CHAPTER-II

REVIEW OF LITERATURE

A number of research studies have been conducted in India on various aspects of priority sector lending by the public sector banks. Some important studies relating to the present topic are reviewed here.

Natrajan (1976)\(^1\) studied the role of commercial banks credit in agricultural development in India. The researcher expressed the view that to channelize the agricultural credit both in terms of adequacy and timeliness, it should be institutionalized. The commercial banks should finance the primary agricultural societies. For increasing the efficiency of farmers, appropriate amount of credit should be available at the right time.

Ghiara (1977)\(^2\) analyzed regional distribution of direct agricultural finance by scheduled commercial banks in India. It was observed that there has been no major shift in the share of states falling in the Northern, North-eastern and the central regions. This has not been achieved by any pruning of the relative share of Southern region, which in fact has increased.

An attempt to examine the role of commercial and co-operative banks in context of rural development was made by Datar (1978).\(^3\) The analysis revealed that if occupation-wise distribution of bank credit and regional advance deposits ratio were considered, the shift was in favour of small industries, agriculture sector and towards more regional distribution of advances. He was of the view that even if credit-deposit ratio was brought to near equality in different regions, it was not going to meet the credit needs of the rural areas.

Basu (1979)\(^4\) evaluated the regional pattern of distribution of the scheduled commercial bank’s credit to agriculture and allied activities excluding plantation in India. The analysis revealed that though the share of agricultural credit in scheduled commercial banks credit has increased, yet these have failed to maintain a minimum degree of uniformity in regional distribution. The influence of the spread of bank offices in augmenting the flow of agricultural credit from commercial banks was doubtful. The farmers with huge land assets influence the flow of agricultural credit from the commercial banks. It was observed that the level of agricultural credit per hectare of net sown area, number of bank offices per lakh of population, per capita bank deposits, degree of urbanization and intensity of cultivation are the significant determinants of level of agricultural credit.

Chawla (1979)\(^5\) highlighted the achievement of priority sector lendings in quantitative terms during the decade of 1960. However, at the same time it is also observed that within the priority sector, it is relatively the well-off, who got the maximum benefit and the poorest of the poor have remained credit starved. Thus there is a need for laying down the priorities in such a manner that the poorest of the poor are benefited.

Pranav (1979)\(^6\) has examined the role of commercial banks in rural development. He is of the view that after nationalization, banking in India has successfully transformed itself from elite banking to that of mass banking. There is also a shift towards the small farmers in agricultural financing. But, the task of lending for rural development is very complex and challenging. It can’t be fulfilled without changing the attitude of bank people, who are to extent passive.

Rawat (1980)\(^7\) identified the problems faced by the commercial banks in the disbursal of credit to agricultural sector in India. The inadequate co-ordination among various types of institutions, lack of systematic and up to date land records and absence of suitable marketing outlets assuring fair prices for agricultural products etc. were some

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of the important problems faced by the commercial banks in financing agriculture in India. The researcher suggested that in order to ensure adequate credit to the agricultural sector, government should take steps to solve these problems.

Sharda (1980) reviewed agricultural financing by the commercial banks. Though, agriculture advances have increased substantially over a period of time, yet the attitude of banks towards agricultural financing is not as per expectations. He is of the view that subsidy provided in some areas by the government will help the small farmers to derive advantages of modern agricultural technology.

Patel and Shete (1981) analyzed the developmental role of commercial banks in financing priority sectors, mainly agriculture. The researcher is of the view that before 1969, the role of commercial banks in agriculture credit was almost negligible. But, with change in time, the government has directed the commercial banks to take active part in agricultural financing. It was concluded that priority sector advances by the commercial banks give a mixed feeling of success and failure.

Sundarm (1981) took up the issue of different problems faced in context to priority sector lendings. One of the neglected area in priority sector lendings i.e. consumption credit was analyzed in great details. The problems of the borrowers not being able to use credit productively is another major issue in priority sector lendings. The strengthening of the institutional framework coupled with proper credit supervision and availability of required manpower were emphasized.

Angadi (1983) highlighted the extent of concentration of priority sector advances in general and agricultural advances in particular, in some selected states of India. A multiple regression technique, based on ordinary least square method was employed to assess the extent of the impact of explanatory variables on agricultural advances. The study revealed that the degree of concentration of priority sector advances and

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agricultural advances in the selected states was less in 1979 as compared to the year 1969-70.

Sablok and Sablok (1984)\(^\text{12}\) in their paper reviewed the financing of agriculture by commercial banks with special reference to innovations. It was emphasized that infrastructural facilities should be provided by the government and the banks must reach the smallest of the farmers to solve their credit problems. The banks should expand their advances in the rural sector so that the process of transformation of traditional agriculture into commercial agriculture may become possible.

Oka (1985)\(^\text{13}\) studied the trend in growth and composition of commercial bank’s agricultural advances in India during the years 1969 to 1981. It was observed that the commercial banks witnessed a phenomenal progress in lending to agriculture sector, especially by way of direct finance. The combined share of marginal and small farmers in total agricultural finance went up subsequently during the reference period. But, the overall recovery of agricultural lending was found to be very poor. Further, there persisted very wide inter-regional and inter-sectoral disparities in the distributional pattern of agricultural credit.

Gadgil (1986)\(^\text{14}\) found that since the adoption of multi-agency approach in the late sixties, agricultural credit supply in India has expanded rapidly, both in nominal and real terms. He was of the view that the basic problem is not one of the expansions in the value of credit, but, what is important is the more effective management of the credit. Since agricultural development is basically related to the adoption of an improved technology, credit without a link with improved technical skills is not likely to be productive.

John and Singh (1986)\(^\text{15}\) analyzed the priority sector lendings and its impact on rural development in Kanyakumari district of Tamil Nadu. The analysis relates to the year 1983. It was observed that banks in Kanyakumari district have achieved their targets,


\(^{15}\) John and Singh, (1986); *the Bank Nationalization- Causes and the Constitution*, NM Tripathy Pvt. Ltd. Publication.
but, the pertinent question is at what cost? To make the system of priority sector lending more efficient the banks should constitute different priorities for different districts and similarly for different states also. The priorities in a particular area can be totally different from generally fixed for the banks as a whole.

