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13 February 2020

Online at <https://mpra.ub.uni-muenchen.de/105575/>
MPRA Paper No. 105575, posted 27 Jan 2021 08:45 UTC

Leaders' Foreign Travel and Foreign Investment Inflows

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Abstract

This paper examines the effect of foreign travel by the leader of a country or the head of state on the ability of the country to attract foreign capital, as reflected by foreign direct investment inflows. The key difficulty in determining a causal effect is the issue of endogeneity. As much as the leader's trips abroad may attract foreign capital inflows, it is also possible that leaders are tempted to visit countries known to have a high level of investment out of their borders. To deal with potential endogeneity, we use instrumental variable panel estimation techniques. The GMM estimation shows that the leader's trips to the United States have a statistically significant positive coefficient on foreign direct investment inflows from the United States and total foreign investment inflows as well. This result implies that these trips by the leaders allow them the opportunity to attract foreign capital from the United States. This also implies that the decision by American firms to invest in the country send a strong signal of the confidence they have in that economy. This may encourage non-American companies to invest there as well.

JEL Code : F21, F23, H11

Keywords : International Investment, Foreign Direct Investment, Executive

« Partout où je vais tout le monde veut avoir des nouvelles du Congo (...) Je fais un travail, ensemble avec mes collaborateurs de chercher des investisseurs, les rassurer, etc. Nous allons continuer. Nous n'allons pas les écouter. Ils avaient promis de tout faire pour que les investisseurs ne viennent pas au Congo. Nous avons pensé qu'ils sont des frères alors qu'ils sont des sorciers...

*Je ris souvent quand j'écoute la polémique sur le voyage présidentiel. On a ramené plus d'un milliard et demi de dollars grâce à ces voyages, et je vais poursuivre pour ramener les investisseurs au Congo ».*¹

Speech by the President of the DRC, Félix Tshisekedi, to the Congolese diaspora in Paris (11/11/2019)

1. Introduction

This paper examines the effect of the number of foreign trips by the leader of the country, or the head of the government, on foreign direct investment inflows. To be specific, this paper investigates whether foreign travel by a country's leader allows the country to attract more foreign capital and to entice foreign firms to invest in their economy. This is the first attempt in the literature to consider the number of trips by heads of state as a determinant of foreign direct investment.

To achieve its objective, the paper uses a novel variable that indicates the number of trips by a leader, or a head of a government, to the United States of America. This variable is derived from the historical archives of the U.S. Department of State from 1960-2015. The paper examines the effect of the number of leader's trips to the United States on foreign direct investment using panel estimation techniques. The baseline results, using pooled Ordinary Least Squares and Fixed Effects estimations, show that the number of leaders' trips does not have a statistically significant coefficient.

¹ Translation : « Everywhere I go everyone wants to hear from the Congo (...) I do a job, together with my colleagues, to seek investors, reassure them, etc. We will continue. We are not going to listen to them. They promised to do everything to prevent investors from coming to the Congo. We thought they were brothers when they were wizards ... I often laugh when I listen to the controversy over the presidential trip. We brought in over a billion and a half dollars through these trips, and I'm going to continue to bring investors back to the Congo. »

However, the key difficulty in determining a causal effect is the issue of endogeneity. First, the association may be spurious due to a failure to account for an unobserved variable that may determine both leader's trips and foreign direct investment inflows. Second, as much as the leader's trips abroad may attract foreign direct investment inflows, it is also possible that leaders are tempted to visit countries known to have a high level of investment out of their borders. In this case, the United States is one of the countries with is a significant capital outflow seeking a better return. Thus, leaders would tend to travel there to attract American capital to their countries. This highlights an issue of reverse causality.

To deal with potential endogeneity, we use instrumental variable techniques for panel data such as the Anderson and Hsiao (1982) instrumental variable approach and the Arellano and Bond (199) Generalized Method of Moments estimation. The results show that the leaders' trips to the United States have a statistically significant positive effect on foreign direct investment inflows from the United States. This is robust even after the inclusion of other control variables. We also focus on the effect of the leader's trips on total foreign direct investment inflows. Our results are robust and similar to those on the effect of the leader's trips on American foreign direct investment inflows.

There are few studies that focus on the political and economic consequences of leader's visits. For instance, Nitsch (2007) examines the effect of state visits on international trade. The author finds that state and official visits are positively correlated with exports, and that there is a strong short-lived effect of visits on bilateral exports growth. Goldsmith and Horiuchi (2009) examine whether U.S. high-level visits to foreign countries affect public opinion in those countries. The authors find that the effect of these visits is initially large and positive, but eventually "exhibited a backlash effect." Our paper differs from these studies in its attempt to examine the effect of leader's visits on foreign direct investment. Thus, this paper's contribution to the pertinent literature is twofold. The paper is the first attempt to

examine the effect of foreign travel by heads of state as a determinant of foreign direct investment inflows. The second contribution of the paper is that it is also one of the first to highlight the economic consequences of a country's leader's trips abroad.

The remainder of the paper is organized as follows: section 2 discusses the hypothesis, section 3 surveys the literature, section 4 includes the detailed description of the data, section 5 includes the empirical estimation and the robustness tests, and section 6 concludes. References, tables and figures are included thereafter.

2. Hypothesis

Leaders and heads of governments travel abroad for a plethora of purposes. One of the most important reasons is to strengthen bilateral economic ties between their country and the countries they are visiting. These economic ties can be fostered by increasing trade and commercial exchange, attracting foreign capital inflows and foreign aid, containing any potential political disputes or border conflicts, and facilitating travel and cultural exchange between the citizens of the two countries. In the context of this paper, these foreign trips allow the leaders to meet with potential foreign officials and investors, to present to them the investment opportunities available in their countries, to persuade them to invest in their economies, to highlight the concessions and incentives that can be afforded to foreign investors, to bargain with them over the terms of their investment, and to negotiate for better economic outcomes for their country. If this effort pays off, these trips can lead to an increase in foreign direct investment inflows. For instance, Kerner and Lawrence (2014) show that bilateral investment treaties with the United States, that are usually signed by high level officials, correlate positively with investments in fixed capital.

Frequent visits to the United States also allow the leaders to interact with American political and economic influential figures. The direct interaction and interpersonal contact

with these figures allow the leaders to cultivate close ties that they can depend on after returning to their home countries. Leaders can, thus, use their influential connections and close contacts in the United States to lobby for foreign capital and to broker deals through formal and informal channels with American firms. This can lead the leader's trips to increase foreign direct investment inflows as well. This is consistent with the arguments in Gift and Krcmaric (2017) who discuss the "socialization" and "transnational linkages" cultivated by leaders during their experiences abroad.

