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PRIORTY SECTOR LENDING IN INDIA: A STUDY OF COMMERCIAL BANKS

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Abstract

An effective banking system lends support to the economy of nation. A banking institute is indispensable in a modern society. It's is comparable to heart of the economic organism pumping out the investible funds in diverse channels. It forms the core of the financial system of country. Although the financial system of India is still characterized by the existence of both the organized and unorganized segments, but amongst the institutions in the organized sectors, commercial banks are the oldest institutions having a wide network of branches, commanding utmost public confidence and having the lion's share in total banking system. They play a pivotal role in the economic development of a country.

Introduction

Financing of priority sector of the economy by the commercial banks is one of the important indications of the socialistic approach of the banks. 1992, over fourth fifth of the advances of commercial banks want to industry and commerce with only about two percent of bank credit for agriculture, mostly to large plantations, and less than two per cent of advances for retail trade. In 1992- 1998 the Government of India initiated social control over banks with a view to aid sectors like agriculture and small scale industries. Future, national credit council set up in February 1998, submitted is report on July 24, 1998 and emphasized that commercial banks should increases the financing to Priority Sectors, viz. agriculture and small scale industries. The report pointed out that the commercial banks met the credit requirement of large scale industries, retail trade and small borrowers were advances very small share of total bank credit. Future, in July 1998, the nationalization of 14 Major commercial banks led to a considerable reorientation of bank lending to the priority sector.

Nationalization of banks

The nationalization of 14 major commercial banks in 1969 led to a significant shift in bank lending, focusing on priority sectors of the economy. This reallocation of banking resources aimed to meet socio-economic needs, involving banks in socially desirable sectors and providing credit facilities to borrowers of all means. The concept of priority sector lending evolved to ensure assistance flowed to vital sectors and national priorities. The priority sector in India includes agriculture, small scale industries (SSI), retail trade, road and water transport operators, professional and self-employed persons, housing, education loans, microcredit, and software. The weaker sections include small and marginal farmers, artisans, village industries, beneficiaries of the Swarnajayanti Gram Swarojgar Yojana, and Scheduled Castes and Scheduled Tribes. Priority sectors for scheduled commercial banks include agriculture (direct and indirect finance), small scale industries (direct and indirect finance), and small business/service enterprises.

Major Issues

Bank profitability in India has been impacted by factors such as increasing deposit resources under statutory liquidity pre-emption, shifts in saver preferences, and non-performing assets. Mandatory credit, high non-performing assets, and quantitative targets have led to concerns about the viability of lending institutions. Government interference in public sector banks has resulted in loans being delivered to the rich, while transaction costs are exacerbated by time-consuming and manpower-intensive sanctioning and monitoring of small advances. These deficiencies have lowered the quality of credit and effectiveness of its delivery.

Growth of Priority Sector in India

Priority sector lending in India began in 1969, requiring SCBs to lend 40% of their adjusted net bank credit or credit equivalent of off balance. Banks in India have been able to meet regulatory obligations in the priority sector by using various methods, such as inter-bank participation certificates, securitization of loans, and depositing shortfalls in funds like the Rural Infrastructure Development Fund. In 2016, the introduction of trading in priority sector lending certificates (PSLCs) allowed banks to buy for shortfall and selling for overachievement of PSL targets without transferring loan, cash flows, or risk. Asset quality plays a significant role in priority sector lending decisions, with banks that face asset quality stress tended to lend less. The introduction of PSLCs has allowed banks to profitably trade in PSLCs while fulfilling regulatory targets.

Impact of Priority Sector Lending

The Priority Sector Lending (PSL) programme has been a significant public policy intervention in India since the 1970s, directing credit to sectors critical for employment and equity. This chapter examines the effectiveness of the PSL programme by analyzing its growth and distribution. Directed Lending Programmes (DLPs) have evolved over time, with international thinking influencing perceptions. The global financial crisis of 2008 highlighted informational asymmetries, credit rationing, and complex products in financial markets. Some countries have liberalized or discontinued their DLPs, while others have continued or strengthened them to deal with financial and economic crises.

Literature Review

Shete (2002) studied the performance of public, private, and foreign banks in disbursing credit to agriculture, small-scale industries, and priority sectors between 1990-91 and 2000-01. Despite financial sector reforms and special programs, few banks achieved the targets set by RBI. Private sector banks struggled to achieve priority sector advances for years after 1991 banking reforms. Foreign banks achieved targets but their share of export credit to total priority sector advances reduced**.**

Kamesam (2003) highlights the significance of small scale industries in India for sustainable growth, employment, entrepreneurial skills development, and export earnings. He highlights challenges faced by these industries and suggests future solutions.

