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Exploring the Impact of Capital Structure on the Financial Resilience of NBFCs in India

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ABSTRACT:

Non-Banking Financial Companies (NBFCs) play a critical role in the financial ecosystem, providing financial services and products that complement the operations of traditional banks. NBFCs specialize in offering loans, asset financing, leasing, and investment solutions, catering to sectors and individuals often underserved by banks. This paper explores the evolution, performance, and challenges faced by NBFCs, with a focus on their contribution to economic growth and financial inclusion in India.

Key areas discussed include risk management practices, capital structure, funding sources, and the impact of regulatory changes. The study also examines the implications of recent crises in the NBFC sector, such as liquidity constraints and defaults, on the broader economy. Furthermore, it evaluates the sector's adoption of sustainability and corporate social responsibility (CSR) initiatives to align with global standards.

The findings underscore the need for robust regulatory frameworks, diversified funding mechanisms, and innovative risk management strategies to ensure the sector's resilience and sustainability. The paper concludes with recommendations for strengthening NBFCs' role in driving inclusive economic development and addressing emerging challenges in a dynamic financial landscape.

This abstract serves as a foundation for deeper exploration of NBFC-related research topics, including performance evaluation, service quality, and the impact of macroeconomic factors.

KEY WORDS: Non-banking, NBFC's, Micro finance, Asset financing, Risk, Financial inclusion.

INTRODUCTION:

Non-Banking Financial Companies are financial companies which performs like banks but they are not actual bank. These types of financial companies have to be registered under Companies act,1956. These financial companies engage in the business of financial loans and advances, acquisition of securities/bonds/debentures which are issued by Government or local authority or the marketable securities of a like nature, leasing, hire- purchase, insurance business, chit business but does not it do not include whose prime principal business is that of agricultural activity, industrial activity, purchase or sale of any goods.

A Non-Banking Financial Companies have head business of accepting stores under any plan or course of action in one singular amount or in portions by method for commitments or in some other way, is additionally a non-banking budgetary organization. NBFCs gainered the attention of the Reserve Bank of India ('RBI') when several depositors lost their money, during the failure of several banks in the late 1950s and early 1960s. In order to prevent the large number of depositors, RBI initiated regulating them by introducing Chapter IIIB in the Reserve Bank of India Act, 1934.

In March 1996, there were around 41,000 NBFCs in India and they were not recognized as a separate class. However, due to the failure of some of the institutions the regulatory structure along with the reporting and supervision was constricted by RBI. In the late 90s, sweeping changes were brought to protect the interest of depositors and ensuring the desired functioning of NBFCs. The capital requirement was changed in the year 1999, NBFCs getting registered on or after the issuance of notification dated April 21, 1991 were required to have the minimum net owned funds of 200 lakhs in order to commence the business of an NBFC. Due to snowballing trend in the sector and to ensure the growth of the sector in a healthy and efficient manner various regulatory measures were taken for identifying the systemically important companies and bringing them under the austere norms.

The NBFC-ND with asset size of 100 crores or more were considered to be systemically important companies. During the FY 2011-12, two new categories of NBFCs were introduced viz., IDF and MFI.

DEFINITION given by (Reserve Bank of India):

The Reserve Bank of India (RBI) defines a Non-Banking Financial Company (NBFC) as a financial institution registered under the Companies Act, 2013, which primarily engages in financial activities but does not hold a banking license. Specifically, the RBI states that an NBFC is a company:

1. **Engaged in Financial Activities**: NBFCs carry out activities related to lending, asset financing, investment in securities, and other financial services. They offer various banking-like services but cannot accept demand deposits (e.g., savings or current accounts).
2. **With Key Financial Thresholds**: According to the RBI, a company is classified as an NBFC if its financial assets constitute more than 50% of its total assets, and income from financial assets exceeds 50% of its total income. This is known as the **"50-50 test"** for NBFC classification.
3. **Distinct from Banks**: Unlike banks, NBFCs do not have the authorization to issue cheques drawn on themselves, and they do not participate in the country's payment and settlement systems.
4. **Regulatory Oversight**: While not as strictly regulated as banks, NBFCs are subject to various regulatory requirements under the RBI Act, 1934. The RBI monitors NBFCs to ensure financial stability, particularly focusing on capital adequacy, liquidity, and risk management.

