Tax Policy and Foreign Direct Investment of a Home Country

SASATRA SUDSAWASD

School of Development Economics, National Institute of Development Administration,
118 Seri Thai Rd., Klong-Chan, Bangkok 10240, Thailand
Email: sasatra@nida.ac.th

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The relationship between an FDI home country's tax policies and its FDI outflows is investigated using panel data of bilateral FDI flows from the OECD countries for the period 1990-2004. Five types of tax policies are examined: corporate income taxes, personal income taxes, property taxes, consumption taxes, and import taxes. Panel regression results suggest that most tax policies of a home country have positive correlations with the level of FDI outflows. With one exception, consumption taxes are negatively correlated with FDI outflows from the OECD countries. This empirical finding appears to be on the same line with theoretical predictions that an increase in consumption tax rates is associated with a lower marginal product of labor. This, in turns, increases the level of employment and the demand for new investment in a home country.

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