Flow Sahu and Rajasekhar (2005) studied the trends in credit to agriculture by scheduled commercial banks from 1980-81 to 1999-2000. They found a decline in agriculture credit, particularly after banking sector reforms. They found a negative relationship between agriculture credit and government security investments, credit subsidies, and cooperative credit. They suggested enhancing credit delivery quality and prompt loan repayment.

Rao ET al. (2008) found that commercial banks' credit to small-scale industries is insufficient, with a continuous decline in the sector's share in total bank credit. Credit growth to small-scale industries fluctuated, with some exceptions. The spread of State Bank of India, foreign banks, and nationalized banks declined, while nationalized banks fluctuated between 2.1% and 3.5%.

Ahmed (2016): Examined a Priority Sector Lending by Commercial Banks in India. The study found that the level of NPAs in priority sector advances of commercial banks and the recovery performance of priority sector advances of banks over the years by the statistical tools like correlation analysis, regression analysis, growth rate analysis, parametric tests. He concluded that the banks are not able to reach the prescribed target of lending to priority sector

H.N. Hirakata et al. (2020): identified that lending to priority sector by private sector showed agrowth rate 34 to 46 percent and publlc sector banks showed 38 to 42 percent and said private sector banks are better than public sector Banks in priority lending.

Bhargava Pandya (2020). Analyzed that priority sector advances showing high impact on the profitability of scheduled commercial banks in India by studying the Variables Return on Assets, Return on Investment, Return on Equity, Ratio of Operating Profit and Ratio of Interest Income to Total Assets.

Objectives of the Study

1. To study the growth of commercial banks in the state of Punjab.
2. To examine the RBl's policy on lending to Priority Sector.
3. To examine the component-wise lending and to evaluate the performance of commercial banks with regard to Priority Sector Lending in the state of Punjab.

Scope of Study

The study investigates the growth and performance of commercial banks in Punjab, focusing on priority sector lending. It includes all existing commercial banks in the state and selects 100 beneficiaries from various sectors and commercial banks.

Research methodology

Data sources: The section discusses the collection of primary and secondary data, with primary data being collected through questionnaires and secondary data via the internet. Both methods will be used for data analysis.

Methods: The Research Method used for project is Descriptive method. Descriptive is used to describe data and characteristics about a population. It aims to determine, describe, or identify what is currently happening without control over variables.

Techniques of data collection and analysis: The research utilized a questionnaire to gather information from banks. The sample was selected using a convenience sampling method, which is a statistical method that selects people based on their ease of volunteering or availability. This method offers quick data collection but has disadvantages such as the risk of not representing the entire population and potential bias by volunteers

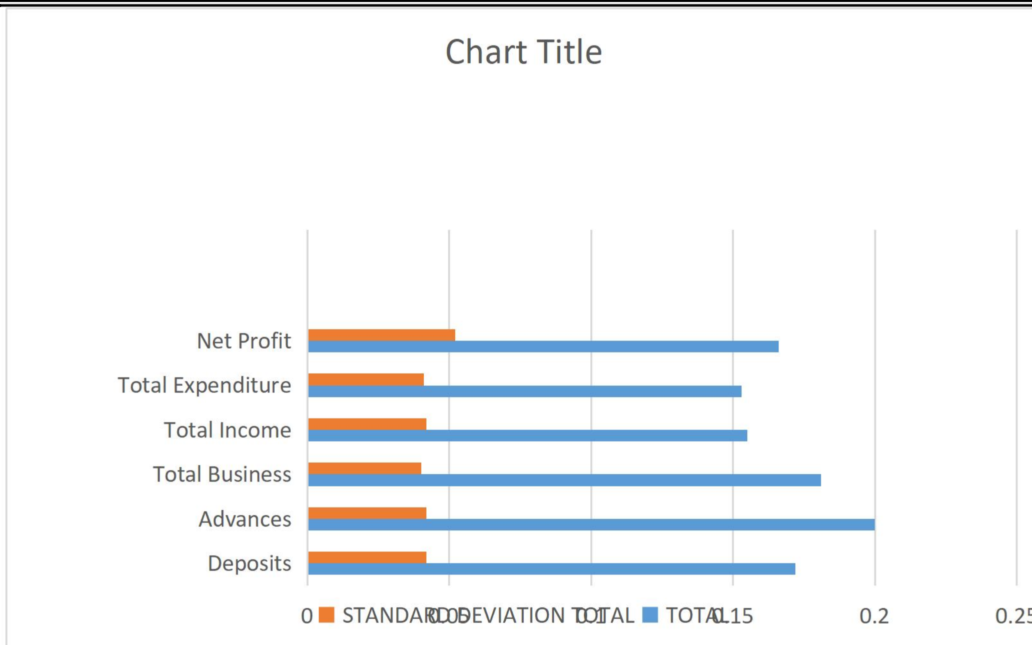
Sample and Sampling Design: A multi-stage sampling technique was used to assess beneficiaries' opinions on priority sector lending in Punjab, selecting 100 beneficiaries from both public and private sector banks in descending order based on their priority sector disbursement.

