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INDUSTRY OUTLOOK

NBFC PERFORMANCE AND OUTLOOK: NAVIGATING A COMPLEX FINANCIAL ECOSYSTEM

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Introduction

India's financial system is highly diverse, with NBFCs playing a key role alongside traditional banks. Originating in the 1960s to provide hire-purchase and leasing services, NBFCs have expanded into vehicle and housing finance, infrastructure lending, microfinance, and wealth management. Regulated by the RBI since 1963, they gained prominence during the 1990s financial liberalization. NBFCs are crucial for financial inclusion, providing credit to underserved households and small businesses, supporting key sectors like infrastructure and MSMEs, and facilitating capital market development through investment and securitization.



The NBFCs are playing a crucial role in credit intermediation, particularly in underserved and unbanked segments such as MSMEs, retail, transport, and infrastructure. Over the past decade, NBFCs have significantly increased their share in the credit portfolio, growing from one-sixth of the total bank credit in 2013 to more than one-fourth now.

This steady growth reflects the sector's ability to reach underserved sectors, particularly small businesses and households, offering customer-friendly credit solutions.

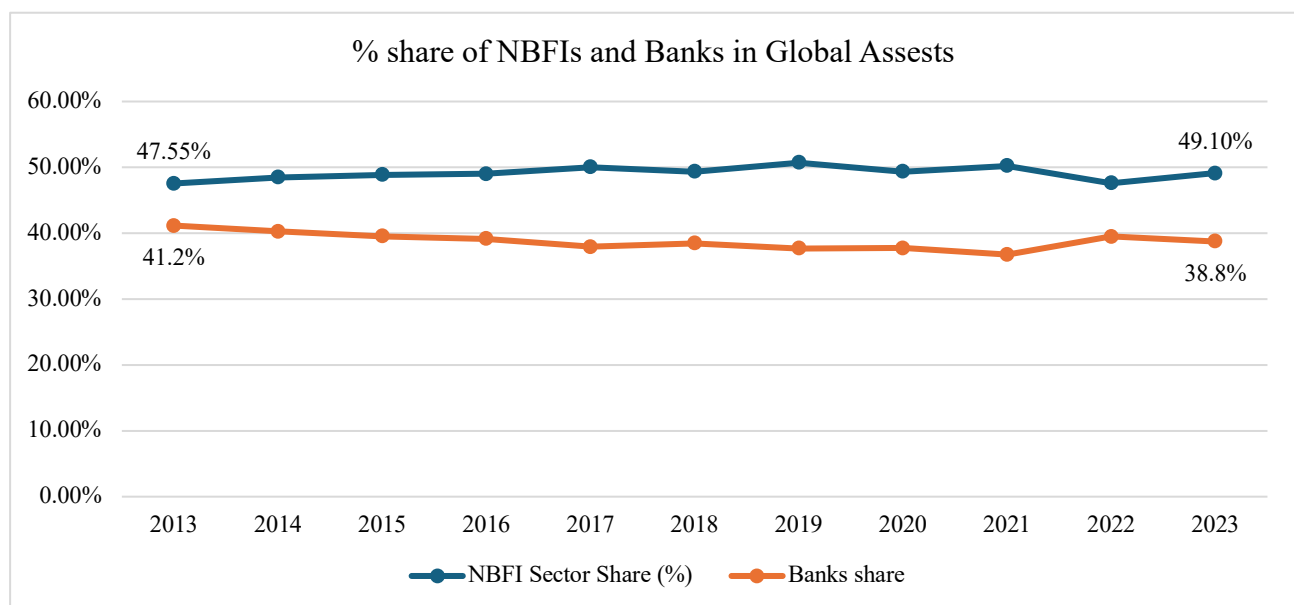
By leveraging technology, NBFCs have expedited and streamlined their credit delivery processes, positioning themselves as a preferred option for many individuals, groups, and companies. However, this rapid expansion has also introduced systemic risks, including rising interconnectedness with the banking sector and exposure to riskier credit segments. In response, the RBI has increased regulatory oversight to ensure stability and resilience within the sector.

Global Non-Bank Financial Intermediation

Globally, non-bank financial intermediation has grown substantially, with assets under management increasing significantly. This growth has been driven by various factors, including the search for yield in a low-interest-rate environment, the rise of fintech, and the increasing demand for alternative financing options.

According to the Financial Stability Report, June 2025, by the RBI, the total global financial assets stood at an estimated US\$ 486.4 trillion at the end of December 2023. Out of this, NBFIs accounted for 49.1%, underscoring their growing prominence (see Chart 1).¹ This marked a notable increase compared to previous years and reflects the trend of deepening financial systems worldwide, particularly the shift from traditional banking to more diverse and specialized financial entities.