From the point of view of multinational corporations, foreign investors can take the trip of the head of state as a strong signal from the highest levels of a country's leadership for their serious commitment to facilitate foreign capital flows, to offer concessions to foreign firms, to ensure the security of foreign property, and to spend on the essential infrastructure for this type of investment. Thus, we would expect that the number of leaders' trips to be positively associated with foreign direct investment. This is especially the case as multinational corporations are seen to be interested in high level diplomatic and foreign policy interactions. As stated in the Harvard Business Review²: "In this new reality, the most successful multinational companies will be those that make expertise in international affairs central to their operations, adopting what can best be described as a corporate foreign policy. Such a policy will have two goals: to improve a company's ability to operate in foreign environments through effective corporate diplomacy, and to ensure its success wherever it is engaged through careful geopolitical due diligence." The article also states that companies "must cultivate wide and deep relations with both government and society. Wherever they wish to operate, they must identify the various stakeholders, understand which groups may be supportive of company goals and which are likely to protest or oppose them, and develop strategies to engage each constituency effectively." This implies that it is imperative for these

² Chipman, John. "Why Your Company Needs a Foreign Policy." Harvard Business Review, September, 2016.

corporations to be aware of the events in the global arena, and in particular in the countries they plan to invest in. The visit of the leader of that country to the United States is obviously an event that cannot be ignored by a corporation pondering whether to invest in that country.

Multinational corporations also have an influence on American foreign policy through lobbying. Kim and Milner (forthcoming) use a dataset on lobbying activities of public firms in the United States, and find strong evidence for an increase in lobbying expenditures when firms become multinational on a diverse set of foreign policy issues. Their finding suggests “that MNCs are important political actors whose distinct interests and influence should be incorporated into our understanding of foreign policy-making.” This implies that if multinational corporations are interested in investing in an economy, they can lobby for diplomatic support to their efforts that can culminate in extending an invitation to the leader of that country to visit the United States. This implies that these visits may lead to a conclusion of agreements that facilitate the investment of American firms in the visiting leader’s country. Thus, the leader’s trips can increase foreign direct investment inflows.

Besides lobbying by these firms, U.S. foreign policy adopts an approach of extending support to American firms overseas. According to a report by the U.S. Government Accountability Office³: “U.S. embassies furnish assistance to U.S. firms overseas, including diplomatic support;” It would come as no surprise that this continuous effort by American embassies can be supported by diplomatic invitations to the country’s leader to visit the United States. This is because the decisions in many countries to facilitate foreign capital flows are solely in the hands of the country’s leadership. Thus, the leader’s trips to the United States can attract American capital to their countries.

³ U.S. Foreign Relations and Multinational Corporations: What's the Connection? PAD-78-58; B-172255. August 23, 1978.

On the other hand, the travel of the head of the government is costly. Leaders usually travel with a large entourage that includes security personnel, policy makers, public officials, expert advisors, private entrepreneurs, staff of the presidential cabinet, members of the press corps and others. These trips are a burden on the coffers of the state due to the need to cover the cost of traveling, lodging, security, transportation, and meetings of the leaders and their retinue. These costly trips increase the opportunity cost for the social and physical infrastructure essential for foreign investment. This can include human capital investment spending that improves the level of skills of domestic workers who can potentially be employed by foreign companies, in addition to spending on the infrastructure for transportation, communication and utilities that are essential for any type of investment. Thus, the leaders' trips can lead to a crowding out effect where an increase in these costly trips abroad may lead to a reallocation of resources away from productive spending that is essential for investment. In addition to the direct cost of the trip, these trips will also take the officials who accompany the leaders away from their other duties for a longer period of time. This may adversely affect their efforts to create a friendly environment for foreign corporations. Thus, these trips can decrease foreign direct investment inflows.

Leaders who travel a lot can also send a negative signal to investors. These trips can be interpreted as a lack of seriousness in dealing with the challenges that these countries face, or lack of commitment to implement reforms needed to attract foreign capital, or lack of interest in spending on the social and physical infrastructure necessary for foreign investment. These trips, and the leader's direct involvement, can also signal the inefficiencies of the other institutions that are supposed to be in the forefront of the efforts of attracting foreign capital, such as the chambers of commerce, the diplomatic corps, or any government agencies in charge of attracting foreign investments. Thus, we would expect that the leaders' trips to have an adverse effect on foreign direct investment.

Given that the effect of the number of leaders' foreign trips on foreign direct investment inflows is inconclusive, an empirical analysis is warranted.

3. Literature

This paper contributes to the literature on the determinants of foreign direct investment. Studies in this literature emphasize the significance of several determinants such as the level of economic and financial development, the suitability of infrastructure, the level of human capital, the quality of institutions, and democratic governance.

Some studies focus on the effect of institutional quality on foreign direct investment. These institutions offer protection for the property of foreign firms, protect foreign investors from the risk of expropriation, limit bribery payments to corrupt public officials, allow foreign firms to enforce contracts, and allows for the judicial independence needed for litigation in case of dispute with a domestic entity. In this context, Du et al. (2008) examine the impact of institutions, including property rights protection and contract enforcement, on the location choice of foreign direct investment. The authors find that U.S. multinationals prefer to invest in Chinese regions that have better protection of intellectual property rights, less government intervention in business operations, less corruption, and better contract enforcement. Du et al. (2012) compare the sensitivity of the location choice of foreign direct investment toward the variation in institutional quality across China. The authors find that enterprises from source countries that are culturally more distant from China exhibit a stronger aversion to regions with weaker institutions. Busse and Hefeker (2007) explore the connection between political risk, institutions, and FDI inflows. Their results show that political stability, internal and external conflict, corruption, ethnic tensions, law and order, government accountability, and quality of bureaucracy are significant determinants of FDI inflows. Asiedu et al. (2009) examine the effect of the risk of expropriation on FDI inflows.

The authors show that the threat of expropriation decreases FDI inflows, and that foreign aid mitigates the adverse effect of expropriation risk but cannot eliminate it entirely.

Other studies focus on the effect of the democratic system of governance on the ability of the country to attract foreign capital. On one hand, democratic institutions hinder foreign capital inflows by limiting the monopolistic approach of multinational corporations, by protecting domestic investors from foreign competition, and by constraining host governments' desire to offer generous financial incentives and fiscal concessions to foreign investors. On the other hand, democratic institutions may promote foreign capital inflows by ensuring more credible property rights protection and by reducing the risk of expropriation.

