The role of state competitiveness and perceived insecurity in attracting foreign direct investment in Mexico

Juan Carlos Botello
Consejo de Ciencia y Tecnología del Estado de Puebla (CONCYTEP) - Universidad Popular Autónoma del Estado de Puebla
Business School, Mexico
juancarlos.botello@upaep.mx

Mariana Echeagaray Santibañez
Universidad Popular Autónoma del Estado de Puebla, Mexico
mariana.echeagaray@upaep.edu.mx

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Abstract
State competitiveness is a key factor influencing a country's capacity to attract foreign direct investment (FDI), as it reflects the efficiency of institutions, infrastructure, macroeconomic stability, and innovation capacity, among others. In Mexico, the Mexican Institute for Competitiveness (IMCO) is responsible for measuring and analyzing state competitiveness through its State Competitiveness Index, which evaluates factors such as economic stability, governance, innovation, and security conditions.This study explores how state competitiveness and perceived insecurity impact the attraction of Foreign Direct Investment (FDI) across Mexican states, using a comprehensive model that incorporates key variables such as state competitiveness, perception of insecurity, political party in power, and GDP. Based on data from 2019 to 2023, the analysis reveals that the State Competitiveness Index is the most significant predictor of FDI, exhibiting a positive relationship with new investments. This indicates that higher state competitiveness tends to attract more foreign investments. Additionally, the Perception of Insecurity Index demonstrates a significant, albeit smaller, effect on FDI, suggesting that increased insecurity perception can still influence investment flows, though to a lesser extent. These findings underscore the complex dynamics between security perceptions, competitiveness, and foreign investment, providing valuable insights for policymakers aiming to enhance investment attraction strategies.

Corresponding author: Juan Carlos Botello
Email address for the corresponding author: Juancarlos.botello@upaep.mx
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Introduction

Foreign direct investment (FDI) is crucial in economic growth, industrial development, and job creation, particularly in emerging economies like Mexico. However, the ability of a country or region to attract FDI depends on multiple factors, including economic competitiveness, security conditions, and political situation. State competitiveness—encompassing infrastructure, human capital, regulatory efficiency, and innovation—is a key determinant in fostering a favorable business environment. Conversely, perceived insecurity, driven by crime rates, violence, and instability, can deter foreign investors, increasing operational risks and costs. Also, the type of government a country has can either favor or impede domestic or international private investment.

This study examines the interplay between state competitiveness, perceived insecurity, and the political parties within Mexico in attracting FDI by 2019 - 2023.

The Mexican Institute for Competitiveness (IMCO) annually publishes the State Competitiveness Index (SCI) that considers that every state of Mexico should comply with the following elements: Innovation and Economy, Infrastructure, Labor market, Society and Environment, Law and Political system and Government to be competitive.

The National Institute of Statistics and Geography (INEGI) Insecurity Perception Index was used taking into account data from the National Survey on Victimisation and Perception of Public Security (ENVIPE) that provides detailed statistics on victimisation and fear of crime, which allows us to contextualize the perception of insecurity in each state, of the INEGI and foreign direct investment statistics provided by the Ministry of Economy.

A Poisson and a negative binomial regression model were used to achieve the highest degree of significance of the relationship between the variables. Understanding these dynamics is essential for policymakers seeking to implement strategies that enhance investment attractiveness while addressing security concerns.

Literature review

The attraction of foreign direct investment (FDI) depends on multiple factors that must be primarily considered by national and subnational governments. The more competitive a country is, the greater the investment flows it will receive, leading to increased economic benefits, (Brooks and Sumulong, 2003; Bengoa and Sanchez-Robles, 2005) such as economic growth, provision of capital, foreign exchange, technology, and improvements in export markets.

Competitiveness significantly influences FDI attraction, as it encompasses various elements such as skilled labor, infrastructure, property rights protection, natural and technological resources, gross domestic product (GDP), tax incentives, and security. Given this, the role of both government and businesses in fostering a country's competitive development is essential for attracting investment.