Kumar et. al., (1987)\(^\text{16}\) in their paper analyzed the growth and disparity in agricultural advances by the commercial banks during the post nationalization period. The extent of disparities between the states has been examined by computing the “Gini Concentration Ratio”. Study shows that the disparity in distribution of bank advances among the states has declined over the period under study.

SBI (1987)\(^\text{17}\) studied the impact of bank credit on weaker sections, financed under Differential rate of Interest (DRI) scheme in Kerala. It was observed that the utilization of bank loans in general raised the income and employment of the borrowers and their quality of life to help them to come out of poverty.

Balister (1989)\(^\text{18}\) critically analyzed the problem of non-repayment of agricultural loans taken from the commercial banks. Twenty three defaulters from Mursan Block and thirty two from Jalsar Block of Agra Division in Uttar Pradesh were selected. It was concluded that the farmers with repayment capacity were defaulters due to slackness on the part of banks to insist on timely recovery of loans. The farmers with non-repayment capacity were defaulters due to low crop yield and crop failure in both the blocks. This problem was found to be more serious in agriculturally backward blocks. It was suggested that the repayment period of loans should be extended. Adequate loans should be provided in time and crop insurance facility should be available to enhance the repayment capacity of the farmers.

Bhuleskar (1989)\(^\text{19}\) observed that the present deterioration in the quality of priority sector lendings is caused by various factors like non-simplification of credit norms,

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\(^\text{19}\) A.V. Bhuleskar, (1989); *Structural Changes and Issues of Indian Economy, Bank Lending to Priority Sectors-Need for Effectiveness*, December, 1989, pp. 115-122.
confusion in the definition of weaker sections, lack of infrastructure and above all non-consideration of linkages due to total absence of co-ordination of schemes at the formulation as well as at the implementation level. Obstacles faced in the recovery of loans have resulted into high over dues, and thus, has affected the recycling of funds in agriculture and other priority sectors of the economy. Indiscriminate lending to priority sector by the government through banking sector has further led to unproductive investment in priority sector. Apart from this the resentment in lending to small and marginal farmers coupled with non-adherence to economic and technical norms in credit deployment led to poor quality of priority sector lending by the commercial banks.

Joshi (1989) discussed the desired norms and techniques to study the performance of the public sector banks. Prior to nationalization, profit was the sole criterion for evaluating the performance of public sector banks. After nationalization, profitability and social banking became the major objectives of public sector banks and thus any evaluation of banks performance has to be in relation to these goals.

Rao and Chandershekhar (1990) in their study of priority sector lendings by the commercial banks in Haryana in particular and India in general observed that, the commercial banks lay emphasis on security lending in place of development lending. It was observed that the nationalized banks have failed in their primary responsibility of meeting the credit needs of rural and priority sectors both in the state as well as at the country level during the period from 1970 to 1980. However, the performance with respect to financing of weaker sections viz. scheduled caste and scheduled tribes at the state level was found to be better than at the All India Level.

The Narasimhan Committee (1991) highlighted the problems of low and declining profitability of the public sector banks and emphasized over the gradual phasing out of directed credit programmes. The Committee emphasized that the priority sector

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21 Rao and Chandeshekhar, (1990); The Priority Sector lendings by Commercial Banks, Paper presented at the Third All India Conference on Institutional Changes in Agriculture and Regional development.

should be redefined and the proportion of credit flowing under this should be fixed at 10 per cent of net bank credit (NBC).

Anand (1992) calculated the economics of priority sector lending and in view of that, looked into the question that whether these advances are the main cause of low profitability of banks or not?. He concluded that fixation of concessional rates at very low levels is not advisable as this often leads to the diversion of loans away from agriculture and also causes inflation. However, the analysis revealed that priority sector lending is not a drag on profitability.

Khusro Committee (1993) recommended that the DRI scheme should continue to support the national plans for agricultural development. It was also of the opinion that the human resource development should be emphasized for improving the quality of agricultural credit system. It laid stress over the pre-lending appraisal and strict monitoring of loans and recoveries. The Committee was of the view that the norms and procedures related to rural lending should be reviewed and simplified. The Committee also suggested that information system should be improved in the banks. The crop insurance scheme should be started and a separate credit guarantee scheme should be formulated. It further recommended that the schemes, which are created for meeting the rural credit, such as IRDP etc. should be thoroughly reviewed.

Patel and Khankhoje (1993) in their study discussed basic issues pertaining to rural banking in context to the financial sector reforms. It was observed that the operation of National Co-operative Bank of India (NCBI) could have perceptible repercussions on the operation of the commercial banks in the rural sector. It was concluded that closure of rural branches was not a viable solution while thinking about restructuring of rural banks. The issues concerning rural banking basically emerge from the fact that its futuristic role is both indispensable and challenging. Hence, clarity and broad consensus on certain aspects of the role and functioning of rural banking becomes essential.

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Ramanujam’s (1993)\(^{26}\) study shows that only less than 25 per cent of the people in a village are served by a commercial bank branch, and he holds the view that measures should be taken to bring more beneficiaries in the fold. For this purpose, the dimension of priority sector lendings and rural financing needs to be changed. He holds that in the present Indian context, commercial banks perhaps may be the only viable agency to extend financial assistance to priority sector and rural development. This is due to their enormous number of branches, huge financial base, professional competence, technical excellence and self-sustained character which the other agencies lack generally. However, more beneficiaries need to be brought under their services.

Balishter and Kumar (1994)\(^{27}\) examined the extent of credit available to different categories of farmers from institutional and non-institutional sources. The study indicated that in areas where commercial banks have extended their operations, these constitute the major source of financing agriculture particularly, marginal and small farmers. The share of co-operative societies is larger in the case of medium and large farmers. It was observed that the co-operative societies still continue to be conservative and security oriented in their loaning operations. The system of directed credit programmes has contributed to an expansion of credit in favour of the weaker sections of the rural society and thus fulfilling the social objectives. There is an immediate need to take appropriate measures to reduce the incidence of overdue to make funds available for the needy farmers and agricultural development.

