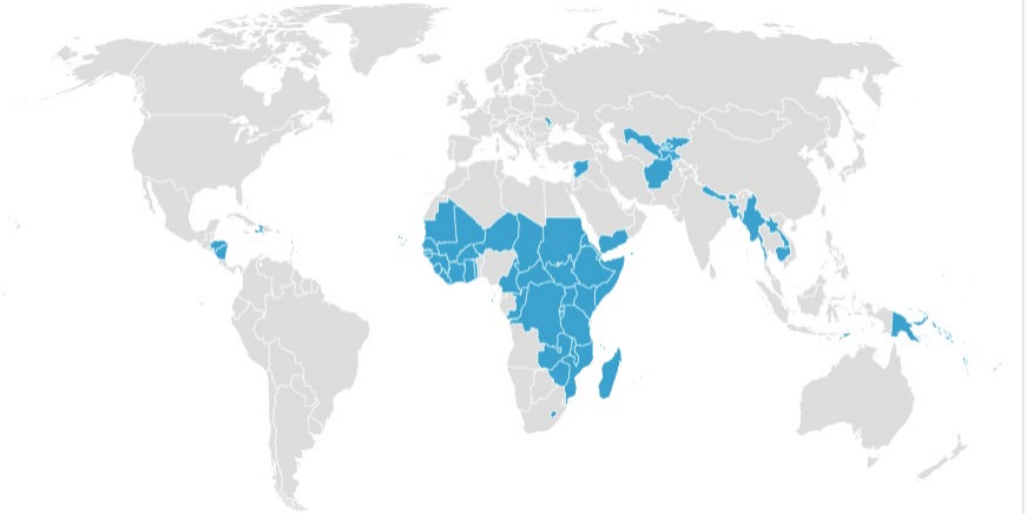


Attracting Investment in Uncertain Times: Fiscal Policy and Institutional Drivers of FDI in Low-Income Countries

