CHAPTER -4

PRIORITY SECTOR LENDING IN INDIA- A FOCUS

4.1 Institutional Credit to Agriculture
4.2 Evolution of Priority Sector Lending
4.3 Formalization and developments in Priority Sector Lending
4.4 Broad categories of Priority Sector Lending
4.5 Targets under Priority Sector Lending
India lives in its villages and growth of Indian economy depends on the growth of the rural economy. The variation in rural income causes variations in the demand for products of the industrial as well as services sector. A recent study based on sectoral demand matrices indicated that in 1993-94, one unit rise in agricultural output was likely to increase the demand for industrial products by 0.297 unit (i.e., more than three times as compared to 1968-69), while demand for services sector increased by around 0.149 unit in 1993-94 as against 0.035 unit in 1968-69 (Tapas Kumar Chakrabarty).85

4.1 INSTITUTIONAL CREDIT TO AGRICULTURE

Agriculture plays a crucial role in India and as such, priority is given to agricultural credit. The genesis of institutional credit to agriculture could be traced back to the enactment of Co-operative Act in 1904. The Reserve Bank of India Act 1934 envisaged a special developmental role for Reserve Bank of India in the sphere of agriculture credit. The Rural Banking Enquiry Committee (Thakurdas Committee, 1950)86 stressed the need for an efficient system of agricultural finance, preferably of a sound co-operative credit structure capable of developing close relations with the Banks. RBI organized an informal conference to follow up the Rural Banking Enquiry Committee’s recommendations. Based on the recommendations, it has decided to organize a Rural Credit Survey and constituted a Standing Advisory Committee on Agricultural Credit.

The All India Rural Credit Survey commissioned in August 1951, covered seventy five districts around the country. Eight villages in each were chosen for the

85 Tapas Kumar Chakrabarty, Rural Income: Some evidence of effect of rural credit during last three decades, RBI Occasional paper, Vol.24, No.3, winter 2003, pp.225
86 Report of Thakurdas Committee rbdocs.rbi.org.in/rdocs/content/PDFs/90025.pdf, pp 231- 235
Survey, which was based on a sample of fifteen households from each of the selected villages. The survey report reveals the negligible presence of cooperatives and other organized credit institutions in rural India. Of the total amount borrowed by cultivators in 1951-52, about 3 per cent each came from the government, cooperatives, and less than one per cent from commercial banks. Money lenders accounted for nearly 70 per cent. According to the Report, “today agricultural credit that is supplied falls short of the right quantity, is not of the right type, does not serve the right purpose and by the criterion of need (not overlooking the criterion of creditworthiness) often fails to go to the right people”.

The report emphasized the need for an integrated system of co-operation and rural credit. They suggested that a state owned bank is needed to help the co-operative institutions and to expand the rural credit. In pursuance of these recommendations, Government of India nationalized Imperial Bank of India and renamed as State Bank of India in 1955 with the broad objective of catering to the needs of the rural people. Consequent to this, its subsidiaries were also nationalized.

4.1.1 Funds for Agricultural Development

A bill was passed in 1955 to appoint a third Deputy Governor to deal exclusively with rural credit. National Agricultural Credit (long term operations) Fund was created authorizing the RBI to specify the purposes for which it make medium term loans. The bill empowered RBI to make long term loans to State Governments. The State Governments in turn subscribe to the share capital of Co-operative Institutions and to

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87 Tapas Kumar Chakrabarty, op. cit., pp.228
Central Land Mortgage Banks. The bill also empowers RBI to set up the proposed special funds.

In 1960, the Committee on Co-operative Credit (Vaikunth Lal Mehta Committee) advised examining the possibility of using P.L.480 funds to give loans for long term productive investment in agriculture. Consequently, the Agricultural Refinance Corporation Bill, 1962 was introduced and it has got the President’s assent in March 1963. This Corporation provided finance for eligible institutions like Central Land Mortgage Banks, State Cooperative Banks, Scheduled Commercial Banks and Co-operative Societies by taking approval of the Reserve Bank.

Green Revolution took place during Kharif season in 1966-67 due to adoption of High Yielding Varieties\(^88\) under High Yielding Variety Programme. This has led to significant increase in demand for credit from farmers. Co-operatives and State Bank of India could not meet the requirements of the farmers due to increased demand for credit in rural areas. Consequently, the All India Rural Credit Review Committee (Chairman: Shri B.Venkatappaiah) was set up in July 1966 to reassess the progress made in the field of rural credit by different credit agencies and to make recommendations for improving the flow of credit to agriculture. The Committee submitted its report in July 1969 and recommended that the commercial banks should play a complementary role, along with co-operatives, in extending rural credit.\(^89\)

\(^{88}\) Http://www.Preservearticles.com
\(^{89}\) Rakesh Mohan, Agricultural Credit in India: Status, Issues and Future Agenda, Reserve bank of India Bulletin, November 2004, pp-994
4.2 EVOLUTION OF PRIORITY SECTOR LENDING

4.2.1 Concept of the term ‘Priority Sector’

Sri Morarji Desai, the then Deputy Prime Minister and Minister of Finance, Government of India made a statement in the Lok Sabha on December 14, 1967 that there have been persistent complaints that several ‘priority sectors’ such as agriculture, small-scale industries and exports have not been receiving their due share of bank credit. This appears to be the first occasion that the term ‘priority sector’ was used. Thus, the concept of priority sector lending was introduced.

4.2.2 Social Control on Banks

Social control on banks was instituted through Banking Laws (Amendment) Bill 1967, which was introduced in the Lok Sabha on December 23, 1967. Through social control, banks were directed to align their operations in line with the national objectives. It was aimed at imposition of certain restrictions on banks to give advances to small industries, agriculture etc. It also facilitates the government to have control over the affairs of the bank management.

