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Lending to Priority Sector in India: Some issues of Credit and NPAs of Public and Private Sector Banks

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Abstract: Priority sector lending has been an essentialfeature of India's credit policy.Priority sector lending has been in use for long, as an instrument to channelize credit to strategic sectors of the economy that have been marginalized by institutionalised credit delivery system. This programme ensures that the necessary bank credit be allocated forstrategically importantsectors of the economy.Priority sector lending was imbibed in the lending policy for the commercial banks in response to shortages of output in agricultural and industrieswhich caused severe imbalances in the economy after the independence and partisan of the country. Hence, the priority sector lending was used as a lively device for directing the credit flow to the neglected entities with a purpose to re-establish sectoral equilibrium. The program requires commercial banks to extend loans to strategic sectors: agriculture, exports, small business, housing, and economically weak sections of the society. Priority sector lending is still relevantfor economies like India as small scale entities have been backbone of our economy being employing the large section of population of the country. The present study is an attempt to analyse the status of credit allocation and NPAs of priority sector lending of public sector banks and private sector banks considering a period of 15 years from 2004-2005 to 2019-2020.

Keywords: Priority Sector Lending (PSL), NPA (Non-performing Assets),Annual Net Bank Credit (ANBC), Compound Annual Growth Rate (CAGR),Public Sector Banks (PSBs), Private sector Banks (PrSBs),

1. Introduction

Financial institutions ensuring allocation of funds play avital role in the growth of the economy. Commercial banks being the back-bone of the financial sector which derive the financial resources from the surplus units and allocate them for the productive activities of the economy. The commercial banks have been the pillars of the financing sector for distribution of necessary financial resource for the progression of the economy. After independence,it was observed that some strategic sectors of the economy i.e. agriculture, marginal entities and small and medium-sized units have not been getting the adequate lending support for the growth of their business from the financial institutions.Data suggests that about two percent advances were given to agriculture and retail trade in the year 1967 by the financial institutions. . So, there was a persistent demand for banking sector be brought under social control to channelize the funds for the neglected sector of the economy. Moreover, the major commercial banks were at that time controlled by the big business houses and financing the big industries of the owners of these banks. As bank-credit being the key source for financing the activities of business,the leadership of the country oriented towards the socialistic pattern of development, has to ensure the distribution of bank-credit for the national priorities. Hence, government nationalized 14 banks in July 1969 to make banks more involved in the funding the priority sectors, such as agriculture, exports, and small-scale industry. The nationalisation of commercial banks in July 1969 led to a substantial reorientation of bank credit distribution, particularly towards the priority sectors, which formerly had not received adequate attention from the organised commercial banking sector. This new orientation of bank credit distribution was desirable for the socio-economic needs of the country.It increased the involvement of banks in the socially desirable sectors. Although the guidelines were framed for financing the priority sector at a later stage butIndia's program of priority sector lending (PSL), has been in operation since 1969.PSL was a programme to ensure that assistance from the banking system flowed in an increasing size to the vital sectors of the economy and according to national priorities. Under the programme the credit facilities at reasonable rates of interest have been extended to a large number of borrowers of small means i.e. small-scale manufacturers, small farmers, road transport operators, retail traders, small businessmen, professionals and self-employed persons for promoting the growth of economy.The programmes of direct lending or priority sector lending have been criticized on the ground that it undermine banks' efficiency and profitability. These types of programmes remained in use in many developing and developed countries of the world in the past but majority of them(except India and Brazil) had discontinuedthese programmes on the ground that the benefit derived were less than the cost to the financial system. So the question re-emerge time and again, asking the justification of programme of priority sector lending in the competitive era where the financial institution (public sector bank, private bank and foreign origin bank) are competing each other for larger share and striving for the efficiency and profitability of their operation.

