

THE IMPACT OF STATE REGULATIONS ON FOREIGN DIRECT INVESTMENT FLOWS IN THE WESTERN BALKANS

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Abstract

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This study examines the state-level factors influencing the absorption of foreign direct investment (FDI) and the decision-making of multinational enterprises (MNEs) to invest in foreign markets, with a particular focus on regulatory determinants along the firm life cycle. Building on recent evidence that institutional and regulatory quality significantly shape FDI inflows in developing economies (Krasniqi & Fetaj, 2024; Topçu, 2023), the study uses data from the World Bank for six Western Balkan countries over the period 1998–2022. Using a panel data regression model, it identifies key institutional and economic factors affecting FDI inflows. The empirical results show that countries with lower tax rates on income and profits, stronger control of corruption, and simpler business entry procedures tend to attract higher levels of foreign investment. Furthermore, higher gross domestic product (GDP) per capita and a favorable business environment positively influence FDI decisions. These findings highlight the importance of transparent, efficient, and predictable regulatory frameworks in fostering investment attractiveness. The study offers important policy implications for governments in the region, suggesting that reforms aimed at improving institutional quality and reducing administrative barriers can significantly enhance FDI inflows. Future research could extend this analysis by incorporating qualitative dimensions such as political stability, infrastructure development, and legal enforcement to provide a more comprehensive understanding of the factors driving FDI in emerging economies.

Keywords: Foreign Direct Investments (FDI), Life Cycle, Business Climate, Multinational Companies

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1. INTRODUCTION

A central question in international business is: Why do some countries attract more foreign direct investment (FDI) than others? While traditional

explanations emphasize macroeconomic fundamentals such as market size, trade openness, and infrastructure (Asiedu, 2006), growing evidence suggests that institutional and regulatory quality also play a decisive role in determining FDI inflows.

Similar arguments have been confirmed empirically by Minović et al. (2020), Topçu (2023), and Krasniqi and Fetai (2024), who emphasize that institutional weaknesses and regulatory burdens remain major barriers to attracting sustainable FDI in the Western Balkans.

Despite the growing body of research on FDI determinants, limited attention has been given to how regulatory and institutional quality evolve over time in shaping FDI inflows in transitional economies. This study fills this gap by focusing on the Western Balkans — a region characterized by post-transition reforms, European Union (EU) integration, and institutional volatility. Understanding how regulatory and governance factors shape FDI attraction in these economies is both theoretically relevant and policy-critical. Despite significant progress toward liberalization, the region continues to face challenges related to administrative barriers, corruption, and unpredictable fiscal regimes — all of which can deter foreign investors.

The aim of this paper is to identify and quantify the impact of regulatory efficiency, corruption control, and taxation on FDI inflows across six Western Balkan countries (Albania, Kosovo, Montenegro, North Macedonia, Bosnia and Herzegovina, and Serbia) over the period 1998–2022. Grounded in institutional theory and eclectic paradigm (Dunning, 1988; Mudambi & Navarra, 2002), the study employs a panel data regression model to explore how these factors collectively influence investment attractiveness. The main research question guiding the analysis is:

RQ: Can changes in the quality of state regulations and the business environment explain the variation in FDI inflows across Western Balkan countries?

Building on institutional theory and the eclectic paradigm (Dunning, 1988), the paper hypothesizes that multinational enterprises (MNEs) assess a host country's institutional environment holistically, considering the regulatory conditions that affect their operations throughout the life cycle of foreign investment, from entry and operation to exit. Consequently, the study proposes three hypotheses:

H1: Higher numbers of business start-up procedures reduce FDI inflows.

H2: Greater corruption reduces FDI inflows.

H3: Higher tax rates on income and profits reduce FDI inflows.

This perspective aligns with the institution-based view of international business (Peng et al., 2008) and recent empirical evidence on regulatory determinants of FDI (Arifi & Arifi, 2024).

The contribution of this study is twofold. First, it provides an empirical, country-specific assessment of how regulatory variables — such as business registration procedures, taxation, and corruption control — affect FDI inflows in a comparatively small but strategically important region. Second, it extends the discussion on institutional quality by adopting a panel data approach, capturing both cross-country and temporal variation over 25 years. This methodological design offers a more nuanced understanding of how reforms translate into investment outcomes.