Mujumdar (1995)\(^{28}\) is of the view that the neglect of priority sector at macro-level was compounded at micro-level, by the new bank culture, which sought to focus on credit to consumer durables, to corporate elite and to capital market related activities. Even public sector banks in India were swept off their feet by the inundating U.S. banking culture which places emphasis on a ‘quick kill’ rather than on the growth potentials.


The study made by Srinivasan (1995)\textsuperscript{29} highlighted the achievements of the banks in securing the desired allocation pattern of credit in different sectors and sub-sectors during the period 1969 to 1989. He derived home the point that the burden of the priority sector lending is borne mainly by the public sector banks and other institutional agencies. It was observed that the regional rural banks and co-operatives have not played their due role owing to certain structural deficiencies in their working. The study revealed that there was a fall in spatial and sectoral imbalances in banking operations over a period.

Patel (1996)\textsuperscript{30} is of the view that the traditional banking ethics were not compatible with the needs of economic development. The balanced development was not possible without strengthening the commercial banks in the backward and neglected areas. With a view to bring the down-trodden, hitherto neglected sectors/households to the mainstream, fundamental changes in the traditional banking norms were called for to move away from security based credit towards programme oriented credit.

Singh (1996)\textsuperscript{31} deals with the problem of non-performing assets (NPAs) faced by the banks in India. He highlighted that the priority sector lending has a higher incidence of non-performing assets. The restrictions imposed on the banks to choose their debtor has led to the problems of NPAs in banks. The removal of political and beaurocratic control and privatization can help in tackling the problem of non-performing assets.

Agarwal, et. al., (1997)\textsuperscript{32} reviewed the structure, performance and problems of rural credit on account of financial sector reforms in the country particularly in context to the agriculture sector. It was observed that on account of market oriented economy and capital intensive technology, the demand of credit for agriculture and rural development will increase sharply in the coming years. It may be practical for the commercial banks, in particular, to aim at a narrow business base leaving the vast rural sector neglected. It would be risky if the banks deploy their lendable resources in

speculative financial activities. It was concluded that there existed a large gap between the demand for and supply of agricultural credit.

Kohli (1997) reviewed both the theory and empirical evidence on directed credit programmes with respect to small scale enterprises in the Indian context. He made a comparison between implementation of such programmes in East Asia and India. The cost and benefits of priority sector lending in India was calculated and was argued that the credit policy needs to be re-appraised and should be geared up towards more specific objectives. These objectives should be defined locally so that on the basis where of the banks are able to decide as to which firms or industries are to be financed. In addition, the researcher suggested for an introduction of the system of periodic review of targeted firms and industries. He argued for designing a sharply focused credit policy with incentives structured to reduce moral hazard and ensure good performance.

Mohanti (1997) while discussing the new set of guidelines for the banks observed that these have been encouraging the banks to move away from lending directly to priority sectors. The banks are unable to fulfill the priority sector credit target not because they do not find enough opportunities, but, it is so because some of these are not interested in funding the need of priority sector. By not lending to priority sector the banks are able to avoid the problem of follow up, maintenance of accounts and the problem of non-performing assets.

Sooden (1997) studied the extent of regional disparities in commercial banks during the years 1975 to 1996. Six indicators of banking development were selected and ultimately with the help of Principal Component Analysis, indices of banking development for 21 states of India were framed. Analysis of deposits, credit and branches pointed out that they registered higher growth rates in the first half of the study (1975-1985) than the later half. Similarly, the objective of regional disparities was also achieved in a more desirable manner during the period 1975 to 1985 than during the years 1986 to 1996.

34 S. Mohanti, (1997); “Banks Parking Funds with SIDBI and NABARD”, the Economic Times, Nov. 6.
Gupta Committee (1998)\(^{36}\) attacked priority sector and recommended for doing away with the target of agricultural lending. It recommended for allowing the commercial banks to freely fix rate of interest for loans of all amounts. It argued for doing away with the subsidy on agricultural loans.

According to Mujumdar (1998)\(^{37}\) since priority sector are critical to high and sustained growth of GDP it should be the business of public sector banks to support these sectors irrespective of whether there are credit targets or not. It is emphasized that the credit policy needs to be reoriented so as to reverse the neglect of priority sector in the recent past. It was observed that small borrowers appeared to be subsidizing the large borrowers during the reform period. The new interest rate structure has become highly regressive and unfriendly to priority sector.

Mujumdar (1998)\(^{38}\) observed that 1990's was a lost decade for the rural credit and agricultural sector. In the waves of liberalization and globalization, the glamorous sectors of the economy like foreign direct investment and capital related activities became the focus of attention of both the policy makers and the RBI, with the result that agriculture became the last choice of policy makers.

Narasimhan (1998)\(^{39}\) in context to financial sector reforms observed that in the priority sector lending, the phenomenal increase in borrower accounts indicate that the systems of directed credit programme clearly contributed to an expansion of credit in the direction that was considered necessary. It was observed that during the reform period, the average size of account has come down sharply indicating that the banking credit system is reaching down to small borrowers.

Narasimhan Committee (1998)\(^{40}\) acknowledged the political compulsion faced by the Government of India with respect to priority sector lending but persisted that this sector must be brought down to just 10 per cent of net bank credit (NBC). It

recommended that given the special needs of weaker sections the current practice of providing 10 per cent of credit to weaker sections must continue. As for the rest, it opposed any directive to meet specific quantitative targets. It also recommended that the definition of priority sector be expanded. The sectors like food processing and related service activities in agriculture, fisheries, poultry and dairy should also be covered under the scope of priority sector lendings.

