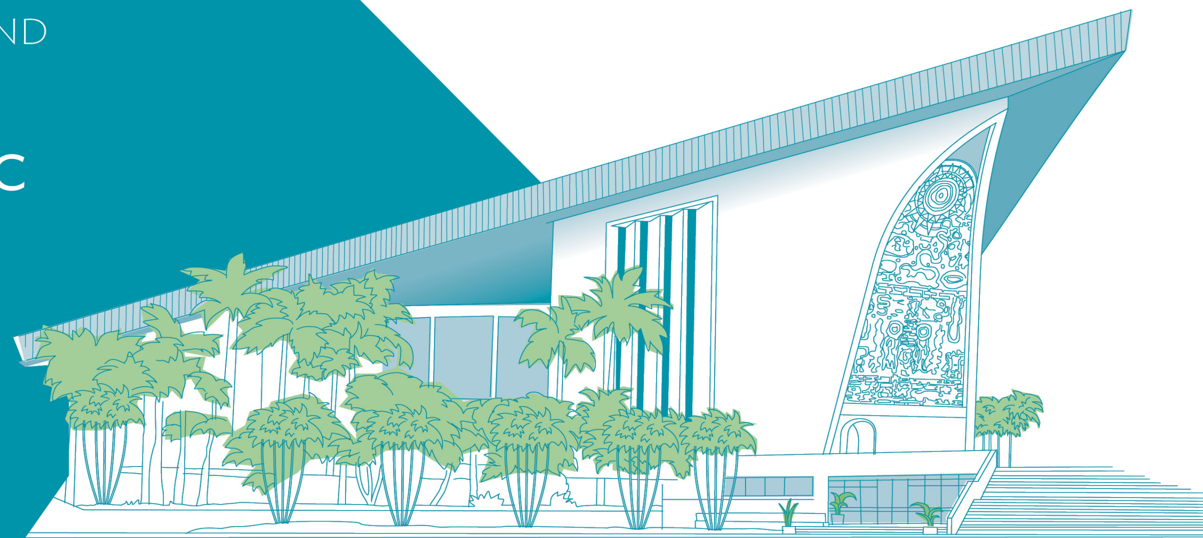
INTERNATIONAL MEDIATION AND ARBITRATION CONFERENCE

2nd South Pacific International Arbitration Conference

25–26 March 2019
Stanley Hotel, Port Moresby
Papua New Guinea



ECONOMICS OF INTERNATIONAL ARBITRATION

Prof. Dr. Jordi Paniagua
University of Valencia, Spain

March 25, 2019

If FDI & trade were a country......they would be a big one

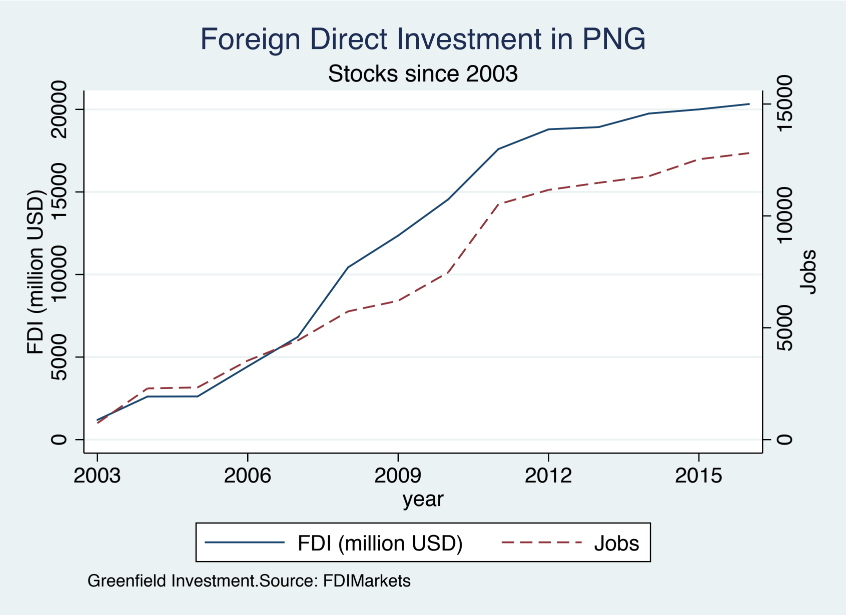
GDP (billions of $)

