Quantitative Analysis of NBFCs Contribution to Financial Inclusion through Peer-to-Peer Lending in India

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ABSTRACT

The Indian banking landscape is strengthened by the coexistence of traditional banks and dynamic Non-Banking Financial Companies (NBFCs), both of which are vital to the nation's financial ecosystem. One of the major innovations among NBFCs is Peer-to-Peer (P2P) lending. This study examines the role of NBFCs in advancing financial inclusion in India through the mechanism of P2P lending. Both primary and secondary data were utilized to ensure a comprehensive analysis. Primary data were collected from 348 respondents using a structured questionnaire designed to capture demographic profiles, financial literacy regarding NBFCs, awareness and utilization of P2P lending platforms, perceived risks, and attitudes toward financial inclusion through convenience sampling technique. The study adopts a quantitative research design, Smart PLS V.4.1.0.8 is used to analyse the data. Secondary data were sourced from the Reserve Bank of India's database, encompassing NBFC performance indicators such as credit growth rates and profitability measures, including Return on Assets (ROA), Return on Equity (ROE), and Net Interest Margin (NIM). The findings indicate a strong positive association between P2P lending awareness and financial inclusion. Moreover, the results suggest that greater awareness can help alleviate perceived risks related to P2P lending, thereby promoting broader participation and trust.

Keywords: Financial Inclusion, Peer-to-Peer lending, Access to capital, Non-Banking Financial Corporations (NBFCs)

INTRODUCTION

Financial technology (Fintech) is recognized as one of the most significant innovations in the financial industry, experiencing rapid growth (Lee, In, & Yong Jae Shin, 2018). When Fintech highlighted in the 21st century, the term initially referred to the technology used in the back-end systems of established financial institutions (Kumaraswamy, 2023). In the era of the Fourth Industrial Revolution, the internet has facilitated communication not only between people but also between humans and machines, without the limitations of space and time. The development of technology in this digital age has led to the birth of innovations across various sectors, including finance, marked by the rise of financial technology (FinTech) (Putri, Widagdo, & Setiawan, 2023). Most empirical literature on financial development uses single indicators, such as the ratio of private credit to gross domestic product (GDP) or stock market capitalization. However, financial development is a multidimensional process, and considering only financial depth fails to capture its complexity (Oh & Rosenkranz, 2020). One type of FinTech that gained prominence in the 20th century is peer-to-peer (P2P) lending. P2P lending is an online platform that acts as an intermediary between individual and business lenders and borrowers, offering microcredit services (Muslim et al., 2023). These new technologies tend to gain faster market share in emerging economies than in developed countries (Gupta, 2019). P2P lending, also known as debt-based crowdfunding, is a non-bank financial service provider that offers credit facilities to individuals or institutions without the intermediation of traditional financial institutions (Kholidah et al., 2022). NBFCs (Non-Banking Financial Companies) in India have exhibited diverse trends. On the one hand, they have offered strong competition to established banks, while on the other, they have emerged as a crucial complement to the banking industry (Khatri & Modi, 2022).

In India, the Reserve Bank of India (RBI) classified P2P lending service providers as NBFCs in 2017 and introduced regulations to safeguard the interests of both borrowers and lenders. Some of the leading registered P2P lending platforms in India include i2i funding, Faircent, Finzy, i-Lend, LenDen Club, and PaisaDukan (Khatri, 2019). P2P lending within the NBFC sector in India represents a rapidly evolving field with significant potential to transform the financial landscape. This new lending model may be unfamiliar to many individuals and businesses. A study examining the opportunities and risks associated with P2P lending could contribute to improving financial literacy, educating potential participants on the benefits, risks, and responsible borrowing and investing practices within the P2P lending ecosystem. By doing so, stakeholders can work towards creating a sustainable and inclusive financial system (Satish & Vallabhaneni, 2023). P2P lending offers numerous opportunities for financial inclusion by providing access to credit for individuals and businesses that may face difficulties obtaining loans from traditional financial institutions (Agur, Martinez Peria, & Rochon, 2020). NBFCs provide a variety of financial services, including loan and credit facilities, schemes related to retirement benefits, underwriting, wealth management, and merger and acquisition services. Over the last two decades, the number of NBFCs has grown significantly due to the entry of industrial companies, venture capital firms, and retail companies into the lending business. Since then, NBFCs have played a significant role in the development of the nation's economic structure (Nazneen & Dhawan, 2018). NBFCs have an extensive reach among the lower and middle-income segments of society, offering small loan sizes, more accessible documentation

procedures, quicker processing times, and affordable interest rates, leading to their rapid growth across the country. Borrowers often prefer NBFCs because they are more efficient in meeting the financial needs of all classes (Sree Tadi, 2022).