The National Credit Council (NCC) has been set up in February 1968 with the responsibility of estimating the demand for bank credit from different sectors of the economy. The report stressed the need for co-ordination between co-operative banks and commercial banks in order to achieve optimum utilization of resources and to substitute the usurious money lenders and indigenous bankers.

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90 Documents from RBI records, rbidocs.rbi.org.in/rdocs/content/PDFs/90025.pdf, pp.800
91 Vimala.P A Study on the Priority Sector Lending by commercial banks in Kerala, Ph.D Thesis, 2002 Mahatma Gandhi University, Kerala
92 Chapter III, Evolution of Banking in India, Report on Currency and Finance 2006-08 Vol.4 pp.96,
4.2.3 Nationalization of Banks

The social control on banks has led the commercial banks to move towards mass banking. Despite commercial banks’ lending to agriculture under a) direct financing and b) Indirect financing, the lending towards agriculture did not exceed two per cent of the total credit.\textsuperscript{93} This shows that social control did not show much impact on rural lending and still, much of the credit went to big business houses. Bank credit to hitherto neglected areas was still a dream. In order to correct the situation, the then Prime Minister Smt. Indira Gandhi nationalized 14 major commercial banks on July 19, 1969 through an ordinance and this was a milestone in banking history of India. The broad objectives of nationalization were:

a. To provide adequate and timely credit for agriculture, small industries and exports

b. To give professional bent to bank management

c. To encourage new class of entrepreneurs\textsuperscript{94}

After nationalization of banks in 1969, the broad categories under priority sector were Agriculture, small scale industries and exports.\textsuperscript{95}

This is the genesis of priority sector lending, which is actually directed lending imposed on the Indian Banks in the name of ‘social control’. The scope of the priority sector lending concept was formalized over a period of time and the targets were raised from time to time.

\textsuperscript{93} Kanagasabai .S, An Economic Analysis of Priority Sector Lending under Lead Bank Scheme in Union Territory of Pondicherry, Ph.D Thesis, 1999, Pondicherry University, Pondicherry , pp.122


\textsuperscript{95} Kanagasabai, op. cit., pp.122
4.2.4 Lead Bank Scheme

The Study Group on the Organizational Frame Work for the Implementation of Social Objectives (Chairman: Prof.D.R.Gadgil) and the Committee of Bankers (Chairman: Shri.F.K.F. Nariman) advised that commercial banks should increase their lending to rural areas and districts are to be allotted to banks, so that they could play a lead role in those districts to provide banking facilities. Following the recommendations of these Groups, RBI introduced ‘Lead Bank Scheme’ in December 1969. The scheme was basically aimed at branch expansion and co-ordinating with other financial institutions and developmental agencies in the district.

4.3 FORMALIZATION AND DEVELOPMENTS IN PRIORITY SECTOR LENDING

4.3.1 Formalization of priority sector lending

Priority sector lending was formalized in 1972 with the recommendations of Informal Study Group on Statistics relating to advances to the priority sectors. As per the recommendations, Priority Sector constitutes:

- Agriculture – direct and indirect advances
- Small scale industries
- Industrial estates
- Road and water transport operators
- Retail traders
- Professionals and self-employed persons
- Education

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97 Vimala.P, op. cit.
Until formalization of priority sectors, advances to transport operators and advances for establishment of industrial estates were treated as part of advances to small scale industries. However, they were treated as separate sectors now. No targets were imposed on banks for giving loans to priority sectors. The items which are included in priority sectors have two advantages. They will get priority in sanctioning of credit and concessions in terms and conditions including rate of interest.

4.3.2 Differential Rate of Interest Scheme (DRI)

The Differential Rate of Interest (DRI) Scheme was initiated in 1972. It was specifically designed to the weaker sections and advances are granted at a concessional rate of interest under this scheme. These advances should constitute one-half per cent of their aggregate advances as at the end of the previous year. This proportion has since been raised to a minimum of 1 per cent in November 1978. Further, it is stipulated that two-thirds of the credit advanced under the DRI scheme should be deployed in rural areas and 40 per cent of the credit should be directed towards scheduled castes/tribes.98

4.3.3 Targets for Priority Sector Lending

Targets for priority sector were laid down in 1974. As per the guidelines, priority sector advances by public sector banks should reach a level of not less than one third of their total outstanding advances by March 1979.99

In 1978, export credit was excluded for the purpose of computation of the total priority sector advances though banks continue to receive concessive refinance facility against export credit from RBI. In the same year, RBI advised private banks also to

99 Chapter III, Evolution of Banking in India, Report on Currency and Finance, 2006-08 vol.4, pp.100
reach a level of not less than one third of their total outstanding by March 1980 on par with public sector banks.\textsuperscript{100}

\textbf{4.3.4 Revision of Targets for Priority Sector Lending}

At a meeting of the Union Finance Minister with Chief Executive Officers of the public sector banks held in March 1980, it was resolved that the banks should raise the proportion of priority sector advances to 40 percent by March 1985.

