Acquisition Finance
A New Growth Driver

Acquisition financing may emerge as a key growth driver for the domestic banking sector as a potential lending opportunity worth an estimated ₹1.2 lakh cr awaits.

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At a time when much of the world is wrestling with slow growth, geopolitical rifts, and disrupted trade, India is charting a different course—one of momentum and optimism. A sturdy domestic economy, easing inflation, and the promise of lower interest rates have created the perfect backdrop for a new wave of corporate deal-making. From infrastructure and manufacturing to technology, renewables, financial services, and healthcare, Indian companies are embracing acquisitions as a way to fast-track transformation and capture new markets. Recent landmark deals—Tata Group's acquisition of Air India, Zomato's merger with Blinkit, Reliance's takeover of Big Bazaar, and Tata Motors' purchase of Iveco Group's business—underscore how India's corporate giants are reshaping the business landscape through bold consolidation moves, each writing a new chapter in India Inc.'s growth story. Collectively, these deals signal how mergers and acquisitions (M&A) is becoming an integral driver of India Inc.'s next phase of growth and competitiveness. M&A activity in India has remained robust, recording deals worth about $50 bn in the first half of 2025. Recognizing this momentum, the Reserve Bank of India (RBI) has proposed to allow banks to finance corporate acquisitions—previously prohibited under prudential norms. By enabling banks to fund consolidation and strategic expansion, the RBI is positioning the banking system at the center of India's next economic transformation—with acquisition finance emerging as a key frontier of opportunity. Indian banks estimate a potential lending opportunity of around ₹1.2 lakh cr, assuming companies financed 30% of the ₹10 lakh cr worth of M&A transactions in FY 2024 through debt.

What is acquisition finance?

Acquisition finance refers to capital raised specifically to fund the purchase of another company, its assets, or its shares. Historically, banks have largely been restricted from participating directly in acquisition financing. As a result, companies relied on alternative funding sources such as internal accruals and cash reserves, non-banking financial companies (NBFCs), domestic private funds, external commercial borrowings (ECBs), and debt or venture capital instruments to finance acquisitions. The RBI has now proposed to permit banks to provide acquisition finance which will position domestic banks as key enablers of the country's next phase of corporate consolidation and strategic expansion.

RBI's regulatory policy shift

Acquisition financing was long viewed as a non-core and high-risk activity for banks, as it involved highly leveraged equity transactions, which expose them to market risk in addition to credit risk and thus unsuitable for conventional commercial banking operations. The intent was to safeguard the banking system—which depends on public deposits—from the volatility and systemic risks associated with buyout and leveraged finance activities. Today, India's financial ecosystem is far more mature—corporates are stronger and more diversified, while banks operate under enhanced capital standards, stricter supervision, and robust risk management frameworks. Acknowledging this progress, the RBI has undertaken a comprehensive review of the regulatory framework governing bank finance for share acquisitions. On October 24, 2025, it released the draft *Reserve Bank of India (Commercial Banks – Capital Market Exposure) Directions, 2025* for public consultation. These Directions will take effect on April 1, 2026, or on an earlier date if a bank adopts them in full.

RBI's draft guidelines on acquisition finance (2025)

The RBI's draft guidelines on acquisition enable commercial banks except SFBs and RRBs to fund corporate takeovers, both domestic and cross-border. The RBI framework aims to strike a balance between enabling banks to support India's corporate consolidation and growth, while embedding strong safeguards to prevent excessive leverage and maintain strong prudential discipline. Under the proposed framework, banks may extend loans to Indian corporates or their wholly owned special purpose vehicles (SPVs) for strategic acquisitions—those aimed at creating long-term value and business synergies rather than short-term financial restructuring. To prevent overexposure, a bank's aggregate acquisition finance exposure will be capped at 10% of its Tier 1 capital and treated within its direct capital market exposure limits. Only listed, profit-making companies with satisfactory net worth for the last three financial years can qualify as acquirers, and both the acquirer and target must have at least three years of audited financials. Financing of financial intermediaries such as NBFCs or AIFs is not permitted, and the acquirer and target cannot be related parties. Banks may finance up to 70% of the acquisition value, with the acquirer contributing at least 30% equity from its own funds, ensuring adequate skin in the game. The loan must be fully secured by pledged shares of the target company, with additional collateral allowed as per bank policy. The post-acquisition debt-to-equity ratio is capped at 3:1, and credit assessment will be based on the combined balance sheet of the acquirer and target. Banks must also establish a board-approved policy governing exposure limits, borrower eligibility, and risk management, along with robust monitoring, early warning systems, and stress testing.

