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POLICY BRIEF

From Payments to Prosperity

EXPANDING CREDIT LINE OVER UPI TO NBFCs



October, 2025

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Suggested Citation

Sharma, R. & Rane, R. (October, 2025). *Policy Brief: From Payments to Prosperity: Expanding Credit Line over UPI to NBFCs*. The Dialogue.

Catalogue No.

TD/DE/PB/1025/10

Publication Date

October 6, 2025

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List of Abbreviations

Abbreviation	Full Form
AA	Account Aggregator
CASA	Current Account and Savings Account
CC-UPI	Credit Card on UPI / Credit Card Linkage on UPI
CICs	Credit Information Companies
CLOU	Credit Line on UPI
CP	Commercial Papers
CRAR	Capital to Risk-Weighted Assets Ratio
DPI	Digital Public Infrastructure
FY	Financial Year (e.g., FY24)
GDP	Gross Domestic Product
IPS	Instant Payment Systems
MCC	Merchant Category Code
MDR	Merchant Discount Rate
MSMEs	Micro, Small, and Medium Enterprises
NBFC-ML	Non-Banking Financial Company - Middle Layer
NBFC-UL	Non-Banking Financial Company - Upper Layer
NBFCs	Non-Banking Financial Companies
NPCI	National Payments Corporation of India
NPA	Non-Performing Asset
NTC	New-to-Credit

ONDC	Open Network for Digital Commerce
PMJDY	Pradhan Mantri Jan Dhan Yojana
RBI	Reserve Bank of India
SBR	Scale-Based Regulation
SFBs	Small Finance Banks
TPAP	Third-Party Application Provider
TPPs	Third-Party Providers
ULI	Unified Lending Interface

Executive Summary

India's Unified Payments Interface (UPI) has redefined the digital payments landscape, delivering instant, seamless transactions to millions and driving the growth of a dynamic fintech ecosystem. Since its inception, UPI has led India's digital public infrastructure journey, emphasising interoperability, openness, and trust. The platform's success rests not only on transaction volumes but also its ability to reduce dependence on cash, deepen financial inclusion, and catalyse innovative business models for banks, fintechs, and merchants. Over the years, progressive enhancements, including interoperability across payment platforms and the integration of new participants, have set the stage for further evolution.

The integration of credit functionality onto UPI marks the next major milestone, with the potential to democratise access to formal credit much as UPI transformed payments. Yet this journey faces significant constraints in both policy and market design. Structural limitations have kept many of the most impactful credit providers, particularly those serving MSMEs and financially excluded segments, from fully participating. The current framework also narrows options for new-to-file consumers and small businesses, weakening the very network effects that powered UPI's success in payments. As a result, UPI's potential to bridge credit gaps and deepen financial inclusion remains only partially realised.

India's broader economic aspirations demand a strong, inclusive, and resilient financial sector. As the country targets higher growth, a five trillion-dollar GDP, and greater global competitiveness, efficiently channeling formal credit, particularly to MSMEs and underserved segments, will be central to this ambition. Expanding UPI's scope to include more lenders and flexible, digital credit solutions aligns with India's growth trajectory and goals of deepening financial participation.

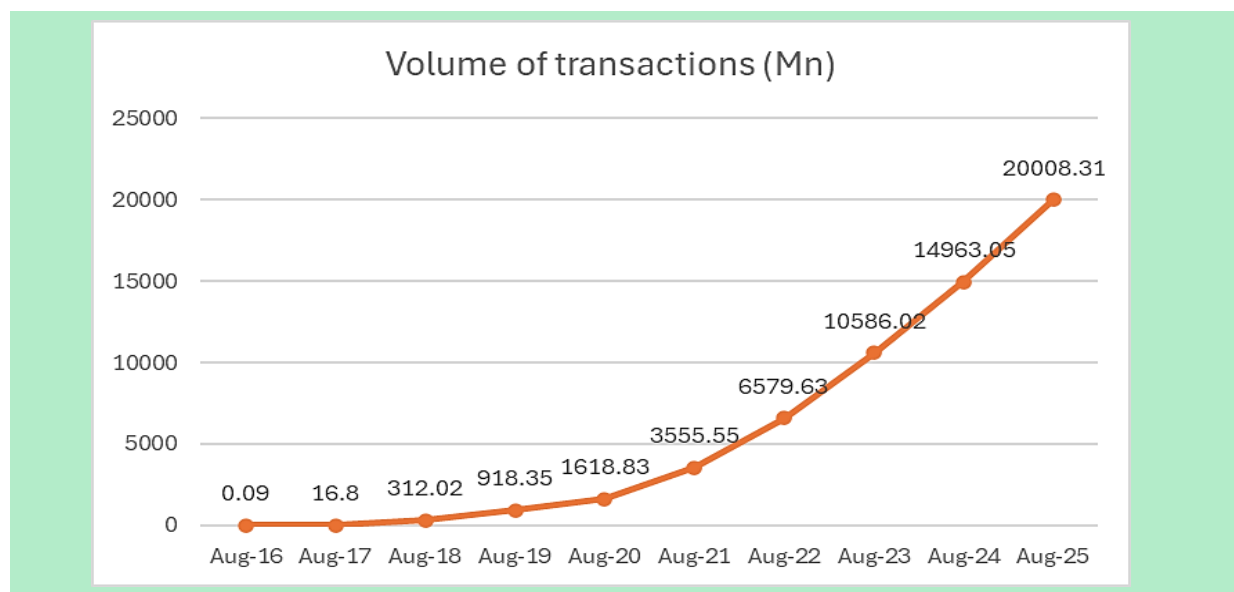
This report analyses the regulatory and market environment for credit on UPI, drawing on market data, policy literature reviews, and consultations with key personnel from banks, NBFCs, payment service providers, and consumers. The findings underscore the urgent need to re-examine existing frameworks and enable a more open, competitive, and sustainable approach to digital credit. The recommendations call for broadening participation for regulated NBFCs, strengthening risk management through digital public infrastructure tools, and fostering ecosystem readiness through clear guidelines. By adopting these reforms, India can unlock the next frontier of digital financial services, fostering greater innovation, competition, and financial inclusion. This vision supports not only a more dynamic credit ecosystem but also India's ambition to build a world-leading, inclusive digital economy.