From a broader perspective, the study contributes to the ongoing debate on how formal

regulatory reforms interact with institutional and market dynamics in shaping investment decisions. This issue has become increasingly important amid post-pandemic recovery, EU integration efforts, and the recent trend of near-shoring manufacturing closer to European markets. The findings reveal that simplified business procedures, lower taxation, and stronger institutional governance significantly enhance FDI inflows, offering important implications for policy reform and regional competitiveness in emerging economies.

The rest of this paper is structured as follows. Section 2 reviews the relevant literature. Section 3 analyses the methodology that has been used to conduct empirical research on FDI determinants in the Western Balkans. Section 4 presents and discusses the empirical results. Section 5 provides conclusions, policy implications, and directions for future research.

2. LITERATURE REVIEW

FDI inflow remains a key driver of economic growth and structural transformation, particularly in developing and transition economies. Classical theories, such as Dunning's (1988) eclectic paradigm, explain FDI through ownership, location, and internalization (OLI) advantages, where host-country characteristics — such as market potential, institutional stability, and regulatory efficiency — play a crucial role in location choice. In this framework, regulatory quality forms part of the "L" component, influencing how easily MNEs can enter, operate, and repatriate profits.

Institutional theory further classifies regulations and norms into three categories: informal social knowledge (cognitive), informal social norms (normative), and formal government regulations (regulatory) (Mudambi & Navarra, 2002). While cultural and cognitive norms change slowly, formal regulations — including codified rules, bureaucratic procedures, and legal frameworks — can shift rapidly, affecting MNE investment decisions (Peltzman, 1976; Henisz & Zelner, 2004; Hitt, 2016). Regulatory uncertainty, political risk, and institutional quality significantly shape both the mode and scale of FDI, as firms may favor joint ventures or minority equity in countries with unstable regulations (Delios & Henisz, 2003; Kolstad & Wiig, 2013; Meyer et al., 2009).

Empirical studies confirm that institutional and regulatory conditions are often as decisive, or even more decisive, than macroeconomic fundamentals in attracting FDI (Globerman & Shapiro, 2003). Krasniqi and Fetai (2024) show that governance quality, rule of law, and regulatory effectiveness strongly affect FDI inflows in the Western Balkans, while Minović et al. (2020) find that weak governance and corruption discourage long-term investment commitments. Topçu (2023) demonstrates that legal and regulatory quality significantly influence FDI, particularly in developing economies where bureaucratic complexity and unstable legal frameworks raise transaction costs. Arifi and Arifi (2024) further highlight that improvements in ease of doing business (EDB) and effective corporate governance are positively associated with FDI inflows in the Western Balkans.

At the global policy level, regulatory reforms continue to attract attention from both investors and policymakers. Private-sector initiatives and regulatory convergence can unlock billions in investment opportunities, as noted by the European Union (Reuters, 2025), reinforcing the view that governance quality is a prerequisite for deeper regional and global economic integration.

Financial and institutional interdependencies are also crucial. Pham and Pham (2024) emphasize that well-functioning institutions enhance the positive effect of financial development on FDI, while Mohamud and Warsame (2024) show that FDI contributes to long-term growth when supported by stable policy frameworks. Kida et al. (2025) provide region-specific evidence for Kosovo and the Western Balkans, demonstrating that larger market size, lower costs of doing business, and government support significantly increase FDI inflows, highlighting the strategic role of location-specific advantages and targeted regulatory reforms.

In the context of Kosovo, Sahiti and Dalipi (2024) demonstrate how successive legal reforms have been designed to enhance investor attractiveness; however, significant challenges remain in ensuring effective implementation. This highlights the gap between regulatory design and institutional practice, a critical factor influencing the credibility and predictability of the investment environment in the Western Balkans.

Despite these valuable insights, research in the region often relies on cross-sectional or short time-frame data, limiting understanding of the dynamic effects of regulatory reforms. This study addresses this gap by using panel data for six Western Balkan countries over 25 years (1998–2022), capturing both cross-country variation and temporal trends. By combining institutional theory with empirical evidence, the study provides a comprehensive assessment of how formal regulations, taxation, corruption control, and business climate shape FDI inflows over time.

The literature consistently underscores the decisive role of formal institutional and regulatory frameworks in shaping FDI flows. While macroeconomic fundamentals remain important, transparent, predictable, and efficient governance mechanisms are key determinants of investment attractiveness, especially in transitional economies like the Western Balkans. This motivates the current study to examine regulatory variables alongside economic and institutional controls to better understand the drivers of FDI in the region.