In this context, Li and Resnick (2003) find that democracy enhances property rights protection which indirectly encourages FDI inflows. The authors also find that after controlling for their positive effect through property rights protection, democracy also decreases FDI inflows. Li (2009) shows that democratic governments are most likely to expropriate foreign investment when leaders face little political constraints and when their countries experience frequent leadership turnover. The author also finds that autocrats are least likely to expropriate foreign assets when they face high political constraints and have stayed in power for a long time. Harms and Ursprung (2002) explore whether political repression boosts foreign investment. The authors arrive at the conclusion that multinational enterprises appear to be attracted by countries in which civil rights and political freedoms are respected. Asiedu and Lien (2011) examine whether the abundance of natural resources in host countries alter the relationship between democracy and FDI. The authors find that democracy increases FDI inflows if the share of minerals and oil in total exports is less than some critical value.

Other studies examine the effect of various types of policies on the ability to attract foreign capital. Some of these policies have direct implications on foreign investors, such as capital controls, while others aim at implementing economic reforms that might attract foreign firms. For instance, Asiedu and Lien (2003) examine the effect on FDI of different types of capital control policies such as the existence of multiple exchange rates, restrictions on capital account, and restrictions on the repatriation of export proceeds. The authors show that in the 1970s and 1980s, none of these policies had a significant effect on FDI, while in the 1990s all were significant. The authors also find that capital controls have no effect on FDI to sub-Saharan Africa and the Middle East, but affects FDI to East Asia and Latin America negatively. Asiedu (2006) shows that lower inflation, suitable infrastructure, higher human capital, openness to FDI, less corruption, political stability and a dependable legal system have a positive effect on FDI. These findings suggest that countries can attract FDI by improving their institutional and policy quality. Asiedu (2002) explores whether factors that determine FDI affect countries in sub-Saharan Africa differently. Their analysis confirms that better infrastructure has no significant effect on FDI to sub-Saharan Africa, while trade openness promotes FDI to all developing countries even though the marginal benefit is less for sub-Saharan Africa. Gastanaga et al. (1998) examine the effects of different policy variables and find a particular positive effect of trade openness on foreign direct investment.

Other studies explore the importance of human capital as countries can enhance their attractiveness as locations for FDI by pursuing policies that increase the level of local skills and labor force capabilities. In this context, Noorbakhsh et al. (2001) find that human capital is a statistically significant determinant of FDI inflows, is one of the most critical determinants, and its importance has increased over time. Cleeve et al. (2015) assess the role of human capital on FDI inflows to sub-Saharan Africa. Their analysis shows that human capital has a significant influence on FDI, but no evidence of the increasing importance of

human capital on the type of FDI flowing to sub-Saharan Africa. Francois et al. (forthcoming) who find that greater educational attainment of the leader of the country is associated with higher FDI, and that the leader having tertiary education in economics and prior experience in business is associated with greater FDI. Asiedu et al. (2015) examine the relationship between HIV/AIDS and foreign direct investment. The authors find that HIV/AIDS has a negative but diminishing effect on FDI.

Besides economic development, some studies argue that the level of financial development is also essential in attracting foreign direct investment. Desbordes and Wei (2017) find that both source and destination financial development have a large positive influence on greenfield, expansion, and mergers and acquisitions FDI, by directly increasing access to external finance and indirectly encouraging manufacturing activities. There are also studies that examine the effect of social capital on economic exchange between countries. Guiso et al. (2009) examine how bilateral trust between European countries affects their trade and financial flows. The authors find that lower bilateral trust leads to less trade between two countries, less foreign portfolio investment, and less foreign direct investment.

The contribution that is closest to ours is Constant and Tien (2010) who examine whether foreign-educated African leaders attract more foreign direct investment to their country. Their analysis shows that leaders' foreign education promotes foreign direct investment, indicating the role of networks and connections that these leaders cultivate while studying abroad. Our paper, however, differs from this study in terms of focusing on the leaders' foreign travel rather than the leader's foreign education. Thus, our study is more concerned about the networks and connections that the leaders cultivate during their travels abroad rather than those established during their education abroad. We argue that our channel is pertinent as the networks created during the leader's education abroad might not be with those foreign figures that will eventually influence bilateral economic and commercial ties

between the two countries. However, the connections made during the leader's trips are with those policy makers and entrepreneurs who are directly in charge of these decisions. Another contribution close to our is Kerner and Lawrence (2014) who show that bilateral investment treaties with the United States correlate positively with investments in fixed capital and have little, if any, correlation with other measures of multinational corporations activity. Our paper differs from this study by arguing that these treaties are more likely to be signed during a high profile visit of the leader of the country to the United States.

3. Data

The estimates are based on a 5-year panel. This is because foreign direct investment decisions undertaken by multinational corporations are not likely to be the outcome of factors occurring more than a few years prior. Mosley (200) show very short time horizons of less than a few years for decisions by portfolio investors, while Hayashi (1978) suggests that the time horizon of multinationals are less than 10 years. Table 1 presents the descriptive statistics for all the variables used in the analysis.

The dependent variable in our analysis is foreign direct investment from the United States. This data is derived from the U.S. Bureau of Economic Analysis⁴. The data provides the value of direct investment in the United States by overseas investors and the value of U.S. investment in other countries. We use the value of U.S. investment in other countries⁵ which

⁴ <https://www.bea.gov/data/intl-trade-investment/direct-investment-country-and-industry>

⁵ Countries included are : Algeria, Argentina, Australia, Austria, Bahrain, Belgium, Benin, Bolivia, Botswana, Brazil, Burundi, Cameroon, Canada, Central African Republic, Chad, Chile, China, Colombia, Congo. Dem. Rep., Congo. Rep., Costa Rica, Cote d'Ivoire, Cuba, Cyprus, Czech Republic, Denmark, Dominican Republic, Ecuador, Egypt. Arab Rep., El Salvador, Fiji, Finland, France, Gabon, Gambia. The, Germany, Ghana, Greece, Guatemala, Guinea-Bissau, Guyana, Honduras, Hungary, India, Indonesia, Iran, Ireland, Israel, Italy, Jamaica, Japan, Jordan, Kenya, Korea. Rep., Lesotho, Liberia, Luxembourg, Madagascar, Malawi, Malaysia, Mali, Mauritania, Mauritius, Mexico, Morocco, Netherlands, New Zealand, Nicaragua, Niger, Nigeria, Norway, Oman, Pakistan, Panama, Papua New Guinea, Peru, Philippines, Poland, Portugal, Rwanda, Saudi Arabia, Senegal, Sierra Leone, Singapore, South Africa, Spain, Sri Lanka, Sudan, Swaziland, Sweden, Switzerland, Thailand, Togo, Trinidad and Tobago, Tunisia, Turkey, United Arab Emirates, United Kingdom, Uruguay, Venezuela, and Zimbabwe.

starts from 1966. So the panel used is from 1966-70, 71-75, 76-80, 81-85, 86-90, 91-95, 96-00, 01-05, 06-10, and 11-15.