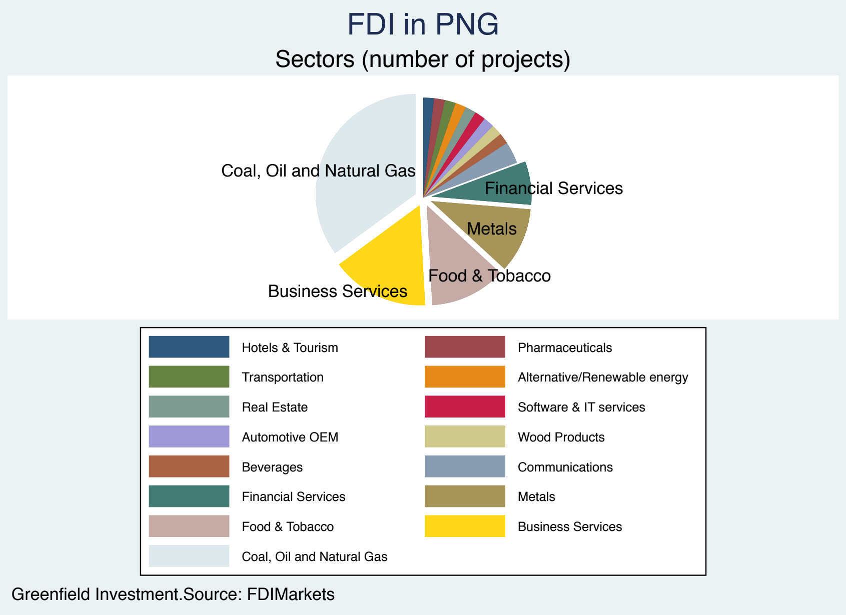
1. United States 18,036
2. Trade 16,576
3. Japan 4,383
4. Germany 3,363
5. United Kingdom 2,861
6. France 2,419
7. India 2,419
8. FDI 2,136
9. Brazil 1,804
10. Canada 1,553
11. Korea 1,378
12. Russia 1,366
13. Australia 1,339
14. Spain 1,193

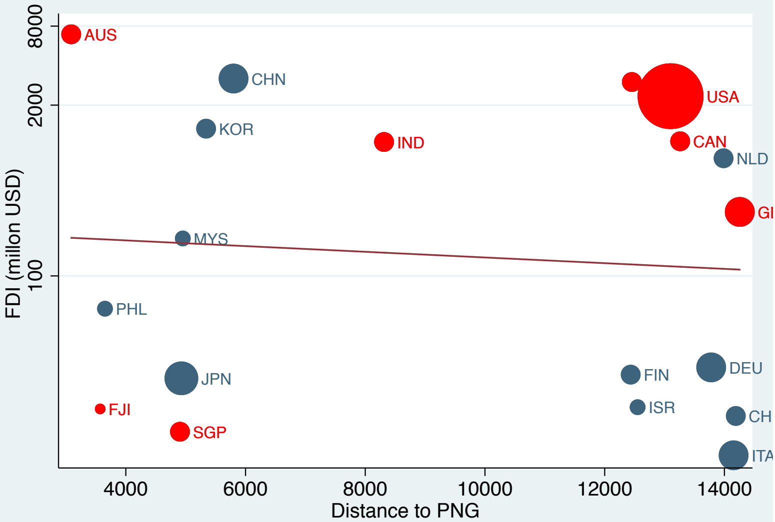
109. PNG 21

Outline

1. Introduction
   - Teaser
   - Objectives
2. Some motivating facts about FDI in PNG
   - How much
   - What
   - From whom: Gravity Falls
3. Fostering International Business through arbitration
   - Determinants of trade and FDI
   - Contractual environment & FDI
   - Economic effects of arbitration on trade & FDI
   - Best practices in the South Pacific
4. Tips & takeaways


