The strategic blueprint of co-lending: Expanding credit access and institutional collaboration in India

MSC
MicroSave Consulting

Indrakshi Banerjee

Indrakshi Banerjee is a Senior Manager in the Banking, Financial Services, and Insurance (BFSI) capability at MSC (MicroSave Consulting). She has nearly three decades of experience across banking, financial inclusion, digital finance, and financial sector development. She specializes in micro, small, and medium enterprise (MSME) finance, digital financial services, financial inclusion, and institutional strengthening. She advises governments, development finance institutions, banks, and multilateral organizations on financial sector transformation.

Zeba Birjis

Zeba Birjis is an Associate in the Banking, Financial Services, and Insurance (BFSI) capability at MSC (MicroSave Consulting). She supports projects across micro, small, and medium enterprise (MSME) financing, inclusive finance, and financial sector research. She has experience in digital lending implementation, market research, product development, and institutional strengthening. She holds a Master of Business Administration (MBA) degree from the Xavier Institute of Management, Bhubaneswar, in India.

Ashwin Shukla

Ashwin Shukla is an Associate in the Banking, Financial Services, and Insurance (BFSI) capability at MSC (MicroSave Consulting). He supports projects across inclusive finance, insurance, micro, small, and medium enterprise (MSME) credit, and institutional strengthening. He brings expertise in financial sector research, credit assessment, and data analytics. He holds a Master of Business Administration (MBA) from the Xavier Institute of Management in India.

Mini Niraj Kumar

Mini Niraj Kumar is an Associate in the Catalytic Finance SPG at MSC (MicroSave Consulting). She supports projects across climate finance, micro, small, and medium enterprise (MSME) development, environmental, social, and governance (ESG) compliance, institutional strengthening, and product development. She conducts market research, undertakes institutional assessments, and facilitates stakeholder engagement. She holds a master's in forestry management from the Indian Institute of Forest Management (IIFM) in Bhopal, India.

Introduction

India has long faced a familiar challenge: how to ensure formal credit reaches millions of underserved borrowers without compromising efficiency, profitability, or risk management? In recent years, co-lending has emerged as one of the country's most promising answers. What began as a regulatory initiative to improve credit flow has evolved into a broader framework for formal credit delivery. The framework enables banks and financial institutions to combine their complementary strengths and deliver formal credit more efficiently. According to CRISIL, co-lending assets under management (AUM) exceeded INR 1 trillion at the end of FY24. CRISIL expects the segment to grow at a healthy rate of 35–40% over the medium term. Co-lending allows institutions to expand their reach and optimize capital deployment. It also enables lenders to share risks and rewards and improve access to finance for underserved segments. These segments include micro, small, and medium enterprises (MSMEs), women entrepreneurs, and rural borrowers.

This evolution has followed a series of regulatory developments by the Reserve Bank of India (RBI). These developments have progressively expanded co-lending while strengthening governance, transparency, and customer protection. As the framework has matured, co-lending has shifted from a niche partnership model to an integral part of India's digital lending ecosystem.

This policy brief examines the strategic blueprint of the co-lending arrangement (CLA) in India. It explains why the model emerged as a collaborative lending structure and how responsibilities are shared between participating regulated entities. It also examines how CLA differs from other lending models. The model provides an overview of the operational framework and strategic dynamics that enable financial institutions to use their complementary strengths, expand credit access, and deliver financing more efficiently.

Why has co-lending emerged as a risk-sharing lending structure?

CLA emerged in the Indian financial landscape around FY20 primarily to bridge the credit access gap for segments that traditional banks could not serve cost-effectively and to improve the flow of credit to the unserved and underserved sections of the economy. The RBI initially designed this framework in 2018 to help banks fulfill their priority sector lending (PSL) mandates more effectively by partnering with specialized lenders who possess deep local networks. Over the years, the model has undergone a significant transformation. Under the revised CLA directions 2025, which take effect from 1st January 2026, the scope has been broadened to include all loan segments, whether secured or unsecured. This evolution has made co-lending a mature instrument for systemic credit growth across all segments of the economy, moving beyond its original focus on priority sectors.

