

# A Study on Non-Performing Assets in Selected Non-Banking Financial Companies

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**Abstract:** Non-Banking Financial Companies are integral to Indian economy as they are in a position to provide loans to areas which might not have access to banks or have not been receiving due attention from the banks. Some risks that NPAs have with regard to smooth operation and long-term survival of NBFCs. The risks originating from NPAs on the economical and efficient functioning of an NBFC come in different forms. In this research paper we would like to discuss the reasons of NPAs and the influence that NPAs have on the operations of the Non-Banking Financial Company. Various reasons for NPAs could include lack of rigorous credit appraisal system, over reliance on select few industries and macroeconomic factors.

**Keywords:** Non-Performing Assets, Non-Banking Financial Companies, Asset Quality, Risk Management, Credit Appraisal

## I. INTRODUCTION

### **Non-Performing Assets:**

Non-Performing Assets refers to the loans or advances to which the financial institution has not received either the principal payment or the interest payment to the corresponding loans and advances. It is one such indicator or metric from which we can know that either the borrower is unable to repay the loan or the financial institution has poor or ineffective mechanism. Rising defaults are always a matter of concern in the financial landscape as they shape the destiny of the financial institution and the economy as a whole.

### **Asset Classification:**

- **Standard Asset**
- **Sub-Standard Asset**
- **Doubtful Asset**
- **Loss Asset**

### **Standard Asset**

An asset which does not carry anything more than normal risk. Such an asset shouldn't be treated as Non-Performing Asset.

### **Sub-Standard Asset**

An asset is said to be sub-standard if it remains as NPA for a period less than or equal to 12 months.

### **Doubtful Asset**

An asset is classified as doubtful if it remains as NPA for a period of more than 12 months.

### **Loss Asset**

An asset is classified as loss Asset when it is detected by either of internal auditors or external auditors or RBI inspection but the amount has not been written off, partly or wholly.

### **Non-Banking Financial Company:**

A Non-Banking Financial Company is a financial institution which is registered under the Companies Act 1956, and is regulated by the Central Bank of India. These financial institution plays a supplementary role to the banks by extending credit to individuals/segment which has been underserved by the existing banking infrastructure. These institutions are not permitted to accept demand deposits but can offer various financial services including offering loans and advances, asset financing, hire purchase, leasing etc.

### **Types of NBFCs (RBI Classification):**

- Investment and Credit Company
- Housing Finance Company
- Infrastructure Finance Company
- Infrastructure Debt Fund (IDF-NBFC)

- Core Investment Company
- Micro Finance Institution
- Non-Banking Financial Company – Factors
- Mortgage Guarantee Company
- Standalone Primary Dealers
- Non-Operative Financial Holding Company
- NBFC – Account Aggregator
- NBFC – Peer to Peer Lending Platform

**Investment and Credit Company:**

- It is a type of NBFC which engages in offering loans, asset financing and investment in securities.
- It was formed in 2019 by merging three types of NBFCs namely Loan Company, Asset Finance Company, and Investment Company.
- These NBFCs should maintain a minimum net owned fund of Rs. 2 crore and should comply with the capital adequacy norms.
- Examples include Bajaj Finance, Tata Capital etc.

**Housing Finance Company:**

- Specializes in offering loans for Housing purposes.
- At least 75% of net assets of HFCs must be in housing loans.
- These NBFCs were earlier regulated by NHB and it is now been regulated under RBI.
- These NBFCs aids individual buyers and developers.
- It also supports government initiatives like Pradhan Mantri Awas Yojana (PMAY).
- Examples include LIC Housing Finance, HDFC Ltd etc.

**Infrastructure Finance Company:**

- Provides long term financing for infrastructure projects such as roads, ports, airports, power plants, telecom projects etc.
- In order to be classified as a NBFC an Infrastructure Finance Company must:
  - Have a minimum net owned fund of Rs. 300 Crore
  - Credit Rating of A or equivalent
  - 75% of funds deployed in infrastructure loans.
- Power Finance Corporation Ltd, Rural Electrification Corporation Ltd are examples of Infrastructure Finance Company.

