

Bankers' Perspective on Challenges of Bad Debt Recovery: *Empirical Evidence from Commercial Banks of Nepal*

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Abstract

The purpose of this paper is to investigate bankers' perspective on challenges of bad debt recovery in commercial banks of Nepal. This study is based on liquidity management theory and adopts explanatory research design to determine causal relationship between variables. Primary data has been collected from 220 bankers through the structured questionnaire by using KOBO Toolbox. SEM is used to analyze data inferentially. Findings indicate that lending decision and loan risk monitoring are significant to bad debt recovery. Unfavorable methods, availability of accurate and proper information about the loans, lack of payment visibility, and lack of flexible payment options are major challenges of bad debt recovery. Thus, commercial banks of Nepal must develop proper monitoring mechanism and government should develop proper regulation for debt collection.

Keywords

bad debt, commercial banks, loan defaults, non-performing loan

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INTRODUCTION AND STUDY OBJECTIVES

A financial institution is a business that receives money from the public and invests it in financial assets like deposits, loans, and bonds rather than

tangible assets like real estate (Chigozie & Ikechukwu, 2015). Non-performing assets have a direct impact on a bank's financial performance, i.e. its profitability (Rai, 2020). When a bank extends credit conditions to an unsuitable consumer or when the customer's circumstances

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change, bad debt occurs. Every business will encounter a customer who is unable to pay, and they will be required to record a bad debt expense. Recovering bad debt is critical since it can influence how potential investors and company leaders see the company's health (Alsharari & Abousamra, 2019a).

Hemming (2003) revealed that the causes of these debts in recent decades may differ; in the 1970s, the causes of the debt crisis included; uncontrolled accumulation of debt, social and economic dislocations of economies, increase in poverty levels, ascendancy in dependence and in the 1980s and 1990s, oil shocks and changes in other worldwide economies resulted in a flurry of demand and supply for financial services (Oware et al., 2015). Because banks are essentially custodians of the funds they lend, interest and dividends must be paid to depositors and investors, respectively. It is important to underline that the importance of credit management cannot be overstated, and that proper credit management necessitates the implementation of solid and efficient government credit laws (Hameed, 2015). Corporate credit evaluation, disbursement, sufficient monitoring, and payback must all be ensured for banks to be successful. However, past experience has demonstrated that insufficient credit investigation and appropriate loan application judgment have resulted in nonperforming loans (Chigozie, 2013).

There are specific ways to recover the bad debt which is specified by the laws and regulations of that nation. One

way could be: when the debt collection officer must recover the outstanding amount from the borrower after receiving an order from the tribunal. Subject to current regulations, the debt collection officer may employ a variety of techniques to recover the principal and interest on a debt (Ndikumana et al., 2019). They could seize or auction the borrower's other movable or immovable property, whether furnished as security or not, and the other way around by seizing or auctioning the guarantor's movable or immovable property, arresting and detaining any individual who is a borrower or guarantor in accordance with the prevailing law. Better financial institution performance is important for any country's economic development, whereas poor financial institution performance causes economic growth to stagnate and has a negative impact on the region. Because bank nonperforming assets (NPA) is a key factor for assessing the financial soundness of the banking system it is critical to identify possible problems and keep a careful eye on them (Sahoo & Majhi, 2020). Alsharari and Abousamra (2019) revealed bad debts are caused by a lack of efficient banking oversight. Likewise, there are many other reasons for the debt turning into bad debt. There are no financial institutions that have escaped the situation of bad debt, as the main reasons of bad debt in an organization are yet not identified.

Loan repayment pattern and inclination to postpone payments may be observed from the start of the financing period. In general, collecting bad debts may be

challenging for financial institutions and enterprises, particularly when cash flow is an issue. Much of the problem stems from the fact that many of their debtors are cash-strapped, which makes cash flow management difficult for both creditors and borrowers. To make matters worse, Loan repayment pattern and inclination to postpone payments may be observed from the start of the financing period. In general, collecting bad debts may be challenging for financial institutions and enterprises, particularly when cash flow is an issue. Much of the problem stems from the fact that many of their debtors are cash-strapped, which makes cash flow management difficult for both creditors and borrowers. To make matters worse, a bevy of reckless borrowers refuse to assume responsibility for their debts (Alharbi, 2016).

Granting a loan is simple, but recovering it has become a headache for many commercial banks due to a lack of appropriate collateral as a result of a large loan investment, which necessitates the study of credit management systems (Abdulnafea et al., 2022). Grunert & Weber (2009) revealed in his study that failure to recover on bad debt has a direct impact on a bank's financial performance since it refers to the efficiency with which a bank optimizes its total resources and so serves the value of assets and the efficacy of management. The problem to recover is not only seen in Nepalese economy but also the problem in all over the world, whether it be the developed or any developing nations. Hence, it is the serious context that needed to be studied in time being.

The problem to recover is not only seen in Nepalese economy but it are also the problems in all over the world, whether it be the developed or any developing nations. As a result, this study investigates the issues of bad debt recovery in order to better loan portfolio management by reducing risks in the Nepalese banking industry. There are a variety of questions that need to be addressed such as What are the debt recovery process of banks? What are the main factors affecting bad debts collection? What are the challenges on the debt recovery process in the context of Nepalese commercial banks? What are the remedial measures to help reduce defaults on loans? This study will help to attain answer to these questions as the general objective of this study is to study the bankers' perspective on challenges on bad debt recovery in commercial banks of Nepal. Likewise, this study will further help to understand the process of bad debt recovery, to identify the key factor affecting bad debt collection, to measure the challenges on the bad debt recovery process and to identify the measures reducing defaults on the loan in Nepalese commercial banks.