1. Introduction

The Unified Payments Interface (UPI) has ushered in a new era of digital finance in India, driving one of the fastest transitions from cash to digital payments globally. In August 2025 alone, UPI recorded 20 billion transactions,¹ underscoring its scale as the default mode of payment for millions of Indians. More than a payments rail, UPI embodies India's DPI approach: building inclusive, interoperable networks that expand access and spark innovation at scale.

Instant payment systems (IPS) worldwide have steadily evolved to offer speed, convenience, and lower costs for users. What makes UPI distinctive is that it goes beyond being merely "instant." Conceived as DPI, UPI is trust-based, open, and interoperable- designed not just for efficiency, but for inclusion. Unlike most IPS that operate within closed or bank-only ecosystems, UPI enables open participation through its Third-Party Application Provider (TPAP) led, interoperable design. This drives competition and innovation while ensuring, under strict data and regulatory safeguards, that payments remain inclusive, secure, and user-centric. This openness allows users to transact seamlessly across platforms fuelling both competition and financial inclusion. This architecture has transformed everyday life in India, making digital payments seamless, universally accessible, and deeply embedded in commerce and society. The societal impact is profound: UPI has reduced dependence on cash, accelerated financial inclusion, and enabled new business models. Its open design has empowered banks, fintechs, and merchants alike, creating a network effect that touches every segment of the economy.

Figure 1: Growth in UPI Payments Volume



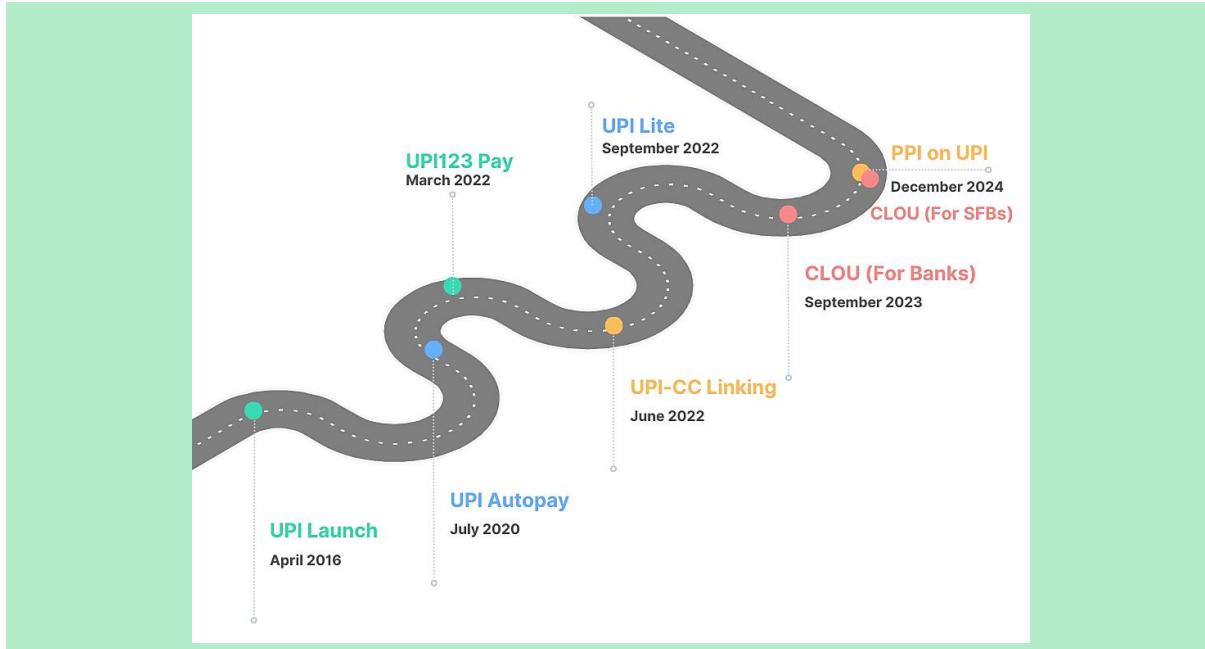
Having established itself as the foundation of digital payments, UPI's next frontier became credit. The pivotal shift came in June 2022, when the Reserve Bank of India (RBI) permitted credit card linkage on UPI- beginning with RuPay credit cards². This step marked the start of embedding credit into India's most widely used payment system, enhancing customer choice and experience. The innovation

