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Priority sector lending: Comparative performance of public and private Banks in India

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Abstract
This study examines the comparative performance of priority sector lending (PSL) between public and private banks in India. PSL is a critical aspect of banking regulation in India, aimed at ensuring equitable access to credit for sectors deemed crucial for socio-economic development. Public and private banks play distinct roles in fulfilling PSL targets, with public banks traditionally shouldering a larger share of PSL obligations. However, recent trends suggest a shifting dynamic, with private banks increasingly contributing to PSL mandates. This study analyzes the factors driving this shift, including regulatory frameworks, market competition, and strategic priorities of public and private banks. By examining the comparative dynamics of PSL between these banking sectors, this study provides valuable insights into the evolving landscape of banking regulation and its implications for inclusive growth in India. The comparison analysis also demonstrates that public banks give larger average loan amounts across sectors, whereas private banks have higher growth rates, indicating a dynamic role in meeting changing market demands.

Keywords: Agriculture lending, MSME lending, education lending, housing lending, weaker section, priority sector lending, public and private banks

1. Introduction

According to the current profile of Priority Sector Lending (PSL) in India, it remains a critical component of banking regulation intended at encouraging inclusive growth and reducing socioeconomic gaps. The Reserve Bank of India (RBI) requires banks to allocate a set percentage of their lending to priority sectors such as agriculture, micro, small, and medium enterprises (MSMEs), export credit, education, housing, and others. The RBI reviews and revises PSL targets on a regular basis to ensure that they are consistent with changing economic priorities and development demands. Because of their greater social duty, public sector banks have historically borne a disproportionate share of PSL duties, but private sector banks have gradually raised their contribution to PSL over time. However, challenges persist in meeting PSL targets, including issues related to credit delivery mechanisms, compliance requirements, and monitoring mechanisms. The RBI continues to introduce measures to enhance the effectiveness of PSL, such as refinements in categorization criteria, incentives for PSL lending, and technology-driven solutions for better monitoring and evaluation. Overall, PSL is an important tool for encouraging equitable growth and development in India, with continuous attempts to assure its continued relevance and efficacy in tackling the country's socioeconomic challenges.

The present directed loan system requires banks to lend 40% of their adjusted net bank credit (ANBC) to priority sector loans. Priority areas include agriculture, MSE, export financing, housing, education, renewable energy, and social infrastructure. Sarvesh & Kanaujiya, K.S. (2023) [8], The examination of priority sector lending (PSL) data from 2012 to 2021 indicates that PSL has a large impact on India's GDP per capita, while inflation has a little impact. As loans to priority sectors increased alongside economic growth, focusing on PSL might boost India's economic prosperity. Inflation must be monitored and controlled in order for the economy to remain stable.

2. Review of literature

Trends, Issues, and Strategies delves into priority sector trends, according to Uppal 2009. According to the report, various bank groups met priority sector lending and target levels. He used financial information from public, private, and international banks. The report determined that priority sector advances by all banking institutions are on the rise. In his analysis, Ghosh (2011) [2] discovered that priority sectors such as agriculture, SSI, and others are also contributing to the rise in nonperforming assets (NPAs) at public and private sector banks. Rani, S., & Garg, D. (2015) [7] It was identified in their study that the public and private sector banks are not able to meet the targets mentioned by the RBI, and the banks are neglecting agriculture and small-scale industries. Kumar, K., and Gambhir, A. (2012) [4] stated that while public sector banks outperformed private sector banks in priority lending, they must address bad loans and non-performing assets. Veena D. & Prasad, G.V. (2020) [10], Public sector banks play a critical role in prioritising loans to essential sectors, thereby promoting economic growth in India. However, private sector banks fall short of reaching proportional lending requirements, notably in agriculture and underserved areas. The RBI must encourage private sector banks to meet their lending responsibilities in order to achieve inclusive growth objectives. Kumar, P., and Kumar, S. (2016) [5] The analysis spanning 2001 to 2014 reveals that while overall targets for priority sector lending were met on average, there's a concerning trend of declining share in net bank credit. Both public and private sector banks fell short in agricultural lending, indicating a need for policy intervention to address this issue promptly. Bag, Ray, and Roy (2022) [1] found no significant association between the profitability of India's public sector banks and advances in priority sector lending. Jain and Singhal's (2023) [3] study on priority sector lending policy highlights a tension between financial and social goals. However, PSL has a favourable impact on poor individuals. Raman (2013) [6] investigates the performance of commercial banks in priority sector lending in Tamil Nadu over a ten-year period (2000-2001 to 2009-2010). Commercial banks' performance on priority sector advances is improving, with rises of 13.9 times for public sector banks, 35.6 times for private sector banks, and 69.1 times for foreign banks. Aside from quantum-level analysis, the NPA generated by priority sector advancements from 2005-06 to 2009-10 was assessed. The share of outstanding priority sector (NPAs in total NPAs has steadily climbed, from 46% in 2008-09 to 52% at the end of 2010-11. (Passah, 2002) [11] examined the Indian financial system, which includes commercial banks, financial institutions, and capital markets. He stated that Indian banking has witnessed significant transformation during the last three decades. Following financial reforms, the Indian banking sector has seen significant changes. Makwana, A. C. (2015) [12] stated that credit management in selected banks is very bad, such as approving loans to priority sectors, and that public sector banks are less concerned with the development of priority sectors.

