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PRIORITY SECTOR LENDING IN INDIA: THEORETICAL AND CONCEPTUAL LITERATURE REVIEW

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ABSTRACT

To ensure the accessibility of financial resources in India, the Government, through the Reserve Bank of India (RBI), mandates lending to sectors that may be neglected by banks and face challenges in accessing loans due to their weaker financial positions. This initiative traces back to 1967 when the then Deputy Prime Minister and Finance Minister, Morarji Desai, first proposed the idea of providing loans to priority sectors. At present, priority sectors encompass agriculture, MSMEs, export credit, education, housing, social infrastructure, renewable energy, professionals, self-employed individuals, and economically Weaker sections of society. To provide a conceptual and theoretical framework read through a large number of previously completed scholarly works that are available in various forms of publications and are closely connected with the present study. It provides insights into terminology, definitions, and methodologies, while also showcasing developed techniques and models. Therefore the researcher aims find the Theoretical and Conceptual Literature Review related to PSL in India. This study endeavors to uncover work and implications of commercial banks' engagement in priority sector lending, which has hitherto been underexplored.

KEYWORDS: *Priority Sector Lending (PSL), Literature Review: Theoretical and Conceptual, PSL Growth.*

1. INTRODUCTION

The foundation of the current Priority Sector Lending (PSL) framework traces back to 1967. On December 14, 1967, Morarji Desai, serving as the Deputy Prime Minister and Minister of Finance for the Government of India, addressed the Lok Sabha, highlighting concerns about the inadequate allocation of bank credit to key sectors like agriculture, small-scale industries, and exports. This marked the inaugural usage of the term "priority sector." Consequently, the concept of priority sector lending was introduced. In response to these concerns, the Banking Laws (Amendment) Bill 1967 was presented in the Lok Sabha on December 23, 1967. This measure sought to impose social control on banks, requiring them to match their actions with national interests. A watershed event occurred during a meeting of the National Credit Council (NCC) in July 1968, when the need for Indian commercial banks to increase their support for key sectors such as agriculture and small-scale enterprises was emphasised.

Table 1: Performance of Priority Sector Lending of Public Sector Banks (value in Rs. Cr.)

Year	Total PSL	% Growth Rate of TPSL	Year	Total PSL	% Growth Rate of TPSL
1969	441	0	2005	310729	27.11
1979	5211	1081.6	2006	409791	31.88
1989	34874	569.26	2007	521181	27.18
1990	39574	13.48	2008	608963	16.84
1991	42312	6.92	2009	719767	18.20
1992	44692	5.63	2010	864954	20.17
1993	48384	8.26	2011	1028616	18.92
1994	52945	9.43	2012	1130200	9.88
1995	60802	14.84	2013	1283680	13.58