Chart 1: Share of NBFIs in Global Assets

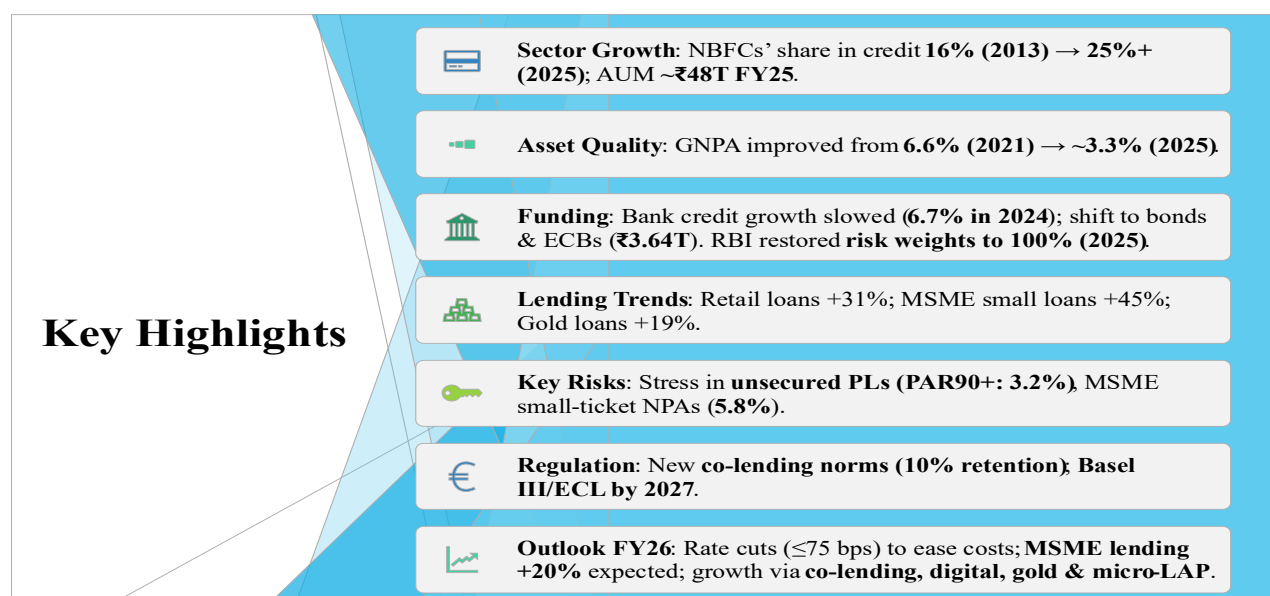


Source: Financial Stability Board | FSR, June 2025, RBI

The expansion of NBFIs globally has been driven by a combination of factors, including financial innovation, regulatory arbitrage, and increased demand for customized financial products. However, this growth has also led to concerns among international regulators. Global experiences highlight both the potential and pitfalls of non-bank financial intermediation. While they foster innovation, credit access, and capital market development, they also introduce systemic risks due to less stringent regulatory oversight, liquidity mismatches, and interconnectedness with banks.

The Financial Stability Board (FSB) has highlighted risks associated with excessive leverage, interconnectedness with the banking system, and liquidity mismatches within the NBFI sector. These concerns have intensified as geopolitical uncertainties and abrupt monetary policy shifts continue to influence capital flows and market stability. Besides, the rising share of synthetic leverage among entities such as hedge funds has added layers of complexity and opacity, elevating the potential for systemic spillovers in periods of stress.

Recent episodes of market turmoil, such as the April 2025 tariff shock and the March 2020 “dash-for-cash” crisis, illustrate how leveraged NBFIs can amplify systemic stress through the forced unwinding of positions. Also, the growing overlap between banks and NBFIs in business models and market exposures heightens the risk of contagion, as evidenced by the 2022 U.K. pension fund crisis, where fire sales by NBFIs contributed to significant market dislocations. Given the sector’s scale and interconnectedness, there is an urgent need for enhanced global monitoring and coordinated policy measures to mitigate systemic vulnerabilities.

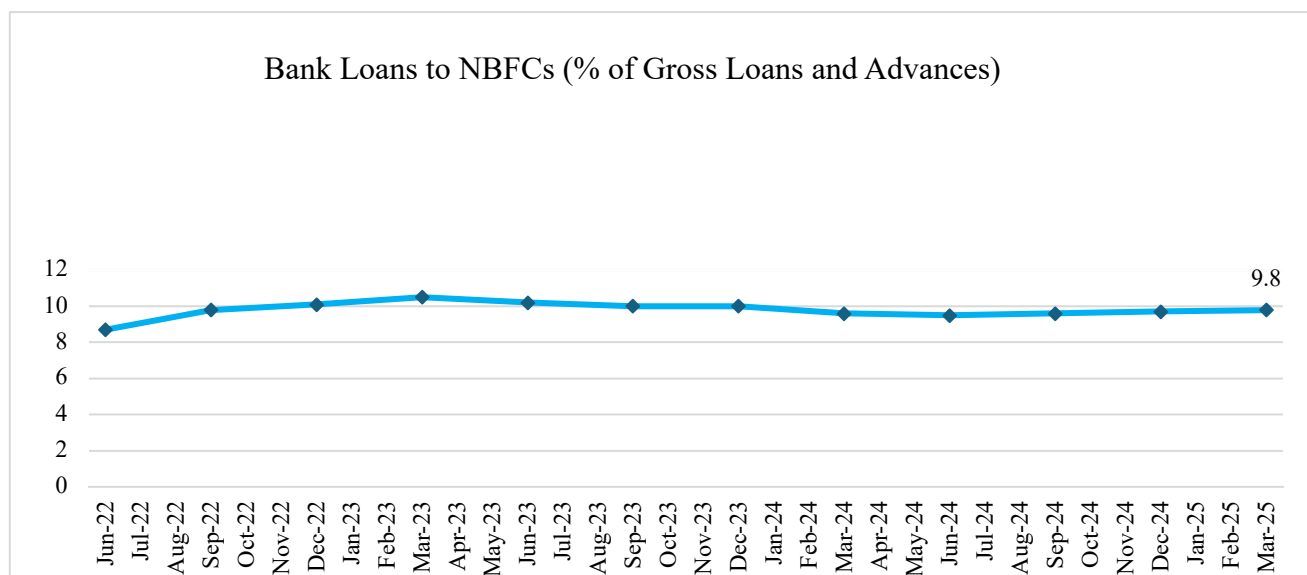


Domestic NBFC Industry

In India, Non-Banking Financial Companies (NBFCs) have become an integral part of the financial system. Registered under the Companies Act, 2013 and regulated by the Reserve Bank of India (RBI), they operate across a wide range of financial activities. Their core functions include lending to individuals and businesses, with a strong presence in sectors such as microfinance, housing finance, and vehicle loans; investing in securities, bonds, and other instruments to provide alternative funding for corporations and governments; and offering asset financing for vehicles, equipment, and infrastructure projects. Over the past decade, the sector has grown rapidly, driven by rising credit demand from individuals, MSMEs, and underserved markets. NBFCs have leveraged their flexibility, customer-centric approach, and ability to penetrate segments often overlooked by banks, positioning themselves as a key pillar in deepening financial inclusion and supporting economic growth.