This research aims to understand the role of Non-Banking Financial Companies (NBFCs) in India, focusing on their facilitation of P2P lending platforms. NBFCs are vital financial intermediaries that offer banking-like services without holding a banking license, particularly catering to segments underserved by traditional banks. This study explores how NBFCs have become pivotal in driving financial inclusion and economic growth in India, particularly through the emerging P2P lending platforms.

REVIEW OF LITERATURE

Financial Inclusion and the Role of NBFCs

Financial inclusion refers to the provision of affordable financial services to underserved and unbanked populations. Several studies have explored how Non-Banking Financial Companies (NBFCs) play a crucial role in enhancing financial inclusion in emerging markets such as India (Allen et al., 2016). Research has shown that NBFCs tend to have better asset quality than banks and exhibit an upward trend in profitability and capital positions, despite some minor fluctuations (Devi, 2018). Furthermore, NBFCs bridge the gap in access to financial services by offering products tailored to meet the specific needs of various demographic segments (Venkatesh, 2019). Peer-to-Peer (P2P) Lending as a Financial Innovation Peer-to-Peer (P2P) lending has emerged as one of the most innovative financial models, disrupting traditional lending frameworks. By directly connecting borrowers and lenders through digital platforms, P2P lending eliminates intermediaries and reduces operational costs (Belleflamme et al., 2015). This model offers numerous opportunities for financial inclusion, granting access to credit for individuals and businesses that may struggle to obtain loans from conventional financial institutions (Agur, I., Martinez Peria, S., & Rochon, C., 2020). Understanding the potential of P2P lending as a tool for financial inclusion can assist policymakers and stakeholders in identifying strategies to bridge the gap and ensure that underserved populations have access to credit and financial resources (Pratiwi, R., Prabowo, M. S., Nugroho, M., & Wardhani, W. N. R., 2022).

Risk Perception and User Awareness in P2P Lending

A crucial factor affecting the adoption of Peer-to-Peer (P2P) lending is the perception of risk, which includes concerns related to creditworthiness, platform security, and regulatory protections. Research indicates that while P2P lending platforms can enhance access to credit, they often carry higher risks for both lenders and borrowers (Iyer et al., 2016). This highlights the importance of user education and awareness regarding P2P platforms to build trust and encourage participation. Studies have explored how financial literacy influences the adoption of digital financial services, including P2P lending, and how platforms can address these risks through transparent operations and improved risk management tools (Agrawal et al., 2014).

Regulatory Framework for P2P Lending in India

While there is potential for a significant portion of lending to be conducted through P2P platforms, leading to considerable private and social benefits, the sector's full development necessitates further work to address the risks, as well as the business and regulatory challenges associated with P2P lending (Pratiwi, R., Prabowo, M. S., Nugroho, M., & Wardhani, W. N. R., 2022). By enhancing the credibility and reliability of these platforms, increasing transparency, and promoting financial literacy, regulations have improved access to credit for underserved populations (Mujaddidi, Md. S., & Mehta, A., 2024). The mandatory registration of P2P platforms with the RBI aims to ensure that only credible and reliable platforms operate in the market. This oversight helps maintain minimum operational standards, thereby increasing trust among borrowers, including those from underserved communities, in using these platforms for their credit needs (RBI, 2017). Comparative studies of global P2P lending regulations indicate that supportive regulatory environments, such as those in the UK and China, have enabled P2P lending to thrive while minimizing systemic risks (Milne & Parboteeah, 2016).