¹ National Payments Corporation of India, "Unified Payments Interface (UPI) Product Statistics," *NPCI*, <https://www.npci.org.in/what-we-do/upi/product-statistics>

² Reserve Bank of India, "Reserve Bank of India Press Release," *RBI*, https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=53831

deepened in 2023, when RBI introduced the Credit Line on UPI (CLOU) framework,³ allowing banks to link pre-sanctioned credit lines seamlessly to UPI. Together, these moves signaled a new era: credit was no longer a parallel system but directly integrated into the country’s ubiquitous payment layer.

Figure 2: Timeline- UPI Evolution



This integration carried far-reaching implications. It positioned UPI not only as a tool for instant payments but also as a lever to democratise credit. By enabling consumers and merchants to access credit precisely at the point of transaction- and through the same familiar interface- UPI created a reinforcing cycle of adoption and utility. For lenders, it opened a low-cost, digital-first channel to expand reach; for users, it offered frictionless access to formal credit.

Policy design, however, has taken a cautious, incremental path. Credit cards on UPI remain confined to RuPay, consistent with RBI and NPCI’s longstanding efforts to promote RuPay as a domestic alternative in the card ecosystem. Similarly, credit lines on UPI were initially permitted only for scheduled commercial banks, with subsequent extension to small finance banks. This step-by-step approach reflects the regulator’s prudential focus, but also leaves much of the ecosystem outside the framework.

Industry stakeholders argue that the potential of “credit on UPI” remains underutilised. The core objectives of embedding credit- expanding access, deepening markets, and leveraging UPI’s network effects- can be realised faster and more broadly if participation widens beyond current confines. Unlocking this potential requires re-examining access boundaries, while preserving the safeguards that make UPI a trusted public infrastructure.

³ Reserve Bank of India, “Operation of Pre-Sanctioned Credit Lines at Banks through Unified Payments Interface (UPI),” RBI, <https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=12532&Mode=0>

2. Policy Considerations

2.1 Regulatory Design and Scope of Access

By excluding Non-Banking Financial Companies (NBFCs), regulators have signalled their preference for a gradual and controlled rollout of this intervention. When the Reserve Bank of India (RBI) and the National Payments Corporation of India (NPCI) introduced credit on UPI, they intentionally designed the feature with a narrow initial perimeter. Credit Line on UPI (CLOU) was first opened only to scheduled commercial banks, and UPI credit card linkage began exclusively with RuPay cards. This reflected a clear philosophy: new innovations should begin with large, and strictly supervised entities; early-stage guardrails are essential in a high-velocity payment environment; and adoption should align with India's broader emphasis on payment sovereignty and domestic digital infrastructure.

Crucially, the design was never intended to be static. As behavioural patterns stabilised and early operational signals strengthened, regulators extended CLOU access to small finance banks, demonstrating a deliberate, phased approach to widening participation. This mirrors a broader DPI playbook in India: start with a cohort, generate real-world evidence, and then expand access in a calibrated, risk-sensitive manner. The evolution of credit on UPI is consistent with this logic, reflecting a regulatory stance that combines prudence with an openness to progressive, system-wide innovation.

2.2 Financial Stability and Prudential Rationale

While NBFCs are also subject to regulatory requirements, including capital and liquidity standards that have moved closer to the bank regime for larger entities, regulators continue to distinguish them from banks in important ways. Banks benefit from stable access to low cost Current Account and Savings Account deposits and are covered by a full suite of prudential tools such as cash reserve, statutory liquidity and liquidity coverage ratio norms that apply system wide. Significant and deposit taking NBFCs are now also required to maintain a 100 per cent liquidity coverage ratio, but most NBFCs still rely more heavily on borrowings from banks and wholesale markets, securitisation and other market instruments, and only a subset can raise public deposits. This leaves their liability structure more exposed to swings in wholesale funding conditions than that of banks.

Regulatory caution on allowing NBFCs to originate credit over UPI also reflects experience with earlier episodes of stress in parts of the NBFC sector and with rapid growth in unsecured retail credit. In the current framework, credit on UPI is available only through banks, including small finance banks, while NBFCs remain outside the perimeter. At the same time, NBFCs today are structurally stronger and more diversified than when earlier restrictions were framed. The share of bank loans in their aggregate funding has declined relative to market borrowings and other diversified instruments, and supervisory intensity has increased under the scale based regulatory framework. The policy question is therefore whether a calibrated opening for better regulated NBFCs can be designed in a way that preserves financial stability while allowing UPI linked credit to benefit from their distribution and risk expertise.