Theoretical Review, Conceptual Review and Hypotheses Formulation

The fundamental goal of a theoretical review is to look into the major subject of theory that has accumulated in relation to a problem, a concept, a theory, or a phenomenon. Many different theories are explored in relation to the issues of bad debt collection in Kathmandu Valley commercial banks such as Keynesian Investment Theory, Extreme Value

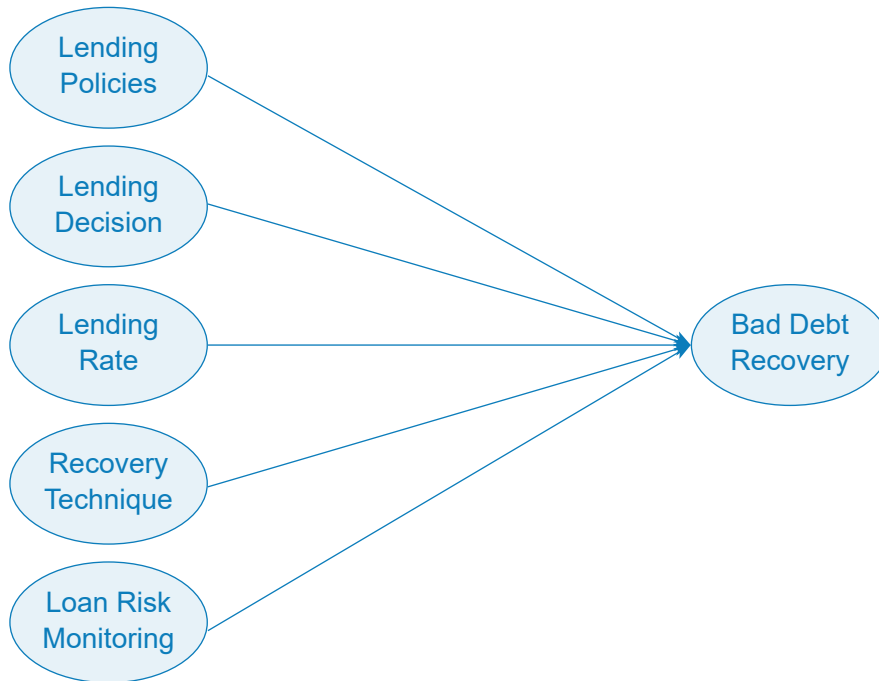


Figure 1. *Conceptual Framework*

Note: The figure shows the conceptual framework for the study of bad debt recovery

Note: Developed by researchers

Theory, Anticipated Income Theory, Shift Ability Theory and Commercial Loan Theory. After reviewing all these theories, Commercial Loan Theory was found to be more appropriate for this study. According to this idea, if commercial banks issue self-liquidating productive loans for a short period of time, the central bank should lend to the banks on the security of such short-term loans. This concept ensures that each bank has the right amount of liquidity, and that the entire economy has the right amount of money supply [Ahtiala \(2005\)](#). By rediscounting sanctioned loans, the central bank was anticipated to raise or eliminate bank reserves. Banks were able to collect extra reserves by rediscounting bills with the central banks as company

grew and trade requirements increased. When business slowed and trade requirements decreased, the number of bills rediscounted decreased, as did the supply of bank reserves and the quantity of bank credit and money ([Nguyen & Vo, 2021](#)).

A financial institution is a business that collects money from the public and invests it in financial assets like deposits, loans, and bonds rather than tangible assets like real estate. To be more specific, a bank is a financial intermediary that accepts deposits, makes loans, and provides the most comprehensive range of services of any financial organization ([Bhattarai, 2017](#)). Because banks are essentially

guardians of the capital they lend, interest and dividends must be paid to depositors and investors, respectively. It is vital to underline the importance of credit management and the fact that effective credit management necessitates the passage of solid and efficient government credit laws (Adhikari et al., 2021).

Mawele (2020) analyzed debt recovery in banks, specifically focusing on bad debt recovery in Zanaco Bank. The objective of this study was to ascertain the difficulties that banks face in the process of debt recovery, the strategies that they employ to retrieve non-performing loans, the underlying reasons for loan defaults in banks, the consequences of loan recovery on the bank, and plausible debt recovery remedies. The study utilized the Commercial Loan Theory and Anticipated Income Theory to achieve these aims. The study conducted an analysis of various independent factors such as debt rescheduling, customer bankruptcy, higher lending rates, poor borrower selection, and flexible payment plans, in relation to the dependent variable of debt recovery.

As shown in Figure 1, it has dependent variables and independent variables to study of bad debt recovery in commercial banks of Nepal. In this framework, bad debt recovery (BR) is a dependent variable whereas Lending policies (LP), lending decisions (LD), recovery techniques (RT), loan risk monitoring (LM) and lending rate (LR) are independent variables.

Lending Policies (LP) and Bad Debt Recovery (BR)

Lending policies are critical components of lending investment management; policies should cover the bank's loan assessment and documenting, lending obligations, and the security appraisal process and laws. According to the Federal Deposit Insurance Corporation (2012), lending policies should be properly defined and made forth in such a way that it permits effective monitoring even by directors; each bank is responsible for creating credit policy and monitoring their execution. The most serious risk connected with financial institutions is poor credit risk management, which poses a danger to the banking system (Rudebusch, 2021)

H₁: Lending policies have significant and positive impact on the bad debt recovery.