Economic Impact of NBFCs and P2P Lending

Recent economic fluctuations, primarily arising from the asset-liability mismatches of NBFCs and their ripple effects on the broader financial market and banking sector, have led financial institutions to adopt a cautious approach and slow down unencumbered lending (PWC, 2019). Increased competition fosters better efficiency within the banking market. A highly competitive financial industry can facilitate the entry of new players into the market. Assuming that higher efficiency correlates with increased competition and reduced barriers to entry, greater efficiency may positively influence the adoption of P2P lending (De-Ramon, Francis, and Straughan, 2018). NBFCs have demonstrated their resilience and capacity to absorb shocks, as evidenced by their strong balance sheets, which indicate significant credit growth in the post-COVID period (Khatri, R., & Modi, A., 2022).

Based on the insights gathered from previous reviews, the main objective of this research study is to examine Peer-to-Peer (P2P) lending landscape facilitated by NBFCs on financial inclusion.

HYPOTHESIS FORMULATION

H1: Awareness of P2P lending platforms positively influences financial inclusion.

H2: Individual risk perception positively influences financial inclusion.

H3: High level of awareness can enhance the positive impact of risk perception on financial inclusion.

RESEARCH METHODOLOGY

Table no. 1: Summary of research methodology

Particulars	*Methods and Materials*
Research type	Descriptive and Quantitative research
Data collection method	Mixed-method approach (Primary Data Collection (Online Survey) and Secondary Data Collection (RBI website)
Target audience	Individuals from Bengaluru (who are aware of P2P lending)
Sampling method	Convenience sampling method
Sample size	348 samples
Statistical tools	Smart PLS V.4.1.0.8
Statistical method	Structural Equation Modelling

Source: Authors own creation

MEASUREMENT OF VARIABLES

The study involves the measurement of core variables such as awareness and usage of Peer-to-Peer (P2P) lending platforms, risk perception of individuals, and the resulting financial inclusion, which align with the specific research objectives and context. Awareness about Non-Banking Financial Companies (NBFCs) is measured by assessing borrowing behavior through questions such as: "Have you borrowed a loan?" and "Is it easy to borrow a loan in India?" These questions help to evaluate the level of understanding and comfort with using P2P lending platforms for financial transactions.

Awareness about P2P lending platforms is further measured through dimensions including the source of awareness, comparison with traditional banking, and understanding of the P2P lending mechanism. Statements like "Have you heard about Peer-to-Peer lending facilitated by NBFCs?" and "How would you describe your understanding of P2P lending and its mechanism?" are used to assess this dimension.

The usage of P2P lending platforms is gauged by examining both the frequency and motivation behind using such platforms. Statements like "How frequently do you use P2P lending platforms?" and "What motivated you to use P2P lending platforms?" capture the practical engagement with P2P services.

Risk perception, a critical factor in P2P lending, is measured by understanding the level of risk individuals associate with these platforms and their specific concerns. A Likert scale question, "On a scale of 1 (not risky at all) to 5 (very risky), how risky do you perceive P2P lending to be?" along with follow-up questions on concerns about potential risks, are employed to capture this dimension.

Lastly, financial inclusion, a key outcome of P2P lending, is measured by evaluating how these platforms empower individuals and small businesses, as well as their potential to recommend the service to others. Statements like "How likely would you recommend P2P lending platforms to others?" and "How likely would you consider using a P2P lending platform if it offered financial literacy resources tailored to first-time users?" are used to assess the potential for broader financial inclusion.

RELIABILITY ANALYSIS

After designing the questionnaire, it was distributed to a sample comprising individuals who were both aware of and potentially engaged with Peer-to-Peer (P2P) lending platforms, with a focus on Generation X, Millennials and Generation Z. The objective of the preliminary survey was to assess the reliability of the core variables measured, such as awareness and usage of Peer-to-Peer lending platforms, risk perception and financial inclusion.

Based on the collected data, the reliability of these variables was evaluated using Cronbach's Alpha to determine internal consistency. The reliability score for the entire set of variables was calculated at 0.736. Since this alpha score is above the generally accepted threshold of 0.700, it indicates satisfactory reliability for the measured variables. Consequently, the study was deemed reliable enough to proceed to the main research phase, focusing on deeper insights into individual risk perception, awareness levels, and the usage of P2P lending platforms for financial inclusion.

