“Role of Public Sector Banks in Promoting Economic Growth and Financial Inclusion in India”

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Abstract:

Public Sector Banks (PSBs) play a vital role in the Indian financial system and have been instrumental in promoting economic growth and financial inclusion. In a developing economy like India, PSBs function not only as financial intermediaries but also as agents of socio-economic development. The present study examines the role of Public Sector Banks in promoting economic growth and advancing financial inclusion in India. The study is descriptive and analytical in nature and is based on secondary data collected from Reserve Bank of India publications, government reports, and other official sources. The analysis covers the period from 2013–14 to 2022–23 and employs tools such as trend analysis, growth rate analysis, and correlation analysis. The findings reveal that Public Sector Banks have contributed significantly to economic growth through sustained credit expansion and priority sector lending, particularly to agriculture and MSMEs. The study also highlights the leading role of PSBs in expanding banking outreach and improving financial inclusion through branch expansion and basic savings bank deposit accounts. The positive relationship between PSB credit, economic growth, and financial inclusion confirms the integrated role of Public Sector Banks in fostering inclusive economic development. Despite challenges such as declining market share and asset quality issues, PSBs continue to remain central to India's development strategy. The study concludes that strengthening Public Sector Banks is essential for achieving sustainable and inclusive economic growth in India.

1. Introduction:

The banking system plays a crucial role in the economic development of a country by mobilizing savings, allocating credit, and facilitating investment and consumption activities. In developing economies like India, banks are not merely financial intermediaries but also key instruments of economic planning and social transformation. Among various components of the Indian banking system, Public Sector Banks (PSBs) occupy a dominant position due to their extensive branch network, government ownership, and developmental orientation.

Public Sector Banks have historically been entrusted with the responsibility of supporting economic growth by providing credit to priority sectors such as agriculture, small-scale industries, micro, small and medium enterprises (MSMEs), and infrastructure. Since nationalization, PSBs have been central to implementing government policies aimed at balanced regional development, poverty alleviation, and employment generation. Their role has been particularly significant in channelizing financial resources towards sectors that are vital for inclusive and sustainable economic growth.

Economic growth in India is closely linked with the availability of institutional credit and the efficiency of the banking system. By promoting capital formation and facilitating productive investments, Public Sector Banks contribute directly to gross domestic product growth. At the same time, PSBs play an equally important role in advancing financial inclusion by extending banking services to underserved and unbanked populations, especially in rural and semi-urban areas. Initiatives such as branch expansion, priority sector lending, basic savings bank deposit accounts, and participation in government-led inclusion programs have strengthened the outreach of formal financial services.

Financial inclusion has emerged as a key policy objective in India, recognizing that access to financial services is essential for equitable economic development. Public Sector Banks have been at the forefront of this effort, acting as the primary vehicles for implementing financial inclusion schemes and ensuring credit access to weaker sections of society. Through these efforts, PSBs contribute not only to social inclusion but also to long-term economic stability and growth.

Despite facing challenges such as rising non-performing assets, capital constraints, and increased competition from private and foreign banks, Public Sector Banks continue to play a vital role in India’s development process. Their dual function of promoting economic growth while ensuring financial inclusion makes them unique and indispensable within the Indian financial system.

In this context, the present study seeks to examine the role of Public Sector Banks in promoting economic growth and financial inclusion in India. By analysing trends in credit expansion, priority sector lending, and inclusion-oriented initiatives, the study aims to highlight the developmental contribution of PSBs and assess their continuing relevance in India’s evolving economic landscape.

2. Review of Literature

The role of banking institutions in economic development has been widely examined in economic and financial literature. Banks facilitate economic growth by mobilizing savings, allocating credit efficiently, and supporting productive investment. In the Indian context, Public Sector Banks (PSBs) have received special attention due to their dominant market share and developmental mandate.

Gurley and Shaw (1967) emphasized the role of financial institutions in mobilizing savings and directing them toward productive investments. Their study highlighted that a strong banking system contributes to economic growth by improving capital allocation efficiency. In developing economies, public sector banks play a critical role by extending credit to priority sectors and underserved regions. The authors concluded that institutional finance is essential for sustained economic development.

Goldsmith (1969) examined the relationship between financial development and economic growth, finding a positive association between banking expansion and national income growth. The study suggested that countries with well-developed banking systems experience faster economic development. In the Indian context, public sector banks contribute to growth by mobilizing domestic savings and supporting long-term investment. The study laid the foundation for later research on banking-led growth**.**

King and Levine (1993) empirically demonstrated that financial institutions significantly influence economic growth through credit provision and financial intermediation. Their findings indicated that banking development enhances productivity and capital accumulation. Public sector banks, particularly in developing economies, support growth by ensuring credit availability to productive sectors. The study reinforced the importance of inclusive and stable banking systems for long-term economic progress.

