

## Priority sector credit by commercial banks in India

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### Abstract

Priority sector includes those activities, which assumed national significance and were assigned priority for development. It primarily comprises all those sectors of the society which are crucial for the development of the nation but were hitherto neglected sectors by banking institutions. Priority sector is classified into three categories such as primary, secondary and tertiary. The former constitutes agriculture and allied activities e.g. dairy, poultry farming, goat rearing and pisciculture etc. and the middle one includes small scale, ancillary, cottage, tiny and small scale services and business enterprises. The latter covers small road and water transport operations, professionals and self-employed, retail trade, small business, education and women entrepreneur. The aspects covered in this study are Commercial banks' Advances to Priority Sector, bank category-wise Priority Sector Advances, Commercial banks Advances' to Differential rate of Interest Scheme, Weaker Section Advances, Advances to Small Scale Industries and Recovery Performance of Commercial banks.

**Keyword:** Priority, sector credit, commercial banks

### 1. Introduction

The priority sector lending is mainly intended to ensure that assistance from banks to those sectors which have not received adequate support. The attainment of socio economic priorities like growth of agriculture, promotion of small entrepreneurs, development of backward areas etc. is the major responsibility of government. Since 1970, Reserve Bank of India (RBI) and Government of India have stipulated guidelines for lending to priority sector lending by banks/ financial institutions. The same was revised during 2007 and overall priority sector lending target was fixed at 40 per cent for domestic banks and 32 per cent for foreign banks. The agricultural advances should be 18 per cent and weaker sections advances should be 10 per cent of total advances [1]. However, the banks are not able reach the prescribed target of lending to priority sector due to overdues mounting and non-performing assets (NPAs). Agricultural sector is the most important sector in India. The demand for agriculture arises due to increase in demand for agriculture produce, high yielding varieties, modernization, green revolution etc. Moreover the demand for and supply of credit varies from region to region due to irrigation, nature and fertility of land climate etc. With this back drop the present study is an attempt to present the various lacunae of priority sector lending faced by commercial banks.

### 2. Commercial banks Advances to Priority Sector including Agriculture

Agricultural advances by commercial banks are direct and indirect. Development envisages transformation traditional subsistence farming into modernized activity. In view of this, commercial banks progressively entered into financing agriculture directly, which can be considered as a novel feature. Commercial banks have provided direct finance to farmers in the form of short-term crop loans for agricultural production and medium and long-term loan for increasing productivity of the land. Short-term crop loans are usually given to farmers for periods ranging from six to twelve months and are mainly used for meeting seasonal requirements like seeds, manures, fertilizers and insecticides. Such advances are expected to be repaid at the time of the harvest.

The period of medium-term credit generally varies from one year to five years and is given for purposes such as purchase of tractors, power tillers, pump sets and bullocks. These loans are to be repaid by half-years or annual installment which usually coincides with the period of harvesting crop. Long-term credit is generally for periods larger than five years against mortgage of immovable property. Apart from supplying direct finance to farmers, commercial banks also provides finance to farmers indirectly through agencies and individuals, farmers' development agency. The commercial banks advances to agriculture (direct and indirect) and priority sector were shown in Table 1.

**Table 1:** Commercial Banks Advances to Priority Sector including Agriculture during 2004-13. (Rs. billion)

Year	Agricultural advances			Priority sector advances	Total advances
	Direct	Indirect	Total		
2004	5148.4 (10.6)	1901.7 (3.9)	7050.1 (14.5)	25098.9 (52)	8908.66 (100)
2005	6217.0 (7.2)	2226.5 (2.6)	8443.5 (9.8)	31133.6 (36)	11578.07 (100)
2006	8303.8 (7.4)	2687.9 (2.4)	10991.7 (9.8)	40077.5 (35.6)	15174.97 (100)
2007	11212.6 (7.4)	4309.3 (2.9)	15521.7 (10.3)	54677.3 (36.2)	19470.96 (100)
2008	14437.2 (7.5)	5824.2 (3.0)	20261.4 (10.5)	70375.6 (36.4)	24170.04 (100)
2009	17613.6 (7.5)	7326.1 (3.1)	24939.7 (10.5)	82477.2 (35)	28575.25 (100)