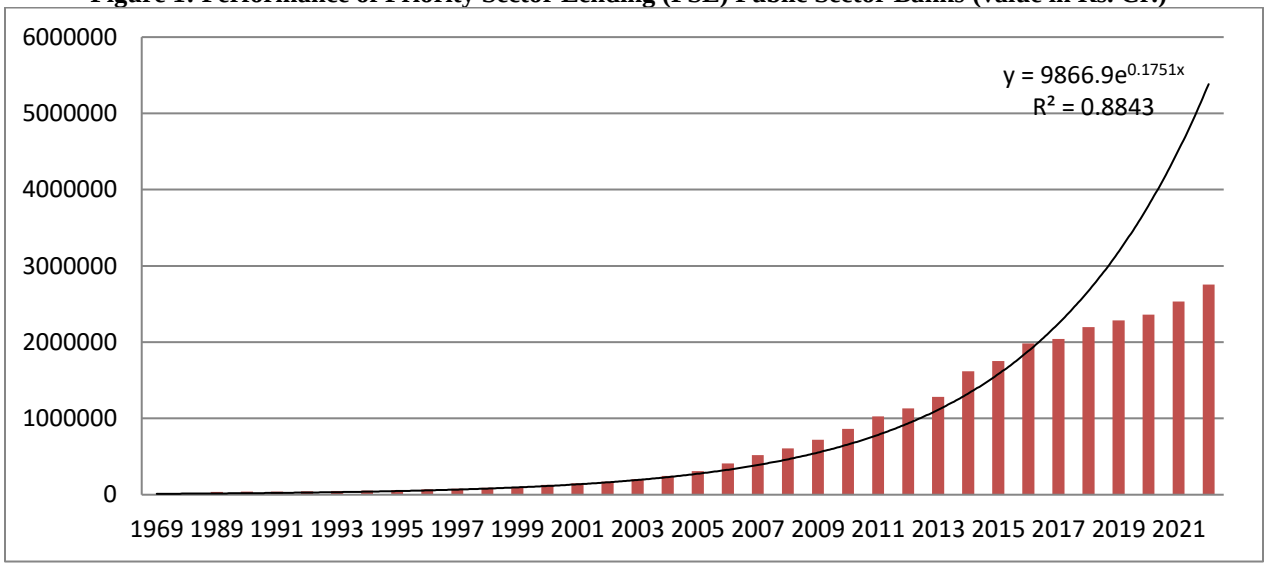
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1996	69606	14.48	2014	1618971	26.12
1997	78719	13.09	2015	1750893	8.15
1998	90738	15.27	2016	1985307	13.39
1999	98447	8.50	2017	2043474	2.93
2000	127478	29.49	2018	2199201	7.62
2001	149116	16.97	2019	2286394	3.96
2002	171483	15.00	2020	2360275	3.23
2003	203097	18.44	2021	2532708	7.31
2004	244454	20.36	2022	2755763	8.81

Source: Author's Compilation and Calculation from RBI

The Reserve Bank of India issues master circulars and guidelines to Indian commercial banks, requiring them to allocate a certain percentage of their total credit to these priority sectors, typically set at 40 percent. The present study based on theoretical aspect of PSL and covers the concept of priority sectors in India, including their brief historical background, the origins of the PSL and review of impotent literature work which has been done by various researchers in their studies. Therefore present work provides a comprehensive understanding, scope and relevance of the PSL in India with the help of existing research work done by researchers any in their various studies.

Figure 1: Performance of Priority Sector Lending (PSL) Public Sector Banks (value in Rs. Cr.)

