Liquidity Glut and Credit Crunch in the Face of Economic Slowdown: Perspectives of Nepalese Stakeholders

Suraksha Subba and Sumit Pradhan*

Abstract

This study examines the liquidity glut and credit crunch in the face of economic slowdown: Perspectives of Nepalese stakeholders. Economic slowdown is the dependent variable. The selected independent variables are government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, and consumer confidence. The primary source of data is used to assess the opinions of respondents regarding government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, consumer confidence, and economic slowdown. The study is based on primary data of 130 respondents. To achieve the purpose of the study, structured questionnaire is prepared. The correlation and multiple regression models are estimated to test the significance and importance of liquidity glut and credit crunch in the face of economic slowdown: Perspectives of Nepalese stakeholders.

The study showed a negative impact of government policies on economic slowdown. It indicates that supportive governmental actions or regulations leads to reduce economic slowdown. Similarly, the study showed a positive impact of exchange rate volatility on economic slowdown. It indicates that frequent fluctuations in currency values can disrupt trade, investment, and overall economic stability, leading to an increase in the pace of economic slowdown. Likewise, the study showed a negative impact of banking sector growth on economic slowdown. It indicates that higher the banking sector growth, lower would be the economic slowdown. Further, the study showed a negative impact of credit demand on economic slowdown. It indicates that higher the credit demand, lower would be the economic slowdown. In addition, the study showed a negative impact of interest rate policies on economic slowdown. It indicates that central bank of Nepal should adopt accommodative interest rate policies, such as lowering interest rates during economic downturns to encourage borrowing and spending. Moreover, the study also showed a negative impact of consumer confidence on economic slowdown. It indicates that pessimistic consumer sentiment can contribute to reduced spending and investment, thereby dampening economic activity.

Keywords: government policies, exchange rate volatility, credit demand, banking sector growth, interest rate policies, consumer confidence, economic slowdown

1. Introduction

Liquidity gluts is not excessive savings, but excessive monetary liquidity that flows causing depressing long-term interest rates (Paraso, 2019). Liquidity risk derives by lack of required liquid assets to meet or fulfill the immediate debt commitments and unexpected withdrawal of deposits or outflow of cash (Diamond and Rajan, 2005). Liquidity is the elephant in the dark room that is the global financial system. One of the disturbing aspects of 'liquidity' is that its meanings and functions as a financial category vary according to the context and level of economic activity, as well as to the phase of the business cycle (Nesvetailova, 2008). Liquidity of the market or a portfolio of assets during 'good' times is not the same as liquidity during an economic downturn or a financial crisis. Assets that

* Ms. Subba is a Freelance Researcher, Kathmandu, Nepal and Mr. Pradhan is the Research Coordinator, Uniglobe College (Pokhara University Affiliate), Kathmandu, Nepal.

are easy to sell when economic agents share a sense of optimism about their profitability, liquidity and safety, often turn out to be unwanted and expensive bundles of 'illiquid' debt when the sense of optimism evaporates. Credit crunch refers to a sudden reduction in the availability of loans or abrupt contraction of the situations required to get a loan from the banking sector, which generally involves a decrease in the availability of credit independent of a rise in official interest rates. An inefficient banking sector may lead to liquidity problems as a result of the credit crunch and shadow economy (Omar *et al.,* 2020). Credit risk is defined as the debtor's failure to fulfil obligations leading to an increase in non-performing loans, can precipitate a banking crisis (Ahmed *et al.,* 2022). Banks with higher capital levels can engage in diverse business activities and achieve greater profitability (Abbas *et al.,* 2019). Credit risks fluctuate with economic conditions, typically easing during recessions and tightening in booms (Kesraoui *et al.,* 2022). The financial sector, often leading to serious banking issues due to customer non-performance (Madugu *et al.,* 2020). Credit risk usually is the most considerable risk impacting the bank's performance (Boffey and Robson, 1995). The rise in the default loan trend appears to be a significant predictor of credit risk, and this has gained significant attention, given the linkage between CR and financial instability (Porath, 2006).