Types of NBFC's:

- **Asset Finance Companies (AFCs)**

AFCs specialize in financing physical assets such as vehicles, machinery, and equipment, catering mainly to businesses and individuals who need financing for asset acquisition.

- **Loan Companies (LCs)**

Loan companies provide a broad range of credit options, including personal loans, corporate loans, and mortgage financing, servicing various consumer and business segments.

- **Investment Companies (ICs)**

Investment companies focus on managing and investing funds in securities, such as stocks, bonds, and other assets, providing returns to their investors through dividends and capital gains.

- **Microfinance Institutions (MFIs)**

MFIs offer small loans to low-income individuals or groups, particularly in rural areas, often for income-generating activities. They play a critical role in financial inclusion and poverty alleviation.

- **Infrastructure Finance Companies (IFCs)**

IFCs focus on financing large-scale infrastructure projects such as highways, ports, and energy production. They are essential in supporting national infrastructure development.

- **Housing Finance Companies (HFCs)**

HFCs provide financing options specifically for residential housing projects, aiding individuals and developers in funding home purchases and construction projects.

ROLE OF NBFC's:

Non-Banking Financial Companies (NBFCs) play a vital role in the financial sector by filling gaps left by traditional banks and supporting economic growth and financial inclusion. Here's a look at the key roles NBFCs play in the financial system:

1. Supporting Financial Inclusion

- Serving the Underserved: NBFCs target market segments that are often underserved by banks, including rural populations, small businesses, low-income households, and informal sectors. They provide financial access to those who may not qualify for traditional banking services.
- Microfinance and Small Loans: Through microfinance and other small loan programs, NBFCs enable low-income individuals and small businesses to meet their financial needs, fostering economic participation and financial independence.

2. Driving Economic Growth

- Credit Support for SMEs: NBFCs play a critical role in financing small and medium- sized enterprises (SMEs), which are essential to economic growth and job creation. By providing tailored financing options, NBFCs support entrepreneurship and industrial growth.

- Infrastructure Development: Many NBFCs, especially Infrastructure Finance Companies (IFCs), specialize in financing large infrastructure projects, including transportation, energy, and urban development, thereby directly contributing to economic development and modernization.

3. Enhancing Credit Availability

- Alternative Credit Channels: NBFCs offer diverse credit options, expanding the overall credit ecosystem. Their flexible credit offerings, including personal loans, vehicle financing, housing loans, and equipment leasing, address various financial needs.
- Flexible and Niche Financing Options: NBFCs offer greater flexibility in lending criteria, terms, and repayment options, often focusing on niche financing markets such as housing finance, vehicle loans, and retail finance, which are not always a priority for banks.

4. Promoting Innovation in Financial Services

- Customized Financial Products: NBFCs are known for developing specialized products tailored to specific customer needs, such as agricultural loans, short-term business loans, and customized asset-financing products.
- Digital and Technological Advancements: Many NBFCs have embraced technology, including digital lending platforms, mobile applications, and online loan management tools, making their services more accessible, user-friendly, and efficient. Their digital- first approach, particularly among FinTech NBFCs, has led to faster loan processing and enhanced customer experience.

5. Fostering Competition in the Financial Sector

- Alternative Financing Options: NBFCs increase competition in the financial services market, offering an alternative to banks and other traditional lenders. This competition drives innovation and keeps lending rates competitive, benefiting consumers and businesses alike.
- Collaboration with Banks: Some NBFCs collaborate with banks to co-lend, share customer bases, or provide services like loan origination for banks. This collaboration helps banks reach a broader market and promotes a more integrated financial ecosystem.

6. Reducing Systemic Risk

- Diverse Financial Model: The NBFC model diversifies the financial system by reducing the concentration of credit risk within traditional banks. NBFCs help distribute credit across the financial system, thus minimizing risks associated with heavy dependence on a single sector.
- Stabilizing Rural Economies: By extending credit and financial services to rural areas and agriculture-related businesses, NBFCs support local economies and reduce financial volatility in these regions. This stabilization is essential, especially in emerging economies where rural financial access is often limited.