In India, the interconnectedness between banks and NBFCs has grown in tandem with the latter's increasing footprint. While the RBI has implemented proactive and prudent regulatory measures to manage these linkages, emerging risks, especially in high-growth areas such as unsecured lending and microfinance which require ongoing vigilance (see Chart 2 and Chart 3).

Chart 2: Banks' Loans to NBFIs¹ as Share of Gross Loans and Advances (Per cent)



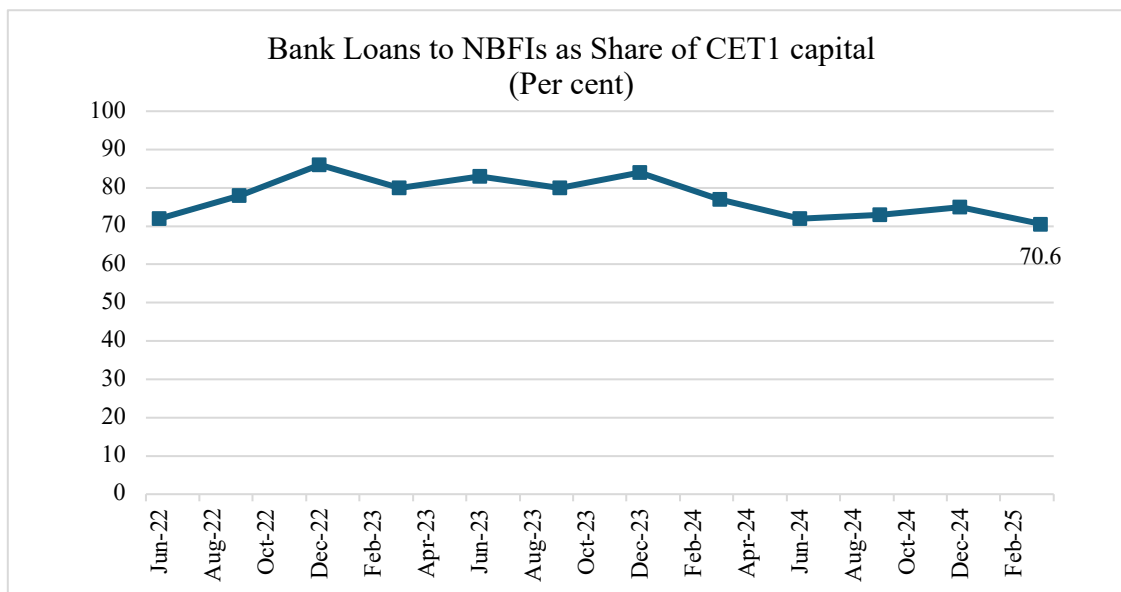
Source: Financial Stability Report, June 2024

¹ Notes: (1) Domestic NBFIs are composed of (1) NBFCs (including MFIs and HFIs), (2) mutual funds, (3) insurance and pension funds, (4) DFIs and (5) other financial intermediation activities.

(2) Lending by PSBs and PVBs.

Over the years, bank loans to NBFCs as a share of gross loans and advances have increased from 8.7% in the quarter ending June 2022 to 9.8% in the quarter ending March 2025, while it was 9.6% in the quarter ending March 2024.

Chart 3: Bank Loans to NBFI as Share of CET1 capital



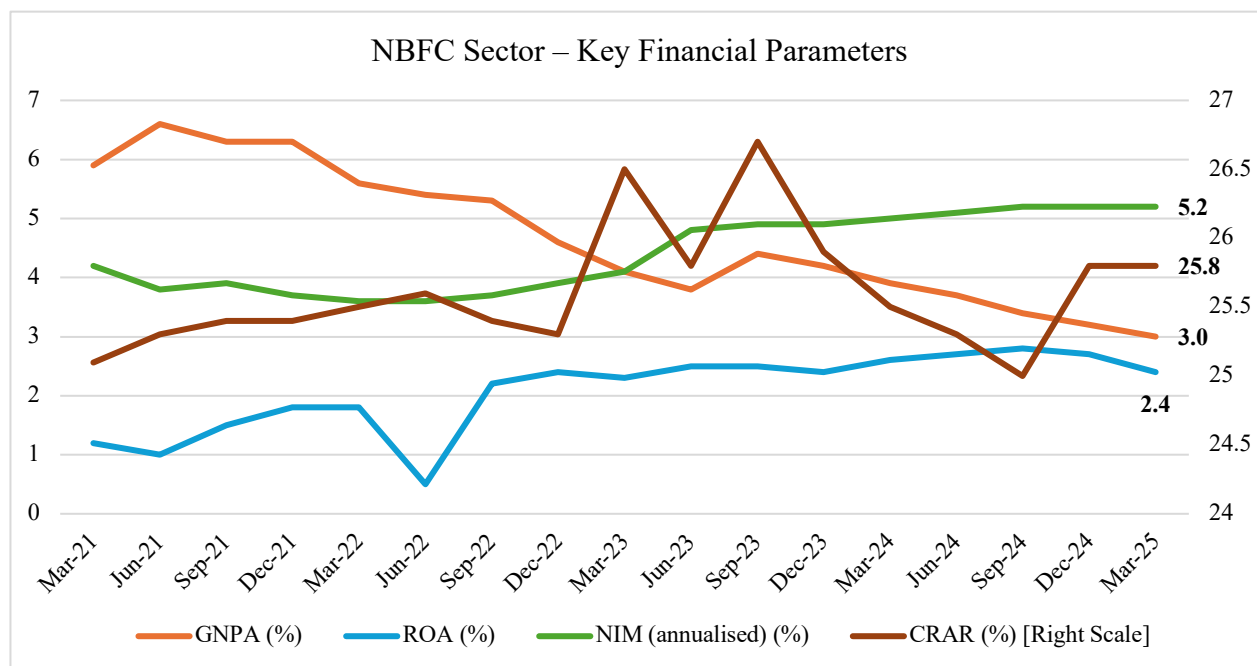
Source: Financial Stability report June 2024

The NBFC sector remains resilient, supported by strong capital adequacy, healthy interest margins, solid earnings, and low impairment ratios, though loan growth has moderated due to the earlier increase in risk weights on select consumer credit segments and on bank lending to NBFCs. With the recent restoration of pre-tightening risk weights and improving financial conditions, credit growth prospects are expected to strengthen.