How it will benefit India

The timing is strategic, as India enters a period of heightened M&A activity

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driven by mergers, divestitures, and synergy-led acquisitions. With Indian conglomerates now leading a more mature phase of consolidation, a supportive bank financing framework can accelerate this shift. Enabling banks to underwrite leveraged buyouts—a space long dominated by private equity and offshore lenders—brings scale, discipline, and transparency to India's dealmaking. Crucially, the new rules shift financing from opaque offshore structures to the regulated domestic system, strengthening oversight, improving capital allocation, and supporting sustained corporate growth. By enabling domestic banks to participate directly in acquisition financing, the RBI is effectively bringing growth capital back onshore—deepening rupee-denominated credit markets and strengthening the resilience of the financial system. Access to bank-led acquisition finance will also give Indian corporates competitively priced, stable funding comparable to their global peers, reducing reliance on costlier NBFC or private credit sources.

A turning point for the domestic banking sector

For decades, banks were excluded from acquisition financing, leaving the field to NBFCs, private credit funds, and offshore lenders. This reform levels the playing field, enabling domestic banks—with their scale and reach—to compete directly in a high-value lending segment. As Indian corporates expand abroad and global investors deepen their presence in India, access to structured acquisition finance will become critical. The RBI's new framework positions banks to evolve from conventional lenders into strategic financial partners, capable of fueling India Inc.'s global ambitions. Until now, most large Indian acquisitions were financed by foreign banks and offshore private credit funds, resulting in valuable lending opportunities and fee income flowing out of the country. With its new proposal, the RBI aims to ensure that India's own growth and consolidation are financed within its domestic banking ecosystem rather than through offshore channels. Acquisition finance typically caters to large, well-rated corporates and private equity-backed acquirers with strong governance and repayment capacity. These transactions are generally secured by the target company's cash flows and assets, offering a structured and relatively predictable credit profile compared with conventional corporate loans. The move opens a high-quality, previously untapped lending segment for domestic banks. Crucially, acquisition finance offers higher yields and richer fee income for banks. Beyond interest spreads, banks can earn significant fees from loan syndication, underwriting, and advisory services—areas where global banks derive a major share of profits. It also helps banks diversify their portfolios, reducing overreliance on retail and working-capital loans, where margins have steadily thinned amid intense competition. Moreover, the entry of Indian banks into acquisition financing can help anchor a robust domestic syndicated loan market, strengthening the ecosystem for structured and leveraged finance. Over time, this could catalyse the development of a secondary loan market, enhance price discovery, and deepen market liquidity—key objectives of India's financial sector reforms. Equally important, the framework will aid in resolving stressed assets under the Insolvency and Bankruptcy Code (IBC). By allowing banks to finance credible bidders for distressed companies, the RBI's move can enhance recovery outcomes, expedite resolution timelines, and facilitate balance sheet cleanup—reinforcing the regulator's broader goal of systemic stability.