3. Challenges Owing to Current Framework

3.1 The Evolving Credit Landscape (2025)

Unsecured credit occupies a critical space in India's financial landscape, especially as the country positions itself as an aspirational economy aiming to become a developed nation. In the current geopolitical and trade environment, accelerating domestic consumption and entrepreneurial activity is not merely desirable but necessary for sustaining growth momentum. Secured credit, while stable, cannot alone unlock the breadth of opportunities needed to drive large-scale economic expansion. For households and individuals still in the early stages of asset formation, unsecured lending often provides the only viable pathway to participate in the formal economy; supporting education, small businesses, consumption needs, and the creation of credit histories that underpin future growth.

At the same time, the very features that make unsecured credit powerful also create vulnerabilities if left unchecked. Rapid expansion without safeguards can amplify systemic risk, heighten borrower distress, and trigger macroeconomic shocks that reverberate across the financial sector. The imperative, therefore, is not to choose between growth and prudence but to strike a balance- leveraging unsecured credit as a catalyst for inclusive development while embedding strong governance, risk management, and regulatory guardrails. The Reserve Bank of India has been mindful of both the promise and risks in this segment. Over time, it has established a calibrated framework that balances innovation with prudence. Initiatives such as the Digital Lending Guidelines,⁴ co-lending frameworks,⁵ and adjustments to capital requirements for certain categories of consumer credit illustrate a risk-based, proportionate approach. These measures do not aim to stifle growth but to ensure that unsecured credit is extended responsibly, with transparency, accountability, and alignment to overall financial stability. In this way, RBI has laid down guardrails that allow the benefits of unsecured lending to be realised while mitigating systemic vulnerabilities. This habit of proactive vigilance, where regulators and the government align to address emerging risks, should also ease anxieties around UPI's credit-enablement journey, offering assurance that the system can continue to evolve without compromising its integrity.

3.2 NBFC Exclusion and the MSME Credit Gap

The exclusion of NBFCs has been particularly consequential for innovation and financial inclusion. NBFCs play a pivotal role in serving "credit thin-file" customers, specially micro, small, and medium enterprises (MSMEs). The MSME sector, which contributes nearly a third of India's GDP, continues to face a credit gap of about 24 percent, or nearly ₹30 lakh crore.⁶

At the same time, NBFCs also play a critical role in reaching beyond MSMEs to other underserved segments such as thin-file individuals, first-time borrowers, and self-employed entrepreneurs. These groups often show reliable repayment potential but lack formal collateral or lengthy credit histories, making them less visible to traditional banks. By leveraging alternative data, innovative underwriting,

⁴ Reserve Bank of India, "Reserve Bank of India (Digital Lending) Directions, 2025," Notification No. 12848, May 8, 2025, <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12848&Mode=0>

⁵ Reserve Bank of India, "Reserve Bank of India (Co-Lending Arrangements) Directions, 2025," Notification No. 12888, August 6, 2025, <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12888&Mode=0>

⁶ Small Industries Development Bank of India (SIDBI), *Understanding Indian MSME Sector: Progress and Challenges*, May 13, 2025, https://www.sidbi.in/uploads/Understanding_Indian_MSME_sector_Progress_and_Challenges_13_05_25_Final.pdf

and last-mile presence, NBFCs have proven effective at responsibly extending small-ticket, short-cycle credit to such customers.

Yet NBFCs remain excluded from offering credit on UPI, leaving out the very institutions that already serve a large share of MSMEs and credit-thin file consumers. For MSMEs, UPI has become the primary rail for sales, supplier payments and tax remittances, but the absence of NBFC-linked credit prevents seamless access to working capital at the point of transaction. The disconnect extends to thin-file individuals, gig workers and self-employed users, whose major and at times only formal credit relationships are with NBFCs. As these lenders cannot link their products to UPI, these customers are unable to access small-ticket, flexible credit on the platform they use most frequently. The result is a structural inefficiency: UPI is ubiquitous for payments but under-leveraged as a channel for inclusive, high-velocity credit delivery, particularly for MSMEs and thin-file users who drive a significant share of India's economic activity.

3.3 NBFCs, CLOU, and Systemic Implications

India's NBFC sector has evolved far beyond the "shadow bank" label, as underlined by RBI leadership and reiterated by the Government of India. Gross loan advances doubled from ₹24 lakh crore in March 2021 to ₹48 lakh crore by March 2025,⁷ while GNPA ratios improved from 6.4% to 3%, reflecting the sector's resilience and maturity. The Scale-Based Regulatory framework, combined with the proposed NBFC SRO model, underscores proportionate oversight and governance.⁸ These measures address long-standing concerns about robust governance and supervisory oversight, signalling a shift from viewing NBFCs as lightly regulated entities to recognising them as systemically important players.