Guidelines for Priority Sector Lending in India:Priority sectors may be defined as the specific sectors of the economic system which are not able to obtain well-timed and good enough advances in the absence of this unique privilege. The programme stipulates that a specific portion of commercial banking lending goes to exact sectors which are priority sector for the lending purpose.The PSL norms stipulate a number of restrictions in terms of type of recipients, use of funds and sub-targets within each sector.According to the RBI circular dated July 7, 2016, there were eight broad categories of the PS Lending viz.Education, Housing, Agriculture, Social Infrastructure, Micro, Small & Medium Enterprises, Renewable Energy and Export Credit and weaker section. A target of 40 per cent of net bank credit has been stipulated for lending to the priority sector by domestic commercial banks. Within this, sub-targets of 18 per cent and 10 per cent of net bank credit respectively, have been stipulated for lending to agriculture and weaker sections. The domestic scheduled commercial banks, having shortfall in priority sector contribute to Rural Infrastructure Development Fund (RIDF) and in the event of failure to attain the stipulated targets and sub-targets, foreign banks are required to contribute to the Small Industries Development Bank of India (SIDBI).

2. Review of Literature

A rich literate is available on the priority sector lending in India. Different scholars studied the various dimensions of priority sector lending in India. The work of some researchers are hereby analysed for the direction of present study. Panda, Panda and Swain (2017) examined the performance of public sector banks using Econometric Analysis covering the period of 10 years from 2006-07 to 2015-16. Based on data collected for all the Public sector banks in India concluded that Deposits, CAR, C/D ratio positively affects PSL. But the result found to be insignificant. CAR positively affects PSL. But the results found to be insignificant. The GNPA shows a negative relationship with Priority sector lending but the results found to be insignificant. Kadiwala (2017) analysed the performance of public sector and private sector banks covering a period of five years from 2014-15 to 2018-19. The researcher found a significant different in priority sector lending between selected banks during the study period. Overall performance of BOB and BOI were better as compare to other banks. Total priority sector advance of these two banks were foundas comparison to other three banks.Solanki (2016) examined the priority sector lending by commercial bank in India. The study pertains to the past and present position of the priority sector lending. The study using Anovaconcluded that no significant difference was there in priority sector lending between selected banks.Dave (2016) studied the performance of public sector banks i.e. SBI, Canara Bank, PNB, BOI, and BOB covering a period of five yearsfrom 2011-12 to 2014-15. Study using one-way Anovaconcluded that selected bank were providing average advances 26% to 29% to priority sector during research period.Shajahan (2014)revealed a significant issue connected to priority sector lending, and there was a large credit gap concerning critical sectors of the economy. The share of credit channelled to key areas of the economy has decreased over time (had fallen from 40.9 percent in 1991 to 37.8 percent in 1996).Raman (2013)evaluated the data spanning a period of ten years, for commercial banks in terms of priority sector lending (2000-2001 to 2009-2010). Commercial bank performance was evaluated using percentage analysis, growth rate, and the average approach using secondary data. The NPA should be scheduled, according to this analysis, to improveefficiency and profitability.Sharma (2012)found that priority sector lending wasa common practice for both private and public sector banks, and it's been investigated by the researcher to understand which is more dedicated. The results showed that while the total lending amount by the two sectors differed, the proportion of the total amount was nearly the same.Ahmed (2010) examined a variety of characteristics that could influence bank financing proposals for priority sectors. Positive interest rates are shown under coefficient, while the bank's business volume is negative, although neither is statistically significant. According to the study, suitable loan recovery techniques should be employed, or banks may suffer the liquidity strain when recycling the funds. The most of studies on the priority sector lending either belongs to one category of banks or covers a limited arena of priority sector lending. The period covered in studies either small enough to observe a clear trend. The present study is a comprehensive one covering a period of 15 years out of which some period belongs to Pre-GFC and also the Post-GFC, so that the trends are clearly visible during the period of study.

3. Objectives of Study

1. To study the level of credit in priority sector lending of Public and Private Sector banks.
2. To compare the Advances and NPA in priority sector lending of Public and Private Sector banks.
3. To study the trends of advances and NPA of priority sectors lending of the Public and Private Sector banks

4. Research Methodology

Present study isdescriptive and analytical in nature and based on the secondary data of 15 years period from 2005-2006 to 2019-2020derived from RBI -Publication: Statistical Table Relating to Banks, Trend and Progress of Banking. Statistical techniques: Compound Annual Growth Rate (CAGR), percentage, average, bar and chart diagrams are applied for the analysis of data. For the study commercial banks have been divided intotwo groups: Public Sector Banks and Private Sector Banks.

