An extraordinary act in the history of the civilized
nations, without precedent, without possible justifi-
cation, a barbarous act because it is an attack on the
most rudimentary principles of international law, an
ignoble act because it is the fruit of an immoral and
cowardly collusion of force and betrayal.

—Cipriano Castro, 1902

This is the great threat, the biggest threat that the
planet faces today. The Yankee empire.

—Hugo Chávez, 2010

In 1900, Venezuelan president Cipriano Castro seized prop-
erties belonging to the American asphalt trust. Venezuelan
troops forcibly ousted the trust’s employees and occupied its fa-
cilities on the shores of Lake Bermúdez, one of the largest natu-
ral tar pits in the world. The McKinley administration protested,
and the Navy Department ordered three warships to the scene,
but the United States did not intervene. Dissatisfied with the
official response, the asphalt trust immediately set out arming
a rebellion to overthrow Castro’s government. American cor-
porate support for the rebels led Castro to seize British-flagged
vessels carrying weapons for Castro’s opponents. That in turn
provoked a confrontation between Castro and the United King-
dom, which caused the German government to get involved
on the British side. The Anglo-German alliance shelled La Güaira, sank two Venezuelan vessels, blockaded several ports, and threatened invasion. The U.S. government was dragged back into the dispute, where it brokered a state-to-state settlement at the International Tribunal at the Hague. The imbroglio was confused, politicized, and violent. But it was not unique. From the confrontation between the Hawaiian sugar planters and Queen Liliuokalani in 1893 to the “dollar diplomacy” of the 1920s, the U.S. government found itself drawn again and again into disputes between American investors and foreign governments over their property rights.

In 2007, Venezuelan president Hugo Chávez seized properties belonging to the American oil giants ExxonMobil and ConocoPhillips. When asked, a State Department official stated, “The government of Venezuela, like any other government, has the right to make these kinds of decisions to change ownership rules. The standard has always been that we want to see them meet their international commitments in terms of providing fair and just compensation.” The oil giants then sued Venezuela’s state-owned oil company at the International Chamber of Commerce (ICC) and the Venezuelan government at the International Centre for Settlement of Investment Disputes (ICSID). The U.S. government was not involved in the suits. The ICC decided that Venezuela owed ExxonMobil $907.6 million in compensation. Chávez blustered, but paid. The dispute was legalistic and relatively orderly. But it was not unique. By 2007, it was perfectly normal for American companies to sue foreign governments in international tribunals over violations of their perceived property rights—and, at least sometimes, to win and to collect.

*The Empire Trap* is about the shift from politicized confrontations like the imbroglio of 1900 to legalized disputes like the more orderly affair of 2007. It advances four basic findings. First, American government intervention on behalf of U.S. foreign investors was astoundingly successful at extracting compensation through the 1980s. Second, American domestic interests trumped strategic concerns again and again, for small economic
gains relative to the U.S. economy and the potential strategic losses. Third, the United States proved unable to impose institutional reform in Latin America and West Africa even while American agents were in place, let alone afterward. Finally, the technology that the U.S. government used to protect American property rights overseas changed radically over time—and ultimately, in a case of unintended consequences, gave U.S. investors a set of tools that they could employ against foreign governments without explicitly calling on the power of the American executive to protect them.

The first finding—that the U.S. government intervened often and intervened successfully on behalf of American overseas direct investors from the 1890s through the 1980s—is particularly true for natural resources. State Department reports provide data on every investment dispute brought to its attention between 1900 and 1987. For investors in oil and hard-rock natural resources, the number of cases in which countries unequivocally managed to avoid paying full compensation—defined as the market value of foregone future income—was almost entirely limited to countries openly allied to the Soviet Union. In only six non-Soviet cases (out of 130) did investors unambiguously receive less than the value of their investment as a going concern: Venezuela in 1900, Bolivia in 1952 and 1969, Ecuador in 1972, Kuwait in 1975, and Iran in 1979. In other words, once you look at the data, one of the major stylized facts about the foreign expropriation of American assets disappears: investors in natural resources rarely suffered economic damage from expropriation. And this was because the U.S. government actively defended the owners and their interests, almost regardless of the strategic situation or ideological preferences.