Concerns around systemic interconnectedness have also evolved. NBFCs today are structurally stronger and more diversified than when earlier restrictions were framed. The share of bank loans in their funding has steadily declined: CRISI estimates that bank borrowings accounted for 47.0% of liabilities by June 2024, down from higher levels in prior years, while non-convertible debentures rose to 28.5%,⁹ and commercial papers, securitisation, and foreign currency borrowings formed a growing share. In FY24 alone, NBFCs raised over ₹5.5 trillion from bond and CP markets,¹⁰ underscoring their deeper integration into market financing. In the near term, bank lending may rise again following RBI's rollback of elevated risk weights on NBFC exposures in early 2025. However, this should be seen as a cyclical recalibration rather than a structural reversal. The sector's strategic pivot toward market borrowings and diversified instruments remains durable and, in essence, mitigates the risk of systemic interconnectedness.

⁷ Indian Masterminds Bureau, "NBFC Loan Book Doubles to ₹48 Lakh Crore; FM Sitharaman Calls for Institutional Co-Lending with Banks," *Indian Masterminds*, July 10, 2025, <https://indianmasterminds.com/news/nbfc-loan-book-doubles-to-rs48-lakh-crore-fm-sitharaman-calls-for-institutional-co-lending-with-banks-details-inside-128490/>

⁸ Reserve Bank of India, "Invitation of Applications for Recognition of Self-Regulatory Organisations (SROs) for NBFCs," *Press Release No. 2024-25/58123*, June 19, 2024, https://www.rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=58123; Reserve Bank of India, "Omnibus Framework for Recognition of Self-Regulatory Organisations for Regulated Entities of the Reserve Bank," *Press Release No. 2023-24/2085*, March 21, 2024, https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=57534

⁹ Malvika Bhotika, "NBFCs diversify funding sources amid rising borrowing costs," *Economic Times*, September 30, 2024, <https://bfsi.economictimes.indiatimes.com/news/nbfc/nbfc-diversify-funding-sources-amid-rising-borrowing-costs/113810500>

¹⁰ Bfsi, E. (2025, June 17). NBFCs shifting funding strategy, tapping public deposits and bond markets for capital: Report. ETBFSI.com. <https://bfsi.economictimes.indiatimes.com/news/nbfc/nbfc-embrace-bond-markets-and-public-deposits-for-capital-amid-lending-boom/121901946>

The industry response to CLOU has also been cautious, particularly among leading banks with strong credit card portfolios. Unlike CLOU, credit cards generate not only interchange income but also lucrative revenue from revolving credit, fees, and cross-selling opportunities. With credit cards now seamlessly linked to UPI, banks see little incentive to promote CLOU aggressively, as it could cannibalise their more profitable card businesses. By contrast, NBFCs view CLOU as a promising entry point. Regulatory restrictions have kept them out of the credit card segment, making CLOU a rare opportunity to participate meaningfully in small-ticket, unsecured lending over UPI without encroaching on banks' territory in the credit card ecosystem.

4. The Multiplier Effect

The preceding analysis has highlighted the constraints and trade-offs inherent in the current, narrowly defined framework for credit-on-UPI. While the cautious, incremental approach reflects a prudent regulatory stance, it also leaves significant economic potential untapped. This section transitions from diagnosing these challenges to making the affirmative case for reform. Expanding participation to include Non-Banking Financial Companies (NBFCs) goes beyond incremental improvement; it represents a transformative step that can create a powerful multiplier effect, amplifying benefits for consumers, enterprises, and the financial system at large. Similarly, fostering a more open, competitive, and inclusive ecosystem can enable policymakers to unlock the full potential of UPI as a democratising force for both payments and credit.

4.1 Empowering the Consumer

Allowing well-regulated NBFCs to offer small-ticket, flexible credit lines can introduce a fundamentally new level of convenience. Consumers would gain frictionless access to formal credit precisely when they need it, transforming UPI from a simple payment tool into a comprehensive financial management platform embedded seamlessly in their daily lives.

Expanding CLOU access to NBFCs can directly address the consumer-side frictions and materially enhance the value proposition of UPI as a financial platform. Today, consumers experience a mismatch between how they pay and how they access credit. UPI powers the majority of everyday digital transactions, yet the credit products available on the platform remain limited to bank-issued credit lines and RuPay credit cards that serve only a narrow set of customer profiles and use cases. For millions of individuals, especially first-time borrowers, gig workers, self-employed users, and those with thin credit files, banks often lack the risk appetite or operational flexibility to support small-ticket, high-velocity credit.