7. Contributing to Capital Market Development

- Investment in Securities: Many NBFCs engage in investments in bonds, stocks, and other capital market instruments, which contributes to capital market growth. Their presence adds liquidity to the market and allows for a more dynamic investment environment.
- Debt Instruments and Bonds: Some NBFCs raise funds by issuing debt instruments and bonds, adding diversity to the financial instruments available to investors and providing funding options for institutional and retail investors.

8. Facilitating Government Initiatives and Economic Policy

- Supporting Financial Inclusion Programs: Many NBFCs align with government policies aimed at financial inclusion, poverty reduction, and rural development. They actively participate in initiatives like the Pradhan Mantri Mudra Yojana, promoting credit access for micro and small enterprises.
- Boosting Formalization of the Economy: By extending credit to informal sector businesses and promoting financial awareness, NBFCs help bring businesses into the formal economy, facilitating growth, tax collection, and better regulatory oversight.

FUNCTIONS OF NBFC's:

1. Providing Credit and Loans

- Retail and Consumer Loans: NBFCs provide personal loans, vehicle loans, and loans for consumer durables. This makes them accessible to a wide range of customers, including individuals who may not meet bank criteria.
- Business Loans and SME Financing: Small and medium-sized enterprises (SMEs) often turn to NBFCs for financing, as NBFCs offer more flexible lending terms and quicker loan processing.
- Microfinance Services: NBFC-MFIs (Microfinance Institutions) provide small loans to low-income individuals, particularly in rural areas. These loans support self- employment, agriculture, and small businesses, promoting financial inclusion.

2. Asset Financing and Leasing

- Vehicle and Equipment Financing: NBFCs play a significant role in financing assets like vehicles, machinery, and equipment for both individual and business use. This service is crucial for businesses needing equipment without full upfront costs.
- Leasing Services: Some NBFCs provide leasing options for equipment and machinery. This allows businesses to use essential assets without the need to purchase them outright, which aids in cost management and flexibility.

3. Infrastructure and Project Financing

- Long-Term Infrastructure Loans: NBFCs, especially Infrastructure Finance Companies (IFCs), specialize in financing large infrastructure projects such as highways, airports, and power plants. By doing so, they support national development and modernization.
- Project-Based Financing: NBFCs provide project financing for large, capital-intensive projects by assessing the projected cash flows and viability of the project rather than the credit history of the borrower.

4. Investment in Securities and Capital Markets

- Investment Companies: NBFCs invest in shares, debentures, bonds, and other securities, adding liquidity to the capital markets and providing returns for their investors.
- Portfolio Management Services: Some NBFCs offer portfolio management services to individual and institutional investors, managing investments on their behalf and generating returns through capital appreciation or dividends.

5. Housing Finance

- Home Loans: Housing Finance Companies (HFCs), a subset of NBFCs, provide loans for purchasing residential property, aiding individuals and families in homeownership.
- Construction and Real Estate Financing: HFCs also finance developers for real estate projects, supporting the housing and real estate sectors' growth.

6. Wealth Management and Advisory Services

- Financial Advisory: NBFCs offer financial advisory services, guiding clients on investments, retirement planning, tax planning, and wealth management.
- Insurance and Mutual Fund Distribution: Some NBFCs act as agents or distributors for insurance and mutual fund products, helping clients diversify their financial portfolios.

7. Money Transfer and Payment Services

- Payment and Remittance Services: Some NBFCs offer remittance and payment services, particularly benefiting individuals who need to transfer money across different regions.
- Bill Payments and Prepaid Instruments: In partnership with other institutions, some NBFCs provide electronic payment facilities, like prepaid instruments and digital wallets, facilitating payments and bill settlements.

8. Microfinance and Rural Development Services

- Micro-Credit Programs: Through microfinance institutions, NBFCs provide small loans to rural entrepreneurs, artisans, and farmers, fostering rural economic development and self-employment.
- Agricultural and Rural Lending: NBFCs support rural development by offering loans for agricultural purposes, like buying seeds, equipment, and fertilizers, which aid in increasing productivity and improving rural livelihoods.

