as in the case of Argentina, which, in turn, may lead a party to file a claim in court even if some of the creditors are satisfied by the restructuring agreement.

To further examine factors that influence the decision to go to court, I re-estimate the models from Table 1 using a reduced sample that excludes Argentina. These results are presented in

Table 2 below. In the reduced sample, default Amount continues to be in the positive direction, but is only statistically significant in Models 3 and 5. Similarly to the estimations in Table 1, an increase in default amount only increases the probability by a small amount. Restructure$_{-1}$ also continue to be significant in the negative direction in all specifications where it was included. A year after a restructing negotiation decreases the probability of going to court by at least .13. Restructure is in the positive direction and statistically significant. Concluding a restructuring negotiation increases the probability of going to court in the same year by at least 0.49. The interaction between Default Amount and Restructure$_{-1}$ and Default Amount and Restructure, are both in the positive direction and statistically significant. When the default amount goes up, there is a likelihood of having a larger and more diverse group of creditors. This can result in dissatisfaction with the debt restructuring negotiation outcome, which may prompt a creditor to file a claim in the SDNY even if some of the creditors are satisfied by the restructuring agreement. In all specifications, Bond Default and Regime Type are insignificant. Overall, the results from Table 1 and Table 2 indicate that while there is a correlation between going to court and default amount, it only increases the probability of going to court by a small amount. Similarly, restructuring negotiations also negatively influence the probability of going to court, but it does not rule out the possibility completely. While Regime Type is insignificant in this analysis, this is probably not the whole story. In relation to restructurings, Enderlein, Trebesch, & Daniels (2012) find that political institutions matter when it comes to relations a sovereign state has with its creditors such that it explains which countries are more likely to enter contracted debt restructuring negotiations than others. Similarly, Ballard-Rosa (2016) finds that autocracies that are reliant on food imports are more likely to default than democracies. As such, regime type may influence the decision to go to court through other variables. In sum, in any analysis that examines the impact of a court ruling, it is necessary to include Default Amount, Regime Type, and Restructure as control variables due to the potential for confounding.

Table 2: OLS Regressions - Factors Influencing Litigation Decision, No Argentina

	Dependent variable: Go To Court				
	(1)	(2)	(3)	(4)	(5)
Default Amount	0.02	0.02	0.02*	0.02	0.02*
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Restructure_{-1}		−0.13***		−0.18***	
		(0.04)		(0.05)	
Restructure			0.58***		0.49**
			(0.20)		(0.23)
Bond Default	−0.01	−0.01	−0.01	−0.01	−0.01
	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Regime Type	−0.02	−0.02	−0.02	−0.02	−0.02
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Default Amount:Restructure_{-1}				0.25*	
				(0.14)	
Default Amount:Restructure					0.61*
					(0.34)
N	3412	3412	3412	3412	3412
Number of Countries	111	111	111	111	111

Note: *p<0.1; **p<0.05; ***p<0.01

Only defaulted countries and years included in sample. Year and Country fixed effects with robust standard errors were utilized. Period under analysis: 1976-2020. This analysis is entirely yearly. In some estimations, Restructure_{-1} is lagged by one year.

4.6 Methods and Results

4.6.1 The Bond Market

To assess how court rulings after defaults affect post-ruling investment, I examine movements in the sovereign bond market. The sovereign bond market, similar to other markets, is one that a country may enter and exit from multiple times. Applying causal inference to longitudinal observational studies is challenging under typical conditions, but even more so in the case where a participants enter and exist a study at different times. As a result, models, such as difference-in-differences, are not appropriate under such a scenario. Adding to the complexity is the fact that certain countries may have undergone the treatment of being sued and ruled against in court once, while others have gone through it multiple times. Moreover, some may

have received multiple treatments consecutively, several months, or years apart. As mentioned earlier, the presence of confounding variables poses a challenge when studying the association between court decisions and market reactions. Therefore, to study the impact of judicial rulings on the bond market, I first use OLS and then conduct further testing with structural nested mean models (SNMMs) to account for confounding.

The dependent variable used here is the month to month change in the EMBI+ bond spread (Δ EMBI+ Monthly Bond Spread) and the treatment variable is Creditor Win, which as a reminder means that after a default, the creditor brought the debtor to court and received a ruling in the Creditor's favor. Also utilized are Restructure, Regime Type, Default Amount, Bond Spread μ_{12}, Start Court, and Court End. Usually, a lesser number of lags are utilized with yearly data, whereas a greater number of lags are employed with monthly data (Wooldridge, 2016). Hence, for this analysis, as the dependent variable is monthly, the yearly variables will not be lagged by any amount. However, in some specifications, Creditor Win$_{-1}$ will be lagged by a month. The following three variables are lagged by six months: Restructure$_{-6}$, Start Court$_{-6}$, and Court End$_{-6}$. They are lagged by 6 months to account for the fact that there is often a time lag between the conclusion of a restructuring negotiation and a court decision and that there is a time lag between the start of a lawsuit and its conclusion.

The base specification is the following:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Creditor Win} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6}$$

Table 3 below presents the results from the OLS regressions with robust standard errors and Month and Country fixed effects. Each model specification builds on the base specification, but contains different lags and in Models 5 and 6, Case End$_{-6}$ is included. The key variables of interest is Creditor Win and Creditor Win$_{-1}$, which are significant and in the negative direction across specifications. This suggests that the bond market may respond to court rulings when the ruling is not in favor of the defendant. Regime Type is in the negative direction and

statistically significant in Models 4-6. The literature has established that democracies do have an advantage in the sovereign bond market, so it is unsurprising that bond spreads are lower for more democratic countries. Default Amount, Bond Spread μ_{12}, Restructure$_{-6}$, and Start Court$_{-6}$ are insignificant across specifications. Case End$_{-6}$ is positive and significant in Model 5, but insignificant in Model 6. Overall, these results imply that what matters to investors is not just going to court, but rather the ruling against the defendant. To further test these results, the models are re-estimated using a sample that excludes Argentina from the analysis, which are presented in Table 4.

Table 3: OLS Regressions of Bond Spread, Full Sample

	Dependent variable: Δ EMBI+ Monthly Bond Spread					
	(1)	(2)	(3)	(4)	(5)	(6)
Creditor Win	−236.87**		−242.29**		−277.14**	
	(117.67)		(121.40)		(132.00)	
Creditor Win$_{-1}$		−219.10*		−253.67*		−260.71*
		(120.28)		(146.24)		(144.51)
Regime Type	−18.71	−19.17	−19.10	−120.73**	−20.03	−119.47**
	(17.15)	(16.53)	(17.43)	(59.96)	(17.45)	(60.07)
Default Amount	76.35	73.09	72.82	166.74	64.21	161.09
	(66.74)	(66.31)	(63.93)	(112.34)	(62.88)	(115.37)
Restructure$_{-6}$	−414.42	−446.26	−415.08	−417.14	−416.01	−419.08
	(374.05)	(360.29)	(374.33)	(372.03)	(372.94)	(371.09)
Start Court$_{-6}$			26.19	5.86	14.83	3.52
			(44.22)	(40.22)	(43.05)	(40.08)
Case End$_{-6}$					76.21*	37.47
					(40.10)	(38.33)
Bond Spread μ_{12}	0.01	0.01	0.01	−0.002	0.01	−0.002
	(0.03)	(0.03)	(0.03)	(0.04)	(0.03)	(0.04)
Treated Units	6	6	6	6	6	6
Defaulted Countries	27	27	27	27	27	27
Number of Countries	35	35	35	35	35	35
Observations	6311	6311	6311	6311	6311	6311

Note: *p<0.1; **p<0.05; ***p<0.01

The dependent variable for each estimation is the change in bond spread from one month to the next. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly and Country fixed effects were utilized with robust standard errors. Variables that are lagged are lagged by month. Bond Spread μ_{12} is the rolling 12 month mean of the bond spread.

Table 4: OLS Regressions of Bond Spread, No Argentina

	Dependent variable: Δ EMBI+ Monthly Bond Spread					
	(1)	(2)	(3)	(4)	(5)	(6)
Creditor Win	−2,292.96**		−2,294.51**		−2,294.49**	
	(1,126.09)		(1,126.92)		(1,127.01)	
Creditor Win$_{-1}$		−2,333.31*		−2,334.87*		−2,334.86*
		(1,191.15)		(1,191.99)		(1,192.09)
Regime Type	−5.12	−4.87	−5.92	−5.66	−5.77	−5.52
	(18.78)	(18.08)	(18.64)	(17.95)	(18.63)	(17.94)
Default Amount	71.28	70.74*	72.05*	71.51*	71.91*	71.37*
	(43.36)	(41.97)	(43.27)	(41.88)	(43.29)	(41.90)
Restructure$_{-6}$	−487.27	−486.69	−487.02	−486.44	−487.03	−486.45
	(350.38)	(348.45)	(349.85)	(347.92)	(349.89)	(347.95)
Start Court$_{-6}$			−103.69	−103.98	−105.27	−105.56
			(75.68)	(75.60)	(75.80)	(75.72)
Case End$_{-6}$					32.71	32.69
					(50.94)	(51.04)
Bond Spread μ_{12}	0.02	0.02	0.02	0.02	0.02	0.02
	(0.03)	(0.03)	(0.03)	(0.03)	(0.03)	(0.03)
Treated Units	5	5	5	5	5	5
Defaulted Countries	26	26	26	26	26	26
Number of Countries	34	34	34	34	34	34
Observations	5987	5987	5987	5987	5987	5987

Note: *p<0.1; **p<0.05; ***p<0.01

The dependent variable for each estimation is the change in bond spread from one month to the next. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly and Country fixed effects were utilized with robust standard errors. Variables that are lagged are lagged by month. Bond Spread μ_{12} is the rolling 12 month mean of the bond spread.

With Argentina removed, Creditor Win and Creditor Win$_{-1}$ continue to be significant and in the negative direction. The effect size has increased because Argentina has a long history of defaulting, so it is possible that ruling against the defendant is more reassuring in other countries than in Argentina. In this analysis, Regime Type is significant in all specifications. Default Amount is in the positive and statistically significant in Models 2-6. This suggests that when the amount defaulted on increases, the bond spread is likely to increase. This is expected as a country that defaulted on a large amount would be riskier than one that defaulted on

a small amount because it would become more difficult to repay and negotiate with creditors over a large amount. Restructure$_{-6}$, Start Court$_{-6}$, Bond Spread μ_{12}, and Case End$_{-6}$ are insignificant across specifications. Overall, the OLS results support Hypothesis 1. A ruling in favor of the plaintiff does, on average, decrease the risk perception of investors. When a judge rules against the state that defaulted, then it follows that in expectation, interest rates decrease, the bond price increases, and the yield decreases.

