Economic freedom, corporate investment and financing constraints.

Alfonsina Iona
School of Economics and Finance
Queen Mary University of London

Leone Leonida
King's Business School
King's College London

CFMS Statistics
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Abstract

Using the economic freedom indices, empirical evidence has been reported about the positive effect of economic freedom on economic growth. Nevertheless, a theoretical model formalizing explicitly the micro-economic channels through which economic freedom affects firm investment has not been developed. Using a generalized Q model of investment, this paper studies the impact of economic freedom on corporate investment, in presence of capital market imperfections. The theoretical predictions of the model are tested on a large and heterogeneous sample of non-financial US firms over the period 2000-2016. E mpirical results support the view that economic freedom enhances economic growth, as they show that economic freedom enhances corporate investment and mitigates the negative impact of financing constraints on corporate investment. These effects are strong and robust for the Economic freedom index and most of the Economic freedom components.