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NBFC Financing and Its Impact on Liquidity Management of Companies

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ABSTRACT: Non-Banking Financial Companies (NBFCs) have emerged as a significant source of financing in developing economies, particularly in India, where they complement the traditional banking system by providing credit to underserved sectors. The study titled “*NBFC Financing and Its Impact on Liquidity Management of Companies*” examines how NBFC lending influences corporate liquidity positions, working capital efficiency, and short-term financial stability. In recent years, NBFCs have expanded their role in providing flexible credit solutions, faster loan disbursement, and customized financing options, which have made them an attractive alternative for businesses facing constraints in bank credit availability. This study analyzes the relationship between NBFC financing and liquidity management practices in companies across various sectors, including manufacturing, retail, and services. Liquidity management, which refers to a firm’s ability to meet its short-term obligations without disrupting operations, is critical for maintaining financial health. The research highlights that NBFC funding often improves liquidity by ensuring timely access to working capital, enabling firms to manage inventory, payroll, and operational expenses more efficiently. However, the study also identifies potential risks such as higher borrowing costs, dependence on short-term credit, and exposure to NBFC sector volatility.

KEYWORDS: NBFC financing, liquidity management, working capital, corporate finance.

I. INTRODUCTION

Non-Banking Financial Companies (NBFCs) have emerged as a significant component of the financial ecosystem, particularly in developing economies like India, where they complement the role of traditional banking institutions. NBFCs are financial intermediaries that provide a wide range of banking-like services, including loans, credit facilities, asset financing, leasing, hire purchase, investment services, and working capital support, but they do not hold a banking license. Over the past few decades, NBFCs have gained substantial importance due to their ability to serve segments of the economy that are often underserved by commercial banks. Their flexible lending practices, faster processing times, and customized financial solutions have made them an attractive source of financing for businesses of all sizes, especially small and medium enterprises (SMEs) and emerging companies.

Liquidity management is a critical aspect of corporate financial management. It refers to the ability of a company to meet its short-term obligations using its most liquid assets without disrupting its normal operations. Effective liquidity management ensures that a firm can pay its suppliers, employees, creditors, and other operational expenses on time while also maintaining sufficient reserves for unforeseen financial needs. Poor liquidity management, on the other hand, can lead to financial distress, operational inefficiencies, and in extreme cases, insolvency. Therefore, companies continuously seek reliable and efficient sources of short-term and medium-term financing to maintain optimal liquidity levels.

In this context, NBFC financing plays a crucial role by providing timely access to funds, thereby strengthening the liquidity position of companies. Unlike traditional banks, NBFCs often have more relaxed eligibility criteria, quicker loan approval processes, and greater willingness to fund high-risk or non-traditional business segments. This makes them particularly valuable for companies that require urgent working capital support or those that may not meet stringent banking norms. NBFCs often bridge the credit gap in the economy by offering financing solutions to businesses that lack sufficient credit history, collateral, or formal documentation. The growing dependence on NBFC financing can be attributed to several structural and operational advantages. First, NBFCs provide faster disbursement of funds, which is critical for businesses facing cash flow mismatches or seasonal liquidity shortages. Second, they offer customized financial products tailored to specific industry needs, such as equipment financing, invoice discounting, supply chain finance, and short-term working capital loans. Third, NBFCs often maintain closer relationships with borrowers, enabling



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better understanding of business cycles and cash flow patterns. This relationship-based lending model allows for more flexible repayment structures, which can ease liquidity pressures on companies.

From a liquidity management perspective, NBFC financing helps companies stabilize cash flows and maintain operational continuity. For instance, businesses operating in sectors with long receivable cycles, such as manufacturing, construction, and wholesale trade, often face delays in cash inflows. NBFCs provide invoice discounting and bill discounting services that convert receivables into immediate cash, thereby improving liquidity ratios such as the current ratio and quick ratio. Similarly, working capital loans from NBFCs enable firms to finance day-to-day operations without relying solely on internal accruals or equity infusion. However, while NBFC financing offers several advantages, it also introduces certain risks and challenges that can impact liquidity management if not properly controlled. One of the primary concerns is the relatively higher cost of borrowing compared to traditional bank loans. NBFCs typically charge higher interest rates due to their higher risk exposure and flexible lending criteria. This can increase the financial burden on companies and reduce net profitability, indirectly affecting liquidity reserves. Additionally, excessive reliance on short-term NBFC borrowings may lead to liquidity mismatches if companies fail to generate sufficient cash inflows to meet repayment obligations.