Over the years, the asset quality of NBFCs has improved, leading to a healthier positioning of their balance sheets. Starting from 5.9% in March 2021, GNPA ratios initially rose to a peak of 6.6% in June 2021, reflecting post-pandemic stress. In the last four years, the stressed assets of NBFCs have reduced by nearly 50%, indicating stronger credit discipline, better underwriting practices, regulatory support, and a recovery in economic activity (see Chart 4).

Chart 4: Key Financial Parameters of NBFC Sector

(Per cent, both left and right scale)



Note: This assessment (done by RBI), based on provisional data as of June 10, 2025, covers NBFCs in the upper and middle layers, excluding HFCs, CICs, and SPDs, but including those currently under resolution.

Source: Financial Stability Report, June 2024.

Types of NBFCs in India

NBFCs in India are categorized broadly into:

1. **Asset Finance Companies (AFCs):** Primarily engaged in financing physical assets like automobiles, machinery, etc.
2. **Investment Companies (ICs):** Deal with acquisition of securities.
3. **Loan Companies (LCs):** Provide finance in the form of loans and advances.
4. **Infrastructure Finance Companies (IFCs):** Provide infrastructure project financing.
5. **Microfinance Institutions (NBFC-MFIs):** Provide small loans to low-income borrowers.
6. **NBFC-Factors:** Specialize in receivables financing.
7. **Housing Finance Companies (HFCs):** Though separately regulated by the National Housing Bank (and later RBI), they form an important subset.

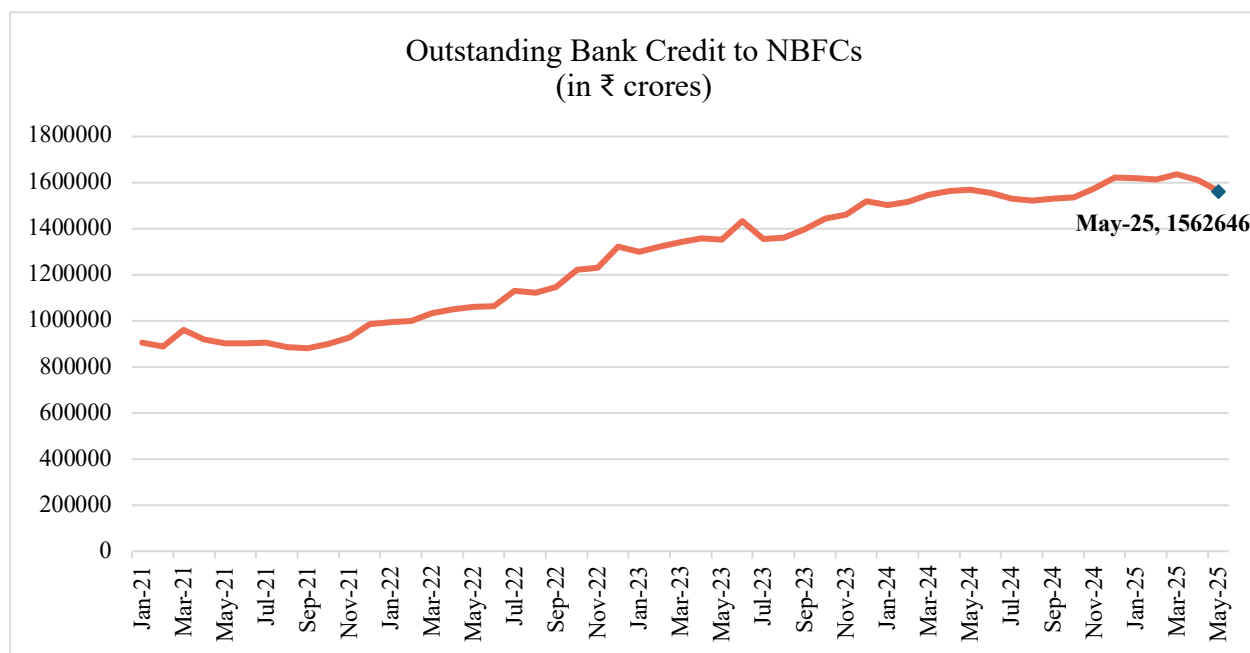
Outstanding Bank Credit to NBFCs

Banks play a significant role in funding NBFCs, providing a substantial portion of their capital requirements. Outstanding bank credit to NBFCs has grown steadily over the years, reflecting the increasing dependence of NBFCs on bank funding.

The post-COVID period has witnessed a strong recovery in bank credit to NBFCs, reflecting the sector's resilience in overcoming the economic shock. NBFCs have continued to play a vital role in credit intermediation, supported by banks' lending stance and the deepening of financial activity, despite occasional short-term fluctuations. Outstanding bank credit stood at about ₹9.06 lakh crore in January 2021 and, after some initial volatility during the pandemic, gained significant traction from early 2022. By March 2022, it had crossed ₹10 lakh crore and maintained a steady upward trend, driven by both the rising funding requirements of NBFCs and banks' growing willingness to lend.

The pace of expansion accelerated through 2023–24, with outstanding credit rising from ₹13.0 lakh crore in January 2023 to ₹16.2 lakh crore by December 2024. As of May 2025, the figure stood at around ₹15.6 lakh crore, nearly 70% higher than the January 2021 level (see Chart 5).

Chart 5: Trend of Outstanding Bank Credit to NBFCs in India



Source: RBI

As of March 2025, NBFCs accounted for a significant portion of the credit in India's financial system, though the exact percentage is not specified in the available data, with growth outpacing that of banks in the fiscal year 2025 (FY25). In fact, NBFCs' credit growth was around 20% in FY25, compared to the banking sector's 12% growth, and their share of the total credit of NBFCs in the Indian financial system is second only to scheduled commercial banks (SCBs). This interdependence creates a potential contagion risk. Stress in NBFCs can spill over to the banking system, as seen during defaults by IL&FS and DHFL. Consequently, the RBI monitors bank exposure to NBFCs closely.