Foreign Direct Investment in PNG
Stocks since 2003
FDI (million USD)
0
5000
10000
15000
20000
Jobs
0
5000
10000
15000
2003
2006
2009
2012
2015
year
FDI (million USD)
Jobs
Greenfield Investment.Source: FDIMarkets


FDI in PNG
Sectors (number of projects)
Coal, Oil and Natural Gas
Financial Services
Metals
Food & Tobacco
Business Services
Hotels & Tourism
Pharmaceuticals
Transportation
Alternative/Renewable energy
Real Estate
Software & IT services
Automotive OEM
Wood Products
Beverages
Communications
Financial Services
Metals
Food & Tobacco
Business Services
Coal, Oil and Natural Gas
Greenfield Investment.Source: FDIMarkets



The size of the bubble represents GDP size. Countries in red use common law

Determining Flows: What

Comparative Advantage

- Comparative advantage: predicts trade patterns and aggregate gains from trade
- Intuition: Export what you do best and import the rest.
  - Relative to Australia, PNG is relatively more efficient at producing metals than textiles ...
  - ... so PNG will export metals, Australia textiles.
- Both countries gain: Trade not a zero-sum game
  - Countries that are different have the potential for large gains

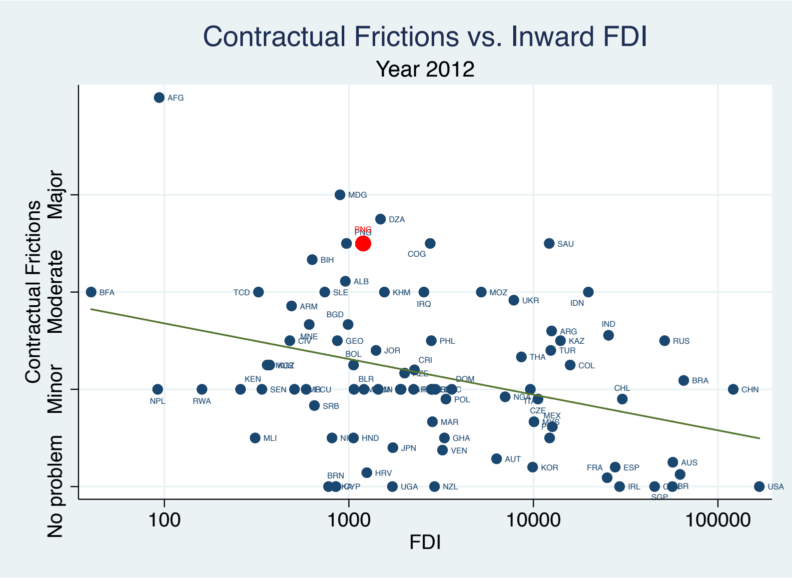