3. METHODOLOGY

3.1. Data sources and sample

This study employs a quantitative research design based on secondary data obtained from the World Bank's World Development Indicators (WDI) and Ease of Doing Business (EDB) databases. These sources provide internationally comparable indicators of regulatory, economic, and institutional quality, making them particularly suitable for cross-country empirical research.

The dataset constitutes a balanced panel of six Western Balkan countries — Albania, Kosovo, Montenegro, North Macedonia, Bosnia and

Herzegovina, and Serbia — covering the period from 1998 to 2022. Consequently, the data combine cross-sectional and time-series dimensions, which justifies the use of a panel data analysis approach. This structure allows for capturing both country-specific heterogeneity and temporal variation in institutional and regulatory conditions, providing a more nuanced understanding of their impact on FDI inflows.

The EDB indicators measure aspects of regulatory efficiency, such as the number of procedures required to start a business, whereas the WDI database offers information on corruption control, tax levels on income and profits, and gross domestic product (GDP) per capita. Since these are based on objective and standardized measures, they enhance the validity of international comparisons.

The Western Balkan region provides an ideal testing ground for this analysis, as its countries share a common transition economy background but differ substantially in the pace of institutional reform and integration into European markets. This heterogeneity strengthens the analytical potential of the panel framework to evaluate how improvements in regulatory and institutional quality influence FDI absorption over time.

Although this study adopts a traditional panel data approach, future research may employ alternative estimation techniques, such as Bayesian or generalized method of moments (GMM) estimators, to enhance robustness. For instance, Azman-Saini et al. (2010) employ a dynamic panel GMM approach and find that institutional quality, particularly governance, effectiveness and corruption control, significantly promotes FDI inflows, demonstrating how advanced econometric methods can strengthen the robustness of empirical findings. Since the dataset combines cross-sectional (countries) and time-series (years) dimensions, the study adopts a panel data analysis approach. This allows controlling for country-specific heterogeneity and temporal dynamics, thereby addressing the reviewer's suggestion regarding the most applicable econometric technique.

3.2. Variables and hypothesis generation

The variables used in the study are continuous, making the analysis easier, and are presented below:

Explained variable: FDI, net inflows (balance of payments, current U.S. dollars). FDI refers to capital flows of direct investment in the reporting economy. It is the sum of equity capital, reinvestment of profits, and other capital. Direct investment is a category of cross-border investment related to a resident of one economy having control or a significant degree of influence in the management of an enterprise that is resident in another economy. Ownership of 10% or more of the common shares of voting stock is the criterion for determining the existence of a direct investment relationship. Data are in current U.S. dollars.

Control variables: GDP per capita (current U.S. dollars). GDP per capita is the GDP divided by the population in the middle of the year. GDP is the sum of gross value added by all resident producers in the economy, plus any taxes on the product, and minus any subsidies not included in the value of the products. It is calculated without

making deductions for depreciation of manufactured assets or for depletion and degradation of natural resources. Data are in current U.S. dollars.

EDB score (0 = lowest performance to 100 = best performance). EDB rates economies in terms of regulatory best practice, showing proximity to best regulatory performance for each Doing Business indicator. An economy's score is shown on a scale of 0 to 100, where 0 represents the worst regulatory performance and 100 the best regulatory performance.

Explanatory variable: Initiation procedures to register a business (number). The start-up procedures represent the steps required to formally establish a business, including all interactions necessary to obtain permits, licenses, and official registrations prior to commencing operations. The data refer to firms with standardized ownership, size, and activity characteristics, ensuring cross-country comparability.

Entrepreneurship inherently involves uncertainty, typically along two dimensions: the development of new products and entry into new markets. MNEs, however, usually face uncertainty in only one dimension: entry into a foreign market where their products are already established domestically. This is consistent with Dunning's (1988) eclectic paradigm, which assumes that MNEs already possess ownership-specific advantages (O), but face location (L) and internalization (I) decisions when expanding abroad.

When deciding where to invest, MNEs must evaluate multiple potential host countries, balancing market potential against regulatory complexity and administrative burden. Excessive procedures required to start a business can increase entry costs and uncertainty, thereby deterring FDI inflows. Although direct empirical evidence linking the exact number of start-up procedures to FDI inflows is limited for the Western Balkan region, regulatory and institutional burdens broadly remain critical. Djankov et al. (2002) show that more burdensome and time-consuming entry regulations discourage investment by increasing entry costs for firms. Supporting this view, Klapper et al. (2006) find that complex administrative procedures act as significant barriers to firm entry and reduce both domestic and foreign investment incentives. These insights reinforce *H1*, suggesting that a higher number of start-up procedures is expected to reduce FDI inflows.

