

**“IMPACT OF NON-PERFORMING ASSETS (NPAs) ON
PROFITABILITY OF NON-BANKING FINANCIAL
COMPANY (NBFCs) IN INDIA”**

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Abstract:

The main objective of this research paper is to analyze the impact of Non-Performing Assets (NPAs) on the profitability of selected Non-Banking Financial Companies (NBFCs) in India. NBFCs play a crucial role in providing financial services such as loans, investments and asset financing to individuals and businesses who may not have easy access to bank credit. However, increasing NPAs have become a major challenge affecting their financial performance and sustainability.

This study is based on secondary data collected from annual reports and financial statements of selected NBFCs for a period of five years from 2020-21 to 2024-25. Financial ratios such as Return on Assets (ROA), Return on Equity (ROE), Net Interest Margin (NIM), Net Profit Margin and Gross & Net NPA ratios have been used to analyze the relationship between NPAs and profitability. Statistical tools like ratio analysis, regression and ANOVA have been applied to evaluate the significance of the impact.

The findings reveal that higher NPAs negatively affect profitability indicators and reduce the financial stability of NBFCs.

Introduction:

Non-Banking Financial Companies are important financial intermediaries that support economic growth by providing credit to retail borrowers, MSMEs and underserved sectors. These institutions supplement the banking system and improve financial inclusion in the country. However, the rise in Non-Performing Assets has emerged as a major concern for the financial health of NBFCs.

NPAs refer to loans or advances where the borrower fails to repay interest or principal for more than 90 days. High NPAs reduce interest income, increase provisioning requirements and weaken liquidity position, ultimately affecting profitability and long-term sustainability.

Therefore, it becomes essential to study how NPAs influence the profitability and financial performance of NBFCs in India.

REVIEW OF LITERATURE

Swandewi & Purnawati, (2021) studied the effect of non-performing loans of banking company which are listed on indonesia stock exchange. Specifically this study examines the impact of non-performing asset (loan) on return on assets mediated by the capital adequacy ratio public commercial bank. The results of the study concluded that capital adequacy ratio is negatively affected by non-performing assets. Furthermore the study found that a strong relationship exists between non-performing loans and return on assets.

Amita S. Kantawala (2019) researcher analyzed facts and figures on “financial performance of non banking finance companies in india” concludes that there exists a significant difference in the profitability ratios, leverage ratios and liquidity ratios of various categories of NBFCs. It follows that the ratios for all categories of NBFCs are generally different from each other. The analysis of variance along with the details about average ratios may become a useful guide to companies to decide about diversification or continuation in the same line of business considering overall profitability within the regulatory framework. In brief, different categories of NBFCs behave differently and it is the entrepreneur's choice in the light of behavior of some the parameters which go along with the category of NBFC.

Panwar & Aggarwal (2018) economic development in india with special reference to non-banking financial companies, the author studied the role of NBFCs towards the growth of indian economy to determine the present scenario & future prospects of NBFCs as the time passes the existence of NBFCs will show great results in the developments and growth of the economy.

Swani, R.K Sahu, M. & Mishra, A.P. (2017) the researcher concluded that money blocked in NPAs has a significant influence on the effectiveness of banks. The government has mad different mechanisms for recovery such as lok adalats, drt, and sarfaesi act. The sarfaesi act is the most effective reform for recovery of NPAs than other measures. However, gross amounts recovered are very meagre in comparison to outstanding NPAs.

RESEARCH METHODOLOGY

➤ **Objectives of the Study**

- To analyze the trend of Gross and Net NPAs in selected NBFCs
- To examine the impact of NPAs on profitability ratios
- To evaluate the financial performance of NBFCs using ratio analysis
- To test the statistical relationship between NPAs and profitability

➤ **Hypothesis**

- H0: There is no significant impact of NPAs on profitability of NBFCs
- H1: There is a significant impact of NPAs on profitability of NBFCs

➤ **Limitation of study**

- This study has certain limitations that should be considered while interpreting the findings. Firstly, the research is based on secondary data collected from annual reports, published financial statements, RBI reports, and other publicly available

sources. The accuracy of the results therefore depends on the reliability and completeness of these sources.