5. Result and Discussion

A perusal view of Figure 5.1, showing the amount of priority sector advancesby the public sector and private sector banksfrom the year 2004-05 to 2019-20, hints that the credit for the priority sector has been increasing with the growth of advances of these banks in the economyin all the years from 2005-06 to 2019-20. Figure 5.2, showing PSL as percent of ANBC, indicates thatthe public falls short of the target of priority sector lending in the years 2006-07, 2011-12, 2012-13, 2013-14, 2014-15, 2015-16, 2016-17, and 2017-18, while the private sector banks fall short of the target inthe year 2011-12 and 2012-13. The private sector banks performed excellent in the year 2008-09, when these banks distributed credit of nearly 46.20% of ANBC for priority sector, while the public sector banksperformed well in the year 2007-08, when these banks distributed credit nearly 44.70% of ANBC for priority sector.An overview of Figure 5.3, indicates that the banks have increased their lending to priority sector as compared to the previous year and all banks have a positive growth rate which means that advances are increasing in all years during the study period. The public sector banks have a CAGR of 14.41%, while the private sector banks have a CAGR of 21.34% during the study period.

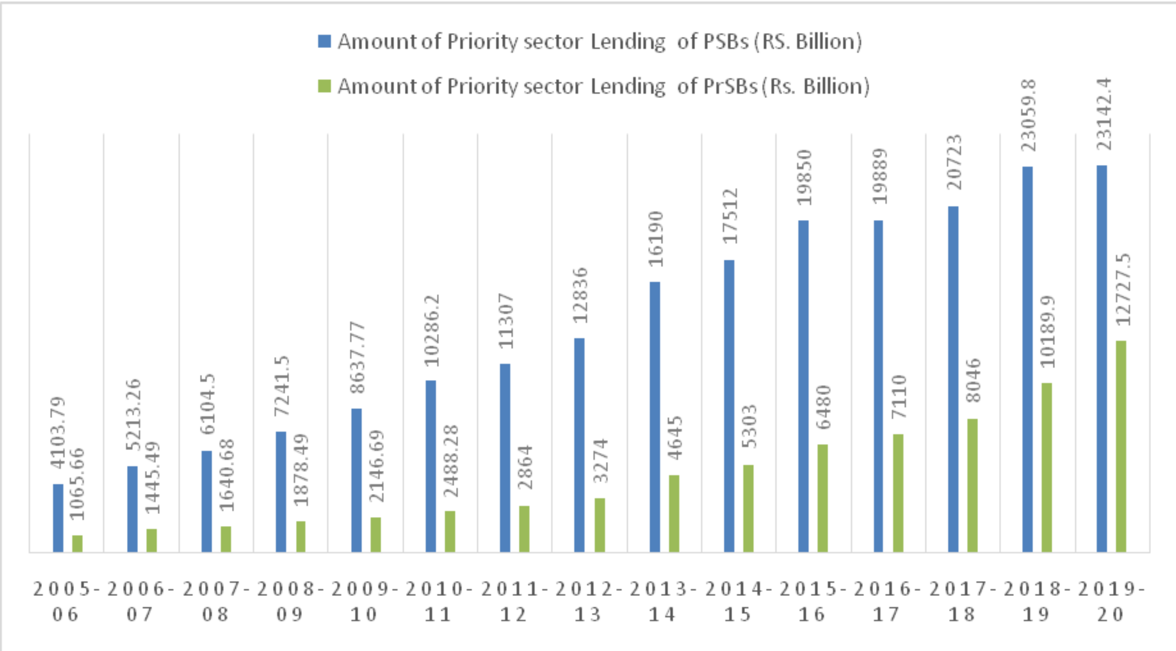

FIGURE 5. 1Priority Sector Lending by Public and Private Sector Banks from 2005-06 to2019-20 (Amount in Rs. Billion)