Structural Nested Means Models

Due to the nature of sovereign debt litigation and the bond market, confounding is an issue. To address this issue, I utilize SNMMs with g-estimation for time-varying exposures that was proposed by J. M. Robins (1989). G-estimation of SNMMs is a statistical technique used to account for time-varying confounding that may be influenced by prior exposure in a longitudinal cohort study. This method is particularly useful when analyzing the combined impact of multiple treatments over time and also when examining mediation analysis where earlier exposure affects a confounding variable in the mediator-outcome relationship (J. Robins, 1986; J. M. Robins, 1994). This is particularly important in this substantive context because how much a country defaults by, whether they engage in restructuring negotiations, and the regime type of a country can all be confounders because they may not only affect sovereign debt litigation and the outcome of litigation, but also bond yields directly.[12]

These models are utilized to investigate how the average value of a continuous variable, such as a bond yield, changes over time in relation to a varying treatment or exposure, while taking into account the known covariate history. With this statistical method, the comparison is focused on two exposure histories that are identical except for a specific point in time, m. Both histories have the same exposure prior to time $m-1$ and have no exposure from time m+1 until the end of the follow-up period. These models simplify the problem by comparing hypothetical outcomes for two distinct exposure scenarios at time point m. This approach keeps exposure constant at observed levels for all prior time points, and assumes no exposure for all subsequent

[12]See Ballard-Rosa, Mosley, & Wellhausen (2019) for a discussion on the relationship between the bond market and regime type.

time points. Structural models are often called "blip functions" because it calculates the impact of a single exposure event, referred to as a "blip," that occurs at any time during the follow-up period, on the ultimate outcome observed at the end of the follow-up period.

The interest here though is not just on structural models, but structural *nested* models. The term "nested" refers to a way of conceptualizing longitudinal data as a series of nested trials. The approach involves analyzing the most recent trial first, while accounting for previous exposures and covariates. After establishing the association between the final exposure and the outcome, the method eliminates the influence of that exposure from the outcome. This procedure is repeated for every time point m, starting from the end of follow-up and working backwards to the beginning, while adjusting for exposures that occurred at all subsequent time points. As a result, a counterfactual outcome is computed for each observation under a treatment regimen.

With SNMMs, the interest is in estimating the average causal effect of treatment "A" within levels of the other variables included in the analysis, "L", which are either confounders or independent variables, such that $E[Y^{a=1} - Y^{a=0}|L]$. There are four assumptions that must be met to use SNMMs. First, is consistency, which means that the observed outcome of an individual must match their potential outcome based on the exposure or treatment history they were actually assigned to. Second, is conditional exchangeability. This means that within the strata of measured confounders, the observed exposures (the treatment) are statistically independent of counterfactual outcomes. Third, models are correctly specified. Fourth, is the stable unit treatment value assumption, which requires that a treatment of one unit does not influence the outcome of another unit. Of particular interest, however, is conditional exchangeability. Under conditional exchangeability $Y^a \perp\!\!\!\perp A|L$, the conditional impact will be consistent between the treated and untreated groups because, within the levels of L, both groups comprise individuals/countries that are on average similar. Expressing conditional exchangeability in terms of the conditional probability of treatment results in: $\text{logit}PR[A = 1|Y^{a=0}, L] = \alpha_0 + \alpha_1 Y^{a=0} + \alpha_2 L$, with α_2 as a vector of parameters, one for each component of L. Consequently, the structural nested means model can be written as the following: $E[Y^{a=1} - Y^{a=0}|A = a, L] = \beta_{1a} + \beta_{2a} L$. Parameters β_1 and β_2 are estimated using g-estimation.[13]

[13]The term "G-estimation" pertains to a parameter estimation technique that is not tied to any partic-

A unit's counterfactual outcome $Y^{a=0}$ is a function of the observed treatment and outcome, but also an unknown parameter ψ, such that $Y^{a=0} = Y - \psi_1 A$. The goal of g-estimation is to estimate ψ, which the formula here would be $H(\psi^\star) = Y - \psi^\star A$ for each unit in the analysis over all possible values. To understand g-estimation it is helpful to express conditional exchangeability in terms of the conditional probability of treatment, which results in: $\text{logit}PR[A = 1|Y^{a=0}, L] = \alpha_0 + \alpha_1 Y^{a=0} + \alpha_2 L$, with α_2 as a vector of parameters, one for each component of L. If conditional exchangeability holds, then α_0 should equal to 0 for the counterfactual. As such, a logistic regression — $\text{logit}PR[A = 1|H\psi^\star, L] = \alpha_0 + \alpha_1 H\psi^\star + \alpha_2 L$ — is estimated for every potential value of $\psi^\star$ until we find the one that results in an $H\psi^\star$ with $\alpha_1 = 0$.

In essence, g-estimation involves using a grid search or optimization algorithm to test hypothetical values for a parameter, which are then used to compute possible outcomes in the absence of exposure or treatment for each individual. Unlike maximum likelihood estimation procedures, g-estimation relies on the assumption of conditional exchangeability and determines which set of candidate counterfactual outcomes is statistically independent of observed exposures based on previously measured covariates and treatments/exposures. This is achieved by including the candidate counterfactual outcome, along with earlier covariates and exposures, in a model that predicts observed exposure and checking whether the coefficient for the candidate counterfactual outcome is zero. The parameter value that was used to calculate the set of candidate counterfactual outcomes with a coefficient of zero is referred to as the g-estimate.

Overall, to estimate SNMMs using g-estimation, there are two main steps involved. Firstly, propensity scores indicating the probability of treatment need to be estimated using logistic regressions, with the treatment variable as the outcome. This step is referred to as g-estimation. Secondly, the main outcome of interest, such as bond yields, needs to be regressed on the covariates "L" and the propensity score from the first step. In brief, SNMMs are useful to examine the impact of a treatment or series of treatments on the average value of an outcome.[14]

ular model specification. However, the majority of applications of g-estimation involve structural nested models and are used instead of inverse probability weighting, which are used for marginal structural models.

[14]See Vansteelandt & Sjolander (2016) and Vansteelandt & Joffe (2014) for more information on SNMMs with g-estimation. The gesttools R package was used for estimation.

To implement an SNMM, a propensity model and outcome model must be specified. Unlike in OLS where the treatment variable and the lag of the treatment variable are in separate regressions, with SNMM, they are included in the same model. The outcome model specifications for the SNMM estimations are the following:

Model 1 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Creditor Win} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Bond Spread}\mu_{12}$$

Model 2 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Creditor Win} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Start Court}_{-6} + \text{Bond Spread}\mu_{12}$$

Model 3 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Creditor Win} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Start Court}_{-6} + \text{Case End}_{-6} + \text{Bond Spread}\mu_{12}$$

The propensity model for each model is simply the outcome model with the dependent variable replaced by Creditor Win such that the propensity model for Model 1 is $\text{Creditor Win} = \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Bond Spread}\mu_{12}$. When using SNMM, I limit the number of time periods post-treatment to 4. If Creditor Win has an impact on monthly bond spreads, the evidence of impact is likely to only be visible for a short time as markets adapt and change quickly to new information. Moreover, as the dependent variable is the change in bond spread, it is unrealistic to expect bond spreads to persistently drop. Realistically, the change in bond spread will be immediate and then taper off to a new lower mean. The results with time fixed effects and bootstrapped standard errors are presented in Table 5 below. The models are re-estimated on a reduced sample that excludes Argentina and these results are presented in Table 6 below.

Table 5: SNMM Results, Full Sample

Models	Period 1	Period 2	Period 3	Period 4
Model 1	-814.90 (-3070.43 , -18.07)	-883.01 (-3198.55 , 54.16)	-198.62 (-980.57 , 235.59)	276.23 (-41.20 , 1191.78)
Model 2	-836.23 (-3070.69 , -45.64)	-898.46 (-3191.55 , 47.45)	-193.91 (-918.35 , 237.52)	286.25 (-33.23 , 1192.32)
Model 3	-800.13 (-3058.11 , -20.66)	-884.81 (-3201.46 , 58.21)	-204.31 (-989.73 , 234.58)	282.84 (-41.64 , 1202.14)

The dependent variable for each estimation is the change in bond spread from one month to the next. The treatment variables is *Creditor Win*. Each time period represents one month post treatment such that Period 4 is 4 months post treatment. Every SNMM model specification matches the corresponding OLS estimations. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly fixed effects were utilized.

Across all model specifications, the effect of the treatment variable — Creditor Win — is in the negative direction and significant 1 month post-treatment (Period 1). However, it loses significance after the first month post-treatment, which is expected. According to the results, a creditor winning a lawsuit decreases bond spreads, on average, by at least 800 basis points and at most, on average, by 836 basis points when Argentina is included in the analysis. These results hold when Argentina is removed from the analysis. However, similarly to the regression results, the effect size is much larger when Argentina is excluded. In the sample where Argentina is excluded, bond spreads decrease by at least 1633 points.

Table 6: SNMM Results, No Argentina

Models	Period 1	Period 2	Period 3	Period 4
Model 1	-1645.46	-1762.40	-293.42	647.94
	(-3643.37 , -67.12)	(-3981.35 , 153.29)	(-1116.31 , 454.39)	(38.78 , 1466.92)
Model 2	-1649.83	-1772.37	-330.01	635.98
	(-3654.94 , -67.42)	(-3997.89 , 151.86)	(-1219.06 , 452.22)	(40.44 , 1465.56)
Model 3	-1633.03	-1777.74	-333.59	656.00
	(-3618.77 , -67.77)	(-4002.34 , 151.64)	(-1212.84 , 451.18)	(40.08 , 1478.76)

The dependent variable for each estimation is the change in bond spread from one month to the next. The treatment variables is *Creditor Win*. Each time period represents one month post treatment such that Period 4 is 4 months post treatment. Every SNMM model specification matches the corresponding OLS estimations. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly fixed effects were utilized.

Placebo Tests

While the results above support Hypothesis 1, to further examine whether the behavior of ruling against the defendant matters and not just the act of going to court, as a placebo test, Defendant Win was substituted in for Creditor Win as the treatment variable.[15] However, the potential impact of the defendant winning the case on markets could go in one of two directions. First, it could increase risk perception of investors because the country just won the case, and the plaintiffs will not be able to recoup their losses. Second, it is also possible that it is the act of going to court that sends a signal and the outcome of litigation matters less. In such a scenario, the result would be that borrowing costs decline irrelevant of litigation outcome. However, I argue that it is the act of ruling in favor of the plaintiff that sends the signal. Absent this signal, there is not much difference between not going to court and having a trial with the outcome leading to a defendant win as the position of the plaintiff has not changed. The results in Tables 7-10 support this argument. Across all specifications, Defendant Win as the treatment variable is insignificant.