9. Risk Management and Insurance Services

- Credit Insurance: Some NBFCs provide credit insurance, protecting borrowers against default and ensuring lenders receive payments.
- Risk Management Services: NBFCs offer advisory and support for risk assessment and management, helping businesses develop strategies to mitigate operational and financial risks.
- Promoting Financial Inclusion Reaching Unbanked Populations: By providing services to low-income and underserved sectors, NBFCs facilitate financial inclusion. They offer products with simpler eligibility criteria, reaching individuals without access to traditional banking.
- Customized Financial Products: NBFCs develop financial products tailored to meet specific needs, such as agriculture loans, seasonal loans, or small-ticket loans for rural customers.

10. Co-Lending and Partnership with Banks

- Co-Lending Arrangements: NBFCs often partner with banks through co-lending models to serve broader customer bases, pooling resources to offer more substantial loans or serve higher-risk markets.

- Providing Specialized Services: NBFCs sometimes originate loans that are financed by banks, allowing them to act as intermediaries and extending banks' reach into markets where NBFCs have specialized knowledge.

DIFFERENCE BETWEEN BANKS AND NBFC's:

TOP NBFC's in INDIA:

REVIEW OF LITERATURE:

- The literature on Non-Banking Financial Companies (NBFCs) highlights their significant role in bridging financial gaps, particularly in emerging economies. Studies emphasize NBFCs' contributions to financial inclusion by providing accessible credit to underserved populations, especially in rural and semi-urban areas. Researchers also note NBFCs' flexibility and innovation in offering specialized financial products such as microfinance, asset financing, and SME loans, which are often not prioritized by traditional banks.

Additionally, literature underscores the regulatory challenges NBFCs face, balancing growth with risks associated with credit quality and liquidity. Scholars have also examined NBFCs' resilience and adaptive strategies in response to economic fluctuations and regulatory reforms, underscoring their evolving importance within the financial sector.

- Priyata chaudury is her article states as, how reserves, loan disbursements, cost-income ratios, total assets, and equity impact profitability in Indian NBFCs from 2001 to 2023. Using Fixed Effects Panel Regression, the findings reveal that high reserves relative to loans disbursed negatively affect profitability, as NBFCs reduce lending to maintain liquidity, cutting interest income. Additionally, larger asset sizes correlate with lower profitability, indicating poor asset quality or low-income-generating loans in risky sectors like housing and infrastructure, which undermines NBFCs' profitability.
- Roshan raj Prajapati is his study examines the financial performance of selected NBFCs from 2017 to 2021, focusing on metrics like Earnings per Share, Net Profit, Debt to Equity, Return on Equity, and Price to Earnings Ratio. Using SPSS v20 for trend and correlation analysis, the findings show that Muthoot Finance and Bajaj Finance performed well, supporting company growth and enhancing shareholder wealth during the period analyzed.
- Dr. K. P. Venugopal rao states in study as examines the profitability of deposit-taking NBFCs (NBFC-Ds) in India from 2012 to 2022, focusing on company-specific and macroeconomic factors. Using panel data regression with a fixed effects model on six listed NBFC-Ds, it finds that operating revenue, cash flow from financing activities, debt- equity ratio, and lending rates significantly impact profitability, with debt-equity ratio negatively affecting it. The study recommends increasing operating income and restructuring liabilities to improve profits, offering insights valuable to financial professionals and analysts.

