Policy Brief

An evaluation of the industrial sector in the Dominican Republic: Risks, Vulnerabilities and Potential Outlook

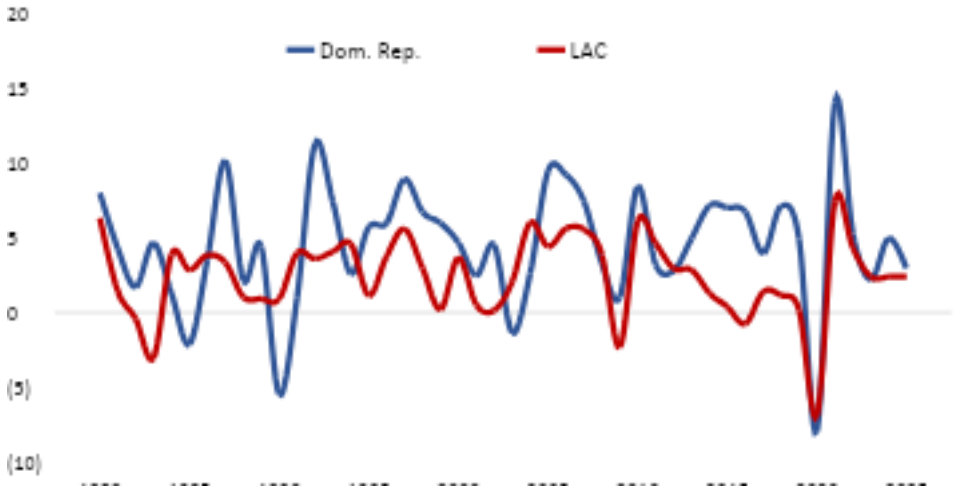
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Abstract

The Dominican Republic's sustained economic growth over the past four decades has been closely linked to the expansion of its industrial sector, particularly through Special Economic Zones (SEZs) and export-oriented manufacturing. Structural reforms since the 1980s have driven diversification away from agriculture, increased foreign direct investment, and strengthened export performance, contributing to greater macroeconomic stability. Despite these gains, key structural challenges persist, including high labor informality, weak linkages between SEZs and the domestic economy, institutional and regulatory inefficiencies, and exposure to external shocks. These constraints raise concerns about the long-term sustainability of the current growth model. To address these issues, policymakers should prioritize reforms aimed at improving productivity, strengthening domestic value chains, and enhancing the business environment. At the same time, emerging opportunities such as nearshoring and global supply chain realignment present a strategic pathway to attract higher-value investment and upgrade industrial capacity. A forward-looking and targeted industrial policy framework will be essential to sustaining growth, boosting competitiveness, and reinforcing economic resilience over the long term.

The Dominican Republic (DR) has been one of the most successful economies of the Americas over the past 50 years. Since the 1980s, real GDP of the DR (4.5%) has grown almost twice as fast compared to the average of Latin American Economies (2.4%), and the growth of real GDP per capita (3.0%) has almost quadrupled that of the region (0.8%) during this period.

Figure 1: Real GDP growth (%)



Source: International Monetary Fund, WEO 2025 Dataset

The current challenge for policy makers is to understand the factors that have driven the success of the Dominican economy, in order to understand whether this rate of growth can be sustained over the next few decades or what structural changes are needed, if any, to achieve this goal.

How did we get here?

Pozo et al. (2010) argue that the economic success of the Dominican Republic can be attributed to three main pillars of the Dominican policy agenda; (1) the structural reforms that began during the 1980s, which helped diversify the economic structure of the country; (2) the implementation of Special Economic Zones (SEZs) that guided a more opened policy stance against the rest of the world, and at the same time attracting FDI; and (3) a social engagement strategy that facilitated learning and the development of human capital.

The first pillar, a sectoral diversification of economic production in the country, began in the 1980s, and continued into the 1990s with the implementation of SEZs. These reforms resulted in an important shift from agricultural production into a more serviced based economy. By the first decade of the 21st century, the Dominican economy had reduced the share of agricultural production from 25% of GDP in 1970, to just 5% in 2018, while the service sector increased from 40% to 60% of GDP during this time (Pozo and Giraldi, 2020). The aim of this policy was to diversify the economy and reduce the vulnerabilities stemming from natural and seasonal factors associated with agricultural production.