**Infrastructure Debt Fund (IDF-NBFC):**

- Funds infrastructure projects through long-term debt with a focus on PPP projects post construction.
- The role of these NBFCs is to provide stable long-term financing for infrastructure projects reducing dependence on banks.
- Their aim is to attract long term investors like insurance companies and pension funds to finance infrastructure projects which require large sums and extended repayment periods.
- Examples include India Infrastructure Finance Company Ltd, GMR Infrastructure Debt Fund NBFC Ltd etc.

**Core Investment Company:**

- Primarily holds shares and investments in group companies.
- It does not engage in lending or trading like other NBFCs.
- It acts as a holding company within a corporate group.
- These NBFCs are essential for conglomerates managing group level investments.
- They must hold:
  - At Least 90% of its investment in group companies.
  - At Least 60% must be in equity shares.
- Examples include Tata Sons Ltd, Aditya Birla Capital Ltd etc.

**Micro Finance Institution:**

- These NBFCs plays a crucial role in ensuring financial inclusion.
- Provides small loans and other financial services to low-income individuals or groups.
- They aim to cater the needs of individuals who lacks access to traditional banking.
- They usually operate in rural and semi urban areas empowering women and small entrepreneurs.
- Examples include Ujjivan Financial Services, Equitas Microfinance Ltd etc.

**Non-Banking Financial Company – Factors:**

- These NBFCs provides liquidity to businesses by purchasing receivables at a discount rate.
- At least 50% of its assets must be in factoring.
- This helps businesses manage their cash flow.
- It is regulated by RBI under the Factoring Act, 2011.

- Examples include SBI Global Factors Ltd, Canbank Factors Ltd etc.

**Mortgage Guarantee Company:**

- Provides guarantees to lenders with at least 90% of turnover from this activity.
- They lessen risk for housing finance lenders by assuring repayment in case of borrower default.
- India Mortgage Guarantee Corporation is an example of this kind.

**Standalone Primary Dealers:**

- They deal in government securities, underwrite auctions and act as market makers by providing liquidity in the secondary market.
- Their funding sources include borrowing from RBI, banks, issuing commercial papers and engaging in repo transactions in government securities.
- Like other NBFCs they don't engage in traditional banking activities.
- Their primary role is develop and deepen the government securities market.
- STCI Finance Ltd is an example of this kind.

**Non-Operative Financial Holding Company:**

- It is a special type of holding company structure introduced by RBI to ensure that new banks promoted by large business groups remain guarded from their non-financial businesses.
- It was first mandated in RBI Guidelines for Licensing of New Banks in the Private Sector (2013).
- The idea is to bring all regulated financial services of a promoter group under one entity for better oversight.

**NBFC – Account Aggregator:**

- Combines financial data from various institutions and shares it with user content.
- They provide a unified view of financial assets like bank accounts, investments and insurance.
- It helps individuals and businesses with financial planning and credit assessment.
- Examples include CAMS Finserv, Finvu etc.

**NBFC – Peer to Peer Lending Platform:**

- It is an online platform that directly connects lenders and borrowers.
- They cannot lend or borrow themselves and are subject to strict transparency norms like exposure limits for lenders and borrowers.
- A Lender can lend up to Rs.50 Lakhs and a borrower can borrow up to Rs.10 Lakhs.
- The credit issued are usually unsecured and may range for a span from 3 months to 36 months.
- Examples include Faircent, Lendbox etc.

## II. NEED FOR THE STUDY

The study is important due to the growing need for NBFCs in Indian financial system and various problems faced by them regarding maintenance of asset quality. NPAs carry severe threat to their profitability, liquidity and existence. Thus, an investigation has become crucial to find out the causes for its growth, trend and effect on NBFCs. The existence of NPAs poses a serious threat to the existence, profitability and liquidity of NBFCs.

Hence a study has become inevitable to analyse the causes of its increasing trend and impact on NBFCs. It helps to explore the deficiencies in credit appraisal, risk management practices and prudential supervision of NBFC.

## III.OBJECTIVES OF THE STUDY

- To assess the rate of Non-Performing Assets in Non-Banking Financial Companies.
- To analyze the NPAs in MSME loans given by NBFCs.
- To identify the factors that contribute to NPAs in NBFCs.
- To study the impact of NPAs and how it affects the NBFCs performance.
- To suggest the potential solutions to prevent NPAs in NBFCs.