On the basis of this suggestion, RBI appointed a Working Group on the Modalities of Implementation of the Priority Sector Lending and 20-Point Economic Programme Dr.K.S.Krishnaswamy) in 1980\textsuperscript{101}. Based on the recommendations of the Committee, RBI fixed the following targets:

1. All the commercial banks(both public sector and private sector) should raise the share of priority sector advances to 40 per cent by March 1985
2. Banks to lend 16 per cent of credit to agriculture by March 1985
3. At least 50 percent of direct agricultural advances should go to weaker sections by 1983.
4. Small scale industrial advances granted to units with credit limits not exceeding Rs.25,000 have been considered as advances to weaker sections and banks were advised to lend at least 12.5 per cent of SSI credit to these units by March 1985.
5. The definition of priority sector was amended to include housing loans and consumption credit. Housing loans up to Rs.5000 for construction of houses for SC/ST and weaker sections, assistance to any governmental agency for

\textsuperscript{100} Vimala.P, op. cit.,

construction of houses for SC/ST and low-income groups (where loan component does not exceed Rs.5000 per unit) and pure consumption loans granted under the Consumption Credit Scheme are treated as priority sector advances.

Further, RBI advised public sector banks, that they should achieve a credit-deposit (CD) ratio of at least 60 per cent by March 1979 in rural and semi-urban branches, while it is not necessary that this ratio should be achieved branch-wise, district-wise or region-wise.  

Based on the recommendations of the Committee(Chairman: B. Sivaram) to review the arrangements for institutional credit for agriculture and rural development, National Bank for Agriculture and Rural Development (NABARD) was set up in 1982 to look after all the major works related to rural credit except works related to Urban Cooperatives. A new Rural Planning and Credit Department was also set up to look into the rural credit policies.

4.3.5 Re-defining the Priority Sector and Weaker Sections

Reserve Bank of India issued the following guidelines to all the banks in February 1983, as per the recommendations of the Working Group headed by Shri.A.Ghosh in 1982.

i. The revised classification of various segments of priority sector was:

Agriculture (both direct and indirect), Small Scale Industries, Small Road and Water Transport Operators, Retail Trade, Small Business, Professional and Self Employed

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103 Tapas Kumar Chakrabarty, *op. cit.*, 230
104 Murthy C.S, *op. cit.*
Persons, State sponsored schemes for Scheduled Castes/Scheduled Tribes, Education, Housing and Consumption loans.

ii. Banks to achieve direct agriculture lending of 15 per cent of total bank credit by March 1985 and 16 per cent by March 1987 and 17 per cent by March 1989 and 18 per cent by March 1990 respectively. The sub target was further bifurcated in October 1993 to a minimum of 13.5 per cent for direct loans and a maximum of 4.5 per cent on indirect loans.

Redefined the weaker sections and advised the banks that loans to weaker sections should reach a level of 25 per cent of priority sector advances by March 1985.

The revised definition of weaker sections\textsuperscript{105} under priority sector would include:

a. Small and marginal farmers with land holdings of five acres and less, landless labourers, tenant farmers and also share croppers.

b. Artisans irrespective of location or small industrial activity viz., manufacturing, processing, preservation and servicing in villages and small towns with a population of not exceeding 50,000 involving utilization of locality available resources and/or human skills, where individual credit requirements does not exceed Rs.25,000.

c. IRDP beneficiaries

d. Scheduled Castes and Scheduled Tribes

e. DRI beneficiaries

\textsuperscript{105} Vimala P P, op. cit.,
RBI advised foreign banks to increase their priority sector advances to reach a level of 15 per cent of their net bank credit (NBC) by the end of March 1992 and 32 per cent of net bank credit by March 1994. Within the enhanced target of 32 per cent, two sub targets of 10 per cent in respect of SSI and 12 per cent for exports were fixed.

4.3.6 Service Area Approach

In April 1989, RBI introduced the concept of Service Area Approach following the recommendations of the Committee (Chairman: Shri. P.D. Ohja), with a view to bring about orderly and planned development of rural and semi-urban areas of the country.  

4.3.7 Developments in Priority Sector Lending (1990-1999)

In September 1990, concessional rates of interest on specific sectors or programmes were removed except in a few areas like agriculture, small industries, differential rate of interest (DRI) scheme and export credit.

The amount of refinance granted by sponsor banks to Regional Rural Banks was included under priority sector category in 1995.

Advances to minority communities were also included in priority segments in 1996 based on the resolution made in a meeting of the National Commission for Minorities at New Delhi on March 11, 1996.

RBI issued instructions to banks to show SHG lending as a separate segment under priority sector as Kalia Committee viewed that the SHG-bank linkage programme

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106 Anant Bhushan, Lead Bank Scheme-Yesterday, today, tomorrow, Scribed.com
108 Circular No.RPCD.No.Plan.BC.128/04.09.01/94-95, dated 03.03.1995
109 Vimala.P. op. cit.,
is cost effective, transparent and flexible to improve the accessibility of credit from formal banking system to the rural poor.\textsuperscript{110}

Following the recommendations of Shi R.V.Gupta Committee (1995), RBI advised commercial banks to prepare Special Agricultural Credit Plans (SACP) in which banks set targets for themselves for disbursements taking into account the annual increment in credit indicated by the Reserve Bank. The target of 18 per cent has not been met despite monitoring credit flow through SACP.\textsuperscript{111}

As recommended by the Banking Sector Reforms Committee (Chairman: Shri. M. Narasimham), activities like food processing, related service activities in agriculture, fisheries, poultry and dairying had been brought under the category of priority sector in 1999.\textsuperscript{112}

4.3.8 Developments in Priority Sector Lending (2000-01):

- Commercial Banks are free to fix their Prime Lending Rate (PLR) subject to approval of their Boards and that rates of interest on loans up to Rs. 2 lakh should not exceed the PLR of the bank.
- Loans to non-banking finance companies for on-lending to agriculture would be reckoned as priority sector lending.
- Micro credit granted by banks to individual borrowers either directly or through any intermediary would be reckoned as part of their priority sector lending.
- Collateral requirements are not necessary for loans up to Rs. 5 lakh for tiny sector.