The government plays a key role in attracting investment. Incentive policy and building the structural and institutional foundations to receive FDI efficiently are governmental factors that must interact to promote a nation's competitive development (ECLAC, 2024). Volpe and Sztajerowska (2019) discuss the functions and dynamics that a country takes to be an attractive destination with a good perception for investors and mention how a good national image can help attract FDI flows.

The Economic Commission for Latin American and the Caribbean (ECLAC) (2024), in a study of Foreign Direct Investment in Latin America and the Caribbean, states that:

"Firstly, the potential of FDI to affect economic growth is greater if the host country has adequate absorption capacity. In general, the least developed countries lack the initial absorption capacity needed to obtain the best results from FDI. This depends not only on macroeconomic and institutional factors and good governance but also on the sectors involved and the policies to promote, regulate and manage FDI".

Armas & Ayvar (2017) mention that access to new markets, productive efficiency, skilled labor, infrastructure, natural resources, and tax exemptions are competitiveness factors that influence the attraction of foreign direct investment (FDI) in Mexico for the manufacturing industry. Ortíz (2022) found that export-oriented firms in Mexico are more likely to use strategic resources such as skilled labor. Those companies are considered part of the maquiladora industry and, due to their competitiveness, can attract foreign direct investment.

The competitiveness of the automotive sector emerges as a key factor in attracting foreign direct investment (FDI), given its impact on the manufacturing of transportation equipment, which accounts for a significant percentage of total investment. The production of cars and trucks, along with automotive spare parts, concentrates a substantial share of foreign investment. This suggests that infrastructure, technological development, and supply chain integration within this sector are crucial determinants of attracting foreign capital (Guizar, 2020).

According to Miranda, Tack, and Pinto De Gracia (2023), the main competitiveness factors influencing the attraction of foreign direct investment in Panama include macroeconomic stability, the availability of skilled labor, business sophistication, infrastructure, and access to advanced technology, all of which directly impact investors' decision-making.

One of the effects of insecurity is in the economic sphere, like the attraction of FDI. Kaukab (2024) mentions that the business environment, security, and environmental sustainability are variables that could negatively affect FDI inflows. Soria-Romo (2017) conducted a study to find the relationship between competitiveness and insecurity in the states of Mexico and found evidence of the negative impact of public insecurity on the competitiveness of the federative entities. The study found that states with higher crime rates and a weak rule of law tend to have low investment and economic growth. That suggests public security is fundamental for maintaining an attractive business environment and fostering economic development.

Likewise, the relationship between security and competitiveness is clear because an insecure city loses its attractiveness for investment and talent (Mazari, 2024).

Botello & Davila (2023) concluded that the decline in FDI can be attributed to multiple factors such as organized crime and the distrust of investors derived from the arrival of a leftist political party to the government. Mogrovejo (2005) argues that the interplay between political and social actors is a key determinant for investment decisions, as firms assess regulatory stability and government incentives before committing capital to foreign markets.Simmons et al. (2018) emphasize that political parties play an important role in shaping economic policies and influencing FDI inflows. Governments that provide legal certainty and transparent business regulations, tend to secure higher levels of foreign investment. Saavedra & Flores (2017) mention how governance functions as an investment attraction mechanism, implying that a higher degree of governance would induce an increase in FDI flows, concerning governance, they take into account the following concepts: indicators of property rights protection, effectiveness of public policies, violence indexes, taxes, political instability and corruption.

Research Methodology

The objective of this research is to find out if the attraction of foreign direct investment in Mexico was positively or negatively impacted by the state competitiveness index, the perception of insecurity, the gross domestic product and the political parties that governed each of the 32 states of the Mexican Republic from 2019 to 2023. To achieve that goal a database was created with information from the 32 states of the Mexican Republic, considering five variables: state competitiveness according to the Mexican Institute for Competitiveness (IMCO), Greenfield investments flows, the perception of insecurity index made by the National Institute of Geography and Statistics (INEGI), the ruling political party in each state and the GDP for the period studied (2019-2023).