II. RESEARCH OBJECTIVES

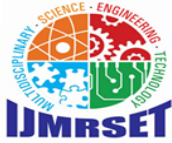
The first and primary objective of this study is to critically examine how Non-Banking Financial Companies (NBFCs) contribute to strengthening the short-term liquidity position and day-to-day operational financial management of corporate enterprises. Liquidity management is a crucial aspect of corporate finance, as it determines a company's ability to meet its immediate financial obligations such as payment to suppliers, employee salaries, utility expenses, short-term debt servicing, and other working capital requirements. In this context, NBFCs have emerged as a significant alternative source of financing, especially for firms that may face constraints in accessing traditional bank credit due to stringent eligibility criteria, collateral requirements, or lengthy approval procedures.

This objective seeks to analyze how NBFC financing instruments—such as working capital loans, invoice discounting, bill financing, trade credit support, and short-term business loans—enhance the liquidity buffers of companies. The study will explore whether NBFC funding provides faster access to capital compared to traditional banking channels and how this speed influences operational efficiency. In many cases, businesses, particularly small and medium-sized enterprises (SMEs), experience liquidity mismatches where cash inflows are delayed while outflows are immediate. NBFCs play a bridging role in such scenarios by offering quick credit solutions that stabilize cash flow cycles.

Furthermore, this objective aims to investigate the extent to which NBFC financing helps companies maintain optimal current ratios and quick ratios, which are key indicators of liquidity health. It will also examine whether firms relying on NBFC credit experience reduced dependence on internal accruals and whether such financing leads to improved working capital turnover ratios. Another important dimension under this objective is the assessment of sector-wise impact, particularly in industries such as manufacturing, retail, infrastructure, and services, where liquidity needs vary significantly. The objective also includes analyzing the flexibility of NBFC lending products. Unlike traditional banks, NBFCs often offer customized repayment structures, shorter approval times, and less rigid documentation processes. This flexibility can directly influence how companies manage seasonal liquidity fluctuations, inventory cycles, and receivables management. The study will further evaluate whether NBFC financing enables companies to avoid liquidity crises during periods of economic slowdown or demand volatility.

In addition, this objective will explore the cost implications of NBFC borrowing on liquidity management decisions. While NBFC loans are more accessible, they often come with higher interest rates compared to bank loans. Therefore, the study will assess whether the benefits of improved liquidity outweigh the cost of borrowing, and how firms strategically balance cost versus liquidity stability. The role of NBFCs during financial stress situations, such as credit crunches or banking sector slowdowns, will also be analyzed to understand their counter-cyclical support function.

Overall, this objective aims to provide a comprehensive understanding of how NBFC financing acts as a liquidity-support mechanism for companies, enabling smoother operational functioning, improved cash flow stability, and enhanced short-term financial resilience.



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III. METHODOLOGY

1. Research Design

This study adopts a descriptive and analytical research design to examine the role of Non-Banking Financial Company (NBFC) financing in influencing the liquidity management practices of companies. The descriptive component focuses on understanding existing financing patterns, NBFC lending behavior, and corporate liquidity practices, while the analytical component evaluates the relationship between NBFC financing and liquidity performance indicators of firms. A quantitative approach is primarily used, supported by qualitative insights where necessary, to ensure a comprehensive understanding of the subject.

The study is structured to analyze how NBFC funding—through working capital loans, short-term credit facilities, invoice discounting, and structured lending products—affects liquidity ratios and cash flow stability of firms across selected sectors.

2. Sources of Data

The research is based on secondary data, collected from multiple reliable sources to ensure accuracy and validity. These include:

- Annual reports of selected companies
- Financial statements (balance sheets and cash flow statements)
- Reports published by Reserve Bank of India (RBI)
- Publications from NBFCs and financial institutions
- Journals, research papers, and academic articles
- Financial databases such as CMIE Prowess, Moneycontrol, and NSE/BSE filings

Where required, qualitative information is supplemented through industry reports, expert opinions, and policy documents related to NBFC regulations and corporate financing trends.

3. Sample Selection

The study uses a purposive sampling technique to select companies that actively rely on NBFC financing for their working capital or short-term liquidity needs. The sample includes firms from sectors such as manufacturing, infrastructure, retail, and small and medium enterprises (SMEs), as these sectors are more dependent on NBFC credit compared to traditional bank financing.