## IV.SCOPE OF THE STUDY

- The study emphasizes on analyzing the causes and impacts of NPAs in NBFCs.
- It analyses the level and growth of NPAs in Select NBFCs.
- It focuses on NPAs in MSME loans within selected NBFCs.
- It examines the effectiveness of recovery practices adopted by NBFCs.
- It recommends possible ways decrease the level of NPAs.

**V.REVIEW OF LITERATURE**

**Sandesh Singh, Dipasha Sharma (2026)** argues that machine learning models can provide early warning signals by analyzing complex, non linear relationships. The dataset includes financial ratios, asset quality indicators, liquidity measures and macroeconomic variables. NPAs are the strongest predictors of instability, directly affecting liquidity and profitability. The liquidity mismatch can be detected early using ML models. Predictive analytics can help regulators and NBFCs to adopt preventive measures such as stricter credit appraisal, diversifying funding sources. The authors also caution that ML models should complement but not replace human judgment.

**Gaurav Kumar, A.V.N. Murty, Srinivas Ravi Kumar Jeelakarra, S. Ganapathy, Savitha G.R. (2025)** emphasizes on the funding models and asset structures of NBFCs which leads them to liquidity risk. NBFCs highly rely on capital markets and wholesale borrowings. The risk also arises due to the mismatch. This mismatch occurs because they borrow for short term but lend for long term and it happens especially in housing and infrastructure finance. Rising NPAs reduce cash flows affecting liquidity. Defaults in real estate, MSMEs and consumer loans pose a threat to liquidity. NPAs not only reduce profitability but also restricts refinancing options. The results from the econometric model confirm that NPAs and funding dependence are the major determinants of liquidity stress.

**Dhruv Kumar Parmar (2025)** begins by explaining the role of NBFCs in addressing the underserved segment by the traditional banks. The author also describes how NBFCs and banks get differ from and they do in terms of regulatory structure, funding sources & lending practices. The study also reveals that metrics such as Net Interest Margin, Return on Assets, Return on Equity can be used to determine the financial performance of NBFCs. It also highlights the IL & FS crisis, which actually opened up the flaws in risk management and regulatory measures. The authors also warn NBFCs to have stricter oversight mechanisms to prevent NPAs. It also shows how NBFCs have played their part by contributing to sectors like housing finance, vehicle loans and microfinance.

**Dr. B. Paramesha (2024)** provides a clear roadmap by illustrating right from the historical background of NBFCs the committee's constituted to review the current framework of NBFCs. This study gives a brief note about the types of NBFCs, recent regulations framework to NBFC by RBI, challenges faced by NBFCs in India including NPAs. For analyzing the debt and recovery challenges faced by NBFCs, the author made use of five selected NBFCs.

**Priyata Chaudhury & Ashish Kumar Sana (2024)** examines the performance of NBFCs that were listed on BSE. The authors made use of ratio analysis such as Return on Assets (ROA), Return of Equity (ROE), Net Interest Margin, Debt-Equity Ratio. This paper states that NPAs significantly affect the performance of NBFCs. Firms with greater NPAs witness lower profitability and solvency. The authors also view transparency in NBFCs as a competitive advantage.

**M. Jayasree, G. Thirumurugan (2023)** conducted a five-year analysis (2018-2022) among selected NBFCs with a focus on Assets Under Management for measuring financial strength. The authors made use of CAMEL model for assessing the performance of NBFCs. NBFCs with high capital buffers are strong enough to combat liquidity shocks. Poor Asset Quality i.e. rising NPAs weakens balance sheet, erodes investor confidence and reduces interest income. The study also evaluated the efficiency of management by taking into account operating expenses and cost to income ratio. It revealed that profitability was affected by NPA levels. NBFCs dependence on short term borrowings calls for robust liquidity management.

**Dr. Rita Khatri, Prof. Arti Modi (2022)** studies the performance of NBFCs before and after COVID. Pre-COVID tenure showed profitability and expansion. The paper points out the structural drawbacks such as dependance on short term borrowings and wholesale weaken liquidity. The pandemic created challenges such as reduced demand for loans and increasing defaults. The uncertainty that existed during the pandemic led to a significant rise in NPAs. The loan moratorium and liquidity support schemes provided by the government was a short term relief. The study shows that profitability indicators such ROA & ROE were declined post COVID.

