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Research Article

PRIORITY SECTOR LENDING IN INDIA- AN ANALYSIS

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ABSTRACT

Nationalization of commercial banks was done by passing the ordinance mainly for providing credit facilities, advancing loans and lending money to the priority sector which plays a major role in contributing to the country's gross development product. Nationalization generally means the central government's undertaking of the privately owned and controlled banks. In the year 1969 fourteen banks were nationalized in order to provide a helping hand to the priority sector and to also develop the rural areas as these banks which had the major power of money concentration in the economy were basically discouraging the priority sector by paving way for urbanization and industrialization. After nationalization these sectors were benefited by as years passed by the status of priority sectors has degraded and their contributions has declined to a greater extent. The researcher in this paper portrays the Historical background of priority sector lending, impact of nationalization of commercial banks on the priority sector lending then and now and the reasons for the reduction in the overall bank credit growth of the priority sector.

INTRODUCTION

Priority sectors lending emerged when private banks were undertaking by central government through Nationalization. The nationalization of the Reserve Bank of India was the first step towards nationalization of bank which took place in the year 1949.

Later during the Indira Gandhi's ministry commercial banks were nationalized through the ordinance passed in the year 1969 which was challenged by R.C. Cooper which is famously known as the Nationalization case. The Supreme Court held that the ordinance is against the constitutional provision and hence was struck down. In the following year by rectifying and resolving all the mischief and faults in the ordinance, legislation namely the Banking Companies (acquisition and transfer of undertaking) Act, 1970 was enacted with the help of the parliament nationalizing fourteen banks. One of the major reasons for nationalization of private commercial banks was to provide and promote credit facilities to priority sectors.

In olden times Agriculture played a crucial role in contributing a major share in the Gross development product and Indian economy was dependent on their growth for development of rural economy. Before nationalization these priority sectors were not provided with huge credit facilities as the commercial banks gave importance to urbanization and industrialization by providing credit by granting loans and advances to big businesses.

The term priority sector lending was first properly defined by the Dr. K.S. Krishnaswamy in the year 1972 when the National Credit Council (NCC) stressed on the commercial banks give importance to these priority sectors. Before nationalization of banks the NCC was established on February 1968 to monitor the priorities of bank's credits in various societies of the economy. The target for priority sector lending was laid down in the year 1974 as 33.33% of total credit of commercial banks. The reserve bank of India looks into operations of banks to provide loans to neglected and weaker sectors who cannot afford to pay higher rate of interest. These weaker sectors are known as priority sector and lending loans and advances to these sectors are called priority sector lending. The researchers in this paper has made an attempt to examine the Historical background of priority sector lending in India, the impact of nationalized banks and commercial banks in priority sector lending and the reasons for the decline in the target rate of priority sector lending recently and the contribution of priority sector towards the gross development product of India.

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OBJECTIVES

1. To examine the historical background of priority sector lending in India.
2. To analyse the impact of nationalized banks in priority sector lending then and now.
3. To examine the decline in the contribution of priority sector towards the gross development product of India.

Historical background of priority sector lending

The word priority sector was first used by Sri Moraji Desai, the Deputy Prime Minister and Minister of Finance made a statement in the Lok Sabha on December 14 in the year 1967 "that there had been continuous complaints that various priority sectors such as agriculture, small scale industries and exports have not been receiving their due share."[1] Thus, the concept of priority sector lending was instituted. The Reserve bank of India to provide incentives to banks for lending money to small borrowers under priority sector established the Credit Guarantee Corporation of India Limited in January 1971.