The implication is that domestic interests trumped strategic imperatives, over and over again—which is the second finding of this book. This result is surprising considering the relative unimportance of foreign direct investment (FDI) to the American economy. FDI was never a significant part of total American investment, and the returns from FDI were never a significant
part of national income. The United States did have strategic interests in securing foreign supplies of raw materials—but never did such security hinge on the de jure ownership of foreign wells and mines. Foreign portfolio investment was slightly more important—but only beginning in the 1970s. From the 1890s to the early 1970s, American investment in sovereign debt was neither a significant proportion of American overseas portfolio investment nor systematically important to the health of the financial system. Nevertheless, American administrations again and again went to bat for private interests in their conflicts with foreign governments. This held true even when the rise of the Axis and the Cold War with the Communists sent the potential strategic costs of such conflicts into the stratosphere. After the Cuban Revolution of 1958, many within the State Department feared that it was the American hard line on expropriation that drove Castro into the arms of the Soviet Union—yet the United States ran such strategic risks again and again and again, in Indonesia and Peru and Ethiopia and elsewhere. Simply put, no U.S. president could afford to take a Solomonic view and ignore the immense pressures that private interests could bring to bear to insist upon the defense of their property rights.

To be sure, some presidents needed more persuasion than others. Theodore Roosevelt and Richard Nixon needed little convincing to punish foreign governments that threatened American-owned property. William Howard Taft and Calvin Coolidge did not require a great deal more persuasion to intervene on behalf of investors. Warren Harding, Harry Truman, Dwight Eisenhower, and John Kennedy, on the other hand, were relatively reluctant. Finally, some presidents needed to be dragged kicking and screaming into intervention. Woodrow Wilson, Franklin Roosevelt, Lyndon Johnson, and Jimmy Carter had little interest in using American power to protect wealthy Americans from foreign governments—but did so nonetheless.

The third finding is that the United States proved incapable of fixing what it believed to be the underlying factors that made property rights insecure in Latin America and elsewhere. Early
twentieth-century economic orthodoxy held that political instability, insecure property rights, poor infrastructure, and what today would be called “underdevelopment” all stemmed from a single, common root: poor revenue collection caused by internal corruption. The inability to collect taxes and tariffs, in this view, trapped states in a vicious cycle. Governments needed to pay tax collectors in order to collect taxes; so without the administrative capacity to raise revenue there was no way to create the administrative capacity to raise revenue! Low revenues, in turn, meant there were few resources to spend on public goods: armies to maintain order, courts to enforce contracts, and infrastructure to move goods and improve health. The result was political instability: without the ability to tax, governments would resort to expropriating private property (including that of foreign investors)—which would in turn mobilize violent opposition. Foreign borrowing could in theory square the circle. The problem was that the borrowing states lacked the ability to tax any resulting increase in economic activity. The result would be at best a cycle of default. At worst, a country would find itself cut off from foreign capital markets and plagued by rampant instability. Neighboring countries could be destabilized as well, and promising investment opportunities would be lost.

The above diagnosis of the problem offered an obvious solution: appoint American officials to manage a country’s revenue institutions. U.S. managers, with the power to hire and fire and enforce new administrative rules, could reduce corruption and enhance efficiency. Revenue would rise. Higher revenue would allow more expenditure on public goods. It would also decrease the chance of default, thereby lowering borrowing costs—enabling even more expenditure on public goods. That would reduce political instability and promote growth, which would in turn attract foreign direct investment, which would in turn create more growth. The end result would be stable prosperous polities in which American investment would be safe.

The only problem with the theory was that it did not work. The United States imposed eight “fiscal receiverships,” most with
the cooperation (even enthusiasm) of the foreign government. Except for the first, in the Dominican Republic, none managed to raise more revenue than the country had previously collected. In the Dominican Republic, the receivership raised revenues not because the Americans reduced corruption, wrote better rules, or brought innovative management, but because Dominican insurgents stopped attacking the customhouses once American officials were in place. Elsewhere, putting executive authority in American hands (and in many cases rewriting legislation) was not enough to change entrenched cultures of corruption. Fiscal receiverships failed even when the United States ultimately took over all government functions, as in Cuba and Haiti. Moreover, with the exception of the first intervention, markets reacted badly to the announcement of a receivership. Bond yields on the debt of other Latin American nations jumped several hundred basis points in the month a receivership was announced. Rather than showing reassurance that the Americans stood ready to improve institutions, investors acted as if the receiverships reminded them of what a risky place Latin America really was.