**Prof. Karam Pal Narwal, Mansi Anand, Simran Arya (2022)** states that NBFCs and DFIs act as a complementary institution in the financial landscape. NBFCs provide retail and niche lending while DFIs provide industrial and infrastructural finance. The paper analyses the interrelations of NBFCs and DFIs through funding flows, asset exposures and borrower linkages. A key issue faced by these institutions is NPA and when borrower default these institutions face a severe setback. The authors argue that this interconnectedness can be beneficial when managed well. It also highlights that regulatory oversight is weak for NBFCs in comparison with DFIs and banks and also highlights the need for policy reforms.

**Yasmeen Khan, K.S. Thakur (2022)** cites the role of microfinance institutions in catering the needs of low-income households, women and rural borrowers. The study highlights that repayment is one of the most prominent challenge faced by MFIs before COVID-19 and it was due to borrower default and weak credit appraisal. The pandemic created a significant rise in NPAs. They also faced challenges with regard to liquidity as collections dropped. As household income dwindled because of the economic downturn during pandemic, it eventually resulted in a sharp rise in NPAs. However, there were support measures such as liquidity support scheme which were not enough to address the repayment crisis in a long run.

**Sundar R, Dr. Sapna Singh, Prof. (Dr.) Mohit Gangwar (2021)** argues that weak credit appraisal mechanisms such as inadequate verification of income, employment stability or repayment capacity leads to higher NPAs. NPAs can be prevented if NBFCs strengthen their pre loan processes. The study reveals that absence of formal credit history among rural borrowers make credit appraisal ineffective. Approaches like alternative credit scoring, community references can improve accuracy. The study recommends NBFCs to adopt standardized pre loan assessment frameworks supported by technology and regulatory oversight.

**Sugandha Jain (2021)** describes shadow banking as activities carried outside the traditional banking system particularly by NBFCs. The study acknowledges the role of NBFCs in addressing the underserved segment. It grew rapidly due to regulatory arbitrage, faster loan approval and innovative lending models. NPAs are a serious concern in NBFCs because of exposure to risky sectors like real estate and infrastructure. The paper also shows a comparison between shadow banks and traditional banks, where shadow banks tend to have weaker regulatory oversight than the latter. The study notes that governance as a key to manage NPAs, when the governance practices are not up to the mark they can contribute NPAs.

**Rajeswari Sengupta, Lei Lei Song, Harsh Vardhan(2021)** describes the role of NBFCs in Indian financial system. They cater the needs of small businesses, infrastructure projects and retail borrowers. The IL & FS crisis exposed the flaws in their model and also reduced lending. The study also reveals the interconnectedness of NBFCs with banks and capital markets. After the crisis there was a significant surge in NPAs in particularly in real estate and infrastructure lending. The pandemic and moratorium led to rising NPAs and weakened their financial health. The authors call for more improved regulation and risk management.

**Priyajit Ray (2021)** cites the importance of NBFCs in the economy as banks tightened lending. The study explains that pandemic was a powerful driver for NPAs and it was due to the job loss, business closures and reduced income levels. The pandemic also resulted in the decline of profits, slowdown of loan disbursements, weakened recovery and so on. In spite of these constraints, NBFCs continued to serve the untapped segment. Rising NPAs and liquidity issues restricts the access to funds for NBFCs and poor credit ratings.

**Pampa Jana (2021)** credits the growth of NBFCs in contributing to GDP by funding infrastructure, housing and others. The author credits their role in aiding entrepreneurship and rural development. The study also reveals that NBFCs face growing NPAs due to exposure towards risky segments like real estate and small enterprises. The author calls for enhancing governance and focus on addressing NPAs to ensure stability.

**Dr. P. Kalyani, Dr. T. Suchitra Rani, P. Shanmuk Yadav (2021)** evaluates the profitability of select NBFCs using financial data (determinants). The firms with stronger capital adequacy ratio are more profitable. NPAs weaken profitability by cutting down interest income. NBFCs which has better credit appraisal mechanisms show stronger performance. Firms with strong liquidity are about to overcome challenges and sustain profitability. The paper also accounts that NBFCs with diversified portfolios are more profitable. NPAs too rise as a result of excessive leverage.