Later under the Banking Laws (Amendments) Bill 1967, which was introduced on December 23, 1967 in the Lok Sabha initiated the social control on banks. Even during the social control of banks the lending of loans and advances to the agriculture sector did not exceed two percent of the total credit. In the year 1968 National Credit Council was setup assigning it with the responsibility of estimating the demand for bank credit from various sectors of the economy.
Nationalization of banks was done to correct the scenario, where there was no improvement even after social control on banks. The then Prime Minister Indira Gandhi in her ministry nationalized fourteen banks in 1969 by passing an ordinance which was a major evolution in the banking history of India. The broad objectives of nationalization were:

a) To provide adequate and timely credit for agriculture, small scale industries and exports generally known as priority sector.
b) To give professional bent to bank management.
c) To encourage new class of entrepreneurs.[2]

The public sector banks granting loans and advances to priority sectors increased to 4791 crores covering 89.1 lakh accounts in the year December 1978 after nationalisation. In the pre-nationalisation period concentration of money in the society was restricted only to large businesses and industries as the top banks private banks lend money to them by seeing the credit worthiness of the borrowers. Only after nationalisation the priority sector lending increased drastically paving way for these sectors to grow and contribute towards the country's GDP.

Even after nationalisation of banks the components of priority sectors was not clear a statistical analysis by the informal study group relating to priority sectors constituted by RBI are[3]: (i) Agriculture - direct and indirect finance, (ii) Small scale industries, (iii) Industrial estates, (iv) Road and water transport operation, (v) Retail traders, (vi) Small business, (vii) Professionals and self-employed persons and (viii) Education. Presently the leading loans to road and water operations and industrial estate don't come under the purview of priority sector lending and treated as separate sectors.[4] Further in the year 1972 the differential rate of interest scheme was implemented for advancing loans with concessional interest under this scheme for promoting and developing the weaker sectors of the country.

The union Finance minister with chief executive officers at a meeting held on March 1980 revised the targets of priority sector lending to be increased to 40% by March 1985. The priority sector categories very revised by the working group headed by Shri.A.Ghosh in 1982 as: Agriculture - direct and indirect finance, (ii) Small scale industries, (iii) Industrial estates, (iv) Road and water transport operation, (v) Retail traders, (vi) Small business, (vii) Professionals and self-employed persons, (viii) State sponsored scheme for SC/ST Education and (ix) Housing and consumption loans.
The priority sector lending has undergone various changes from time to time according to the financial status and crisis to provide adequate and timely flow of credit to the weaker sectors of the society.

Impact of nationalisation in Priority Sector Lending

Table 1 Advances to Priority Sector of Scheduled Commercial banks in India
(Rs. billion)

Year	Priority Sector Advances	Trend %	Share of PSA in Total Advances (%)	Trend %
2000	1557.79	100	35.4	100
2001	1822.55	117	31.0	88
2002	2056.06	132	34.8	98
2003	2546.48	163	35.1	99
2004	2638.34	169	34.5	97
2005	3814.76	245	36.7	104
2006	5101.75	327	35.3	100
2007	6553.17	421	33.1	94
2008	7814.76	502	31.6	89
2009	9089.29	583	30.3	86
2010	10915.10	701	31.2	88
2011	13158.59	845	30.6	86
2012	14710.5	944	29.5	83
2013	16411.0	1053	28.8	81
Average	7013.58	450	32.71	92
r	0.97		-0.74	

Sources: compiled from trends and targets of Banking,various issues

The reserve bank of India in 2015 has revised the norms relating to the priority sector lending based on the recommendations given by the working group (2014). New segments of Priority sector lending were included: medium enterprises, social infrastructure and renewable energy. The small and marginal farmers and microenterprises and weaker sections were provided with separate target and food and agro processing units were included under the agriculture are. Moreover the non achievements in the priority sectors will be supervised on quarterly average basis at the end of the respective year 2016-17.

1 www.legalservicesindia.com/article/article/priority-sector-lending-in-india-2417-1-html
2 Shodhganga, "priority sector lending in India-a focus."
3 Shodhganga, "Progress of priority sector lending."
4 www.shodhganga.infibnet.ac.in

Reasons for the decline in the overall credit growth to priority sector

The priority sectors have been hit hard due to demonetization. The decline in the growth of loan was experienced by the banking sector. Loans to micro and small industries fell to 7.4%. Only the construction companies and home loans witnessed loan growth. The loans granted to the priority sector is to ensure that even the credit flow to these sectors of the society. The below table shows the loan growth these sectors have decreased.

