Foreign Direct Investment, Military Spending and Geopolitical Risk in the Middle-Eastern Europe

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In both developed and developing economies, foreign direct investment (FDI) is a critical factor in driving economic growth. Defence economists are passionate about the influence of military expenditure on economic growth; however, there is a dearth of research on the impact of military spending (MS) on FDI. The empirical literature on this topic is quite scarce (Drazen, Hite-Rubin, 2016), and the majority of existent studies concentrate on developing countries (Hansen and Rand, 2006; Aziz and Khalid, 2019). Furthermore, researchers differ in their assessments of the direction and magnitude of the MS-FDI relationship. On the one hand, a rise in defence load may result in increased national security, political stability, and support business environment; on the other hand, it may trigger a crowding-out effect, limiting resources available to the civilian sector and signaling the emergence of a geopolitical threat.

Given the aforementioned, the MS-FDI relationship is cognitively intriguing in the context of Central and Eastern Europe, as the economies of this region are currently confronted with a dual challenge: on the one hand, they require foreign capital to avoid the middle-income trap and continue the integration process (Brixová et al. 2026; Farkas, 2026), and on the other hand, they must increase defence spending due to their high exposure to security threats (Waszkiewicz and Taksas, 2023).

The authors employed panel models (parametric and non-parametric) to diagnose the relationship between MS and FDI, in accordance with the experiences of Poland, Hungary, Romania, Bulgaria, Slovakia, Lithuania, Latvia, and Estonia from 1995 to 2024. The results obtained suggest that the economies of the region are highly heterogeneous, and that the scale of foreign investment flowing into host economies is influenced by military expenditure and geopolitical risk.

Literature:

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