[15] When conducting a placebo test, you have the option to either exclude the original treatment from the estimation or include it. In this case, it is included because some countries have received both treatments at different times in their history, making it necessary to control for Creditor Win.

Table 7: Placebo Test OLS Regressions, Full Sample

	Dependent variable: Δ EMBI+ Monthly Bond Spread					
	(1)	(2)	(3)	(4)	(5)	(6)
Defendant Win	−340.63		−336.61		−332.31	
	(212.58)		(210.34)		(211.00)	
Defendant Win$_{-1}$		−83.53		−83.17		−71.60
		(145.84)		(141.95)		(146.00)
Creditor Win	−210.75*		−251.19*		−274.87**	
	(109.35)		(138.11)		(139.69)	
Creditor Win$_{-1}$		−211.66*		−216.28*		−253.04*
		(124.02)		(126.31)		(153.26)
Regime Type	−13.16	−14.61	−117.38*	−14.97	−115.48*	−113.79*
	(16.88)	(17.41)	(62.93)	(17.35)	(62.92)	(62.95)
Default Amount	64.38	60.73	141.89	57.92	133.20	138.45
	(66.38)	(69.38)	(112.24)	(63.87)	(114.10)	(123.49)
Restructure$_{-6}$	−400.84	−434.68	−370.81	−435.91	−371.31	−412.00
	(355.34)	(357.56)	(367.05)	(348.57)	(365.01)	(368.79)
Start Court$_{-6}$			18.49	21.62	14.68	3.94
			(44.60)	(50.28)	(44.54)	(43.46)
Case End$_{-6}$					68.41	41.43
					(43.54)	(40.63)
Bond Spread μ_{12}	0.01	0.01	0.01	0.01	0.01	0.004
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Placebo Treated Units	9	9	9	9	9	9
Defaulted Countries	27	27	27	27	27	27
Number of Countries	36	36	36	36	36	36
Observations	6311	6311	6311	6311	6311	6311

Note: *p<0.1; **p<0.05; ***p<0.01

The dependent variable for each estimation is the change in bond spread from one month to the next. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly and Country fixed effects were utilized with robust standard errors. Variables that are lagged are lagged by month. Bond Spread μ_{12} is the rolling 12 month mean of the bond spread.

In Table 7 above and Table 8 below, Defendant Win and Defendant Win$_{-1}$ are insignificant. However, Creditor Win and Creditor Win$_{-1}$ continue to be statistically significant in both Tables. Defendant Win is not a substitute for the creditor winning a case. The act of going to court by itself does not illicit a decrease in investor risk perception. Hypothesis 1 is still supported. A US judge's decision against the defendant is perceived as valuable by investors,

Table 8: Placebo Test OLS Regressions, No Argentina

	Dependent variable: Δ EMBI+ Monthly Bond Spread					
	(1)	(2)	(3)	(4)	(5)	(6)
Defendant Win	−780.83		−775.61		−775.55	
	(533.87)		(534.20)		(529.55)	
Defendant Win$_{-1}$		−68.14		−70.62		−64.47
		(215.97)		(210.21)		(221.13)
Creditor Win	−2,229.76*		−2,237.83*		−2,231.48*	
	(1,340.57)		(1,359.10)		(1,343.19)	
Creditor Win$_{-1}$		−2,367.16**		−2,368.89**		−2,366.52**
		(1,206.12)		(1,173.33)		(1,204.83)
Regime Type	2.43	2.39	−134.85**	1.58	2.07	−130.34*
	(9.95)	(19.73)	(59.92)	(19.02)	(9.70)	(67.88)
Default Amount	54.21	58.05	201.88*	58.75	54.56	212.45*
	(47.16)	(41.64)	(108.50)	(40.39)	(47.73)	(117.76)
Restructure$_{-6}$	−462.39***	−450.40***	−458.99***	−450.65***	−462.61***	−446.18***
	(149.84)	(144.77)	(144.55)	(140.78)	(149.88)	(138.64)
Start Court$_{-6}$			−78.73	−113.05	−62.58	−129.47
			(98.95)	(75.67)	(85.74)	(80.14)
Case End$_{-6}$					20.31	28.28
					(40.37)	(55.09)
Bond Spread μ_{12}	0.04**	0.03	0.03	0.04	0.04**	0.03
	(0.02)	(0.03)	(0.02)	(0.03)	(0.02)	(0.04)
Placebo Treated Units	8	8	8	8	8	8
Defaulted Countries	26	26	26	26	26	26
Number of Countries	35	35	35	35	35	35
Observations	5987	5987	5987	5987	5987	5987

Note: *p<0.1; **p<0.05; ***p<0.01

The dependent variable for each estimation is the change in bond spread from one month to the next. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly and Country fixed effects were utilized with robust standard errors. Variables that are lagged are lagged by month. Bond Spread μ_{12} is the rolling 12 month mean of the bond spread.

which is why there is a decrease in the bond spread when a judge rules against the defendant. In Table 7, Regime Type is in the negative direction and statistically significant in Models 3, 5, and 6, but in Table 8 it is only significant in Models 3 and 6. Start Court$_{-6}$, Case End$_{-6}$, Restructure$_{-6}$, Default Amount, and Bond Spread μ_{12} are insignificant across model specifications in Table 7. When Argentina is removed from the sample, Start Court$_{-6}$ and Case

End_{-6} continue to be insignificant. However, Default Amount is in the positive direction and statistically significant in Models 3 and 6, Restructure_{-6} is significant across all specifications, and Bond Spread μ_{12} is statistically significant and in the positive direction in Models 1 and 5.

The SNMM models are re-estimated with the inclusion of Defendant Win and the results are presented in Tables 9 and 10 below. The outcome model specifications for the SNMM placebo test estimations are the following:

Model 1 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Defendant Win} + \text{Defendant Win}_{-1} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Bond Spread}\mu_{12}$$

Model 2 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Defendant Win} + \text{Defendant Win}_{-1} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Start Court}_{-6} + \text{Bond Spread}\mu_{12}$$

Model 3 Specification:

$$\Delta\text{EMBI+ Monthly Bond Spread} = \text{Defendant Win} + \text{Defendant Win}_{-1} + \text{Creditor Win}_{-1} + \text{Regime Type} + \text{Default Amount} + \text{Restructure}_{-6} + \text{Start Court}_{-6} + \text{Case End}_{-6} + \text{Bond Spread}\mu_{12}$$

Tables 9 and 10 for the full sample and restricted sample respectively, indicates that Defendant Win has no impact on bond spreads across all specifications. The act of going to court itself does not elicit a response by investors. Investors respond to a court ruling when it is against the defendant. By ruling against the defendant, the judge increases the confidence of investors.

Table 9: Placebo Test SNMM Results, Full Sample

Models	Period 1	Period 2	Period 3	Period 4
Model 1	-2.08	-62.91	-199.41	145.53
	(-306.11 , 260.57)	(-223.15 , 38.00)	(-553.68 , 33.48)	(-51.62 , 504.15)
Model 2	-3.74	-62.24	-198.66	142.08
	(-307.98 , 251.43)	(-221.66 , 36.91)	(-552.87 , 34.85)	(-51.50 , 493.84)
Model 3	-0.84	-61.28	-201.84	142.90
	(-308.10 , 251.17)	(-221.36 , 37.35)	(-552.74 , 39.14)	(-51.32 , 497.14)

The dependent variable for each estimation is the change in bond spread from one month to the next. The treatment variables is *Creditor Win*. Each time period represents one month post treatment such that Period 4 is 4 months post treatment. Every SNMM model specification matches the corresponding OLS estimations. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly fixed effects were utilized.

Table 10: Placebo Test SNMM Results, No Argentina

Models	Period 1	Period 2	Period 3	Period 4
Model 1	-94.1733	-112.62	-317.34	152.80
	(-174.94 , 440.19)	(-242.83 , 45.43)	(-793.32 , 66.65)	(-108.95 , 639.47)
Model 2	-94.74	-111.81	-316.96	153.67
	(-175.55 , 443.20)	(-241.95 , 43.91)	(-793.78 , 66.99)	(-109.71 , 639.55)
Model 3	-94.85	-111.54	-317.26	153.81
	(-175.67 , 443.19)	(-241.46 , 43.93)	(-793.76 , 67.68)	(-109.60 , 639.49)

The dependent variable for each estimation is the change in bond spread from one month to the next. The treatment variables is *Creditor Win*. Each time period represents one month post treatment such that Period 4 is 4 months post treatment. Every SNMM model specification matches the corresponding OLS estimations. The time range represented in the data set is from 1993-12-01 to 2022-08-01. Monthly fixed effects were utilized.

4.6.2 Import of Intermediate Goods

While the evidence thus far suggests that the risk perception of investors is reduced with a ruling in favor of the plaintiff, it remains uncertain as to whether rulings against a defendant in the sovereign debt arena may spillover into other economic areas. To examine whether spillover effects exist, I focus on the import of intermediate goods as this area of trade should be most sensitive to the legal environment than exports. Using data on the import of intermediate goods, I construct five different dependent variables to examine the impact of a judicial ruling on trade. The dependent variables for Models 1, 2, 3, 4, and 5 are the growth rates in the amount imported (IG) over 1, 2, 3, 4, and 5 years, respectively. The independent variables included in this analysis are Creditor Win, Default Amount$_{-1}$, Restructure$_{-1}$, Regime Type$_{-1}$, log of GDP per capita$_{-1}$, and an interaction between Creditor Win and Default Amount$_{-1}$. Unlike the bond data, this data is yearly as such the Restructure and Creditor Win variable are scaled up to the yearly level. Of most interest is the interaction between Creditor Win and Default Amount$_{-1}$. This is because a default is an extreme act that typically occurs during peak economic distress when trade is also declining. Therefore, it is crucial to understand the impact of a ruling against the defendant in a default situation on the trade arena. Table 11 below presents the OLS regression results with robust standard errors and country and year fixed effects. The time frame for this analysis spans from 1990 to 2021.