\textsuperscript{110} RPCD. No. PL.BC.120/04.09.22/95-96 April 2, 1996
\textsuperscript{111} Recommendation of R.V. Gupta Committee quoted in V.S.Vyas Committee Report, Para 2.7 to 2.10, June 2004, www.rbi.org.in
\textsuperscript{112} Circular RPCD No. Plan.BC.60/04.09.01/98-99 dated 28.01.1999. www.rbi.org.in
• Composite loan limit for providing working capital and term loan through single window has been increased from Rs.10 lakh to Rs.25 lakh.

• RBI advised public sector banks to open at least one specialized small scale industry (SSI) branch in every district and in centres having cluster of SSI units. As at the end of March 2001, there were 390 specialized SSI bank branches in the country.\(^{113}\)

4.3.9 Developments in 2001-02:

The scope of priority sector lending was further expanded during the year 2000-01.

- Advances for small and marginal farmers for setting up of agri-clinics and agri-business centres and purchases for agricultural purposes were included
- The limits for financing for distribution of inputs for allied activities such as cattle feed, poultry feed, etc. under priority sector was increased to Rs. 25 lakh from Rs. 15 lakh.
- Credit limits for marketing of crops was increased to Rs. 5 lakh from Rs. 1 lakh and the repayment period for such loans was enhanced to 12 months from 6 months.
- Funds financed to RRBs for on lending to priority sectors are excluded for counting the performance of sponsoring banks under priority sector advances.

\(^{113}\) Policy perspectives, Trends and progress of banking in India 2000-01, www.rbi.org.in

The limit for dispensation of collateral requirements has been raised to 15 lakh for the SSI units having a good track record and financial position. As at end of March 2002, 395 specialized SSI bank branches are operating in the country.

Banks have been permitted to categorize their general branches having 60 per cent or more of their advances to SSI sector as specialized SSI branches.

4.3.10. Developments in 2002-03:

The limit on advances granted to dealers in drip irrigation / sprinkler irrigation system / agricultural machinery was increased from Rs.10 lakh to Rs.20 lakh irrespective of their location.

The existing overall limit of Rs.10 lakh in respect of setting up of small business was increased to Rs.20 lakh without any ceiling for working capital. Further, banks are free to fix individual limits for working capital depending upon the requirements of different activities.

Individual credit limit to artisans, village and cottage industries was raised to Rs.50,000 from the existing limit of Rs.25,000. This will be under the overall limit of 25 per cent advances to weaker sections under priority sector or 10 per cent of net bank credit.

The limit for housing loans for repairing the damaged houses was increased from Rs.50,000 to Rs.1 lakh in rural and semi-urban areas and to Rs.2 lakh in urban areas.

Housing loans up to Rs.10 lakhs in rural and semi-urban areas are considered as part of priority sector lending.

To make available timely credit to the priority sector, a time frame has been fixed for disposal of loan applications.

Banks are allowed to increase the loan limit from Rs.15 lakh to Rs.25 lakh (with their board approval) for dispensation of collateral requirement to SSI units having good track record.

All new loans granted by banks to NBFCs for the purpose of on-lending to SSI sector would also be reckoned under priority sector lending.

Following the recommendations of the Advisory Committee on flow of credit to agriculture (Chairman: Prof. V.S. Vyas) in May 2004, RBI issued the revised guidelines on agricultural credit: 116

1. Waiver of margin requirements for agricultural loans up to Rs.50,000 and in the case of agri-business and agri-clinics for loans up to Rs.5 lakh.

2. Modified the NPA norms for agricultural advances aligning the repayment dates with the harvesting of crops.

3. Loans to storage units and cold storage units which are designed to store agricultural produce/products, irrespective of their location, would be treated as indirect agricultural finance under the priority sector.

4. Investments by banks in securitized assets representing direct (indirect) lending to agriculture may be treated as their direct lending to agriculture under the priority sector.

4.3.11 Developments in 2004-05:

A few changes were made in the mid-term review of annual policy of 2004-05 relating to priority sector lending.\textsuperscript{117}

- Credit limit for dealers in agricultural machinery was increased from Rs.20 lakh to Rs.30 lakhs. Credit limit for distribution of inputs to allied activities has increased from Rs.25 lakhs to Rs.40 lakhs.
- Housing loans limit increased to Rs.15 lakhs, irrespective of location.
- Loans to distressed urban poor to prepay their debt to non-institutional lenders, against appropriate collateral or group securities have been classified as priority sector advances.
- The composite loan limit for SSI entrepreneurs enhanced from Rs.50 lakh to Rs.1 crore.
- 40 per cent of the direct advances under special agricultural credit plans should be disbursed to small and marginal farmers by March 2007.
- Private sector banks are also required to formulate special agricultural credit plans from 2005-06 with an annual growth rate of 20-25 per cent.
- Investments made by banks in securitized assets representing direct lending to the SSI sector have been classified as their direct lending to SSI sector under priority sector advances.

Further, the following changes have been took place in priority sector lending (PSL) norms in 2004-05.\textsuperscript{118}

\begin{flushright}
\textsuperscript{117} Ibid.  
\textsuperscript{118} Policy Developments in Commercial Banking, Trends and Progress of banking in India 2004-05, www.rbi.org.in pp16-26
\end{flushright}
1. Ceiling on credit limit to farmers against pledge/hypothecation of agricultural produce (including warehouse receipts) was increased from Rs.5 lakh to Rs.10 lakh.

2. Investments by banks in the mortgage backed securities have been classified as direct lending to housing within the priority sector subject to conditions.