**Mrudula Malankar & Dr. Smita Jape (2021)** studies the impact of NBFC crisis and how they reshape financial landscape. NBFCs were growing rapidly and was filling the gap left out by traditional banks. This paper showcase that credit rating agencies underplayed in assessing and identifying risks. They also provide empirical evidence which reflect decline in profitability, rising NPAs after the crisis. This paper also highlights the need for stronger internal controls and prudent lending practices.

**Joseph Antony P & Dr. D. K. Maheswari (2021)** analyses the performance of NPAs among leading NBFCs for the period 2011-2015 in India. The authors used statistical tools such as Spearman's rank correlation, trend analysis etc. to analyze the performance. During that period Muthoot Finance has a comparatively good revenue generation capacity.



**Joseph Antony P & Dr. Vinita Mittal (2021)** this paper is a detailed investigation into the examination of NPAs in NBFCs for the period 2016-2020. This study highlights the objectives, growth and types of NBFCs along with the formal definition, causes, norms related to NPAs and categories of NPAs which gives immense detail in an easier form.

**Dr. P. Govindaraj & N. Gopalsamy (2020)** examined the performance of NBFCs in disbursing MUDRA loans. The study shows that NBFCs are issuing MUDRA loans at a rapid phase in comparison to public sector banks. Following the liquidity crisis which arose as a result of the bankruptcy of IL & FS, NBFCs saw a dip in disbursement. Further, it states that there is no solvency issue but disbursement became slower in NBFCs. Later, NBFCs saw a 68% rise in NPAs. The Parliament standing committee recommended the commencement of new refinance institution for NBFCs to ease their liquidity stress.

**S.R. Shah, D.Y. Chacharkar (2020)** highlights the role of NBFCs and states the benefits of NBFCs such as flexibility, quick loan disbursements, and their reach towards the rural and semi urban areas. Rising NPAs in NBFCs particularly in real estate and infrastructure lending, reduce their profitability and erodes public confidence. NBFCs are more vulnerable to asset quality issues because of weaker regulatory oversight and dependence on short term financing.

**Haareca Chintala (2020)** begins by regarding the support of NBFCs in complementing banks and identifies the key challenges faced by them. They include liquidity constraints, reliance on wholesale funding, regulatory gaps and rising NPAs. The paper highlights that besides these challenges governance and transparency also remain as a serious concern for NBFCs. The study emphasizes on the co-origination of loans framework introduced by RBI. The analysis detected challenges in it such as differences in risk appetite, credit appraisal standards and operational processes. Despite these challenges this co-origination has an ability to expand credit, reducing costs for NBFCs and improve financial inclusion.

**Riya Regmi, Poornima Kukreti (2019)** examines the IL & FS crisis. It led to liquidity shortages among NBFCs as they were unable to refinance short term borrowings due to the panic of debt markets. Increasing NPAs in real estate and MSME lending degraded the crisis, reducing cash inflows and eroding investor confidence. The Government and RBI interventions such as liquidity support schemes, partial credit guarantees were introduced to stabilize NBFCs. These interventions stabilized short term liquidity but did not solve structural issues.

## **VI. RESEARCH METHODOLOGY**

### **Research**

Research is a systematic and structured process of inquiry aimed at discovering, interpreting, and revising facts, events, behaviors or theories. It involves the collection, analysis and interpretation of data to enhance knowledge and understanding across various disciplines. It is the creation of new knowledge in a new and creative way so as to generate new concepts and methods.

### **Research Design**

#### **Descriptive Research**

It is a research method describing the characteristics of the phenomenon being studied. It focuses more on “what” of the research subject than the “why” of the research subject. It predominantly makes use of quantitative data.

### **Data Sources**

The entire study is carried out with the help of secondary data.

The major source of the data for this study is annual reports of the select NBFCs and RBI Website (FAQ's).

The Select NBFCs taken for the study include:

Bajaj Finance Limited

Ugro Capital Limited

Mahindra Finance

IIFL Finance

Manappuram Finance Limited

### **Data Analysis tools**

#### **Trend Analysis**

Trend Analysis is a statistical approach to identifying patterns or changes in data over time. It is used to help predict future business dynamics and inform decision making.