Shajahan (1998) raised issues relating to priority sector advances by the commercial banks in India in context to changed economic set up. It was observed that financial liberalization has a negative impact on lending to priority sector by the commercial banks. The drop in overall priority sector advances in the year 1996 over the year 1991 has no doubt come about alongside the decline in overall deposit ratio of the banks. But, what is more disturbing is that the percentage share of poor states in the priority sector credit has fallen further. This is on account of the manner in which priority sector lendings is done by linking it to bank credit rather than total deposits mobilized. The system of targeting has led to regressive outcomes. The continuation of policy of targeting priority sector credit was emphasized.

Bhatia and Verma (1998-99) observed that priority sector advances influence negatively the profitability of public sector banks. The profitability of public sector banks depends both on exogenous, i.e. policy determined variables such as reserve requirement, directed credit programmes; and on endogenous variables such as composition of deposits, establishment expenses, spread and burden etc. The need of curtailing priority sector advances was emphasized.

Ramesha (1998-99) observed that there have been substantial variations across states in the distribution of scheduled commercial banks credit to the small scale industries sector. It is disturbing to observe that the inter-state variations with respect to scheduled commercial banks credit to SSIs has widened between 1989-90 and 1995-96. The ratio of credit to output indicates that the states of Madhya Pradesh,

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Bihar and Orissa are extremely credit deficit states. Contrary, Jammu & Kashmir, Maharashtra, Kerala, West Bengal, Karnataka and Punjab received scheduled commercial banks credit in excess of their respective contribution to the total SSI output. It was found that high credit states also happened to be highly developed states in regard to the SSI sector and vice-versa. The study suggested that redistribution/opening of specialized branches in credit deficit states with a special thrust on financing micro-enterprises would ensure increased flow of credit to this sector. However, in the long run the flow of credit is critically dependent on availability of infrastructure and support services to SSIs.

Ambumani and Niranjana (1999)\textsuperscript{44} analyzed priority sector lending in context to achievement of social objectives by the public sector banks during the year 1992-1993. Mean lending rates, interest subsidy rates and consequent income loss was calculated with the help of formula developed by T.N. Bishnoi in 1991. The study supported the hypothesis that priority sector policy has been responsible for low profitability of public sector banks. After liberalization, proportion of credit flowing to each earmarked sector has declined except export sector. It was argued that the reduction of priority sector advances will in no way affect either the output of agriculture or small scale industries.

Kohli (1999)\textsuperscript{45} while evaluating the effectiveness of bank branch licensing policy in the background of financial sector reforms observed that in view of changed banking perspective in India, performance evaluation parameters have changed. Earlier performance indicators like, deposits, priority sector lending and branch expansion, have yielded to new ones i.e. efficiency and profitability. It was observed that the Indonesian Bank Rakyat could be accepted as a model relevant for rural branches of public sector banks in India. It was suggested that a strategy of either a closure of public sector banks or gradual substitution by private sector banks should be adopted in order to make the rural banking more viable.

\textsuperscript{44} V. Ambumani and S. Niranjana, (1999); ‘The Indian Economic Association’, 82\textsuperscript{nd} Conference, Vol. 2000.

Puhazhendi and Jayaraman (1999)\(^{46}\) in their paper reviewed the performance of rural credit delivery system in three focused areas viz. agriculture and non-agriculture sector and poverty alleviation. The challenges that the commercial banks are likely to encounter in the next decade are also discussed. The analysis revealed that though rural credit has increased very rapidly in the country, yet the declining trend registered in priority sector advances, especially agricultural loans, is going to have serious repercussion on the economy.

As per RBI bulletin (1999)\(^{47}\) the target of 40 per cent of net bank credit to priority sector has led to high level of non-performing assets (NPAs). It is so because credit to these sectors is quite sticky. The higher proportion of non-performing assets in priority sector advances was attributed to the directed and pre-approved nature of any security, lack of effective follow-up and due to large number of accounts etc.

Shajahan (1999)\(^{48}\) raised the issues of rationalizing priority sector lending in the Indian context. The study covers the time period from 1995 to 1999. It was observed that, though the percentage of priority sector lending by the public sector banks has surpassed the stipulated target of 40 per cent to total advances in the year 1999 itself, yet, it has possibly not, resulted in the required amount of credit being actually channelized to areas considered to comprise priority sector of the economy. The high ratio achieved was possibly the result of widening of the scope of priority sector lending which allowed the banks to part funds from areas originally considered as constituting the priority sector. It was observed further that the decline in priority sector NPAs have pushed down the total NPAs of the banks.

Tara (2000)\(^{49}\) found that the commercial banks have weakened considerably during the decade of 1980s and 1990s. There has been a deceleration in the growth of commercial bank credit to rural areas, in terms of both disbursal and outstanding. Also notable is the relative fall in the proportion of bank credit flowing to the priority

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sector, particularly agriculture, since the mid 1980s. The movement of the credit-deposit ratio in rural areas further reinforced the above trend. During the period 1970s to 1980s, the credit-deposit ratios in rural areas increased steadily. However, this trend reversed and by the end of 1990s reached what it was in the early 1970s.

The objective of the study made by Dass (2001) was to evaluate the performance of public sector banks with respect to priority sector lending and expansion of banking services to the unbanked areas during the pre and post-reform period. It was observed that the percentage share of priority sector in total bank credit has been increasing but, at a decreasing rate in the post-reform period as compared to pre-reform one. It is concluded that the impact of financial sector reforms on regional equalities and the priority sector lending has been much averse.

Jayabal (2001) observed that priority sector and weaker sections lending have enabled the borrowers to undertake self-employment ventures or to acquire income generating capital assets to improve their standard of living. These directed credit programmes have helped in raising the income of the target group.

Rangaswamy and Ramnath (2001) analyzed the performance of public sector banks, private sector banks, and some other agencies such as Tamil Nadu Industrial Corporation Limited, Madurai District Central Co-operative Bank etc. in priority sector lending in Madurai district of Tamil Nadu. Krushkal-Wallis test was applied to carry the analysis. It was observed that the performance of different agencies differ significantly with respect of overall and priority sector lending in the district.