Lending Decision (LD) and Bad Debt Recovery (BR)

One of the most important variables in a bank's profitability is the selection of the right entrepreneur or lending decision. In the credit evaluation, two important criterions, namely the intention to repay and, as a result, the capacity to repay should be appropriately handled. Entrepreneurs with the necessary willingness, competence, traits, and expertise for effectively establishing and operating an industrial unit should be selected with caution. This is frequently the easiest method of securing a bank's investment and assuring accurate and timely return (Chukwunulu et al., 2019). Nonetheless, loan decisions are still

Table 1
Variable Construct

| Construct | Indicators | Variables | Explanation |
|---------------------------|------------|-------------------------|---|
| Lending Policies (LP) | LP1* | Simplicity | Lending policies are simply stated and easy to understand. |
| | LP2 | Influence on collection | Lending policies have an influence on the collection of bad debts. |
| | LP3 | Borrowers' preferences | Lending policies reflect borrowers' preferences. |
| | LP4 | Loan portfolio | Loan portfolios have an impact on lending policies. |
| | LP5* | Evaluation | Lending policy must be properly evaluated by concerned departments. |
| Lending Decisions (LD) | LD1 | Decision criteria | The lending decision dependent upon lending criteria. |
| | LD2* | Prejudiced | Lending decisions are prejudiced on bad debt. |
| | LD3 | Loan portfolio | Lending decisions have an impact on loan portfolios |
| | LD4* | Influence on recovery | Lending decisions have an influence on the recovery of bad debts. |
| | LD5 | Decision with caution | Lending decisions should be made with caution. |
| Recovery Techniques (RT) | RT1* | Recovery policy | All Nepalese commercial banks have a recovery policy. |
| | RT2 | Recovery strategy | Recovery strategies utilized by Nepalese commercial banks have more efficient. |
| | RT3* | Follow ups | Bank needs to do follow up on regular basis. |
| | RT4 | Recovery procedure | Recovery procedures utilized by Nepalese commercial banks produce positive results in bad debt recovery |
| | RT5 | Methods utilized | Various methods is utilized in recovery reduce the NPL ratio |
| Loan Risk Monitoring (LM) | LM1 | Monitoring | Bad debt risk is monitored in Nepalese commercial banks or not |
| | LM2 | Regularity | Bad debt risk is monitored on a regular basis by Nepalese commercial banks. |
| | LM3* | Favorable impact | Monitoring bad debt risk has a favorable impact on the loan portfolio. |
| | LM4 | Issues with monitoring | Numerous problems might affect loan risk monitoring in Nepalese commercial banks. |
| | LM5* | Prevention | Loan risk monitoring helps in preventing reduce bad debt. |

| Construct | Indicators | Variables | Explanation |
|------------------------|------------|------------------------|---|
| Lending Rate (LR) | LR1 | Appropriateness | Banks appropriately helps to determine lending rates. |
| | LR2* | Effectiveness | Lending rates have more effectiveness on credit risk. |
| | LR3 | Possibility | Having the higher rates, the greater the possibility of bad debt. |
| | LR4* | Arbitrarily | Lending rates are more established arbitrarily. |
| | LR5 | Rules and principle | Lending rates are set as per banking rules and principles. |
| Bad Debt Recovery (BR) | BR1* | Predetermine of policy | Bad debt recovery procedure is predetermined in the organization. |
| | BR2 | Distinct unit | Recovery process is handled by a distinct unit in banks. |
| | BR3 | Challenge | Bad debt recovery is one of the most difficult challenges for banks. |
| | BR4 | Specific rules | Recovery process is likewise governed by specific rules and principles |
| | BR5* | Principles | Recovery process is likewise governed by specific rules and principles. |

Notes. (Richard, 2011; Chukwunulu et al., 2019; Ahmed, 2008)

Notes: The items including LP1 and LP5 from construct 1; LD2 and LD2 from construct 2; RT1 and RT3 from construct 3; LL3 and LL5 from construct 4; LR2 and LR4 from construct 5 and BR1 and BR5 from construct 6 were drop after performing Confirmatory and Explanatory Factor Analysis and these items value remains below 0.5.

highly reliant on the loan officer's use of data and information. Banks are expected to employ the Know Your Customer (KYC) principle as part of a credit risk management plan (Polyviou, 2019).

H₂: Lending decision selection has significant and positive impact on the bad debt recovery.

Lending Rate (LR) and Bad Debt Recovery (BR)

A bank's principal assets include capital and interest receivable. Of them, interest provides a bank's major source of revenue and consequently profit. As a result, it's critical for a bank's borrowers to stick to their contractual obligations and pay interest and capital on time. Defaults are unavoidable, but once they occur, a bank should take appropriate corrective measures or, if that is not possible, immediately recover the overdue interest and capital. These increased rates will inevitably be reflected in the bank's lending rate. Higher lending rates may have an adverse effect on future lending quality, forcing the bank to lend to high-risk borrowers (Njeri & Wanyoike, 2012).

H₃: Lending rate has significant and positive impact on the bad debt recovery.

Recovery Techniques (RT) and Bad Debt Recovery (BR)

The loan recovery unit is involved in the day-to-day function of ensuring that the loans granted to the bank's clients are returned in accordance

with the contract schedule agreed by the bank and its customers (Ahmed, 2008). Debt recovery entails creating and maintaining a list of outstanding debts, as well as managing and arranging the loans practically by following up on defaulters. The loan recovery section works with attorneys to condense demand letters sent to lending borrowers and sends same letter to clients who are in delinquency.