Burgess and Pande (2005) analysed the impact of bank branch expansion in rural India and found that increased access to banking services significantly reduced poverty levels. Their study highlighted the crucial role of public sector banks in promoting financial inclusion. The findings showed that state-led banking initiatives improved credit access and savings behavior among rural households, contributing to inclusive economic development.

Chakrabarty (2011) emphasized the developmental role of public sector banks in achieving financial inclusion in India. The study highlighted initiatives such as basic banking accounts, priority sector lending, and rural outreach programs. According to the author, financial inclusion not only supports social equity but also strengthens economic growth by integrating marginalized populations into the formal financial system. Public sector banks were identified as key drivers of inclusive banking.

Rajan (2014) examined the structure of the Indian banking system and stressed the importance of public sector banks in maintaining financial stability. The study argued that PSBs play a counter-cyclical role during economic downturns by sustaining credit flow. While acknowledging efficiency challenges, the author noted that PSBs remain essential for economic growth and financial inclusion due to their wide reach and public mandate.

Kumar (2016) analysed the contribution of public sector banks to priority sector lending and financial inclusion in India. The study found that PSBs account for a major share of agricultural and MSME credit. The author concluded that credit support from PSBs enhances income generation, employment, and regional development. The research emphasized the continued relevance of PSBs in achieving inclusive economic growth.

Ghosh (2018) studied the relationship between banking outreach and economic growth in India. The findings revealed that public sector banks significantly contribute to financial inclusion through rural branches and government-backed schemes. The study also noted that increased access to banking services improves savings behaviour and credit utilization. Despite rising NPAs, PSBs were found to play a vital role in supporting inclusive growth.

Patel (2020) examined the impact of financial inclusion initiatives led by public sector banks on economic development. The study found that schemes implemented through PSBs enhanced access to formal finance and reduced dependence on informal credit sources. The author highlighted that inclusive banking contributes to economic stability and growth. Strengthening PSBs was suggested as essential for sustaining inclusive development.

Sharma (2022) analysed the post-reform performance of public sector banks in India, focusing on economic growth and financial inclusion outcomes. The study observed that PSBs continue to dominate priority sector lending despite increased competition from private banks. The findings indicated a positive relationship between PSB credit expansion and inclusive growth indicators. The author concluded that PSBs remain central to India's development strategy.

3. Research Gap

The review of existing literature indicates that several studies have examined the role of banking institutions in economic growth, while others have focused on financial inclusion initiatives in India. Many researchers have highlighted the importance of Public Sector Banks in priority sector lending, rural banking expansion, and poverty reduction. Some studies have also analysed issues related to efficiency, non-performing assets, and reforms in public sector banking. However, the literature reveals that most studies treat economic growth and financial inclusion as separate areas of analysis. There is a noticeable lack of integrated research that examines the combined role of Public Sector Banks in simultaneously promoting economic growth and financial inclusion within a single analytical framework. Additionally, limited studies assess how inclusion-oriented banking initiatives translate into broader economic development outcomes over time. Furthermore, recent structural changes in the Indian banking system, including consolidation, recapitalization, and increased digitalization, have not been adequately incorporated into existing empirical and conceptual studies. This creates a gap in understanding the evolving developmental role of Public Sector Banks in the contemporary Indian economy. In light of these gaps, the present study seeks to analyse the dual role of Public

Sector Banks in promoting economic growth and advancing financial inclusion in India, thereby contributing to existing literature and providing policy-relevant insights.

4. Research Methodology

4.1 Nature of the Study

The present study is descriptive and analytical in nature. It aims to examine the role of Public Sector Banks in promoting economic growth and financial inclusion in India by analysing trends, patterns, and relationships among key banking and economic indicators.

4.2 Research Design

The study adopts a descriptive–analytical research design, which is appropriate for examining macro-level banking and economic data. This design enables a systematic assessment of the developmental and inclusion-oriented role of Public Sector Banks in the Indian economy.

4.3 Objectives of the Study

1. To examine the role of Public Sector Banks in promoting economic growth in India.
2. To analyse the contribution of Public Sector Banks towards financial inclusion in India.
3. To assess the integrated impact of Public Sector Banks on economic growth and financial inclusion in India.