RBI (2001) in its report admitted that there has been a deceleration in the growth of loans outstanding for small and marginal farmers during the decade of 1990's as compared to that of 80's. The deceleration in credit disbursal to small/marginal farmers has been highest during the decade of 1990's. Thus, these categories of farmers continue to be both credit and demand constrained. It was observed that size

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and flow of financial resources to agriculture, both in terms of investment and working capital have shrunk significantly.

Reddy (2001)\textsuperscript{54} observed that due to accumulation of losses on account of monitoring NPAs, the flow of credit of public sector banks to rural areas has not been up to the mark in the recent years. He further noted that, there are some commercial banks that have failed to reach the prescribed target of lending to agriculture, even after accounting for allocation to Rural Infrastructure Development Fund (RIDF). During the reform era, public investment in agriculture has slackened and banks have partially failed to serve this purpose fully. The researcher pointed out that inadequate finance and outdated banking practices are the major reasons of their poor performance. It was recommended that the institutional reforms are needed immediately, requiring changes in the mindset and redefining the role of government.

Vyas committee (2001)\textsuperscript{55} observed that commercial Banks seem to be reluctant in extending rural credit as they are dealing vast number of small accounts. The Committee recommended that the mandated rates of 18 per cent of credit outstanding for agricultural loans and 40 per cent for priority sector loans should be reviewed after five years. It also recommended a substantial reduction in (Rural Infrastructure and Development Fund) RIDF interest rates to cover the interest cost of deposits. The committee suggested retaining the upper limit of 4.5 per cent on indirect credit while reckoning the achievement of 18 per cent target for agricultural lending.

Bhide and Ghosh (2002)\textsuperscript{56} made a critical analysis of banking sector reforms and highlighted some of the weaknesses of the system. The issue of direct lending was observed to be a major area of concern. The direct agricultural lending of public sector banks also shows a declining trend. The story of regional rural banks also points out the same picture. Decline in the flow of funds to agriculture appears to have affected the growth of gross capital formation in agriculture sector during the post-reform period.

\textsuperscript{55} Report of the Expert Committee on Rural Credit (V.S. Vyas Committee), 2001, NABARD, Mumbai, November 12.
Dasgupta (2002)\(^{57}\) observed that the priority sector credit in the present context lacks a proper focus and rationality. In the pre-reform period, there was to some extent an emphasis on weaker sections and neglected sectors of the economy. But, in the post-reform period there appears to be a basic shift in banks approach towards lending to priority sector. The commercial banks have become a medium to please politicians and vocal segments of the community. RBI policies have failed to protect the interest of small and marginal farmers, rural artisans and weaker sections of the economy. A mandatory credit for agriculture and allied activities, to small and marginal farmers, to small trade and services and to cottage and tiny industries was emphasized.

Jha (2002)\(^{58}\) evaluated the role of commercial banks in providing credit to priority sector in the Mithilia region in particular and in India in general during the year 1994-95. It was observed that the contribution of commercial banks in lending to the weaker sections in Maithili region in Bihar and in India, in general is praiseworthy. Proper utilization of priority sector lendings can help in the development of weaker sections on the condition that the administration, the bank authorities and general public offer a helping hand in the attainment of different earmarked objectives.

Shete (2002)\(^{59}\) observes that there is a growing feeling that the process of financial sector reforms has by passed the agriculture sector in general and weaker sections in particular. He found that lendings to priority sector by banks, both in terms of amount and the number of borrowers does give an impression that flow of credit to this sector has come down substantially despite expansion of scope/area of priority sector definition. A large number of public sector banks are not able to reach the prescribed targets of lendings to agriculture and weaker sections. The small and marginal farmers have continued to be credit starved. Priority sector/ agriculture finance at present is thus at crossroads.


\(^{58}\) J.T. Kant, (2002); Banking and Financial Sector Reforms in India, “Priority Sector Lending - a Case Study in Maithili Region in Madurai (Bihar)”, 2002, pp. 264-281.

\(^{59}\) N.B. Shete, (2002-03); “Priority Sector advances of Banks during the Post-Reform Period”, Prajin, Vol. XXXI, No. 1, pp. 21-37.
Chandak (2003)\textsuperscript{60} observed that the growth in credit is a necessary condition for steady and all-round economic growth. Adequate liquidity, depth and resiliency of the financial system are essential for this. Deployment of bank credit involves complex regulatory framework, structural rigidities, delays and higher transaction cost, especially for small businesses. Many business entities are tempted to shift a part or whole of their business activities into informal sector which is facilitated by finance and trade credit which are more compatible with the needs of business. An efficient and effective trade credit system ensures the success of the financial system.

Kapoor (2004)\textsuperscript{61} observed that priority sector lending as such registered a lower rate of growth in the post-reform period, yet when explained in terms of branches, it registered higher rate of growth in the second half of the study. However, the falling rate of priority sector advances to total advances is a serious matter of concern for the policy makers. The banks in their enthusiasm to achieve the economic goals in the post-reform period seem to have forgotten their social objectives. It was suggested that there has to be a proper balanced co-ordination between economic and social goals. If priority sector advances are not given proper attention this may have a negative cumulative effect on the whole economy and the process of development.

Sabnani (2004)\textsuperscript{62} acknowledged that retail trade and housing loans have contributed significantly in the growth of overall advances of commercial banks in the recent years. However, in order to be able to cater to the growing needs of the retail customers and housing loans, commercial banks need to look into the diversified aspects of the retail trade banking. It is high time that the banks seriously take up the issue like proper required framework for managing credit. They have to evolve ways to reduce operational risk and improve the supervision and monitoring framework. Intensive competition in the retail market also calls for appropriate strategies on the part of the banks to retain/increase the market share.

\textsuperscript{60} B.L. Chandak, (2003); "Trade Credit and Industrial Slowdown", Vinimaya, \textit{NIBM Publication}, Vol. XXIX, No.1, April-June.
Ahmed (2005)\(^{63}\) found that the commercial banks together have gradually increased the quantum of advances to small scale industries. However, the relative share of small sector has not grown in proportion to increase in priority sector lending during the reform regime. The weak infrastructure facilities may have prevented the greater flow of credit to small scale industries. It was suggested that the industrial campaign, awareness programmes and industrial training to the prospective entrepreneurs by the appropriate authority may be useful in this regard.

