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Problems and prospects of priority sector Lendings by commercial banks in India

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Abstract
The priority sector lending norms have been fulfilled by a good margin by public sector banks at present. While public sector banks, continued to meet the target till 2009, however marginally fell short of the target of 40 per cent in March 2010. They also failed to achieve the various sub-targets for agriculture, tiny sector within the SSI sector, advances to weaker sections, etc. An important fact that the issue of priority sector lending, an important concern against privatization, is no longer that crucial. It is an interesting fact to note that the share of export credit in total net bank credit has been significantly above the prescribed sub-target of 12 per cent. Looking at the percentage share of credit to the sub-groups of the priority sector, it is observed that the credit to SSI sector of public sector bank groups has been declined by 6.4 per cent and 6.9 per cent respectively over time. On the other hand, the credit to other priority sector by public sector bank groups has been increased by 7.0 per cent and 12.3 per cent respectively over time.

Keywords: Priority, sector, Lendings, public sector bank, weaker and sections

Introduction
Priority Sector Lending' came through the idea of 'Direct Lending' by the banks to few needy and in adequately serviced sectors. RBI the central bank of India and also the Indian banks believed lending to the specific sectors and regulating the core sectors can bring about balanced growth, stability in the economy. Priority Sector includes the sectors of national importance, once they were not considered or neglected by the banks for the purpose of accessibility of credit are now considered to be as priority to provide credit as they are the corner stones for the country's true development. At Present the scope of the priority sector is very wide with many categories, targets and sub targets.
Extension of credit to small borrowers in the hitherto neglected sector of the economy has been one of the key tasks assigned to the public sector banks in the post-nationalisation period. At a meeting of the National Credit Council held in July 1968, it was emphasized that commercial banks should increase their involvement in the financing of priority sectors, *viz.* agriculture and small scale industries. The description of the priority sectors was later formalized in 1972 on the basis of the report submitted by the Informal Study Group on Statistics relating to advances to the priority sectors constituted by the Reserve Bank of India in May 1971. On the basis of this report, the Reserve Bank prescribed a modified return for reporting priority sector advances and certain guidelines were issued in this connection indicating the scope of the items to be included under the various categories of priority sector. Although initially there was no specific target fixed in respect of priority sector lending, in November 1974 the banks were advised to raise the share of these sectors in their aggregate advances to the level of 33.33 per cent by March 1979. Subsequently, on the basis of the recommendations of the Working Group on the Modalities of Implementation of Priority Sector Lending and the 20-Point Economic Programme by banks, all commercial banks were advised to achieve the target of priority sector lending at 40 per cent of aggregate bank advances by 1985. After this the priority sector advances has undergone several changes, since then, several new areas and sectors has being brought within the purview of this sector.
A need has therefore, been felt to review the concept and the segments of priority sector. Consequently, in paragraph 89 of the annual policy Statement of Reserve Bank of India for

the year 2005-2006, it was stated that prescriptions relating to priority sector lending have been modified from time to time and generally, the eligibility criteria have been enlarged to include several new areas. On the basis of this recommendation an Internal Working Group was set up in the Reserve Bank to examine the need for continuance of priority sector lending prescriptions, review the existing policy on priority sector lending, including the segments constituting the priority sector targets and sub-targets and to recommend changes, if any, required in this regard. It was decided to include only those sectors as part of the priority sector, that impact large segments of the population, the weaker sections and the sectors which are employment-intensive such as agriculture, and tiny and small enterprises.

The guidelines on lending to priority sector were revised with effect from April 30, 2007 based on the Report of the Internal Working Group on Priority Sector Lending (Chairman: Shri C.S. Murthy). The priority sector broadly comprises agriculture, MSEs, retail trade, micro credit, education and housing subject to certain limits. The guidelines take into account the revised definition of MSEs as per the Micro, Small and Medium Enterprises Development Act, 2006.

Review of Literature

Review of related literature makes the investigator fully aware with the previous work that has been done. It also provides an opportunity of gaining insight into the method, measures, subject and approaches employed.

Das, Uday Kumar, Lal (2002) [1], in his book Banking Reforms in Lead Bank Scheme, (Deep and Deep Publication, new Delhi) was the critical evaluation of the lead bank scheme in the light of banking sector reforms. Das in this book observed that high level of NPAs, large number of un-remunerative branches, low productivity, overstaff and archaic methods of operations have affected the profitability of public sector banks. Das sincerely felt that the whole banking sector in India is to be revolutionized to cope with the changing dimensions of the satellite one world. Further, he felt that the backward areas should be given more funds for investment in priority sectors and more and more people should be brought under its coverage and the procedures of extending credit should be simplified and there should be least hassle cost.