Determining Volumes: How much

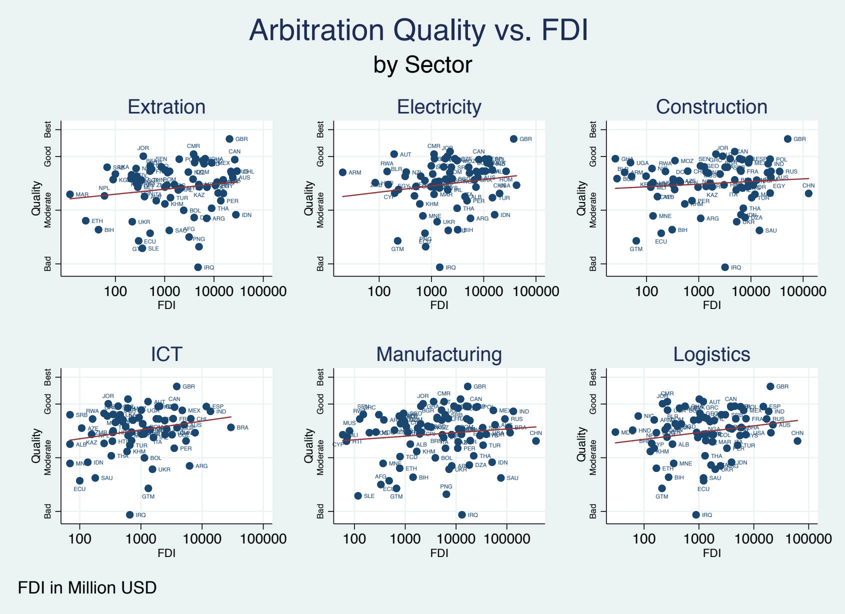
Gravity equation

- Trade volumes follow the law of gravity:

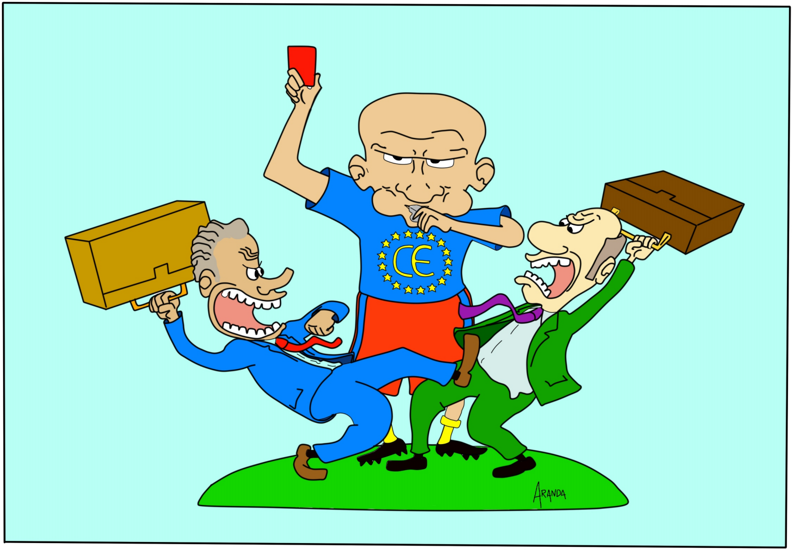
$$FDI_{i \to j} = \underbrace{\frac{GDP_i GDP_j}{GDP_{world}}}_{\text{Economic size}} \times \underbrace{\left(\frac{\text{Contractual environment}}{Distance_{i \to j}}\right)}_{\text{Frictions}}$$

- FDI & trade increase with economic activity (more consumers & producers)
- FDI & trade falls with certain frictions:
  - Natural: Distance & History & Culture & Language
  - Man-made: Contractual & institutional environment


Contractual Frictions vs. Inward FDI
Year 2012
Contractual Frictions
Major
Moderate
Minor
No problem
FDI
100
1000
10000
100000
AFG
MDG
DZA
PNG
SAU
COG
BIH
ALB
BFA
TCD
SLE
KHM
IRQ
MOZ
UKR
IDN
ARM
BGD
IND
ARG
KAZ
RUS
MNE
CIV
GEO
PHL
JOR
TUR
THA
BOL
CRI
COL
AZE
DOM
BRA
KEN
BLR
CHL
CHN
SEN
ECU
NPL
RWA
POL
SRB
CZE
MEX
MYS
MAR
MLI
HND
GHA
JPN
VEN
AUT
KOR
FRA
ESP
AUS
HRV
BRN
UGA
NZL
IRL
SGP
USA


Arbitration Quality vs. FDI
by Sector
Extration
Electricity
Construction
ICT
Manufacturing
Logistics
Quality
Bad
Moderate
Good
Best
FDI
100
1000
10000
100000
FDI in Million USD

What is International Commercial Arbitration?