Chandak (2005)\(^{64}\) observed that the slowdown in the growth of institutional credit to small scale industries may be attributed to the financial vulnerability of trade and industry, which together resulted in higher levels of NPAs. At the same time, no attempts have been made to examine the non-institutional credit sources to SSIs. Given the complementarities between institutional and non-institutional credit, measures to increase the supply of the former without addressing the systemic fragility of the latter will be short-lived. He found that the success of the economy and especially industrial sector can be better ensured through a confident, reliable and efficient financial system in which both institutional and non-institutional credit sources can play mutually supportive roles.

The internal working group of RBI (2005)\(^{65}\) identified the issues relating to priority sector lending by the public sector banks. The group recommended the need for priority sector lending targets, its composition in terms of agriculture, small scale industries, small road and water transport operators, small business, professional and self-employed persons, and education and housing loans. The existing system of computation of priority sector obligations in relation to net bank credit (NBC) is based on the outstanding advances of banks. Linking the priority sector obligations to outstanding advances has its shortcomings. Outstanding tend to decline as a result of better recovery and write-offs. In order to improve the flow of credit to this, the computation of priority sector lending obligations should be linked to the total disbursements made by the banks during the previous year.

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\(^{65}\) RBI Internal Working Group, (2005); *Priority Sector Lending*. Rural Planning and Credit Department Central Office, RBI, Mumbai, September.
Satish (2005)\textsuperscript{66} highlighted that there are two classes of borrowers in agricultural credit. One class, which have smaller land holding, lesser capital equipment and are at a lower end of economic prosperity. The other class which emerges as the capitalist farmer who takes up farming on a commercial basis and has large holdings and higher amount of capital equipment. To assess the credit needs of these two types of borrowers, regression model with dummy variables was used for analyzing the differences in characteristics among the commercial banks and co-operative bank borrowers. It was observed that the commercial banks should be the preferred institution for the second category of borrowers while, the co-operatives with their less formal and more user friendly system can serve the small borrower. It was suggested that the co-operative banking and commercial banking system should tune their lending practices to suit these characteristics.

Sahu et. al. (2005)\textsuperscript{67} studied the trends in credit to agriculture by the commercial banks during the period 1981 to 2000. It was found that the share of credit to agriculture in net bank credit has significantly declined, particularly after the introduction of banking sector reforms. Across bank groups, a similar decline was observed. It was also observed that the share of those farmers, borrowing less than Rs. 25,000, declined in both the total number of loan accounts and total loan amount during the reform period. Banks have failed to lend to the activities having high social return. Banks have also failed to lend to the creditworthy borrowers who had been traditionally marginalized in the credit market.

Sunanda, et. al. (2005)\textsuperscript{68} observed that the percentage share of loans to the small scale industrial sector in total priority sector lending has squeezed during the post reform period. One possible reason for this may be the fact that the loans to the 'other priority sectors' witnessed a sheer jump with the introduction of financial sector reforms. It was found that the NPAs of the priority sector lending by the public sector banks as a whole have been much higher as compared to non priority public lending. NPAs, recorded for the SSI sector, which have been the highest of all priority sector

\textsuperscript{67} G.B. Sahu and D. Rajashekar, (2005); “Banking Sector Reforms and Credit Flow to Indian Agriculture”, Economic and Political Weekly, Jan. 8.
\textsuperscript{68} S. Sunanda and G. K. Soumya, (2005); “Basel Norms, Indian Banking Sector and Impact of Credit on SMEs and the Poor”, Economic and Political Weekly, March 19, pp. 1167-1180.
credits, are observed to be declining for both public and private sector banks, over the years.

Kaveri and Kulkarni (2005-06) observed that it is disheartening to note that the share of small scale industries credit has declined and this calls for a detailed introspection. Along with contraction of credit, delays in sanction and disbursement have further eroded the quality of credit. Whereas, on the one hand the commercial banks are providing limited range of services, on the other, the needs of the SSI sector have increased. There is a need to increase credit supply to this sector. It is important that various credit policies, systems and procedures should be more effective and forceful in this regard. Above all, the outlook of bankers and borrowers needs an orientation.

Arabi (2006) examined the role of bank credit in the economic development and that how it is channeled to the different sectors in India in the recent years. It is observed that although the importance of bank credit in the conduct of monetary policy waned in some advanced economies during the 1970s and 1980s, subsequent developments have led to a renewed focus on the behavior of credit conditions and credit aggregates. His research is an outcome of an attempt to understand the effective performances of credit delivered to different development sectors which is based on secondary data. The research paper also deliberated the analysis on the bank credit to the various sectors like, agriculture, small scale industries (SSIs), micro finance, housing finance and infrastructure lending. It was observed that there is the need to make and further liberalize the interest rate structures to ensure efficiency in financing the credit to core sectors which in turn will contribute for growth in India.

Karmakar (2006) observed that farming is a risky proposition and even more so for the small/marginal farmers whose average landholding is increasingly being fragmented. Farmers constitute the largest private sector in the land but lack credit access, market access, insurance, infrastructure, quality inputs, storage and extension services. The institutional credit system has been unable to edge out the ubiquitous

moneylender who provides a range of services for a very high fee. Various innovations in rural credit delivery like self help groups (SHGs)/ joint liability groups (JLGs)/ Kisan credit card (KCC) have been able to provide some financial services to very poor rural people, especially women. For providing effective delivery of deposits, credit and insurance products to small/marginal farmers, innovations are required in banking operations. Micro-finance agencies proliferate where the rural banking system is already strong. However, it is not the case in the eastern/north-eastern areas where the banking network is weak.