During the 1990s, a second important reform aimed to foster the openness of the country with the rest of the world and promote exchange rate flexibility, by providing fiscals incentives to export based companies. These incentives were intended to attract foreign companies to invest in the

country, boosting employment, exports, and human capital through the SEZ sector, both in manufacturing and services. Furthermore, these reforms, along with the fiscal reform mentioned below, were the first attempt by the country to move toward complying with WTO trade standards (WTO, 1996)

As a result of these policies, other important reforms were necessary to balance the economy, such as a tax reform to compensate for the foregone revenue by the government, and other institutional reforms such as the constitutional and the labor reforms (Andujar, 2005), and later, the social security reform. While it is difficult to isolate the direct impact of each reform on the success of the Dominican economy, it is safe to argue that it has been a combination of all these policies that fueled the economic growth during the las 30 years.

What have we achieved?

The reforms mentioned before had a direct and indirect impact on the Dominican economy. The agricultural sector that once represented over 20 percent of the economy, was reduced to around 5 percent in the 2010s and 2020s. The decrease in agriculture was compensated by the industrial sector, and an increase in the service sector, particularly tourism (Pozo and Giraldi, 2020).

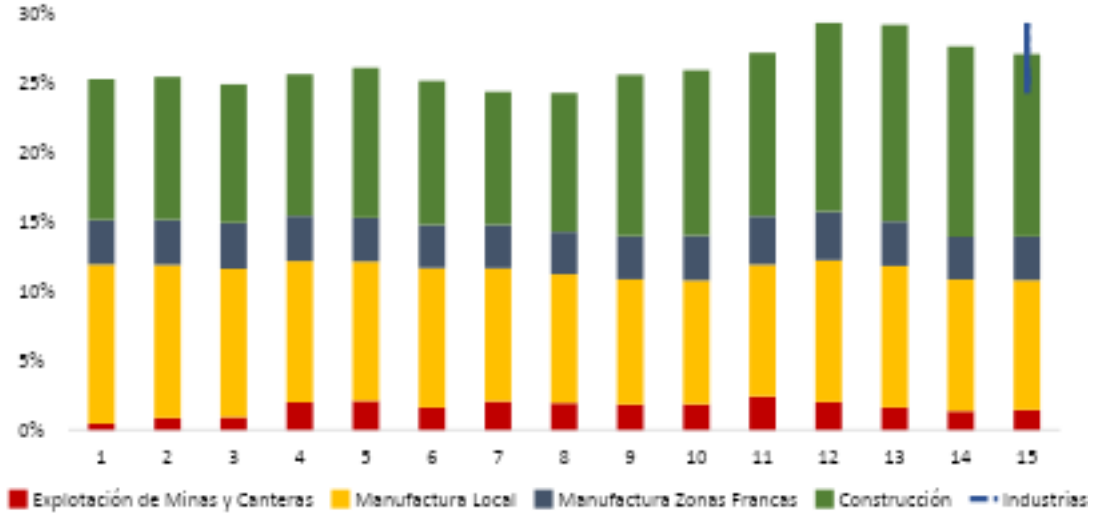
Figure 2: Foreign Direct Investment – millions of USD



Source: Central Bank of the Dominican Republic

The incentives directed toward the SEZs attracted foreign investment, boosting FDI from less than US$200 million in 1993 to over US$1,300 million in 1999, an increase over 600% during that period. FDI continued growing over the next decade (figure 2), with the industrial and tourism sectors representing almost 50 percent of the increase.

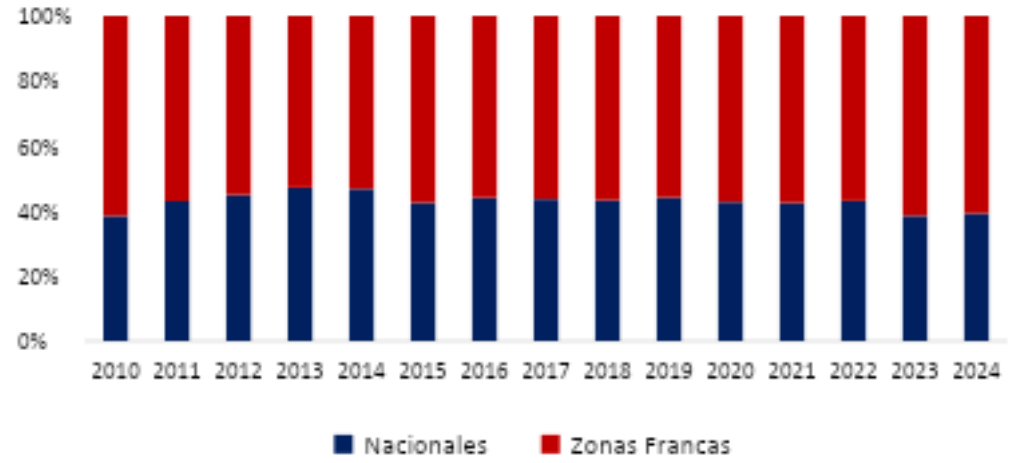
Figure 3: Share of the Industrial Sector as percent of GDP