The fourth finding is that the technology of intervention to compel compensation changed dramatically over time. In order to defend the property rights of Americans (or at least the value of the income streams those rights generated) in conflicts with foreign governments, the United States needed to do one of three things: bribe the foreign government, threaten the foreign government, or change the foreign government. The most obvious way to protect American investors in foreign territory was to make the territory no longer foreign—that is, bring the area into the United States under the purview of the Constitution. That strategy ran into trouble when Americans began investing in areas with largely nonwhite populations: racist voters would not accept full annexation, which the Fourteenth Amendment ensured would also bring citizenship. Hawaii was the exception for a variety of special circumstances not to be repeated.

The first new “technology” to be introduced was annexation without the Constitution—as in, for example, imperial rule.
The U.S. Supreme Court, in the infamous “Insular Cases,” allowed annexation without citizenship or the full protection of the Constitution. Unfortunately for investors, that in turn also proved problematic. Democratic anti-imperialists in Congress deliberately wrote rules that restricted private American investment in the two largest and most economically important U.S. possessions: the Philippine Islands and occupied Cuba. That left informal imperialism: carrots and sticks to be rolled out against nominally independent governments. From 1904 to the Great Depression, the stick was military force (usually via the threat of blockades) and the carrot was access to the American credit market. In the 1930s the set of carrots and sticks broadened: Franklin Roosevelt added public loans, foreign aid, and access to U.S. markets to the carrots, and the threat of denial became a stick. Later, during World War II, the United States developed an entire branch of government dedicated to covert action against foreign states. It became only natural that the new tool would be repurposed to defend the private property rights of Americans abroad.

Beginning in the third quarter of the twentieth century, a series of mostly—but not entirely—unplanned innovations removed the concept of absolute sovereign immunity from legal action and gave investors direct access to international arbitration without the need to get their home governments to “espouse” the complaint. Other changes allowed the resulting decisions to be enforced in national courts. The changes gave investors a third option between cooperation with the foreign government and convincing Washington to back them in confrontation. The new option had the salubrious side effect of depoliticizing investment disputes and freed the U.S. government from the domestic pressures that had dragged it again and again into conflict with foreign states.
The Empire Trap

The above findings suggest the possibility of an “empire trap,” in which one American administration’s promise to intervene on behalf of U.S. investors makes it harder for future administrations to refrain from such intervention. If a president credibly commits to use the power of the United States to defend property rights in a foreign country, the perceived risk of investing in that country will fall. More capital will flow in, increasing the political pull of investors in that area. In addition, investors (as a matter of historical fact) will perceive that the promise applies to similar countries—in fact, for such countries to become more attractive, investors need only perceive the possibility that the promise applies. More American capital will flow in. Future administrations can default on the implicit promise—but only if they are willing to confront the owners of those investments. That entails political costs, the more so the more wealth that investors have at risk. In short, successful intervention on behalf of overseas investors begets more overseas investment, which creates more pressure to intervene when those investments come under threat. The result is an “empire trap,” where U.S. administrations find it difficult to resist pressures to defend American overseas property rights.

The rub for investors is that American presidents have multiple reasons to refrain from exercising American power on their behalf. Interventions bear domestic political costs. Voters do not necessarily think that the interests of private investors are the same as the national interest. Some may oppose intervention for ideological reasons. Others oppose intervention because it fails a perceived cost-benefit test. After all, the benefits to voters from overseas investments are generally small given the immense size of the U.S. economy. The costs of getting involved in a foreign quagmire, on the other hand, can loom large. Such quagmires do not have to be military. For example, an economic confrontation with an expropriating government might cause that government to collapse, requiring expensive aid flows to stabilize
its successor. Similarly, covert action can engender terrorism or other forms of blowback. Finally, the public might oppose intervention because it lacks sympathy for the co-nationals who lost their property. For example, the bankers and bondholders who held Latin American debt in 1929 enjoyed little to no public sympathy—and moves to support them incurred high domestic political costs.