- Abhyuday Harsh states in study as, NBFIs have become crucial in global finance, expanding rapidly post-crisis. In India, NBFCs primarily bridge lenders and borrowers, though recent growth and interconnectedness have prompted regulatory updates. By December 2022, the NBFC sector showed double-digit balance sheet growth, maintaining strong capital buffers despite slight profit moderation. The pandemic spurred digital service adoption, presenting both opportunities and challenges for NBFCs.
- Kavita Chavali in her study states that explores the capital structure of Indian NBFCs and its impact on profitability from 2006 to 2016, analyzing 23 finance companies listed on the NSE. Using correlation analysis, it examines the relationship between capital structure and metrics like Net Profit, Return on Capital Employed, Return on Equity, Return on Assets, and Interest Coverage Ratio. The study highlights NBFCs' growing role as an alternative to banks, especially in infrastructure financing, where their advances reached 47% in 2013.
- Dr. M. Anbukarasi in his study analyses as, the financial performance of select Indian banks (HDFC, SBI, ICICI, Kotak Mahindra) and NBFCs (Shriram Transport, Sundaram Finance, Shriram City Union, Sakthi Finance) from 1994-95 to 2017-18. Using secondary data and financial tools like profitability, liquidity, and solvency ratios, along with statistical tests (ADF test, Semi-log Growth Model), the study finds that ICICI Bank and Shriram City Union Finance have the best financial performance among the companies analyzed.
- Ritesh Bhardwaj in his research states as, factors influencing the capital structure of 20 Indian nationalized banks from 2014 to 2018, using a Fixed Effect Panel Data Regression Model. Key findings indicate that Return on Assets, Firm Size, and Audit Committee Meetings positively impact the Debt-to-Equity Ratio, while Return on Equity and Assets Tangibility have a negative effect. For Financial Leverage, Firm Size is positively significant, while Return on Equity and Auditor numbers are negatively significant. The study is limited to nationalized banks in India and a five-year period.
- Kurada T S S Satyanarayana study examines capital structure changes in Indian public sector banks from 2011 to 2022, aiming to validate capital structure theories. Using regression and correlation, it explores the relationship between debt components and financial performance variables, providing insights into capital structure behavior under regulatory frameworks in the banking sector.
- Monika Barak and Rakesh Kumar Sharma(2024) study examines the impact of intellectual capital (IC) on the financial performance of 12 public and 17 private Indian banks from 2010 to 2022. Using the modified value-added intellectual coefficient (MVAIC) model and FMOLS, the study finds that human, capital employed, and structural capital positively impact financial metrics like ROA, ROE, ROCE, and ROS in public banks, with some variations. In private banks, relational capital negatively affects ROS but positively correlates with ROCE. The findings offer insights for policymakers and executives to enhance intellectual capital's effectiveness in improving bank performance.
- Dr. J. Shanmuganandavadivel states in his study as, NBFCs play a crucial role in India's financial system by channeling resources to the commercial sector, complementing banks in meeting corporate financial needs. This study assesses NBFCs' performance, focusing on asset quality, profitability, exposure to sensitive sectors, and capital adequacy. While NBFCs have seen some decline in asset quality, it remains better than that of banks, with stronger profitability and capital positions. The RBI continues to implement regulatory changes to ensure the sector's long-term stability.

RESEARCH AND METHODOLOGY:

Meaning of Research methodology is the specific procedures or techniques used to identify, select, process, and analyze information about a topic. In a research paper, the methodology section allows the reader to critically evaluate a study's overall validity and reliability.

OBJECTIVES OF THE RESEARCH:

- **Objective 1**: Assess how varying levels of leverage affect NBFCs' ability to withstand financial stress and maintain stability during economic downturns.
- **Objective 2**: Investigate how different funding sources (e.g., short-term vs. long-term borrowings, bonds, or equity) impact NBFCs' liquidity positions, loan performance, and asset quality under different economic conditions.
- **Objective 3**: Determine how the balance of debt and equity financing influences profitability metrics (e.g., Return on Equity, ROE) and efficiency ratios, analyzing which capital structures lead to optimal financial performance.
- **Objective 4**: Explore how compliance with capital adequacy norms (such as those mandated by the Reserve Bank of India) affects NBFCs' capital structure decisions and their implications on overall financial resilience and sustainability.