To consider total foreign direct investment inflows, we use foreign direct investment inflow as a percentage of Gross Domestic Product⁶. This is derived from the World Development Indicators. For foreign direct investment, we use a 5-year panel as follows: 71-75, 76-80, 81-85, 86-90, 91-95, 96-00, 01-05, 06-10 and 11-15.

The variable of interest is leaders' trips, which is calculated as the number of trips by the government's leader to the United States of America during the period 1960-2015. These include state visits, official working visits, summits, private visits, informal visits, meetings, and working visits. This data is derived from the Office of the Historian, which is affiliated with the Department of State of the United States of America⁷. Figure 1 shows a world map of leader's trips to the United States during the period 1960-2015. Several control variables are used in the analysis. These are variables identified in the literature as determinants of foreign direct investment. Appendix A presents the data source and description of all the variables used in this study.

⁶ The countries included in the analysis are: Afghanistan, Albania, Algeria, Angola, Argentina, Armenia, Australia, Austria, Azerbaijan, Bahrain, Bangladesh, Belarus, Belgium, Benin, Bhutan, Bolivia, Botswana, Brazil, Bulgaria, Burkina Faso, Burundi, Cape Verde, Cambodia, Cameroon, Canada, Central African Republic, Chad, Chile, China, Colombia, Comoros, Congo. Dem. Rep., Congo. Rep., Costa Rica, Cote d'Ivoire, Croatia, Cyprus, Czech Republic, Denmark, Djibouti, Dominican Republic, Ecuador, Egypt. Arab Rep., El Salvador, Equatorial Guinea, Eritrea, Estonia, Ethiopia, Fiji, Finland, France, Gabon, Gambia, Georgia, The, Germany, Ghana, Greece, Guatemala, Guinea, Guinea-Bissau, Guyana, Haiti, Honduras, Hungary, India, Indonesia, Iran, Iraq, Ireland, Israel, Italy, Jamaica, Japan, Jordan, Kazakhstan, Kenya, Korea. Rep., Kuwait, Kyrgyz Republic, Lao PDR, Latvia, Lebanon, Lesotho, Liberia, Libya, Lithuania, Luxembourg, Macedonia, Madagascar, Malawi, Malaysia, Mali, Mauritania, Mauritius, Mexico, Republic of Moldova, Mongolia, Montenegro, Morocco, Mozambique, Myanmar, Namibia, Nepal, Netherlands, New Zealand, Nicaragua, Niger, Nigeria, Norway, Oman, Pakistan, Panama, Papua New Guinea, Paraguay, Peru, Philippines, Poland, Portugal, Qatar, Romania, Russian Federation, Rwanda, Saudi Arabia, Senegal, Sierra Leone, Singapore, Slovak Republic, Slovenia, Solomon Islands, South Africa, Spain, Sri Lanka, Sudan, Swaziland, Sweden, Switzerland, Tajikistan, Tanzania, Thailand, Togo, Trinidad and Tobago, Tunisia, Turkey, Turkmenistan, Uganda, Ukraine, United Arab Emirates, United Kingdom, Uruguay, Uzbekistan, Venezuela, Vietnam, Yemen, Zambia, and Zimbabwe.

⁷ <https://history.state.gov/departmenthistory>.

4. Estimation

This section conducts an empirical estimation of the effect of the number of leaders' trips to the United States of America on foreign direct investment inflows to their country during the period 1960-2015. Figure 2 shows a positive relationship between the number of leader's trips and foreign direct investment inflows from the United States. To explore this relationship we use the following equation

$$FDI_{it} = \theta + \delta_i LeadersTrips_{it-1} + \mathfrak{N}_{it-1}\gamma + \mu_i + \sigma_t + e_{it} \quad (1)$$

FDI_{it} is foreign direct investment flows from the United States to country i in year t . $LeadersTrips_{it-1}$ is the number of trips by the leader of country i to the United States in year $t-1$. \mathfrak{N}_{it-1} is a vector of control variables of country i in year $t-1$. The vector of control variables includes those commonly identified in the literature as determinants of foreign direct investment. Thus, we control for the total natural resources rents as a percentage of GDP, the logarithm of GDP per capita, annual GDP growth rate, trade openness, the inflation rate, and the level of democracy. The μ_i denotes a full set of country dummies, the σ_t denotes a full set of time effects that capture common shocks to foreign direct investment of all countries, and e_{it} is an error term capturing all other omitted factors, with $E(e_{it}) = 0$ for all i and t .

4.1. Baseline Results

To collect the variable on leaders' trips, we use historical data from the Department of State of the United States of America. We use the number of leaders' trips to the U.S.A. from 1960 to 2015. Initially, the objective was to use the total number of leaders' trips to all countries. However, the unavailability of this type of data did not allow us to have such a distribution. Thus, instead of considering all destination countries we only consider leaders' trips to the main country with capital outflows. This is a fact that deserves to be emphasized as the United States is identified as a major investor according to (OECD 2020). This fact can justify our focus on travel by leaders to the United States.

The baseline results are included in table 2. Columns 1-3 of table 2 include the Pooled OLS and the Fixed Effects OLS results using White (1980) heteroskedasticity correction. Columns 4-6 of table 2 include the Pooled OLS and the Fixed Effects OLS results using robust standard errors clustered by country. The Pooled OLS is identical to our regression equation except for the omission of the fixed effects that reflect country dummies. These country dummies capture any time-invariant country characteristics that affect foreign direct investment. When the true model is given by our regression equation, Pooled OLS estimates are biased and inconsistent. In this context, the fixed effects estimator is more consistent. The results in table 2 of the Pooled OLS and Fixed Effects show that the coefficient of leader's trips does not have a statistically significant effect in all specifications. However, we do not assume that these estimations indicate a causal effect of leader's trips on foreign direct investment. In the following section, we conduct an instrumental variable strategy to account for this issue.

