Quest Journals
Journal of Research in Business and Management
Volume 13 ~ Issue 6 (June 2025) pp: 149-154
ISSN(Online):2347-3002
www.questjournals.org

Research Paper

Priority Sector Lending in India: An Analysis

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ABSTRACT
The nationalization of commercial banks in 1969 involved taking over 14 privately-owned banks, mainly to provide credit facilities to the priority sector and boost rural development. Nationalisation of Banks means transferring control and ownership of private banks into the hands of the government. This means the government becomes the majority shareholder in an erstwhile private bank, and the bank operates as a public sector entity. This measure was intended to counteract the influence of the urban economy and promote the growth of the rural sector. Initially, nationalization led to significant benefits for priority sectors. However, over time their status has deteriorated and their contribution has decreased substantially. The main objective of the study is to examine the performance of the priority sector lending of the banks.

***R**eceived 15 June., 2025; **R**evised 27 June., 2025; **A**ccepted 29 June., 2025 © The author(s) 2025.*
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I. INTRODUCTION

The banking sector plays a crucial role in the development of a nation's economy. "The key players in the development of the economy are commercial banks in general and public sector banks in particular." (Mahesha NM, 2018) Bank credit has an enormous role in the development of the economy. Besides economic growth, it should also lead to the removal of poverty and equitable distribution of income for which several committees have looked into the aspect of rural credit and priority sector credit in India. (K. C. Chakrabarty, 2012). Priority Sector means those sectors which the Government and RBI consider important for the country's development and are to be given priority over other sectors. The primary goal of Priority Sector Lending (PSL) is to ensure that banking assistance flows increasingly to the sectors of the economy that contribute to the national product development but have not received sufficient institutional finance support. The government has designated the priority sectors which are granted precedence in credit disbursement. This prioritization supports national development and the achievement of national goals by providing loans to the various sectors at concessional rates, promptly

Historical Background:

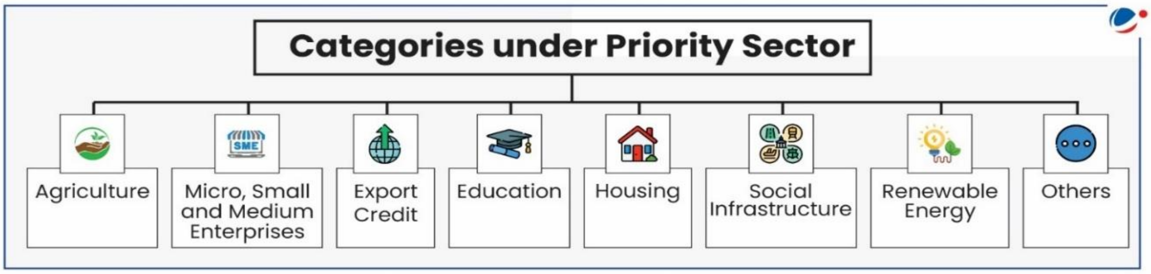
1969 – Gadgil Committee: Recommended the *Area Approach*, leading to the adoption of the *Lead Bank Scheme.*

1972 – Formalization of PSL: Aimed to ensure credit flow to sectors that were creditworthy but lacked access to institutional finance and later in 1982 Ghosh Committee: Recommended revision Targets/Sub-targets for Priority sector and reclassification of priority sector categories.

Categories	Targets/ Sub-targets			
	Domestic Commercial Banks & Foreign Banks with 20 branches and above	Foreign Banks with Less than 20 branches	Regional Rural Banks	Small Finance Banks
Total Priority Sector	40%	40% (upto 32% in form of Export Credit and not less than 8% can be to any other priority sector.)	75%	75%

Agriculture	18%	NA	18%	18%
Micro Enterprises	7.5%	NA	7.5%	7.5%
Weaker Sections	12%	NA	15%	12%
Note: Percentages mentioned above are as a percentage of Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-Balance Sheet Exposures (CEOBSE), whichever is higher.				

Categories that fall under Priority Sector Lending norms:



II. Literature Review:

Several pertinent studies have been scrutinized in an endeavour to comprehend the nuances of priority sector lending in diverse contexts.