Credit exposes the banks to loan (investment) default or CR. The Basel committee indicated CR as to the probability of borrowers not reimbursing the loan (investment) in full or in part. LR considers the "profit lowering cost" where a problem loan (investment) or loan (investment) default enhances this LR due to the reduced and blocked cash inflow and the allowances it requires against the increasing amount of credit risk (Dermine, 1986). Credit risk (CR) relates to a loan or finance given by a bank, which on time isn't reimbursed partially or fully by the borrowers (Campbell, 2007). Credit crunch is a situation where there is a significant decrease in the supply of credit compared to the demand for credit, thus forming a new equilibrium (Belke and Polleit, 2009). The IMF also defined credit crunch as a decrease in the supply of credit from banking institutions as a result of a decline in the capital value of banks as well as the effects of regulators and certain situations that make banks decide to hold more of their capital. Liquidity can be taken as synonymous with the customary monetary aggregates, which in turn are broadly defined as corresponding to certain deposits by the domestic non-bank sector with commercial banks. Money supply thus arises chiefly as a result of monetary transactions between the domestic non-bank sector and other sectors (Heise *et al.,* 2005). Savings and credit cooperatives (SACCOs) are the most important financial institutions that provide funds for economic activities particularly in developing countries where capital markets and financial sector at large are still in development stages. SACCOs are influenced by factors which determine their ability to continue performing their functions effectively. Liquidity is one of the factors that affect the functioning of SACCOs (Hessou, 2018).

An effective liquidity management requires financial institutions to estimate and plan for liquidity demands over various periods and to consider how funding requirements may evolve under various scenarios, including adverse conditions (Njeri, 2014). IB's liquidity risk sources are different from those faced by conventional banks (CBs). Such as, first, investment venues of IBs are limited. However, they have to pay profits on their collected deposit, which produces liquidity risk. Second, the money market of IBs is restricted; it is difficult for IBs to generate funds during a short-term liquidity crisis. Third, as per regulatory requirements, all banks have to maintain reserves with the central bank, and under Islamic banking law, IBs are not allowed to receive interest from the central bank. Therefore, IBs need to keep more liquid

assets in cash (Hassan *et al.,* 2019). For the purpose of our study to address those issues, we use different liquidity risk indicators. In Commercial Bank, liquidity refers to the Bank's capacity to meet all its financial commitments when required. Such obligations comprise providing loans (investments) (investments), deposit and matured liability withdrawals, and investments during the bank's normal operations (Amengor, 2010).

Kluza (2014) investigated impact of the economic slowdown on local government investments, debt and productivity in the Eu countries. The growing level of debt is becoming a true concern for local governments. Taking into consideration also the lasting fiscal strains, this shows the limited potential for further stimulation of the economy with debt / deficit instruments, such policies appear to be unsustainable, both in the context of future debt repayments, as well as the failure to lead to increased productivity. As a result, this may undermine the pace of future economic revival, despite the generally positive impact of local government policies on the economy during the crisis. This indicates a strong need for further research on how to conduct the deleveraging process in local government sectors without causing negative spillover effects on economic growth. Hanipah *et al.* (2023) examined analysis of the impact of government fiscal and monetary policies on economic growth in Indonesia: government economic approach. Fiscal policy and monetary policy are crucial instruments in government economics, influencing economic growth in countries like Indonesia. Fiscal policy, including government spending on infrastructure projects and social programs, positively impacts economic growth. Monetary policy, such as interest rate policy and banking regulations, has a less significant impact. Both policies play a crucial role in overcoming economic challenges and promoting economic growth.

Tula *et al.* (2024) highlighted the importance of government policies in fostering entrepreneurship, highlighting the US's success in this area through tax incentives, Small Business Administration programs, and innovation initiatives. It also highlighted the need for flexible regulations to promote innovation while ensuring consumer protection. In Africa, the study examined the diversity of government approaches, including entrepreneurial ecosystems, funding mechanisms, and regulatory frameworks. It emphasizes the need for context-specific policies that consider the unique socio-economic conditions of each African nation. The review underscores the critical role of government policies in fostering entrepreneurship and driving economic development. Nor *et al.* (2012) examined the impact of exchange rate volatility on the stock market in Malaysia. The study investigated the relationship between the stock market and exchange rate, focusing on the impact of exchange rate volatility on the stock market in Malaysia. Using the Johansen co-integration test approach, the results show a co-integrating relationship between the stock market and exchange rate volatility, with both factors contributing to the stock market. The study also reveals a volatility spillover effect, suggesting the integration of these markets is time-dependent. Effect of economic policy uncertainty on exchange rate volatility in Pakistan was examined by Shair (2023). The study explored the impact of economic policy uncertainty on Pakistan's exchange rate, highlighting the widening inflow-outflow gap in foreign exchange. Volatility in the exchange rate, primarily due to nominal variables, slows down productivity and GDP growth. The EGARCH model suggested that economic policy uncertainty positively affects the exchange rate, with an increase in uncertainty causing increased volatility. Recommendations are provided to stabilize the foreign exchange market in Pakistan.