CLA combines the low-cost funding of the partner entity with the agile digital capabilities of the originating entity. The partner entities are usually commercial banks, All-India Financial Institutions (AIFIs), or non-bank finance companies (NBFCs). This collaboration enhances affordability through a blended interest rate mechanism that passes the bank's lower cost of capital directly to the borrower. This model enables lenders to reach new-to-credit segments without the need to build extensive physical distribution infrastructure, while providing a structured risk-sharing framework.

Division of roles between the originating RE and the partner RE

The division of responsibilities in a CLA is governed by a formal, ex-ante (upfront) agreement that details the specific duties and share ratios of each participant. This framework applies to scheduled commercial banks, excluding small finance banks, local area banks, and regional rural banks. It also applies to All-India Financial Institutions, namely Export-Import Bank of India (India EXIM Bank), Small Industries Development Bank of India (SIDBI), National Bank for Agriculture and Rural Development (NABARD), National Housing Bank (NHB), and National Bank for Financing Infrastructure and Development (NaBFID), and to NBFCs, including Housing Finance Companies.

In a CLA, the originating regulated entity (RE) typically serves as the customer acquisition entity and the borrower's single point of contact. It manages sourcing, onboarding, and the full range of loan servicing functions. The partner RE jointly funds the portfolio through an irrevocable commitment to take its pre-agreed share of individual loans onto its own books, on a back-to-back basis, as the originating RE originates each loan. Both entities share risks and revenues according to the agreed structure.

Both entities must fund the loan in a pre-agreed ratio to ensure that both have skin in the game and share the financial rewards and credit risks. Under the 2025 revised standards, each participating lender must retain a minimum 10% share of every individual loan on its own books. A critical new mandate requires both lenders to reflect their respective loan shares on their books without delay and, in any case, within 15 calendar days of disbursement. If this window is missed, the originating RE must keep the full exposure on its own books. To provide a seamless borrower experience, the NBFC must generate a unified customer statement, although each lender must maintain a separate borrower account in its own ledgers for its respective share of the exposure. The originating RE may provide a default loss guarantee (DLG) to further mitigate credit risk for the partner entity. This acts as a credit enhancement capped at 5% of the outstanding loan portfolio. Mandatory escrow accounts also secure operational risk and fund flows. Additionally, the framework requires synchronized borrower-level asset classification. If either lender classifies an account as a special mention account (SMA) or non-performing asset (NPA), the other partner must mirror that status.

Operational duties for each lender include managing financial flows and ensuring regulatory compliance. All transactions, such as disbursements and repayments, must pass through a dedicated escrow account to ensure transparency and prevent the intermingling of lenders' funds. While both partners remain individually responsible for know your customer (KYC) compliance, the bank may rely on the NBFC to conduct the customer identification process. Finally, each entity must independently report its share of the loan to credit information companies (CICs) and include co-lending assets in its internal and statutory audits.

How co-lending is different from other models

While CLA shares certain characteristics with other collaborative lending arrangements, it remains a distinct lending model with its own regulatory framework, operational structure, and risk-sharing mechanism. Unlike traditional lending, where a single institution originates and funds the loan, or loan transfer arrangements, where loan exposures move after origination, CLA involves two regulated entities that jointly originate, fund, and service a loan under a pre-agreed partnership. This collaborative approach combines the complementary strengths of participating institutions while ensuring shared accountability throughout the loan lifecycle. The following table summarizes the key distinctions:

Parameter	Traditional lending	Co-lending arrangement	Consortium lending	Loan transfer arrangements (direct assignment or loan participation)
Lenders involved	One lender	Multiple lenders	Multiple lenders	One originating lender and one or more transferees
Loan origination	Single lender originates and sanctions the loan	Jointly originated under a pre-agreed co-lending arrangement	Joint financing for a common borrower	A loan originated by one lender and transferred later
Funding	Entire loan funded by one institution	Loan funded jointly in an agreed ratio	Each lender contributes its committed share	Funding transferred after origination