Looking at the above review of literature, no research has been able to explain what kind of relationship the priority sector lending of public and private banks has with the performance of their sub-sectors and bank groups.

3. Research Objectives

The objective of this study is to analyse the comparative dynamics of Priority Sector Lending (PSL) between public and private banks in India. Specifically, the study aims to:

1. To analyses sectoral performance of PSL in public and private banks in India.
2. To compare overall performance of PSL in public and private banks in India.

4. Research hypothesis

1. **H_0:** There is no significant difference in PSL lending between bank groups during the study period.
2. **H_0:** Performance of banks groups is not significantly different sector-wise.

5. Research methodology

5.1 Data sampling

The research evaluates the economy from 2012-2013 to 2021-22. The majority of the data came from secondary sources, including numerous issues of the Reserve Bank of India's Report on Trends and Progress and Statistical Tables Relating to Indian Banks.

5.2 Tools and techniques

Statistical approaches such as Mean, S.D., C.V., and CAGR have been utilized to examine the loan pattern of agriculture, MSME, education, housing, and the weaker segment of India's priority sectors. The normality test, specifically the Kolmogorov-Smirnov (K-S) test, is a statistical method used to determine whether a dataset follows a normal distribution. The T-test statistics for difference in lending between bank groupsthe performance of public and private banks in India.

6. Results and Discussion

6.1 Descriptive data analysis

Table 1: PSL by selected public banks (value in Rs. Cr.)

Year	Agriculture	MSME	Education	Housing	Weaker Section
2013	522506.67	464212.51	50782.35	199238.86	341915.36
2014	672005.14	565233.38	54834.03	218830.82	427847.53
2015	734988.65	625433.81	56656.70	231362.07	478491.80
2016	865278.54	703225.72	58732.99	254643.14	527765.69
2017	905418.50	710733.91	59302.15	274456.21	575805.90
2018	919157.59	828638.38	57845.06	269252.50	592753.56
2019	975354.10	905684.55	58139.29	338367.82	657333.18
2020	975766.47	928118.77	57522.70	372043.57	731917.45
2021	1125565.90	991686.37	56573.50	392584.92	835853.74
2022	1209788.24	1043992.93	55908.70	412701.48	893964.17
Mean (Cr.)	890582.98	776696.03	56629.75	296348.14	606364.84

S.D. (Cr.)	205668.10	192908.99	2450.83	76674.01	176128.17
C.V. (%)	23.09	24.84	4.33	25.87	29.05
CAGR (%)	8.76	8.44	0.97	7.55	10.09