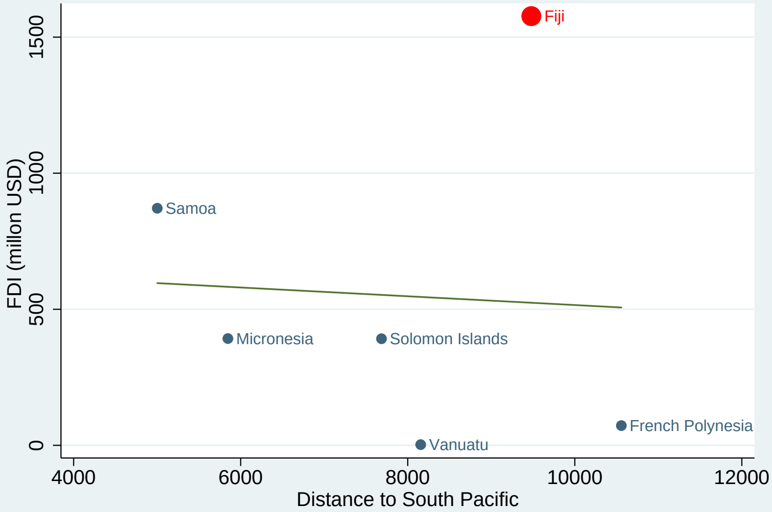
Mechanisms by which arbitration affects FDI & trade

- Arbitration provides an effective and predictable dispute settlement mechanism:
  1. Flexible, confidential & final:
     - Award can be executed worldwide
  2. Increases the trust between parties:
     - High cost of engaging in nuisance suits
  3. Reduces the uncertainty of litigation in domestic courts in trade disputes:
     - Choice of law

Economics of arbitration: options and effects?

1. International agreements
   - Ratifying the NY convention on arbitration has increased FDI flows by 77% and trade flows by 19%
2. Domestic law reform
   - Implementing UNCITRAL Model Laws has increased FDI flows by 67% and trade flows by 7%

- Arbitration increases the size of FDI projects, rather than their number
  - The effect is greater for larger projects, distant countries and weaker contractual environments



The size of the bubble represents GDP size. Countries in red ratified NY Convention

International Business Promotion

Countries have three basic ways to escape the "gravity push" and promote trade and FDI

1. Get closer
   - Play for gravity (not against it): Common language, historical links
   - Be social: What happens in PNG stays online!
2. Grow bigger
   - Seek comparative advantages & economic growth
     - Human capital, knowledge, innovation
3. Be smarter!
   - Reduce man-made frictions
     - Provide a better contractual environment via arbitration

tenk yu tru

Thanks and acknowledgments*

Contact details:

- www.uv.es/jorpaso2
- jordi.paniagua@uv.es

*Much of the research leading on which this lecture draws has received funding from the Spanish Government MINECO and the European Regional Development Fund (ECO2015-68057-R), the Generalitat Valenciana (GV/2017/052), the World Bank and the Asia Development Bank.

Background

1. Berkowitz, D., Moenius, J., and Pistor, K. (2006). Trade, law, and product complexity. *The Review of Economics and Statistics*, 88(2):363-373.
2. Myburgh, A. and Paniagua, J. (2016). Does International Commercial Arbitration Promote FDI? *Journal of Law and Economics,* 59(3). 597-627.
3. Myburgh, A. & Paniagua, J. (2017) The impact of UNCITRAL on Foreign Direct Investment, in Modernizing International Trade Law to Support Innovation and Sustainable Development, proceedings of the *Congress of the United Nations Commission on International Trade Law* (pp. 1-10). Vienna: United Nations.
4. Gil-Pareja, S., Llorca-Vivero, R. & Paniagua, J. (2018). Trade Law and Trade Flows. Working Papers 1804, Department of Applied Economics II, Universidad de Valencia.
5. Paniagua, J., Korzynski, P., & Mas-Tur, A. (2017). Crossing borders with social media: Online social networks and FDI. *European Management Journal*, 35(3), 314-326