H₄: Recovery techniques have significant and positive impact on the bad debt recovery.

Loan Risk Monitoring (LM) and Bad Debt Recovery (BR)

Banks have introduced loan usage monitoring by debtors not only to verify that funds are used properly, but also to guarantee that they are prepared to deal efficiently with any issue that arises. Banks have used loan data files to evaluate loans to track them (Richard, 2011). Institutions can detect distressed borrowers and excellent value with these categories of borrowers using an effective surveillance method (Embrechts et al., 1999).

In these cases, the loans become bad debt, which has an impact on the issuing bank. As a result of this tendency, there is an increased requirement to guarantee that loans are used effectively by effectively monitoring borrowers (Farhan et al., 2012).

H₅: Risk monitoring has a significant and positive impact on the bad debt recovery.

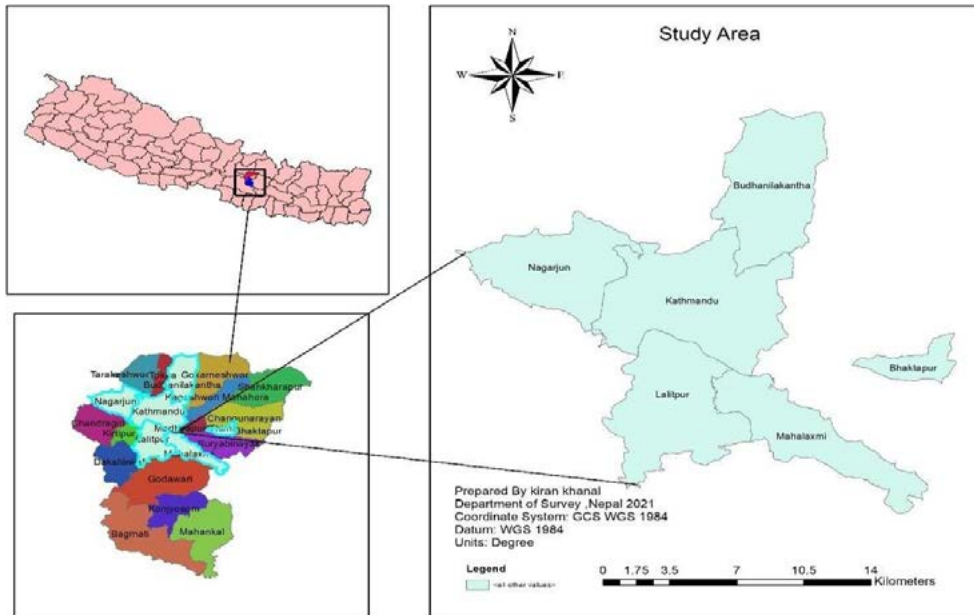


Figure 2. Study Area

Note. Researchers' Work

Note. Photo of Study Area drawn from ArcMap

Variable and its Definition

This section deals with the variables used for the study. The variables used for the study have been identified and defined. Firstly 5 items of lending policies, 5 items of lending decisions, 5 items of lending decisions, recovery techniques, 5 items of monitoring, lending rate and bad debt recovery were adapted for the study. But during clearing and management of data some items were deleted due to low loading. However, the variables given below may not be the only variable used in the study and necessary variables are taken as per the essential of the study. The detailed description of observed variables that SEM has verified is shown in the table 1:

RESEARCH METHODS

Study Area and Population

As for this study, Kathmandu Valley which is situated at Bagmati Province, Nepal is taken as a study population. The valley of Bhaktapur, Kathmandu, and Patan was 899 kilometers square, although Kathmandu is only 665 kilometers. It is located in the Kathmandu region between 27° 32'13" and 27° 49'10" "north" at latitudes north and 85° 11'31" and 85 31'38" east and 1300 meters above sea level. The valley encompasses the entire district of Bhaktapur, half of Lalitpur, and 85 percent of Kathmandu.

The population selected for this study in commercial banks of Kathmandu Valley,

Nepal were banking employees. This choice was made due to their specialized knowledge in debt recovery, direct interaction with customers, and familiarity with internal processes. Examining the viewpoints of stakeholders facilitates a thorough comprehension of obstacles and approaches in the retrieval of delinquent debts, thereby enhancing recovery percentages and the overall fiscal well-being of financial institutions.

Sampling Technique

The present study employed convenience sampling to select a sample of banking employees from multiple commercial banks located in Nepal. The selection of participants was based on their availability and voluntary participation, which may have restricted the extent to which the findings can be generalized. The investigator conducted visits to various commercial banks and solicited participation from employees who were readily accessible and willing to partake in the research.

Sample Size Determination

The sample size determination technique is used to pick the number of observations for the inquiry. [Burmeister and Aitken \(2012\)](#)'s confirmed sample size determination aids in the organization of investigations by assisting in the achievement of strategically relevant outcomes through the efficient and ethical use of research resources. The unavailability of a dependable source of data pertaining to banking employees in Kathmandu valley posed a challenge for the researcher. The researchers employed a non-probability sampling

technique and utilized a statistical formula to determine the necessary sample size for the study. The formula is presented below:

$$N = z^2 pq / l^2$$

Where,

n_0 = sample size required for study,

Standard tabulated value for 5% level of significance (z) = 1.96

p = Prevalence of consumer who purchase products and services through startups 50 % = 0.5

So, $p = 0.5$

$q = 1 - p = 0.5$

Allowable error to be tolerated (e) = 6 %

Total population for the study $n_0 = z^2 pq / e^2$
 $= (1.96)^2 \times 0.5 \times 0.5 / (0.06)^2 = 266.78$

Non-response error 5%,

i.e., $266.78 \times 5 / 100$

$= 13.34$

Thus, sample size taken for study was $(266.78 + 13.34) = 280.12 (\approx 280)$. Due to the COVID-19 researcher was able to calculate 220 samples only.