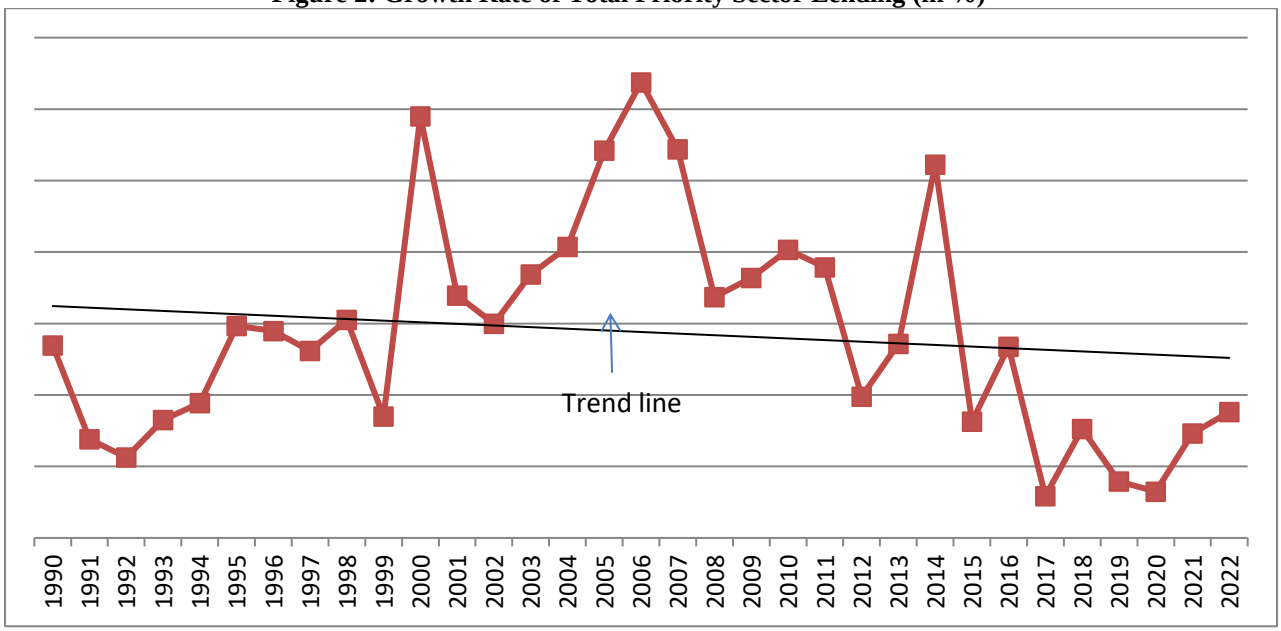


Source: Authors Construction and calculation based on the basis Table 1

Figure 1 shows the progress and performance of Priority Sector Lending (PSL) in India since 1969 to 2022. After 2001 exponential changes reflected in Priority Sector Lending. The table 1 shows the Total PSL (Public Sector Loans) over years from 1969 to 2022, starting at Rs. 441 crore in 1969 and growing to Rs. 2,755,763 crore by 2022. After 2001 exponential changes reflected in Priority Sector Lending. The Growth Rate of TPSL indicates the percentage increase in Total PSL compared to the previous year. The growth rates vary annually, reflecting fluctuations in public sector borrowing trends. Notable increases occurred in the early 2000s and around 2014, with growth rates peaking at 31.88 percent in 2006 and while the value of R^2 is 0.885 till 2022. Overall, the data highlights significant growth in public sector loans over the decades, influenced by economic conditions, policy changes, and fiscal decisions impacting borrowing and investment in various sectors.

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Figure 2: Growth Rate of Total Priority Sector Lending (in %)



Source: Authors Construction and calculation based on the basis Table 1

Figure 2 shows the annual growth rates (%) of Total Priority Sector Lending (TPSL) from 1990 to 2022. TPSL refers to the portion of bank lending targeted towards sectors deemed vital for socio-economic development, such as agriculture, small businesses, and education. The data shows fluctuating growth rates over the years, reflecting economic conditions, policy changes, and sectoral priorities. Years with higher growth rates, like 2006 and 2005, indicate periods of increased lending focus on priority sectors, possibly due to supportive policies or economic stimuli. Lower growth rates, such as in 2017, might result from economic slowdowns or shifts in lending priorities.

2. NEED OF THE STUDY

A literature review is a report on information found in the current literature about a specific area of study. To make available a conceptual and theoretical framework read through a large number of previously completed scholarly works that are available in various forms of publications and are closely related to the present study. It provides insights into terminology, definitions, and methodologies, while also showcasing developed techniques and models. Furthermore, it suggests potential research areas and allows researchers to build upon previous work, ensuring that proposed studies are original and contribute meaningfully to the field. Additionally, a literature review helps justify the chosen research topic, refine its focus, and demonstrate how it relates to existing scholarship, ultimately enhancing the understanding and integration of knowledge within the field

3. OBJECTIVE

The researcher aims find the Theoretical and Conceptual Literature Review related to PSL in India. This study endeavors to uncover work and implications of commercial banks' engagement in priority sector lending, which has hitherto been underexplored. Upon comprehensive examination, it becomes evident that there is a notable absence of research investigating the financial performance of public sector banks concerning their lending activities within the priority sector in India

4. EXPLANATION: REVIEW OF LITERATURE RELATED TO PSL

Due to systematic presentation and a many number of review works, which I found and reviewed, the entire literature work related to PSL has been categorized into the two important segments like first is related to theoretical and conceptual aspect of Priority Sector Lending and second is, other important work related to Priority Sector Lending in India.