Sidhu and Gill (2006)\textsuperscript{72} found that despite significant growth in agricultural advances, much more is expected from the commercial banks. Further, there are wide variations in the availability of institutional credit per hectare of gross cropped area in different states. Poor availability of credit is adversely affecting the adoption of modern technology and private capital investment, which in turn lowers the productivity and production and also pushes the farmers to borrow from non-institutional sources.

Mohan (2006)\textsuperscript{73} observed that per capita extension of agricultural credit by the commercial banks in the eastern and north-eastern regions is extremely low. The researcher pointed out that why do public sector bank with similar management and staff, behave so differently across different regions? If it is possible for banks to do direct lending to agriculture sector in the southern states, why not in the other regions? It was also found that the proportions of NPAs are indeed higher for agriculture than they are for the non-priority sector; however they are not as high as those for small-scale industries and for other priority sectors.

Roy (2006)\textsuperscript{74} found that during the years 1996-97 to 2004-05, the share of priority sector lending by the public sector banks continued to hover at around 32 to 33 per cent of net bank credit. Within the priority sector, the share of credit to small scale industries has declined secularly during the period under review, while that of agriculture has continued to be almost stagnant. The share of credit to 'other priority

\textsuperscript{72} R.S. Sidhu and S.S. Gill, (2006); “Agricultural Credit and Indebtness in India: Some Issues”, \textit{Indian Journal of Agricultural Economics}, Vol. 61, No.1, Jan.-March, pp. 11-35.


\textsuperscript{74} M. Roy, (2006); “A Review of Bank Lending to Priority and Retail Sectors”, \textit{Economic and Political Weekly}, Vol. XLI, No. 11, March 18, pp. 1035-1040.
sectors’, on the other, has shown a sharp and secular increase during the same period, offsetting the decline in credit to SSI sector. The average growth in credit to ‘other priority sectors’ has been very high during the period under study, mainly on account of a sharp growth in credit to retail trade and housing loans.

Thorat (2006)\(^{75}\) found that the commercial banks are more focused on profitability and thus give less priority to marginal and sub-marginal farmers. Rural credit in general and agricultural credit in particular faces the problem of inadequacy. Further, constraints on timely availability of credit, high interest rates, neglect of small and marginal farmers, low credit-deposit ratio in several states and continued presence of informal markets make the scenario of agricultural financing all the more worst. Competition and search for higher returns are deriving commercial banks’ to look for profitable avenues and activities like contract farming, extending credit to value chain and financing traders.

Biswa (2007)\(^{76}\) maintains that though the performance of small scale industries has been commendable, yet, the flow of institutional credit, particularly that of public sector bank continues to be a major area of concern. The public sector banks and others concerned must remember that made-to-fit all enterprises types of solutions are not going to be effective enough with respect to small scale industrial sector. Apart from learning lessons from their own successful experiences in supporting SSIs, banks must play the role of ‘banking partner’ in extending credit support to SSIs. Towards this end, what is needed is a change in the mind-set of bankers.

Das Gupta et. al. (2007)\(^{77}\) found that the commercial banks had huge problems in the beginning of the reform period in maintaining the ratio of 18 per cent of net bank credit to be deployed in agriculture sector. During the reform period, the flow of commercial banks credit to agriculture sector declined because the formal sector had not reached out to the small and marginal farmers. The credit needs of other farmers have declined because there were not many incentives to make more investment in agriculture sector. To increase the quantum of credit to agriculture sector, it was


suggested that the commercial banks should respect market principles, take
cognizance of the fact that for a huge segment of population, agriculture sector is the
only source of income and realize that agricultural production is a highly risky
business, yet it is the foundation for the industrialized process.

EPW Research Foundation (2007) observed that the target of doubling of bank
credit for agriculture is being obviously met because of a dictate from the
Government but, the quality of such lending will be weak and a large proportion will
come back as non-performing assets (NPAs). Without the expansion of rural branch
network by the financially strong and dominant public sector banks with staff
appropriately qualified for dealing with agriculture and micro-enterprises, the
objective of a rapid credit expansion is not going to be met efficiently. These banks
have to expand their network even as they co-opt for co-operatives and other local
agencies to supplement their banking business and undertake to expand their credit
base in the informal sector.

Satish (2007) studied the various issues concerning the growth of agricultural credit
deployment by the commercial banks during the reform period. It was observed that
the negative policy of credit for agriculture and other priority sectors, which has been
prevalent since the beginning of the post-reform era, has manifested itself in the two
broad areas, disincentivisation of credit flow to agriculture through the mechanical
application of Basel norms and the squeeze on the resources available for agricultural
credit operations. The researcher argues that the for successful promotion of the
deepening of rural financial markets, which would ensure uninterrupted flow of credit
to agriculture, will require a systematic rather than isolated effort, with related actions
being undertaken on several fronts simultaneously. It was suggested that a set of
reforms which will reverse the policy for agricultural credit such as entire supervisory
responsibilities of rural branch network of public sector banks to National Bank for
Agriculture and Rural Development (NABARD), comprehensive reforms of Basel
norms for agricultural credit, refinancing function of RBI through NABARD and the

78 EPW Research Foundation. (2007); “Rural Credit Structure Needs Genuine
Revitalization”, Economic and Political Weekly, Vol. XLII, No. 20, May 19, pp. 1802-
1808.
79 P. Satish, (2007); “Agricultural Credit in the Post-Reform Era-A Target of Systematic
Policy Correction”, Economic and Political Weekly, July 30, pp. 2567-2575.
need to strengthen the arrangement of resources for refinancing investment credit to agriculture in the interest of capital formation as is required.

**Sooden and Kumar (2007)** examined the growth and structure of priority sector lending of the public sector banks in the post-reform period. It was found that shrinking share of priority sector, neglect of agriculture coupled with its' sub-optimal structure, neglect of small scale industries, falling number of accounts across different categories of priority sector lending are some serious issues which need immediate attention of the policy makers. Banks appear to be deviating from their role of a social agent, by not paying required assistance to weaker sections in the post reform period. Further, it was also observed that there appears to be some serious doubt about the sustainability of the system of priority sector lending as evident from growing value of NPAs. It was suggested that the public sector banks need to go for a balanced approach regarding their role as development agent and at the same time must ensure their financial sustainability too.