***Source*:** Author calculation using RBI data

The table-1 provides data on the disbursement of loans in various sectors over a period of ten years from 2013 to 2022, categorized into Agriculture, MSME (Micro, Small, and Medium Enterprises), Education, Housing, and Weaker Section. The Standard Deviation (S.D.) indicates the dispersion or variability of the loan amounts within each sector from their respective means. A higher S.D. suggests greater variability, while a lower S.D. indicates less variability. For instance, the Agriculture sector shows an S.D. of 205,668.10 crore, implying a considerable variance in loan disbursements over the years compared to its mean of 890,582.98 crore. The Coefficient of Variation (C.V.) is a relative measure of variability, expressed as a percentage of the mean. It allows for the comparison of the variability between sectors, irrespective of their magnitudes. A higher C.V. indicates higher relative variability. In this table, the Weaker Section sector has the highest C.V. at 29.05%, indicating relatively high variability compared to its mean disbursement amount. Conversely, Education has the lowest C.V. at 4.33%, indicating relatively low variability. These metrics provide insight into the stability and sustainability of loan disbursements across sectors over a specified period, aiding public banks in risk assessment and decision-making processes for lenders and policy makers.

Table 2: PSL by selected private banks (value in Rs. Cr.)

Year	Agriculture	MSME	Education	Housing	Weaker Section
2013	99649.89	125684.46	1374.65	62355.05	43791.40
2014	132775.27	166331.36	1587.41	73245.98	53029.26
2015	164927.72	190458.14	1787.42	76052.15	65651.23
2016	245114.00	263925.68	1950.38	88104.42	113306.54
2017	269345.91	314239.14	2327.62	91077.75	134994.35
2018	328909.99	357153.22	2662.83	86727.81	172436.52
2019	391923.44	504175.85	2891.46	120666.77	234679.39
2020	480344.01	571908.56	3037.12	129769.20	292229.83
2021	497045.10	721977.01	3479.99	136209.18	298935.87
2022	594526.89	926087.64	3600.30	145331.88	344634.31
Mean (Cr.)	320456.22	414194.10	2469.92	100954.02	175368.87
S.D. (Cr.)	167828.92	262528.87	786.63	29390.07	111006.41
C.V. (%)	52.37	63.38	31.85	29.11	63.30
CAGR (%)	19.56	22.11	10.11	8.83	22.91

***Source*:** Author calculation using RBI data\

Table 2 shows the tremendous expansion in lending by private banks across sectors with a focus on agriculture, MSMEs and the poor. Notably, the CAGR of private banks is much higher than that of public banks, indicating a proactive attitude towards expanding lending activity. In the data presented, sectors such as micro, small and medium enterprises (MSME) and weaker sections have larger SD and CV values, indicating greater variability in the disbursement amount compared to the average. For example, the SD of MSME disbursements was Rs 262,528.87 crore and the CV was 63.38%, indicating high variation around the average disbursement value. Similarly, SD of weaker sections is Rs 111,006.41 crore and CV is 63.30%, showing significant variation from the average disbursement. However, loan amounts vary more widely, as shown by the comparatively high CV values, indicating large variations in lending policies among private banks.

6.2 Comparative analysis of bank groups (public and private)

Table 3: Test of normality for bank groups

Sector	Bank Group	Statistic	DF	Sig.	Decision Criteria at level (5%)
Total (Public & Private)	Public	0.085	10	0.200	Accept normality
	Private	0.146	10	0.200	

***Source*:** Author calculation

For the public bank group in Table 3, the test statistic is 0.085 with 10 degrees of freedom, giving a p-value of 0.200. Similarly, for the private bank group, the test statistic is 0.146 with 10 degrees of freedom, resulting in a p-value of 0.200. Since both p-values are larger than the significance level of 0.05 (5%), we cannot reject the null hypothesis for either group. As a result, we accept the assumption of normality for the distribution of priority sector credit in both public and private bank groups at the 5% significance level.