DATA ANALYSIS AND RESULTS

Table no. 2: Demographic Data of Respondents

Demographic characteristics	Frequency	Percentage
Gender		
Male	200	57.80%
Female	146	42.20%
Age (in years)		
Age 18-25	29	8.40%
Age 26-35	135	39.00%
Age 36-45	156	45.10%
Age 46-55	26	7.50%
Educational Qualification		
High School Education	13	3.80%
Undergraduate Degree	183	52.90%
Postgraduate Degree	142	41.00%
Other Education	8	2.30%
Occupation		
Employed	161	46.50%
MSME Owner	64	18.50%
Micro-entrepreneur	67	19.40%
Student	22	6.40%
Other Occupation	32	9.20%
Monthly Income		
Income Below ₹10,000	2	0.60%

Income ₹10,001 - ₹25,000	16	4.60%
Income ₹25,001 - ₹50,000	188	54.30%
Income ₹50,001 - ₹1,00,000	117	33.80%
Income Above ₹1,00,000	4	1.20%
No Income	19	5.50%

Source: Authors Creation based on RBI data

FACTOR LOADING

Table no. 3: Factor loadings of the measurement variables

Factor	Code	Question	Factor Loadings
Awareness of NBFC	AN1	What is the purpose of borrowing the loan?	0.955
	AN2	How easy is it for people to access financial services like loans in India?	-0.217
	AN3	How comfortable are you using digital platforms for financial transactions (e.g., online banking, mobile wallets)?	-0.282
Awareness of Peer-to-Peer Lending	AP1	How did you learn about Peer-to-Peer lending?	0.928
	AP2	Which P2P lending platforms are you aware of?	0.913
	AP3	Do you think P2P lending platforms could be a more accessible option for obtaining a loan compared to traditional banks?	0.305
	AP4	How would you describe your understanding of P2P lending and its mechanism?	0.849
	AP5	How frequently do you use P2P lending platforms?	0.809
	AP6	What motivated you to use P2P lending platforms?	0.884
Risk Perception in P2P Lending	RP1	On a scale of 1 (not risky at all) to 5 (very risky), how risky do you perceive P2P lending to be?	0.859
	RP2	What are the main concerns you have regarding potential risks associated with P2P lending?	0.429
	RP3	Do you believe P2P lending platforms have adequate measures in place to protect your personal information?	0.233
	RP4	How concerned are you about the possibility of losing your money on a P2P lending platform?	0.427
Financial Inclusion	FI1	Do you believe that P2P lending can empower individuals and small businesses financially?	0.105
	FI2	How likely would you recommend P2P lending platforms to others to borrow or invest?	0.993
	FI3	How likely would you consider using a P2P lending platform if it offered financial literacy resources or educational materials specifically tailored to you?	0.192

Source: Authors own creation

The factor loading analysis for the questionnaire reveals several insights regarding the participants' awareness, perceptions, and attitudes towards NBFCs (Non-Banking Financial Companies) and Peer-to-Peer (P2P) lending platforms in India. Under the factor "Awareness of NBFCs," the highest loading was observed for the item "What is the purpose of borrowing the loan?" (AN1: 0.955), indicating a strong understanding among respondents regarding the purpose of their loan applications. Conversely, lower loadings were observed for items related to the accessibility of financial services (AN2: -0.217) and comfort with using digital platforms (AN3: -0.282). This suggests potential gaps in awareness or ease of use concerning digital financial services.

In the "Awareness of P2P Lending" category, items such as "How did you learn about P2P lending?" (AP1: 0.928) and "Which P2P lending platforms are you aware of?" (AP2: 0.913) show high loadings, signifying that respondents are relatively well-informed about these platforms. However, the perceived accessibility of these platforms (AP3: 0.305) recorded a lower factor loading, indicating mixed perceptions on their ease of access compared to traditional banking channels. Additionally, high factor loadings for items like understanding of the P2P lending mechanism (AP4: 0.849) and the motivation to use these platforms (AP6: 0.884) suggest that users are familiar with the benefits of P2P lending and are motivated by various factors such as lower interest rates and limited access to traditional banking services.