Presidents also have strategic reasons to refrain from intervention. The United States has many interests, and defending private property rights can endanger those interests. For example, applying sanctions against a government that expropriates U.S.-owned property risks pushing that nation’s government to ally with a hostile power. Military intervention can be expensive, trigger nationalist reaction in the target country, and tie up forces needed elsewhere. Nonmilitary intervention risks angering otherwise friendly governments and igniting popular anger against all U.S. businesses operating in or dealing with the target nation. Worse still, intervention of any type risks igniting popular anger outside the target state. The small value of foreign investment set against the massive size of the U.S. economy and the multiplicity of American strategic interests militates against intervention.

American investors abroad therefore confronted the flip side of the classic collective action problem: the U.S. government was powerful enough to protect them, but their interests were small relative to the overall welfare of the United States. (These two facts were related: the reason why the U.S. government could protect them was that the United States was so much more powerful than the countries in which they invested.) They therefore needed to convince the government to use its power on their behalf despite the fact that they were a small minority and that such actions generated political and strategic costs.

As an empirical matter, American investors in the twentieth century generally succeeded in trumping domestic opposition and strategic interest. The particular political strategies they employed changed over time. In the early twentieth century, over-
seas investors mostly used individual political connections to influence policy. This became easier as the dynamics of the empire trap set in. Later on, in the 1930s, investors began to employ more sophisticated strategies, linking the defense of their interests to other interests valued by the government of the day. After World War II, they mobilized public and congressional opinion to pressure the executive branch. Companies tied national interests such as anticommunism to the protection of their property rights and argued that the preservation of their income streams had the salubrious effect of denying such streams to hostile governments. Segments of the U.S. public considered the expropriation of their fellow citizens’ property to be an attack against the nation. Others feared that if one expropriation were allowed, others might follow, so that at some point the economic damage might become large enough to affect their well-being. Such fears did not have to be realistic; they only had to be believed. In all these strategies, overseas investors benefited from the fact that the costs of intervention tended to be diffuse and spread over the entire society. Similarly, private investors benefited from changes in the technology of intervention: the political costs of denying aid or employing covert action were (at least in the short term) lower than the costs of blockading harbors or installing a fiscal receivership.

Cycles of Empire

The empire trap was not an ineluctable or monotonic process. Investors did not always get their way. Investor desires for greater property rights protection (and the strategies they employed to get their way) interacted with the American political system, voter preferences, and the technology of intervention to produce cycles of expansion and withdrawal. Note that these cycles involved only the use of American power to protect American property—they were not about the expansion of democracy, or the containment of the Soviet Union, or the prevention of geno-
earn enough revenue to continue servicing their debt. Owners of direct investments disagreed: taxes and austerity measures ate into their profits and reduced the value of their investments. Ultimately, such measures had the potential to generate instability that threatened the very survival of their investments. In the battle between bondholders and direct investors, the direct investors won: the Depression had devastated the domestic influence of the financiers.

Accordingly, the great wave of Latin American defaults began in 1931 when the Americans who controlled Bolivian government finances signed off on default—which they had in fact been actively pushing for over a year. A similar story played out across America’s other financial protectorates. In Cuba, however, President Gerardo Machado refused to default, even in the face of economic meltdown. Not unlike the Romanian Communist dictator Nicolae Ceaușescu, Machado preferred to raise taxes to confiscatory levels and stop paying government officials. The end result was the extraordinary spectacle of the Roosevelt administration orchestrating the overthrow of a Cuban president because he refused to default on his debts to American investors.

The underlying logic of the empire trap, however, continued to hold. The players were different: bondholders were no longer important, since the Great Depression destroyed most of the sovereign debt market. (It would not revive in any serious way until the syndicated bank loans of the 1970s.) Direct investors were now primary, and policy revolved around dissuading expropriation or obtaining adequate compensation afterward. The tools were also different. Under Franklin Roosevelt, the United States began to provide foreign aid (in the form of grants and loans) and rolled out perhaps the first case of modern covert action against the government of Cuba. Both tools were perfected during the Second World War, which saw the creation of entire agencies of government dedicated to providing official transfers and covertly manipulating the affairs of foreign states. In addition, the development of sophisticated trade controls al-
owed targeted action against the exports of other nations; for example, after 1948 the United States could attempt to influence certain Latin American governments by granting or withholding quotas for sugar. These new tools reduced the political cost of intervention—making it easier for American administrations to fall back into the empire trap. Chapter 7, “Falling Back In,” shows how the return to the empire trap played out, starting with Franklin Roosevelt in Mexico through Eisenhower in Guatemala and faraway Iran.