Table 4: T-test statistics for lending differences

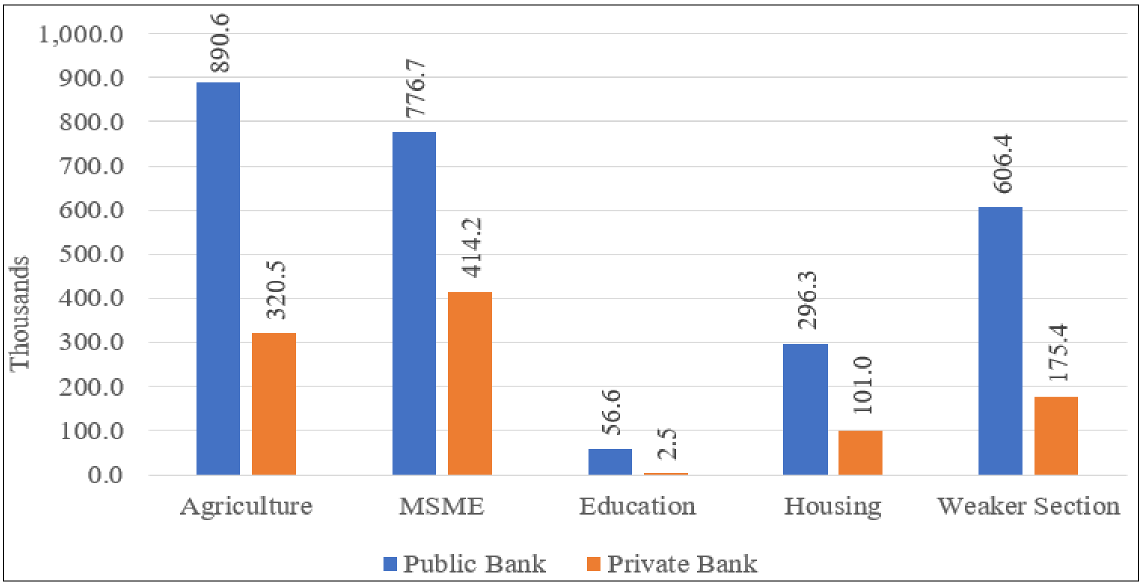
Group Statistics				
Bank Group	**No. of Obs.**	**Mean**	**S.D.**	**S.E.**
Public	10	2626621.74	645389.41	204090.05
Private	10	1013443.13	567361.98	179415.61
Independent Samples T-test				
Variances	**Levene's Test**		**t-test for Equality of Means**	
	F	**Sig.**	**t-stat**	**Sig.**
Equal	0.08	0.78	5.94	0.00
Not Equal			5.94	0.00

***Source*:** Author calculation

The null hypothesis (H0) in Table 4 states that there is no significant difference in PSL lending among these groups during the study period. Descriptive statistics show that for the public bank group the average PSL lending is approximately 2,626,621.74 units, with a standard deviation of 645,389.41, while for the private bank group, the average

PSL lending is approximately 1,013,443.13 units, with a standard deviation of 567,361.98. Levene's test for equality of variances, which assesses whether the variance of PSL borrowing amount is equal between two groups, returns a non-significant result (F = 0.08, p = 0.78), indicating that equal the assumption of differences is fulfilled. The t-test for equality of means indicates a significant difference in PSL lending between the two bank groups (t = 5.94, *p*<0.05), both under the assumption of equal variances and unequal variances. Therefore, we reject the null hypothesis and conclude that there is a statistically significant difference in PSL lending between public and private bank groups during the study period, with the average PSL lending of public banks being significantly higher than that of private banks.