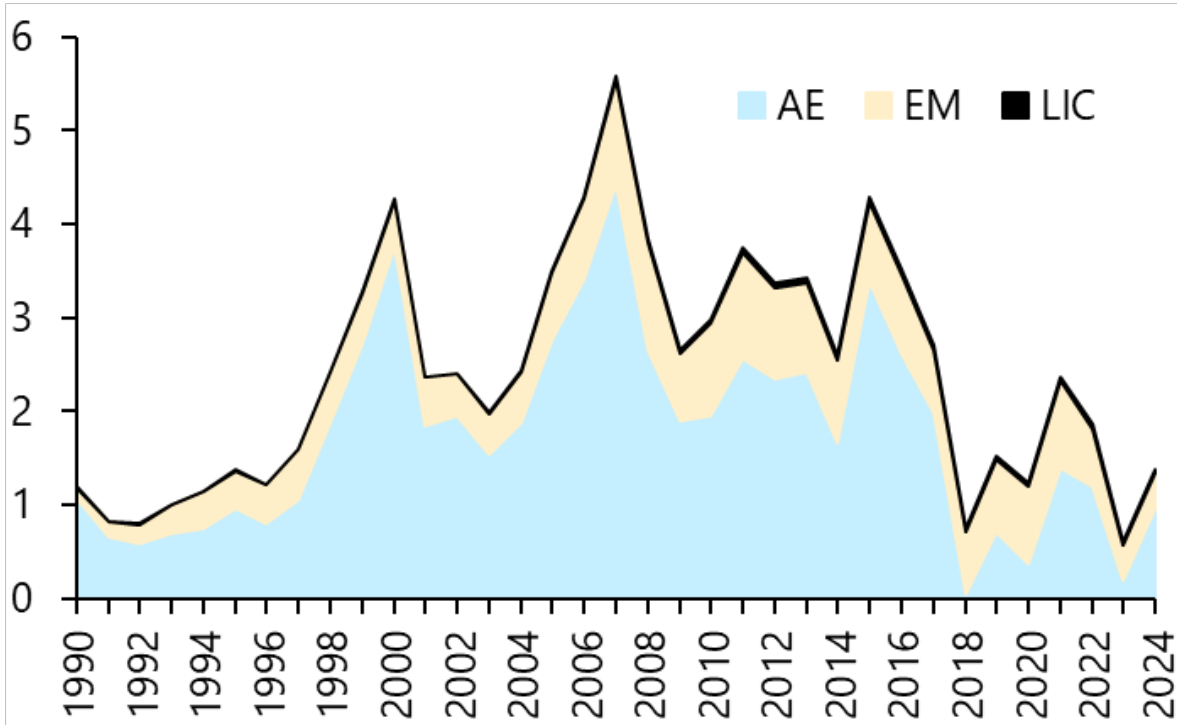
June 30, 2026

International Monetary Fund

Fiscal Affairs Department

Low-income countries receive only a small share of global FDI…

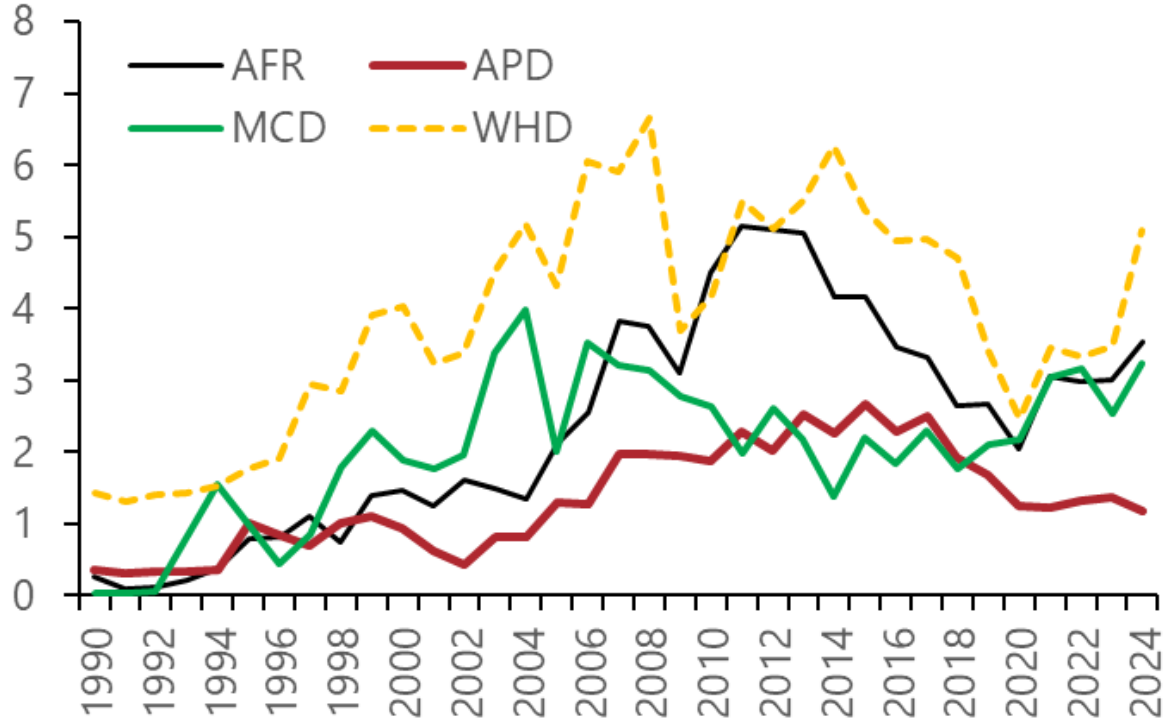
Global FDI Inflow by Income Group
(Percent of Global GDP)



Sources: IMF Balance of Payment Statistics, World Economic Outlook, and IMF staff calculations.

Note: Low-income countries (LICs) refer to the 70 countries currently eligible for the International Monetary Fund's Poverty Reduction and Growth Trust (PRGT) facilities. Country group classifications are held constant over the sample period.