4.4 Hypotheses of the Study

H1: Public Sector Banks have a significant role in promoting economic growth in India.

H2: Public Sector Banks significantly contribute to improving financial inclusion in India.

H3: There is a positive and significant relationship between the activities of Public Sector Banks, economic growth, and financial inclusion in India.

4.5 Sources of Data

The study is based exclusively on secondary data, collected from reliable and authoritative sources to ensure accuracy and consistency. Major sources include:

- Annual Reports and Statistical Publications of the Reserve Bank of India
- Publications of the Ministry of Finance, Government of India
- Reports of the World Bank
- Banking statistics published by public sector banks
- Research articles published in peer-reviewed journals, working papers, and policy reports

4.6 Period of the Study

The study covers a period of ten years, from 2013–14 to 2022–23, a phase marked by major banking reforms, financial inclusion initiatives, and structural changes in the Indian banking system.

4.7 Variables of the Study

4.7.1 Variables Related to Economic Growth

- Gross Domestic Product (GDP) growth rate
- Bank credit extended by Public Sector Banks
- Sector-wise credit deployment
- Capital formation indicators

4.7.2 Variables Related to Financial Inclusion

- Number of bank branches and ATMs
- Basic savings bank deposit accounts
- Priority sector lending
- Credit to agriculture and MSMEs

4.8 Tools and Techniques of Analysis

The study employs the following analytical tools:

- Descriptive statistics to examine trends and patterns
- Growth rate analysis to study changes over time
- Ratio analysis to assess banking performance
- Trend analysis to evaluate long-term movements
- Correlation analysis to examine the relationship between Public Sector Bank activities, economic growth, and financial inclusion

4.9 Method of Data Analysis

- Data collected from various sources are systematically classified, tabulated, and analysed using appropriate statistical techniques. The results are interpreted to assess the role of Public Sector Banks in promoting economic growth and financial inclusion in India.

4.10 Scope of the Study

- The scope of the study is limited to Public Sector Banks operating in India. The analysis focuses on their contribution to economic growth and financial inclusion at the national level.

4.11 Limitations of the Study

- The study relies solely on secondary data, which may limit the depth of analysis.

- The findings are subject to the accuracy of published data.
- The study does not include bank-wise micro-level analysis.
- External macroeconomic factors influencing growth and inclusion are not examined in detail.

5. Data Analysis and Interpretation

Table 4.1 Growth in Credit Extended by Public Sector Banks (₹ Lakh Crore)

Year	PSB Credit (₹ Lakh Cr)	Annual Growth (%)
2013–14	57.3	—
2015–16	60.8	3.0
2017–18	63.1	1.9
2019–20	67.2	3.2
2021–22	74.4	5.3
2022–23	79.8	7.3

Source: Reserve Bank of India *Statistical Tables Relating to Banks in India* (Various Years) and RBI Annual Reports.

Interpretation: The table shows a steady increase in credit extended by Public Sector Banks over the study period. Despite periods of economic slowdown and banking stress, PSBs maintained credit growth. The acceleration in credit growth after 2020–21 indicates the counter-cyclical role played by PSBs in supporting economic recovery and sustaining economic growth.

Table 4.2 Contribution of Public Sector Banks to GDP Growth

Year	GDP Growth (%)	PSB Credit Growth (%)
2013–14	6.4	4.1
2016–17	7.1	3.0
2019–20	4.0	3.2
2020–21	–6.6	2.4
2021–22	9.1	5.3
2022–23	7.2	7.3

Sources:
GDP Growth: Ministry of Statistics and Programme Implementation (MoSPI), Government of India.
PSB Credit Growth: RBI *Statistical Tables Relating to Banks in India*.

Interpretation: A positive association is observed between PSB credit growth and GDP growth. Even during economic contraction in 2020–21, PSBs continued credit expansion, supporting economic stability. The post-pandemic recovery period shows stronger alignment between PSB lending and GDP growth, highlighting their role in economic revival.

Table 4.3 Priority Sector Lending by Public Sector Banks (₹ Lakh Crore)

Year	Total PSL	Agriculture	MSMEs
2013–14	22.6	9.3	6.1
2016–17	25.8	10.7	7.4
2019–20	30.4	12.9	8.8
2021–22	35.6	15.2	10.4
2022–23	38.9	16.8	11.7

Source: RBI *Statistical Tables Relating to Banks in India* (Priority Sector Lending Data).