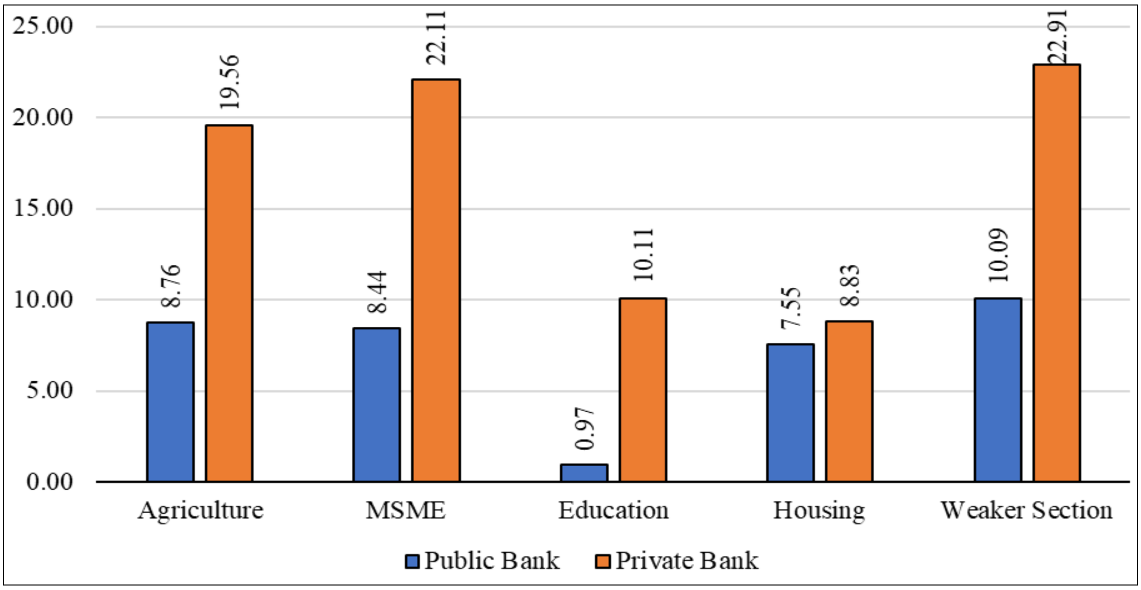
6.3 Performance of priority sectors by bank groups



Source: Author Construction

Fig 1: Sectoral performance (on the basis of mean) by bank groups

Figure 1 A comparison of average lending amounts by public and private banks in various regions of India indicates considerable disparities. When it comes to agriculture, MSME, education, housing, and weaker segment lending, public banks have much greater average loan amounts than private banks. The disparity in agricultural credit is particularly significant, with public banks averaging ₹890,582.98 compared to private banks' ₹320,456.22, suggesting a more pronounced focus by public banks on financing agricultural activities. Similarly, public banks exhibit higher average loan amounts in MSME, education, housing and weaker section lending, indicating their wider involvement in supporting priority sectors and weaker sections of the society. In contrast, the average loan number of private banks is comparatively lower across sectors, indicating possible differences in strategic priorities and market positioning. Overall, the comparative analysis underlines the distinct roles played by public and private banks in meeting priority sector credit obligations and addressing socio-economic needs in India.