Similarly to the impact of a creditor winning on the bond market, the outcome of a plaintiff's win on the growth of the import of intermediate goods is unlikely to generate permanent growth since global value chains are influenced by several economic factors that tend to fluctuate over time. As displayed in Table 12, the interaction between Creditor Win and Default Amount$_{-1}$ is in the positive direction across specifications. However, it is only significant in Models 1-4 and loses significance when the dependent variable is the 5 year Import Growth rate for intermediate goods. While the growth in intermediate goods is not sustained over time, it is the case that when a Creditor Wins a case during a debt crisis, the import of intermediate goods increase. Compared to entities that were not ruled against or not taken to court, a defendant state benefits from a ruling against it during a default as it results in increased imports

Table 11: OLS Regressions, Intermediate Imported Goods

	(1) IG_1	(2) IG_2	(3) IG_3	(4) IG_4	(5) IG_5
Creditor Win	−12.00	−11.14**	−18.42***	−15.24	−0.49
	(7.38)	(5.03)	(7.05)	(12.29)	(18.91)
Default $Amount_{-1}$	−1.45	−3.73	−7.51	−7.52	−19.03
	(3.28)	(5.98)	(9.87)	(15.73)	(21.19)
Regime $Type_{-1}$	0.24	2.70	12.68	20.42	34.31
	(3.90)	(8.66)	(11.92)	(16.34)	(21.56)
$Restructure_{-1}$	−1.69	−8.50*	−15.04	−25.60***	−32.96***
	(2.35)	(4.87)	(10.24)	(7.35)	(6.54)
Log GDP $per\ capita_{-1}$	−10.42***	−1.39	11.51	24.92	43.56*
	(3.67)	(6.43)	(11.43)	(17.51)	(25.60)
Creditor Win:$Default\ Amount_{-1}$	18.46**	28.13***	55.83***	45.54**	22.34
	(8.16)	(8.54)	(13.38)	(21.14)	(28.52)
Number of Countries	34	34	34	34	34
Observations	879	845	811	777	743

Note: *p<0.1; **p<0.05; ***p<0.01

Each dependent variable (IG) represents the growth rate of intermediate goods, however, they are calculated over distinct time frames of 1 year, 2 years, 3 years, 4 years, and 5 years, respectively. The data on intermediate goods is only available starting from 1990 and extends to 2021. Year and Country fixed effects with robust standard errors were utilized.

of intermediate goods. Overall, these results suggest that a ruling in favor of the plaintiff in sovereign debt arena can have positive spillover effects into the trade arena during an economic crisis. Hypothesis 2 is supported.

4.6.3 Economic Growth

Considering that a plaintiff's win could potentially lower borrowing costs for a country, it may allow the government to secure financing for infrastructure development and other projects, while also increasing the import of intermediate goods that lead to job creation through the linkages between factories and sectors. Therefore, it's plausible that countries that are ruled against may experience greater economic growth than those that were not subject to a ruling or never went to court.

To test this implication, I use the same model specifications as used for the examination of

Table 12: OLS Regressions, GDP per capita Growth and Sovereign Debt Resolution

	(1) γ_1	(2) γ_2	(3) γ_3	(4) γ_4	(5) γ_5
Creditor Win	-3.37^{**}	-3.72^{**}	-7.50^{***}	-7.25^{***}	-2.62
	(1.54)	(1.85)	(2.33)	(2.71)	(4.43)
Default Amount$_{-1}$	-1.07	-3.08^{**}	-6.17^{***}	-7.16^{**}	-7.58^{**}
	(0.86)	(1.45)	(2.13)	(2.85)	(3.49)
Regime Type$_{-1}$	-0.44	0.10	-0.45	-2.80	-4.06
	(1.29)	(2.04)	(2.65)	(3.36)	(3.91)
Restructure$_{-1}$	-0.28	-2.17	-3.85^{*}	-5.49^{**}	-7.83^{**}
	(0.89)	(1.76)	(2.25)	(2.77)	(3.19)
Log Import Amount$_{-1}$	-0.50	0.81	1.38	2.27	3.80^{*}
	(0.60)	(1.03)	(1.40)	(1.82)	(2.22)
Log GDP per capita$_{-1}$	-6.08^{***}	-3.51	4.66	16.17^{***}	29.88^{***}
	(1.47)	(2.53)	(3.68)	(5.02)	(6.26)
Creditor Win:Default Amount$_{-1}$	6.52^{**}	12.34^{***}	21.80^{***}	19.09^{***}	8.95
	(2.61)	(3.69)	(4.98)	(5.93)	(7.88)
Number of Countries	34	34	34	34	34
Observations	799	799	799	799	799

Note: *p<0.1; **p<0.05; ***p<0.01

Each dependent variable represents the GDP per capita growth rate (γ), however, they are calculated over distinct time frames of 1 year, 2 years, 3 years, 4 years, and 5 years. Due to data availability and to have as close as possible time frame as the analyses above, the period under consideration is from 1990-2018. Year and Country fixed effects with robust standard errors were utilized.

the implications of a court ruling on the growth of the import of intermediate goods. The independent variables included in this analysis are Creditor Win, Default Amount$_{-1}$, Restructure$_{-1}$, Regime Type$_{-1}$, log of GDP per capita$_{-1}$, log of Import Amount$_{-1}$, and an interaction between Creditor Win and Default Amount$_{-1}$. Five different specifications of GDP per capita growth were utilized for the dependent variable. The dependent variables for Models 1, 2, 3, 4, and 5 are the growth rates in GDP per capita (γ) over 1, 2, 3, 4, and 5 years, respectively. Robust standard errors with Country and Year fixed effects are used in all the OLS models. To make this analysis comparable to the other analyses, the time frame for this analysis spans from 1990 to 2018.

As before, the key variable of interest is the interaction between Creditor Win and Default

Amount as the implication that is being tested is whether economic growth occurs among countries that are ruled against to a greater extent than those that did not receive a ruling against them or who were never taken to court. The OLS regression results are presented in Table 12 above. In Models 1-5, the interaction between Creditor Win and Default Amount$_{-1}$ is in the positive direction. However, this interaction is only significant in Models 1-4. The absence of significance in Model 5 might be attributable to the fact that a court ruling cannot sustain economic growth permanently, as seen from the lack of significance in intermediate goods growth by year 5. However, this lack of significance could also stem from data availability issues, as the analysis only covers the period from 1990 to 2018, and calculating a 5-year growth rate increases the amount of missing data. Nevertheless, the results in Table 12 support Hypothesis 3. Countries that defaulted and received a judicial ruling against them are more likely to experience higher economic growth than those who were not ruled against.

4.7 Discussion

In the event that a country defaults on its debt, would a ruling made by a US court under the FSIA have any impact on the bond market and, in turn, on the economy of the debtor state? I argued that a ruling in favor of a plaintiff would lower investors' perception of risk for that specific country. An investor may be more willing to engage and sign contracts with a country that just defaulted if it believed that its investments would be protected. A ruling by a judge in favor of the plaintiff sends information. It lets the plaintiff and the investment community know that the actions of the state are illegitimate, and the complaints made by the plaintiff are valid. Although the court lacks the power to enforce its decisions, it can delegitimize the actions of a state and signal to the international community that third-party sanctions may be appropriate. In this regard, other scholars have found that countries will avoid re-entering the market until all debts are paid when a court is involved (Schumacher et al., 2021). While the ability to enforce may vary by several factors, such as the size of a hedge fund, the argument here is not about actual enforcement, but (a) making it socially acceptable to enforce and (b) increasing the possibility of recouping losses after a default. A ruling in favor of the plaintiff

makes it acceptable to punish a state for abrogating a contract and increases the likelihood that losses will be recouped. As such, an investor may be more willing to return to a country shortly after default when a judge rules in favor of the plaintiff because with a win in the courtroom an expectation that they may not have to bear their full losses is developed.

Whether this expectation is realized or not is irrelevant as long as the possibility to recoup losses exists. Due to this possibility, the perceived risk of investing in a country, whether it be through buying bonds or setting up factories for final or intermediate goods production, post-default is minimized. If the plaintiff is successful in obtaining favorable judicial rulings under the FSIA, which leads to a reduction in investors' risk perception, there are three potential unintended consequences that could emerge. The first unintended consequence of a ruling in favor of the plaintiff is that borrowing costs for the defendant may decrease. A country that is viewed as high-risk will typically have high interest rates and, in turn, a high bond yield. A lower risk country will have low interest rates and a low bond yield, which means that the borrowing costs is lower. Therefore, if a ruling in favor of the plaintiff decreases the risk perception of a country, there ought to be a corresponding reduction in borrowing costs. To test this implication, I utilize OLS and SNMMs. The dependent variable was the month-to-month change in EMBI+ spreads.

Table 3 and 4 presented the results from the OLS estimations with the full and reduced samples, respectively. In both configurations, Creditor Win was statistically significant and in the negative direction. To address the issue of confounding, SNMMs were utilized with Creditor Win as the treatment variable. The results with the full sample were presented in Table 5 and the restricted sample in Table 6. Creditor Win was statistically significant and in the negative direction across all model specifications in the first period. This suggests that the bond market reacts to information from a US judge as the bond spread on currently issued bonds decreases, which indicates that risk perception decreases.[16] The impact of the ruling, however, is insignificant after the first period. Markets are continually incorporating new information as it arises, which means that, except for a financial crisis, it is improbable for any event to have a

[16]In future analysis, the rates of new issuance's after a court ruling will be compared to those issued prior to default.

prolonged effect. That said, the insignificance in the following periods does not mean that bond spreads return to the pre court ruling level. Overall, Hypothesis 1 is supported by the results presented in Tables 3-6.

As a placebo test, Defendant Win was substituted in for Creditor Win and the results in Tables 3-6 were re-estimated. A placebo test was conducted because it is possible that just the act of going to court could influence bond markets. It could do so in two ways. First, it could increase risk perception of investors because the country just won the case, and the plaintiffs will not be able to recoup their losses. In this scenario, the bond spread or yield would increase. Second, it is also possible that it is the act of going to court that sends a signal and the outcome of litigation is irrelevant. In such a scenario, the result would be that borrowing costs decline irrelevant of litigation outcome. However, I argue that it is the act of ruling in favor of the plaintiff that sends the signal. Absent this signal, there is not much difference between not going to court and having a trial with the outcome leading to a defendant win as the position of the plaintiff has not changed. The results in Tables 7-10 support this argument and, in turn, Hypothesis 1. Across all specifications, Defendant Win as the treatment variable is insignificant. For investors, the act of going to court does not provide information about the legality of the actions of a state. Furthermore, a ruling in favor of the defendant did not impact the risk perception of an investor since it would neither benefit nor harm any investors who held defaulted bonds. When a judge rules in favor of the plaintiff, it imparts information to investors that prompts them to adjust their risk assessment, which is then manifested in the bond spread. Overall, the results suggests that there is a relationship between a judicial ruling in favor of the plaintiff and bond market reactions.