During FY 2023-24, India's NBFC sector also recorded robust growth in assets under management (AUM), expanding by approximately 23% year-on-year, driven by strong demand for retail, MSME, and infrastructure credit, along with favourable funding conditions. This momentum pushed NBFCs' AUM to about ₹47 trillion by March 2024. In FY25, however, growth is expected to moderate due to tighter regulatory norms, cautious bank lending, and rising credit quality concerns. Industry estimates project NBFC AUM to cross ₹50 trillion in FY25, implying a tempered growth of 12-15%, broadly in line with historical averages. From FY19 to FY25, the compound annual growth rate (CAGR) is estimated at 13.2%, with total AUM increasing from about ₹23 trillion to nearly ₹48 trillion.

NBFCs' share in the overall systemic credit has also expanded significantly, from around 12% in FY08 to 21% in FY25, highlighting their growing importance in India's financial landscape. This trend reinforces the sector's critical role in inclusive credit delivery but also calls for a calibrated regulatory approach to balance growth with financial stability.

Recent Funding Dynamics

In 2024, NBFCs experienced a notable shift in their funding mix due to regulatory and market factors. Bank credit to NBFCs grew by only 6.7%, reaching ₹16.22 lakh crore as of December 2024, its slowest pace in four years, compared to a robust 15% growth in 2023. This slowdown was primarily triggered by the Reserve Bank of India's (RBI) decision in November 2023 to raise the risk weight on loans to NBFCs by 25 basis points to 125%. Higher capital requirements made banks more selective in extending credit, forcing NBFCs to diversify their funding sources.

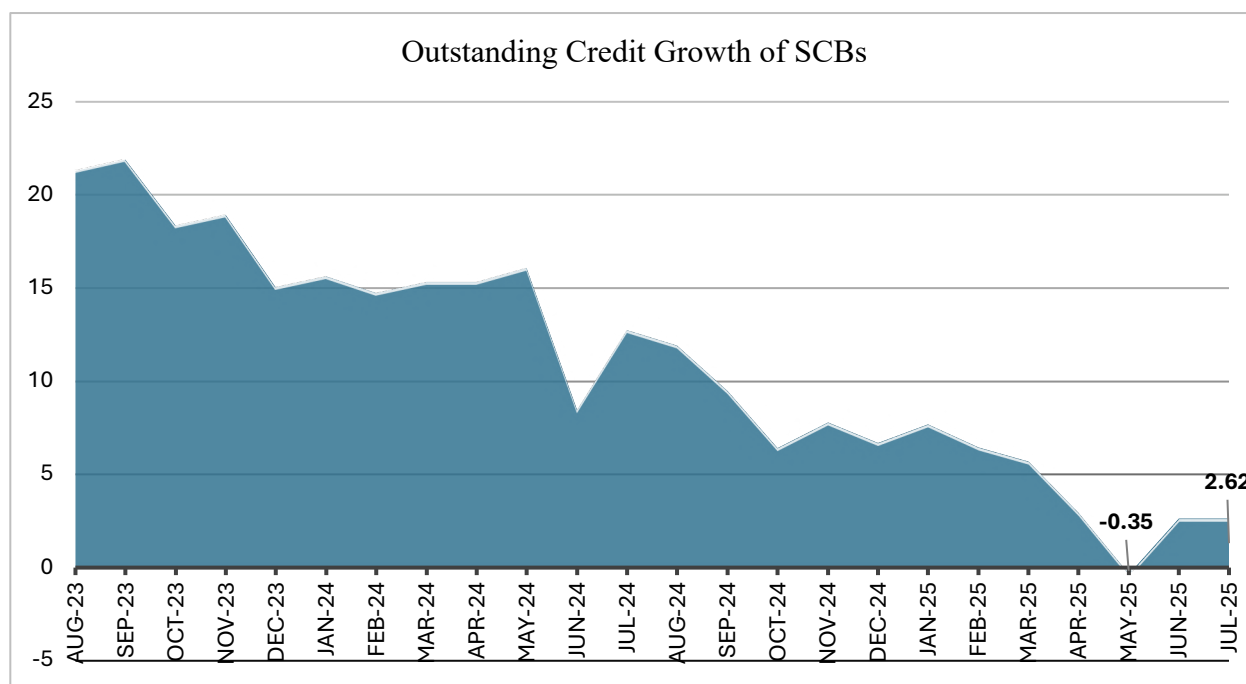
In response, NBFCs increasingly tapped domestic capital markets through bond issuances and explored overseas funding avenues, including dollar bonds and syndicated loans. External Commercial Borrowings (ECBs) reached a five-year high of ₹3.64 lakh crore in

2024, with major players like Shriram Finance and Muthoot Finance raising \$1.277 billion and \$400 million, respectively. However, ECBs remain subject to caps under the automatic route, limiting borrowing to \$750 million per company per year. This shift underscores NBFCs' efforts to mitigate funding risks and achieve greater financial stability amid a changing regulatory landscape.

Moderation in Growth

The data further reveal a strong recovery followed by moderation in bank credit to NBFCs. While outstanding credit grew steadily to ₹16.2 lakh crore by December 2024, it slowed to ₹16.4 lakh crore in March 2025 and further contracted to ₹15.6 lakh crore by May 2025.² This reversal reflects the combined impact of higher risk weights, banks' cautious stance, and rising stress in unsecured and small-ticket lending segments. The trend underscored NBFCs' increasing dependence on banks as a funding source while also exposing their vulnerability to regulatory shifts and banking sector risk perceptions (see Chart 6).

Chart 6: Trend of Outstanding Credit of SCBs (Y-o-Y % Change)



Sources: CMIE Economic Outlook | Infomerics Economic Analysis

In a relief to the sector, the RBI restored risk weights on bank loans to NBFCs to 100% (from 125%) effective April 1, 2025. This move is expected to ease borrowing costs, revive credit flow, and strengthen NBFCs' lending capacity,

while also balancing broader financial stability concerns. The November 2023 hike was prompted by the RBI's warnings about rapid growth in certain consumer credit segments and the need for stronger surveillance.