NBFCs are uniquely equipped to fill this gap. Their underwriting models rely on alternative data, behavioural insights, relatively higher risk appetite and shorter credit cycles that mirror the cash-flow patterns of everyday consumers. Allowing these institutions to offer credit lines on UPI would transform the user experience. It would shift UPI from a pure payment interface to a unified financial layer where payments and responsible credit consumption converge in one seamless experience. Such an expansion would also reinforce financial resilience for low-income and cash-flow-volatile households. Small-ticket credit accessed responsibly through UPI, supported by MCC-based gating, dynamic limits and real-time usage alerts, can provide a safe and regulated alternative to informal borrowing that is common among these segments. The repayment behaviour generated on UPI creates a verifiable digital trail that helps previously invisible consumers build credit histories and improves their long-term access to formal finance.

In essence, NBFC participation does more than broaden product availability. It reshapes the consumer journey and ensures that UPI serves not only as India's most trusted payment rail but also as a gateway to responsible, embedded and democratised access to credit that is designed around the needs and realities of the everyday user.

4.2 A Definitive Step Towards Closing the MSME Credit Gap

As detailed in Section 3, the MSME credit gap remains substantial, and NBFCs have successfully brought significant numbers of new-to-credit firms into formal finance. Broadening participation in UPI credit offers a unique opportunity to address this chronic and debilitating gap faced by India's Micro, Small, and Medium Enterprises (MSMEs), a sector that contributes nearly a third of the nation's GDP but

struggles with timely and adequate finance.

NBFCs have proven particularly effective in bridging this gap, demonstrating agility and risk appetite that often exceed those of traditional banks, specially at the micro-enterprise level. Their specialised underwriting models leverage alternative data and deep local market knowledge, enabling them to serve credit-thin-file customers and new-to-credit (NTC) borrowers whom banks may overlook.

The current UPI framework, by excluding these vital institutions, sidelines the very players best positioned to leverage digital rails for financial inclusion. The true innovation of credit-on-UPI lies in embedding credit access directly into a merchant's daily transaction flow. Allowing an NBFC-sanctioned credit line on UPI would enable an MSME owner to access working capital seamlessly at the precise moment of making a supplier payment via a QR code scan. This represents a revolutionary shift from the current paradigm, which requires businesses to apply for discrete, episodic term loans or cash advances, a cumbersome process ill-suited for managing dynamic liquidity needs. Credit transforms from a high-friction, pre-planned activity into a fluid, on-demand utility.

Enabling NBFC credit on UPI also serves as a direct policy tool to accelerate MSME formalisation, a key government objective. By embedding digital credit into daily business transactions, it creates a strong incentive loop that aligns small business interests with the goals of the digital economy. The RBI has explicitly noted that formalisation, through measures such as Udyam registration, GST filing, and adoption of digital payments like UPI, is essential for improving creditworthiness in the eyes of lenders.

Currently, for many MSMEs that continue to rely on informal credit channels, UPI functions only as a payment rail. Integrating NBFC credit directly into this platform would transform it into a gateway to formal finance. An MSME that records daily sales through UPI suddenly acquires a tangible incentive to deepen its digital footprint, since this very data can be leveraged (with consent, via the Account Aggregator framework) by an NBFC to underwrite a competitive credit line. This integration establishes a virtuous cycle. Regular UPI transactions create a reliable data trail; this data trail, in turn, enables NBFCs to extend flexible, risk-assessed credit; access to such credit empowers MSMEs to expand their businesses; and expanding businesses, in turn, conduct greater volumes of digital transactions, further strengthening their creditworthiness. The result is a self-reinforcing loop that advances the twin policy goals of formalisation and financial inclusion. Crucially, it achieves this not through top-down mandates but through market-based incentives that align the interests of small enterprises with those of the digital economy.

4.3 Fortifying the Financial System

The regulatory landscape governing NBFCs has evolved significantly, rendering obsolete the “shadow bank” narrative that may have shaped earlier policy choices. The RBI's Scale-Based Regulation (SBR) framework¹¹ now provides a multi-tiered supervisory architecture that calibrates regulatory intensity to systemic importance. These encompass stricter requirements for capital adequacy, liquidity buffers, governance, and disclosure, effectively addressing the risks associated with their scale and interconnectedness. This marks a structural shift in the sector's risk profile and supervisory visibility. Including such well-regulated, systemically important NBFCs is therefore a prudential imperative. It diversifies both credit origination and risk-holding capacity, reducing the burden on banks as the sole intermediaries. Furthermore, the NBFC sector itself has taken proactive steps to de-risk its funding profile. Reliance on bank borrowings has steadily declined, constituting 47% of liabilities by mid-2024,

¹¹ Reserve Bank of India, “What is Scale Based Regulatory Framework or SBR Framework for NBFCs?” *FAQs on Non-Banking Financial Companies (NBFCs)*, accessed October 2, 2025, <https://www.rbi.org.in/commonman/english/scripts/FAQs.aspx?Id=1167>

while market-based instruments such as non-convertible debentures and commercial papers account for a growing share of funding. This diversification of funding reduces the risk of systemic contagion, where stress in the NBFC sector could otherwise disproportionately affect bank balance sheets..