A study by Bano and Sharma (2020) examined the paradigmatic shift in priority sector lending guidelines, observing that nascent non-performing assets (NPAs) and burgeoning transaction costs deter banks from lending to priority sectors, consequently thwarting their ability to achieve set targets. Damodaran et al. (2014) analysed the lending efficiency of Indian commercial banks, employing regression models to decipher the impact of NPAs on bank asset bases, noting that Other Private Sector Banks exhibit higher growth rates compared to Public Sector Banks. Conversely, Public Sector Banks demonstrate more pronounced growth. Dankwa and Badu (2013) investigated lending principles and practices in Ghana's banking sector, finding that respondents overwhelmingly benefit from lending models, albeit a minority indicated otherwise. Dave (2016) delved into priority sector lending patterns among selected Indian Public Sector banks, with ANOVA analysis confirming equal norms with respect to priority sector advances relative to total advances. Subsequent research by Goyal (2015) revealed significant positive correlations between Non-Performing Assets (NPAs) and priority sector lending for public and private sector banks. In a related study, Goyal (2016) utilised panel regression modelling to demonstrate a statistically significant effect of priority sector lending on NPA generation for agricultural, Small Scale Industries and other sectors. Goyal et al. (2015) conducted an in-depth analysis of trends and practices in priority sector lending from 2000 onwards, noting that several prominent banks fail to meet targets, including Jammu and Kashmir Bank, Yes Bank and SBI. Ibrahim (2017) elucidated the concept, targets, and classification of priority sector lending in India, also highlighting the primary focus of private sector banks on Micro, Small, and Medium Enterprises (MSMEs) and the declining performance of foreign banks.Jaiswal and Bhasin (2015) examined the performance of regional rural banks in priority sector lending, recommending that governments establish additional branches in underdeveloped areas to improve access to credit for small borrowers. Jethwani and Ramchandani (2017) explored the impact of priority sector advances on commercial bank profitability, demonstrating statistically significant relationships between various ratios and priority sector advances relative to total advances. Kumar and Gambhir (2012), as well as Manjushree and Giridhar (2019), critically examined the policy framework of priority sector lending, focusing on the efficacy and problematic issues associated with this lending approach. Conversely, Naruka and Yadav (2017) conducted a comparative analysis of various lending institutions' performance regarding priority sector lending, revealing significant differences in the execution of financing programs, particularly in agricultural, MSME, and total priority sectors. Moreover, the impact of priority sector lending on rural banks was investigated in a study by Ota and Sarkar (2016), highlighting a disparity between the cost of lending and returns on investment. In a comprehensive evaluation, Panda (2017) examined the influence of multiple determinants on priority sector lending by Indian public sector banks, yielding insights into the positive association between bank size, performance, and priority sector lending, as well as a negative correlation between lending efficiency and priority sector lending. Furthermore, Kanyan and Singh (2024) assessed the contributions of priority and non-priority sectors to gross non-performing assets across public, private, and foreign sector banks, revealing that non-priority segments predominate in the accumulation of net non-performing resources.

Overall, the literature underscores complex challenges inherent in the operationalization of priority sector lending, including unduly expansive definitions, concerns about project viability, the prevalence of bad debts, and the need for a balanced approach to lending across sectors. This examination synthesises existing research concerning the efficacy of priority sector lending in fostering the profitability of scheduled commercial banks. A longitudinal analysis spanning 2005 to 2014 is conducted by one academic (Pandya) to establish a causal relationship between priority sector advances and various metrics of bank profitability. Conversely, another researcher (Patel) investigates the role of commercial banks in Gujarat in prioritizing lending to vulnerable economic sectors. Subsequent studies (Raj and Stephen, Rajamohan and Durairaj) explore customer perceptions of banking services in priority sector lending, while also identifying obstacles and inefficiencies faced by customers. Furthermore, an evaluation by Raman of commercial banks operating in Tamil Nadu from 2001 to 2012 posits that the nationalisation of banks and introduction of priority sector lending led to the adoption of a social banking model and increased focus on rural communities.

Objectives:
The main objective of the study is to examine the performance of the priority sector lending of the banks areas follows:
i) To examine the lending pattern of the public, private and foreign sector banks in India.
ii) To examine the growth rate of priority sector lending of public, private and foreign sector banks in India.
iii) To find out the difference of the performance of priority sector lending in public and private sector banks in India.
4) To find the revised priority sector guidelines issued by RBI.

III. Research design

Research design means a way to systematically solve the research problem. It comprises a series of steps that are taken together to provide a roadmap for carrying out a research project.
Sample size and selection: The empirical work is based on a study of performance of priority sector lending in India. For the purpose of analyzing the contribution of the selected category of banks, the study has been made on those sectors for which data for all years is available for the period 2013 to 2022.
Data Type: The entire study is based on the secondary/quantitative data collected from the annual reports of RBI.
Research methods applied: Based on the objectives of the study, the researchers applied the Growth Rate (CAGR) during the period and Kruskal Wallis test for comparing the performance of public and private sector banks.

IV. Analysis and Findings

The findings of the study are presented below.