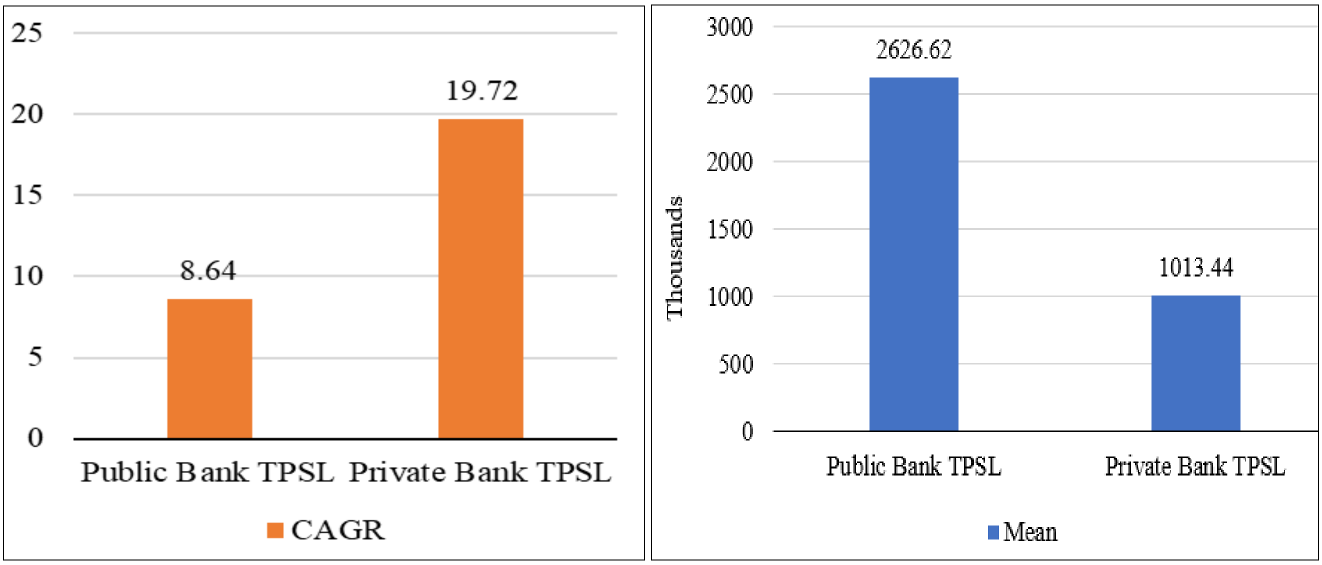


Source: Author construction

Fig 2: Comparison (On the basis of CAGR) of lending by bank groups

Figure 2 shows a comparative analysis of groupings of public and private banks based on CAGR, with private banks showing a CAGR of 19.56% in agricultural lending, which is significantly greater than public banks' CAGR of 8.76%. Similarly, in micro, small and medium enterprise (MSME) lending, private banks exhibit a strong CAGR of 22.11%, while public banks have a CAGR of 8.44%. This trend extends to education lending, where private banks exhibit a CAGR of 10.11% compared to the lowest CAGR of 0.97% for public banks. Despite relatively comparable CAGR in housing loans, with public banks at 7.55% and private banks slightly higher at 8.83%, private banks show a more proactive stance in response to the growing demand for housing finance, potentially driven by urbanization trends and government initiatives. Is inspired. Furthermore, private banks exhibit a higher CAGR of 22.91% in lending to the weaker section compared to 10.09% CAGR of public banks, which is likely driven by corporate social responsibility and strategic positioning, making a difference in addressing the financial needs of the weaker sections. Overall, these trends underline private banks' agility and focus on innovative loan products tailored to different sectors, contributing to their accelerated growth trajectory compared to public banks.

The comparative analysis of average lending amounts (figure-1) by public and private banks in different regions of India highlights significant differences, with public banks demonstrating higher average loan amounts across various sectors, indicating a broader involvement in priority sector lending. Conversely, private banks exhibit a more proactive stance in terms of Compound Annual Growth Rate (CAGR), with notably higher growth rates (figure-2) observed in agriculture, MSME, education, housing, and weaker section lending. This underscores private banks' agility and strategic focus on innovative lending products, contributing to their accelerated growth trajectory compared to public banks, thus emphasizing the distinct roles played by both sectors in meeting priority sector credit obligations and addressing socio-economic needs in India.



***Source*:** Author construction

Fig 3: PSL Performance (On the basis of CAGR and Mean) of public and private banks

Figures 3 and 4 depict the performance of banks through average and CAGR, in which the average TPSL of public sector banks is around Rs 2,626,621.74 crore with a CAGR of around 8.64%, which is reflected in the growth in lending activities in various priority sectors over the specified period indicating steady but moderate growth (Makwana, A. C., (2015) [12]. In contrast, private banks exhibit a significantly lower average TPSL of around Rs 1,013,443.13 crore but a significantly higher CAGR of around 19.72%, suggesting more aggressive and faster expansion in lending efforts. These figures underline the contrasting approaches between public and private banks in lending to key sectors, with private banks showing greater dynamism in adapting to market demands and promoting growth in priority sector lending.

7. Conclusions

The data underscores the contrasting approaches of public and private banks in priority sector lending (PSL) across various sectors in India. Public banks exhibit a steady growth trajectory, particularly emphasizing agriculture, MSME, housing, and weaker sections, reflecting their micro-level lending focus. In contrast, private banks show remarkable expansion across all sectors, with a proactive emphasis on agriculture, MSME, and serving economically disadvantaged segments. Private banks display a significantly higher Compound Annual Growth Rate (CAGR) compared to public banks, highlighting their agility and innovative lending strategies. The comparative analysis further reveals that public banks generally provide higher average loan amounts across sectors, while private banks demonstrate higher growth rates, indicating a dynamic role in addressing evolving market demands. Recommendations include fostering collaboration between public and private banks to leverage their respective strengths, enhancing public banks' agility through innovation and technology adoption, and promoting targeted initiatives to support priority sectors and weaker sections, ensuring inclusive and sustainable economic development.

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