In the context of Nepal, a non-performing loan (NPL) is a sum amount of borrowed

money in which the debtor has not made the scheduled payments for a specified period. NPL indicates the quality of assets of the banks. As per central bank regulation banks should be made a provision against NPL prescribed by NRB. Credit risk is a major risk of commercial banks, hence, measurement, control, and management of credit risk is the core task of risk management. The risk of commercial banks mainly indicates by the accumulation size of non-performing loans (Tang *et al.,* 2009). Liquidity means allocation of funds in close relation to their respective sources. Liquidity is the status and part of the assets which can be used to meet the obligation in the commercial banks. Liquidity can be viewed in terms of liquidity stored in the balance sheet and in terms of liquidity available through purchased funds. Liquidity is the ability of a bank to pay cash to depositors on demand (Poudel, 2021). In Nepalese scenario, first type of liquidity risks arises when depositors of commercial bank seek to withdraw money. They become insolvent if the assets are not enough to meet the liability withdrawals. Similarly, the second types of liquidity risk arise when money supply cannot meet the demand of unexpected loans due to the lack of funds (Baral, 2005). Credit risk and liquidity, which are internal factor influencing banks profitability, and focused on its relationship with bank profitability, and sought some solutions to increase efficiency and profitability for bank managers. Shrestha (2012) revealed that the overall profitability of the sample banks has normally an increasing trend. The overall trend of liquidity ratios is not largely smooth.

The above discussion shows that empirical evidences vary greatly across the studies on the liquidity glut and credit crunch in the face of economic slowdown: Perspective of stakeholders. Though there are above mentioned empirical evidences in the context of other countries and in Nepal, no such findings using more recent data exist in the context of Nepal. Therefore, in order to support one view or the other, this study has been conducted.

The major objective of the study is to examine the liquidity glut and credit crunch in the face of economic slowdown: Perspective of stakeholders. Specifically, it examines the relationship of government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, and consumer confidence with liquidity glut and credit crunch in the face of economic slowdown.

The remainder of this study is organized as follows: section two describes the sample, data, and methodology. Section three presents the empirical results and final section draws the conclusion.

2. Methodological aspects

The study is based on the primary data which were collected from 130 respondents through questionnaire. The study employed convenience sampling method. The respondents' views were collected on government policies, exchange rate volatility, credit demand, banking sector growth, interest rate policies, consumer confidence, and economic slowdown. This study is based on descriptive as well as causal comparative research designs.

The model

The model estimated in this study assumes that the economic slowdown depends upon liquidity glut and credit crunch. The dependent variable selected for the study is economic slowdown. Similarly, the selected independent variables are government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, and

consumer confidence. Therefore, the model to be estimated in this study is stated as follows:

Economic slowdown = *f* (government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies and consumer confidence).

More specifically,

$ES = \beta_0 + \beta_1 GP + \beta_2 ERV + \beta_3 BSG + \beta_4 CD + \beta_5 IRP + \beta_6 CC + e$

Where,

ES = Economic slowdown

GP = Government policies

ERV = Exchange rate volatility

BSG = Banking sector growth

CD = Credit demand

IRP = Interest rate policies

CC = Consumer confidence

Economic slowdown was measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "I perceive the current economic conditions to indicate a significant slowdown", "I am concerned about the ongoing economic slowdown" and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.788$).

Government policies were measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include, "Government policies have effectively mitigated economic slowdown in Nepal", "Policies regarding taxation and fiscal incentives have positively influenced economic activity in Nepal" and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.701$).

Exchange rate volatility was measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "Exchange rate volatility impacted the confidence of Nepalese shareholders amidst the economic slowdown", "Fluctuation in exchange rates have contributed to the current economic slowdown in Nepal" and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.861$).