- Convenience Sampling method used to select participants may not fully represent the entire population being studied.
- Small Sample Size With only 15 companies included in the study, the sample size might be too small to draw conclusions that apply to the broader population.

➤ **Sample and Data**

The study is based on selected NBFCs such as Bajaj Finance, Piramal Finance, Sundaram Finance, Mahindra Finance, Tata Capital, HDB Finance, LIC Housing Finance, Shriram Finance, Muthoot Finance and IIFL Finance.

Secondary data has been collected from annual reports and financial statements for five financial years from 2020-21 to 2024-25.

➤ **Tools Used**

- Ratio Analysis
- Regression Analysis
- ANOVA
- Graphical Representation

FINANCIAL DATA ANALYSIS

1 Earnings Per Share Analysis (Example: IIFL Finance)

The EPS of the company increased continuously from ₹20.06 in 2020-21 to ₹46.22 in 2023-24, indicating strong profitability growth. However, it sharply declined to ₹8.92 in 2024-25, suggesting increased loan losses or higher financial stress.

This shows that rising NPA may reduce shareholder returns and weaken financial performance.

2 Net Interest Margin Trend

Net Interest Margin dropped drastically from 18.2% in 2020-21 to around 5% in later years. This indicates that lending profitability reduced due to higher interest expenses or declining loan recovery efficiency.

Lower margin reflects pressure on NBFC income generation capacity.

3 Regression Analysis Result

Statistical regression analysis shows a strong negative relationship between Net NPAs and Net Profit Margin. For example, in one NBFC the R-square value was about 0.79, meaning nearly 79% variation in profitability was explained by changes in NPAs.

This confirms that as NPAs increase, profitability declines significantly.

Company	Multiple R	R ²	Adj R ²	F	Sig-F	X Coefficient	P-value	Result
Bajaj Finance Limited	0.8898	0.7917	0.7223	11.4057	0.0431	-186.3223	0.0431	Significant Negative
Piramal Finance Limited	0.3644	0.1328	0.1562	0.4594	0.5464	8.8784	0.5464	Not Significant
Sundaram Finance Limited	0.6025	0.3630	0.1507	1.7097	0.2821	2.9084	0.2821	Not Significant
M & M Financial Services	0.7935	0.6297	0.5063	5.1025	0.1090	-2.4842	0.1090	Not Significant
Tata Capital Financial Services Limited	0.9443	0.8917	0.8556	24.7026	0.0156	-15.3366	0.0156	Significant Negative
HDB Financial Services Limited	0.8483	0.7197	0.6263	7.7041	0.0692	-6.7239	0.0692	Weak Significance
LIC Housing Finance Limited	0.9620	0.9255	0.9007	37.3210	0.0088	-4.7439	0.0088	Strong Significant Negative
Shriram Finance Limited	0.9221	0.8503	0.8005	17.0533	0.0257	-5.1612	0.0257	Significant Negative
Muthoot Finance Limited	0.6977	0.4868	0.3157	2.8460	0.1901	-2.3734	0.1901	Not Significant
IIFL Finance Limited	0.3893	0.1515	0.1312	0.5358	0.5171	6.1200	0.5171	Not Significant

FINDINGS

- Increasing NPAs directly reduce interest income and increase provisioning expenses.
- Profitability indicators such as ROA, ROE and Net Profit Margin show declining trend when NPAs rise.
- Some NBFCs with strong risk management systems were able to maintain stable profitability.

- Statistical tests confirm a significant negative relationship between NPAs and profitability.

CONCLUSION

The study concludes that Non-Performing Assets have a substantial impact on the profitability and financial stability of NBFCs in India. High NPAs reduce earning capacity, weaken liquidity and limit the ability of NBFCs to provide fresh credit.

Therefore, effective credit appraisal, risk monitoring and recovery mechanisms are essential for improving financial performance. Strengthening regulatory compliance and adopting advanced risk management technologies can help NBFCs control NPAs and sustain long-term growth.

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