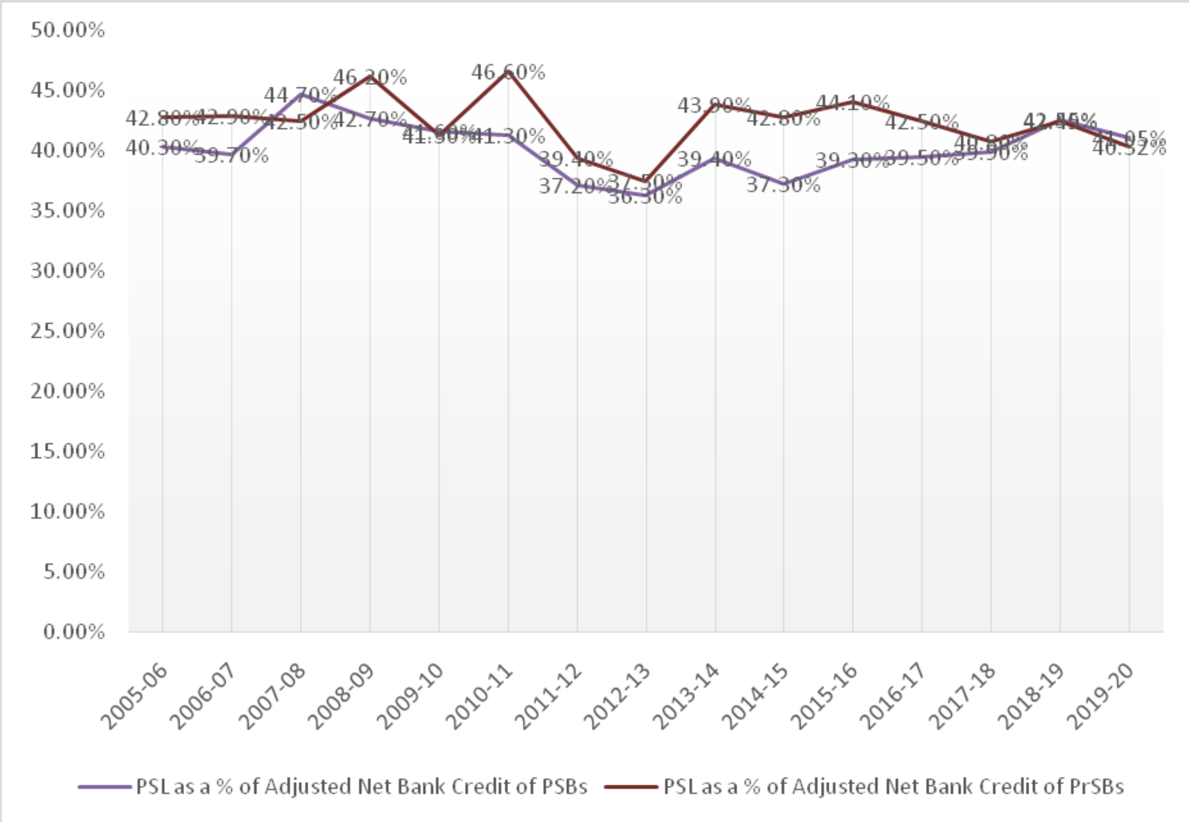

FIGURE 5. 2 Priority Sector Lending as percentage of ANBC of Public and Private Sector Banks from 2005-06 to 2019-20