3. Investment limit in plant and machinery for seven items belonging to sports goods, which are reserved for manufacture in the SSI sector, was enhanced from Rs.1 crore to Rs.5 crore for the purpose of classification under priority sector advances.

4. Investments made by banks on or after April 1, 2005 in the special bonds issued by certain specified institutions would not be eligible for classification under PSL and investments already made by banks up to March 31, 2005 would cease to be eligible for classification under PSL in a phased manner.

5. Investments made by banks in venture capital on or after July 1, 2005 are not eligible for classification under PSL and investments already made up to June 30, 2005 would not be eligible for classification under PSL from April 1, 2006.

6. Another significant development to promote banking habits among the rural poor is financial inclusion.

Based on the recommendations of the Working Group on Flow of Credit to SSI Sector (Ganguly Committee) in 2004, the tenure of deposits made by foreign banks with SIDBI has been increased from one year to three years from the year 2005-06. The rates of interest also have been revised to make the deposits unattractive. They are inversely
linked to the extent of shortfall in the overall target or aggregate shortfall in the sub-targets whichever is higher.

As per the recommendations of the High Level Committee on Credit to SSI (Kapur Committee) to study the flow of credit to Small Scale Industries, RBI issued the following guidelines:

- 40% of the resources of SIDBI are earmarked for tiny sector enterprises whose investment in Plant and Machinery does not exceed Rs.5 lakh.
- Banks are advised to give a lot of publicity to the margin money scheme of KVIC.
- The limit of composite loans enhanced from Rs. 2 lakh to Rs. 5.00 lakh so that the entire requirement of such units is met by single documentation, security, and charge creation process. This facility is extended to all SSI units requiring loans up to Rs. 5.00 lakh irrespective of their location.

4.3.12 Developments in 2005-06

The scope of priority sector lending was further enlarged in the Annual policy 2005-06.

i. 50 per cent of the credit outstanding on loans issued under General Purpose Credit Cards (GCC) scheme in rural and semi-urban areas is eligible for classification as indirect finance to agriculture within the priority sector from December 2005.

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119 Report of Working Group on Flow of Credit to SSI Sector (Ganguly Committee), 2004. www.rbi.org.in
120 Policy Developments in Commercial Banking. Trends and Progress of Banking in India 2005-06, www.rbi.org.in
ii. Loans issued to power distribution corporations/companies for reimbursement of expenditure already incurred by them for providing electricity connections to individual farmers for their wells are classified as indirect finance to agriculture.

4.3.13 Developments in 2006-07

Priority sector lending norms were changed from 30 April 2007, based on the recommendations of the Internal Working Group (Chairman: Shri C.S. Murthy) and feedback received from governments, banks etc. Major changes made in the guidelines are:

- Loans above Rs.1 crore sanctioned to big Corporates will get only one-third weightage for being counted under direct agriculture advances.
- Investment in bonds of financial institutions shall not be treated as priority sector loans.
- Priority sector lending is linked to the credit equivalent to the off balance sheet exposure as some banks are showing nil Net Bank Credit in their balance sheets.
- The overall target of 40 per cent and 32 per cent for the domestic and foreign banks has remained unchanged. Nevertheless, instead of Net Bank Credit (NBC), this is now calculated as a percentage of adjusted net bank credit (ANBC). (New targets are linked to ANBC or the credit equivalent amount to off-balance sheet exposures, whichever is higher as on March 31 of the previous year)

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122 An asset or debt that does not appear on a company’s balance sheet. Items that are considered off balance sheet are generally ones in which the company does not have legal claim or responsibility for.

123 ANBC includes Net Bank Credit plus investments made by banks in non-SLR bonds held in (Held to Maturity) HTM category.
• The outstanding FCNR (B) and NRNR deposits balances are withdrawn from computation of ANBC for priority sector lending purposes.

• Revised definition of MSMED Act, 2006 will be considered for SSI units.

Further, RBI advised banks in July 2007 to ensure that:

✓ 40 per cent of the total advances to small enterprises sector should go to micro (manufacturing) enterprises having investment in plant and machinery up to Rs.5 lakh and micro (service) enterprises having investment in equipment up to Rs.2 lakh.

✓ 20 per cent of the total advances to small enterprises sector should go to micro (manufacturing) enterprises with investment in plant and machinery above Rs.5 lakh but up to Rs.25 lakh, and micro (service) enterprises with investment in equipment above Rs.2 lakh but up to Rs.10 lakh. Thus 60 per cent of small enterprises advances should go to the micro enterprises.

As per the recommendations of the Working Group to examine procedures and processes for obtaining agricultural loans (Chairman: Shri C.P.Swarnakar) in December 2006, RBI advised all the commercial banks to dispense with the no dues certificate for small loans up to Rs.50000/- from small and marginal farmers, share croppers and instead obtain a self declaration form from the borrower.

Further RBI had set up a High Level Committee on Lead Bank Scheme\(^\text{124}\) under the Chairmanship of Smt.Usha Thorat to examine the status of Lead bank scheme in the country. The important recommendations of the Committee are:

\(^{124}\) Report of High Level Committee on Lead Bank Scheme Para Nos.3.7 to 3.10, www.rbi.org.in
Lead Bank Scheme is useful and it should continue.

The scope of the Lead Bank Scheme should be broadened to cover the area of financial inclusion.

The Committee also recommended that in every district, a sub committee of the District Consultative Committee may draw up a road map to provide banking services through a banking outlet in every village with a population of over 2000 at least once a week on a regular basis. Such a banking outlet could be through various forms viz. mobile banking, extension counters, satellite offices or business correspondents (BCs). The time limit for such road map should not be later than March 2011.