Parameter	Traditional lending	Co-lending arrangement	Consortium lending	Loan transfer arrangements (direct assignment or loan participation)
Credit risk	Entirely borne by one lender	Shared among lending partners	Shared among consortium members	Economic interest or loan exposure transferred after origination
Customer interface	One lender throughout	Single and coordinated customer interface despite multiple lenders	Multiple lender interactions, depending on the consortium structure	Borrowers generally continue to interact with the originating lender
Typical use case	Retail, MSME, corporate, and consumer lending	Retail, MSME, agriculture, housing, and other collaborative lending segments	Large-value corporate and infrastructure financing	Portfolio management, liquidity management, and capital optimization
Regulatory framework	Governed by respective lending regulations	Governed by the RBI's co-lending arrangements directions	Governed by a consortium and multiple banking arrangements	Governed by the RBI transfer of loans and exposures directions

Key difference between CLM 1 and CLM 2

In the first model, the co-lending model (CLM) 1, the bank typically acts as the principal lender, with both parties agreeing to book their respective share of each loan in their respective books. The CLM 2 model is typically more NBFC-led, in which the NBFC originates and disburses the loans and books 100% of them. After a few months, the bank agrees to purchase its agreed share. CLM 2, which was akin to a direct assignment (DA) transaction, has been eliminated under the revised CLM guidelines to increase transparency and lender participation.

The operational framework and strategic dynamics of CLAs

In a CLA, system integration and data exchange are fundamental to regulatory compliance and operational harmony. Under the applicable CLM 1 model, partner lenders must mirror their respective status on their own books by the next working day. Participating REs must implement robust IT infrastructures that allow near-real-time information sharing to achieve this level of synchronization. Additionally, the move toward a unified model requires API-based systems to enable seamless data exchange, ensuring that both parties have up-to-date records of repayment behavior and loan performance.

The operational efficiency of the model is largely driven by India's digital public infrastructure (DPI) and advanced fintech tools. Technologies, such as e-KYC, e-Sign integrated with NeSL for paperless Digital Document Execution (DDE), and AI-powered credit scoring, streamline customer verification and accelerate the loan approval process. These technologies make the model highly scalable. Efficiency also improves through mandatory escrow accounts, which centralize financial flows and prevent the intermingling of funds, thereby reducing operational risks and increasing transparency. Additionally, a single point of interface for the borrower, typically the originating NBFC, simplifies the customer journey and reduces administrative friction.

Historically, the CLA has been best suited for PSL segments, such as MSMEs and agriculture, where credit access has traditionally remained limited. It is particularly effective for reaching underserved or new-to-credit borrowers in rural and semi-urban areas who may lack extensive documentation or collateral. However, the latest regulatory evolution has broadened the model's scope to include all loan segments, both secured and unsecured. This marks a shift from co-lending, which was primarily used for priority sector lending, to a model that can support lending across a wider range of customer segments and credit products.