Research Instruments and Data Collection

To accomplish the goals of this research paper, an explanatory design, which is also referred to as an analytical research design, has been utilized. This design facilitates a comprehensive evaluation and analysis of the topic at hand. The primary data collection instrument used in this study is a structured questionnaire. The use of a structured questionnaire is essential in collecting data from participants and enables

researchers to obtain the information needed to address their research questions. The questionnaire comprises a predetermined set of questions that are intended to elicit specific information from the respondents. The questions have been meticulously designed to ensure that they prompt responses that are both robust and focused. This approach allows the researchers to obtain valuable insights into the subject matter.

The surveys are conducted and monitored using the Kobo Toolbox to ensure the accuracy and reliability of the collected data. This digital platform functions as a tool for conducting surveys and guarantees that the data collection process meets the rigorous standards demanded by Grade A bank clients. This research paper aims to provide a comprehensive understanding of the subject matter by employing an explanatory design and utilizing a structured questionnaire. The goal is to draw meaningful conclusions and make informed recommendations. Adopting a rigorous approach to collecting and analyzing data is crucial in ensuring the validity and credibility of research findings. This, in turn, enhances the overall quality and reliability of the study.

Data Collection Technique

It is carried out using an assessment based on a mean, medium, and mode assessment, and an infernal analysis consisting of structural equation modeling based on numerous latent structures. It is founded on a descriptive examination. For data entry and research

tabulation, data analysis and the usage of Microsoft Excel software such as STATA and SPSS AMOS were used.

The data underwent both descriptive and inferential analysis, incorporating structural equation modeling that relied on various latent constructs. The data analysis process involved the utilization of software tools such as KOBO Toolbox, Microsoft Excel, and SPSS, AMOS. Additionally, Microsoft Excel was employed for data entry and tabulation purposes.

RESULT AND ANALYSIS

Socio Demographic Characteristics

The table presented here displays the distribution of respondents in the commercial banking sector of Nepal, with a focus on variables such as age, gender, level of education, and work experience. After analyzing the data mentioned above, several noteworthy observations can be made regarding the recovery of bad debt and the use of commercial banks. The findings indicate that a considerable percentage of the participants (74.09%) were male, implying a notable gender disparity in the banking sector. The findings indicate that individuals between the ages of 31 to 35 (30%) and 36 to 40 (17.27%) played a significant role in the process of bad debt recovery. This suggests that they were actively involved in this field. Furthermore, a significant proportion of the participants, precisely 155 respondents, possessed a Master's degree, whereas only 57 respondents had a Bachelor's degree. The discovery

Table 2
Socio-Demographic Characteristics

| | Variable | In Percentage/ No. |
|-------------------------------------|------------------|--------------------|
| Sex | Male | 74.09% |
| | Female | 25.90% |
| Age | 21-25 | 7% |
| | 26-30 | 19.09% |
| | 31-35 | 30% |
| | 36-40 | 17.27% |
| | 41-45 | 15% |
| | 46 & above | 11.36 |
| Education Level | Higher Secondary | 5 |
| | Bachelors | 57 |
| | Masters | 155 |
| | Above masters | 3 |
| Experience level of the Respondents | Below 5 years | 46.82% |
| | 5-10 years | 18.64% |
| | Above 12 years | 34.54% |

Note. The surveyed respondent's profile
Note. Authors' Survey

implies that debt recovery personnel possess a greater degree of educational achievement compared to those in charge of other forms of collections. Regarding the professional experience levels of the individuals, a significant proportion of them (34.54%) had more than 12 years of experience. However, the majority of people either had less than five years of experience (46.82%) or had 5-10 years of experience (18.64%). Improving the resolution of gender inequalities and leveraging the expertise of trained professionals are two key strategies that can enhance the effectiveness of commercial banks' debt collection procedures in Nepal.

Bad Debt Recovery Process of Bank

The respondents were then asked if their banks are facing the problem of bad debt, then most respondents spoke of facing the problem of bad debt. Out of 220 respondents, 163 respondents are facing the problem of bad debt, and the remaining 57 of the respondents have responded that their bank is not facing the problem of bad debt. This result shows that banks face the problem. From the responses it was found that 32.72% of the respondents said it is due to improper selection of borrowers, 30.45% said it was due to lack of follow-up measures, similarly 16.38 % said due to inadequate collateral and 20.45% said due to all above factors.

The main obstacle of bad debt recovery as responded by the banker is the customer going bankrupt, which shows that if only the customer has nothing to pay back then it becomes the main hurdle in the bad debt recovery process of the banks. Further, 67 of the respondents added that the customer falling out of their business unexpectedly is also the other main reason the hurdle in the bad debt recovery process. For the recovery, it was seen that the written communication is the procedure of the bad debt recovery that the banks are adopting in their organization as 117 respondents have responded on the argument that written communication is the main recovery process adopted. Only 22 responded that offering incentive for prompt payment is the other procedure of the bad debt recovery, likewise 48 respondents responded that rescheduling the bad debt is the other recovery process.