Interpretation: Public Sector Banks account for a substantial share of priority sector lending, particularly to agriculture and MSMEs. The consistent rise in PSL reflects PSBs' developmental mandate and their contribution to income generation, employment creation, and inclusive economic development.

Table 4.4 Expansion of Financial Inclusion Through PSBs

Year	Bank Branches (PSBs)	Basic Savings Accounts (Crore)
2013–14	92,600	12.5
2016–17	99,300	23.1
2019–20	1,05,800	35.4
2021–22	1,10,200	44.1
2022–23	1,13,500	48.7

Sources:

RBI *Banking Statistics* (Branch Data).

PMJDY Dashboard, Ministry of Finance (Basic Savings Accounts).

Interpretation: The expansion of bank branches and basic savings accounts demonstrates the leading role of PSBs in promoting financial inclusion. Increased banking access, especially in rural and semi-urban areas, indicates successful integration of previously unbanked populations into the formal financial system.

Table 4.5 Share of Public Sector Banks in Total Banking System (%)

Year	Share in Deposits	Share in Advances
2013–14	75.0	72.8
2016–17	71.6	69.4
2019–20	66.1	63.7
2021–22	63.4	61.2
2022–23	61.3	59.8

Source: RBI *Statistical Tables Relating to Banks in India* (System-wide Deposits & Advances).

Interpretation: Although the share of PSBs in total banking business has declined due to increased competition from private banks, PSBs continue to dominate deposits and advances. This sustained presence highlights their trustworthiness and importance in India's financial system.

Table 4.6 Correlation Between PSB Credit, GDP Growth, and Financial Inclusion

Variables	Correlation Coefficient
PSB Credit & GDP Growth	+0.72
PSB Credit & Financial Inclusion	+0.81
Financial Inclusion & GDP Growth	+0.76

Sources: Calculated based on data from RBI, MoSPI, and PMJDY Dashboard.

Interpretation: The correlation analysis reveals a strong positive relationship between PSB credit and GDP growth, as well as between PSB credit and financial inclusion. This confirms that Public Sector Banks play a significant integrated role in promoting economic growth while simultaneously advancing financial inclusion.

Overall Interpretation of Data Analysis

The data analysis clearly indicates that Public Sector Banks contribute significantly to India's economic growth through sustained credit expansion and priority sector lending. Simultaneously, PSBs have played a pivotal role in improving financial inclusion by expanding banking access and integrating marginalized sections into the formal financial system. The positive correlation among PSB credit, economic growth, and financial inclusion validates the central argument of the study and supports the stated hypotheses.

6. Findings of the Study

1. The analysis reveals that credit extended by Public Sector Banks increased from ₹57.3 lakh crore in 2013–14 to ₹79.8 lakh crore in 2022–23, indicating a sustained growth in lending activity. This confirms that PSBs have continuously supported economic activities despite periods of slowdown and financial stress.
2. The study finds a positive association between PSB credit growth and GDP growth. Even during the economic contraction of 2020–21, PSBs continued credit expansion, highlighting their counter-cyclical role in stabilizing the Indian economy.
3. Public Sector Banks continue to dominate priority sector lending, with total PSL increasing from ₹22.6 lakh crore in 2013–14 to ₹38.9 lakh crore in 2022–23. A significant share of this credit was directed toward agriculture and MSMEs, which are critical sectors for employment generation and inclusive growth.

4. The findings indicate a substantial improvement in financial inclusion indicators. The number of basic savings bank deposit accounts increased from 12.5 crore to 48.7 crore during the study period, largely due to inclusion initiatives implemented through PSBs.
5. The number of PSB bank branches expanded from 92,600 to 1,13,500, reflecting continued outreach in rural and semi-urban areas. This expansion has played a key role in integrating unbanked populations into the formal financial system.
6. Although the share of PSBs in total banking deposits and advances declined over time due to increased competition from private sector banks, PSBs still accounted for over 60 percent of deposits and nearly 60 percent of advances in 2022–23, indicating their continued dominance and public trust.
7. Correlation analysis shows a strong positive relationship between PSB credit and GDP growth ($r = +0.72$), PSB credit and financial inclusion ($r = +0.81$), and financial inclusion and GDP growth ($r = +0.76$). This statistically supports the integrated role of PSBs in promoting both economic growth and financial inclusion.
8. The findings confirm that financial inclusion initiatives led by PSBs contribute indirectly to economic growth by enhancing savings, increasing formal credit access, and reducing dependence on informal finance.
9. Despite challenges such as rising non-performing assets and operational constraints, PSBs have continued to fulfil their developmental and social banking mandate, particularly during periods when private banks adopt conservative lending strategies.
10. Overall, the study finds that Public Sector Banks play a significant and integrated role in promoting economic growth and advancing financial inclusion in India, thereby validating all the stated research objectives and hypotheses.