4.3.14. Developments in 2007-08

The shortfall in lending to weaker sections by domestic scheduled commercial banks would also be taken into account for the purpose of calculating amounts for contribution to the Rural Infrastructure Development Fund (RIDF) or funds with other financial institutions with effect from April 2009.125

The Government constituted the Expert Group on Agricultural Indebtedness (Chairman: Dr. R. Radhakrishna). The Committee reviewed the issues related to the creation of credit absorption capacities, need for risk mitigation practices, introduction of cyclical credit system, setting up of dispute resolution mechanisms and a debt redemption fund.

125 Policy developments in commercial banking, Trends and Progress of banking in India 2007-08
Following the recommendations of Expert Group, an Internal Working Group (Chairman: Shri V.S. Das) was constituted to examine those recommendations that were relevant to the banking system in general and the Reserve Bank in particular. Consequent to these recommendations, RBI initiated certain measures in August 2008. They were:

a) Banks were advised to select one rain fed district for financing a new product on a pilot basis where by:

   (i) 80 per cent of the crop loan requirement of individual borrowers could be released through a short-term production loan in conformity with the extant norms/practices;

   (ii) The remaining 20 per cent representing the ‘core component’ (expenses for land preparation, pre-sowing operations, etc., besides self-labour/consumption) could be sanctioned as a ‘clean credit limit’ to ensure year-round liquidity.

Banks were also advised to allow overdraft in the ‘clean credit limit’ as long as the farmers continued to service the interest. The asset classification is same as in the case of non-agricultural cash credit/over draft accounts. In case of re-schedulement of loans, the outstanding balance in clean credit limit is to be clubbed with the loan account of the farmer and a fresh ‘clean credit limit’ should be made available to the farmer. Under normal circumstances, the extant guidelines of borrower-wise asset classification would prevail for the new product also, unless specifically dispensed.
RBI constituted a Working Group (Chairman: Professor S.S. Joshi)\textsuperscript{126} to suggest measures for assisting distressed farmers and the Committee recommended that financial and livelihood counselling is important for increasing the viability of credit. Further, the Working Group constituted to examine procedures and processes for agricultural loans (Chairman: Shri C.P. Swarnkar) had also recommended that banks should open counselling centres, either individually or with pooled resources, for credit and technical counselling with a view to give special thrust for credit delivery in the relatively underdeveloped regions.

In the light of the recommendations of these two Groups, in May 2007, RBI advised the convener banks of SLBCs to set up a financial literacy-cum-counselling centre in any one district on a pilot basis and extend it to all other districts in due course.

\subsection*{4.3.15 Developments in 2008-09}

Commercial banks have been advised to link the tenor of loans to Housing Finance Companies (HFCs) in line with the average portfolio maturity of housing loans up to Rs.20 lakh extended by HFCs to individual borrowers, otherwise such loans would not be eligible for classification under priority sector. Banks have been advised to ensure the end-use of funds strictly as per the guidelines on lending to priority sector.\textsuperscript{127}

\subsection*{4.3.16 Developments in 2009-10}

Government of India constituted a High Level Task Force (Chairman: Shri T. K. A. Nair) to consider various issues relating to the Micro, Small and Medium Enterprises (MSMEs). Following the recommendations of the Task Force, in June 2010, RBI

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\textsuperscript{126} Report on Trends and Progress of Banking in India, 2007-08, www.rbi.org.in
\textsuperscript{127} Report on Trends and Progress of Banking in India, 2009-10, www.rbi.org.in
\end{flushright}
advised commercial banks to achieve a share of 60 per cent in Micro and Small Enterprises lending in three stages.

- 50 per cent in 2010-11,
- 55 per cent in 2011-12 and
- 60 per cent in 2012-13

with an annual growth of 10 per cent in number of accounts and 20 per cent in amount.

RBI constituted a Working Group (Chairman: Shri V. K. Sharma) to review the working of the Credit Guarantee Scheme of Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE). Consequent to the recommendations of the Working Group, RBI instructed the commercial banks on May 6, 2010, to issue collateral free loans up to Rs.10 lakh to the units in Micro and Small Enterprises sector.

4.3.17 Developments in 2010-11.128

✓ Advances to NBFCs for on-lending to individuals or other entities against gold jewellery will not be eligible for classification under priority sector advances as agricultural advances.

✓ Investments made by banks in securitized assets originated by NBFCs, where the underlying assets are loans against gold jewellery and purchase/assignment of gold loan portfolio from NBFCs are not eligible for classification under agriculture sector.

✓ To promote financial inclusion, RBI instructed banks to allocate at least 25 per cent of their total number of branches to be opened during a year to unbanked

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128 Policy Environment, Report on Trend and Progress of Banking in India 2010-11 pp.33 www.rbi.org.in
rural centres. In this context, prior approval of RBI is not necessary for opening branches in Tier 2 centres (with population of 50,000 to 99,000 as per 2001 census) subject to reporting.

The above study reveals that the scope of priority sector lending has widened over the years and norms have undergone several changes in order to provide adequate and timely flow of credit to the needy sectors of the society. At present, the broad categories of priority sector are as follows:

4.4 BROAD CATEGORIES OF PRIORITY SECTOR LENDING\(^\text{129}\)

4.4.1. Agriculture (Direct and Indirect Finance)

4.4.1a. Direct Finance

- Finance to individual farmers (including self-help groups) or joint liability groups, i.e. groups of individual farmers, (provided banks maintain disaggregated data on such finance) for agriculture and allied activities (dairy, fishery, piggery, poultry, bee-keeping etc.)
- Short term loans for raising crops i.e. for crop loans. This will include traditional/non-traditional plantations and horticulture.
- Advances up to Rs.10lakh against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months, irrespective of whether the farmers were given crop loans for raising the produce or not.
- Working capital and term loans for financing production and investment requirements for agriculture and allied activities.