For this study, we used Greenfield foreign direct investment (FDI) flows as the dependent variable and the insecurity perception index, state competitiveness, political party and GDP as independent variables.

Methodology

The initial database included a categorical variable (political party), which was converted into a dichotomous variable to enable comparison with other numerical variables and to perform a multiple regression model that would allow us to understand the relationship between the variables. Once the results were obtained, the Poisson model was applied to improve the study and analyze the relationship between the dependent and independent variables to get an accurate result.

The Poisson model is ideal when the variable of interest represents event counts over a specific period or space. The Greenfield investments variable measures the number of new investments in each state during the study years. The model uses a logarithmic link function, meaning that changes in the independent variables affect investment in an exponential rather than a linear manner. This is useful because the relationship between factors such as competitiveness, perception of insecurity, and political parties with foreign direct investment may not be completely linear.

Model 1. The equation for the Poisson Model

$$E(INVESTMENTS) = e^{\beta_0+\beta_1 \cdot COMPETITIVENESS+\beta_2 \cdot PERCEPTION+\sum_i \beta_{3i} \cdot POLITICAL\ PARTY_i+\sum_k \beta_{5k} \cdot GDP_k}$$

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Where:

$E(INVESTMENTS) E(INVESTMENTS)$ is the expected number of investments in each state.

$\beta_0 \beta_0$ is the intercept, which represents the logarithm of the expected investment when all variables are 0.

$\beta_1 \cdot COMPETITIVENESS \beta_1 \cdot COMPETITIVENESS$ is the effect of state competitiveness.

$\beta_2 \cdot PERCEPTION \beta_2 \cdot PERCEPTION$ is the effect of the perception of insecurity.

$\sum_i \beta_{3i} \cdot POLITICAL\ PARTY_i \sum_i \beta_{3i} \cdot POLITICAL\ PARTY_i$ represents the influence of each political party in the state government (dummy variables).

$\sum_k \beta_{5k} \cdot GDP_k \sum_k \beta_{5k} \cdot GDP_k$ is the impact of the state GDP on foreign investment.

Additionally, the model assumes that the mean and variance are equal or very similar. However, we calculated the mean and variance, finding that the variance was much greater than the mean, indicating overdispersion. As a result, the Poisson model with adjusted dispersion or a Negative Binomial Regression model better fits the study, as it handles overdispersion more effectively.

Model 2. The equation for the Negative Binomial Regression Model

$$E(INVESTMENTS) = exp(\beta_0 + \beta_1 \cdot COMPETITIVENESS + \beta_2 \cdot PERCEPTION + \sum_i \beta_{3i} \cdot POLITICAL\ PARTY_i + \sum_k \beta_{4j} \cdot GDP_k)$$

Where:

$E(INVESTMENTS) E(INVESTMENTS)$ is the expected number of investments in each state.

$\beta_0 \beta_0$ is the intercept.

$\beta_1\beta_1$, $\beta_2\beta_2$, $\beta_{3i}\beta_{3i}$, $\beta_{4j}\beta_{4j}$ are the coefficients of each independent variable

The summation term represents the dummy variables for political parties and GDP.

We also analyzed the Akaike Information Criterion (AIC), obtaining a much lower value for the negative binomial model than the Poisson´s, which fits the data better.