2010	21563.5 (7.8)	8378.0 (3.0)	29941.5 (10.8)	96574.3 (34.8)	33456.19 (100)
2011	26507.1 (8.2)	10565.9 (3.3)	37073 (11.5)	114040.6 (35.1)	40741.68 (100)
2012	36025.3 (9.1)	14692.3 (3.77)	50717.6 (12.87)	133886.0 (34)	47908.74 (100)
2013	44075.80 (9.6)	14258.53 (3.1)	58344.33 (12.65)	149697.1 (32.5)	55064.95 (100)
Mean	19110.4300	7217.0430	26328.4530	79803.810	28504.9010
CGR (%)	26.94	25.09	26.47	21.95	22.43
T- cal	4.6281*	4.8161*	4.6947*	5.8185*	5.7591**

**Source:** RBI, Relevant issues of Report on Trend Progress of Banking in India

**Note:** \*Significant at 1 level, figures in the parentheses are percentage to total.

Table 1 reveals the advances to agriculture and priority sector advances. It can be seen from the table that both the percentages of advances to agriculture and priority sectors are below prescribed norms due to inclusion of foreign banks. As segregations of advances bank-wise are not available only total

advances are considered. The annual compound growth rates are impressive and significant both at 1 and 5 per cent levels.

### 3. Bank category wise share of priority sector advances

To present a clear picture of priority sector advances bank wise share is presented in Table 2.

**Table 2:** Bank Category- wise Priority Sector Advances of Commercial Banks in India during 2004-13 (Rs.crores)

ending 31 <sup>st</sup> March	Priority sector advances of commercial Bank in India		
	Public sector Banks	Private sector Banks	Foreign Banks
2004	199786 (41.2)	36648 (44.1)	11835 (34.0)
2005	244456 (43.6)	48920 (47.3)	17960 (34.4)
2006	307046 (43.6)	69886 (43.6)	23843 (35.3)
2007	409748 (40.3)	106586 (42.8)	30439 (34.4)
2008	521376 (39.7)	144549 (47.8)	37831 (33.4)
2009	610450 (44.7)	164068 (46.8)	50254 (39.5)
2010	720083 (42.5)	190207 (46.8)	55453 (34.3)
2011	864564 (41.7)	215552 (46.0)	60290 (35.1)
2012	1022925 (41.0)	249139 (46.7)	66796 (39.1)
2013	1129993 (37.4)	280419 (39.4)	80559 (40.9)
Mean	603042.70 (41.57)	150597.40 (45.13)	43526 (36.04)
CGR(%)	21.23	25.37	23.75
T cal	4.8946*	5.6323*	6.0681*

**Sources:** 1. RBI, Relevant issues of Report on Trend and progress of banking in Indi

2. RBI, Relevant issues of Report on Currency and Finance

**Note:** \* Significant at 1 level, figures in brackets are percentage to Net Bank credit (NBC) up to 2007; there offer they are percentages to Adjusted Net Bank credit (NABC) or credit equivalent to off balance sheet exposure which is higher in the respective groups.

It is clear from table 2 that public sector banks in India achieved the prescribed norm (40 per cent) by RBI all the years except in 2008 and in 2013. The share of priority sector advances fell short of only 0.3 in 2008 and 2.6 per cent in 2013. Private sector banks also achieved the targets (40 per cent) of lending except in 2013, the share of priority sector advances fell short of only 0.6 percent. Foreign banks have exceeded their target of 32 per cent prescribed by RBI in all the years. The Compound annual growth rates are impressive and significant both at 1 and 5 per cent levels.

### 4. Differential Interest Rate Scheme (DRI)

This is one of the constituents of priority sector comes under tertiary sector.