LICs: FDI Inflows by Regional Group
(Percent of GDP)

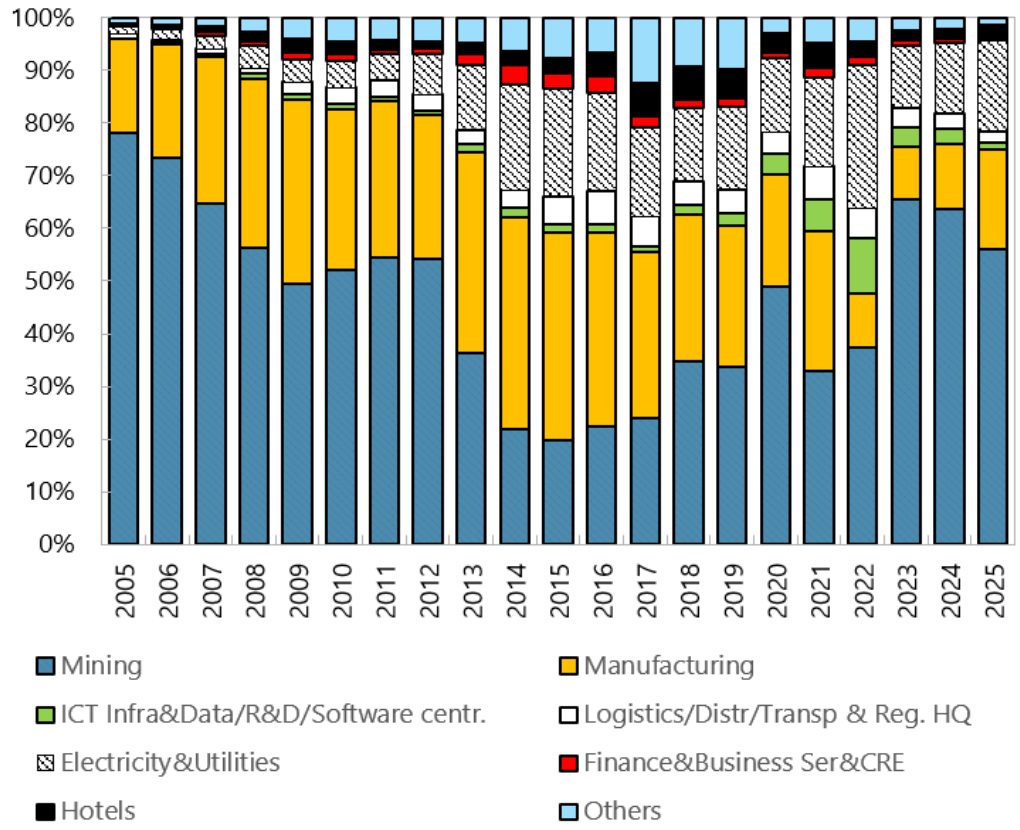


Sources: IMF Balance of Payment Statistics, World Economic Outlook, and IMF staff calculations.

Note: The figure excludes the Europe Department (EUR), as it includes only one LIC (Moldova). AFR = African Department; APD = Asia and Pacific Department; MCD = Middle East and Central Asia Department; WHD = Western Hemisphere Department.