The current priority sector targets are:

CATEGORIES	Domestic scheduled commercial banks and Foreign banks with 20 branches and above	Foreign banks with less than 20 branches
Total Priority Sector	40 percent of Adjusted Net Bank Credit ANBC	40 percent of Adjusted Net Bank Credit ANBC
Agriculture	18 percent of ANBC or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher.	Not applicable
Micro Enterprises	7.5 percent of ANBC or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher to be achieved in a phased manner	Not applicable
	10 percent of ANBC or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher.	Not applicable

Source: RBI Master circular-priority sector lending-targets and classification

The reason behind this is that the inflation rates have come, goods and service tax and demonetization of money has made it hard on the banks as well as these sectors. The loan growth to agriculture in June 2014 was 12% but in June 2017 it is only 5.8%.[5]

SCHEDULED COMMERCIAL BANKS CREDIT FOR PRIORITY SECTOR

Loan growth has slowed across sectors, including loans to weaker sectors.

Year-on-year change (in %)

	Total	Agriculture and allied activities	Micro and small enterprises		Housing	Micro-credit	Education loans	Weaker sections
			Manufacturing	Services				
Jun 2014	**16.72**	18.79	21.65	17.62	7.81	2.38	6.93	25.34
Sep	**15.81**	18.81	18.09	25.26	9.45	2.23	5.03	22.57
Dec	**12.56**	18.3	13.24	18.08	8.45	4.13	4.05	14.91
Mar 2015	**9.87**	15	9.14	16.88	6.75	2.91	2.22	4.89
Jun	**10.2**	11.14	5.98	16.21	4.23	2.49	2.84	13.29
Sep	**10.89**	12.83	5.12	15.29	4.7	10.78	3.41	16.98
Dec	**10.96**	12.72	2.5	15.17	6.27	6.41	2.97	16.47
Mar 2016	**10.72**	15.24	-2.25	13.28	6.17	6.47	1.61	17.91
Jun	**9.73**	13.69	-3.81	13.75	8.25	4.4	2.04	17.7
Sep	**11.42**	15.39	-4.55	14.95	8.08	-4.62	2.31	11.97
Dec	**4.08**	7.8	-8.16	4.77	5.54	-1.63	-0.04	11.16
Mar 2017	**9.42**	12.27	-0.47	11.79	7.62	0.25	0.5	16.07
Jun	**4**	7.35	0.5	4.49	2.81	-22.8	-2.92	6.71

CONCLUSION

Priority sector lending is a crucial and essential services of all the commercial banks to promote and develop the priority sectors who are basically the weaker sectors in the society due to lack of financial support and credit facilities. The nationalization of banks was a major and huge milestone in the banking history to provide a helping hand to these sectors. The Reserve bank of India being the apex bank analyses the norms framed related to the priority sectors periodically and by the recommendations of the working groups setup for the purpose to examine the negative and positive aspects of the norms and the problems, issues and challenges that sprout to reduce the target rates of these sectors, RBI revises the target and sub targets accordingly. Banking sector plays a major role towards the contribution in the country's gross development product. The banks when provide loans to these priority sectors eventually their contribution in the country's GDP increases. The priority sectors after the implementation these loans, credit facilities and schemes have been largely benefitted and have witnessed immense growth in their sectors but recently their contribution in the GDPs have declined and as well as the bank's credit growth on these sectors. Banking sector is just a small part in the priority sectors decreasing contribution in the country's GDPs there are various other reasons. The priority sectors scenario has become very pathetic as they have no proper supports form all aspects.

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5 www.livemint.com/Bank-credit-growth-to-priority-sector-slows-drastically.html