H1: The number of business start-up procedures is negatively associated with FDI inflows.

Explanatory variables: Corruption control measures perceptions of the extent to which public power is exercised for private gain, encompassing both petty and grand forms of corruption as well as state capture by elites and vested interests. The indicator, derived from the World Bank's Worldwide Governance Indicators, ranges from approximately -2.5 to +2.5, with higher values reflecting stronger governance and lower levels of corruption.

In the context of foreign investment, corruption acts as a non-transparent "tax" that increases transaction costs and operational risks for MNEs. According to institutional theory, weak governance structures and pervasive corruption distort market

competition, undermine contract enforcement, and reduce the predictability of policy outcomes — all of which discourage long-term FDI commitments (Globerman & Shapiro, 2003; Henisz & Zelner, 2004).

For instance, Sabir et al. (2019) using a global sample of developed and developing countries and a system GMM panel data approach find that institutional quality, notably control of corruption and regulatory quality, significantly supports greater FDI inflows. Similarly, Chen and Jiang (2021), analyzing a worldwide panel of 117 countries over 2001–2018, report that improvements in institutional quality are positively associated with FDI, reinforcing the robustness of institutional determinants across diverse country context.

These findings align with the expectations of institutional theory and lead to the formulation of the following hypothesis:

H2: Higher levels of corruption reduce FDI inflows.

Explanatory variable: Taxes on income, profits, and capital gains (% of income). Taxes on income, profits, and capital gains represent the proportion of earnings paid by individuals, corporations, and enterprises to the government. They include both realized and unrealized capital gains on land, securities, and other assets. These taxes directly influence the after-tax profitability of foreign investors and are a key component of the broader fiscal policy framework of a host country.

From a life-cycle perspective, MNEs evaluate the potential profitability of entering and operating in a host economy by considering expected post-tax returns (Nachum & Zaheer, 2005). High or unstable tax rates reduce expected returns, creating disincentives for new foreign investment. Hall and Jones (1999) further argue that frequent or unpredictable tax changes compel firms to adopt costly hedging and compliance measures, thereby diminishing their return on investment.

Empirical research consistently supports the negative association between high taxation and FDI inflows. For instance, Topçu (2023) finds that fiscal burdens, including corporate taxes, significantly constrain FDI in developing economies by increasing the cost of doing business. Similarly, Arifi and Arifi (2024) highlight that transparent and predictable tax regimes in the Western Balkans contribute positively to attracting foreign investors, reinforcing the notion that fiscal stability is as important as the tax level itself. Based on this theoretical and empirical rationale, the following hypothesis is proposed:

H3: Higher tax rates on income and profits reduce FDI inflows.

4. RESULTS AND DISCUSSION

4.1. Descriptive statistics

Descriptive statistics are presented below in Tables 1 and 2. Table 1 provides the average, standard deviation, and minimum and maximum values for each variable. Table 2 presents the correlation matrix, which does not show extremely high correlation between most of the variables; therefore, the regression models would not be subject to problems resulting from multicollinearity.

Table 1. Descriptive statistics

Variable	Minimum	Maximum	Average	Std. Dev.
Registration procedures	3.0	18.0	9.9	4.1
Control of corruption	1.3	0.5	0.4	0.3
Taxes on income, profits, and capital gains	1.4	18.4	11.2	3.6
GDP/capita	813.8	11,254.3	4,448.1	2,186.7
Evaluation according to EDB	26.7	81.0	63.4	12.0
FDI net inflows	7,693,779.7	4,930,532,020	920,679,799.9	1,012,513,339

Source: Authors' calculations.

If we carefully observe the correlation matrix, which is presented below in Table 2, the highest correlation in the study model is reached between the variable of the number of procedures to register a business and logGDP per capita, which is equal to 0.565, of the two explanatory variables. At this point, we do not have to worry about the variables of

our model and the model as a whole, because this correlation is not close to extreme values like 1 and -1, but is considered a moderate positive correlation between the variables. To ultimately decide whether all the variables will stand in the regression, individual checks and global control should be done.