Sahu and Rajasekhar (2005) [2], in their research paper, analysed the trends in credit flow to agriculture by scheduled commercial banks during 1980-81 to 1999-2000. They observed that the share of credit to agriculture in total bank credit for all the bank groups declined significantly, especially after banking sector reforms in spite of many efforts. They analysed that scheduled commercial banks provided large quantum of funds to better-off farmers and to the activities earning high interest income only. They established the negative relationship between agriculture credit and investment in government security, credit subsidy and proportion of credit provided by the co-operative. They recognized that increasing lending rate reduced the credit disbursed to agriculture by scheduled commercial banks and affected the average quality of their loan portfolio so they suggested not to increase the interest rate to offset losses from defaults or to meet the lending cost, but to strengthen the quality of credit delivery system and ensure prompt repayment of loans for supporting the agriculture sector.

Rao (2006) [3], in his article, demonstrated the importance and progress of priority sector for economy during the period 1994-95 to 2003-04. He highlighted in his study that priority sector credit including farm credit of scheduled commercial banks declined during the said period indicating the preference of banks for bigger borrowers with higher credit limits instead of large number of small borrowers. He observed the decline in indirect credit to agriculture and small scale industries sector but relatively better position in credit to other priority sectors during the study period. He referred the recommendations of the Narasimham Committee 1991 and 1998 to redefine the concept of priority sector and also referred the observations of RBI committee to stress much on direct agriculture lending, small scale industrial lending, lending to small road and water transport operators (owning more than five vehicles), retail trade and small business under priority sector. In his study, he highlighted various problems of rural credit and suggested to improve input delivery system, water management system, power supply, irrigation facilities, market information and general rural infrastructure, educational and medical facilities, reforming RRBs, state and central co-operatives and scheduled commercial banks for extending rural credit in rural areas.

Uppal (2009) [4], in his research paper, evaluated the performance of public, private and foreign banks in India and analysed the target achievement by them during 2006-07. He found that priority sector advances of public and private sector banks were higher than foreign banks. He observed that public sector banks were unable to achieve the target of priority sector, while private sector banks have achieved the target. Private sector banks could not achieve the target for weaker section. Foreign banks could achieve the targets for priority sector, small scale industries sector and export sector. He further, found that NPAs of public sector banks was highest followed by private sector banks and foreign banks. Main reason for more NPAs in public and private sector banks was found to be more NPAs in agriculture sector. He examined various issues related to priority sector like, low Profitabilty, more NPAs, Government interference, high transaction cost, etc. He also suggested various strategies to overcome these issues.

Objectives of the study

The major objectives of the study was based on the following headings:

- To analyse the performance of commercial banks for priority sector Lendings.
- To study the prospects and major challenges for commercial banks in priority sector Lendings.

Methodology

The research design is qualitative in nature. The source of data is all secondary in nature. Published data in the form of journals, magazines and online- sources are being consulted. From those resources, articles, research papers.

Result and Discussion

The priority sector lending targets (40 per cent and 32 per cent for domestic and foreign banks, respectively) have been linked to the adjusted net bank credit2 (ANBC) or the credit equivalent amount of off-balance sheet exposures, whichever is higher, as on March 31 of the previous year, as against the previous practice of linking targets to the ongoing net bank credit. The formats used by banks to inform the Reserve Bank about their priority sector advances were revised with effect from September 2007. SCBs should furnish data on priority sector advances on a half-yearly (*ad hoc*) basis as on the last reporting Fridays of March and September of a particular year (within fifteen days from the reference date), asalso on a yearly basis (final data) as on the last reporting Friday of March of a particular year. RRBs were permitted to extend direct finance up to Rs.10 lakh to the housing sector in rural and semi-urban areas as part of priority sector lending, with the prior approval of their boards. In August 2011, the limit of board-approved direct finance to housing by RRBs was raised to Rs.35 lakh, irrespective of the area.

The Reserve Bank, in December 2011, allowed all loans granted by commercial banks/sponsor banks to RRBs for on-lending to agriculture and allied activities sector to be classified as indirect finance to agriculture in the books of the lenders. Consequently, the loans granted by RRBs out of the funds borrowed from commercial banks/sponsor banks may not be classified as their priority sector lending. RRBs should not include such advances as part of their bank credit for the purpose of computing their achievement level under priority sector lending. Following the announcement made in the Annual Policy Statement for 2011-12, in May 2011, the Reserve Bank allowed RRBs to sell the loan assets held by them under the priority sector categories in excess of the prescribed priority sector lending target of 60 per cent.

Domestic SCBs, both in the public and private sector, which fail to achieve the priority sector and/or agriculture lending targets, are required to deposit into the Rural Infrastructure Development Fund (RIDF) such amounts as may be allocated to them by the Reserve Bank. The Fund has completed thirteen years of operation. Domestic SCBs are required to lend 10 per cent of their ANBC or credit equivalent amount of off-balance sheet exposure, whichever is higher, to weaker sections. It was, however, noted that most banks were not meeting this sub-target for lending to weaker sections and hence in May 2011, the Reserve Bank advised that the shortfall in lending to weaker sections would also be taken into account for the purpose of allocating amounts to banks for contribution to the RIDF or funds with other financial institutions with effect from April 2012.