Source: Central Bank of the Dominican Republic

The industrial sector has maintained its relevance in the Dominican economy, representing around 25 percent of GDP (figure 3), and 16 percent of formal employment. Similarly, SEZs export has continued growing, representing around 60 percent of industrial exports (figure 4).

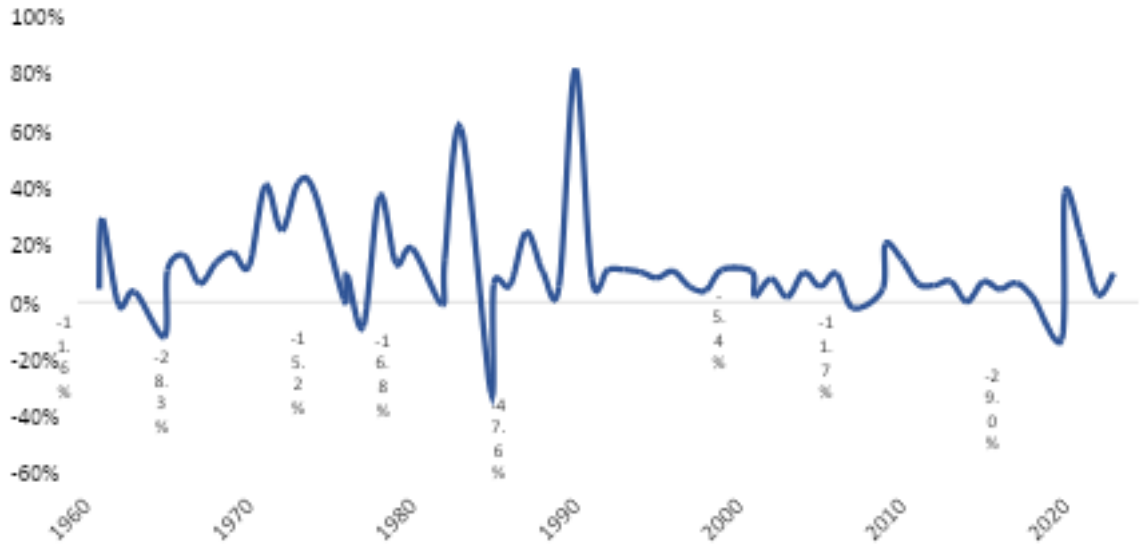
Figure 4: Share of total exports by sector



Source: Central Bank of the Dominican Republic

It is important to point out that the growth of SEZs and tourism exports has also reduced the vulnerabilities of the external sector, given that Dominican exports were mainly concentrated on agricultural products. For example, constants changes in the US sugar quota policies during the 1960s through 1980s, played an important role on the development of Dominican exports during this period, which resulted in periods of high volatility with several years of large contractions. Since the 1990s, Dominican exports have continued to grow but with significantly lower volatility (figure 5). Furthermore, the only periods of contractions since the 1990s have coincided with either domestic or global crisis (2001, 2009 and 2020). In fact, in 2022 the DR was subject to a sugar import ban by the US, which resulted in a decrease of domestic export. However, the reduction in sugar exports was compensated for by an increase in both tourism exports and SEZ exports, resulting in an expansion of total exports during that year.

Figure 5: Total exports of the Dominican Republic - annual growth (%)



Source: World Bank - World Development Indicators.

Therefore, the policies implemented during the 1990s has played a crucial role, not only on boosting investment and employment, but also by helping diversify the country's composition of exports, which has allowed the DR to sustain its exports growth with lower volatility and fewer downturns.

Legal Framework – Special Regimes for the Industrial and Export Sectors

Based on the legal framework outlined in the Tax Expenditure Report (Ministerio de Hacienda, 2025), these are the main regulations associated with the industrial and export sectors:

Free Trade Zones (Law 08-90, Decree 977-02, Laws 139-11 & 253-12)

- Promote national development through foreign trade, job creation, and technology transfer.
- Fiscal incentives: exemptions from income tax, asset tax, municipal taxes, VAT (ITBIS), import/export duties, and construction-related taxes.
- Local sales subject to a small tax (currently 3.5%).