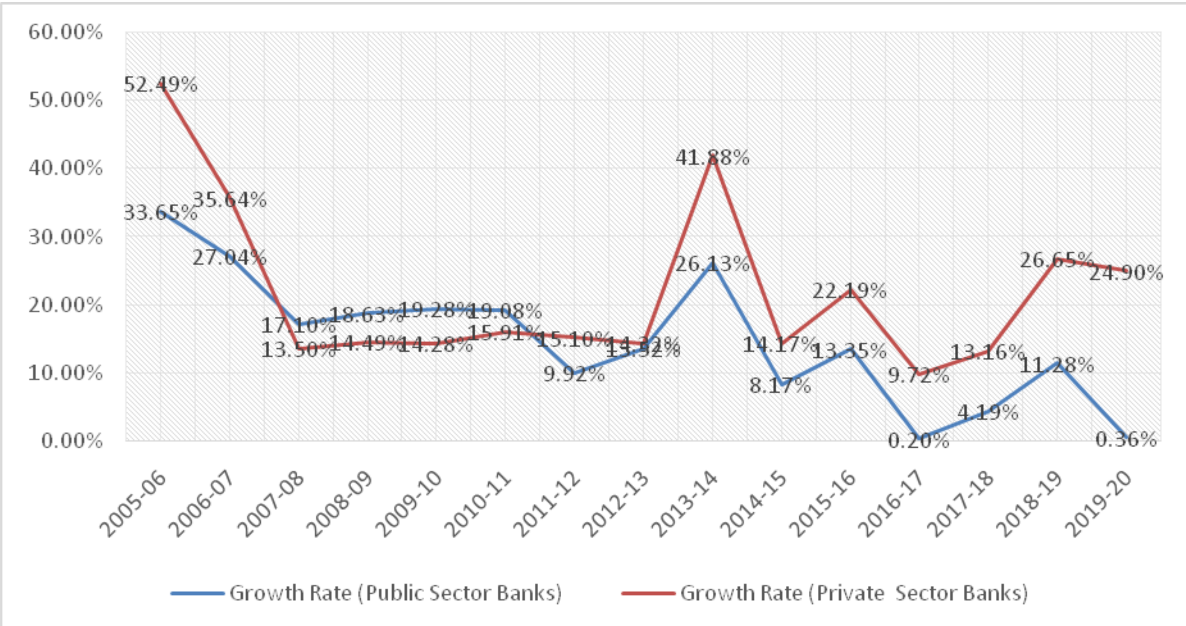

FIGURE 5. 3 Growth Rate of Priority Sector Lending of Public and Private Sector Banks from 2005-06 to 2019-20

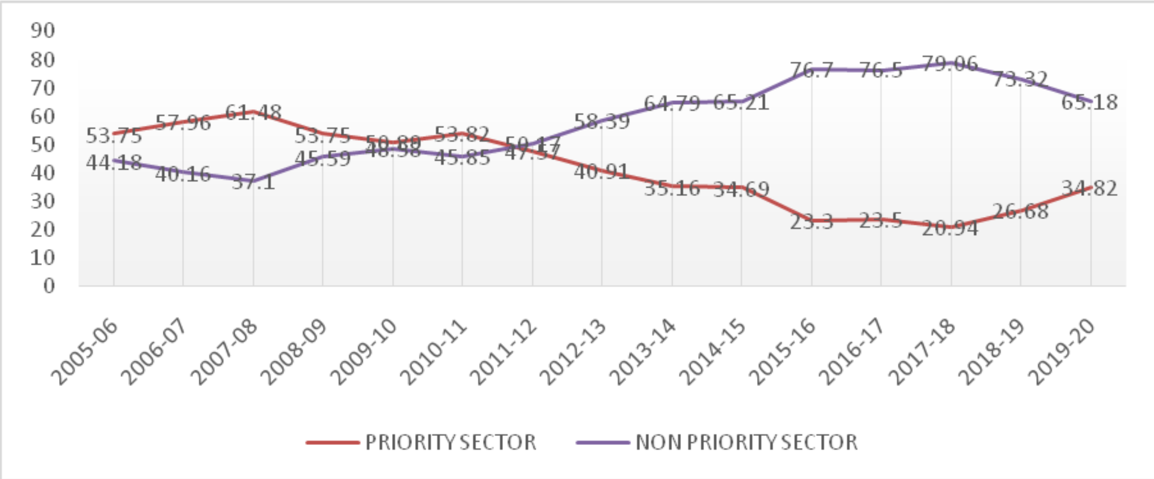

FIGURE 5. 4 Composition of NPAs of Public Sector Banks from 2005-06 to 2019-20

An overview of Figure 5.4, showing the priority sector and non-priority sector NPA as percentage of total NPAs of the public sector banks hints thatthe NPA of priority sector in thesebanks have been more as compared to NPA in non-priority sector from the year 2005-06 to 2011-12 . From the year 2007-08, the share of NPA of non-priority sector has beenshowing a rising trend till year 2019-20. The share of NPA of non-priority sector exceeds that of the PSL from year 2011-12 onwards.