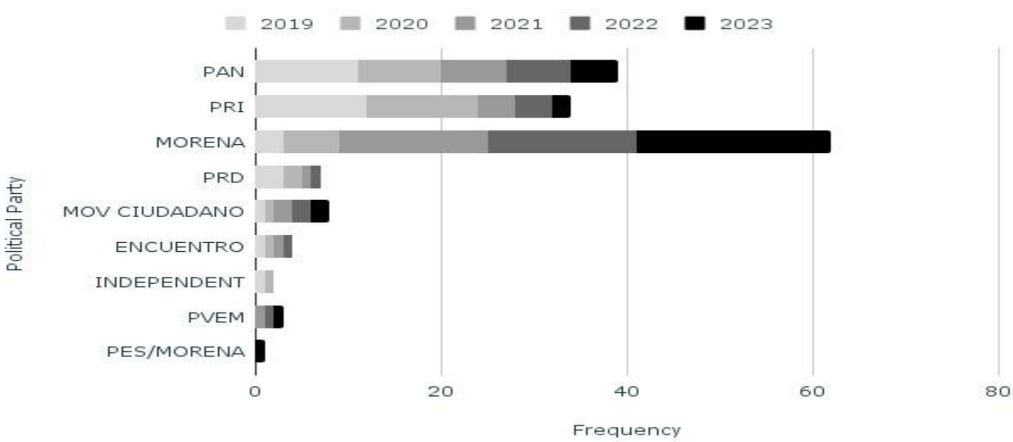
Findings/results

We found a positive relationship between FDI attraction and the independent variables (Competitiveness, Insecurity Perception Index, GDP, and Political Party). Competitiveness (p.value=0,02352121192) and GDP (p.value=0,007542286616) exhibit lower p-values, indicating their significant role in attracting investment. The Competitiveness variable, based on the IMCO index, is composed of several factors such as labor, infrastructure, technology, security, natural resources, education, health, and government, among others. The more competitive a state is, the more capital it attracts. Mexican States with higher competitiveness scores are those that receive greater investment. The GDP variable considers economic activity, representing the total value of production. Mexican States with higher GDP tend to attract more capital, as investors seek regions with strong productive activity. For this reason, these variables are the most significant. Investors prioritize states with higher competitiveness and economic productivity than other states when making investment decisions.

Although the Perceived Insecurity Index is farther from zero and closer to one (p.value=0,8916020726), it suggests that insecurity perception is not significant for investment within this model. Typically, a p-value closer to zero would indicate a stronger negative effect on investment. However, the results show the opposite: capital continues to flow despite the insecurity level. This implies that while insecurity perceptions exist, other economic drivers may outweigh risk factors in investors' decision-making.

Finally, the political parties that governed the states of the Mexican Republic during the studied period were: the Ecologist Green Party of Mexico (PVEM), the National Action Party (PAN), the Institutional Revolutionary Party (PRI), the National Regeneration Movement (MORENA), the Party of the Democratic Revolution (PRD), the Citizens' Movement (MOV CIUDADANO), the Social Encounter Party (ENCUENTRO SOCIAL), an Independent Candidate (INDEPENDENT), and the coalition between the Social Encounter Party and the National Regeneration Movement (PES/MORENA).

Graph 1. Frequency of political parties in the period 2019 to 2023.



Source: Own elaboration with National Electoral Institute (INE) data.

The most significant result is **p.value = 0.2620413567**, which indicates that San Luis Potosí, governed by the PVEM, has successfully attracted foreign investment. However, it is important to highlight that this political party has only been for three years and has never previously governed this state. Therefore, it could be expected that, as its first time in office, it would strive to achieve positive results. (See table 1 and 2).

The second political party with the best results is the Party of the Democratic Revolution (PRD), with a **p.value = 0.6832345506**. This party has governed the states of Michoacán, Quintana Roo, and Mexico City, meaning its national presence is minimal. However, having governed Mexico City for three years contributed to this **p.value**, as most multinational corporations in Mexico establish their headquarters there, making it a city with strong capital attraction. (See table 1 and 2).

The third-best result, with **p.value = 0.7499508395**, corresponds to the National Regeneration Movement (MORENA), which currently governs 23 of the 32 states of the Mexican Republic. Despite its territorial dominance, the result in attracting foreign direct investment is not favorable due to its political ideology. (See Graph 1).

The fourth place, with a **p.value = 0.7996661199**, corresponds to a political party with an Independent Candidate who governed only the northern state of Nuevo León for two years during the studied period. Despite being the most productive state in the country, its impact on investment attraction was limited. (See table 1 and 2).

