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Some Empirical Results on Commercial Banks Lending to Priority Sector in India

Dr. Sanjeev Kumar

Associate Professor, Department of Economics, Himachal Pradesh University, Summer Hill, Shimla HP-171005.

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***Abstract** - The role of commercial banks viz. public and private sector banks has a new meaning and significance, in view of the changing structure and requirements of a developing economy. The priority sector lending is and will continue to be a crucial area of concern of public and private sector banks due to the socio-economic realities of the Indian economy. The objective of a research paper is to analyze the growth and structure of priority sector lending by commercial banks in India during the period from 2010 to 2019. The paper is based upon secondary data of 25 public sector banks and 17 private sector bank, collected from the various relevant issues on banking statistics published by RBI. The growth of credit to the priority sector and its various components has been with the help of a compound annual rate of growth. The behavior of inter-year disparities in priority sector lending is explained with co-efficient of variation. The performance of the two bank groups in priority sector lending has been compared with the t-test. The study highlighted that, although, on an average, the prescribed target of priority sector lending has been achieved in many years, one important issue of concern is the shrinking share of priority sector credit in net bank credit over a period of time by both banks group, which required immediate attention of the policymakers. The public and private sector banks could not deploy 18 percent of net bank credit in the agriculture sector and thus failed to achieve the stipulated target of agricultural lending.*

***Keywords** - Agriculture Credit, Priority Sector Lending, Inter-year disparities, t-test, Net Bank Credit.*

I. INTRODUCTION

The banking system is a crucial component of the service sector and acts as a backbone of economic development. The banks provide important services to the masses belonging to the various sectors of the economy. The banking system is one of the institutions that bump on the economy and impact its performance for better or worse. A developing economy faces various types of problems like poverty, scarcity of capital, unemployment, lack of good entrepreneurship, etc. The public and private sector banks can work as motivator agents of growth by making the right kind of policies in their working, depending upon the socio-economic conditions that exist in the country. These banks have adequate investment potential and can make an important contribution in eradicating poverty, unemployment and in bringing about a progressive reduction in inter-regional, inter-state as well as inter-sectoral disparities through the rapid growth of banking services. In India, commercial banks are those banks that are listed in the second schedule of the RBI Act 1934 and are regulated under the Banking Regulation Act 1949. Commercial banks in India are categorized into public sector banks, private sector banks, foreign sector banks, and regional rural banks.

The priority sector occupied a significant place in the Indian economy and is a special feature of the Indian banking system. Priority sector lending is the essence of the social banking system. Under the priority sector lending, banks are provided the credit on liberal terms and conditions to various sectors. The socialization of bank credit is the main theme of priority sector lending by these bank groups. Priority sector lending is and will also continue to remain, its importance by both ways, literally and figuratively, of Indian economic development. Since the priority sector is also critical to the high and sustained growth of GDP, so it should be the responsibility of public and private sector banks to support these sectors. In 1980, a major review of the various components of priority sector lending was analyses by a working group chaired by K.S. Krishnaswamy. The group recommendation on the incorporation of weaker sections under the priority sector so that the benefit that is being offered to the priority sector as a class could be oriented to meet the needs of the weaker sections also. Some credit was earmarked to the weaker sections of the society, i.e., small and marginal farmers, small businessmen, self-help groups, landless laborers, SC/ST, etc.; for achieving this object, banks opened more and more branches in rural areas where has no banking facilities yet.

At present, the broad categories of priority sector for all scheduled commercial banks include agriculture credit, small scale industries credit, and 'Other Priority Sector' credit. The 'Other Priority Sector' component includes the credit to retail trade credit, microcredit, education loan, housing loan, and weaker sections credit. The commercial banks, i.e., public and private sector banks (excluding regional rural banks) and foreign banks with 20 branches and above, are required to lend 40 percent of Adjusted Net Bank Credit (ANBC) or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher to priority sector. However, for the agriculture sector, the target of these banks is 18 percent of ANBC or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher.