Exporters (Law 84-99)

- Companies may import raw materials, inputs, and machinery duty-free under the Temporary Admission regime.
- Condition: final products must be re-exported.
- Main benefit: elimination of import duties and taxes on raw materials used for exports.

Textile Chain (Law 56-07)

- Grants priority and incentives to textile, apparel, footwear, and leather manufacturing sectors.
- Benefits: exemption from VAT (ITBIS), income tax, other taxes under Law 11-92, and export tariffs (up to 100% for finished goods).
- Applies only to companies compliant with tax obligations and authorized by the National Free Trade Zone Council.

PROINDUSTRIA (Law 392-07, amended by Laws 542-14 & 242-20)

- Aims to modernize and strengthen the national manufacturing industry.
- Incentives include:
    - Deduction of up to 50% of taxable income for investments in machinery/technology.
    - Exclusion of modernized assets and approved imported machinery from asset tax.
    - Choice between accelerated depreciation or investment credit (not both).
    - Incentives extended for 15 years under Law 242-20.

Therefore, the Dominican industrial and export laws provide broad tax exemptions and incentives to encourage investment, exports, and modernization, especially in Free Trade Zones, export-oriented industries, textiles, and manufacturing under PROINDUSTRIA.

However, whether these benefits are still effective, or whether they are enough to keep boosting productivity and growth over the next few decades is an open question for policymakers[1]. It is imperative to evaluate if these incentives need to be redefined or extended to other potential sectors that would drive new investments and jobs. The following section outlines some of these potential opportunities for the country, as well as some of the challenges it could face moving forward.

Future outlook and balance of risks

The Dominican Republic's growth model remains robust but is heavily depended on its ability to address external exposure, productivity constraints, and sustain business confidence. While the reforms implemented during the 1990s and early 2000s have boosted investor´s confidence and economic growth, the country will face some challenges to sustain this level of growth over the medium term. First, the Dominican economy is much different now than what it was thirty years ago. Second, as the country continues to close the gap to advance economies, it becomes more difficult to sustain high levels of growth, due to diminishing returns and the concavity of the growth function. Furthermore, the last decade has presented a complex global environment, introducing new sources of potential risks on the global scale, such as climate change, the global pandemic and supply chain disruptions, restrictive trade policies, among others.

Therefore, policy makers need to plan strategically to design a structural plan that will help the economy navigate these challenges, while continuing to build the structural and economic infrastructure to support long term growth. The table below presents the current balance of risks for the Dominican economy, with potential sources of levers that could help to foster future investments:

Table 1: Dominican Republic – Risk balance assessment

Type of Risk	Specific Risk	Time Horizon	Economic Impact	Potential Lever for Investment & Growth
Productivity	▪ High informality (~50% of employment) ▪ Weak linkages between free zones and local economy	Long term	High	▪ Labor formalization policies; Small and medium enterprises support; ▪ Develop local supplier ecosystems ▪ Cluster-based industrial policy

[1] World Bank (2016) presents a detailed description of the gains and challenges of SEZs in the Dominican Republic.

Type of Risk	Specific Risk	Time Horizon	Economic Impact	Potential Lever for Investment & Growth
Institutional / Business Climate	▪ Bureaucracy ▪ Regulatory	Medium–long	High	▪ Streamline permits; judicial reform; ▪ Strengthen rule of law and enforcements
External / Cyclical	▪ High dependence on U.S. economy (exports, remittances) ▪ Tourism sensitivity to global shocks	Short-term	High	▪ Diversify export markets; Strengthen regional trade integration; ▪ Expand high-value exports ▪ Upgrade tourism (luxury, eco, cultural) ▪ Strengthen the link between tourism and domestic supply chains
Macroeconomic/ Exogenous	▪ Climate and natural disasters	Short–medium	High	▪ Invest in climate-resilient infrastructure ▪ Expand insurance and mitigation mechanisms

While these risks pose a challenge in the medium and long term, policymakers have plenty of options to choose from in order to foster innovation and investment. For example, the country could take advantage of recent developments on global supply chain realignments by exploiting near shoring opportunities focused on higher value production and knowledge transfer, given its strategic location. Furthermore, policymakers should take advantage of the macroeconomic stability and investors' confidence observed over the past decades to capitalize on the country's sound economic and institutional fundamentals.

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