Credit to Micro, Small and Medium Enterprises (MSMEs) Sector

MSMEs are crucial to economic development as they further the objectives of employment generation, equitable distribution of national income, regional dispersal of industries, mobilisation of capital and entrepreneurial skills and enhancement of export earnings. MSMEs produce a wide range of products, from simple consumer goods to high precision tools and sophisticated highend products. To ease the difficulties faced by small manufacturing and services enterprises in accessing credit, the Code of Banks' Commitment to MSEs was formulated.

The SLBCs were advised in May 2011 to apprise all their members about the Government of India's decision to continue the credit linked capital subsidy scheme (CLCSS) for technology upgradation of MSEs during the Eleventh Five Year Plan (2007-12), subject to the following terms and conditions: (a) ceiling on the loan under the scheme would be Rs.1 crore; (b) the rate of subsidy would be 15 per cent for all MSE units up to the loan ceiling at (a) above; (c) calculation of admissible subsidy to be done with reference to the purchase price of plant and machinery instead of the term loan disbursed to the beneficiary unit; and (d) SIDBI and NABARD to continue as the implementing agencies for the scheme.

To ensure bank channelise a part of their credit to these sectors, the RBI has set guidelines defining targets for lending to priority sector as whole and in certain cases, sub-targets for lending to individual priority sectors. In addition to these limits, also a provision has been made that banks which could not meet the priority sector targets can deposit funds in the financial institutions like National Bank for Agriculture and Rural Development (NABARD) under Rural Infrastructure Development Fund (RIDF) or some banks can do so in the Small Industries Bank of India (SIDBI) for lesser interest rates, which in turn would be lent to the priority sectors.

Priority sector lending by scheduled commercial bank

Table 1: Priority Sector Lending by Schedule Commercial Banks (Amount in crore)

Item	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Priority Sector Advances	127478 (40.2)	149116 (43.7)	171185 (43.1)	203095 (42.5)	244456 (43.6)	307076 (42.8)	409748 (40.3)	521376 (39.7)	610450 (44.7)
Agriculture	45296 (14.3)	53571 (15.7)	63082 (15.9)	73507 (15.4)	84435 (15.1)	109917 (15.3)	155220 (15.3)	202614 (15.4)	249397 (18.3)
Micro and Small Enterprises	46045 (14.6)	48400 (14.2)	49743 (12.5)	52988 (11.1)	58311 (10.4)	67800 (9.5)	82434 (8.1)	102550 (7.8)	151137 (11.1)
Other Priority Sector	30816 (9.7)	40791 (12.0)	53712 (13.5)	71448 (15.0)	101710 (18.1)	125114 (17.4)	163756 (16.1)	206661 (15.7)	-

***Source*:** Report on Trend and Progress of Banking in India, RBI, Mumbai

The priority sector lending norms have been fulfilled by a good margin by public sector banks at present. While public sector banks, continued to meet the target till 2009, however marginally fell short of the target of 40 per cent in March 2010. They also failed to achieve the various sub-targets for agriculture, tiny sector within the SSI sector, advances to weaker sections, etc. An important fact that the issue of priority sector lending, an important concern against privatization, is no longer that crucial. It is an interesting fact to note that the share of export credit in total net bank credit has been significantly above the prescribed sub-target of 12 per cent.

Looking at the percentage share of credit to the sub-groups of the priority sector, it is observed that the credit to SSI sector of public sector bank groups has been declined by 6.4 per cent and 6.9 per cent respectively over time. On the other hand, the credit to other priority sector by public sector bank groups has been increased by 7.0 per cent and

12.3 per cent respectively over time. The increase in the share of priority sector credit in all bank groups could because of the substantial increase in the housing credit, as housing credit also forms a part of priority sector credit.

Conclusion

Public Sector Banks are the main pillars for the successful lending to priority sectors in India, the active participation by PSBs in meeting the targets of priority lending can increase the economy of India and also these banks are the motivating factor for all the banks in order to reach the targets of priority as well as the national interest of lending. PSBs are actively meeting RBI norms including agriculture, Micro, Small and Medium Enterprises and weaker sections. The Banking sector is now witnessing a new wave of evolution with innovations in the fintech space, espically with the proliferation of prepaid wallets. Finally the banking sector will need to master a new business model by building management and customer services. Thus, it is concluded from all the tables that lending to priority sectors are higher by the public sector banks. Public sector banks have achieved the overall target and sub-target. Non-achievement of agriculture lending target by many public sector banks is due to low capital formation in agriculture resulting in poor credit absorption and write-off of non-performing loans leading to reduction in the outstanding advances in the case of some banks. Lending to priority sector creates many problems for the Indian banks like low profitability, high NPAs, transaction cost etc. it is a need of the hour to find out solutions for these problems otherwise progress of the Indian banks will cease.

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