Table – 1: National Scenario of Priority Sector Advances Year-Wise of Public Sector Banks in India
(Amount in Rupee Billion)

Yea r	Tot al Priority Sector	% of A N B C	Agric ulture	% of A N B C	MSM E	% Of A N B C	Educatio n	% of A N B C	Hou sing	% o f A N B C	Gro wth Per cent in PSL
2014	8859	35.66	3578	14.40	3675	14.79	335	1.35	1271	5.12	
2015	9985	35.69	3543	12.66	4647	16.61	367	1.31	1427	5.10	12.71
2016	12454	39.04	5312	16.65	5231	16.40	390	1.22	1521	4.77	27.86
2017	14318	41.89	6244	18.27	5922	17.33	407	1.19	1745	5.11	21.05
2018	14900	41.06	6571	18.11	6037	16.64	425	1.17	1868	5.15	6.57
2019	21728	40.61	9611	17.96	8633	16.14	586	1.10	2898	5.42	77.07
2020	22775	41.73	9754	17.87	9057	16.59	581	1.07	3384	6.20	11.82
2021	23335	40.27	9758	16.84	9281	16.02	575	0.99	3720	6.42	6.31
2022	25664	41.91	11256	18.38	9917	16.19	566	0.92	3926	6.41	26.30
2023	27224	42.74	12098	18.99	10440	16.39	559	0.88	4127	6.48	17.61
CAGR	13.29%		14.49%		12.30%		5.87%		13.98%		

Source: Computed by the Authors

In the above table no – 1, showing the advances given by the public sector banks in respect of priority sector from 2014 to 2023. It also reveals that all the sector i.e., Agriculture, MSME, Education, Housing and the total of these four sector advances as well as % of ANBC (Adjusted Net Bank Credit) of all the group were also computed. From the growth percent in PSL shows significant fluctuations that means minimum growth rate (6.31%) in the year 2020 and maximum growth rate (77.07%) in the year 2018 out of ten years i.e., from the year 2014 to 2023. Another calculation (CAGR) is made on these five sector from the period 2014 to 2023. From the above table it is shown that CAGR is 13.29% for PSL, 14.49% for Agriculture sector, 12.30% for MSME sector, 5.87% for Education sector and 13.98% for Housing sector which clearly depicted that RBI has constant effort towards priority sector advances of the economy.

Table – 2: National Scenario of Priority Sector Advances Year-Wise of Private Sector Banks in India (Amount in Rupee Billion)

Yea r	Total Priorit y Sec tor	% of AN BC	Agric ulture	% of AN BC	MSM E	% of AN BC	Educatio n	% of A N B C	Hou sing	% of A N B C	Gro wth Perc ent in PSL
2014	3208	36.76	1120	12.83	1417	16.24	18	0.21	653	7.48	
2015	4131	38.88	1478	13.91	1868	17.58	21	0.20	765	7.20	28.76
2016	4801	39.09	1818	14.80	2166	17.63	23	0.19	794	6.47	16.22
2017	6538	43.72	2669	17.85	2923	19.55	25	0.17	921	6.16	36.17
2018	7531	41.62	2972	16.43	3557	19.66	28	0.16	973	5.38	15.19
2019	8586	40.03	3690	17.20	3924	18.30	31	0.15	940	4.38	14.01
2020	12428	43.88	4919	17.37	5944	20.99	43	0.15	1522	5.37	44.75
2021	14232	43.72	5746	17.65	6692	20.56	41	0.13	1753	5.39	14.52
2022	16367	44.37	6126	16.61	8343	22.62	46	0.13	1852	5.02	15.00
2023	18895	46.49	6866	16.89	10077	24.79	46	0.11	1906	4.69	15.45
CAGR	21.78%		22.32%		24.35%		10.84%		12.64%		

Source: Computed by the Authors

In the above table no – 2, showing the advances given by the private sector banks in respect of priority sector from 2014 to 2023. It also reveals that all the sector i.e., Agriculture, MSME, Education, Housing and the total of these four sector advances as well as % of ANBC (Adjusted Net Bank Credit) of all the group were also computed. From the growth percent in PSL shows no significant fluctuations in the growth rate i.e., minimum growth rate (14.01%) in the year 2018 and maximum growth rate (44.75%) in the year 2019. Another calculation (CAGR) is made on these five sector from the period 2014 to 2023. From the above table it is shown that CAGR is 21.78% for PSL, 22.32% for Agriculture sector, 24.35% for MSME sector, 10.84% for Education sector and 12.64% for Housing sector which clearly depicted that private sector banks has pivotal role playing towards priority sector advances of the economy.

