Banks may rework priority-sector lending plans after RBI tweaks

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The Reserve Bank of India's (RBI's) recent tweak to the incentive framework may push banks to take their plans for priority-sector lending (PSL) back to the drawing board to increase staff strength in branches and tone up working of Business Correspondent Network in 196 districts with low credit penetration.

The central bank recently revised the incentive structure for PSL to boost credit flow to regions with lower coverage. For 196 districts with per capita PSL less than ₹9,000, RBI has assigned a higher weight of 125 per cent to incremental priority credit flow. For 198 districts with higher PSL (those with per capita PSL of higher than ₹42,000), the risk weight is 90 per cent.

In a notification last week, RBI said the lists of districts have been updated after a review. These lists will remain valid until FY 2026-27. Senior public sector bankers said the ambit of PSL has expanded over the period to include a wide range of areas, like food processing and renewable energy.

While this reflected the importance for emerging priorities, the core PSL i.e. regions with small and marginal farmers and households have received less attention in relative terms.

Banks are required to provide at least 40 per cent of their total loans to priority sectors, according to the RBI rules. For low coverage districts, lenders would now look at deploying more staff at branches, enhance monitoring and make changes in policies for affiliated BCs to encourage more business, they added. Those already active in these areas may step up lending to get benefits from incentives. Some lenders may look at making this a focus area, said a Bank of Baroda executive.

According to RBI data, PSL in agriculture and allied sectors grew by 19.4 per cent year-on-year (Y-o-Y) in FY24 to ₹20 trillion, Small & Micro Enterprises (SME) by 20.1 per cent to ₹19.76 trillion.

The credit to medium enterprises under PSL rose by 15.8 per cent to ₹4.9 trillion and housing at 6.1 per cent to ₹7.5 trillion.

Besides direct loans in PSL category, banks also try to enhance performance by buying priority sector lending certificates (PSLC) from those who have exceeded targets in subcategories.

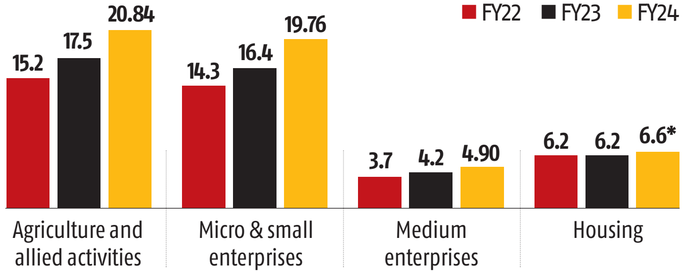
The trading volume of PSLCs was the highest in the small and marginal farmers (SMF) category in FY23, according RBI's trend and progress report FY23.

Another banker pointed out that if this move (incentive tweak) enhances PSL performance of institutions, which are falling behind PSL targets, they will have to park less amounts in with institutions like National Bank for Agriculture and Rural Development. The lenders have to place money as deposits to the extent of PSL sector shortfall in targets.

A NABARD official pointed out that while the incentive structure may have limited impact, the rules for PSLC's also need to change to curb the tendency for purchasing certificates instead of actual lending in credit deficient districts.

EXPOSURE CHECK

Priority-sector lending outstanding in ₹ trn)



*Excludes HDFC's merger with HDFC Bank

DISTRICTS IN SELECT STATES WITH PER CAPITA CREDIT LESS THAN ₹9,000

Number of districts

Arunachal Pradesh	22
Bihar	22
Uttar Pradesh	21
Assam	19
Chattisgarh	16
Nagaland	14

Source: RBI