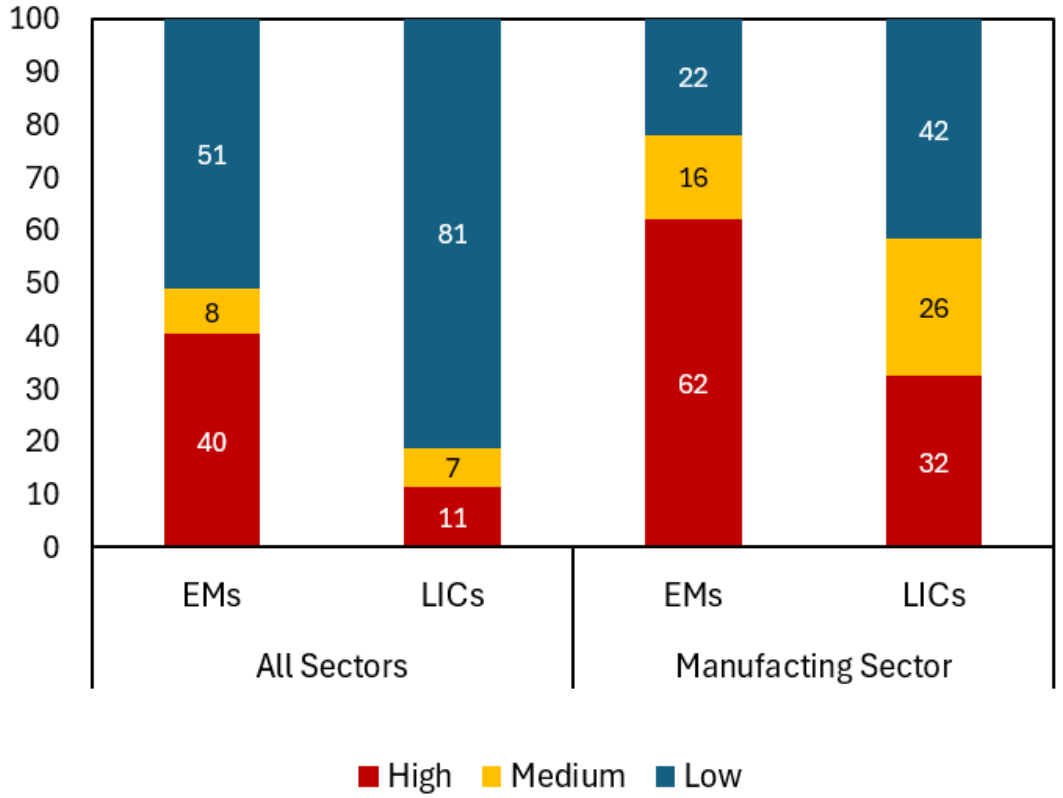
…with FDI projects in LICs concentrated in low R&D-intensity sectors

LICs: FDI Inflows by Sector
(Percent of GDP)



Sources: Orbis Cross-border Investment and IMF staff calculations.

LICs and EMs: FDI Projects by R&D Intensity, 2003-25 (Percent)



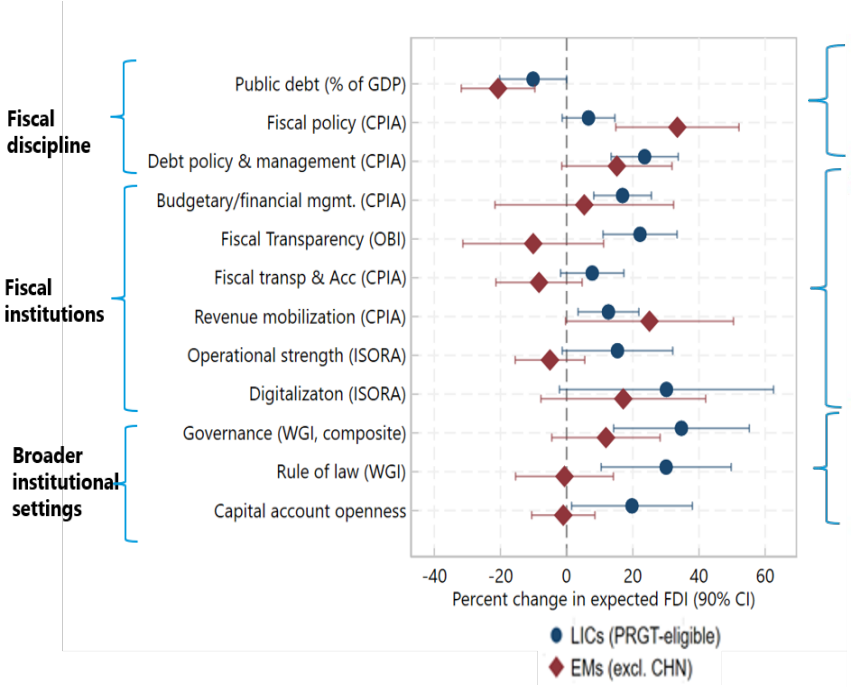
Sources: Orbis Cross-border Investment and IMF staff calculations.