\(^{129}\) RBI circular No. RPCD.CO.PLAN.BC.10/04.09.01/2010-11 DATED July 1, 2010. www.rbi.org.in
• Loans to small and marginal farmers for purchase of land for agricultural purposes.

• Loans to distressed farmers indebted to non-institutional lenders, against appropriate collateral or group security.

• Loans granted for pre-harvest and post-harvest activities such as spraying, weeding, harvesting, grading, sorting, processing and transporting undertaken by individuals, SHGs and cooperatives in rural areas.

• Loans granted for agricultural and allied activities, irrespective of whether the borrowing entity is engaged in export or otherwise. The export credit granted by banks for agricultural and allied activities may, however, be reported separately under heading “Export credit to agricultural sector”.

• Finance to others (such as corporate, partnership firms and institutions) for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.)

• Loans granted for pre-harvest and post harvest activities such as spraying, weeding, harvesting, grading, sorting and transporting.

• Finance up to an aggregate amount of Rs. one crore per borrower for the purposes raising crops and advances up to Rs.10 lakh against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months, irrespective of the purpose.

• Granting of Working capital loans and term loans for agriculture and allied activities. Loans granted for pre-harvest and post harvest activities such as spraying, weeding, harvesting, grading, sorting and transporting.

• One-third of loans in excess of Rs. one crore in aggregate per borrower for agriculture and allied activities.
4.4.1b. Indirect Finance

- Finance for Agriculture and Allied Activities:
- Two-third of loans to entities covered under Finance to others (such as corporate, partnership firms and institutions) in excess of Rs. One Crore in aggregate per borrower for agriculture and allied activities.
- Loans to food and agro-based processing units with investments in plant and machinery up to Rs.10 crore, undertaken by those other than loans granted for pre-harvest and post-harvest activities such as spraying, weeding, harvesting, grading, sorting, processing and transporting undertaken by individuals, SHGs and cooperatives in rural areas.
- Credit for purchase and distribution of fertilizers, pesticides, seeds etc.
- (ii)Loans up to Rs. 40 lakh granted for purchase and distribution of inputs for the allied activities such as cattle feed, poultry feed etc.
- Finance for setting up of Agriclinics and Agribusiness centres.
- Finance for hire purchase schemes for distribution of agricultural machinery and implements.
- Loans to farmers through Primary Agricultural Credit Societies(PACS), Farmers’ Service Societies (FSS) and Large-sized Adivasi Multi Purpose Societies(LAMPS).
- Loans to cooperative societies of farmers for disposing of the produce of members.
- Financing the farmers indirectly through the co-operative system(otherwise than by subscription to bonds and debenture issues)
Loans for construction and running storage facilities (warehouse, market yards, godowns etc.), including cold storage units designed to store agriculture produce/products, irrespective of their location. If the storage unit is registered as SSI unit/micro or small enterprise, the loans granted to such units may be classified under advances to Micro and Small Enterprises sector.

Advances to Custom Service Units managed by individuals, institutions or organizations who maintain a fleet of tractors, bulldozers, well-boring equipment, threshers, combines, etc., and undertake work for farmers on contract basis.

Finance extended to dealers in drip irrigation/sprinkler irrigation system/agricultural machinery, irrespective of their location.

Loans to Arthias (commission agents in rural/semi-urban areas functioning in markets/mandies) for extending credit to farmers, for supply of inputs as also for buying the output from the individual farmers/SHGs/JLGs.

Credit outstanding under loans for general purposes under General Credit Cards (GCC).

Loans to Non-Banking Financial Companies (NBFCs) for on lending to individual farmers or their SHGs/JLGs.

Loans granted to NGOs/MFIs for on-lending to individual farmers or their SHGs/JLGs.

Loans granted to RRBs for on-lending to agriculture and allied activities sector.

Overdrafts, up to Rs.25,000 (per account), granted against ‘no-frills’ accounts in rural and semi-urban areas.

4.4.2. Micro and Small Enterprises
4.4.2a Direct Finance in the micro and small enterprises sector will include credit to

- Manufacturing Enterprises
- Small (manufacturing) Enterprises
- Enterprises engaged in the manufacture/production, processing or preservation of goods and whose investment in plant and machinery does not exceed Rs. 5 crore.
- Micro (manufacturing) Enterprises
- Enterprises engaged in the manufacture/production, processing or preservation of goods whose investment in plant and machinery does not exceed Rs. 25 lakh, irrespective of the location of the unit.
- Service Enterprises
- Small (Service) Enterprises:
  - Enterprises engaged in providing/rendering of services and whose investment in equipment does not exceed Rs. 2 crore.
- (b)Micro (service) Enterprises
  - Enterprises engaged in providing/rendering of services and whose investment in equipment does not exceed Rs. 10 lakh.
- The small and micro(service) enterprises shall include small road and water transport operators, small business, professional and self-employed persons, and other service enterprises.
- Khadi and Village Industries Sector (KVI)
- All advances granted to units in the KVI sector, irrespective of their size of operations, location and amount of original investment in plant and machinery,
such advances will be eligible for consideration under the sub-target (60 percent) of the micro and small enterprises segment within the priority sector.

4.4.2b. Indirect Finance

- Indirect finance to the micro and small (manufacturing as well as services) enterprises sector will include credit to:
- Persons involved in assisting the decentralized sector in the supply of inputs to and marketing of outputs of artisans, village and cottage industries.
- Advances to cooperatives of producers in the decentralized sector viz. artisans village and cottage industries.
- Loans granted by banks to NBFCs for on-lending to micro and small enterprises (manufacturing as well as service).