SAMPLING METHODS USED:

Sampling methods that can be used for knowing the impact of capital structure on financial performance of nbfc:

- Stratified sampling method. (stratas)
- Purposive or judgemental sampling. (high degree leverage)

Step 1: Define strata by NBFC category (e.g., ICC, AFC, etc…)

1. **Investment and Credit Companies (ICC):**
   - **Bajaj Finance Limited- 1,87,411.66 cr**
   - Mahindra & Mahindra Financial Services Limited- **32,963.94 cr**
   - L&T Finance Limited- **35,056.95 cr**
   - Tata Capital Financial Services Limited- **unlisted**
   - HDFC Ltd. (Housing Development Finance Corporation)- **13,20,577.77 cr**
   - Aditya Birla Finance Ltd. **unlisted**
   - Muthoot Finance Ltd. **72,547 cr**
   - Shriram City Union Finance Ltd. Merged into Shriram finance- **1,12,453.02 cr**
   - Cholamandalam Investment and Finance Co. Ltd. **1,05,509.13 cr**
   - Manappuram Finance Ltd. **13,432.92 cr**
2. **Asset Finance Companies (AFC):**
   - Sundaram Finance **Limited 47,820 cr**
   - Mahindra Finance (Mahindra & Mahindra Financial Services Ltd.)- **32,963.94 cr**
   - Tata Motors Finance Ltd. **Subsidiary of tata motors- 2,91,166.45 cr**
   - Reliance Capital Ltd.- **suspended (bankruptcy)**
   - SREI Infrastructure Finance Ltd.- **104 cr**
   - Shriram Transport Finance Co. Ltd. Merged with Shriram finance- **1,12,453.02 cr**
   - Magma Fincorp Ltd.- **28,502 cr**
3. **Infrastructure Finance Companies (IFC):**
   - Power Finance Corporation Ltd.- **1,58,190.38 cr**
   - Rural Electrification Corporation Ltd.- **1,39,000 cr**
   - India Infrastructure Finance Company Ltd. (IIFCL) **suspended**
   - IDFC Ltd. (Infrastructure Development Finance Company)- **17,280 Cr**
   - L&T Infrastructure Finance Company Ltd.- **35,094 cr**
4. **Microfinance Institutions (MFIs):**
   - CreditAccess Grameen Ltd.- **14,626 cr**
   - Spandana Sphoorty Financial Ltd.- **2,638 cr**
   - Ujjivan Financial Services Ltd.- **7,190 Cr**
   - Bandhan Financial Services Ltd. **28,103.39 cr**
   - Jana Small Finance Bank- **4,403 cr**
   - Satin Creditcare Network Ltd. **1,674 cr**
   - Arohan Financial Services Ltd. **3,935.31 Cr**
5. **Housing Finance Companies (HFC):**
   - HDFC Ltd. -**13,20,577.77 cr**
   - LIC Housing Finance Ltd.- **34,544 cr**
   - Indiabulls Housing Finance Ltd. **suspended**
   - PNB Housing Finance Ltd.- **25,398 cr**

- Can Fin Homes Ltd.- **11,200 cr**
- Dewan Housing Finance Corporation Ltd. (DHFL) **524 cr** (2021)

6. **Systemically Important Core Investment Companies (CIC):**
   - Tata Sons Ltd.- **33,70,000 cr**
   - Reliance Capital Ltd.- **suspended**
   - Aditya Birla Capital Ltd.- **52,457.98 cr**
   - L&T Finance Holdings Ltd.- **35,094 cr**
   - Bajaj Holdings and Investment Ltd.- **1,19,762.95 cr**
7. **Other Prominent NBFCs:**
   - IIFL Finance Ltd.- **18,672 cr**
   - Hero FinCorp Ltd.- **33,962 cr**
   - Fullerton India Credit Company Ltd.- **pvt comapny**
   - Religare Enterprises Ltd.- **8,257 cr**
   - Capital First Ltd.- **5,818 cr**
   - Motilal Oswal Financial Services Ltd.- **58,172 cr**

Step 2: Use a proportional sample size, perhaps focusing on 30% of each category's companies.

