Accepted Manuscript

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PII: S0939-3625(18)30064-5
DOI: https://doi.org/10.1016/j.ecosys.2017.03.003
Reference: ECOSYS 643

To appear in: *Economic Systems*

Received date: 8-2-2016
Revised date: 30-1-2017
Accepted date: 13-3-2017

The impact of value added components of GDP and FDI on economic freedom in Europe

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Highlights

- Growth in the industrial and service sector positively affects economic freedom.
- Growth in the agricultural sector decreases economic freedom.
- Marginally significant evidence is found for a relationship between FDI and economic freedom.
- The impact of GDP growth and FDI on economic freedom is fairly consistent among CEECs and Western European countries.

Abstract

This paper investigates the possibility of a long-run relationship between the Economic Freedom Index (EFI), Foreign Direct Investment (FDI) and value added components of GDP in thirty Eastern, Central and Western European countries. The study further examines whether the FDI and sector-specific components of GDP have any significant impact on economic freedom for these countries. We use annual data and employ Pedroni and KAO panel cointegration analyses to assess the long-run relationships. The results indicate that there is a significant long-run relationship between the variables under study. Moreover, the evidence shows that the service and industry value added components positively affect EFI, while the agriculture value added component has a negative effect on EFI. However, contrary to the prior literature, we