Sectoral Credit Trends

Alongside sectoral diversification on the lending side, the liability profile of NBFCs has also evolved. Agriculture, MSMEs, trade, and retail loans have seen significant growth, particularly in microfinance, vehicle finance, and consumer loans. For instance, retail loans expanded by over 31% in FY24, with sharp increases in credit cards, education loans, and unsecured segments. While this diversification supports financial inclusion, it also raises asset quality risks, especially in unsecured lending categories.

Table 1: Credit to Various Sectors by NBFCs

(₹ crore)

Item	End-March 2022	End-March 2023	End-March 2024	End- September 2024	YoY % change	
	2022	2023	2024	2024	2022-23	2023-24
Gross Advances	2,895,753	3,399,655	4,027,528	4,292,708	17.4	18.5
1. Agriculture and Allied Activities	52,069	60,674	84,175	89,800	16.5	38.7
2. Industry (2.1 to 2.4)	1,115,957	1,269,175	1,496,425	1,590,339	13.7	17.9
2.1 Micro and Small	42,353	69,410	100,627	121,589	63.9	45.0
2.2 Medium	16,013	19,483	20,961	21,504	21.7	7.6
2.3 Large	890,104	1,021,373	1,232,434	1,300,359	14.7	20.7
2.4 Others, if any, please specify	167,486	158,908	142,404	146,887	-5.1	-10.4
3. Services (3.1 to 3.10 equals 3.a to 3.d)	392,121	468,009	566,932	608,246	19.4	21.1
3.1 Transport Operators	103,283	120,245	132,810	141,289	16.4	10.4
3.2 Computer Software	1,652	2,107	3,082	2,579	27.5	46.3
3.3 Tourism, Hotel and Restaurants	5,971	7,519	7,439	7,860	25.9	-1.1
3.4 Shipping	172	185	272	216	7.6	46.9
3.5 Professional Services	20,154	23,580	25,239	29,377	17.0	7.0
3.6 Trade	49,837	69,520	92,324	105,415	39.5	32.8
3.6.1 Wholesale Trade (other than Food Procurement)	9,290	10,657	14,500	17,632	14.7	36.1
3.6.2 Retail Trade	40,547	58,863	77,824	87,784	45.2	32.2
3.7 Commercial Real Estate	80,264	81,662	88,512	89,482	1.7	8.4

3.8 NBFCs	33,774	47,664	60,356	64,319	41.1	26.6
3.9 Aviation	1,143	826	455	438	-27.7	-44.9
3.10 Other Services	95,873	114,700	156,442	167,272	19.6	36.4
Total 3.a to 3. d	392,121	468,009	566,932	608,246	19.4	21.1
3.a Micro and Small	111,482	160,253	209,555	224,653	43.7	30.8
3.b Medium	17,503	20,322	28,550	25,073	16.1	40.5
3.c Large	76,915	78,518	80,697	95,366	2.1	2.8
3.d Others	186,221	208,917	248,129	263,155	12.2	18.8
4. Retail Loans (4.1 to 4.10)	819,433	1,045,168	1,369,820	1,502,697	27.5	31.1
4.1 Housing Loans (incl. priority sector Housing)	22,340	32,172	33,600	38,467	44.0	4.4
4.2 Consumer Durables	24,771	31,541	40,957	48,142	27.3	29.9
4.3 Credit Card Receivables	32,710	44,007	55,736	61,171	34.5	26.7
4.4 Vehicle/Auto Loans	326,347	382,825	474,839	517,092	17.3	24.0
4.5 Education Loans	14,145	25,324	44,904	58,466	79.0	77.3
4.6 Advances against Fixed Deposits (incl. FCNR(B), etc.)	41	213	151	202	419.5	-29.3
4.7 Advances to Individuals against Shares, Bonds, etc.	11,473	13,389	21,780	23,991	16.7	62.7
4.8 Advances to Individuals against Gold	118,501	128,774	153,481	174,325	8.7	19.2
4.9 Micro finance loan/SHG Loan	76,223	115,187	148,503	144,162	51.1	28.9
4.10 Other Retail Loans	192,881	271,735	395,868	436,679	40.9	45.7
5. Other Credit	516,173	556,630	510,174	501,626	7.8	-8.3

Notes: 1. Data are provisional. 2. Data given for 2021-22, 2022-23, 2023-24 are for NBFCs (excluding CICs, HFCs & SPDs) falling in Upper layer and Middle layer as on March 31, 2024. 3. Percentage figures are rounded off. Source: Quarterly returns of NBFCs, RBI.

NBFC's Source of Funds

NBFCs in India draw from a diverse mix of funding sources to sustain operations. Bank borrowing remains the largest component, accounting for nearly half of total funding through term loans, working capital finance, and subordinated debt. Market borrowings are another critical avenue, with NBFCs raising long-term resources via non-convertible debentures (NCDs), while commercial papers (CPs) provide a flexible and cost-effective option for short-term needs.

The securitization of loan assets has also gained traction, enabling NBFCs to unlock liquidity by packaging receivables and selling them to banks or investors, a trend that has strengthened following regulatory changes encouraging direct assignment and pass-through certificate transactions. In addition, equity and quasi-equity funding from IPOs, FPOs, private equity, and venture capital continues to support capital adequacy and growth plans. Public deposits, though limited to deposit-taking NBFCs (NBFC-Ds), contribute a smaller share of funding, having declined under tighter regulatory oversight.

The reliance of NBFCs on bank funding decreased over the last year as the impact of higher risk weight on bank lending to NBFCs played out. Dependence of NBFC-UL on bank borrowings and public deposits was higher than NBFC-ML.

NBFCs continue to rely heavily on bank borrowings and debentures. Banks' exposure to NBFCs grew by 13.6% y-o-y as of March 2024. The share of long-term borrowings in total borrowings rose, while short-term borrowings declined (see Table 2).