II. REVIEW OF SOME RELATED STUDIES

A number of research studies have been conducted in India on various aspects of priority sector lending by the public and private sector banks. For example, Sooden and Kumar (2007) found that the shrinking share of priority sector, neglect of agriculture coupled with its sub-optimum structure, and neglect of small scale industries are some main problems that need immediate attention for the policymakers. Kumar and Gupta (2008) observed that agricultural lending by the public sector banks has somewhat stagnated. The percentage share of small-scale industries in priority sector lending registered a continuous decline, and the percentage share of 'other priority sector' in the priority sector lending registered a continuous increase during the period under context. Uppal (2009) found that in his study that public sector banks have failed to achieve the target of 40 percent, private sector banks have succeeded in achieving the overall target. Shabbir (2013) found that the majority of public and private sector banks are fulfilled their target of overall priority sector lending but not be able to fulfill the sub-target of 18 percent in the agriculture sector. Shilpa and Garg (2015) examined the trends, issues, and strategies of priority sector lending. They pointed out the various issues in priority sector lending as low profitability, higher NPAs, govt. Interferences, tractions cost and vesting decision of discretionary power to bank mergers. Kumar (2017) studied the trends of priority sector lending across various bank groups from the years 2001 to 2014 in India. It was found that priority sector lending is indispensable in the Indian economy. However, its quality across various bank groups and different states need to be reappraised and improved in a big way. Kumar (2019), in his study of priority sector lending in India, pointed out that without improvements in priority sector lending, we cannot achieve the objective of financial inclusion in India. It was suggested that RBI and government should strengthen the public sector banks in priority sector lending within the commercial banks.

III. RESEARCH METHODS

The objective of the study is to analyze the growth and structure of priority sector lending in India from 2010 to 2019 by commercial banks. The research paper is based upon secondary data collected from the various relevant issues on banking statistics published by the Reserve Bank of India. The commercial banks include public sector banks and private sector banks. Further, the period of study is divided into two parts, i.e., phase I, which includes the years from 2010 to 2014, and phase II, stretching over the years 2015 to 2019. With a view to analyzing the growth of priority sector lending, exponential growth has been used. The exponential growth rate is calculated as follows:

$$Yi = a_0 * b_i^t$$

$$\ln (Y_i) = \ln (a_0) + t^* \ln (b_i)$$

$$g = (b-1)$$

Where Y_i is the value of the ith indicator,
a = constant,
b_i = regression co-efficient of ith indicator,
t = time period,
In = common log value,
g = growth rate.

The structure of priority sector lending is analyzed by the mean value (Average) of an indicator which, is calculated for the first and second phases separately.

$$\text{The mean (X)} = \frac{x1 + X\,2 + X3 + \cdots \ldots\ldots\ldots X\,n}{n1 + n2 + n3 + \cdots \ldots\ldots\ldots n}$$

$$Xi \quad = \frac{\sum_{i=1}^{n} xi}{\sum_{i=1}^{n} ni}\ i{=}1$$

Where n_i stand for a number of observations (number of years) and
X_i stands for the value of NBC, priority sector credit, agriculture credit, SSIs credit, and 'Other Priority Sector' credit.

The performance of public and private sector banks under priority sector lending will be analyzed with the help of a t-test during both phases of the study. The null hypothesis states that there is no significant difference in the mean value of credit deployed (credit to priority sector and its various components) by two bank groups (H_0: $\mu_1=\mu_2$) in the first and second phases. Whereas the alternative hypothesis shows that there is a significant difference in the mean value of credit deployed by two bank groups (H_1: $\mu_1\neq\mu_2$) in two periods. The null and alternative hypotheses are tested at a 5 percent level of significance with the help of a t-test. The value of the t-test will be calculated as follow:

$$t = \frac{X1-X2}{S}\sqrt{\frac{n1n2}{n1+n2}}$$

Where n1 and n2 = size of two independent samples, i.e., no. of years for study
X_1 and X_2 are the Mean Value, i.e., Mean Value of priority sector lending by both bank groups.
S=average standard deviation of two samples.