The sample size is determined based on data availability and consistency over a defined period (generally 5–10 years). Companies with incomplete financial data or inconsistent reporting are excluded to maintain reliability.

Additionally, a selection of prominent NBFCs is considered to understand lending patterns, credit distribution, and financing structures provided to corporates.

4. Period of Study

The study covers a time frame of five to ten financial years, depending on data availability. This period is selected to capture both stable and volatile economic phases, including changes in monetary policy, credit cycles, and regulatory developments affecting NBFCs.

A longitudinal approach helps in analyzing trends in liquidity ratios before and after significant changes in NBFC credit exposure.

IV. BACKGROUND

Finance plays a vital role in the growth and sustainability of modern businesses. In recent decades, the financial sector has experienced rapid transformation due to globalization, technological advancement, industrial expansion, and increasing demand for flexible credit systems. Among the various financial institutions operating in the economy, Non-Banking Financial Company (NBFCs) have emerged as significant contributors to business financing and liquidity support. NBFCs are financial institutions that provide banking-like services such as loans, asset financing, leasing, hire purchase, investment, and credit facilities without holding a full banking license. They function under the regulatory supervision of the Reserve Bank of India in India and have become an essential part of the Indian financial system.

The growth of NBFCs has been particularly remarkable in developing economies like India, where traditional banking institutions often fail to meet the financial requirements of all sectors. Many companies, especially small and medium enterprises (SMEs), startups, infrastructure firms, and manufacturing units, face difficulties in obtaining timely credit



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from commercial banks due to strict documentation, collateral requirements, lengthy approval procedures, and regulatory constraints. In such situations, NBFCs provide an alternative source of financing by offering flexible lending policies, quicker loan disbursement, customized financial products, and customer-oriented services. As a result, NBFC financing has become an important mechanism for supporting industrial growth, business expansion, and working capital management.

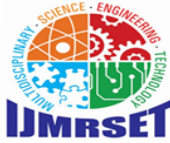
Liquidity management is one of the most crucial aspects of corporate financial management. It refers to the ability of a company to meet its short-term financial obligations efficiently while maintaining sufficient cash flow for operational activities. Effective liquidity management ensures that a company can pay salaries, purchase raw materials, settle debts, and continue production without financial disruptions. Poor liquidity management may lead to operational inefficiencies, delayed payments, reduced profitability, and even business failure. Therefore, companies constantly seek reliable financial sources to maintain an optimal balance between liquidity and profitability. In the contemporary business environment, the increasing dependence on external financing has highlighted the importance of NBFCs in managing corporate liquidity. Companies often require short-term funds to manage day-to-day operations, bridge cash flow gaps, and finance working capital needs. NBFCs fulfill these requirements through various financing options such as term loans, invoice financing, equipment financing, microfinance, vehicle loans, trade credit, and asset-backed lending. Unlike traditional banks, NBFCs are more flexible in evaluating borrowers and are willing to finance sectors that may be considered risky by commercial banks. This accessibility makes NBFC financing highly attractive to companies seeking quick liquidity support.

V. LITERATURE REVIEW

Non-Banking Financial Companies (NBFCs) have emerged as significant financial intermediaries in modern economies, especially in developing countries like India. NBFCs play a crucial role in extending credit to sectors that are often underserved by traditional banking institutions, such as micro, small and medium enterprises (MSMEs), rural businesses, startups, and individual borrowers. Over the last two decades, the rapid expansion of NBFC financing has substantially influenced the liquidity management practices of companies. Liquidity management refers to the ability of firms to maintain sufficient cash flow and liquid assets to meet short-term obligations while ensuring operational efficiency and profitability. Researchers have increasingly focused on understanding how NBFC financing affects corporate liquidity, working capital management, financial flexibility, and risk exposure. Early studies on liquidity management primarily emphasized the role of commercial banks in providing working capital finance to companies. However, the growing importance of NBFCs changed the financial landscape by offering faster credit processing, flexible lending norms, and customized financial products. Almeida, Campello, Cunha, and Weisbach explained that liquidity management is essential for firms facing financial constraints because adequate liquidity enables companies to continue investment and operational activities even during periods of financial stress. Their conceptual framework highlighted that external financing institutions significantly influence a firm's liquidity decisions and working capital policies.