- ICC (10 companies): 30% of 10 = 3 companies
- AFC (7 companies): 30% of 7 = 2 companies
- IFC (5 companies): 30% of 5 = 2 companies
- MFIs (7 companies): 30% of 7 = 2 companies
- HFC (6 companies): 30% of 6 = 2 companies
- CIC (5 companies): 30% of 5 = 2 companies
- Other Prominent NBFCs (6 companies): 30% of 6 = 2 companies

Step 3: Selecting companies within each category based on their **market cap.**

- **ICC**: select 3 companies from the 10 listed (e.g., using a random number generator or drawing names).
- **AFC**: select 2 companies from the 7 listed.
- **IFC**: select 2 companies from the 5 listed.
- **MFIs**: select 2 companies from the 7 listed.
- **HFC**: select 2 companies from the 6 listed.
- **CIC**: select 2 companies from the 5 listed.
- **Other Prominent NBFCs**: select 2 companies from the 6 listed.

Step 4: Collect financial data for analysis, then compare financial performance by capital structure within and across these strata.

- **Capital Structure**: Debt-to-equity ratio, long-term debt, short-term debt, equity capital, etc.
- **Financial Performance**: Profitability ratios (e.g., return on assets, return on equity), liquidity ratios, solvency ratios, and overall financial health.

Step 5: compare financial performance by capital structure.

- **Compare within categories:** Look at the companies' capital structure and compare their financial performance within each NBFC category.
- **Compare across categories:** Compare financial performance based on capital structure across different categories of NBFCs (e.g., ICC vs. AFC, HFC vs. MFIs, etc.).

Analysis and discussion:

NBFCs have reported high profitability, supported by high credit demand in the retail sector. Parameters such as Return on Assets (RoA) and Net Interest Margin (NIM) have been high, and the cost-to-income ratio has also turned around. It is a measure of good operation and good cost management in the sector.

But there are hindrances. For instance, Bajaj Finance experienced a 77% quarter-on-quarter rise in loan loss provisions and losses in the second half of 2024, leading to a marginal decline in projected profits. This highlights the necessity for careful risk evaluation and management, especially in areas of unsecured lending.

The solvency position of the NBFCs has improved with the Capital to Risk-Weighted Assets Ratio (CRAR) at 26.6% as of March 2024, significantly higher than the regulatory requirement. This healthy capital cushion is an improvement in the sector's capacity to absorb possible losses and is a promise of continued credit growth.

Asset quality has also improved, as evident from the decline in the Gross Non-Performing

Assets (GNPA) ratio from 6.0% as of September 2022 to 4.0% as of March 2024. The decline is a testament to good credit risk management and recovery.

Liquidity positions of NBFCs have been healthy, with short-term liabilities as a percentage of total assets being less than 25%. Two-thirds of the total assets have been kept in the form of long-term assets, reflecting a good asset-liability management strategy. Further, dependence on commercial papers has been minimal, forming less than 2% of total assets, thus maintaining the risk of short-term funding volatility at a low level.

SOURCES:

- Bajaj Finance Limited - Investor Relations
- Mahindra Finance - Investor Relations
- NSE - Financials of Listed Companies
- BSE - Financial Reports
- SEBI Filings Portal
- MCA - Company Financial Filings
- Bloomberg
- Reuters
- CRISIL - Research
- ICRA - Ratings & Research
- CARE Ratings
- RBI - Financial Stability Report
- NITI Aayog
- Moneycontrol
- Economic Times – Financials
- Capitaline
- FactSet

Conclusion:

Indian Non-Banking Financial Companies (NBFCs) capital structure is a major driver of their financial stability in the light of economic uncertainty as well as regulatory reforms. This study establishes the impact of debt-equity ratio on liquidity, profitability, and risk

management and thus determines the long-term viability of these institutions.

There is evidence that while increased reliance on debt can contribute to short-term expansion, high leverage increases financial risk, especially in periods of market stress.

Diversified funding structure with equity capital and other sources of finance, on the other hand, increases financial strength and increases the ability of NBFCs to withstand economic downturns.

Moreover, risk management practices and regulatory frameworks are powerful drivers for capital structure choices, which have impacts on how NBFCs remain financially healthy and in line with industry benchmarks. The study points to strategic capital structuring as one key determinant of long-term survival and investor confidence.

Future research can also examine the evolving patterns of funding within the NBFC sector, particularly as a response to digital revolutions and shifting trends in the international economy. With the incorporation of responsible financial practices, NBFCs can improve their resilience, promote economic development, and remain significant contributors to India's financial sector.