Table 2: NBFC Sources of Funds

(in %)

Item Description	NBFC-UL		NBFC-ML		NBFC-(UL+ML)	
	Mar-24	Mar-25	Mar-24	Mar-25	Mar-24	Mar-25
1. Share Capital, Reserves and Surplus	19	18.6	24	24.5	22.8	22.8
2. Total Borrowings	69.1	71.1	67.6	67.5	68	68.5
2(i) Borrowing from banks	30.1	29.9	25	26.4	26.4	25.7
2(ii) CPs subscribed by banks	0.8	0.8	0.8	0.7	0.8	0.8
2(iii) Debentures subscribed by banks	3.5	3.2	2.1	2.1	2.4	2.4
Total from banks [2(i)+2(ii)+2(iii)]	34.4	33.8	27.9	26.4	29.6	28.9
2(iv) CPs excluding 2(ii)	3.2	3.6	1.6	1.7	2.4	2.5
2(v) Debentures excluding 2(iii)	16	16.3	23.7	23.8	21.8	21.6
3. Public Deposits	7.2	6	0.5	0.5	2.1	2.1
4. Others	4.3	4.3	7.9	7.5	7.1	6.6
Total	100	100	100	100	100	100

Source: RBI FSR, June 2024

Institutional Initiatives

The RBI's regulatory framework for NBFCs has shifted increasingly towards a principle-based, proportionate, and consultative approach, with agility to adapt to evolving risks. In recent years, it has rationalised prudential norms for Urban Cooperative Banks, restored risk weights on bank lending to NBFCs as risks eased, and revised priority sector lending (PSL) guidelines to enhance credit flow to underserved segments.

Provisioning requirements on government-guaranteed security receipts were relaxed, while regulations governing Alternative Investment Funds (AIFs), co-lending, non-fund-based facilities, project finance, and gold loans were streamlined. These initiatives highlight RBI's focus on balancing financial stability with growth, while reducing unnecessary regulatory frictions.

Looking ahead, the RBI plans to implement Basel III guidelines on market, credit, and operational risks from April 2027, supported by draft frameworks on credit risk and Expected Credit Loss (ECL). It also intends to finalise the Forms of Business circular, consolidate regulations across categories of entities, and ease the governance burden by confining Board approvals to strategic policies. In parallel, the RBI is examining measures to expand credit to productive sectors and reduce intermediation costs. To ensure regulations remain effective and relevant, a new Regulatory Review Cell will be established to periodically assess each regulation for efficiency, clarity, and responsiveness to emerging risks.

The RBI has issued final guidelines on co-lending arrangements, expanding their scope beyond the earlier framework limited to bank-NBFC partnerships. Under the new norms, co-lending has been extended to all commercial banks (excluding small finance banks), financial institutions, and NBFCs, including housing finance companies. Each participating lender must now retain a minimum of 10% of every loan on its books, compared with the earlier 20% requirement for NBFC originators, thereby enhancing flexibility and promoting capital-efficient growth. For smaller, mid-sized, and digital NBFCs, this move is particularly significant as it allows collaboration with larger NBFCs in addition to banks, creating wider funding avenues and opening opportunities to serve diverse borrower segments such as retail, MSMEs, and consumption credit. The guidelines also mandate the timely transfer of loans within 15 days, uniform classification of stressed assets across lenders, transparent disclosure of co-lending partners, and robust mechanisms for data-sharing and grievance redressal, thereby standardising operations and ensuring borrower protection.

Risks and Challenges

Despite the significant growth and potential of the NBFC sector, it continues to face a host of risks and challenges that need careful management. Asset quality concerns remain prominent, particularly in microfinance and infrastructure financing, while asset-liability mismatches arising from short-term borrowings against long-term lending often trigger liquidity crises.

The sector's higher exposure to riskier borrower segments raises credit risk, and dependence on short-term funding further heightens liquidity vulnerabilities. Regulatory arbitrage, though reduced, persists with differences in capital adequacy and provisioning norms compared to banks, alongside the increasing burden of compliance with governance standards and reporting requirements. Intense competition from domestic and global players, coupled with systemic risks stemming from greater interconnectedness with the financial system, amplifies contagion threats in times of stress. Also, past crises such as IL&FS and DHFL underline the sector's corporate governance weaknesses, while growing digital integration exposes NBFCs to cybersecurity and data privacy risks. Besides these, macroeconomic headwinds including rising interest rates, inflation, and economic slowdown add further pressure on profitability and margins.

Of late, the NBFCs are facing rising stress across unsecured personal loans, credit cards, and microfinance, with early signs of strain also emerging in MSME and vehicle finance segments.

In MSME credit, borrowers holding three to five active loans now account for nearly 22% of the total portfolio, while the portfolio-at-risk (PAR) in unsecured business loans rose by 20 basis points year-on-year. Small-ticket MSME loans (up to ₹1 million) have seen bad loans increase to 5.8% in January 2025 from 5.1% a year earlier, data from CIBIL and Macquarie Capital show.³ Banks too reported a higher concentration of risky borrowers in FY25, with 'not scored' and 'very high-risk' categories forming 10% and 16% of the MSME book, respectively, and PAR for these segments deteriorating to 3.6%. In the unsecured personal loan segment, PAR for 90+ day delinquencies surged to 3.2% by March 2025, compared with just 0.2% a few years ago. With ageing-related provisions adding to pressure, credit costs are expected to rise further in FY26 as stress builds across unsecured portfolios.

The rate cuts of up to 75 basis points in FY26 could provide relief by lowering borrowing costs, particularly for NBFCs with high bank borrowings and fixed-rate loan portfolios. The benefits may be unevenly distributed. Large players such as Bajaj Finance and Cholamandalam Finance have already seen a re-rating due to weaker-than-expected growth in AUM and asset quality, highlighting that margin expansion alone may not guarantee stronger valuations. Mid-sized NBFCs are relatively better placed, but narrowing net interest margins and higher provisioning needs could temper overall profitability.