Chapter 8, “The Empire Trap and the Cold War,” shows how the empire trap continued to drive policy in the context of the worldwide contest with the Soviet Union. The Cold War had two opposing effects on the empire trap. On one hand, it raised the strategic cost of intervention. American pressure on a foreign government, if unsuccessful, could push that country into the Soviet bloc. (Many in the U.S. government, for example, believed that it was precisely the American reaction to Fidel Castro’s nationalizations that drove him into the arms of the Soviets.) On the other hand, the advent of the Cold War also raised the domestic costs of acquiescing to foreign nationalizations. Private interests rapidly learned that the fear of communist expansion made it easier to manipulate intelligence and mobilize public and congressional opinion. The Kennedy administration tried to ignore Third World expropriations, only to have Congress *mandate* the imposition of crushing sanctions in the event. Nixon sanctioned Peru and, at great strategic risk, took hard positions with Arab oil nations that were closely allied to the United States. Carter launched severe sanctions against Ethiopia, despite being warned that the target country might move into the Soviet bloc as a result—which, in fact, it did.

However challenging and frustrating this new world might be for American policymakers, it was on the whole quite good for American investors. Chapter 9 shows how American pressure obtained fair compensation for the vast majority of natural resource investors.4 There was, of course, one other difference between the Cold War–era empire and its pre-Depression prede-
cessor: in the second empire, the United States essentially gave up trying to directly alter the domestic institutions of foreign countries. There would be massive aid programs, and American advisers would become omnipresent in places like South Vietnam, but once the occupation governments were withdrawn from Germany, Austria, Japan, and Korea there would be no more “fiscal receiverships” or occupations—save for a few brief months in the Dominican Republic and mere days in Grenada and Panama. Where the United States did take a more active role, it had little to do with the protection of American property rights and more to do with the containment of Communist expansion.

Beneath the surface, however, the tectonic plates governing investor-state interactions were shifting. Chapter 10, “Escaping by Design?” recounts how over the course of the 1950s, 1960s, and 1970s a series of small legal and political innovations began to allow private investors to use international tribunals to sue foreign governments and then use American and European courts to enforce the decisions. Before 1945, the doctrine of absolute sovereign immunity held that no state could be held accountable for its actions in the courts of another state. (This led to some ironies. In 1938, the Mexican government expropriated American and British oil companies. When the Mexicans docked some expropriated tankers in Mobile, Alabama, an Alabama state judge blocked the Mexican Eagle Oil Company from repossessing its own expropriated tankers.) After 1945, reforms began to chip away at sovereign immunity. At first, the changes were driven by the rise of state-owned companies: how could Air France do business in Italy if it enjoyed absolute immunity by dint of its ownership? Later, reforms arose from efforts to depoliticize investment disputes: first by giving private investors the right to take foreign governments to arbitration without the need to have their home government “espouse” the claim; then by giving national courts the right to enforce arbitration judgments against foreign governments. These changes were not mere window dressing. They meant that in the case
of the expropriation of export-oriented assets, investors could demand compensation, enjoy an element of due process in its determination, and then use national courts in other countries to enforce a blockade of production from the expropriated assets if the foreign government reneged on compensation.

These developments were not seen as dramatically game changing at the time. As far as the investors of the 1960s and 1970s were concerned, the old system of sanctions still worked. Moreover, the Soviet Union stood ready to provide an alternative market for nations allied with it, weakening the efficacy of the new systems. But the new institutions were quietly working a revolution: they reduced the political costs that the American executive branch would incur by not acting on behalf of investors. Combined with the development of political risk insurance, these new institutions fundamentally changed the nature of international property rights. By the 1990s, American managers faced with a foreign investment dispute had a third option beyond acquiescing to the demands of the local government or asking the United States for help: they could sue in international tribunals—and more often than not, if they won, they could collect.