IV. INTERPRETATION OF THE DATA

A. Priority Sector Lending by Public vis-vis Private Sector Banks

The priority sector credit by public sector banks, on average, increased at a rate of growth of 16.97 percent during the first phase, and this rate declined to 6.90 percent during the second phase (Table 1). The commercial banks, i.e., public and private sector banks, are required to lend 40 percent of NBC to the priority sector as per RBI norms. The public sector banks, on average, deployed 39.33 percent of NBC in the priority sector during the first phase. It was observed that only in the years 2010 and 2011 the prescribed target of priority sector lending was achieved by public sector banks. However, the prescribed target of priority sector lending was achieved during the second phase, and on average, 40.03 percent of NBC was deployed by public sector banks.

Table 1. Priority Sector Lending

(Amount in ₹ Crores)

Year	*Public Sector Banks*			*Private Sector Banks*		
	NBC	*Total PSAs*	*% to NBC*	*NBC*	*Total PSAs*	*% to NBC*
			Phase-I			
2010	2078397	864954	41.62	468589	215551	46.00
2011	2493500	1028616	41.25	533966	248828	46.60
2012	3018400	1130200	37.44	726954	286420	39.40
2013	3530808	1283680	36.36	872270	327406	37.53
2014	4048175	1618971	39.99	1062553	466650	43.92
Avg.	*3033856*	*1185284*	*39.33*	*732866*	*308971*	*42.69*
Growth Rate*	18.14	16.97		22.71	21.30	
			Phase-II			
2015	4584974	1750893	38.19	1228405	530287	43.17
2016	4886633	1985307	40.63	1495298	662030	44.27
2017	5329716	2043474	38.34	1809536	758713	41.93
2018	5350290	2199201	41.10	2144819	871306	40.62
2019	5458341	2286394	41.89	2832260	1245178	43.96
Avg.	*5121991*	*2053054*	*40.03*	*1902064*	*813503*	*42.79*
Growth Rate	4.46	6.90		23.22	23.79	

Source: - Complied on the Basis of Relevant Issues of 'Report on Trend and Progress of Banking in India' and 'Statistical tables relating to Banks in India,' Published by RBI.

*Note: - *Growth rate in %.*

Whereas, the priority sector credit by the private sector banks increased at a rate of 21.30 percent per annum in the first phase and increased by a small margin to 23.79 percent during the second phase (Table 1). The private sector banks, on average, deployed 42.69 percent of NBC in the priority sector during the first phase and 42.79 percent during the second phase. In the three years, i.e., 2010, 2011, and 2014 the prescribed target of priority sector lending was achieved in the first phase. During the second phase, the prescribed target of priority sector lending was achieved in all years by private sector banks.

B. Sector-wise Deployment of Priority Sector Lending by Public Sector Banks

The sector-wise analysis revealed that agriculture credit, on average, recorded a rate of growth of 14.77 percent during the first phase, but this rate of growth declined to 6.57 percent in the second phase (Table 2). As per the Reserve Bank of India norms, public sector banks are required to lend 18 percent of net bank credit to the agriculture sector from 1990 onwards. The public sector banks, on average, deployed 16.22 percent of net bank credit in the agriculture sector and failed to achieve the stipulated target during the first phase. Further, in the second phase, only in the year 2016 (18.52 percent) the prescribed target of agricultural lending was achieved by public sector banks. The public sector banks, on average, deployed 17.72 percent of NBC in the agriculture sector in the second phase. Under the new policy guidelines of 1991, the public sector banks in default in meeting the priority sector sub-target of 18 percent of net bank credit to agriculture would compensate the deficiency by contributing to Rural Infrastructure Development Fund (RIDF) and to the consortium fund of Khadi and Village Industries Commission (KVC). In this way, the banks could move away from their responsibility of direct lending to priority sectors, especially the risky venture like agriculture.