4.2. Endogeneity

The relationship found so far assumes that the leaders' trips are exogenous to foreign direct investment. However, the problem of endogeneity cannot be ignored. First, the association may be spurious due to the failure to account for an unobserved channel which is affecting both variables. It is likely that economies that are different for a variety of causes will differ both in the number of leaders' trips and their foreign direct investment inflows as well. Second, our leader's trips variable only considers travel to the United States. This country is among the countries where there is a significant outflow of capital seeking a better return. In this sense, political leaders would be tempted to travel there. This means that as much as a larger number of leader's trips can attract more foreign capital, it is also possible that leaders are tempted to travel to countries known to be major investors out of their borders such as the United States. This highlights the possibility of reverse causality.

To solve this issue, we need a source of exogenous variation in leader's trips by using an instrumental variable approach. To account for these sources of potential endogeneity, we implement two estimation techniques. The first is the Anderson and Hsiao (1982) approach. This technique eliminates the fixed effects by taking first differences, and then conducts instrumental variable estimation using lagged values as instruments. Column 7 of table 2 includes the results of the Anderson and Hsiao (1982) estimation. The results show that the coefficient of the leader's trips does not have a statistically significant effect on foreign direct investment inflows.

However, the Anderson and Hsiao (1982) estimator does not exploit all the pertinent moment conditions. Arellano and Bond (1991) develop a generalized method of moments GMM estimator using all of these moment conditions. When these conditions are valid, this GMM estimator is more efficient than the Anderson and Hsiao (1982) estimator. In the Arellano and Bond (1991) technique, first differences of the regression equation are taken to eliminate the individual effects. Then, lags of the dependent variable are used as instruments for differenced lags of the dependent variable. Therefore, we estimate the following equation

$$FDI_{it} = \theta + \delta_i LeadersTrips_{it-1} + \sigma_i FDI_{it-1} + \mathfrak{X}_{it-1} \gamma + \mu_i + \sigma_t + e_{it} \quad (3)$$

The standard techniques that can be employed for panel estimation, such as fixed effects and random effects, cannot be used in this case. The problem with these techniques is that the equation contains a lagged endogenous variable, which is the lagged FDI indicator. In this case, estimation by fixed effects and random effects is not consistent. In addition, we also have the problem of endogeneity of leader's trips. To deal with potential endogeneity and the lagged dependent variable, we use the Arellano and Bond (1991) estimation technique. This GMM estimator first-differences each variable so as to eliminate the country specific effect and then uses all possible lagged values of each of the variables as instruments. This not only corrects for the bias introduced by the lagged endogenous variable but also allows for a certain degree of endogeneity in the other explanatory variables.

Column 8 of table 2 shows the results of the Arellano and Bond (1991) dynamic GMM estimation. In addition, column 9 of table 2 shows the results of the Arellano and Bond (1991) systems GMM estimation. When the variance of the individual effect term across individual observations is high, then the Arellano–Bond (1991) estimator may perform poorly in finite samples. Blundell and Bond (1998) derived a condition under which it is possible to use an additional set of moment conditions. These additional moment conditions can be used to improve the small sample performance of the Arellano–Bond (1991) estimator. This method is referred to as systems GMM.

The results show a positive and statistically significant coefficient for leader’s trips. The coefficient of the leaders’ trips variable is 0.107. This implies that a one standard deviation increase in the number of leaders' trips to the United States translates into an increase in foreign direct investment by 0.23.

4.3. Before and after the end of the Cold War

We also conduct some tests to check the robustness of our results. The first test compares the effects of the leader’s trips on foreign direct investment before and after the end of the cold war. This is because the confrontational climate during the cold war caused countries around the world to attempt to cope with a highly antagonistic environment, and to survive in a global arena squeezed between the conflicting interests of the two super powers. This implies that high level visits to the United States likely focused on geopolitical developments in the context of the cold war rather than on strengthening bilateral ties through the promotion of trade exchange or capital flows. In addition, many countries became independent after the collapse of the Soviet Union at the end of the cold war. This implies that there are more countries whose leaders are interested in visiting the United States, and are eager to strengthen bilateral relationships through trade and capital flows.

The results are included in table 3, and show that the leader's trips to the United States do not have a significant effect on foreign direct investment inflows before the end of the cold war, but has a statistically significant positive effect after the end of the cold war. This implies that during the cold war, leader's trips to the United States were more focused on discussing other geostrategic issues than promoting economic ties. However, after the end of the cold war these trips seem to be focused on strengthening bilateral economic ties through attracting American capital.

4.4. Effect on total FDI

So far, we focused on the inflow of American foreign direct investment. In this section, we examine whether the leader's trips to the United States affect total foreign direct investment inflows, regardless of the origin. This is because attracting American capital can send a strong signal to other foreign multinational corporations of the confidence American firms have in that economy. This could induce more non-American foreign corporations to decide to invest in that country as well.

To consider this effect, we run the regression with total foreign direct investment inflows as our dependent variable. Table 4 includes the baseline results and show a statistically positive significant effect of leader's trips when we use the Arellano and Bond (1991) systems GMM estimation, as shown in column 9. In column 9, the coefficient of the leaders' trips variable is 0.571. This implies that a one standard deviation increase in the number of leaders' trips to the United States translates into an increase in foreign direct investment by 1.23.

We also conduct similar robustness tests to those we presented earlier, while focusing on the effect of the leader's trips on total foreign direct investment inflows. We also examine the effect of the leader's trips before and after the end of the cold war. Table 5 shows that the

effect is positive and statistically significant only after the end of the cold war. These findings are similar to our earlier results.

5. Conclusion

This paper examines the effect of foreign travel by the leader or the head of state on the ability of the country to attract foreign capital, as reflected by foreign direct investment inflows from the United States. To deal with potential endogeneity, the Arellano and Bond (1991) GMM estimation shows that the leader's trips variable has a statistically significant positive coefficient. This result implies that these trips by the leaders allow them the opportunity to attract foreign capital. This is particularly the case after the end of the cold war. We find similar results when we focus on the effect of the number of leader's trips on total foreign direct investment inflows. This implies that the decision by American firms to invest in the country send a strong signal of the confidence they have in that economy. This may encourage non-American companies to invest there as well.

Future research can explore the effect of leader's trips on trade inflows, foreign portfolio investment, foreign aid, and foreign debt. Future scholarly endeavors can also explore the possibility of expanding the data set of the number of leaders' trips to other countries besides the United States.