In presenting these findings, this book shamelessly trespasses across the social sciences. It employs a form of the “analytic narrative” pioneered by Bates, Greif, Levi, Rosenthal, and Weingast.7 There is a vast and almost bewildering amount of economic, institutional, and historical data available about the history of the United States’ attempts to protect the property rights of its citizens outside its boundaries. Analytic narrative allows placement of these data within a theoretical context to move forward from specific to more general conclusions, reasoning from the “thick” to the “thin,” as the method’s authors described it. The Empire Trap offers an account that diverges at several points from the received view. Its traipsing across different fields means that something should be said about the implications of its findings for each one.
Political Science

A major portion of the trespassing of this book is through territory that has traditionally been the province of political scientists. Political scientists have long recognized that the U.S. government went to bat for American investors in conflicts with foreign states. Examples include the work of Jessica Einhorn, George Ingram, Paul Sigmund, and Sidney Weintraub. What these authors have not fully recognized, however, is the success the government achieved in obtaining compensation for U.S. investors that equaled or exceeded the value of their investments as going concerns. Moreover, the United States generally managed to retain the strategic advantages that came from access to raw materials.

In *Defending the National Interest*, Stephen Krasner explicitly rejected the “liberal” interest group model. Rather, he adopted the view that the nation itself had interests and ideologies that it acted upon. Krasner hypothesized that one of the primary objectives for the United States was to maintain a secure supply of raw materials. In his view, corporations followed the lead of the state. The “pivot of the state”—the White House and the State Department—was “insulated from specific societal pressures.” The analysis was based on a stylized fact: when American strategic interest conflicted with the economic interest of American investors in foreign raw materials whose property had been expropriated, strategic interests won.

*The Empire Trap* takes direct issue with Krasner’s interpretation. First, the United States was remarkably successful in obtaining compensation for its nationals, especially in natural resources. Second, the U.S. government was consistently willing to run large geopolitical risks to do so. To give one example, when Indonesia nationalized American property, Lyndon Johnson said, “If we cut off all assistance, Sukarno will probably turn to the Russians”—and then proceeded to cut off assistance and watch Sukarno turn to the Russians. There is overwhelming
evidence of private interests pressuring the U.S. government to obtain compensation and the government running large strategic risks in order to obtain it.

In contrast, Charles Lipson in *Standing Guard* (1985) proposed a rather less apocalyptic view of investment disputes. Lipson believed that over the twentieth century, host country development catalyzed a shift from an international regime that favored investor rights to a new regime based on sovereign rights. Lipson argued that investors lacked the political “concentration” to restrain expropriations. Investors instead petitioned the U.S. government to finance political risk insurance schemes to protect them against further takings. He predicted further expansion in the use of the Calvo Doctrine, which held that jurisdiction in international investment disputes lay solely with the host country.

The ending of the Cold War falsified part of Lipson’s model. Instead of seeing a hundred Calvo Doctrines bloom, the world saw a rapid convergence to a new set of international legal norms for investors. Lipson’s oversight was to view the Soviet Union as the primary example of an expropriating host country, rather than as the actor lurking behind the curtains in any “bilateral” negotiation between the United States and an expropriating country in the postwar period. After the Soviet Union disintegrated, institutions designed to depoliticize investment disputes became more effective, not less. In addition, Lipson missed two other factors. U.S. presidents did make great efforts to avoid invoking laws that mandated American retaliation for expropriation—but only by dint of imposing the sanctions those laws mandated anyway. Second, Lipson gave short shrift to the creation of the modern system of investor-state arbitration—which Congress explicitly discussed in terms of “settling investment disputes discreetly so that friendly political relations might continue.” The findings here are, however, consistent with two of Lipson’s hypotheses: (1) that the U.S. government was not autonomous, and corporate preference mattered; and (2) “What
were once international clashes [became] businesslike negotiations over the distribution of future economic gains.”