Data Interpretation & Analysis

Table - Average Growth of Indian Commercial Banking

Stasticstial Findings	Mean			Std. Deviation		
	Public Sector (N=25)	**Private Sector** (N=17)	**TOTAL** (N=42)	**Public Sector** (N=25)	**Private Sector** (N=17)	**TOTAL** (N=42)
Deposits	0.165	0.181	0.172	0.025	0.058	0.042
Advances	0.193	0.210	0.200	0.013	0.063	0.042
Total Business	0.174	0.191	0.181	0.014	0.059	0.040
Total Income	0.144	0.171	0.155	0.012	0.062	0.042
Total Expenditure	0.141	0.170	0.153	0.014	0.060	0.041
Net Profit	0.156	0.181	0.166	0.029	0.073	0.052

The chart presents a comparison between the total values and their corresponding standard deviations for six key financial indicators: Net Profit, Total Expenditure, Total Income, Total Business, Advances, and Deposits. The blue bars represent the total values, while the orange bars reflect the standard deviations, indicating the variability in each category. Among all, Deposits show the highest total value at approximately 0.20, followed closely by Advances and Total Business. These categories also display relatively low standard deviations, suggesting stable and consistent performance. Net Profit, although moderate in total value (~0.16), exhibits a slightly higher standard deviation, indicating more fluctuations compared to other metrics. Both Total Income and Total Expenditure maintain lower total values with minimal variability. Overall, the data indicates that the financial indicators are generally strong and stable, with minimal volatility across most categories, reflecting sound financial management and consistency in performance.



Findings

The findings from the chart indicate that the financial performance across all six categories—Deposits, Advances, Total Business, Total Income, Total Expenditure, and Net Profit—is generally stable and consistent. Deposits have the highest total value, followed closely by Advances and Total Business, suggesting these are the strongest areas of performance. The standard deviations for all categories are relatively low, which means there is minimal fluctuation in the data, indicating reliable and steady financial operations. However, Net Profit shows slightly higher variability compared to the other metrics, pointing to some inconsistency in profitability over the period analyzed. Overall, the organization demonstrates strong financial health with controlled variations, reflecting effective management and operational efficiency.

Suggestions

Previously, term loans were disbursed by term-lending institutions (ICICI and IDBI) and cash-credit facilities by banks. However, term-lending has disappeared, and banks now provide both term loans (TLs) and cash credit. Interestingly, term-lending of banks is still under PSL guidelines, and Tls to identified sectors are not covered under PSL. As banks have become the sole provider of institutional term credit, there is no need for a distinction between Tls and Cash Credit (CC) in meeting PSL targets. A survey questionnaire revealed that around 37% of managers face problems with inadequate and quality staff at the branch level to understand and process priority sector loans. Some respondents also raised issues of KYC, higher NPA, and profitability. The knowledge gap and lack of staff at the branch level are critical issues in a service-led industry like banking. Banks need to place the right person at the desired place to contribute more to the organization.

The government should make laws more stringent by amending the SARFAESI Act and DRT laws to effectively deal with bad loans, especially those created by suspected wilful defaults. The government should move swiftly to bring about changes to alleviate banks facing a continuous rise innon-performingassets.

In the last one and a half year, banks have opened around 18 crore of PMJDY accounts, and the government should fix a target for each bank to open and service PMJDY accounts in a year. This move will incentivize banks to open and maintain more PMJDY accounts.

Conclusion

Priority sector bank lending is a crucial part of India's financial policy, aiming to restore sectional balance in credit disbursement and channel credit to weaker sectors. The Bank Company Acquisition Act 1969 led to the nationalisation of 14 commercial banks, reorienting banking policy through social orientation and administrative intervention. The objective is to ensure that banking assistance flows more to sectors contributing significantly to the national product, such as agriculture, small scale industries, and weaker sections. Commercial banks have directed their lending towards large industrial houses, neglecting the agricultural sector, small scale industries, and weaker sections due to risk factors and urban bias. To ensure equitable credit distribution, targets and sub-targets financing of specific sectors have been envisaged. The share of priority sector in total bank advances is 40%, with sub-targets for agriculture and weaker sections fixed at 18% and 10%, respectively. Concessional rates of interest for priority sector advances and relatively higher rates for other sectors have been a special feature.

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