**Correlation**

Correlation is a statistical technique used for measuring the relationship or interdependence of two or more variables and how strong and in what direction two variables are linked. It is a basic measure of the strength of the relationship between two variables.

$$r_{xy} = \frac{n \sum x_i y_i - \sum x_i \sum y_i}{\sqrt{n \sum x_i^2 - (\sum x_i)^2} \sqrt{n \sum y_i^2 - (\sum y_i)^2}}$$

**Regression**

Regression is a statistical method used to estimate relationships between a dependent variable and one or more independent variable. It allows to predict or explain the variation in one variable based on another variable.

$$Y = a + bx$$

$$a = \frac{[(\sum y)(\sum x^2) - (\sum y)(\sum xy)]}{[n(\sum x^2) - (\sum x)^2]}$$

$$b = \frac{[n(\sum xy) - (\sum x)(\sum y)]}{[n(\sum x^2) - (\sum x)^2]}$$

**Exponential Moving Average**

An Exponential Moving Average that places greater emphasis on recent data points, making it more sensitive to recent changes than simple moving average.

$$EMA = (\text{Value} * \text{Smoothing Factor}) + (\text{EMA Previous Year} * (1 - \text{Smoothing Factor}))$$

**Impact of NPAs in NBFCs and how it affects the performance of NBFCs****Impact of NPAs in NBFCs:**

- **Reduced Profitability:**  
When loans become NPAs, NBFCs stop generating interest income on them. Moreover, they are required to make provisions for these unrecovered loans, which directly reduces net profit.
- **Lack of Liquidity:**  
Higher NPAs lock funds in unrecovered loans, thereby reducing the availability of funds in hand for the fresh issue of new loans to borrowers affecting the entire the growth and operation of NBFCs.
- **Increased cost of funds:**  
When asset quality worsens as a result of growing NPAs, lenders may view NBFCs as riskier, thereby NBFCs face hurdles with regard to raising funds from external parties to facilitate the workflow.
- **Credit Rating and Investor Confidence:**  
The credit rating of NBFCs get downgraded as a result of rising NPAs which eventually reduces the trust and confidence of investors and which in turn affects the entire operation of NBFCs. It also reduces the share prices of the NBFCs to fall in the market significantly affecting the value of NBFCs.
- **Lending Policy:**  
As a result of surge in NPAs, it creates the need for introspection of NPAs into their lending policies. To combat and withstand such a situation they are in a need to revamp their lending policy and make it stricter as compared to the earlier one.
- **Regulatory Action:**  
High level of defaults requires effective management and oversight. It thereby makes RBI to step in have a robust oversight over the operations of NBFCs.

**VII. How NPAs affect performance metrics?****➤ Net Interest Margin:**

It measures the difference between interest income generated from lending and interest paid on borrowings relative to the earning assets.

$\text{Net Interest Margin (NIM)} = \frac{\text{Interest Income} - \text{Interest Expense}}{\text{Average Earning Assets}} \times 100$

It falls significantly when interest is not received from bad loans while interest expense for borrowing continues.

**➤ Return on Assets and Return on Equity:**

Return on Assets is a profitability ratio that measures how efficiently an institution uses its assets to generate income.

$\text{Return on Assets (ROA)} = \frac{\text{Net Income}}{\text{Total Assets}}$

Return on Equity is a profitability ratio that measures how effectively an institution generates profit from the money invested by its shareholders.

$\text{Return on Equity (ROE)} = \frac{\text{Net Income}}{\text{Shareholders Equity}}$

High NPA levels have a strong negative correlation with ROA and ROE indicating poor asset utilization and reduced return to shareholders.

**➤ Provisioning Coverage Ratio:**

Provisioning Coverage Ratio measures how well a financial institution has set aside funds to cover potential losses from NPAs.

$\text{Provisioning Coverage Ratio (PCR)} = \frac{\text{Total Provisions}}{\text{Gross NPAs}} \times 100$

It increases as the NBFC is forced to make higher provisions for sub-standard and doubtful assets.

**VIII. CONCLUSION**

The NBFCs are indispensable part of the credit delivery mechanism. The increasing trend of NPAs of the NBFCs poses a risk to the system stability and growth. Additional risk has been introduced into the system by extending credit in few really vulnerable sectors such as real estate & infrastructure sectors. The increased level of supervision, good quality of credit appraisal and good technology-based surveillance will reduce the system risk. The survival and further growth of the system require balanced development between extension of credit and prudent risk management policies.

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