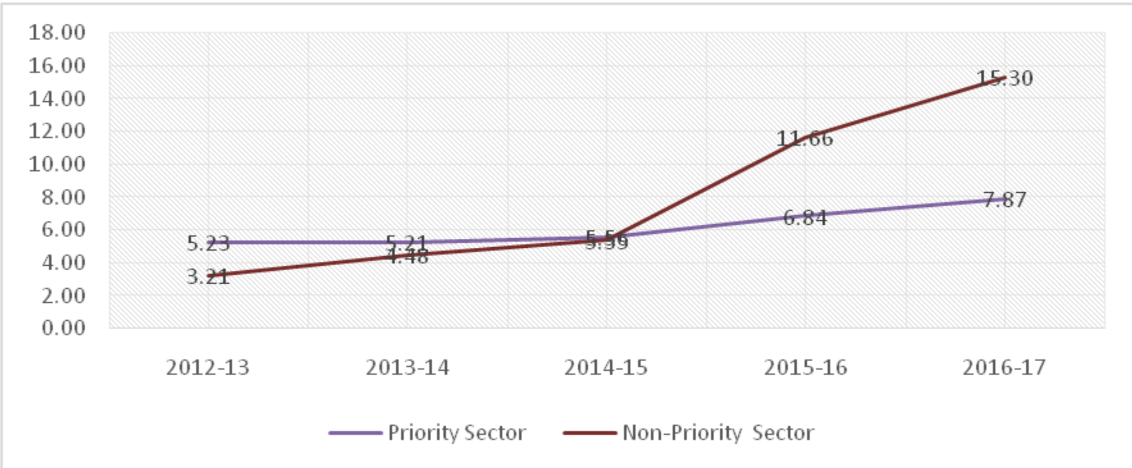

FIGURE 5. 5 Priority Sector and Non-priority Sector Gross NPA as percentage of Gross Advances of Public Sector Banks

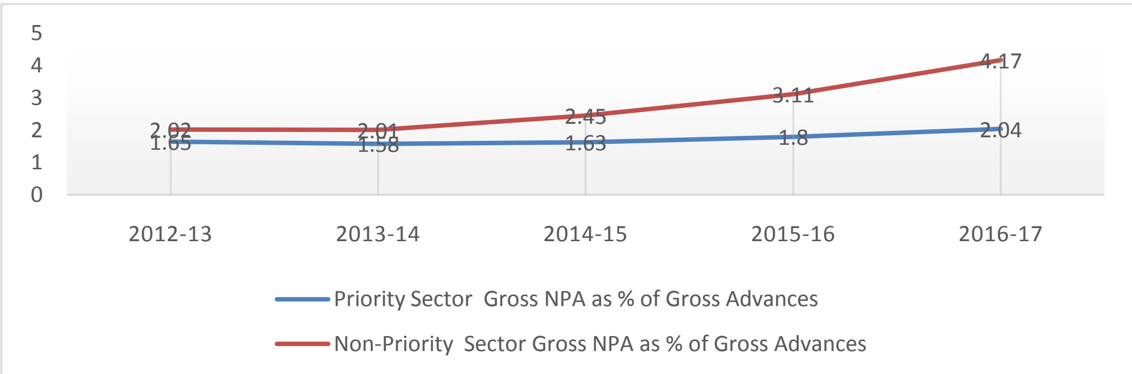

FIGURE 5. 6 priority sector and non-priority sector gross npa as percentage of gross advances of private sector banks