The Differential Rate of Interest Scheme (DRI Scheme) was introduced during 1972, following the recommendations of the committee under the Chairman of DR.R.K. Hazari<sup>2</sup>. The scheme was meant to ensure and provide access to institutional credit for certain sections of the poor. The eligible persons obtain loans at a uniform concessional interest rate of 4 per cent. At present 1 per cent of the total advances of commercial banks should earmark under DRI scheme. A Formal obligation was also laid on the private sector banks in December, 1978 to implement the scheme and to achieve the target of lending at least one per cent of their aggregate advances outstanding at the end. The progress achieved under DRI scheme is presented in Table 3

**Table 3:** Commercial Banks' Lending under DRI scheme during 2004-13 (Number of accounts in million and amount in billion)

Year	Number of accounts	Amount outstanding for DRI	Advances	DRI percentage to total advances
2004	0.37	3.85	8908.66	0.04
2005	0.33	3.37	11578.07	0.03
2006	0.39	4.90	15174.97	0.03
2007	0.26	6.34	19470.99	0.03
2008	0.26	6.69	24170.04	0.03
2009	0.31	7.53	28575.25	0.03
2010	0.37	7.52	33456.19	0.02
2011	0.42	7.15	40741.68	0.02

2012	0.43	8.02	47908.74	0.02
2013	NA	NA	55064.95	-
Mean	0.3489	6.1522	28504.9540	0.02
CGR(%)	1.90	9.61	22.43	-
T-cal	16.5781*	10.8412*	5.7591	

**Source: RBI:** Relevant issues of Statistical Tables relating to Banking

**Note:** \*Significant at 1 level, NA= Not available

It is evident from Table 3, the number of borrowed accounts under DRI scheme increased from 0.37 million in 2004 to 0.43 million in 2012. The amount outstanding against these accounts also increased from Rs.3.85 billion in 2004 to Rs.8.02 billion in 2012 though there is a setback in the amount outstanding. Despite this increase, however, the share of the DRI advances to total advances was below stipulated norm (1 per cent) by RBI for the study years. The compound annual growth rates are significant at both 1 and 5 per cent levels. This is quite

understandable that there is no obligation for foreign exchange banks and the other reason is the mounting overdues.

### 5. Advances to weaker sections

This is also one of the constituents of priority sector comes under tertiary sector.

As per the RBI norm, commercial banks advances to weaker sections should be 10 per cent of total advances<sup>[3]</sup>. Commercial banks advances to weaker section was presented in Table 4 (Number of accounts in million and amount in billion)

**Table 4:** Commercial Banks' Advances to Weaker Sections during 2004-13

Year	Number of accounts	Amount outstanding for weaker sections	Total advances	Percentage of weaker sections advances to total
2004	29.20	271.9	8908.66	3.05
2005	38.34	291.8	11578.07	2.52
2006	21.19	398.2	15174.97	2.62
2007	39.67	129.9	19470.99	2.62
2008	22.33	1269.35	24170.04	5.25
2009	24.10	1670.41	28575.25	5.85
2010	26.13	2095.62	33456.19	6.26
2011	28.79	2463.15	40741.68	6.05
2012	32.97	2939.60	47908.74	6.13
2013	NA	NA	55064.95	NA
Mean	29.1911	1281.1033	28504.9540	5.01
CGR(%)	1.53	34.66	22.43	-
T-cal	13.1586*	3.6105*	5.7591*	

**Source: RBI:** Relevant issues of Statistical Tables relating to Banking

**Note:** \* Significant at 1 level, NA= not available

It is evident from table 4 that the number of borrowed accounts under weaker section advances increased from 29.20 million in 2004 to 32.97 million in 2012. The amount outstanding against these accounts also increased from Rs.271.9 billion in 2004 to Rs.2939.60 billion in 2011. Although both number of accounts and amount outstanding on them increased, the commercial banks failed to meet the norm (10 per cent of total advances) set up by RBI. This is due several reasons like i) mounting of overdues and non-performing assets (NPA) ii) foreign banks has no obligation iii) weaker section finance is not profitable avenue for commercial banks. The compound annual growth rate are significant at 1 per cent level.

### 6. Commercial banks credit to small scale industries

Small scale industries constitute secondary sector of priority sector. These units satisfy the criteria for investment in plant and machinery and equipment as per Micro Small and Medium Enterprises development act 2006(MSMED ).Investment in plant and machinery should not exceed twenty five lakhs rupees for Micro enterprises for Small enterprises it should be more than twenty five lakhs rupees but should not exceed five crore rupees. For the investment the criteria is; it should not exceed ten lakh rupees for Micro enterprises for Small enterprises more than ten lakh rupees but should not exceed two crore rupees<sup>4</sup>.