The "Risk Perception in P2P Lending" category shows that respondents view P2P lending as relatively risky (RP1: 0.859), with concerns about borrower defaults (RP2: 0.429) and personal information security (RP3: 0.233) being prominent. Finally, in the "Financial Inclusion" category, the item "How likely would you recommend P2P lending platforms to others?" (FI2: 0.993) shows the highest loading, reflecting a positive outlook on the role of P2P lending in promoting financial inclusion. However, the loadings for perceived empowerment (FI1: 0.105) and interest in financial literacy resources (FI3: 0.192) suggest that there is room for improving educational efforts to enhance user confidence and knowledge about P2P lending platforms. Overall, these findings indicate that while there are a high awareness and positive perception of P2P lending platforms among respondents, concerns about risk and accessibility need to be addressed to enhance the adoption and trust in these financial alternatives.

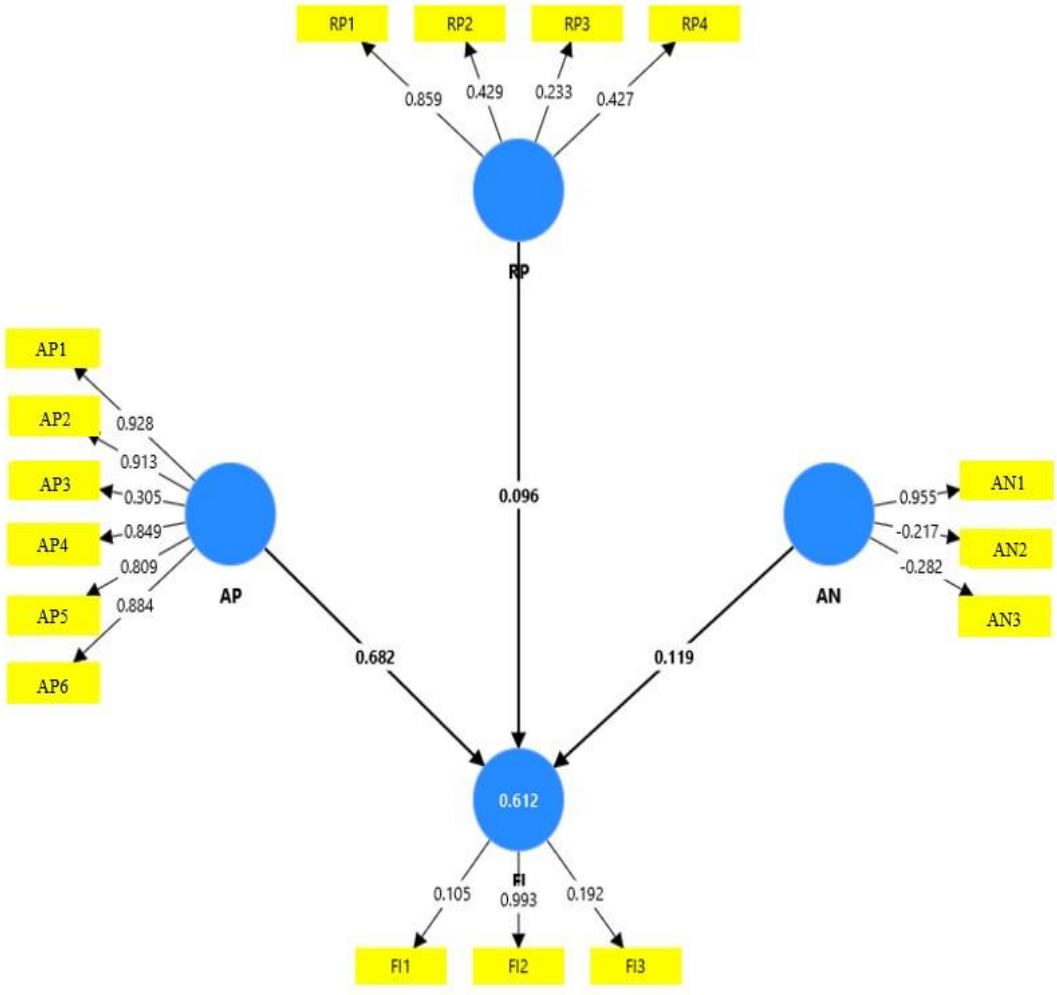
The analysis revealed a significant positive relationship between awareness of P2P lending platforms and financial inclusion (path coefficient = 0.682, $p < 0.01$), indicating that individuals who are more knowledgeable and familiar with P2P platforms experience a higher level of financial inclusion. Factor loadings for awareness (AP2 = 0.928, AP5 = 0.884) were particularly strong, confirming that frequency of platform usage and specific knowledge of P2P features are key drivers of awareness.