Note: The figure uses project-level greenfield FDI data from the Orbis Cross-border Investment database. Projects are classified into high-, medium-, and low-R&D-intensity groups based on the OECD taxonomy of economic activities.

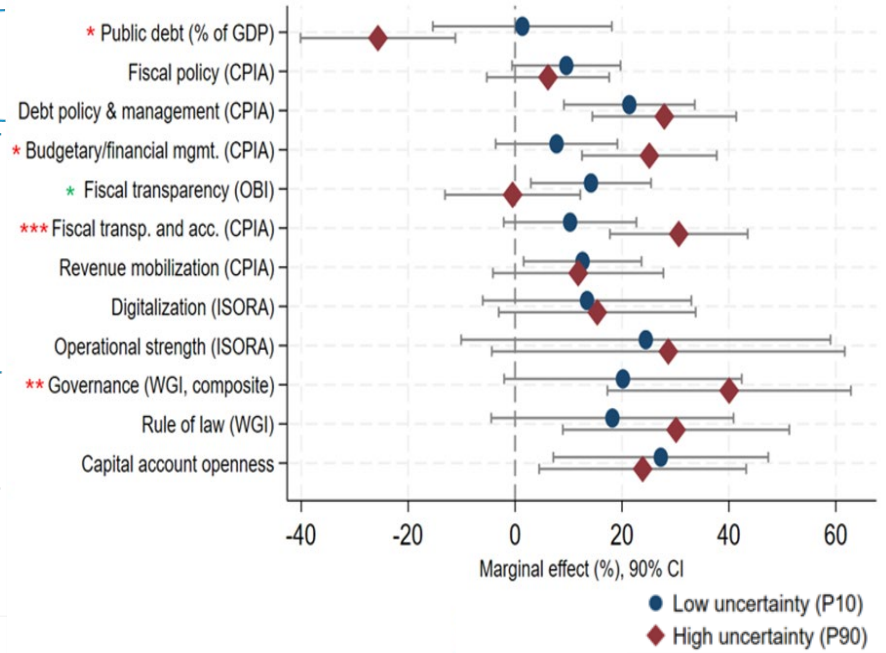
Stronger fiscal institutions—such as revenue administration and public financial management—are associated with higher FDI…

Estimated Effects of Fiscal Drivers on FDI
(Percent changes in FDI in 2017 US$)

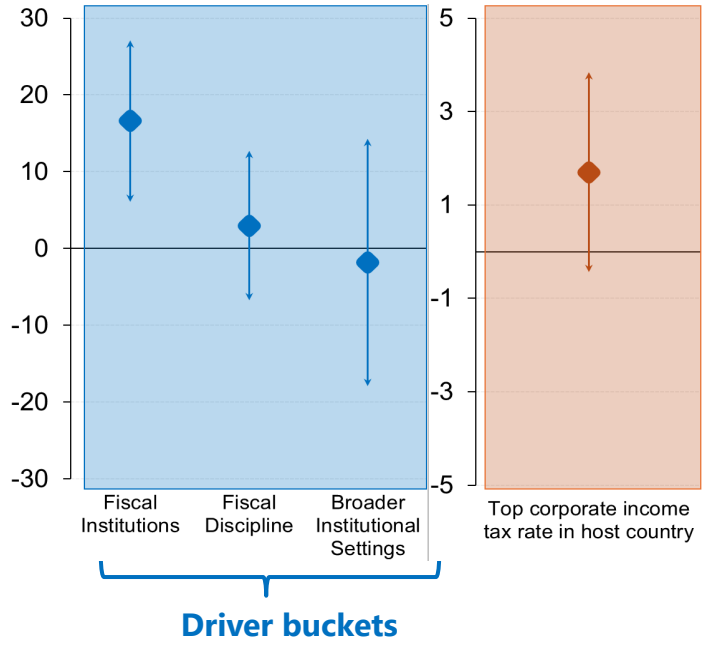
LICs versus EMs



High versus Low Uncertainty



LICs: Relative Importance of Fiscal Drivers
(Percent changes in FDI in 2017 US$)