The strengthening of NBFC sector has been further reinforced by the RBI's recent recognition of the Finance Industry Development Council (FIDC) as a Self-Regulatory Organisation for the sector. This introduces an additional layer of discipline through standard setting, peer oversight and industry-wide adherence to responsible conduct. Together, the SBR framework and the SRO architecture materially enhance supervisory comfort, reduce residual risks and help fortify the broader financial ecosystem.

The policy question, therefore, is no longer whether NBFCs are sufficiently regulated to participate in critical infrastructure, but why this highly supervised subset continues to be excluded. Their risk profile is now subject to close proactive oversight by the RBI itself. Maintaining their exclusion from UPI credit implies a lack of confidence in the efficacy of the RBI's own new regulatory framework. It suggests that despite the rigorous standards imposed by the SBR, these entities are still deemed too risky for participation in a payment rail that is central to the future of digital finance. Reversing this stance would serve as a powerful affirmation of the success and sufficiency of the SBR framework, signaling that it has effectively mitigated the very risks that once justified a more restrictive policy approach.

5. A Calibrated Path Forward in Strengthening CLOU

The case for expanding the Credit Line on UPI framework is compelling, with the potential to deliver significant benefits for consumers, MSMEs, and the broader financial system. Yet, progress must be balanced with prudence. The following recommendations outline a pragmatic, phased roadmap that seeks to unlock innovation and deepen financial inclusion while embedding prudential guardrails at every stage. This ensures that UPI's next evolution remains both transformative and stable

The current experience with Credit Line on UPI shows a consistent pattern: large banks have not fully embraced CLOU, largely because its economics, customer profile, and risk-reward dynamics do not align with their established credit businesses. For most banks, credit cards on UPI offer clearer strategic value and better commercial traction, making CLOU a secondary proposition.

A comparable trend is visible among top-tier, Upper Layer NBFCs. While NBFCs cannot issue credit cards and therefore do not have an equivalent product alternative, the largest NBFCs mirror banks in scale, risk appetite, product structures, and target customer segments. As seen in past innovation pilots, these entities tend to behave like banks in their willingness to adopt new credit rails- often prioritising products that align with their existing economics and customer base.

This highlights a key insight: a calibrated expansion of CLOU cannot be based on size alone. If participation is restricted only to the largest NBFCs, adoption is likely to remain slow, replicating the very inertia observed today. To unlock CLOU's intended inclusion and innovation impact, participation must prioritise entities for whom CLOU is strategically attractive and operationally aligned, particularly resilient, well-governed Middle Layer NBFCs with strong last-mile orientation and demonstrated appetite for small-ticket, high-velocity credit.

A phased admission model grounded in suitability rather than scale would allow the Reserve Bank to preserve prudential rigour while enabling meaningful early adoption. Eligibility should be based on transparent, evidence-based criteria, collectively forming a **CLOU Suitability Framework**, which includes

1. **Demonstrated credit discipline.** Participating NBFCs should maintain gross and net NPA ratios within thresholds prescribed by the regulator. These thresholds may be reviewed annually, with entities required to address deterioration in asset quality within defined timelines. Participation can be reassessed if performance deviates materially from the prescribed norms.
2. **Sustained profitability.** Entities should exhibit stable earnings capacity, such as net profits in at least two of the preceding three financial years, ensuring resilience and shock-absorption capability.
3. **Portfolio guardrails.** To contain concentration risk, the Reserve Bank may cap the proportion of an NBFC's outstanding portfolio that can be deployed toward CLOU exposures. Separate performance triggers for the CLOU book such as defined NPA ceilings can be used to determine whether the NBFC continues, pauses, or scales down participation, with corrective windows provided where appropriate.
4. **MCC-based usage gating.** Network-level enforcement of permitted merchant categories would ensure that credit deployed on UPI flows only into approved end-uses, mitigating diversion to speculative or high-risk segments.

A phased expansion of CLOU participation should operate through **eligibility-based sequencing** rather than additional approvals, consistent with the Reserve Bank's broader approach to calibrated innovation. CLOU itself demonstrates this model: participation initially began with banks and was subsequently extended to small finance banks once early operational signals and system readiness were validated. Other digital public infrastructure pilots have followed the same trajectory. The Unified Lending Interface expanded lender participation gradually as operational data accumulated, while the retail CBDC pilot began with a limited group of banks and widened only after behavioural insights and system performance were established, with fintechs joining later under defined safeguards. CLOU can

progress similarly. Once transparent suitability criteria are published, **interested NBFCs that meet the framework can be onboarded into a structured pilot cohort**, with expansion paced in line with observed outcomes.

Such an iterative framework would enable regulators to build empirical evidence on repayment behaviour, loss patterns, merchant acceptance and user experience before broadening participation, ensuring that risk calibration evolves with real-world performance. A longer pilot horizon consistent with ULI and CBDC pilots creates the necessary evidentiary foundation to refine guardrails, strengthen operational readiness and expand participation with confidence. This approach reflects the Reserve Bank's established philosophy: **calibrated liberalisation grounded in data**, where innovation advances without compromising systemic stability.