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Table 1. Summary Statistics

Variable	Obs	Mean	Std. Dev.
Leaders' trip to USA	1,570	1.526752	2.157202
FDI, net inflow	1,195	3.051363	5.325316
Inflation	1,419	38.8236	292.4955
Total natural resources rents (% of GDP)	1,281	8.276036	11.27628
Log of GDP per capita	1,449	8.063406	1.540387
Trade openness	1,438	36.38039	23.30941
GDP growth (annual %)	1,422	3.983719	4.573222
Democracy	1,540	1.014654	7.275895
US FDI, net inflow	686	.5438134	1.427739

Figure 1. World Map of Leader's Trips

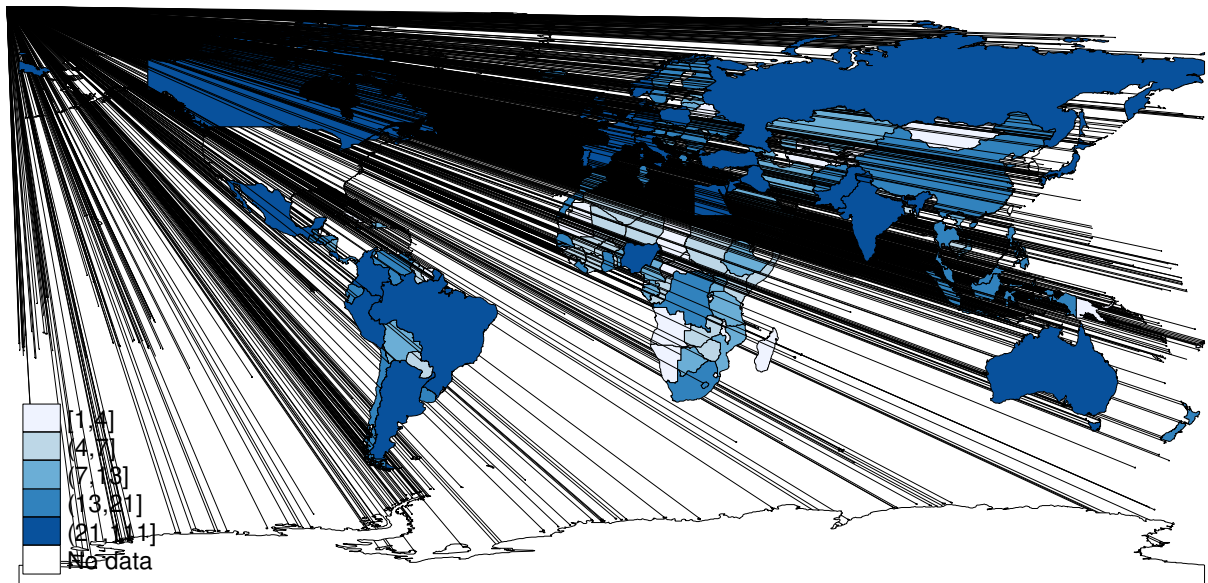


Figure 2. Leaders' Trips and U.S. FDI

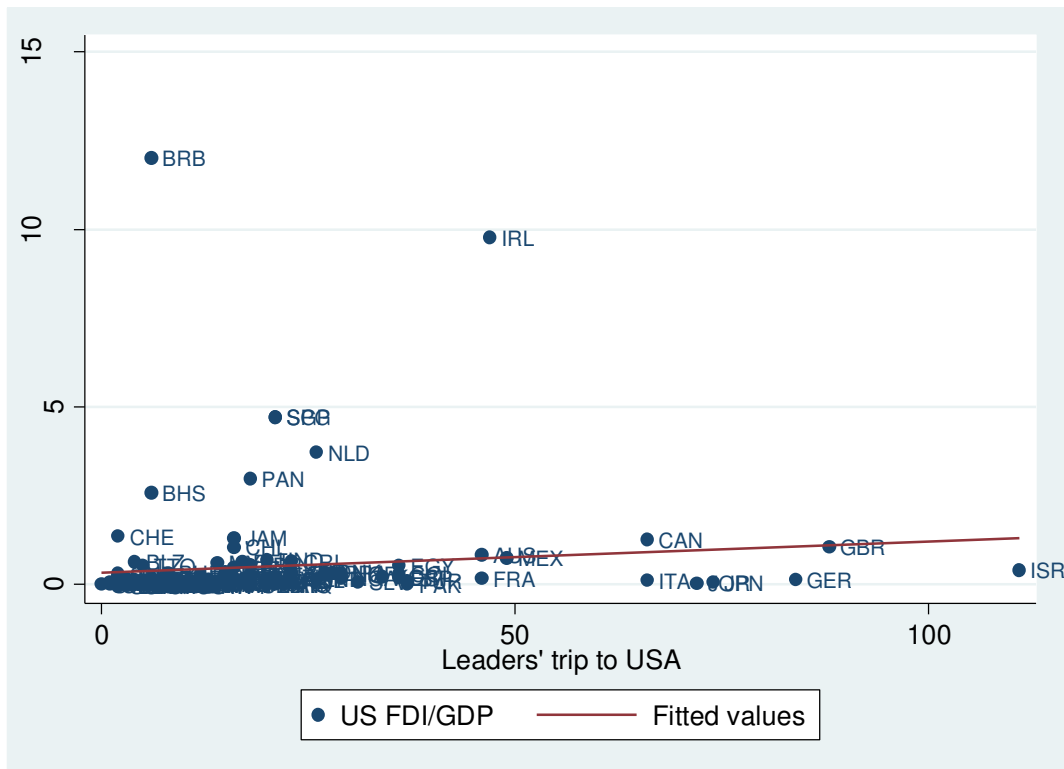


Table 2. The effect of leader's trips on FDI from U.S.A.