The first implication of a court a ruling in favor of the plaintiff is the lowering of borrowing costs. The second implication is spillover into the trade arena. In regards to spillover into the trade arena, I argued that global value chains, in particular the importation of intermediate goods, were especially susceptible to the nullification of contracts. As a result, it is this area of trade that is most sensitive to events in other areas of the economy. A ruling in favor of the plaintiff in the sovereign debt arena could result in decreased risk perception of a country that was just ruled against among firms participating in GVCs as it implies that relying on the

US legal system to resolve conflicts is an effective dispute resolution mechanism. Hence, when a judge rules in favor of the plaintiff over sovereign debt, I expect there to be spillover in the trade arena as the import of intermediate goods is reliant on contractual agreements. A ruling in favor of the plaintiff in the sovereign debt arena, is likely to increase the confidence of firms that export intermediate goods to a country that defaulted.

To test this second implication, I use OLS regression with robust standard errors and Country and Year fixed effects. The results were presented in Table 11. As the theoretical interest here is of the impact of a court ruling on trade during a default, the interaction between Default Amount$_{-1}$ and Creditor Win is the key variable of interest. The dependent variables are the growth rates in the amount imported over 1, 2, 3, 4, and 5 years. In all specifications, the interaction effect is in the positive direction. In Models 1-4 the interaction is statistically significant. This suggests that although a sovereign default is often associated with a decline in trade, a ruling in favor of the plaintiff in case over debt could lead to an increase in trade. The interaction in Model 5 is insignificant, but it is still in the positive direction. It can be inferred that the treatment effect of Creditor Win may not lead to permanent growth in intermediate goods as a multitude of factors influence global value chains. Overall, Hypothesis 2 is supported. On average, a ruling in favor of the plaintiff is likely to increase the import of intermediate goods in comparison to countries that either did not go to court or who were not ruled against.

Building on the first and second implication, the third implication of a creditor winning a court case leading to decreased risk perception of investors is economic growth. As a court ruling in favor of the plaintiff leads investors to perceive a high-risk country as lower risk, borrowing costs decline and the import of intermediate goods increase. The lowering of borrowing costs can potentially permit a country to invest in items that attract foreign direct investment such as public infrastructure. Furthermore, intermediate goods often act as a multiplier in the economy as it generates new jobs and sustains existing jobs. As a result, Economic growth can be influenced by both factors, which I am examining by utilizing data on GDP per capita and OLS with robust standard errors and Country and Year fixed effects. Similarly to the analysis on the import of intermediate goods, the key variable of interest here is the interaction between Creditor Win and Default Amount$_{-1}$. Five dependent variables were utilized, which are the growth rates

in GDP per capita over 1, 2, 3, 4, and 5 years. The results were presented in Table 12. Across all specification the interaction between Creditor Win and Default Amount$_{-1}$ is in the positive direction and is significant in Models 1 - 4. The interaction was insignificant in Model 5, but this could be attributed to data limitations or that the impact of Creditor Win wanes over time similarly to that of bond spreads and the growth of intermediate goods importation. Overall, Hypothesis 3 is supported. Countries that defaulted and received a judicial ruling against them are more likely to experience higher economic growth than those countries who never went to court or received a negative judicial ruling.

4.8 Conclusion

Courts are responsible for making decisions over contentious issues and provide information. The Foreign Sovereign Immunities Act was purposely created to give US courts the power to decide over commercial disputes between a sovereign state and a non-state actor. By entrusting US courts with a responsibility previously held by the State Department, there has been a shift in authority regarding issues that challenge the conventional concept of absolute sovereignty. This is especially true when it comes to sovereign debt, where traditionally, decisions were made solely by domestic political actors. Given this violation of absolute sovereignty, it is important to understand if US judges have an impact on the economy of a state being sued.

What impact, if any, does a court ruling have on the debt market and the economy of a debtor state? I argue that judicial decisions by US courts can impact the market because a ruling against the defendant lowers the perceived risk by an investor, which leads to positive unintended consequences for the debtor state. By ruling in favor of the plaintiff the judge sends the following information: (1) the action of the debtor state was illegitimate, (2) claims made by the creditor (the plaintiff) are valid, (3) actions to enforce the ruling are acceptable, and (4) given (1) - (3) it may be possible to recoup losses after a default. As such, an investor may be more willing to return to a country shortly after default when a judge rules in favor of the plaintiff because with a win in the courtroom an expectation that they may not have to bear their full losses is developed. The fulfillment of these expectations is not a prerequisite for the debtor state to experience the favorable outcomes.

While the court itself cannot enforce their judgments, a court ruling can impose costs via third parties that they send information to through their rulings. In regard to sovereign debt litigation, when a judge rules in favor of the plaintiff, the defendant state is typically required to pay back creditors. In most cases, this is typically the full worth of the bond. While this may cost a sovereign state in the short term, a ruling against the state and in favor of the plaintiff may be beneficial for them. A judgment against the defendant should increase investor confidence that their investments will be protected and, as such, they would be more willing to reinvest in a country that just transgressed upon an agreed upon contract. If a ruling in favor of the plaintiff reduces the risk perception of an investor, then there are three possible implications that benefit the debtor state.

First, borrowing costs should decrease for the defendant country. Due to "original sin", most developing and emerging market countries issue bonds in US dollars[17] to keep borrowing costs low. While having bonds denominated in US dollars can pose a problem for a country as they cannot unilaterally alter the terms of the agreement, investors prefer US dollar denominated debt because it ties the hand of the issuing country. Not only is a debtor state unable to unilaterally alter agreement terms when bonds are issued in US dollars, but as these bonds are issued in US dollars any dispute involving these bonds can be seen in US courts due to the FSIA. As such, these bonds are less risky than those denominated in local currency. However, while these bonds are more desirable to investors, which is why borrowing costs are lower for US denominated debt than local currency debt, it does not mean that the interest rate for these bonds do not rise and fall. Similarly to a bond denominated in the local currency or other securities, the value of dollar denominated bonds rise and fall with the economic conditions of the country.

Given that investors can take legal action against a country in case of a default on US dollar denominated debt, I expect a reduction in borrowing costs if a debtor state is taken to court and ruled against. This is due to the boost in investor confidence it provides. By ruling against the debtor state, the judge is not only sending information about the legality of the action taken by the state, but also that the FSIA is more than just window dressing legislation. As such, even though the state may have a history of default, an investor would be willing to

[17]They could potentially issue bonds in Sterling or the Euro as well.

reinvest in the country and buy US dollar denominated debt issued by that country. To examine this first implication, I use OLS and SNMMs on US denominated bonds. The results suggest that when a creditor wins a suit, the debtor state benefits by realizing lower spreads and bond yields. This result held even when Argentina was removed from the sample. Most importantly, however, when using cases where the defendant won a case in lieu of cases where the plaintiff won as the treatment, the treatment effect of the defendant winning was insignificant. Going to court by itself does not induce investor confidence. In order for investors' risk perception towards a particular country to decrease, a ruling against the defendant is necessary. This creates expectations of repayment and strengthens the value of the FSIA because it is seen as a viable tool for investors to use.

The second and third implications consider the spill-over effects of a court decision in the sovereign debt arena. For the second implication, I expect a creditor win in the sovereign debt arena to spill over into the trade arena. Specifically, I expect the import of intermediate goods to increase upon the creditor winning a sovereign debt case. GVCs are arguably more reliant on contracts compared to more traditional forms of trade. This is because multiple countries are involved in the production of a single item, and any disruption in one location can become quite costly for a firm. Businesses that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and therefore closely monitor the economic climate. This includes sovereign defaults. When a sovereign default occurs, imported intermediate goods and trade more generally will decrease.

However, if the FSIA does decrease investor risk perception when a defendant state is ruled against in the sovereign debt arena, the amount of imported intermediate goods should increase in comparison to states that defaulted without being ruled against by a US court or were not taken to court. By ruling against the defendant in a sovereign debt litigation case, a judge is stepping in to enforce a contract. As a result, this may not only increase confidence among investors involved in the sovereign bond market, but there may be spillover into the trade arena. More precisely, it could result in enhanced trust among firms participating in GVCs as it implies that relying on the US legal system to resolve conflicts is an effective dispute resolution mechanism. Even though these firms typically have multiple venues to choose from

to settle a dispute, having a US judge rule in favor of the plaintiff during a sovereign default episode reassures firms that (a) the economy may turn around and (b) that US courts may be a viable option if needed. To test the second implication, I used OLS and found that countries that defaulted and were also subject to a negative ruling observed a rise in their imports of intermediate goods.

Given the first and second implications, I examine the likelihood of the third implication, which is economic growth. If a creditor winning a case in the sovereign debt arena leads to lower borrowing costs and an increase in the import of intermediate goods, it follows that a country may experience economic growth. Lower borrowing costs makes it easier for a country to service its present debt amount and potentially makes it feasible for them to make infrastructure investments that attract foreign direction investments. Moreover, intermediate goods often act as multiplier in an economy as it creates linkages between factories and sectors that generates jobs. As a result, it is possible for a country that was ruled against in court to experience economic growth. Using OLS with robust standard errors and Country and Year fixed effects, the results suggest that a country that defaults and also receives an unfavorable court ruling is more likely to experience an increase in its economic growth compared to a country that defaulted but did not receive such a ruling.

What impact can a court ruling have on a country that defaulted on its debt? While the leader of a country would not want to lose a sovereign debt litigation case as it may require them to repay the debt in full, losing a case may lead to unintended positive benefits. A judge does not set out to improve the economic fortunes of a debtor state. However, by ruling in favor of the plaintiff and, therefore, reducing the risk perception of investors, a recently defaulted country benefits. It benefits the debtor state by reducing borrowing costs, increasing the import of intermediate goods, and increasing economic growth post-default. US courts can govern the market and have an impact on the economy on the debtor.

Chapter 5

Conclusion

In this dissertation, I investigate the evolution of the global governance architecture as it relates to sovereign debt. In turn, I ask what actions can creditors take against a sovereign country that fails to repay its debts? Can legislation passed in one country to regulate international transactions have economic consequences in other countries? To answer these questions, I focus on the evolution and application of the Foreign Sovereign Immunities Act (FSIA), which provides a legal framework for determining when a foreign sovereign state can be subject to lawsuits in US courts and argue that the US judiciary via the application of the FSIA can impact the sovereign bond market and the economy of a state in default.