4.4.3. Micro Credit

- Loans of very small amount not exceeding Rs.50,000 per borrower provided by banks either directly or indirectly through a SHG/JLG mechanism or to NBFC/MFI for on-lending up to Rs.50,000 per borrower.
- Loans to poor indebted to informal sector.
- Loans to distress persons (other than farmers) to prepay their debt to non-institutional lenders, against appropriate collateral or group security, would be eligible for classification under priority sector.
4.4.4. State Sponsored Organisations for Scheduled Castes/Scheduled Tribes

Advances sanctioned to State Sponsored Organisations for Scheduled Castes/Scheduled Tribes for purchase and supply of inputs and/or marketing of the outputs of the beneficiaries of these organizations.

4.4.5. Education

- Educational loans granted to individuals for educational purposes up to Rs. 10 lakh for studies in India and Rs.20 lakh for studies abroad. Loans granted to institutions will not be eligible to be classified as priority sector advances.
- Loans granted by banks to NBFCs for on-lending to individuals for educational purposes up to Rs.10 lakh for studies in India and Rs.20 lakh for studies abroad.

4.4.6. Housing

- Loans up to Rs.20 lakh, irrespective of location to individuals for purchase/construction of a dwelling unit per family, excluding loans granted by banks to their own employees.
- Loans given for repairs to the damaged dwelling units of families up to Rs.1 lakh in rural and semi-urban areas and up to Rs.2 lakh in urban and metropolitan areas.
- Assistance given to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of Rs.5 lakh per dwelling unit.
- Assistance given to a non-governmental agency approved by the NHB for the purpose of refinance for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of loan component of Rs.5 lakh per dwelling unit.
Loans granted to Housing Finance Companies (HFCs), approved by National Housing Bank for the purpose of refinance, for on-lending to individuals for purchase/construction of dwelling units, provided the housing loans granted by HFCs do not exceed Rs.20 lakh per dwelling unit per family.

4.4.7. Weaker Sections

The weaker sections under priority sector shall include the following

(a) Small and Marginal farmers with land holding of 5 acres and less, and landless labourers, tenant farmers and share croppers
(b) Artisans, village and cottage industries where individual credit limits do not exceed Rs.50,000;
(c) Beneficiaries of Swarnajayanti Gram Swarojgar Yojana (SGSY)
(d) Scheduled Castes and Scheduled Tribes
(e) Beneficiaries of Differential Rate of Interest (DRI) Scheme
(f) Beneficiaries under Swarna Jayant Shahari Rozgar Yozana (SJSRY)
(g) Beneficiaries under the scheme for Rehabilitation of Manual Scavengers (SRMS)
(h) Advances to Self-Help Groups
(i) Loans to distressed poor to prepay their debt to informal sector, against appropriate collateral or group security

4.4.8. Export Credit

This category will form part of priority sector for foreign banks only.
<table>
<thead>
<tr>
<th>Category of priority sector advances</th>
<th>Domestic Commercial banks</th>
<th>Foreign banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Priority sector advances</td>
<td>40 per cent of Adjusted net bank credit (ANBC) or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher</td>
<td>32 per cent of adjusted net bank credit (ANBC) or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher</td>
</tr>
<tr>
<td>Total agricultural advances</td>
<td>18 percent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher. (Of this, indirect lending in excess of 4.5% of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher, will not be reckoned for computing performance fewer than 18 per cent target. However, all agricultural advances under the categories ‘direct’ and ‘indirect’ will be reckoned in computing performance under the overall priority sector target of 40 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.)</td>
<td>No target</td>
</tr>
<tr>
<td>Micro and Small Enterprise advances (MSE)</td>
<td>Advances to micro and small enterprises sector will be reckoned in computing performance under the overall priority sector target of 40 percent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.</td>
<td>10 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher</td>
</tr>
<tr>
<td>-----------------------------------------</td>
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</tr>
</tbody>
</table>
| Micro enterprises within Micro and Small Enterprises Sector | (i) 40 per cent of total advances to micro and small enterprises sector should go to micro (manufacturing) enterprises having investment in plant and machinery up to Rs.5 lakh and micro (service) enterprises having investment in equipment up to Rs.2 lakh.  
(ii) 20 per cent of total advances to micro and small enterprises sector should go to micro (manufacturing) enterprises with investment in plant and machinery above Rs.5 lakh and up to Rs.25 lakh, and micro (service) enterprises with investment in equipment above Rs.2 lakh and up to Rs.10 lakh. (Thus, 60 per cent of micro and small enterprises advances should go to the micro | Same as for domestic banks |
(iii) The increase in share of micro enterprises in MSE lending to 60 per cent should be achieved in stages, viz. 50 per cent in the year 2010-11, 55% in the year 2011-12 and 60% in the year 2012-13.

<table>
<thead>
<tr>
<th>Category</th>
<th>Target/Requirement</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Export Credit</td>
<td>No target</td>
<td>12 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher.</td>
</tr>
<tr>
<td>Advances to weaker sections</td>
<td>10 per cent of ANBC or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher</td>
<td>No target</td>
</tr>
<tr>
<td>Differential Rate of Interest Scheme (DRI)</td>
<td>1 per cent of total advances outstanding as at the end of the previous year. It should be ensured that not less than 40 per cent of total advances granted under DRI Scheme go to schedules castes/scheduled tribes. At least two third of DRI advances should be granted through rural and semi-urban branches</td>
<td>No target</td>
</tr>
</tbody>
</table>