Several researchers have examined the evolution and increasing significance of NBFCs in India's financial system. A recent systematic review of Indian NBFC literature observed that NBFCs have become vital contributors to financial inclusion, credit expansion, and economic growth. The review emphasized that NBFCs bridge the financing gap left by traditional banks by serving borrowers with limited access to formal credit. The study also noted that NBFCs support liquidity requirements of businesses through flexible lending practices and digital financing models.

The literature indicates that NBFC financing positively affects corporate liquidity by improving access to short-term and medium-term funds. Companies often depend on NBFCs for working capital loans, trade financing, equipment financing, and invoice discounting. Such financing helps firms maintain cash flow stability, manage inventory cycles, and meet operational expenses efficiently. Scholars argue that NBFCs provide quicker loan disbursement compared to traditional banks, enabling firms to respond rapidly to liquidity shortages and market opportunities. This flexibility becomes particularly important for small and medium enterprises that may not possess strong collateral or credit history. Another important dimension discussed in literature is the relationship between NBFC financing and liquidity risk. Liquidity risk arises when firms are unable to meet financial obligations due to insufficient cash or liquid assets. Studies on NBFC liquidity management suggest that while NBFC financing improves liquidity availability for companies, excessive dependence on NBFC borrowing may increase financial vulnerability.



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VI. DISCUSSION

The rapid growth of Non-Banking Financial Companies (NBFCs) has significantly transformed the financial landscape in many developing economies, particularly in India. NBFCs play an important role in providing financial assistance to sectors and businesses that often face difficulties in obtaining credit from traditional banking institutions. The topic “NBFC Financing and Its Impact on Liquidity Management of Companies” has gained increasing importance because liquidity management is one of the most critical aspects of corporate financial stability and operational efficiency. Effective liquidity management ensures that companies maintain sufficient cash flow to meet short-term obligations, sustain production activities, and respond to unexpected financial challenges. In this context, NBFC financing has emerged as a valuable alternative source of funding for businesses across various industries. NBFCs differ from traditional banks in terms of their operational structure, regulatory framework, and lending approach. Unlike banks, NBFCs generally provide faster loan processing, flexible repayment structures, reduced documentation requirements, and customized financial products. These features make NBFC financing particularly attractive for small and medium enterprises (SMEs), startups, and companies operating in sectors with fluctuating cash flows. Many businesses experience delays in receiving working capital loans from banks due to strict credit assessment procedures and collateral requirements. NBFCs bridge this gap by offering timely financial support, thereby improving the liquidity position of companies.

Liquidity management refers to the ability of a company to maintain adequate cash and liquid assets to meet operational and financial obligations. Poor liquidity management can lead to delayed payments, disrupted production, loss of supplier confidence, and even insolvency. Therefore, companies continuously seek financing options that can provide immediate funds without creating excessive financial burdens. NBFC financing contributes positively to liquidity management by ensuring quick access to working capital and short-term funds. This enables businesses to manage inventory, salaries, operational expenses, and emergency financial needs more effectively.

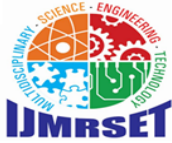
VII. CONCLUSION

Reserve Bank of India regulated Non-Banking Financial Companies (NBFCs) have emerged as an important pillar of the Indian financial system by providing credit facilities and financial services to businesses that may not always receive adequate support from traditional banks. The study on “NBFC Financing and Its Impact on Liquidity Management of Companies” highlights that NBFCs play a significant role in improving the short-term and long-term liquidity position of companies, especially small and medium enterprises. Through flexible lending procedures, quicker loan approvals, customized repayment options, and reduced documentation requirements, NBFCs help businesses maintain smooth working capital operations and meet urgent financial needs effectively. The analysis also shows that NBFC financing contributes positively to liquidity management by enabling firms to manage cash flow fluctuations, inventory requirements, operational expenses, and expansion activities. Companies often rely on NBFCs during periods of limited bank credit availability, economic uncertainty, or immediate funding requirements. This accessibility improves operational efficiency and allows businesses to continue production and market activities without major interruptions. Furthermore, NBFCs support sectors such as manufacturing, transport, infrastructure, retail, and services, thereby strengthening overall economic growth.

However, the study also reveals certain challenges associated with NBFC financing. Higher interest rates compared to commercial banks may increase the financial burden on borrowing companies if not managed carefully. Excessive dependence on short-term borrowings from NBFCs can also create repayment pressure and affect financial stability during adverse market conditions. Therefore, companies must adopt balanced financial planning and proper risk management practices while utilizing NBFC funds.

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