Table – 3: Results of Kruskal Wallis Test

Variable	Mean	S.D	Chi-Square	Sig. (p)	Decision
Agriculture	5756.45	3300.66	7.000	0.008	Reject
MSME	5987.55	2947.32	3.863	0.049	Reject
Education	255.65	239.96	14.296	0.000	Reject
Housing	1898.30	1108.24	6.606	0.010	Reject
Total	13897.95	7390.77	7.000	0.008	Reject

Source: Computed by the Authors

From the above table, it is observed that all the significance value is less than 0.05. So, we have sufficient evidence that there is a statistical significant difference between the lending pattern of public and private banks in Agriculture, MSME, Education, Housing and across the total of the four priority sector.

Table – 4: National Scenario of Priority Sector Advances Year-Wise of Foreign Banks in India
(Amount in Rupee Billion)

Year	Total Prior ity Secto r	% of ANB C	Agri culture	% of AN BC	MS ME	% of AN BC	Housing	% of ANB C	Gro wth Perce nt in PSL
2014	238	10.15	2	0.09	199	8.47	37	1.59	
2015	248	9.48	17	0.67	196	7.49	35	1.33	4.28
2016	281	9.35	15	0.50	231	7.72	34	1.14	12.99
2017	389	12.01	65	2.02	288	8.89	36	1.10	38.59
2018	559	15.67	186	5.23	336	9.43	36	1.01	43.73
2019	866	23.73	336	9.21	478	13.10	52	1.43	54.98
2020	1209	31.11	465	11.96	691	17.78	53	1.37	39.56
2021	1339	33.67	528	13.28	776	19.52	34	0.86	10.77
2022	1401	27.89	526	10.48	852	16.97	22	0.44	4.58
2023	1550	28.59	610	11.26	921	16.99	18	0.34	10.64
CAGR	23.13%		88.82%		18.57%		-7.62%		

Source: Computed by the Author

In the above table no – 4, showing the advances given by the foreign banks in respect of priority sector from 2014 to 2023. It also reveals that all the sector i.e., Agriculture, MSME, Education, Housing and the total of these four sector advances as well as % of ANBC (Adjusted Net Bank Credit) of all the group were also computed. From the growth percent in PSL shows significant fluctuations that means minimum growth rate (4.28%) in the year 2014 and maximum growth rate (54.98%) in the year 2018 out of ten years i.e., from the year 2013 to 2022. Another calculation (CAGR) is made on these five sector from the period 2013 to 2022. From the above table it is shown that CAGR is 23.13% for PSL, 88.82% for Agriculture sector, 18.57% for MSME sector and -7.62% for Housing sector which clearly noticed that foreign banks have more efforts in the agricultural sector than the other sector for growing in our economy.

V. REVISED PRIORITY SECTOR NORMS

- Higher Loan Limits for Education: The RBI has increased the loan limit under PSL for education from Rs 20 lakh to Rs 25 lakh per individual.
- Renewable Energy Loans: Loan limits for renewable energy projects like solar power, biomass, and micro-hydel plants raised from Rs 30 crore to Rs 35 crore per borrower. Loans for individual households for renewable energy remain capped at Rs 10 lakh per borrower.
- PSL Targets for Urban Cooperative Banks (UCBs): Revised PSL target for UCBs reduced to 60% (from 75%) of Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-Balance Sheet Exposure (CEOBE), whichever is higher.
- Housing sector: Loans limits are increased to boost affordable housing, particularly in Tier-III to Tier-VI cities.
- Expansion of the 'Weaker Sections' Category: The list of eligible borrowers under the 'Weaker Sections' category has been expanded, it now includes transgenders, promoting financial inclusion and better credit access for underprivileged groups.

Note: ANBC is the total net bank credit after making necessary deductions and adjustments, and CEOBE is the amount representing the credit risk exposure of off-balance sheet items such as guarantees and letters of credit.

VI. CONCLUSION:

Commercial banks currently play a pivotal role in the development of society and economy via their priority sector lending services. Notably, the Reserve Bank of India (RBI) revised its guidelines for priority sector lending on September 4, 2020, with a focus on supporting vulnerable groups and weaker sections of society in a phased manner. Through these revised guidelines, the RBI aims to facilitate economic development in a sustainable manner by extending financial assistance to marginalized communities. Specifically, bank credit has been extended to non-banking financial companies (NBFCs) to provide funding and employment opportunities for micro, small, and medium enterprises (MSMEs) operating in rural areas. In India, public sector banks are considered crucial pillars for the effective delivery of priority sector lending services, as they actively adhere to

RBI norms and regulations. However, public sector banks tend to focus primarily on meeting RBI requirements, resulting in an unequal distribution of total advances.

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