	Pooled OLS (1)	Fixed effects OLS (2)	Fixed effects OLS (3)	Pooled OLS (4)	Fixed effects OLS (5)	Fixed effects OLS (6)	Anderson-Hsiao IV (7)	Arellano-Bond GMM (Dynamic) (8)	Arellano-Bond GMM (System) (9)
Leaders' trips to USA _{<i>t-1</i>}	0.038 (0.024)	0.024 (0.024)	0.025 (0.024)	0.038 (0.033)	0.024 (0.034)	0.025 (0.034)	-0.137 (0.273)	0.120 (0.119)	0.107*** (0.040)
Openness _{<i>t-1</i>}	0.023*** (0.005)	0.022*** (0.005)	0.022*** (0.005)	0.023*** (0.007)	0.022*** (0.007)	0.022*** (0.007)	0.102 (0.171)	0.003 (0.014)	0.010*** (0.002)
Log of GDP per capita _{<i>t-1</i>}	0.047 (0.047)	0.035 (0.044)	0.034 (0.044)	0.047 (0.059)	0.035 (0.056)	0.034 (0.057)	1.776 (9.759)	0.090 (0.482)	0.005 (0.049)
Inflation _{<i>t-1</i>}	0.000** (0.000)	0.000 (0.000)	0.000 (0.000)	0.000** (0.000)	0.000 (0.000)	0.000 (0.000)	-0.001 (0.002)	-0.000 (0.000)	0.000 (0.000)
GDP growth (annual %) _{<i>t-1</i>}	-0.028 (0.025)	-0.027 (0.025)	-0.025 (0.025)	-0.028 (0.024)	-0.027 (0.025)	-0.025 (0.025)	0.168 (0.620)	-0.087** (0.044)	-0.057*** (0.020)
Total natural resources rents (% of GDP) _{<i>t-1</i>}	-0.026** (0.010)	-0.028** (0.011)	-0.028*** (0.011)	-0.026* (0.015)	-0.028* (0.015)	-0.028* (0.016)	0.669 (1.216)	-0.007 (0.015)	-0.019*** (0.007)
Democracy _{<i>t-1</i>}	-0.009 (0.010)	-0.017 (0.011)	-0.017 (0.011)	-0.009 (0.011)	-0.017 (0.012)	-0.017 (0.012)	-0.220 (0.598)	-0.008 (0.027)	-0.018* (0.010)
FDI ₍₋₁₎								0.407*** (0.080)	0.642*** (0.044)
Countries	No	No	YES	No	No	YES	No	No	No
Years	No	Yes	Yes	No	Yes	Yes	Yes	No	No
Constant	-0.486 (0.367)	-0.601 (0.416)	-0.668 (0.412)	-0.486 (0.500)	-0.601 (0.544)	-0.668 (0.514)	-3.772 (5.665)		-0.105 (0.389)
Hansen J test								0.155	0.000
AR(2) test								0.172	0.000
Number of observations	468	468	468	468	468	468	369	361	457
R2	0.178	0.201	0.202	0.178	0.201	0.202	.		

note: .01 - ***; .05 - **; .1 - *; Columns 1, 2 and 3 are estimated using White (1980) heteroskedasticity correction. Pooled cross-sectional OLS and Fixed effects OLS estimations in columns 4, 5 and 6 with robust standard errors clustered by country in parentheses. Column 7 uses the instrumental variables technique of Anderson and Hsiao (1982), with White (1980) heteroskedasticity correction, and columns 8 and 9 use the GMM of Arellano and Bond (1991), with robust standard errors; in both methods we instrument for Leaders' trips to USA using a double lag.

Table 3. The effect of leader's trips on FDI from U.S.A. before and after the end of the cold war

	Before Cold War			After Cold War		
	Anderson-Hsiao IV (1)	Arellano-Bond GMM (Dynamic) (2)	Arellano-Bond GMM (System) (3)	Anderson-Hsiao IV (4)	Arellano-Bond GMM (Dynamic) (5)	Arellano-Bond GMM (System) (6)
Leaders' trips to USA _{<i>t-1</i>}	0.203 (0.542)	-0.507* (0.297)	-0.184 (0.152)	-0.681 (1.349)	0.929** (0.411)	0.870*** (0.256)
Openness _{<i>t-1</i>}	-0.084 (0.167)	0.054 (0.034)	0.068*** (0.007)	0.449 (0.679)	-0.051 (0.110)	0.069*** (0.011)
Log of GDP per capita _{<i>t-1</i>}	1.588 (2.566)	-0.128 (1.261)	-0.071 (0.105)	-2.371 (25.206)	-3.346 (2.508)	-0.854*** (0.201)
Inflation _{<i>t-1</i>}	-0.008 (0.016)	-0.001** (0.000)	-0.000 (0.001)	-0.004 (0.011)	-0.000 (0.000)	0.000 (0.001)
GDP growth (annual %) _{<i>t-1</i>}	0.050 (0.106)	-0.070 (0.061)	-0.015 (0.032)	-0.268 (0.800)	-0.059 (0.155)	-0.134*** (0.049)
Total natural resources rents (% of GDP) _{<i>t-1</i>}	-0.016 (0.179)	0.003 (0.035)	0.045*** (0.016)	0.828 (3.815)	-0.019 (0.088)	0.018 (0.020)
Democracy _{<i>t-1</i>}	0.051 (0.167)	0.047 (0.054)	0.046** (0.022)	-0.033 (1.093)	0.233*** (0.080)	0.050 (0.037)
FDI ₍₋₁₎		-0.687 (0.556)	-0.429*** (0.118)		0.509 (0.497)	0.590*** (0.051)
Year	Yes	No	No	Yes	No	No
Constant	-0.262 (0.710)		0.063 (0.747)	9.736 (25.332)		4.876*** (1.174)
Number of observations	123	161	262	246	640	682
Hansen J test		0.162	0.000		0.035	0.000
AR(2) test			0.000		0.374	0.003

note: .01 - ***; .05 - **; .1 - *; Columns 1 and 4 uses the instrumental variables technique of Anderson and Hsiao (1982), with White (1980) heteroskedasticity correction, and columns 2, 3, 5 and 6 use the GMM of Arellano and Bond (1991), with robust standard errors; in both methods we instrument for Leaders' trips to USA using a double lag.

Table 4. The effect of leader's trips on total FDI.