**Sinha (2008)** observed that the banking sector reforms have posed new challenges before the banks as they have to conform to the new prudential asset classification, income recognition and capital adequacy standards and still maintain priority sector lending quota. A comparison of selected public and private sector banks was made for the period 2000-01 to 2004-05 on the basis of: (i) technical efficiency, (ii) scale efficiency, and (iii) Malmquist total factor productivity index. The results indicated substantial fluctuations in mean efficiency scores for the observed years. The mean technical efficiency scores were found to have declined particularly during the year 2004-05. The mean technical efficiency scores of the observed public sector banks was, however, marginally higher than those observed for private sector banks. The mean scale efficiency of the observed private sector banks is about 97 per cent of that of public sector banks. So far as total factor productivity growth is concerned, the private sector commercial banks exhibited marginally higher Malmquist TFP Index than the public sector banks. All the observed commercial banks registered positive total factor productivity growth during the period.

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Kumar and Gupta (2008)\textsuperscript{82} in their study of priority sector lending by the public and private sector banks during the period 1997 to 2005, observed that agricultural lending by the public sector banks has somewhat stagnated. The percentage share of small scale industries in overall priority sector lending recorded a continuous decline during the period under study. As against it, the percentage share of ‘other priority sector’ in the overall priority sector lending registered a continuous increase during under context. It was found that priority sector NPAs of public sector banks are nearly double than that of private sector banks. Whereas, in the public sector banks 50 per cent of the NPAs are contributed by priority sector lending alone, in case of private sector banks it is not so. Though all the three sectors i.e. agriculture, small scale industries and ‘other priority sector’ are contributing towards NPAs of public sector banks, yet, the share of SSIs is highest.

Ahmed (2009)\textsuperscript{83} observed that the shrinking share of priority sector in net bank credit, neglect of agriculture, falling number of accounts across the different categories of priority sector, loan recovery mechanism are some of the serious issues which need immediate attention of the policy makers. It was also found that the banks are not able to reach the prescribed target of lending to priority sector. There is a big gap between demand and supply of funds for priority sector.

Chatterjee (2009)\textsuperscript{84} examined the expansion of institutional credit in a district of West Bengal since bank nationalization. The study compared the district level performance of the institutional agencies viz. commercial banks, regional rural banks and co-operatives in supplying rural credit during pre and post-reform period. The analysis reveals that the performance of the all institutional agencies in supplying credit in rural West Bengal has deteriorated during the post-reform period. It was concluded that the policy changes in the sphere of rural credit are urgently required as finance plays an important role in determining agricultural productivity.


\textsuperscript{84} S. Chatterjee (2009); “Expansion of Institutional Credit-A District Level Study of Rural West Bengal”, Prajnan, Vol. XXXVII, No.4, Jan.-March.
Uppal (2009)\textsuperscript{85} threw light on the problems/issues of priority sector lending by public, private and foreign sector banks. It was observed that whereas, public sector banks have failed to achieve the target of 40 per cent, private sector banks have succeeded in achieving the overall target. Foreign sector banks have succeeded in achieving the target set for the small scale industries, export credit and overall target. Further, it was also found that NPAs of public sector banks have increased because of high priority sector advances.

Parimalarani (2011)\textsuperscript{86} examined the performance of the commercial bank in the area of priority sector lending during the period 1995–1996 to 2009–2010. The performance of the commercial banks in the area of priority sector advances exhibit an encouraging trend. Priority sector lending by the public sector banks increased by 13.99 times and that by private sector banks, by 35.63 times during this period under context. In case of foreign sector banks it increased by 69.09 times. Further, it was found that during the period 2005–06 and 2006–07, the level of non-performing assets was very high for priority sector and stood more than that of non-priority sector advances. However, the share of priority sector advances to the total advances has declined considerably during the later years of the study.

Veerakumar (2012)\textsuperscript{87} studied the priority sector lending by bank group-wise and targets achieved. He also studied priority and non-priority sector NPAs during the period 2001 to 2010. It was found that NPAs have choked off quantum of credit, restricted the recycling of funds and has lead to asset-liability mismatch. It has also affected profitability, liquidity and solvency position of the Indian banking sector. It was observed that one of the major reasons for NPAs in the banking sector is the ‘Direct Lending System’ (DLS) by the RBI. It was recommended that the bank management should speed up recovery of good and bad loans through various modes to decelerate growth of NPAs from the present level.


Najmi (2013) observed that during the period 2000 to 2010, the share of agriculture credit in net bank credit has increased which shows that banks are now more willing to lend credit to agriculture. Further, as compared to scheduled commercial banks as a whole, the share of public sector banks in credit to small scale industries has been higher. The growth rate of lending to small scale industries continuously increased during the period 2004 to 2007. This is due to several favorable policy initiatives undertaken by the central government and the Reserve Bank of India.

2.1 CONCLUSION

The review of literature reveals that the studies made in the past can be grouped into three groups, those made in the pre, early and later reform period. The studies (Pranav: 1979, Angadi: 1983, Gadgil: 1986 and Balister: 1989) made in the pre-reform period, took up the issues relating to developmental role of public sector banks in financing priority sectors particularly agriculture and small scale industries during the post-nationalization period.

Most of the studies (Ramanujam: 1993 and Mujumdar: 1995) carried out in early 1990’s, are in context to rationale and prospective of Financial Sector Reforms introduced in the economy in 1991. It was only since late 1990’s that studies evaluating the performance of public sector banks in priority sector lending during the reform period started appearing in the various books and journals. Majority of the studies (Kohli: 1997, Shajahan: 1998 and Ramesha: 1999 etc.) concluded that

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financial liberalization has a negative impact on lending to priority sector by public sector banks.


Thus, the review of literature revealed that though priority sector lending suffer from in-depth deficiencies, yet they are indispensable from overall economic development point of view.