Jeffry Frieden reintroduced economics as the causal variable in the political science literature on intervention. “The most relevant considerations in this regard are the potential costs of imperial intervention in enhancing the return to metropolitan economic interests, and the potential benefits that intervention might bring to these interests.” Frieden argued that colonial-style intervention became less attractive because of a shift in investment away from primary products toward government debt and local-oriented manufacturing and services. The findings in *The Empire Trap* run against some of Frieden’s empirical assertions—but have the paradoxical effect of strengthening his overall argument. The United States did not become less likely to protect American-owned property after the Second World War, but protection was easier to obtain for natural resource investments than for utilities or sovereign debt.

Most recently, Michael Tomz has argued that retaliation is not important in sovereign debt markets. In work with Mark Wright, he also documented that expropriation and default occurred in alternating (rather than coincident) waves—countries in default did not expropriate, and countries in the midst of expropriation rarely defaulted. The evidence presented here is consistent with Tomz’s argument about sovereign debt—Tomz does not address most of the episodes discussed in this book. In addition, the evidence presented here may explain Tomz’s finding about alternating waves of default and expropriation. U.S. debt policy during the 1980s was actually more hard-line than it was during the 1930s, but Washington in the 1980s helped Latin American economies adjust by providing official credit. As Peru under Alan García discovered, such credit would not be forthcoming if American property rights were disrespected. In other words, the alternating pattern may be endogenous: countries in default were less likely to expropriate because they needed American official credit.
Economics

One of the contributions that historians can make to economics is to convert stylized facts—that is, facts accepted as true for the purpose of argument—into real facts, verified by data and evidence. The evidence mustered in *The Empire Trap* contradicts the accepted stylized facts of expropriation. In the stylized version of the “obsolescing bargain,” a sovereign government and an investor strike a deal. Once the investors sink their capital, however, the government has incentives to renege on the initial deal—and it does so. Empirically, however, even using a rigorous standard, it appears that almost all the major nationalizations of American-owned resource investments were fairly compensated. The implication is that foreign investment in extractive industries (at least for Americans) was (and is) far less risky than most economists assumed. This fact may also explain investors’ apparent short memories in the wake of expropriation.

In analyzing expropriation, economists also generally assume that foreign retaliation is a decision variable for the government. This ignores the panoply of international institutions, backed by a large body of domestic law in most Western countries (and many non-Western ones) and designed to prevent expropriation without compensation. It is incorrect to assume that states are free from judicial penalties when violating the property rights of foreigners. These mechanisms, however, are very slow—by design—and empirical attempts to analyze expropriation disputes need to take those delays into account.

Finally, the failed record of America’s fiscal receiverships casts some doubt on the feasibility of Paul Romer’s “charter city” concept as a means to improve governance and promote growth. Romer’s concept rests on the assumption (almost certainly correct!) that poor countries are poor because of badly designed institutions that encourage corruption, monopolies, and inefficiency. The idea behind a charter city is that a country creates a greenfield locale in which better foreign rules apply. The country would retain sovereignty, but foreigners or a for-
eign government would act as “guarantors” in order to ensure “that the charter will be respected and enforced for decades into the future.” Honduras recently made provisions for a charter city on the country’s Atlantic coast (although its supreme court declared the provisions void and the project is now in limbo). Under the Honduran plan, the charter city will have its own public administration, tax system, legal regime, police, and “the power to sign treaties and international agreements concerning trade and cooperation in matters under their control, subject to the ratification of the national Congress.” The rules will be enforced by a “Transparency Commission” of five foreigners: two American economics professors, the former head of the INCAE Business School in Costa Rica, a former International Academy of Business Disciplines vice president, and a former Singaporean general. Jurisdictional conflicts with Honduran law will be settled by an arbitration panel of three judges selected from a pre-assigned list of forty people, half selected by the Honduran Congress and half selected by the Transparency Commission.

The American fiscal receiverships paralleled the charter cities concept, in the sense that the host nations retained sovereignty but American managers took over state functions. The Americans had the ability to hire and fire and rewrite internal regulations and processes. In some cases, they recommended changes to the tax and customs code; in others, changes were a prerequisite to the receivership. Unlike other forms of foreign intervention, the fiscal receiverships had the advantage that their success or failure was easy to measure: either revenue increased (against various counterfactuals), or it did not. They can now serve, therefore, as a partial test of the viability of the charter cities concept.