By prioritising NBFCs that sit at the intersection of **interest, capability, and inclusion**, CLOU can demonstrate its potential early, creating the confidence and momentum necessary for broader adoption across the financial system.

India's digital infrastructure has repeatedly shown that thoughtfully designed rails can unlock new markets at population scale. Credit Line on UPI is poised for a similar transition from a promising innovation to a foundational layer of everyday credit access. Broadening participation to suitably regulated NBFCs is not a dilution of prudence but an extension of the very logic that made UPI successful: calibrated expansion, strong guardrails, and competition that rewards capability. A phased, suitability-based admission framework can enable early movers to demonstrate viability, build real-world performance data, and catalyse wider adoption without compromising systemic stability. By steering CLOU through this disciplined yet forward-leaning path, India has the opportunity to create a globally distinctive model for embedding responsible, real-time credit within public digital infrastructure—strengthening inclusion, deepening credit markets, and reinforcing its leadership in financial innovation.

Conclusion

The evolution of UPI from a fast and inclusive payments rail to a platform that can responsibly deliver credit is at a defining moment. The current bank-only model has provided a stable foundation, but it also limits the broader potential of credit on UPI to deepen financial access, strengthen formalisation, and support enterprise growth. Allowing suitably regulated NBFCs to participate is a logical next step that aligns with the objectives of innovation, competition, and inclusion while respecting prudential boundaries.

NBFCs already serve the very customer segments that CLOU is designed to empower. They have a proven track record in reaching thin-file borrowers, micro and small enterprises, and individuals whose cash flows and credit behaviour are better suited to small ticket, high velocity credit. Their participation would allow UPI to function as a unified layer for both payments and responsible credit, and would give consumers and businesses a more seamless and relevant financial experience. The improvements in NBFC regulation under the Scale Based Regulatory framework, along with stronger governance and diversified funding profiles, provide a high degree of prudential comfort for a carefully controlled expansion.

A suitability based admission framework can ensure that participation is both safe and meaningful. Transparent eligibility criteria, clear portfolio guardrails, usage restrictions through MCC based gating, and ongoing supervision can create the discipline and control necessary for a phased rollout. Early cohorts can generate real world evidence on repayment behaviour, user experience, and system level dynamics. This will build the confidence needed for an orderly expansion that preserves stability while allowing innovation to flourish.

India's digital public infrastructure has repeatedly shown that thoughtfully designed rails can create transformative outcomes at population scale. Credit on UPI is well positioned to follow this path if the ecosystem is allowed to widen gradually in a responsible manner. By enabling well governed NBFCs to join the framework under a calibrated model, policymakers can unlock a new cycle of financial inclusion and economic participation. This creates an opportunity to strengthen UPI's role not only as a platform for payments but also as a trusted and widely accessible gateway to formal credit for millions of Indians.

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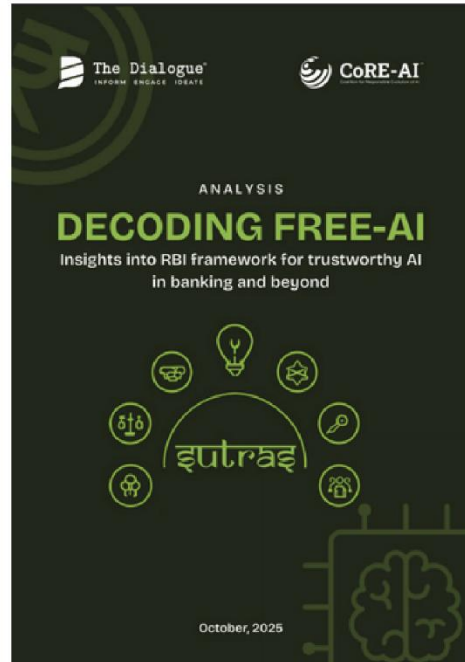
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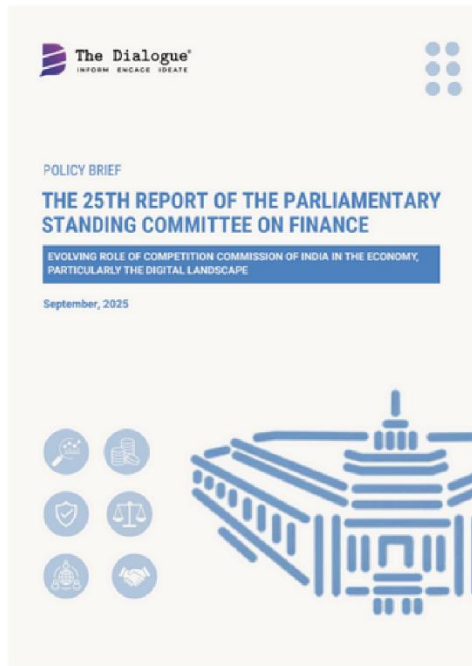
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