Table 2. Sector-wise Priority Sector Lending by Public Sector Banks

(Amount in ₹ Crores)

Years	*Agriculture*			*SSIs*			*Other Priority Sector*		
	Credit	*%age to TPSAs*	*%age to NBC*	*Credit*	*%age to TPSAs*	*%age to NBC*	*Credit*	*%age to TPSAs*	*%age to NBC*
				Phase-I					
2010	370729	42.86	17.84	278398	32.19	13.39	278827	32.24	13.42
2011	414990	40.34	16.64	369430	35.92	14.82	244196	23.74	9.79
2012	475148	42.04	15.74	396993	35.13	13.15	258059	22.83	8.55
2013	530677	41.34	15.03	478444	37.27	13.55	274559	21.39	7.78
2014	643287	39.73	15.89	587424	36.28	14.51	388260	23.98	9.59
Avg.	*486966*	*41.26*	*16.22*	*422138*	*35.36*	*13.88*	*288780*	*24.84*	*9.83*
Growth Rate	*14.77*			*20.52*			*8.63*		
				Phase-II					
2015	756233	43.19	16.49	650434	37.15	14.19	344226	19.66	7.51
2016	904772	45.57	18.52	734055	36.97	15.02	346480	17.45	7.09

2017	946851	46.34	17.77	741958	36.31	13.92	362568	17.74	6.80
2018	961076	43.70	17.96	863307	39.26	16.14	374818	17.04	7.01
2019	975354	42.66	17.87	905685	39.61	16.59	405355	17.73	7.43
Avg.	*908,857*	*44.29*	*17.72*	*779,088*	*37.86*	*15.17*	*366,689*	*17.92*	*7.17*
Growth Rate	*6.57*			*8.63*			*4.17*		

Source: - As per Table 1

The credit to SSIs, on average, increased at a rate of 20.52 percent in the first phase, but it declined to 8.63 percent during the second phase. However, the public sector banks, on average, deployed 13.88 percent of net bank credit to SSIs in the first phase. This share rose marginally increase to 15.17 percent during the second phase, in the absence of any clear guidelines by RBI (as it is there in the case of agriculture). It was due to that the public sector banks have gradually increased the number of advances to small scale industries, but, the share, in which net bank credit in priority sector has expanded, the relative share of the small sector has not grown in the same ratio during the period of study**.** The credit of public sector banks to 'other priority sector,' on average, increased at a rate of 8.63 percent during the first phase (Table 2). However, this rate declined and stood at 4.17 percent per annum during the second phase. The public sector banks, on average, deployed 9.83 percent and 7.17 percent of net bank credit in the 'other priority sector' during the first and second phase, respectively, in the absence of any clear guidelines by RBI.

C. Sector-Wise Deployment of Priority Sector Lending by Private Sector Banks

The agriculture credit increased at a rate of 13.27 percent during the first phase. However, this rate increased to 28.26 percent in the second phase. The private sector banks, as per the Reserve Bank of India norms, are also required to lend 18 percent of net bank credit to the agriculture sector. The banks, on average, deployed 15.41 percent of net bank credit in the agriculture sector and thus failed to achieve the stipulated target of agriculture credit in the first phase (except 2010). During the second phase, in none of the years, the prescribed target of lending was achieved, and on average, 16.73 percent of net bank credit was deployed in the agriculture sector by private sector banks.

Table 3. Sector-wise Priority Sector Lending by Private Sector Banks

(Amount in ₹ Crores)