TABLE 5. 1 GNPA as percent of Gross Advances in Priority Sector and Non-priority Sector of Public Sector Banks

NPAs as percentage of Gross Advances of Public Sector Banks from 2012-13 to 2016-17						
Year	**Priority Sector**			**Non-Priority Sector**		
	Gross Advances	**Gross NPAs**	**Gross NPAs as % of Gross Advances**	**Gross Advances**	**Gross NPAs**	**Gross NPAs as % of Gross Advances**
2012-13	12,79,000.00	66,900.00	5.23	27,76,900.00	89,000.00	3.21
2013-14	15,19,297.93	79,192.41	5.21	30,71,160.45	1,37,546.78	4.48
2014-15	16,85,954.00	93,685.00	5.56	31,59,315.00	1,69,060.00	5.35
2015-16	18,73,748.00	1,28,116.00	6.84	32,08,408.00	3,73,952.00	11.66
2016-17	19,59,915.00	1,54,276.00	7.87	31,82,309.00	4,86,780.00	15.30
Source: Data derived from RBI Publication: Statistical Table Relating to Banks						

TABLE 5. 2 GNPA as percent of Gross Advances in Priority Sector and Non-priority Sector of Private Sector Banks

NPAs as percentage of Gross Advances ofPrivate Sector Banks from 2012-13 to 2016-17						
Year	**Priority Sector**			**Non-Priority Sector**		
	Gross Advances	**Gross NPAs**	**Gross NPAs as % of Gross Advances**	**Gross Advances**	**Gross NPAs**	**Gross NPAs as % of Gross Advances**
2012-13	3,15,700.00	5,200.00	1.65	7,30,900.00	14,800.00	2.02
2013-14	3,83,055.48	6,054.75	1.58	8,28,675.91	16,689.11	2.01
2014-15	4,42,762.00	7,211.00	1.63	9,94,577.00	24,365.00	2.45
2015-16	5,61,977.00	10,139.00	1.80	12,29,704.00	38,241.00	3.11
2016-17	6,52,004.00	13,293.00	2.04	14,52,876.00	60,549.00	4.17
Source: Data derived from RBI Publication: Statistical Table Relating to Banks						

An overview of Figure 5.5 indicating the NPA as a % of Gross Advances from 2012-13 to 2016-17for the priority sector and non-priority sector hints that the NPA of the priority sector as percent of Gross advances have been high up to the year 2014-15 and afterwards the NPA of non-priority sector have increased at an alarming rate and much high as compared to the priority sector.Figure 5.6 indicates that the NPA as a % of Gross Advances of private sector banks has been low in all the years from 2012-13 to 2016-17.Table 5.3 and 5.4, showing the NPA of priority sector and non-priority sector as % of Gross Advances from 2012-13 to 2016-17, indicates that the NPAs of public sector banks have been high as compared private sector banks for both the priority sector and non-priority sectorin all the years from 2012-13 to 2016.

6. Conclusion and Suggestions

The result of the study indicates that private sector banks have performed nowhere less than the public sector banks in assigning the necessary resources for the priority sector and even directed more percent of funds than the stipulated, for this strategic important sector of the economy. Even though in the earlier years, the NPAs of priority sector have been remained higher in the public sector banks but in the later years, the NPAs of non-priority sector have been substantial in these banks. It seems the problem with the policies and practice of lending i.e.project appraisal and non-follow up of credit distributed by these banks. Moreover, the NPAs in priority-sector lending of private sector banks suggests that the sector is more bankable as compared to non-priority sector, as the NPAs are found lower than the non-priority sector.

Priority sector lending has been an essential feature of India's credit policy and has to be there, as the programme ensures that the necessary bank-credit be allocated for strategically important small and marginal entities. The growth of prioritysector influences the sectoral growth as well provides social and economic justice. Even though the direct lending may have been discontinued in some developed and developing economies, thepriority sectorlending is still pertinent for economies like India, as benefitedstrategic sectorhave beenthe backbone of our economy affecting the large section of population of our country.

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