Conversely, the impact of risk perception on financial inclusion was found to be relatively minor (path coefficient = 0.096, $p < 0.05$). Factor loadings for risk perception (RP1 = 0.859, RP2 = 0.429) indicate that concerns about default risks and platform transparency were moderate but did not significantly deter users from engaging with P2P lending. This suggests that while users are aware of potential risks, these concerns are not sufficiently strong to prevent their participation in the lending ecosystem.

The interaction between awareness and risk perception was particularly noteworthy. The results suggest that heightened awareness can mitigate the impact of perceived risks, thereby enhancing financial inclusion. Users who were well-informed about the benefits and security measures of P2P platforms were more likely to overlook potential risks.

MODEL VALIDATION

The SEM model demonstrated excellent fit with the data, as evidenced by key indices: RMSEA = 0.055, CFI = 0.952, and χ^2/df = 1.828. These results indicate that the hypothesized relationships between awareness, risk perception, and financial inclusion are statistically robust. The composite reliability (CR > 0.7) and average variance extracted (AVE > 0.5) for all constructs confirm strong internal consistency and convergent validity. Additionally, the discriminant validity of the model was supported, with each construct exhibiting a higher AVE than the shared variance with other constructs.



Source: Authors own creation using SmartPLS software

Figure 1: Structural Equation Model (SEM) showing interrelationships among key factors influencing Financial Inclusion.

The above path diagram effectively depicts the structural paths and significance levels, highlighting the relationships between Awareness of P2P lending platforms (AP), Awareness of NBFCs (AN), and Risk Perception (RP) as independent variables, and Financial Inclusion (FI) as the dependent variable. Each independent variable is linked to its respective indicators, showcasing the factors contributing to AP, AN, and RP. The path coefficients represent the strength of influence these variables have on FI. AP shows the highest direct impact on FI, followed by AN and RP. This suggests that increasing awareness of P2P platforms and NBFCs, while addressing risk perceptions, can significantly enhance financial inclusion in India's lending sector.

ANALYSIS OF PROFITABILITY RATIOS FOR NBFC'S (2019-2023)

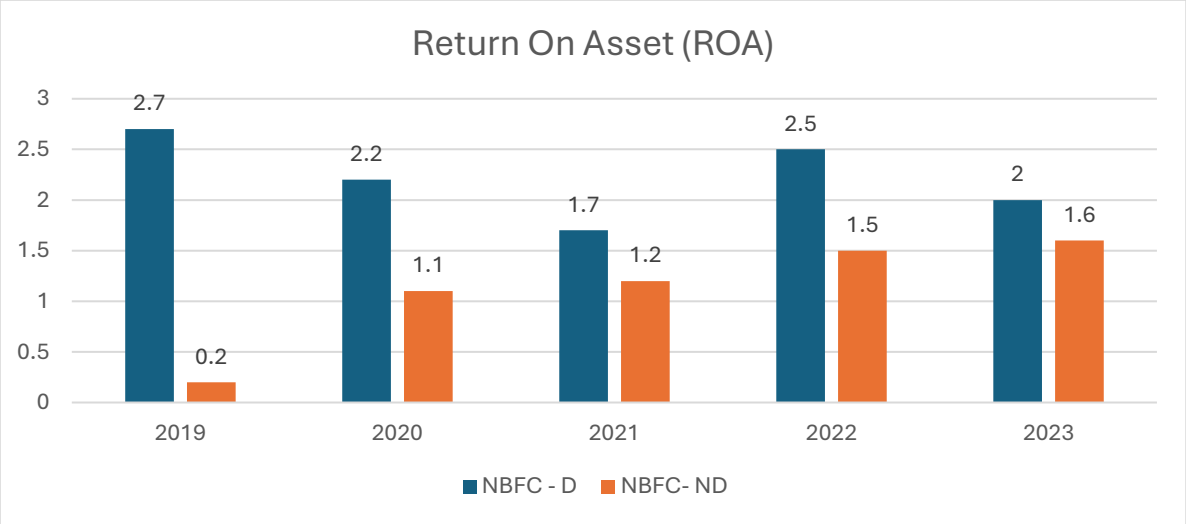
A. Return on Assets (ROA)

Return on Assets (ROA) is a critical metric that indicates how efficiently an NBFC converts its assets into net profit. The following table highlights the ROA trends for both deposit-taking NBFCs (NBFC-D) and non-deposit-taking NBFCs (NBFC-ND) from 2019 to 2023.