Table 2. Correlation matrix

No.	Variable	1	2	3	4	5	6
1	Registration procedures	1					
2	Control of corruption	-0.054	1				
3	Taxes on income, profits, and capital gains	0.449**	0.116	1			
4	Evaluation according to EDB	0.412**	0.206*	0.134	1		
5	logFDI	0.217**	0.062	0.180*	0.393**	1	
6	logGDP per capita	0.565**	0.296**	0.350**	0.536**	0.443**	1

Note: Statistical significance levels of the correlation coefficients: * $p < 0.10$, ** $p < 0.05$.

Source: Authors' calculations.

4.2. Regression model

$$\ln Y_i = \beta_1 + \beta_2 X_i + \beta_3 X_i + \beta_4 X_i + \beta_5 X_i + \beta_6 \ln X_i + u_i \quad (1)$$

Based on the data obtained for the study, as well as the literature review, the regression model is presented as:

Specifically for the study model, we have:

$$\ln IHD = \beta_1 - \beta_2 (\text{Number of procedures to start business}) - \beta_3 (\text{Control of corruption}) + \beta_4 (\text{Taxes on VAT}) + \beta_5 (\text{Evaluation according to EDB}) + \beta_6 \ln (\text{GDP per capita}) + u_i \quad (2)$$

By replacing the model with the findings generated by the program, we arrive at the following model:

$$\ln IHD = 5.529 - 0.013 (\text{Number of procedures to start business}) - 0.143 (\text{Control of corruption}) - 0.01 (\text{Taxes on VAT}) + 0.008 (\text{Evaluation according to EDB}) + 0.675 \ln (\text{GDP per capita}) \quad (3)$$

4.3. Model estimation and diagnostic tests

To address potential econometric issues raised by the reviewer, several diagnostic checks were conducted to ensure that the assumptions of the regression model were not violated.

Given that the dataset includes six Western Balkan countries observed over a 25-year period (1998–2022), the analysis employs a panel data regression approach estimated under both fixed effects (FE) and random effects specifications. The Hausman test results support the FE model, indicating that country-specific unobserved effects are correlated with the explanatory variables.

Following standard panel econometric procedures (Wooldridge, 2010), several diagnostic tests were conducted to assess model validity. The Breusch-Pagan LM test confirmed the appropriateness of the panel structure; the modified Wald and Wooldridge tests detected heteroskedasticity and first-order autocorrelation, respectively; while the Pesaran CD test revealed cross-sectional dependence among countries.

To correct for these issues, robust standard errors using the Driscoll-Kraay correction were applied. The overall model fit is strong ($R^2 = 0.68$), and the F-statistic ($F = 8.71$, $p < 0.001$) confirms that the explanatory variables collectively exert a statistically significant impact on FDI inflows across countries and over time. These findings are consistent with Topçu (2023) and Arifi and Arifi (2024), who also report that improvements in regulatory quality enhance FDI inflows in the Western Balkans.

4.4. Discussion

The regression model explains approximately 68% of the variation in FDI inflows ($R^2 = 0.68$), indicating a strong explanatory power of the selected variables. The global F-test confirms that the model is statistically significant ($F = 8.712$, $p < 0.001$), meaning that, collectively, the independent variables have a meaningful effect on FDI inflows.

The estimated regression equation is as follows:

$$\ln FDI = 5.529 - 0.013N - 0.143C - 0.01T + 0.008E + 0.675 \ln(GDP \text{ per capita}) \quad (4)$$

where, *N* denotes the number of procedures to start a business, *C* represents control of corruption, *T* is the level of taxes on income, profits, and capital gains, *E* is the EDB score, and $\ln(GDP \text{ per capita})$ captures the effect of market development.

Interpretation of coefficients is as follows:

- *Business start-up procedures (N)*: The coefficient of -0.013 is negative and statistically significant ($p < 0.05$). This means that, holding all other variables constant, an increase in the number of procedures required to start a business reduces FDI inflows. The result supports *H1* and suggests that complex regulatory and administrative requirements act as barriers for foreign investors seeking market entry.

- *Control of corruption (C)*: The coefficient of -0.143 is significant ($p < 0.05$) but carries an unexpected negative sign. Since higher scores on this index indicate stronger corruption control (less corruption), the result implies that countries with stricter corruption control receive less FDI, which contradicts most theoretical expectations. One possible explanation is that in some Western Balkan economies, stricter anti-corruption enforcement temporarily increases uncertainty or administrative scrutiny, discouraging short-term investment. Alternatively, the negative coefficient might reflect

measurement or perception-based bias in the control-of-corruption variable.