The National Action Party (PAN) ranked fifth in significance, with a **p.value = 0.8044891308**. By 2019, this party governed eleven states in Mexico, but by 2023, it had reduced to just five states. The loss of six states contributed to a decrease in the significance of its relationship with foreign investment attraction. (See graph 1).

The Citizens' Movement Party yielded weakly significant results, with a **p.value = 0.8278609352**. In 2019 and 2020, it only governed the state of Jalisco, and in 2021, Nuevo León was added. Its limited national political participation contrasts with MORENA’s growing dominance. It is worth noting that both Jalisco and Nuevo León are highly productive states. However, despite this, the relationship between the Citizens' Movement Party and investment attraction is not particularly significant. (See table 1 and 2).

The Institutional Revolutionary Party (PRI) ranked seventh, with a **p.value = 0.9242030211**. This result demonstrates a significant loss of credibility for this party in the country, despite having been Mexico’s dominant party for decades. By 2023, it governed only two states: Coahuila and Durango, with the former being highly productive. (See table 1 and 2).

Among the lowest-ranking parties are the Social Encounter Party and its coalition with MORENA, which governed only one state in the country. (See Graph 1).

It is important to highlight that during this period, **the COVID-19 pandemic** was a determinant factor affecting foreign direct investment inflows, as well as the presence of the MORENA party in the presidency of the republic. (See table and graph 1).

Table 1. Negative Binomial Regression Model Results

Variables	Estimate	Std.error	Statistic	P.value
INTERCEPT	3,066701664	1,311757251	2,337857604	0,01939463622
COMPETITIVENESS	0,2670087824	0,117891908	2,26486098	0,02352121192
INSECURITY PERCEPTION INDEX	-0,00097088994	0,00712437051	-0,1362772948	0,8916020726
GDP	0,2072539015	0,07756795295	2,671901135	0,007542286616
POLITICAL PARTY "ENCUENTRO SOCIAL"	0,06466420305	1,541828809	0,04193993696	0,9665465793
POLITICAL PARTY "INDEPENDENT"	-0,3624448854	1,428189709	-0,2537792305	0,7996661199
POLITICAL PARTY MORENA	0,3555746932	1,115688805	0,3187041868	0,7499508395
POLITICAL PARTY "MOV CIUDADANO"	0,2725453075	1,253394165	0,2174458084	0,8278609352
POLITICAL PARTY "PAN"	0,2750097702	1,110964028	0,2475415613	0,8044891308
POLITICAL PARTY "PES/MORENA"	-31,6365262	514675,841	-0,0000614688386	0,999950955
POLITICAL PARTY "PRD"	0,4929103997	1,207955946	0,4080532916	0,6832345506
POLITICAL PARTY "PRI"	-0,1072072298	1,126827524	-0,09514076248	0,9242030211
POLITICAL PARTY "PVEM"	1,472184733	1,312599771	1,121579301	0,2620413567

Source: Own elaboration using R Studio programming language.

Table 2. Political parties by state in the period from 2019 to 2023.