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4.1 Related to Theoretical Aspect of Priority Sector Lending

Joshi (1972) requested the RBI to give clear descriptions of the components of the priority sector. The amount of loans for agriculture is a subject of uncertainty for certain bankers. They would be better able to channel farm finance if the RBI had clear rules. According to Nambiar (1977), commercial banks play more than only funding in important areas. Nambiar also emphasised the consequence of smooth collaboration between government agencies and banks. According to Angadi (1983), there are certain states where high-yield varieties, branch growth, deposit mobilisation, focused crop cultivation, and repayment discipline have an impact on priority sector lending, especially in the agricultural sector.

Patel (1984) asserts that banks increased their proportion of borrower accounts and outstanding balances with the growing demand for DRI loans from SC/ST borrowers. However, because of the scheme's limited funding, banks have difficulty providing for the demands of all eligible recipients. The RBI's developmental role in strengthening and extending the financial system was emphasised by Rangarajan (1988). He emphasised the need for special measures to guarantee sufficient credit flow to priority industries and those in need given market faults and rigidities. According to Rajasekhar & Vyasulu (1991), the 40% lending target to priority sectors is crucial. They contended that banks might improve credit quality and recoup at least 90% of their losses by using more professional banking procedures. Additionally, they proposed that a reduction in political meddling in bank operations could lead to a decline in the percentage of nonperforming assets.

Ghosh (1992) disagreed with the Committee on the Financial System's recommendation to lower the priority lending objective. He contended that if this was done, it would be seen as a move away from the core objectives of lending, which could deter lenders. Renaming the priority sector as microfinance and putting more emphasis on expanding the number of accounts than rigidly following to the existing 40% of outstanding credit requirement were the recommendations made by Kaladhar (1997). He maintained that commercial banks would be more inclined to actively participate in microfinance if they acknowledged the bankability of the poor and the financial benefits of doing business with them. Essentially, he recommended a tailored microfinance plan to take the place of the current priority sector approach, particularly in rural and semi-urban areas.

Mujumdar (1998) argued vehemently that public sector banks ought to lend to priority sectors irrespective of prescribed lending targets, stressing the importance of these sectors in attaining robust and continuous GDP growth. Although the sector's importance was recognised in the Ninth Plan, he recommended reorienting lending policy to overcome recent neglect.

Ganesan (1998) discovered that the marginalised groups within the scope of precedence sector advancements frequently did not benefit from them. The study stated that, avoid further setbacks in progress, the priority sector idea needed to be urgently redefined, emphasising the necessity of growth and development in these underserved industries.

The Department of Banking Supervision, RBI (1999) conducted a study on the impact of primary sector loans on non-performing assets and found that as on March 31, 1996, primary sector loans accounted for 48.27 percent of total NPAs. Although this share was lower than the share of undeclared notices in the non-primary sector, it shows that the prevalence of undeclared notices in the primary sector is significantly higher, although advances in the primary sector accounted for only 30-32 percent during the entire period of bank loans. However, the number of undeclared loans in non-prime sectors has gradually increased in recent years, especially in the accounts of industrial borrowers. In the piece "Priority Sector Challenges for Overseas Banks," Prasad (2014) noted that in 2012, the RBI required overseas banks operating with over 20 branches in the country to dedicate a minimum of 40 percent of their adjusted net bank credit to priority sectors, with 18 percent of this amount specifically earmarked for agriculture. Nonetheless, owing to their restricted presence in rural areas, the majority of overseas banks opted to adhere to the earlier standard of dedicating 32 per cent of their net bank credit to priority sectors.