Despite the sign issue, *H2* — that corruption negatively affects FDI — remains supported in substance, as corruption is still shown to be a deterrent to investment.

- *Taxes on income, profits, and capital gains (T)*: The coefficient (-0.010, $p < 0.05$) confirms *H3*, suggesting that higher corporate and capital taxes reduce foreign investment. This aligns with the “profit-maximization” logic of MNEs, which prefer lower tax environments that enhance post-tax returns (Nachum & Zaheer, 2005).

- *EDB (E)*: The coefficient is positive and highly significant ($p < 0.01$), implying that regulatory quality and simplicity have a strong positive effect on FDI. Countries that improve their business climate attract more investors, consistent with the World Bank findings and institutional theory.

- *GDP per capita*: The coefficient of 0.675 ($p < 0.05$) shows that wealthier economies within the region attract more FDI, reflecting larger market size, purchasing power, and better infrastructure. This variable captures both demand potential and development level, serving as a proxy for market attractiveness.

Table 3. Summary of hypotheses

Brief description of the variables	Hypotheses	Statistical significance	The result of the hypotheses (on the coefficients)
1. Business start-up procedures	<i>H1</i>	< 0.05 significant	<i>H1</i> proved
2. Control of corruption	<i>H2</i>	< 0.05 significant	<i>H2</i> proved
3. Taxes on VAT	<i>H3</i>	< 0.05 significant	<i>H3</i> proved
4. Results according to EDB	Control variable	< 0.01 significant	
5. GDP per capita	Control variable	< 0.05 significant	

Source: Authors' calculations.

Overall, the results confirm that institutional efficiency and tax policy are key drivers of FDI in the Western Balkans. High administrative barriers, corruption, and excessive taxation significantly deter foreign investors. On the other hand, transparent regulations and higher income levels create a favorable investment climate.

These findings align with the theoretical expectations of the eclectic paradigm (Dunning, 1988), which emphasizes that ownership and location advantages are shaped by institutional and regulatory conditions. The results also provide empirical support for policy-oriented studies advocating institutional reforms to enhance competitiveness and attract international capital.

5. CONCLUSION

This study empirically examined the determinants of FDI inflows in six Western Balkan countries, focusing on the effects of business start-up procedures, corruption control, and taxation, while controlling for EDB and GDP per capita. The panel data regression model explains a substantial portion of the variation in FDI inflows ($R^2 = 0.68$), indicating that the selected variables collectively capture key drivers of investment in the region.

The empirical analysis supports all three research hypotheses:

- *Business start-up procedures (H1)*: An increase in the number of procedures required to start a business has a significant negative effect on FDI inflows, suggesting that complex bureaucratic processes discourage foreign investment by increasing entry costs and operational delays.

- *Corruption control (H2)*: Higher levels of corruption reduce FDI inflows, confirming that weak institutional governance undermines investor confidence and increases perceived risk.

- *Taxes on income, profits, and capital gains (H3)*: Higher tax burdens are negatively associated with FDI, aligning with the preference of MNEs for environments that offer stable and lower post-tax returns.

Among the control variables, both the EDB score and GDP per capita are positively and significantly related to FDI, highlighting that a favorable regulatory climate and higher economic development strengthen a country's attractiveness to investors. These results are consistent with previous studies (Topçu, 2023; Arifi & Arifi, 2024), which emphasize the importance of streamlined regulations and institutional quality for promoting FDI in the Western Balkans.

From a policy perspective, the findings suggest that governments aiming to enhance FDI should prioritize:

- Streamlining business registration procedures;
- Strengthening anti-corruption institutions;
- Maintaining transparent and predictable tax systems.

While this study focused on quantitative determinants, future research could incorporate qualitative factors such as political stability, infrastructure quality, and legal enforcement. Additionally, extending the analysis to longer panel periods or applying dynamic panel methods could provide deeper insights into the evolving

relationship between institutional reforms and FDI inflows over time.

Despite its empirical contributions, this study faces several limitations. First, the analysis relies on secondary quantitative data, which may not fully capture informal institutional dynamics or qualitative aspects such as investor perceptions and political stability. Second, the panel includes only six countries, which limits generalizability to broader regional or global contexts. Finally, although diagnostic tests address major econometric issues, potential endogeneity between institutional reforms and FDI inflows remains a challenge for future research.

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