	Pooled OLS (1)	Fixed effects OLS (2)	Fixed effects OLS (3)	Pooled OLS (4)	Fixed effects OLS (5)	Fixed effects OLS (6)	Anderson- Hsiao IV (7)	Arellano-Bond GMM (Dynamic) (8)	Arellano-Bond GMM (System) (9)
Leaders' trips to USA _{t-1}	0.137* (0.077)	0.088 (0.078)	0.085 (0.078)	0.137 (0.096)	0.088 (0.099)	0.085 (0.100)	-2.604 (16.047)	0.778** (0.372)	0.571*** (0.191)
Openness _{t-1}	0.120*** (0.017)	0.112*** (0.017)	0.113*** (0.017)	0.120*** (0.021)	0.112*** (0.021)	0.113*** (0.021)	-0.844 (3.371)	-0.054 (0.096)	0.051*** (0.008)
Log of GDP per capita _{t-1}	-0.435*** (0.156)	-0.332** (0.161)	-0.324** (0.161)	-0.435** (0.209)	-0.332 (0.226)	-0.324 (0.227)	-16.607 (143.352)	-2.912 (2.215)	-0.599*** (0.143)
Inflation _{t-1}	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.004 (0.011)	-0.000 (0.000)	0.000 (0.000)
GDP growth (annual %) _{t-1}	0.060 (0.060)	0.055 (0.062)	0.050 (0.062)	0.060 (0.040)	0.055 (0.037)	0.050 (0.039)	-0.050 (3.768)	-0.046 (0.124)	-0.094** (0.039)
Total natural resources rents (% of GDP) _{t-1}	0.060*** (0.023)	0.043* (0.024)	0.043* (0.024)	0.060* (0.032)	0.043 (0.034)	0.043 (0.034)	6.262 (31.418)	-0.007 (0.061)	0.018 (0.016)
Democracy _{t-1}	0.157*** (0.027)	0.105*** (0.027)	0.104*** (0.027)	0.157*** (0.037)	0.105*** (0.039)	0.104*** (0.039)	-4.644 (22.366)	0.203*** (0.062)	0.054* (0.028)
FDI ₍₋₁₎								0.521 (0.433)	0.603*** (0.043)
Countries	No	No	YES	No	No	YES	No	No	No
Years	No	Yes	Yes	No	Yes	Yes	Yes	No	No
Constant	1.189 (1.121)	-1.202 (1.374)	-0.767 (1.374)	1.189 (1.496)	-1.202 (1.882)	-0.767 (1.886)	-22.092 (110.119)		3.742*** (0.893)
Hansen J test								0.002	0.000
AR(2) test								0.683	0.045
Number of observations	991	991	991	991	991	991	834	801	944
R2	0.294	0.325	0.327	0.294	0.325	0.327	.		

note: .01 - ***; .05 - **; .1 - *; Columns 1, 2 and 3 are estimated using White (1980) heteroskedasticity correction. Pooled cross-sectional OLS and Fixed effects OLS regression in columns 4, 5 and 6 estimated with robust standard errors clustered by country in parentheses. Column 7 uses the instrumental variables method of Anderson and Hsiao (1982), with White (1980) heteroskedasticity correction, and columns 8 and 9 use the GMM of Arellano and Bond (1991), with robust standard errors; in both methods we instrument for Leaders' trips to USA using a double lag.

Table 5. The effect of leader's trips on total FDI before and after the end of the cold war

	Before Cold War			After Cold War		
	Anderson-Hsiao IV (1)	Arellano-Bond GMM (Dynamic) (2)	Arellano-Bond GMM (System) (3)	Anderson-Hsiao IV (4)	Arellano-Bond GMM (Dynamic) (5)	Arellano-Bond GMM (System) (6)
Leaders' trips to USA _{<i>t-1</i>}	-1.647 (2.981)	-0.507* (0.297)	-0.184 (0.152)	1.974 (4.755)	0.929** (0.411)	0.870*** (0.256)
Openness _{<i>t-1</i>}	0.528 (1.102)	0.054 (0.034)	0.068*** (0.007)	0.133 (0.870)	-0.051 (0.110)	0.069*** (0.011)
Log of GDP per capita _{<i>t-1</i>}	-1.429 (21.574)	-0.128 (1.261)	-0.071 (0.105)	12.975 (27.274)	-3.346 (2.508)	-0.854*** (0.201)
Inflation _{<i>t-1</i>}	-0.034 (0.083)	-0.001** (0.000)	-0.000 (0.001)	0.001 (0.003)	-0.000 (0.000)	0.000 (0.001)
GDP growth (annual %) _{<i>t-1</i>}	0.111 (0.796)	-0.070 (0.061)	-0.015 (0.032)	0.807 (0.676)	-0.059 (0.155)	-0.134*** (0.049)
Total natural resources rents (% of GDP) _{<i>t-1</i>}	-0.246 (0.658)	0.003 (0.035)	0.045*** (0.016)	-2.420 (8.154)	-0.019 (0.088)	0.018 (0.020)
Democracy _{<i>t-1</i>}	0.958 (1.982)	0.047 (0.054)	0.046** (0.022)	1.184 (4.770)	0.233*** (0.080)	0.050 (0.037)
FDI _{<i>t-1</i>}		-0.687 (0.556)	-0.429*** (0.118)		0.509 (0.497)	0.590*** (0.051)
Year	Yes	No	No	Yes	No	No
Constant	1.293 (2.442)		0.063 (0.747)	-12.316 (49.115)		4.876*** (1.174)
Number of observations	184	161	262	650	640	682
Hansen J test		0.000	0.815		0.035	0.000
AR(2) test					0.374	0.003

note: .01 - ***; .05 - **; .1 - *; Column 1 and 4 uses the instrumental variables method of Anderson and Hsiao (1982), with White (1980) heteroskedasticity correction, and columns 2, 3, 5 and 6 use the GMM of Arellano and Bond (1991), with robust standard errors; in both methods we instrument for Leaders' trips to USA using a double lag.

Appendix A. Data Sources

Variables	Definition	Sources
Inflation	The price inflation rate	World Bank WDI online Database
Trade openness	(Sum of exports and imports of goods and services as a share of GDP)/2	World Bank WDI online Database
Democracy	The Polity score captures a country's political regime on a 21-point scale ranging from -10 (strongly autocratic) to +10 (strongly democratic).	Polity IV Project
Leaders' trips to USA	Number of trips by heads of governments or state leaders to the USA during the period 1960-2015.	https://history.state.gov/departm enthistory
GDP growth (annual %)	Annual growth rate of real GDP per capita 1960-2015.	World Bank WDI online Database
Log of GDP per capita	GDP per capita, PPP (constant 2011 international \$) 1960-2015.	World Bank WDI online Database
Africa	Dummy variables that take on the value of one when a country belongs to a Africa and 0 otherwise	Own Calculation
Asia	Dummy variables that take on the value of one when a country belongs to a Asia and 0 otherwise	Own Calculation
America	Dummy variables that take on the value of one when a country belongs to a America and 0 otherwise	Own Calculation
Oceania	Dummy variables that take on the value of one when a country belongs to a Oceania and 0 otherwise	Own Calculation
Europe	Dummy variables that take on the value of one when a country belongs to a Europe and 0 otherwise	Own Calculation