Commercial banks advances to Small scale industries were shown in Table 5.

**Table 5:** Commercial Banks' Advances to Small Scale Industries during 2004-13 (Rs. billion)

Year	Amount outstanding for Small scale industries	Total advances	Percentage of small scale industries advances to total advances
2004	712.09	8908.66	8.0
2005	834.99	11578.07	7.2
2006	1012.85	15174.97	6.68
2007	1273.22	19470.99	6.53
2008	2643.2	24170.04	10.93
2009	NA	28575.25	-
2010	3622.91	33456.19	10.83
2011	4785.27	40741.68	11.75
2012	5275.85	47908.74	11.01
2013	7297.00	55064.95	13.25
Mean	3050.8200	28504.9540	10.70
CGR(%)	33.76	22.43	
T-cal	3.8949*	5.7591*	

**Sources:** 1. RBI, Relevant issues of Statistical Tables relating to Banking

2. RBI, Relevant issues of Report Trend and Progress of Banking in India

**Note:** \*Significant at 1 level, NA= not available

Table 5 reveals that the amount outstanding of small scale industries advances increased from Rs.712.09 billion in 2004 to Rs.7297. billion in 2013. The increase rate is 10.24 times. The percentage of outstanding advances for small enterprises was increased from 8 per cent in 2004 to 13.25 per cent in 2013. The compound annual growth rates are impressive and significant at both 1 and 5 per cent levels.

### 7. Recovery performance of commercial banks

The problem of overdues has been quite challenging task to credit institutions in the country. Poor recovery of overdues cripples the capacity of credit institutions to draw refinance from NABARD. Recycling of funds becomes an impossible task, when the overdues reach the danger level. The banking sector is expected to achieve some of the socio-economic objectives of planned development. However they perform the role when banks are financially sound. Because of the phenomenon of mounting overdues, banks are very much affected. There will be always some bad and doubtful debts. But with greater attention to priority sector the problem of overdues has assumed greater proportions statedn <sup>[5]</sup>. the recovery performance of commercial banks was shown in Table 6

**Table 6:** Recovery Position of Commercial Banks during 2004-12 (Rs. Crores)

Year	Demand	Recovery	Percentage of Recovery to Demand
2004	33544	25002	74.5
2005	45454	45733	84
2006	46567	37298	80
2007	73802	58840	79.7
2008	95100	71739	75.4
2009	119084	90660	76.1
2010	124400	92000	74.09
2011	182200	138300	75.9
2012	191800	142900	74.51
Mean	101327.89	78052.44	77.03

#### Sources:

1. RBI, Relevant issues of Report on Currency and Finance
2. RBI, Relevant issues of Report Trend and Progress of Banking in India

Table 1.14 reveals the recovery position of commercial banks. The recovery rate is 74.5 per cent in 2004. It is 84 per cent in 2005 which best performance in terms of recovery when compared with that of other years. But in 2006 the recovery rate decrease to 80.1 per cent. In 2007it is 79.7 per cent again it is decreased to 75.4 per cent in 2008. There is minor improvement of recovery in 2009 with the per cent of 76.1 where as it is decreased to 74.09 per cent in 2010. It is slightly improved in 2011 with the percentage of 75.9 percent and it is decreased to 74.51 per cent in 2012.

### 8. Conclusion

The percentage of agricultural advances by commercial banks below stipulated norm due to inclusion of foreign banks. Public sector banks failed to achieve the norm during 2008 and 2013 but for the rest years their achievement is good while private sector banks achieved the target except in 2013 whereas foreign banks reached the norm for all the years. The percentage of Commercial banks' lending under DRI scheme is below the stipulated norm for all the years. The share of weaker section advances by commercial banks is also below the norm. It is due

to mounting of overdues and Non-Performing Assets (NPAs). Commercial banks' advances to small scale industries are satisfactory. The overall average recovery rate of commercial banks is 77.03 per cent.

### 9. References

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