Well before the United States provided investors a legal option to settle disputes with sovereign states, the only choice creditors had was to either accept the loss from a default, enter restructuring negotiations, or to pressure their home governments to get involved. Creditors could pressure their home governments—usually through lobbying—to put in place trade sanctions, initiate diplomatic negotiations, or utilize gunboat diplomacy. The latter primarily occurred in the 19th and early 20th centuries. While gunboat diplomacy may not have been an option of first resort, when it did occur, a country was more likely to improve its fiscal discipline (Mitchener & Weidenmier, 2010). Of course, with a changing geopolitical environment, the use of gunboat diplomacy to safeguard the interests of investors diminished.

In lieu of gunboat diplomacy, three mechanisms were developed to manage sovereign default resolution after WWII. The first of which is the Paris Club that was formed in 1956 by the

major creditor countries[1] to jointly agree to rescheduling and reducing the debts of developing countries. The purpose of the Paris Club is to oversee state-to-state loans. The London Club, established in 1976, serves as the counterpart to the Paris Club and comprises commercial banks. This organization is meant to manage the restructuring of commercial bank debt. However, neither of these institutions has extensive formal rules, such as an agreement to meet when a debt default occurs or provide a dispute settlement mechanism for other types of debt, such as bonds.

With the expanding international economic influence of the United States, the United States itself emerged as the primary home base for numerous individual investors, hedge funds, and banks. As the Paris Club did not serve the needs of a growing class of international non-state actors, the State Department issued the Tate Letter in 1952. The Tate Letter changed the official US foreign policy of granting absolute sovereignty to restrictive sovereignty. This meant that a country could no longer claim sovereign immunity over commercial transactions, thereby potentially facilitating investors' access to the legal system if a dispute emerged. However, two weaknesses existed under the Tate Letter regime that led to its replacement. First, a sovereign state could file an absolute sovereign immunity request with the State Department. This meant that two branches of government—the Executive and Judicial—could simultaneously be involved in deciding the outcome of a lawsuit. Second, a definition of "commercial" was lacking in the Tate Letter, which gave judges leeway in the application of restrictive immunity. This was particularly problematic for investors who owned sovereign debt as under the Tate Letter it was unclear as to whether sovereign debt was a commercial issue or an issue where absolute sovereignty is applied. As a result, there was pressure from investors to replace the Tate Letter regime with a dispute settlement process that was free of interference from the State Department and had a clearly defined definition of "commercial."

The signing of the FSIA in 1976 marked a significant shift in the approach to sovereign litigation and dispute settlement. Formally, the FSIA has rectified the issues of the Tate Letter. The US judiciary were given sole oversight in disputes involving a sovereign state. As a result, US

[1]Current list of Paris Club members: Australia, Austria, Belgium, Brazil, Canada, Denmark, Finland, France, Germany, Ireland, Israel, Italy, Japan, Netherlands, Norway, Russia, South Korea, Spain, Sweden, Switzerland, United Kingdom, and the United States.

judges could now make decisions without the involvement of the State Department. Moreover, the FSIA clarified what acts of a state should be considered a commercial act and how to make this determination. Under the FSIA, to determine whether an act is commercial or not, the "nature of the act" test is used. This means that when evaluating a case to determine whether it falls under the purview of the FSIA, a judge needs to consider the nature and not the purpose of the act. For example, prior to the FSIA, sovereign debt would typically not be considered a commercial act because of its purpose, which is to fund government activities and goals. However, under the FSIA, the purpose of sovereign debt would be disregarded. Instead, the nature of the act, which is the same as that of a corporation taking out loans or issuing bonds, would be considered. Consequently, under the FSIA, sovereign debt is a commercial issue and, for this reason, sovereign states can be sued in US courts in the event of a default.

By examining the historical context, the transition to and the application of the FSIA, this research sheds light on the complexities and implications of sovereign debt default resolution. As a sovereign default can pose a significant threat to the stability and well-being of the economy of the defaulted state and that of the global economy, it is important to understand if the FSIA plays a role in sovereign debt resolution such that there is economic recovery post-default. The findings highlight the challenges faced by states in balancing economic cooperation, interdependence, and the preservation of sovereignty. The absence of a dedicated international institution for sovereign debt resolution in the realm of finance has led to the reliance on ad hoc negotiations and the US legal system. As a result, *how* the FSIA is applied by the US judiciary is of key importance to understand. Overall, this dissertation contributes to the understanding of sovereign debt politics and the role of the FSIA in shaping the dynamics of sovereign debt default resolution.

5.1 Summary of Findings

To understand whether the FSIA is a tool that can be used by investors to punish a sovereign country that fails to repay its debts and whether this legislation can have economic consequences, I first examine the political roots of this legislation. Specifically, Chapter 2 examines how the judiciary under the Tate Letter (1952-1977) decided whether to grant absolute sovereign

immunity or restrictive sovereign immunity. As the Tate Letter did not provide a definition of what is or is not commercial, this created an unclear policy environment as the Act of State doctrine, which enshrined absolute sovereignty, coexisted simultaneously with the Tate Letter. I argued that due to the unclear policy environment, if the defendant country was a democracy or if the dispute pertained to a sovereign default, the judiciary tended to rely on the Act of State doctrine (absolute sovereignty), resulting in a favorable outcome for the defendant.

This argument was tested by utilizing two original data sets and employing OLS and machine learning techniques. The first data set includes all immunity requests sent to the State Department from 1952 to 1977. The second data set consists of all sovereign litigation cases that arrived in US courts between 1811 and 1976. The analysis in Chapter 2 suggests two key findings. First, the State Department in practice impacted judicial decision-making to a small degree. Second, the application of the Tate Letter by the judiciary was inconsistent. This is because the Act of State doctrine maintains that a judge should be respectful of the laws and rulings of foreign countries. As a result, democracies were more likely to be awarded absolute sovereignty because judges were more likely to defer to the decisions made by a country with similar institutions to the US than autocracies. Moreover, since sovereign debt is commonly utilized for domestic financing purposes, it remained perceived as an internal sovereign matter. For this reason, the judiciary was unwilling to prescribe economic policy to an independent state. The regime type of the defendant state did not affect this issue area.

While the State Department retained the ability to intervene in cases when requested by the defendant state, the State Department at times would ignore requests or even deny a country absolute sovereignty. A state going to the State Department did not guarantee that the State Department would grant them absolute sovereignty. Naturally, with the delegation of authority by the State Department to US courts, there is an anticipation that a US judge may align with the State Department's stance if they were to intervene. However, this was not necessarily the case. In several cases, the judiciary would often rule differently than the State Department. The State Department and the US judiciary are separate entities with varying organizational cultures and responsibilities, which meant that their preferences were not always in agreement. Despite investors perceiving the State Department as a threat to their access to the court, the data

and analysis indicate that the judiciary's lack of clarity regarding the application of absolute or restrictive immunity mattered more than the involvement of the State Department.

Consequently, although the State Department issued the Tate Letter with the intention of providing investors with a dispute settlement mechanism in case of sovereign defaults, asset expropriation, and similar scenarios, it proved to be an ineffective tool in practice for safeguarding investors' interests and investments. During this period, the judiciary was not more inclined than the State Department to consistently apply restrictive immunity. Nonetheless, investors advocated for the removal of the State Department from the judicial decision-making process, and their pressure ultimately resulted in the replacement of the Tate Letter with the FSIA. However, in addition to removing the State Department, the FSIA also addressed the procedural deficiencies of the Tate Letter, such as the absence of a clear definition of "commercial."

As the FSIA was supposed to be an improvement for investors, Chapter 3 examines whether this is the case. It examines the factors that impact judges' decision-making. Hypothetically, one would assume that with the removal of political interference from the State Department and the establishment of clear criteria for determining what constitutes a commercial act under the FSIA, the process would now be free from political influences. I suggest, however, that politics is still present through judicial assignment. Specifically, I argue that a judges' ideological inclination affects their decisions. Conservative judges, unlike their liberal counterparts, practice judicial restraint on economic issues meaning that they are more likely to uphold the FSIA and rule against the defendant because conservatives are pro-business and less interventionist in the economy. This difference in ruling propensity between conservative and liberal judges is most pronounced when the defendant is a democracy, as democracies tend to engage in intra-industry trade with the United States to a greater extent.

To test this argument, I focus on sovereign debt litigation and the United States District Court for the Southern District of New York (SDNY). This decision was made because (a) the main issue area in the Tate Letter period that caused confusion and disagreement over whether it was a commercial act or a sovereign act was sovereign debt, (b) the occurrence of a sovereign default is difficult to dispute, making it an ideal issue area to study due to the similarity in the quality of cases brought to court, and (c) sovereign debt cases are exclusively handled by the

SDNY, which means that investors cannot forum shop within the United States for a court that they may view as being more sympathetic towards them. This, in turn, makes causal inference a feasible strategy in this context. Overall, the economic issue area of sovereign debt is a hard test for the FSIA, as it is classified as commercial under the FSIA, but during the Tate Letter period, investors experienced a high rate of loss in these cases.

I gathered an original data set encompassing all sovereign debt cases filed in the SDNY between 1976 and March 2022 to test this argument. As the data contains multiple observations for the same judge, country, and nominating president of the judge, this lends itself to hierarchical modeling. Therefore, a Bayesian hierarchical model is first estimated to examine what influences the outcome of a case. In this analysis, as trade ties with the United States increase, so did the probability of the creditor winning a case. Moreover, an interaction between the regime type of the country and whether a judge was nominated by a republican judge was in the positive direction, which suggests that when a conservative judge rather than a liberal judge is assigned to a case where the defendant is a democracy, the creditor is more likely to win. While these results suggest that judicial assignment is a factor in determining case outcome, to further test these results, I exploit the quasi-random assignment of judges to cases.

I leverage the quasi-random assignment using Virtual Twins (VT), a causal inference machine learning approach. With this method, judicial assignment is the treatment variable. The VT estimation found that the greatest difference between conservative and liberal judges occurs among defendants who are democracies. There is a subgroup of countries where the ideology of a judge who is assigned to a case can change outcomes. Overall, differences along ideological lines are most visible when the defendant is a democracy due to their involvement in international trade. Conservative and liberal judges tend to rule most similarly when the defendant is an autocracy, but are more likely to rule differently when the defendant is a democracy. In sum, although the FSIA represents an improvement for investors over the Tate Letter by clearly defining the responsible decision-making branch in disputes involving investors and foreign sovereign states and providing a clear definition of what constitutes a commercial act, politics still permeates the process, even in straightforward issue areas such as sovereign debt defaults.