Factors Affecting Bad Debt Recovery in Nepalese Commercial Banks

Lending policies, lending decisions, lending rates, recovery techniques, loan risk monitoring & Bad Debt Recovery are the variables taken in this study. These variables are measured in five scale under Likert scale (1 = Strongly Disagree, 2 = Disagree, 3 = Neutral, 4 = Agree, 5 = Strongly Agree).

Lending policies are critical components of lending investment management; policies should cover the bank's loan assessment and documenting, lending obligations, and the security appraisal process and laws. It was observed that

most of the respondents agreed that lending policies also plays an important role in the bad debt recovery. Similarly, the lending decision is another variable selected. Most of the respondents have agreed that the lending decision is also important for the bad debt recovery process. While lending loan to any clients, the required precautions and the set procedures are followed, so that it can help reduce bad debt. Furthermore, Banks have used loan data file to evaluate loans in order to track them (Richard, 2011). The study has revealed that most of the respondents agreed that loan risk monitoring procedure has been monitored fine by all the related and responsible authorities.

Debt recovery comprises compiling and keeping a list of outstanding debts, as well as managing and organizing the loans practically through follow-up on defaulters. The loan recovery team works with attorneys to condense demand letters sent to lending borrowers, and then sends the identical letter to delinquent consumers. It was seen that recovery techniques are satisfactory. However, a certain area of improvements is still there to reduce the ratio of bad debt. The banks should have applied other improved techniques to reduce the bad debt ratio of the banks. "Lending rates are set as per banking rules and principles & Lending rates are not established arbitrarily." Both of these statements were agreed with by the majority of the respondents and hence it can be concluded that the lending rates of the banks are set properly. Further. It was also asked if the rate has

a relationship with bad debt or not and it was proved that the lending rates also determines the bad debt of the bank. It was further found that the bankers consider the bad debt recovery process as the main challenges for the banks in the overall operation of the business. In The statement “The bad debt recovery procedure is predetermined in the organization.” Most respondents agreed upon the statement, through which it can be concluded that bad debt recovery process is the predetermined procedure in every organization.

Inferential Analysis

Summary statistics seem to be the most effective way of summarizing the features of big sets of data since they are a quick summary and synthesis of data acquired from a set of people of analysis (Mtembu, 2017). There are a total of 220 replies received from commercial banks in the Kathmandu valley. The skewness of each variable in the preceding table ranged from - 1 to 0. It suggests that the data was biased unfavorably. Similarly, the kurtosis values in the preceding table were greater than +1, indicating that the

Table 3
Reliability and Validity

| Construct | Indicators | Factor loading | Cronbach's Alpha | CR | AVE | MSV |
|----------------------|------------|----------------|------------------|-------|-------|-------|
| Lending polices | LP2 | 0.880 | 0.922 | 0.824 | 0.362 | 0.362 |
| | LP3 | 0.897 | | | | |
| | LP4 | 0.912 | | | | |
| Lending decision | LD1 | 0.820 | 0.857 | 0.923 | 0.166 | 0.166 |
| | LD3 | 0.811 | | | | |
| | LD5 | 0.794 | | | | |
| Recovery techniques | RT2 | 0.877 | 0.910 | 0.859 | 0.338 | 0.338 |
| | RT4 | 0.895 | | | | |
| | RT5 | 0.908 | | | | |
| Lending rate | LR1 | 0.750 | 0.819 | 0.911 | 0.181 | 0.181 |
| | LR3 | 0.847 | | | | |
| | LR5 | 0.766 | | | | |
| Loan risk monitoring | LM1 | 0.843 | 0.881 | 0.884 | 0.362 | 0.362 |
| | LM2 | 0.837 | | | | |
| | LM4 | 0.763 | | | | |
| Bad debt recovery | BR2 | 0.805 | 0.782 | 0.783 | 0.338 | 0.338 |
| | BR3 | 0.789 | | | | |
| | BR4 | 0.754 | | | | |

Note. This table contains the gaskination test, validity test and reliability test.

Note. Researchers' Calculation

Table 4
Inter-construct correlation Matrix

| | LR | LP | LD | RT | LM | BR |
|----|-------|-------|-------|-------|-------|-------|
| LR | 0.781 | | | | | |
| LP | 0.404 | 0.894 | | | | |
| LD | 0.514 | 0.407 | 0.819 | | | |
| RT | 0.313 | 0.179 | 0.359 | 0.879 | | |
| LM | 0.602 | 0.348 | 0.514 | 0.426 | 0.847 | |
| BR | 0.454 | 0.367 | 0.581 | 0.299 | 0.503 | 0.739 |

Note. Inter-construct correlation matrix and discriminant validity

Note. Authors' Estimation from AMOS and Gaskination

variation is excessive. The bigger value of kurtosis was 2.876, while the smaller value was -0.968.

Exploratory Factor Analysis (EFA)

Exploratory Factor Analysis (EFA) is a multidimensional mathematical method that has fundamentally formulated and proven hypotheses and measures (Watkins, 2018). For data validity and dependability, we examine the KMO and Bartlett Test, Communalities of data, and rotated compounded matrix in this part. KMO is $0.854 > 0.5$ and BTS is $0.00 < 0.001$, indicating that there is no problem with data dependability and validity. Common method bias is "variance attributable to the measuring procedure rather than the structures of interest." Before analyzing the psychometric qualities (reliability and validity) of the constructs under consideration, it is recommended to ensure that the data gathered is free of biases such as common method bias and social desirability bias (Sreeram, 2017). Harman's single-factor test is used to see if the first extracted

component explains more than 50% of the variation in the results of an EFA study (Aguirre-Urreta & Hu, 2019). The overall variation for a single element in this study is 41.11 %, which is less than 50%, indicating that the study is free of common technique bias.