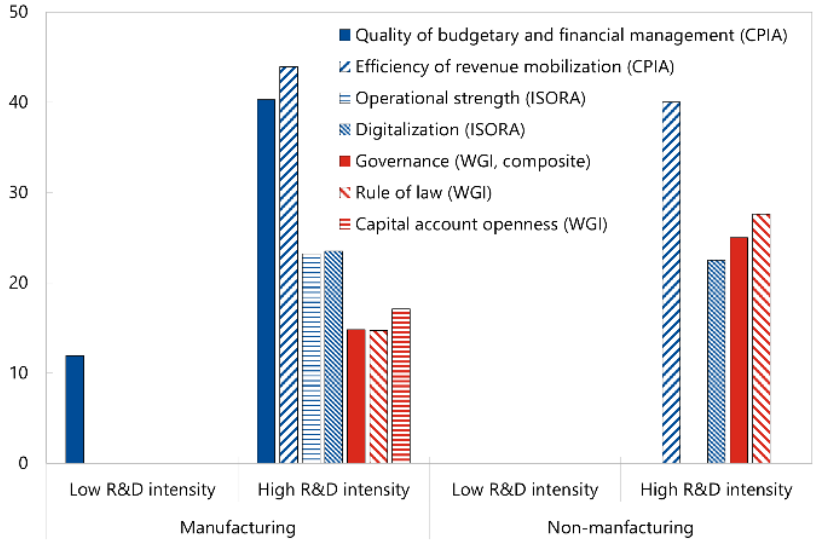


Source: "Macroeconomic Developments and Prospects in Low-Income Countries", March 2026, IMF.

Note: All estimates are based on gravity model regressions. The left panel compares the effects of fiscal and institutional drivers between LICs and EMs, while the middle panel compares their effects under high- and low- uncertainty. In both panels, each fiscal variable is added individually to a common baseline specification, and estimates show the percent change in expected FDI (in 2017 US$) associated with a one-standard-deviation increase in the variable, standardized over the pooled LIC–EM sample; horizontal bars denote 90 percent confidence intervals. The right panel summarizes the joint effects of three fiscal and institutional driver buckets—fiscal institutions, fiscal discipline, and broader institutional settings—constructed using principal component analysis (PCA). Estimates for each bucket show the percent change in expected FDI associated with a one-standard-deviation increase in the corresponding PCA index, while the estimate for the top corporate income tax rate reports the effect of a one-percentage-point increase in the tax rate. Vertical bars denote 90 percent confidence intervals.

…and higher-quality FDI, while fiscal incentives work only where institutions are strong

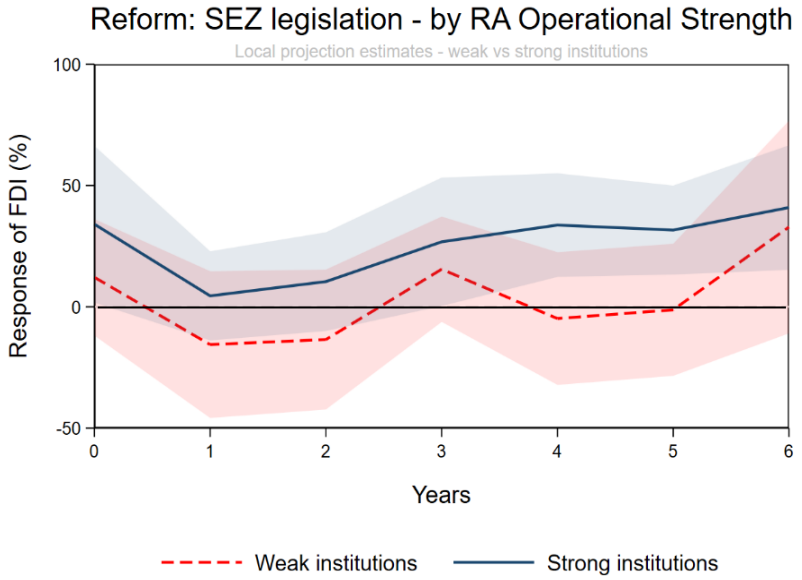
EMDEs: Effect of Institutions on Quality of FDI