Nevertheless, it is essential to ascertain whether the FSIA is merely a superficial legislation that has no impact on the behavior of those involved in a lawsuit or if it can indeed influence behavior. What impact, if any, does a court ruling have on the debt market and the economy of a debtor state? Chapter 3 aims to address this question by investigating market reactions in the bond market, as well as examining the growth in importation of intermediate goods and the growth in GDP per capita of the state in default. In this chapter, I argued that judicial decisions by US courts can impact the market because a ruling against the defendant lowers the perceived risk by an investor, which leads to positive unintended consequences for the debtor state. By ruling in favor of the plaintiff the judge sends the following information: (1) the action of the debtor state was illegitimate, (2) claims made by the creditor (the plaintiff) are valid, (3) actions to enforce the ruling are acceptable. As such, an investor may be more willing to return to a country shortly after default when a judge rules in favor of the plaintiff because with a win in the courtroom an expectation that they may not have to bear their full losses is developed. The fulfillment of these expectations is not a prerequisite for the debtor state to experience the favorable outcomes.

If a ruling in favor of the lender lowers perceived risk for investors, then there are three possible implications. First, the cost of borrowing should decrease for the debtor country. By ruling in favor of the plaintiff, a judge not only creates the expectation of full repayment for investors holding defaulted bonds, but also boosts investor confidence in bonds that are not in default, as it signals that the FSIA is more than a mere window dressing. Second, the import of intermediate goods should increase. Firms that manufacture final products using intermediate goods sourced from multiple countries are highly vulnerable to disruptions and closely monitor the economic climate. Although these firms typically have multiple venues to choose from to settle a dispute, a plaintiff receiving a favorable court ruling from a US judge during a sovereign default episode reassures firms that (a) the economy may turn around and (b) US courts may be a viable option if needed. Third, a debtor state that defaults and receives an unfavorable court ruling is more likely to experience economic growth afterward. Lower borrowing costs can enable a country to service its current debt and invest in public infrastructure that attracts foreign direct investment. Furthermore, an increase in the importation of intermediate goods

can have a multiplier effect on the economy, creating jobs and contributing to further growth.

In Chapter 3, I continue to utilize the original data on FSIA sovereign debt court rulings. To test whether court rulings can impact the bond market, I utilize OLS and Structural Nested Means Models (SNMM). The treatment variable is whether the creditor (plaintiff) won the case. The assumption here being that the rulings of courts are exogenous because investors have no way of predicting or guaranteeing how a judge will rule. To analyze bond market reactions, the outcome variable used is the change in Δ EMBI+ Monthly Bond Spread. The OLS and SNMM results suggest that when a creditor wins a suit, the debtor state benefits by realizing lower spreads and bond yields. This result held even when Argentina was removed from the sample. Most importantly, however, when using the defendant winning a case as the treatment rather than the plaintiff, the treatment effect of the defendant winning was insignificant. This means that going to court by itself does not induce investor confidence. In order for investors' risk perception towards a particular country to decrease, a ruling against the defendant and in favor of the plaintiff is necessary.

To test the second and third implications, I employed OLS regressions with robust standard errors and included Country and Year fixed effects. The dependent variable for the second implication, which is the import of intermediate goods, was measured by the growth rates in the amount imported over 1, 2, 3, 4, and 5 years. The variable of interest in this analysis was the interaction between the default amount and the treatment variable, indicating whether the creditor won the case. Default amount was utilized because the extent of a country's default can impact the economy. A small default generally has a lesser negative effect on the economy compared to a large default. In the analysis, the interaction between default amount and the treatment variable was in the positive direction and significant with all dependent variables, except for the 5-year growth rate. This suggests that while a sovereign default is typically associated with an overall decline in trade, a ruling in favor of the plaintiff in a sovereign debt litigation case could result in an increase in the import of intermediate goods. However, the impact of the treatment variable diminishes over time. Nonetheless, on average, a ruling in favor of the plaintiff is likely to increase the import of intermediate goods compared to countries that did not pursue legal action or were not ruled against.

For the third implication, the dependent variables used are the growth rates in GDP per capita over 1, 2, 3, 4, and 5 years. The key variable of interest in this analysis remains the interaction between the default amount and the treatment variable. In all specifications, this interaction term shows a positive and significant effect, except when the 5-year GDP per capita growth rate is used. The lack of significance in this case could be attributed to data limitations or the possibility that the treatment's impact diminishes over time, similar to the 5-year growth rate of intermediate goods importation. Overall, however, countries that defaulted and received a judicial ruling in their favor are more likely to experience higher economic growth compared to those countries that never went to court or received a negative judicial ruling.

What actions can creditors take against a sovereign country that fails to repay its debts? Can legislation passed in one country to regulate international transactions have economic consequences in other countries? The chapters in this dissertation attempted to answer these questions. I argued that US courts are a critical tool in managing sovereign debt markets and in influencing investors' decision to invest. As globalization and the power of the United States in the global economy increased, a formal mechanism to handle disputes between investors and a foreign sovereign state was needed. In response to this need, the State Department announced the Tate Letter, which formally changed US foreign policy to one that upheld restrictive sovereignty. While the formal switch to a type of sovereignty that allows investors to sue foreign states in US courts was a significant move, the Tate Letter had weaknesses that made it difficult to effectively utilize the US courts. To address problems present in the Tate Letter, the FSIA was passed in 1976.

With the passage of the FSIA, investors were given legislation that clearly defined how to determine what constitutes a commercial act. Although politics are still present in the decision-making process as conservative and liberal judges rule differently when the defendant is a democracy, the FSIA is more than just symbolic legislation. Even though a judge cannot enforce a ruling by themselves, when a judge rules in favor of the plaintiff, it sends a signal that taking action to enforce the ruling is acceptable for third parties, which may involve seizing assets. This has the potential to bolster investor confidence by offering the opportunity to recover lost assets. In sum, judicial decisions by US judges can impact the market because

a ruling against the defendant increases investor confidence to reinvest in a country, creating positive unintended consequences for the debtor state. These unintended consequences include lower bower costs, an increase in the importation of intermediate goods, and economic growth over the medium term.

5.2 Implications for Future Research

At the time of this writing, developing countries are facing a sovereign debt crisis, partially attributed to the impact of the COVID-19 pandemic. Since 2020, there have been 14 distinct instances of default across nine different sovereign entities. This is a significant rise in defaults when compared to the 2000-2019 time period where there were 19 defaults observed across 13 different countries. The current surge of defaults, both recent and anticipated, raises unanswered questions that have not been addressed within this dissertation.

First, is the question of how states in Africa will negotiate debt restructurings with China. All countries have a portfolio of debt from different creditors. Usually, this encompasses various forms of financial instruments, including but not limited to bonds, loans from the International Monetary Fund (IMF) and/or World Bank, as well as loans from other countries. Of course, within each of these categories, there is further variation by loan or bond maturity, currency it is issued in, and the owner of the debt. For this reason, a key problem for all developing countries is how to get a heterogeneous group of creditors to agree to a debt restructuring. This is problematic for countries who have Chinese loans as China is not a member of the Paris Club.

Related to this is the question regarding the prioritization of creditors. Sovereign defaults fundamentally entail matters and concerns rooted in domestic politics. The focus of this dissertation was primarily on sovereign bonds and to a lesser extent on bank loans and trade credits. However, it may be the case that some countries avoid defaulting on bonds or choose to default on them first. Countries that want to avoid IMF interference are likely to default on other types of debt first. Of course, some leaders may welcome IMF interference as it provides an opportunity to utilize the IMF as a scapegoat for implementing austerity policies that would otherwise be unpopular. These issues are rooted in domestic politics as they ultimately revolve around the matter of political survival. As leaders want to stay in power, who they default on

and how much they default on depends on domestic context. Naturally, political survival and the strategies a leader may choose will vary with political institutions.

Lastly, there is the question of whether countries may move away from issuing bonds in US dollars following the historical saga between Judge Griesa and Argentina. Most developing countries suffer from "original sin," which is the inability of a developing country to issue bonds in their own currency as they are not attractive to investors. Although being taken to court and ruled against has positive consequences for a country, it may have negative consequences for the leader in power as the short-term costs may lead to them losing office as it did for Cristina Fernández de Kirchner of Argentina. Given the attention the Argentine legal saga drew, it is possible that risk-averse leaders may adjust their debt portfolios in a manner that minimizes their potential exposure to US judges.

Moving forward, further research can continue to explore the evolving nature of sovereign debt politics, including the incorporation of domestic politics, the analysis of court rulings' impact on investor behavior and market dynamics, and the examination of the potential establishment of specialized institutions in the field of finance to address the challenges presented by sovereign debt crises.

Chapter 6

Appendices

6.1 Appendix for Chapter 2

6.1.1 Machine Learning Counterfactuals - Cuba

Specifically Mothilal et al. (2020) use c = arg min yloss$(f(c), y) + |x - c|$, where in the first part of the equation the counterfactual, c, is pushed by yloss towards a different prediction and the second part of the equation ensures that the counterfactual does not stray too far from the original value. Generating the counterfactual relies on the two concepts of diversity, as we want diverse outcomes, and feasibility because we want results that are not unreasonable. To obtain a diversity measure, determinantal point processes (DPP) are used to select a subset of counterfactuals where a determinant of the kernel matrix is calculated via $dpp_diversity = det(K)$ and $K_{i,j} = \frac{1}{1+dist(c_i,c_j)}$ where $dist(c_i, c_j)$ is a distance metric between the two counterfactuals. Of course, the most useful results are those that are closest, but different from, the original outcome. Therefore, a proximity measure is also used ($Proximity = \frac{1}{k}\sum_{i=1}^{k} dist(c_i, x)$) Using these definitions of diversity and proximity, a loss function is used over all generated counterfactuals ($C(x) = \arg\min \frac{1}{k}\sum_{i=1}^{k} yloss(f(c_i), y) + \frac{\lambda}{k}\sum_{i=1}^{k} dist(c_i, c_j) - \lambda_2$ dpp_diversity$(c_1, ..., c_k)$).