Confirmatory Factor Analysis (CFA)

LISREL 8.80 was used as component of a confirmatory component analysis, as recommended by Castor (2009). Several fit indicator values, such as CMINDF, RMR, GFI, CFI, IFI, TLI, and RMSEA, are compared with variable outcomes for the confirmatory analysis. The table below indicates that the latent variables CMINDF, RMR, GFI, CFI, TLI, IFI, and RMSEA meet the requirements of fit. This result shows that the chosen model is suitable for the investigation. When compared to other areas of concern, we may conclude that our validity and dependability are adequate, although there is space for improvement. "Validity" is defined as "the computation as to anything that test is used to measure or presumes to measure" (Guion, 1980).

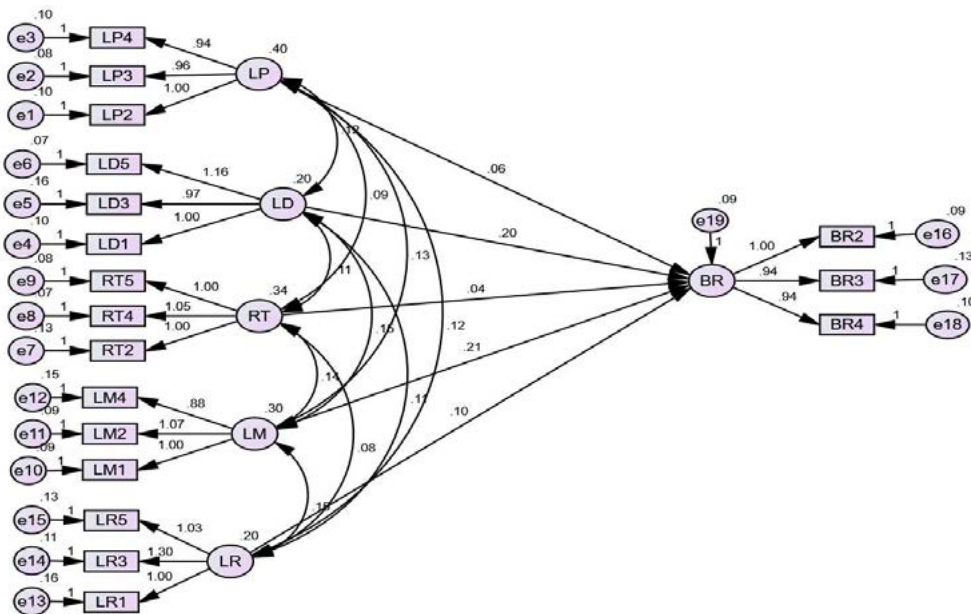


Figure 3. *Structural Model*
 Note. Path analysis drawn from AMOS
 Note. Researchers' Calculation

In this part, we assess the reliability of the data acquired for the study (N=287). Convergent validity is the degree to which two conceptually equivalent construction tests are now connected. An effective Discriminant validity evaluation, on the other hand, demonstrates that a concept test is not so intimately related to certain other tests that evaluate possibly separate ideas (Campbell & Fiske, 1959).

For the validation of data, they must assure certain condition, they are $AVE > 0.5$, $CR > 0.70$, $CR > AVE$, $AVE > MSV$, $AVE > ASV$ and $\sqrt{AVE} > r$ (correlation). When these criteria are compared to the above-mentioned results, the data meet all the validity requirements (see table 3). As a result, we may infer that there is no validity issue. Table 4 shows the inter-construct

correlation matrix which shows the square root of AVE and indicates there is no issue of discriminant validity in dataset.

Path Analysis and Hypotheses Testing

Path analysis is an extension of multiple regression that evaluates the strength and importance of alleged causal relationships between groups of elements (Gonzalez et al., 2022). When changes in one variable result in changes in another, this is known as a directional causal relation in character. Using Path analysis, which started with the formation of a line graph on the graphical AMOS screens application, the structural model was verified. Latent variables, observable variables, and error variables are the three variables.

Table 5
Test of Hypothesis

| Hypothesis | Estimate | S.E. | C.R. | P | Hypothesis Result |
|------------|----------|------|-------|------|-------------------|
| LP→ BR | .059 | .051 | 1.147 | .251 | Rejected |
| LD→ BR | .198 | .099 | 2.001 | .045 | Accepted |
| LR→ BR | .101 | .093 | 1.084 | .278 | Rejected |
| RT→ BR | .036 | .055 | .660 | .509 | Rejected |
| LM→ BR | .212 | .080 | 2.664 | .008 | Accepted |

Note. level of significance is 5%

Note. Researchers' Calculation

Figure 3 shows the structural model, which consists of 6 latent constructs, 18 observable variables and 19 error variables. Here, construct LP explains only 6% to dependent variable BR, LD explains 20% to BR, RT explains only 4% to BR, LM explains 21% to BR and LR explains 10% to BR, respectively. Similarly, in hypotheses testing there are 5 hypotheses which are tested at 0.05 level of significance Table 5 displays the results of the hypothesis testing conducted by the authors, who tested a total of 5 hypotheses. LD→BR and L→BR were found to be statistically significant among them.

