

Misallocation of Factors of Production

What is the issue?

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India is facing major problem of misallocation of factors of production which primarily involves land and capital.

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What are the issues with allocation of land and capital?

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- **Land** -In India land misallocation is worse than labour misallocation.

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- Low-productivity firms have better access to land and buildings than high-productivity firms.

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- **Capital** -Firms in the organised sector have much higher access to loans compared to firms in the unorganised sector.

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- There are urban-rural and gender based disparities in access to finance, with rural locations lagging their urban counterparts.

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What are the impacts of misallocation?

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- In India start-ups are often backed by bank loans for which land is used as collateral.

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- Due to highly distorted land allocation bank loan allocation is also distorted, given the misplaced collateral channel.

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- Empirical evidence provides substantial confirmation in the links between land misallocation and financial misallocation at the district level.
- It leads to low proportion of manufacturing establishments access financial loans in India (8 per cent), it also covers huge spatial, sectoral, and gender differences.

What measures needs to be taken?

- Economic growth can be enhanced only by the reallocation of the factors of production from less-productive to more-productive firms.
- Bank and corporate restructuring may not be enough to put growth on a higher trajectory, policy makers need to pay more attention to addressing the underlying causes of factor misallocation.
- This would involve removing land market distortions, better land-use regulations, and more efficient taxation of properties.

- Disparity against women-owned enterprises and other gender gap in business environment needs to be addressed to attain an inclusive growth.

Source: Business standard