6.1.2 Court Outcomes pre and post Tate Letter Period

Court Outcomes - Tate Letter Period

	Type Economic					
	Debt-Bond	Debt-Other	Debt-Trade	Exprop.-Payments	Exprop.-Physical	Other
Winner						
Defendant	7 (18%)	0 (0%)	10 (25%)	2 (5.0%)	11 (28%)	10 (25%)
Plaintiff	1 (2.8%)	2 (5.6%)	7 (19%)	11 (31%)	8 (22%)	7 (19%)
Total	8 (11%)	2 (2.6%)	17 (22%)	13 (17%)	19 (25%)	17 (22%)

Court Outcomes - Pre Tate Letter Period

	TypeEconomic					
	Debt-Bond	Debt-Other	Debt-Trade	Exprop.-Payments	Exprop.-Physical	Other
Winner						
Defendant	5 (22%)	0 (0%)	8 (35%)	0 (0%)	2 (8.7%)	8 (35%)
Plaintiff	1 (5.0%)	0 (0%)	2 (10%)	0 (0%)	0 (0%)	17 (85%)
Total	6 (14%)	0 (0%)	10 (23%)	0 (0%)	2 (4.7%)	25 (58%)

Cuba Court Cases - No State Department Involvement

Date	Type Economic	Case Name	Defendant Winner?
1960-02-19	Exprop.-Physical	Flota Maritima Browning de Cuba v. Ciudad Habana	0
1960-12-13	Debt-Trade	Berlanti Construction Co. v. Republic of Cuba	1
1961-03-31	Exprop.-Physical	Banco Nacional de Cuba v. Sabbatino	0
1961-11-24	Debt-Trade	Three Stars Trading Co. v. Republic of Cuba	0
1961-11-27	Debt-Other	Banco Nacional De Cuba v. Steckel	0
1962-05-15	Exprop.-Payments	Gonzalez v. Industrial Bank	1
1962-07-06	Exprop.-Physical	Banco Nacional de Cuba v. Sabbatino	0
1962-11-01	Exprop.-Payments	Gonzalez v. Industrial Bank	0
1962-12-19	Exprop.-Physical	Kane v. Republica De Cuba	0
1964-03-23	Exprop.-Physical	Banco Nacional de Cuba v. Sabbatino	1
1964-05-18	Exprop.-Physical	Kane v. Republica De Cuba	1
1972-03-17	Exprop.-Payments	Menedez v. Faber, Coe & Gregg, Inc.	0
1973-09-24	Exprop.-Payments	Menedez v. Saks & Co.	0
1976-05-24	Exprop.-Payments	Alfred Dunhill of London, Inc. v. Republic of Cuba	0

6.2 Appendix for Chapter 3

6.2.1 Data Collection - Court Case Selection Process

As there is no PACER search function that allows one to limit a search to sovereign debt litigation cases, using RSelenium, I supplied a list of state-owned entities and country names, as listed in the United Nations, to the website to enable a thorough search, which then downloaded all court cases in HTML format from the SDNY. After saving all court dockets that are produced from this search, I then remove all cases that are not sovereign debt litigation cases.

6.2.2 Bayesian Hierarchical Model

Bayesian Hierarchical Model: Factors Influencing Litigation Outcome

	Dependent variable: Creditor Win						
	Mean	SD	Lower95	Upper95	P>0	MCerr	psrf
Intercept	0.54	1.09	-1.64	2.72	0.69	0.02	1.00
Trade Competition$_{-1}$	0.30	0.07	0.16	0.43	1.00	0.00	1.00
Republican Nominated	-0.44	1.14	-2.82	1.74	0.35	0.02	1.00
Regime Type$_{-1}$	-4.86	1.70	-8.30	-1.70	0.00	0.03	1.00
Republican Nominated*Regime Type$_{-1}$	1.19	1.84	-2.44	4.81	0.74	0.03	1.00
Hedge Fund	-0.75	0.18	-1.10	-0.39	0.00	0.00	1.00
Attachment Attempt	1.48	0.31	0.86	2.07	1.00	0.00	1.00
IMF Program$_{-1}$	0.36	0.49	-0.59	1.37	0.78	0.00	1.00
Investment Profile$_{-1}$	0.09	0.13	-0.17	0.33	0.75	0.00	1.00
Type Economic	-0.42	0.29	-1.01	0.12	0.06	0.00	1.00

Note:

Presented are the results from a Bayesian probit hierarchical model with country, president, and judge random effects. The dependent variable is Creditor Win. Default Amount$_{-1}$ is removed from this analysis.

6.2.3 Virtual Twins - Full Sample with Argentina Binary Variable

Virtual Twins Results - Full Sample with Argentina Binary Variable

	Estimate	SE	Lower CI	Upper CI	P-Value
Subgroup Treatment	0.548	0.001	0.547	0.549	0e+00
Subgroup Treatment - Bootstrapped	0.385	0.014	0.359	0.411	0e+00
Overall Treatment	0.236	0.059	0.121	0.352	1e-04

Note: Presented are the treatment effects from the Virtual Twins estimation. With the re-substitution method (RM), probabilities are estimated from the data and substituted into the equation for Q(A). In contrast, for Subgroup Treatment - Bootstrapped a parametric bootstrap approach is used. The dependant variable is Creditor Win. The treatment variable is the Republican Nominated variable. 'Overall' is the treatment effect for the entire population. The RM and bootstrapped subgroup treatment effects are for the identified subgroup, which are located on the right hand side of Figure 6.1.

Figure 6.1: Regression Tree Results from Virtual Twins- Full Sample with Argentina Binary Variable

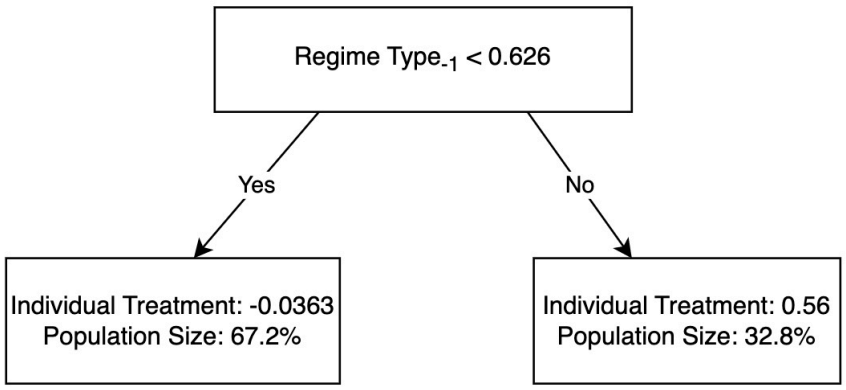


Figure 6.1 presents the estimated regression tree from VT. Each box contains the population size of each category and the mean estimated *individual* differential treatment effect, which is the difference for an individual observation between being assigned a liberal vs. conservative judge. This is not the overall subgroup differential treatment effect, which is presented in Table 6.2.3. However, the overall subgroup differential treatment effect is estimated from the right hand side outcome (the "no" branch). This figure says that the difference in case outcome is greatest when a conservative rather than a liberal judge is assigned to country that has at least some democratic features (i.e., has a score of .626 or greater from the V-dem measure).

6.2.4 Virtual Twins - Argentina Removed

Virtual Twins Results - No Argentina

	Estimate	SE	Lower CI	Upper CI	P-Value
Subgroup Treatment	0.063	0.086	-0.106	0.232	0.462
Subgroup Treatment - Bootstrapped	0.031	0.060	-0.087	0.149	0.606
Overall Treatment	0.020	0.081	-0.138	0.178	0.801

Note: Presented are the treatment effects from the Virtual Twins estimation. With the re-substitution method (RM), probabilities are estimated from the data and substituted into the equation for Q(A). In contrast, for Subgroup Treatment - Bootstrapped a parametric bootstrap approach is used. The dependant variable is Creditor Win. The treatment variable is the Republican Nominated variable. 'Overall' is the treatment effect for the entire population. The RM and bootstrapped subgroup treatment effects are for the identified subgroup, which are located on the right hand side of Figure 6.2.

Figure 6.2: Regression Tree Results from Virtual Twins - Argentina Removed

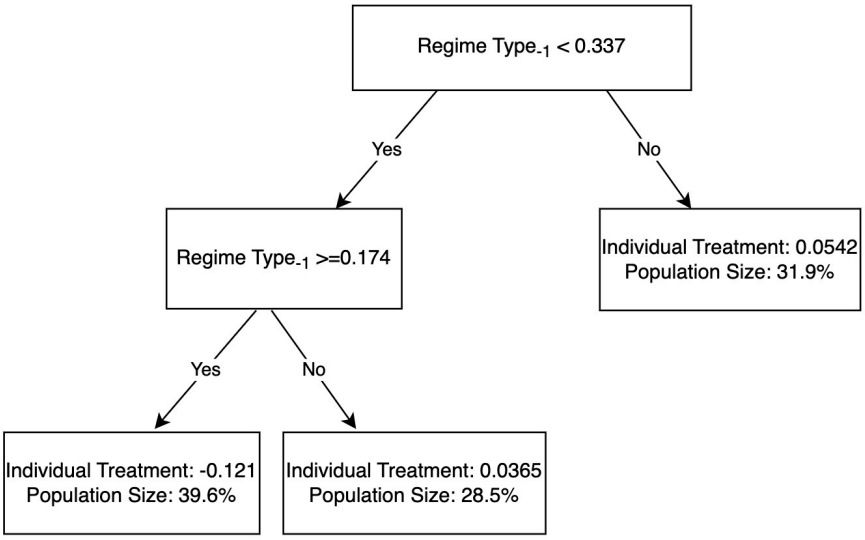


Figure 6.2 presents the estimated regression tree from VT. Each box contains the population size of each category and the mean estimated *individual* differential treatment effect, which is the difference for an individual observation between being assigned a liberal vs. conservative judge. This is not the overall subgroup differential treatment effect, which is presented in Table 6.2.4. However, the overall subgroup differential treatment effect is estimated from the right hand side outcome (the "no" branch). This figure says that the difference in case outcome is greatest when a conservative rather than a liberal judge is assigned to country that has at least some democratic features (i.e., has a score of .337 or greater from the V-dem measure).

6.3 Appendix for Chapter 4

6.3.1 List of Countries Included in Analyses

- Argentina
- Belize
- Brazil
- Bulgaria
- Chile
- Colombia
- Dominican Republic
- Ecuador
- Egypt
- El Salvador
- Gabon
- Ghana
- Hungary
- Indonesia
- Iraq
- Jamaica
- Kazakhstan
- Lebanon
- Malaysia
- Mexico
- Pakistan
- Panama
- Peru
- Philippines
- Poland
- Russia
- Serbia
- South Africa
- South Korea
- Sri Lanka
- Tunisia
- Turkey
- Ukraine
- Uruguay
- Venezuela
- Vietnam

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