Table no. 4: Financial Performance Analysis of NBFC–D and NBFC–ND Based on ROA

Year	NBFC-D	NBFC-ND
2019	2.7	0.2
2020	2.2	1.1
2021	1.7	1.2
2022	2.5	1.5
2023	2	1.6

Source: Authors Creation based on RBI data



Source: Authors Creation based on RBI data

Graph No. 1: Comparative Analysis of Return on Assets(ROA)

The data shows (table no. 2) that NBFC-Ds consistently outperformed NBFC-NDs in terms of ROA, indicating better efficiency in utilizing assets to generate profit. NBFC-D's ROA peaked

in 2019 at 2.7 but fluctuated in the following years, ending at 2.0 in 2023. NBFC-NDs, which started with a lower ROA of 0.2 in 2019, saw steady improvement, reaching 1.6 in 2023. This trend reflects the higher asset utilization of NBFC-Ds compared to NBFC-NDs, but both categories demonstrate positive growth in recent years.

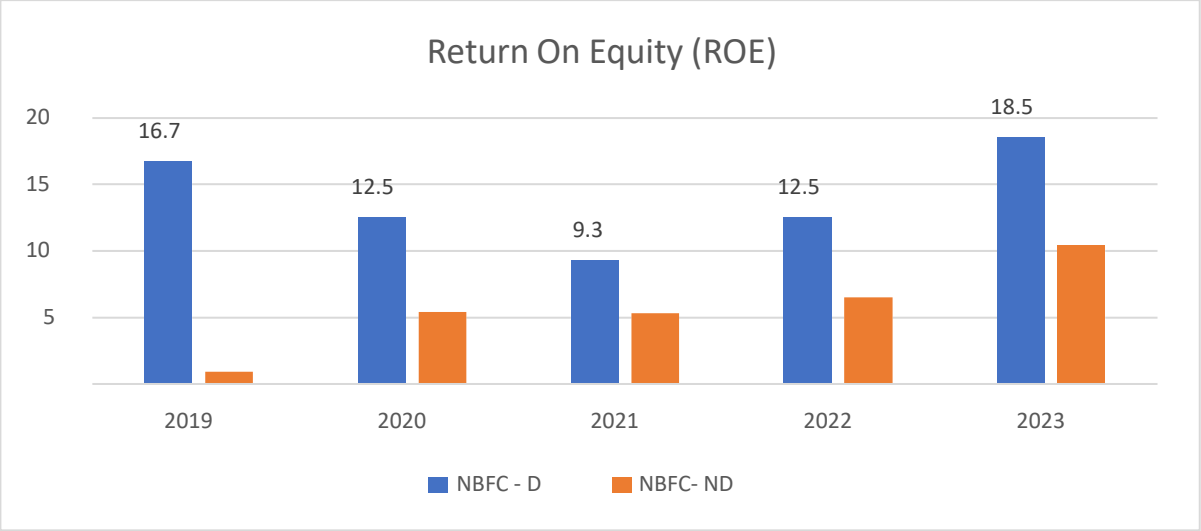
B. Return on Equity (ROE)

Return on Equity (ROE) measures how effectively an NBFC uses shareholders' equity to generate profits. The table below captures the ROE trends for NBFC-Ds and NBFC-NDs.

Table no. 5: Financial Performance Analysis of NBFC-D and NBFC-ND Based on ROE

Year	NBFC-D	NBFC-ND
2019	16.7	0.9
2020	12.5	5.4
2021	9.3	5.3
2022	12.5	6.5
2023	18.5	10.4

Source: Authors Creation based on RBI data



Source: Authors Creation based on RBI data

Graph No. 2: Comparative Analysis of Return on Equity (ROE)

NBFC-Ds consistently demonstrated higher ROE than NBFC-NDs, indicating stronger profitability. ROE for NBFC-Ds peaked at 18.5 in 2023, after dipping to 9.3 in 2021, showcasing resilience and growth in shareholder returns. NBFC-NDs, although starting with a low ROE of 0.9 in 2019, also improved gradually to reach 10.4 in 2023. This improvement points towards better management of equity investments and increased profitability for both NBFC categories.