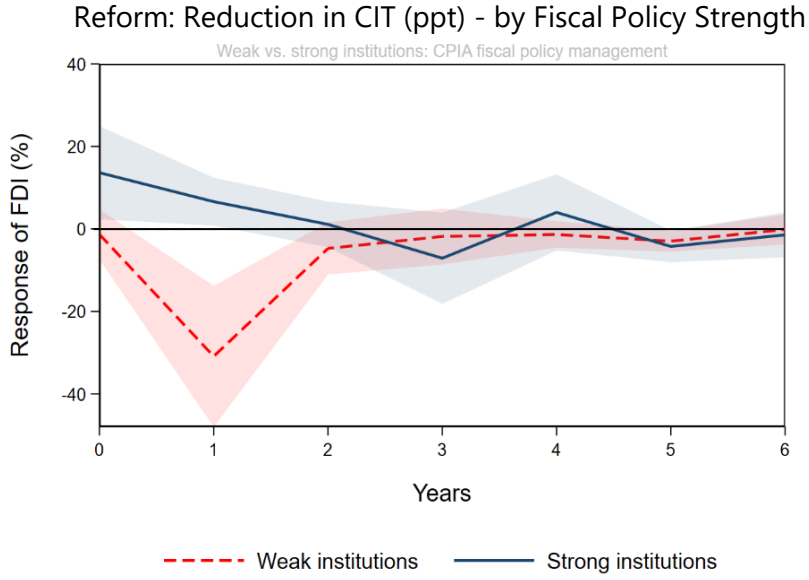
Source: "Macroeconomic Developments and Prospects in Low-Income Countries", March 2026, IMF.

Notes: Bars show coefficients that are statistically significant at 10 percent level; missing bars indicate estimates not statistically different from zero. Regressions are estimated for emerging and developing economies (EMDEs), as LIC sample is insufficient for sector-level analysis. Host- and source-country fixed effects are excluded due to limited within-country variation at the sectoral level.

LICs: FDI Response to SEZ Legislation (Percent)



LICs: FDI Response to CIT METR Reduction (Percent)



Source: "Macroeconomic Developments and Prospects in Low-Income Countries", March 2026, IMF.

Note: The figures show local projection estimates of the response of FDI to policy changes, with results grouped by countries with weak and strong institutional strength. In the left panel, the policy change is the introduction of SEZ legislation, and institutional strength is measured by revenue administration operational strength, proxied by the ISORA operational strength indicator. In the right panel, the policy change is a one-percentage-point reduction in the corporate income tax (CIT) marginal effective tax rate (METR), and institutional strength is measured by the CPIA fiscal policy management indicator. Countries are classified into weak and strong groups based on the median average value of the relevant institutional indicator over the sample period. The dependent variable is the log of FDI liabilities, and responses are expressed as percent changes. Regressions include country and year fixed effects, lagged FDI, and standard macroeconomic controls. The right-panel regressions additionally control for lagged effective tax rates. Shaded areas denote 90 percent confidence intervals based on standard errors clustered at the country level.

Four takeaways

- **Fiscal discipline** and **fiscal institutions**—such as revenue administration and public financial management (PFM)—are positively associated with FDI inflows in LICs, with these effects stronger in LICs than in EMs and during periods of **heightened uncertainty**.
- **Stronger fiscal institutions** are also associated with **higher-quality of FDI**, measured by R&D-intensity.
- **Fiscal institutions** emerge as **the more important institutional correlate** of FDI when fiscal discipline, fiscal institutions, and broader institutional quality are considered jointly.
- **Fiscal incentives**—such as special economic zones (SEZs) and tax cuts—are positively associated with higher FDI only where **fiscal discipline** and **fiscal institutions** are strong; they appear ineffective otherwise.