STATE	2019	2020	2021	2022	2023
Aguascalientes	PAN	PAN	PAN	PAN	PAN
Baja california	PAN	MORENA	MORENA	MORENA	MORENA
Baja california sur	PAN	PAN	MORENA	MORENA	MORENA
Campeche	PRI	PRI	MORENA	MORENA	MORENA
Chiapas	MORENA	MORENA	MORENA	MORENA	MORENA
Chihuahua	PAN	PAN	PAN	PAN	PAN
Coahuila	PRI	PRI	PRI	PRI	PRI
Colima	PRI	PRI	MORENA	MORENA	MORENA
CDMX	PRD	MORENA	MORENA	MORENA	MORENA
Durango	PAN	PAN	PAN	PAN	PRI
Estado de México	PRI	PRI	PRI	PRI	MORENA
Guanajuato	PAN	PAN	PAN	PAN	PAN
Guerrero	PRI	PRI	MORENA	MORENA	MORENA
Hidalgo	PRI	PRI	PRI	PRI	MORENA
Jalisco	MOV CIUDADANO	MOV CIUDADANO	MOV CIUDADANO	MOV CIUDADANO	MOV CIUDADANO
Michoacán	PRD	PRD	MORENA	MORENA	MORENA
Morelos	ENCUENTRO SOCIAL	ENCUENTRO SOCIAL	ENCUENTRO SOCIAL	ENCUENTRO SOCIAL	PES/MORENA
Nayarit	PAN	PAN	MORENA	MORENA	MORENA
Nuevo León	Independiente	Independiente	MOV CIUDADANO	MOV CIUDADANO	MOV CIUDADANO
Oaxaca	PRI	PRI	PRI	PRI	MORENA
Puebla	PAN	MORENA	MORENA	MORENA	MORENA
Querétaro	PAN	PAN	PAN	PAN	PAN
Quintana Roo	PRD	PRD	PRD	PRD	MORENA
San Luis Potosí	PRI	PRI	PVEM	PVEM	PVEM
Sinaloa	PRI	PRI	MORENA	MORENA	MORENA
Sonora	PRI	PRI	MORENA	MORENA	MORENA
Tabasco	MORENA	MORENA	MORENA	MORENA	MORENA
Tamaulipas	PAN	PAN	PAN	PAN	MORENA
Tlaxcala	PRI	PRI	MORENA	MORENA	MORENA
Veracruz	MORENA	MORENA	MORENA	MORENA	MORENA
Yucatán	PAN	PAN	PAN	PAN	PAN
Zacatecas	PRI	PRI	MORENA	MORENA	MORENA

Source: own elaboration with National Electoral Institute (INE) data.

Discussions and conclusions

The study demonstrates that state competitiveness is the most influential factor in attracting Foreign Direct Investment (FDI) in Mexico. States with higher competitiveness, as measured by IMCO's State

Competitiveness Index (SCI), tend to attract more foreign investment. In addition, state GDP also has a positive relationship with FDI attraction, suggesting that investors prefer regions with strong economic activity.

On the other hand, although the perception of insecurity harms investment, its effect is less than expected. Despite high rates of insecurity in some states, investment continues to flow, indicating that other factors such as infrastructure, regulation, and economic stability, can counteract the effects of insecurity.

The analysis of political parties in government shows that some states governed by the Green Ecologist Party of Mexico (PVEM) and the Party of the Democratic Revolution (PRD) have had better results in attracting FDI compared to MORENA, which, although it dominates territorially, has a political ideology could generate uncertainty for investors.

The study highlights the importance of generating public policies that strengthen competitiveness and economic stability to maintain and increase foreign investment.

Limitations and direction for future research

Restricted temporal data:

The research covers from 2019 to 2023, which limits the possibility of analyzing long-term trends. Conjunctural factors, such as the COVID-19 pandemic, could have influenced investment flows.

Use of specific models: While Poisson and negative binomial regression models were adequate for the analysis, other econometric approaches could provide greater precision in assessing the impact of insecurity and competitiveness.

Factors not considered: Although competitiveness, GDP, perception of insecurity, and political party in power were analyzed, other elements such as infrastructure quality, fiscal incentives, and trade agreements were not included in the model.

Measurement of perception of insecurity: INEGI's Insecurity Perception Index was used, which may differ from actual crime rates, affecting the interpretation of its impact on FDI.

Direction for future research

- Extending the study period
- Analyzing historical data and projecting future trends could provide a more complete picture of the impact of competitiveness and security on FDI.
- Incorporation of more variables: Infrastructure and tax incentives, could be included in future models to assess their impact on investment.
- International comparisons: Comparative studies with other Latin American countries could identify best practices in attracting FDI.
- Effects of government policies: Evaluate how changes in public policies affect the perception of risk and competitiveness of the states.
- Sectoral analysis: Identify which economic sectors are more sensitive to competitiveness and the perception of insecurity within foreign direct investment.

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