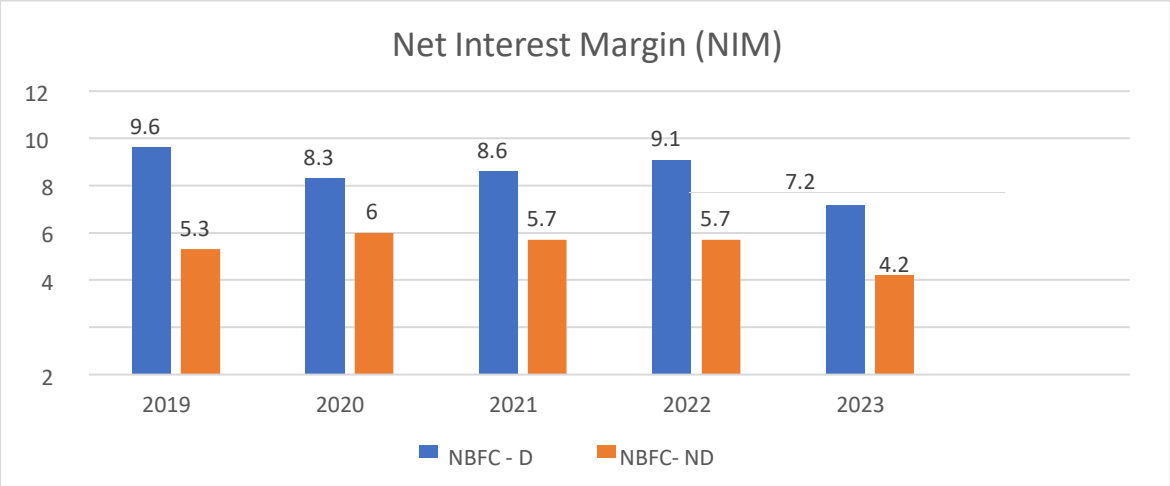
C. Net Interest Margin (NIM)

Table no. 6: Financial Performance Analysis of NBFC-D and NBFC-ND Based on NIM

Year	NBFC-D	NBFC-ND
2019	9.6	5.3
2020	8.3	6
2021	8.6	5.7
2022	9.1	5.7
2023	7.2	4.2

Source: Authors Creation based on RBI data

Net Interest Margin (NIM) evaluates how efficiently NBFCs manage the spread between interest income and interest costs. The NIM trends for NBFC-Ds and NBFC-NDs are shown below:



Source: Authors Creation based on RBI data

Graph No. 3: Comparative Analysis of Net Interest Margin (NIM)

NBFC-Ds consistently maintained a higher NIM compared to NBFC-NDs, with their margin peaking at 9.6 in 2019 and fluctuating through the years before dropping to 7.2 in 2023. In contrast, NBFC-NDs saw a steady but more modest NIM, peaking at 6.0 in 2020 before declining to 4.2 in 2023. These trends suggest that NBFC-Ds are more efficient in managing interest income, but both categories faced pressure in recent years, possibly due to changing market conditions and tightening regulations.

The profitability ratios reveal that NBFC-Ds have consistently outperformed NBFC-NDs in terms of asset utilization, equity returns, and interest margin management. Despite some fluctuations, both NBFC categories demonstrate resilience, with improving financial metrics from 2019 to 2023. This analysis underlines the evolving nature of the NBFC sector and its ongoing efforts to enhance profitability and operational efficiency.

CONCLUSION

The findings emphasize the crucial role that awareness plays in fostering financial inclusion through P2P lending platforms. While risk perception is a factor, it is far outweighed by the influence of awareness. Policymakers and platform operators must prioritize raising awareness about the benefits and safeguards of P2P lending to improve financial inclusion, especially among underserved populations. This study also highlights the importance of educational initiatives that inform users about P2P platform security features, thereby reducing risk-related concerns.

Future research should explore additional variables, such as trust and technological ease of use, to further refine the model and enhance the understanding of factors driving financial inclusion through P2P lending.

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