Way forward

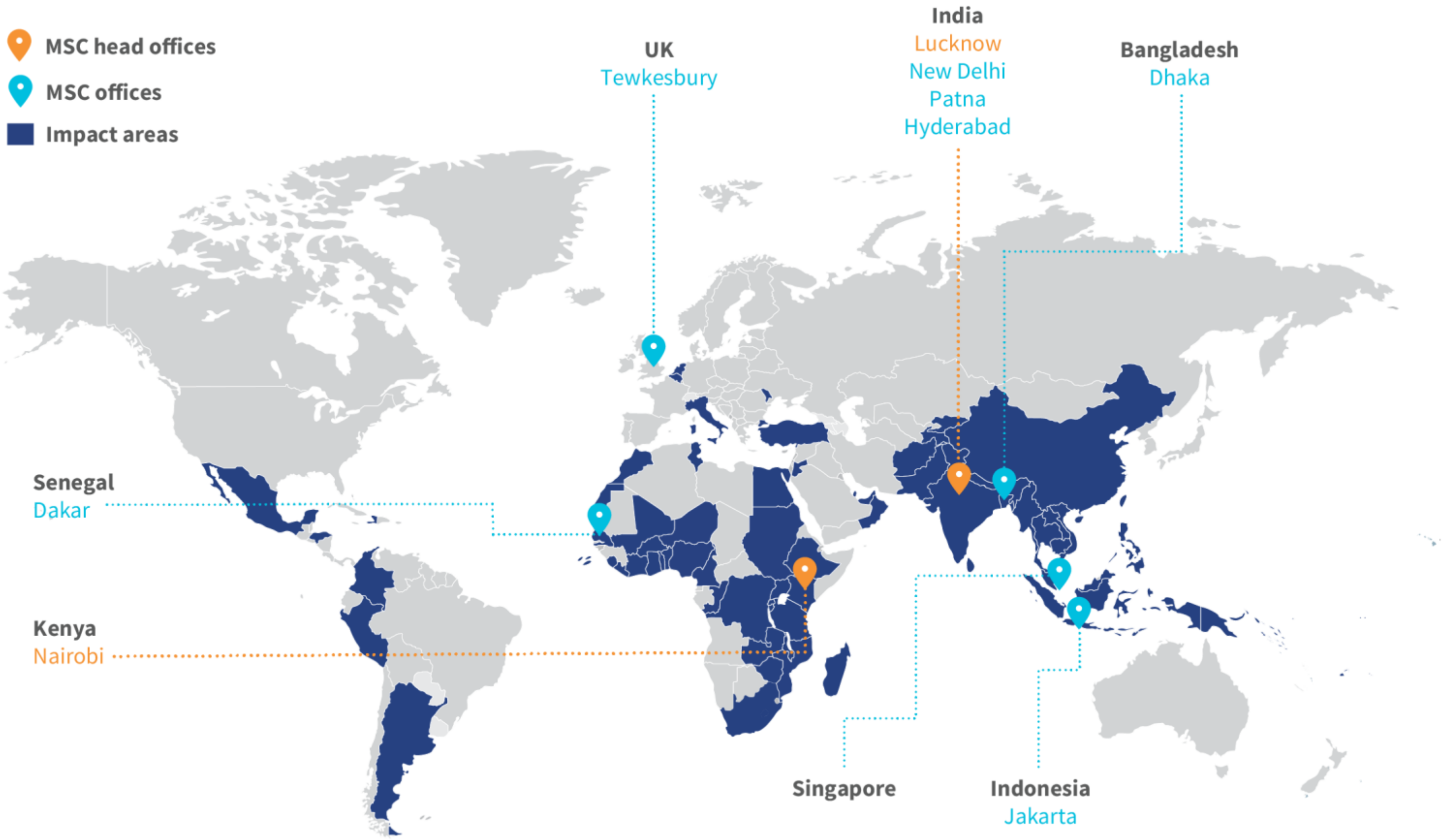
Co-lending has evolved from a regulatory initiative into a strategic framework for expanding formal credit across India. The model combines the strengths of different financial institutions to improve credit access, strengthen risk sharing, and support financial inclusion across diverse customer segments. However, understanding the concept is only the beginning. As the CLA ecosystem continues to mature, the focus shifts toward stronger governance, clearer regulatory expectations, technology-driven operations, and practical implementation across institutions.

In the next brief of this series, we will explore **how India's co-lending framework has evolved over time**, tracing the regulatory journey from the 2018 Co-origination Model to the latest **CLA Directions, 2025**. We will examine the key policy changes, the expanded role of regulated entities, and the implications of these developments for lenders, borrowers, and the broader financial ecosystem.

The final brief will shift from policy to practice by exploring how collaborative lending can strengthen institutional capacity, expand credit access in rural and semi-urban markets, and create a scalable model to serve **MSMEs and other underserved customer segments through technology, partnerships, and operational excellence.**

MSC

MicroSave Consulting



Asia head office

28/35, Ground Floor, Princeton Business Park, 16 Ashok Marg,
Lucknow, Uttar Pradesh, India 226001
Tel : +91-522-228-8783 | Fax : +91-522-406-3773

Africa head office

Landmark Plaza, 5th Floor, Argwings Kodhek Road
P.O. Box 76436, Yaya 00508, Nairobi, Kenya
Tel: +254-20-272-4801/272-4806

Email: info@microsave.net | Website: www.microsave.net