Muted growth in home and vehicle finance continues to be a drag on overall loan expansion, with risks further amplified by the proposed move to externally benchmark NBFC lending rates. Regulatory changes in this area may compress spreads and increase competition from banks. Although loans against property (LAP) and gold loans remain bright spots, seasonal factors such as extreme weather conditions and election-related disruptions could affect collections and short-term asset quality.

NBFCs are expected to expand their MSME lending by nearly 20% in FY26, outpacing banks and reinforcing their dominance in the micro-LAP space (loans below ₹10 lakh). However, stress in unsecured and microfinance portfolios is spilling over into the micro-LAP segment, where delinquency levels (PAR90+) remain elevated compared to larger LAP exposures. This has translated into higher credit costs and provisioning requirements, putting additional pressure on margins even as growth opportunities remain strong.

Although branch expansion, digital transformation, and co-lending arrangements are expected to support business volumes, these growth drivers come with associated costs. Rising operating expenses, along with higher capital requirements from forthcoming regulatory changes, may moderate profitability in the near term. Operating leverage could offset some of these pressures, but only for players with scale and diversified portfolios.

While NBFCs retain a dominant 45% share in the micro-LAP segment, their position in larger LAP exposures (above ₹10 lakh) is being challenged by private banks, which now command a 42% market share compared to NBFCs' 37%. Sustaining competitiveness will require NBFCs to innovate in product design, pricing flexibility, and customer acquisition strategies, particularly as banks aggressively target the profitable MSME and retail credit markets.⁴

Roadmap Ahead

NBFCs have emerged as one of the strongest pillars of India's financial ecosystem, complementing banks by serving underserved sectors and catalysing inclusive growth. While their rapid growth brings opportunities for deepening credit penetration, it also introduces vulnerabilities that require robust regulation, diversified funding, and strong governance.

Globally, non-bank financial intermediations have shown both the promise of financial innovation and the perils of systemic risk. For India, the challenge lies in learning from these experiences while charting a path that ensures NBFCs remain agile, resilient, and inclusive.

By embracing digital transformation, strengthening governance, and maintaining regulatory vigilance, NBFCs can continue to drive India's journey toward becoming a \$5 trillion economy while ensuring financial stability and inclusion.

The future of NBFCs in India will hinge on balancing growth, innovation, and systemic stability, with multiple opportunities shaping their trajectory. The integration of digital technologies and fintech partnerships has already transformed the sector, with NBFCs increasingly using digital platforms for loan origination, credit scoring, and customer service. Going forward, greater adoption of AI, big data, and blockchain will enhance credit assessment, fraud detection, and operational efficiency, provided compliance with RBI's digital lending norms is ensured.

Diversifying funding sources will be crucial, with NBFCs expected to tap infrastructure bonds, green bonds, insurance sector investments, and securitization markets to secure long-term capital. At the same time, NBFCs are poised to play a vital role in advancing financial inclusion by expanding microfinance, small-ticket lending, and developing innovative credit models tailored for MSMEs, farmers, and informal sector workers, particularly in underserved rural regions. Service diversification will also continue, as NBFCs broaden their offerings across financial products and solutions for individuals and businesses. To expand their reach and strengthen capabilities, NBFCs are likely to deepen collaborations with fintech, banks, and corporates, while a stronger regulatory framework from the RBI will bring tighter liquidity norms and harmonization with banks, reducing regulatory arbitrage. Governance standards are also set to improve with stricter enforcement of board independence, risk management practices, and transparency in asset classification and provisioning.

The global integration will play a role in shaping the sector's future, as well-regulated NBFCs gain access to external commercial borrowings under safeguards and attract greater foreign institutional investment in their debt instruments. Collectively, these drivers position NBFCs to evolve into more resilient, inclusive, and technologically advanced financial institutions in the years ahead.

The NBFC sector in India has grown significantly over the years, driven by increasing demand for credit, diversification of funding sources, and technological advancements. While some risks and challenges need to be addressed, the sector is poised for further growth and innovation, driven by digital transformation, financial inclusion, and diversification of services.

The outlook for the NBFC sector in FY26 is characterized by cautious optimism, balancing growth opportunities with emerging risks. The RBI cut the policy repo rate by 50 bps to 5.50% on June 6, 2025; any further easing is uncertain and will depend on incoming data. This will provide some buffer for net interest margins in the second half of FY26 and into FY27 to some extent. But the slower growth in FY25 indicates that expansion will likely be more measured, driven by prudent risk management and regulatory compliance.

On the upside, NBFCs are well-positioned to benefit from strong demand for MSME credit, with lending in this segment forecasted to grow nearly 20% in FY26. Their leadership in the micro-LAP market and increasing participation in co-lending initiatives with banks emphasize their ongoing role in financial inclusion and last-mile credit provision. Continued demand for LAP and gold loans, combined with innovation in consumer finance and affordable housing offerings, further broadens growth options. Digital transformation, branch expansion, and advanced analytics are boosting operational efficiency and expanding reach, especially in semi-urban and rural areas.

At the same time, several challenges remain. Stress in unsecured personal loans and microfinance portfolios is beginning to affect MSME and micro-LAP segments, pushing up credit costs and requiring higher provisioning. Slow growth in home and vehicle loans, along with the proposed external benchmarking of NBFC lending rates, could further squeeze spreads and margins. Competition from private banks, particularly in larger LAP exposures, is intensifying, urging NBFCs to differentiate through product innovation, customer acquisition tactics, and improved risk management.

Looking ahead, NBFCs must focus on strengthening their liability profiles by diversifying funding sources, accessing capital markets, and utilizing external commercial borrowings, while managing asset risks with solid underwriting standards. Regulatory changes, including the phased adoption of Basel III guidelines by 2027 (as of now for banks only) and the implementation of Expected Credit Loss (ECL) frameworks, will require higher capital buffers and stronger governance. While these measures may impact short-term profitability, they are expected to enhance resilience and investor confidence.

In the medium term, aligning with policy priorities such as MSME development, affordable housing, and green financing will provide NBFCs with growth momentum and regulatory support. The sector's ability to seize these opportunities while managing profitability challenges and rising credit risks will shape its future as a vital pillar of India's financial system.

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