4.2 Other Important Study Related to Priority Sector Lending

We have also examine and review few more literature related to PSL advances especially based on performance, progress, profitability and NPA of banks effected by Priority Sector Lending.

Shri C. S. Murthy, Chief General Manager-in-Charge, led the RBI Internal Working Group (2005), which was formed to evaluate India's Priority Advances. This report discussed the origins and development of India's Priority Sector, and

insights from global direct lending practices. It analyzed the loan allocation trends of scheduled commercial banks in India for sectors like agriculture, small-scale enterprises, industrial estates, and road and water transport operators. The study also presented a categorization framework for advancements in the priority sector. Ibrahim (2017) emphasized in her paper on "Priority Sector Lending in the Indian Banking Sector" that banking encompasses activities beyond just taking deposits. She specifically pointed out the collaboration between the Indian government and the RBI to tackle these issues through Priority Sector Lending (PSL) policies. In a study Shabbir (2013) conducted a comparative analysis covering the period from 1969 to 2011, examining the progress in agriculture and small-scale industries by both Scheduled Commercial Banks as a whole and Public Sector Banks in particular. Meanwhile, Najmi & Mujoo (2014) also examined the trends in priority sector lending and Non-Performing Assets (NPA) across private, public, and foreign banks.

Sarvesh and Kanaujiya (2023) undertook a research work where they examined how Priority Sector Lending (PSL) data impacted India's economic growth from 2012 to 2021 within public and private sector banks. They found that expenditures in the priority sector had a significant influence on GDP per capita, while inflation had a minimal impact. In another study conducted by Sarvesh and Kanaujiya (2024), they compared the performance of Priority Sector Lending (PSL) in public and private banks in India. The study indicated that public banks generally offered larger average loan amounts across various sectors, while private banks demonstrated higher growth rates, showcasing their dynamic response to evolving market demands. In a research paper, Pandya (2015) presented his findings on the impact of scheduled areas on scheduled commercial banks in India's development.

Ganesan's (2003) study pointed out an increase over time in interest rates, subsidies, and outstanding loans in priority sectors. After the financial sector reforms, banks began to lower their targets for priority sector lending, which led to lower income loss ratios and higher profitability ratios, signaling growth in the priority sector. However, the profitability of Indian public sector banks (PSBs) was reduced due to cross-subsidization of concessional loans and advances. In a study conducted by Goyal, Agrawal, and Aggarwal (2016), it was discovered that priority sector lending has a substantial impact on non-performing assets (NPAs) in public and private banks, with public banks being affected more significantly than private banks. Ahmed's (2010) research paper delved into the advancement and importance of Priority Sector Lending (PSL) in the Indian commercial banks, specifically analyzing the scenario in Barak Valley.

Desai (2021) explored the impact of priority advances on the profitability of banks in their paper. Priority lending targets economically disadvantaged segments of the economy. The study revealed that agricultural lending has a pessimistic outcome on bank profitability, whereas lending to the service sector contributes positively to financial performance. Industrial and personal credit lending were found to have insignificant effects on profitability. In a different study by Desai (2017) examined the relationship between loans to particular industries and Non-Performing Assets (NPAs) in priority industries. Therefore, lending to the agricultural, industrial, and personal sectors has a affirmative correlation with NPAs in the priority sector, while lending to the service sector has a negative correlation. Bag, Ray, and Roy (2022) investigated the connection between priority sector lending and public sector banks' profitability using secondary panel data. According to their findings, public banks are not considerably more profitable when it comes to the growth of loans to the priority advances.

5. CONCLUSION

As per the above review of literature we can say that, A comprehensive literature review will serves as the basic foundation for future research by incorporating existing knowledge and identifying relevant concepts and materials. Through this research, the future research will be play as a vital role of commercial banks in fostering socio-economic development through targeted lending initiatives, marking a significant step forward in understanding the dynamics of banking practices in making India in and also in the support of priority sectors.

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