DISCUSSION

The recovery of bad debts is a crucial factor in determining the financial health and stability of banking institutions. This analysis provides a thorough examination of the main themes and arguments related to the factors that affect the recovery of bad debts. According to the Federal Deposit Insurance Corporation (2012), it is crucial to establish clear lending policies that allow for efficient monitoring, including by directors. It is the responsibility of each

bank to develop credit policies and ensure their proper implementation. [Chukwunulu et al. \(2019\)](#) emphasize the importance of carefully selecting entrepreneurs to effectively secure and manage a bank's bad debts. The study recommends that caution should be exercised when selecting entrepreneurs who possess the necessary willingness, competence, traits, and expertise for establishing and operating industrial units. By following this method, there is a greater chance of protecting the bank's investments and achieving precise and punctual returns.

Despite the initial hypothesis that lending rates have an insignificant impact, it has been discovered that they have a significant influence on bad debt recovery. According to [Njeri and Wanyoike \(2012\)](#), increased lending rates can have a negative impact on the quality of future lending. This could result in banks being compelled to lend to borrowers with a high-risk profile. Furthermore, [Mawele \(2020\)](#), banks will modify their lending rates to manage the incidence of defaulting loans, highlighting the correlation between interest rates and the quality of lending.

Emerson (2017) emphasized the importance of recovery techniques in reducing bad debts. Emerson's study highlights the crucial role of loan recovery units, which contradicts the hypothesis that suggested no impact and was ultimately rejected. These units are responsible for ensuring that the bank's clients repay their loans according to the agreed schedule daily. These units minimize the risk of bad debts by actively engaging in loan recovery.

Hypothesis 5 and a study conducted by Embrechts et al. (1999) both provide evidence for the importance of loan risk monitoring in the recovery of bad debt. Institutions can effectively detect distressed borrowers and accurately determine their value using surveillance methods. Maintaining sound banking performance and minimizing bad debts are crucial, and proactive risk monitoring plays a vital role in achieving these goals.

Effective managerial communication is an important aspect of balancing banking performance in Nepal, as highlighted by Parajuli et al. (2020); Paudel et al. (2020); and Kayastha et al. (2022). Although not directly linked to bad debt recovery, it plays a crucial role in overall banking operations. Effective communication among managers is crucial for the efficient functioning of banking institutions and can significantly improve overall performance.

The analysis of several studies indicates the interrelated factors that impact the recovery of bad debt in the banking industry. This highlights the importance

of having clearly defined lending policies, setting appropriate lending rates, implementing effective loan recovery techniques, monitoring loan risks, and maintaining effective communication among managers. It is clear that a thorough strategy for tackling bad debts is crucial in maintaining the financial stability of banking institutions in the long run, as demonstrated by the incorporation of these significant themes and arguments.

CONCLUSION AND IMPLICATIONS

This research has illuminated the viewpoints of bankers regarding the obstacles of recovering bad debts in commercial banks in Nepal. The objective of the study was to gain an understanding of the debt recovery process, identify the main reasons for bad debts, recognize any obstacles that may arise during the recovery process, and suggest ways to reduce loan defaults. The results indicate that the process of recovering bad debts is significantly affected by lending rates, policies, and other related factors. The relationship between bad debt, interest rates, and other factors has received significant attention. This has prompted other researchers in the field of monetary economics to further investigate the causation and long-term impact of interest rates on bank credit defaults.

Although lending is essential for banks to maintain their operations, it also involves inherent risks. The significant challenge faced by Nepalese banks is credit grant risk due to the alarming extent of non-performing assets. Hence, it is crucial

to carefully select clients and customers proactively during the loan approval process. The banking sector in Nepal operates in a society and economy that is diverse, which requires them to have flexible and comprehensive banking operations to cater to the varying needs of individuals and businesses.

To ensure successful recovery of bad debts, it is essential for Nepalese banks to strictly comply with the regulations and rules established by the Nepal Rastra Bank [NRB]. Incorporating an enhanced credit evaluation system can assist in reducing the likelihood of unpaid debts. Once bad debt has been incurred, the presence of a supportive legal system becomes crucial. This is because the recovery process often involves litigation and court orders to recover stock loans. During times of economic slowdown and decreasing inflation, the likelihood of bad debt increases. Therefore, it is crucial for bank management to prioritize the implementation of measures aimed at controlling and managing bad loans, particularly during such challenging times.

The implications for bankers working in Nepalese commercial banks are significant. Bankers must prioritize risk management strategies, including

rigorous client selection, adherence to regulations, and the implementation of robust credit evaluation systems. Furthermore, it is crucial to uphold a robust legal framework for debt recovery to expedite the effective resolution of delinquent debts. Bankers can ensure the financial stability of their institutions by closely monitoring economic indicators and proactively managing loan portfolios to minimize the impact of bad debts.

Additional research is necessary to enhance the comprehension of bad debt recovery in commercial banks of Nepal. Further research could investigate additional variables that impact bankers' perspectives to obtain a more comprehensive understanding. In addition, it is worth noting that this study was limited to commercial banks located in the Kathmandu Valley. Therefore, it is crucial to conduct further research in other banks to obtain a more comprehensive understanding of the challenges associated with bad debt recovery in Nepal. Undertaking such research will offer valuable insights to bankers, enabling them to make informed decisions and develop effective strategies to address the challenges associated with bad debt recovery in the Nepalese banking sector.

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