Years	***Agriculture***			***SSIs***			***Other Priority Sector***		
	Credit	***%age to TPSAs***	***%age to NBC***	***Credit***	***%age to TPSAs***	***%age to NBC***	***Credit***	***%age to TPSAs***	***%age to NBC***
Phase-I									
2010	89768	41.65	19.16	64825	30.07	13.83	60958	28.28	13.01
2011	92136	37.03	17.26	87857	35.31	16.45	68835	27.66	12.89
2012	100900	35.23	13.88	110500	38.58	15.20	75020	26.19	10.32
2013	111968	34.20	12.84	141735	43.29	16.25	73703	22.51	8.45
2014	147754	31.66	13.91	186793	40.03	17.58	132103	28.31	12.43
Avg.	*108,505*	*35.95*	*15.41*	*118,342*	*37.46*	*15.86*	*82,124*	*26.59*	*11.42*
Growth Rate	*13.27*			*30.29*			*21.33*		
Phase-II									
2015	181768	34.28	14.80	216578	40.84	17.63	131941	24.88	10.74
2016	266857	40.31	17.85	292342	44.16	19.55	102831	15.53	6.88
2017	297244	39.18	16.43	355702	46.88	19.66	105767	13.94	5.84
2018	368988	42.35	17.20	392440	45.04	18.30	109878	12.61	5.12
2019	491870	39.50	17.37	594400	47.74	20.99	158908	12.76	5.61
Avg.	*321,345*	*39.12*	*16.73*	*370,292*	*44.93*	*19.23*	*121,865*	*15.94*	*6.84*
Growth Rate	*28.26*			*28.31*			*4.76*		

Source: - As per Table 1.

Further, the credit to SSIs, on average, recorded a higher rate of growth of 30.29 percent during the first phase, but the rate of growth declined to 28.31 percent in the second phase (Table 3). The private sector banks, on average, deployed 15.86 percent of net bank credit to SSIs during the first phase; however, this share increased to 19.23 percent during the second phase. The 'other priority sector' credit by private sector banks grew at a very high rate of 21.33 percent in the first phase vis-vis 4.76 percent in the second phase. The 'other priority sector' credit, on average, stood as high as 11.42 percent of NBC in the first phase and declined to 6.84 percent per during the second phase of the study in the absence of any guidelines on lending to 'other priority sector' by RBI.

V. RESULTS AND HYPOTHESIS TESTING

A. t-test with respect to Priority Sector Lending by Public and Private Sector Banks

The null hypothesis states that there is no significant difference in the mean value of credit deployed by two bank groups (H_0: $\mu_1=\mu_2$) in the first and second phases. Whereas the alternative hypothesis shows that there is a significant difference in the mean value of credit deployed by two bank groups (H_1: $\mu_1\neq\mu_2$) in two periods.

Table 4. T-test with respect to Priority Sector Lending by Banks

Phase-I	***Mean Value***	***Std. Dev.***	***t-test***	***d. f. (v)***	***Sig. (2-Tailed Test)***
Public Sector Banks	47411.37	11453.50	5.37	8	0.001
Private Sector Banks	18174.76	5737.60			
Phase-II	***Mean Value***	***Std. Dev.***	***t-test***	***d. f. (v)***	***Sig. (2-Tailed Test)***
Public Sector Banks	82122.15	8289.49	4.46	8	0.003
Private Sector Banks	47853.11	15997.45			

Source: Authors own Calculations from the data given in Table 1.
Note:- $n_1=5$ *and* $n_2=5$ *(Number of Years).*
Degree of freedom, d. f. (v) = $n_1+n_2-2=5+5-2=8$.
The value of the t-test for the two-tailed test for v=12 is $(t_{0.05}) = 2.17$.

Since the calculated value of the t-test during the first phase and second phases are 5.37 and 4.46 respectively (Table 4), which are more than the table value *(for v =8,* $t_{0.05}$ *=2.17)* and are found significant at 5% level (Significance, two-tailed test= 0.001 and 0.003), so the null hypothesis is rejected, and the alternative hypothesis is accepted. So it is concluded that there is a significant difference in the mean value of credit deployed by public and private sector banks (H_1: $\mu_1 \neq \mu_2$) during the first and second phases of the study.

B. Test of Hypothesis with respect to Credit Deployed to Various Components of Priority Sector

The calculated value of the t-test with respect to agriculture credit during the first and second phase are 7.33 and 5.29 respectively (Table 5), which are more than the table value *(for v =8,* $t_{0.05}$ *=2.17)* and are found significant at 5% level (Significance, two-tailed test=0.000 and 0.001), so the null hypothesis is rejected, and the alternative hypothesis is accepted, and we conclude that there is a significant difference in the mean value of credit deployed to agriculture sector by both bank groups (H_1: $\mu_1 \neq \mu_2$) during the two phases of the study.