The American fiscal receiverships failed. For all save one, revenue did not increase. In Panama the American receivers were corrupted; in Peru, they were threatened by their subordinates (despite the vocal support of Peru’s president). The one time they succeeded, in the Dominican Republic in 1905, it was because the U.S. presence dissuaded insurgents from attacking the custom-
houses, not because of lowered corruption or higher efficiency. (In other words, the Dominican receivership succeeded because it was akin to a modern U.N. peacekeeping mission, not a charter city.) The American experience does not, of course, invalidate the concept, but it does imply that it may be more difficult to alter institutions than current proponents of charter cities hope.

History

*The Empire Trap*’s primary contribution is to make concrete what was previously vague. It quantifies the fiscal and market effects of American intervention in Latin America, the extent of the American sanction regime that began in the 1930s, and its success for investors. It also documents that American anti-imperialist politicians were very well aware of the political dynamics of the empire trap in 1898 when they limited American investment in the new possessions.

*The Empire Trap* offers a nuanced picture of the American stance on overseas property rights. Many accounts rely on an exaggerated caricature of Theodore Roosevelt’s pugnacious defense of American interests. Yet, as Michael Tomz has indicated, and this book has confirmed, early interventions were not uncompromisingly focused on debt collection. In fact, the United States *encouraged* Latin American countries to default on their sovereign debt during the early years of the Depression. When bondholders and direct investors were pitted against one another, direct investors won handily.

The evidence gathered on compensation payments contradicts the standard narratives about Latin American economic nationalism. The canonical Mexican oil expropriation of 1938 in particular looks vastly different when measured against the available data. The standard story is that the Mexicans paid much less than the value of the assets. That is false: Mexico paid far more than the *market* value of the assets and did so in order to avoid American economic sanctions. Two other near-canonical
Stories of economic nationalism—the dozen-plus firms expropriated in Peru by the Revolutionary Military Government in 1968–74 and Venezuela’s oil nationalization of 1975—also look quite different in light of the data. Economic nationalism had many effects, but transferring value from American shareholders to Latin American governments was not one of them.

The analysis also suggests a new periodization of American economic imperialism. Rather than shifting with each presidential election, America’s informal empire rose and fell in two distinct waves over the twentieth century. The first empire emerged when political pressures compelled the U.S. government to defend its nationals’ overseas interests in the 1900s. That informal empire then ended when the Great Depression destroyed the political coalitions that sustained it. The second wave of economically motivated intervention arose during the late 1930s and lasted through the 1980s. It was geographically much larger, was influenced by aggressive anticommunism, and was much less likely to involve direct military intervention; but the second “empire” (like the first) saw investors manipulating the U.S. political system, often with considerable success, either to protect their investments or to ensure that they were compensated for losses. The second empire did not so much end as be superseded by the development of judicialized dispute resolution mechanisms that private investors found as attractive as asking Washington for support.

Finally, this book makes a methodological statement about history and the social sciences. The social sciences are fundamentally about the study of social processes—the ways that human beings interact, and the institutions that structure those interactions over time. Thus, social scientists do not really have a choice regarding the use of history—their interest in change over time gives them little choice but to make historical arguments. The real choice for social scientists is whether the historical arguments they make are supported by systematically gathered and carefully analyzed evidence, or whether they are supported by “stylized facts.”
At the same time, coherent history requires a theoretical framework and a set of analytic tools that draws from the social sciences. Historians do not really have a choice regarding the use of quantitative evidence and the analytic tools necessary to analyze that evidence. At some point, the construction of historical narratives requires discussion of trends, frequencies, and distributions. The real choice they confront is whether the inferences they draw are the product of systematic methods or vague impressions. Similarly, historians do not really have a choice regarding the use of theory. Writing a coherent narrative requires them to adopt a scheme by which to order facts and events, and explain the causal relationships among them. Whether they realize it or not, the scheme they employ to do this constitutes a theory. The real choice historians face is whether the theory they employ is implicit or explicit, vague or clearly specified, confused or logically consistent. In sum, the study of social processes requires the integration of tools and methods taken from what have come to be thought of as distinct disciplines. There is much to be gained by the integration of these disciplines into a single, coherent approach to historical social science.