Boon for public sector bank

The move opens a transformative opportunity for public sector banks (PSBs) to redefine their role in India's evolving corporate credit landscape. Traditionally focused on project finance, working capital, and priority-sector lending, PSBs have largely been absent from high-margin, structured lending segments. Acquisition finance offers access to a large-ticket, fee-rich business involving well-rated corporates and private equity-backed acquirers with strong governance. It promises superior yields and risk-adjusted returns while helping PSBs diversify beyond low-yield retail and government exposures. Participation in major M&A transactions will also strengthen corporate relationships and unlock cross-selling opportunities in treasury, advisory, and cash management services—enhancing profitability and competitiveness vis-à-vis private and foreign banks. However, PSBs may hesitate to pursue acquisition financing because the fear of post-facto scrutiny by auditors, vigilance authorities, or investigative agencies often deters commercially-driven decisions. According to news reports, India's two largest PSBs are formulating a joint strategy to capture the ₹1.2 lakh cr opportunity in M&A financing. Through the Indian Banks' Association (IBA), they have also sought modifications to certain provisions in the RBI's draft framework. Key concerns include the proposed cap limiting acquisition finance exposure to 10% of Tier 1 capital, as well as restrictions related to financing acquisitions of only listed companies. They want the RBI to revisit the 10% cap and adopt a more flexible limit—up to 40% of the bank's net worth—to enable financing of larger transactions

Key challenges for banks

While the RBI's move to permit acquisition, financing unlocks fresh growth opportunities, it also brings a new set of challenges for Indian banks to navigate.

Acquisition loans often carry higher leverage and complex deal structures, with repayment depending on anticipated synergies and future cash flows rather than proven earnings. This makes credit assessment more challenging and exposes banks to elevated credit and market risks compared with traditional corporate lending. Assessing the viability of an acquisition requires a deep commercial, technical, and regulatory understanding of the industry and its entire value chain.

Valuation and due diligence in M&A transactions require sophisticated analytical skills and deep sectoral understanding—capabilities still maturing across much of the Indian banking system. Assessing fair value is particularly challenging for digital-first and high-growth companies, where future potential often outweighs current earnings, increasing the risk of overvaluation and unfulfilled synergy assumptions. The RBI's requirement that acquisition loans be fully secured by the target company's shares adds another layer of risk, as market volatility can quickly diminish the value of pledged collateral, undermining the loan's security coverage. Banks will face equally complex challenges in tracking post-acquisition performance and integration outcomes—areas where current risk frameworks offer limited visibility. A significant share of M&A failures stems from weak post-merger integration, underscoring the difficulty of translating projected synergies into real gains and aligning diverse organizational cultures. Acquisition loans are subject to stringent regulatory and capital norms, including an exposure cap of 10% of Tier 1 capital, which may limit the ability of mid-sized banks to participate meaningfully. At the same time, Indian lenders will face competition from experienced global banks and private credit funds that have long specialized in this space, intensifying pressure on pricing, deal structuring, and risk management standards.

Governance and reputa-tional risks also loom large, especially in promoter-driven or high-profile acquisitions. To operate effectively in this evolving space, banks will need to develop specialized capabilities in deal structuring, financial modelling, and stress testing, supported by strong oversight and governance frameworks. Moreover, managing the interplay of multiple regulations—including the Companies Act, FEMA, and SEBI guidelines—will demand advanced legal, regulatory, and financial expertise.

Final thoughts

While acquisition finance offers exciting opportunities for diversification, higher yields, and deeper corporate engagement, its long-term success will depend on how effectively banks balance ambition with discipline. It opens a gateway to high-value, strategic lending while empowering banks to participate meaningfully in the country's next wave of corporate transformation. Yet, the true impact will hinge on how prudently banks translate this regulatory freedom into sustainable business models.

Going forward, banks must build institutional depth; specialized acquisition finance teams skilled in valuation, structuring, and stress testing; strong partnerships with investment bankers, legal advisors, and rating agencies; and real-time systems to monitor integration and performance. At the same time, regulators must ensure sound capital buffers, transparent disclosure norms, and supervisory oversight that keeps pace with innovation.

If executed with vision and prudence, this reform could redefine the role of Indian banks—from conservative lenders to strategic catalysts of corporate transformation—powering the next phase of India's consolidation, competitiveness, and global growth. ■

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