Table 5. T-test within Agriculture, SSIs, and 'Other Priority Sector' by Public vis-à-vis Private Bank

Agriculture Credit					
Phase-I	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	19478.65	4251.03	7.33	8	0.000
Private Sector Banks	6382.66	1388.70			
Phase-II	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	36354.29	3572.28	5.29	8	0.001
Private Sector Banks	18902.67	6858.70			
Small Scale Industries (SSIs) Credit					
Phase-I	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	16885.51	4671.68	4.20	8	0.004
Private Sector Banks	6961.30	2803.80			
Phase-II	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	31163.51	4151.05	2.37	8	0.055
Private Sector Banks	21781.91	8351.70			
'Other Priority Sector' Credit					
Phase-I	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	11551.21	2291.64	5.36	8	0.001
Private Sector Banks	4830.81	1675.15			
Phase-II	*Mean Value*	*Std. Dev.*	*T-test*	*d. f. (v)*	*Sig. (2-Tailed Test)*
Public Sector Banks	14667.58	998.22	9.95	8	0.000
Private Sector Banks	7168.53	1391.66			

Source: Authors own Calculations from the data given in Tables 2 and 3.
Note:- $n_1=5$ *and* $n_2=5$ *(Number of Years).*
Degree of freedom, d. f. (v) = $n_1+n_2-2=5+5-2=8$.
The value of the t-test for the two-tailed test for v=12 is $(t_{0.05}) = 2.17$.

In the case of SSIs, the computed value of the t-test during the first and second phase is 4.20 and 2.37, which are greater than the table value *(for v =8,* $t_{0.05}$ *=2.17)*, and it is found in-significant at 5% level (Significance, two-tailed test=0.004 and0.055), so the null hypothesis is rejected, and the alternative hypothesis is accepted, and we conclude that there is no significant difference in the mean value of credit deployed to Small Scale Industries by public and private sector bank groups (H_1: $\mu = \mu_2$) during the first and second phase by the public and private sector banks.

The values of the t-test with respect to 'Other Priority Sector' during the first and second phase is 5.36 and 9.95 respectively (Table 5), which are more than the table value *(for v =8,* $t_{0.05}$ *=2.17)* and are found to significant at

5% level (Significance, two-tailed test=0.001 and 0.000), so the null hypothesis is rejected, and the alternative hypothesis is accepted, and we conclude that there is a significant difference in the mean value of credit deployed to 'Other Priority Sector' by public and private sector banks (H_1: $\mu_1 \neq \mu_2$) during the first and second phase.

VI. CONCLUSION

The study points out that the priority sector lending by private sector banks registered a higher rate of growth vis-à-vis public sector banks during both phases. It was found that, on average, the prescribed target of priority sector lending was achieved by public and private sector banks during the first and second phases (except some years). Although the prescribed target of priority sector lending has been achieved by these bank groups, one important issue of concern is the inter-year disparities in the share of priority sector credit in net bank credit of both the public and private sector banks, which needs immediate attention of the policymakers. The public and private sector banks, on average, could not deploy 18 percent of net bank credit in the agriculture sector and thus, failed to achieve the stipulated target of agricultural lending during both phases. This is due to the fact that under the new policy guidelines of 1991, the public and private sector banks in default in meeting the priority sector sub-target of 18 percent of net bank credit to agriculture would compensate the deficiency by contributing to Rural Infrastructure Development Fund (RIDF) and to the consortium fund of Khadi and Village Industries Commission (KVC). In this way, the banks have been successful in a move away from their responsibility of direct lending to a risky venture like agriculture. It was found that within the priority sector, the share of agriculture and SSIs credit has increased while that of 'other priority sector' by both the bank groups has decreased continuously during the period under study. One more issue of concern is that the percentage share of NBC deployed by public and private sector banks in 'other priority sector' has declined throughout the period, despite the fact that the scope and definition of 'other priority sector' have expanded within the priority sector in recent times.

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