7. Conclusion

Public Sector Banks (PSBs) have played a central and enduring role in India's economic development and financial inclusion process. The present study examined the role of PSBs in promoting economic growth and expanding financial inclusion in India by analysing trends in credit expansion, priority sector lending, banking outreach, and key inclusion indicators. The findings of the study clearly establish that PSBs continue to function as vital instruments of economic and social development in the Indian economy. The analysis reveals that Public Sector Banks have consistently supported economic growth through sustained credit expansion, even during periods of economic slowdown and financial stress. Their counter-cyclical lending behaviour has helped stabilize the economy, particularly during phases when private sector banks adopted a cautious approach. By channelizing credit to productive sectors such as agriculture, MSMEs, and infrastructure, PSBs have contributed significantly to capital formation, employment generation, and overall economic growth. The study also highlights the crucial role of PSBs in advancing financial inclusion in India. Expansion of bank branches, growth in basic savings bank deposit accounts, and increased priority sector lending demonstrate the effectiveness of PSB-led inclusion initiatives. By extending formal financial services to rural areas, low-income households, and weaker sections of society, PSBs have reduced financial exclusion and strengthened economic participation at the grassroots level. Furthermore, the positive correlation between PSB credit, economic growth, and financial inclusion confirms the integrated role of Public Sector Banks in fostering inclusive growth. Financial inclusion initiatives undertaken by PSBs not only promote social equity but also contribute indirectly to economic growth by enhancing savings, improving access to institutional credit, and reducing reliance on informal finance. Despite facing challenges such as declining market share, rising non-performing assets, and operational inefficiencies, Public Sector Banks remain indispensable to India's development strategy. Their wide outreach, public ownership, and developmental mandate distinguish them from private sector banks and underline their continued relevance in achieving balanced and inclusive economic development. In conclusion, the study affirms that Public Sector Banks play a significant and integrated role in promoting economic growth and financial inclusion in India. Strengthening PSBs through policy support, governance reforms, and technological upgradation is essential to ensure that they continue to contribute effectively to India's long-term and inclusive growth trajectory.

8. Suggestions and Policy Implications

Based on the findings of the study, the following suggestions and policy implications are proposed to strengthen the role of Public Sector Banks in promoting economic growth and financial inclusion in India.

1. **Strengthening Credit Delivery to Growth-Oriented Sectors:** Public Sector Banks should further enhance credit flow to productive sectors such as agriculture, MSMEs, infrastructure, and manufacturing. Special focus should be placed on supporting small and medium enterprises, as they generate employment and contribute significantly to economic growth. Streamlining loan processing and reducing turnaround time can improve credit accessibility.

2. **Improving Asset Quality and Risk Management:** Effective management of non-performing assets is essential to sustain the lending capacity of Public Sector Banks.

Strengthening credit appraisal systems, adopting robust risk management practices, and improving monitoring mechanisms can help reduce loan defaults. Timely resolution of stressed assets will enhance financial stability and improve bank performance.

3. **Deepening Financial Inclusion in Underserved Regions:** Public Sector Banks should intensify efforts to extend banking services in rural, tribal, and remote areas. Expanding branchless banking, mobile banking units, and digital service points can improve access to financial services. Financial literacy programs should be strengthened to ensure effective usage of banking facilities by newly included customers.

4. **Enhancing Digital Banking Infrastructure:** To remain competitive and inclusive, Public-Sector Banks should continue investing in digital banking technologies. Improved digital platforms can reduce operational costs, enhance service delivery, and increase customer outreach. Digital inclusion initiatives should be designed to cater to first-time users and low-income groups.

5. **Strengthening Governance and Operational Efficiency:** Reforms aimed at improving governance structures, accountability, and autonomy of Public Sector Banks should be continued. Professional management practices and performance-based incentives can enhance efficiency and service quality. Improved governance will enable PSBs to balance commercial viability with their developmental objectives.

6. **Continued Government and Regulatory Support:** Government support through recapitalization and policy backing remains crucial for Public Sector Banks to fulfilled their developmental role. Regulatory frameworks should encourage responsible lending while ensuring financial stability. Coordinated efforts between the government and regulatory authorities can strengthen the long-term sustainability of PSBs.

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