Credit demand was measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "The demand for credit among Nepalese shareholders changed due to the ongoing economic slowdown", "I am optimistic about future credit demand trends among Nepalese shareholders as economy navigates through this period of slowdown." and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.811$).

Banking sector growth was measured using a 5-point Likert scale where the

respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "Growth of Nepal's banking sector influences the severity of liquidity gluts and credit crunches during economic slowdown", "I am satisfied with the responsiveness of banks in Nepal towards providing financial assistance and support to shareholders affected by the slowdown." and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.763$).

Interest rate policies was measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "Interest rate policies impact consumer spending and investment behavior during economic slowdown", "Interest rate stability plays a crucial role in maintaining investor confidence and supporting economic growth in Nepal" and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.877$).

Consumer confidence was measured using a 5-point Likert scale where the respondents were asked to indicate the responses using 1 for strongly disagree and 5 for strongly agree. There are 5 items and sample items include "I am optimistic about a potential rebound in consumer confidence levels among Nepalese shareholders as sign of recovery emerge from this current phase of slow growth", "I believe that targeted marketing strategies aimed at rebuilding consumer trust, could positively impact overall consumption trend among Nepalese shareholders during challenging economic times" and so on. The reliability of the items was measured by computing the Cronbach's alpha ($\alpha = 0.829$).

The following section describes the independent variables used in this study along with the hypothesis formulation.

Government policies

Government policies includes various decisions, actions, and controls made by leaders to achieve certain goals in society. These policies may include taxation, spending, administration, trade, health, welfare, education, and more. It is the framework within which governments solve problems, create business operations, and influence social dynamics. Maula *et al.* (2023) revealed that fiscal policy and monetary policy are crucial instruments used by the government to control economic growth. In Indonesia, fiscal policy, particularly government spending on infrastructure projects and social programs, positively influences economic growth. However, monetary policy, such as interest rate policy and banking regulations, has a less significant influence. Both fiscal and monetary policies play a significant role in fostering economic growth. Toni *et al.* (2023) showed that there is the negative relationship between Chile's economic slowdown and its internal policy regime change, indicating a significant and negative impact on its economic performance. The slowdown deviates from its previous growth trajectory, with the primary cause attributed to internal policy regime change rather than external factors like global economic shocks. The estimated loss of almost 10% in real GDP per capita further underscores the negative impact of the policy shift on Chile's economic prosperity. Makogon & Chugunov (2016) argued that government policy plays a crucial role in promoting economic growth and stability. Effective regulation systems can influence social and economic processes, achieving strategic goals. The significance of budget policy lies in its ability to accelerate social and economic processes. The focus on strengthening investment, innovation, tax revenue structures, and managing public debt is essential to mitigate negative impacts and promote stability during

challenging economic periods. Based on it, this study develops the following hypothesis:

H_1: There is a positive relationship between government policies and economic slowdown.

Exchange rate volatility

Exchange rate volatility refers to the degree of fluctuation or instability in the value of a currency relative to other currencies in the foreign exchange market. Essentially, it reflects how much a currency's value changes over a specific period of time. Mareeh *et al.* (2024) explored the relationship between economic sanctions and exchange rate volatility, revealing a positive correlation and an inverse relationship between reserves-to-GDP ratios and economic growth. The negative correlation suggests the need for adaptive policies and international cooperation to maintain economic stability and promote prosperity, particularly in managing reserves under sanctions constraints. Niyonsaba (2023) showed that the volatility of the exchange rate has a higher influence on economic growth, emphasizing the need for effective policy interventions. Based on it, this study develops the following hypothesis:

H_2: There is a negative relationship between exchange rate volatility and economic slowdown.

Banking sector growth

Globally, banking sector stability has been acknowledged as the central pillar of financial sector growth and, by extension, the global economy Edet *et al.* (2024). The relationship between banking stability and economic growth in Nigeria is predominantly positive, with a unit increase in bank stability, financial depth, and performance fostering a conducive environment for financial activities. However, excessively high interest rates can hinder growth, suggesting a need for moderate interest rates to foster economic growth and enhance Nigerian banks' international competitiveness. Amaegberi & Krokeyi (2023) study found a significant positive relationship between changes in Nigeria's banking industry and economic growth. The liquidity ratio showed a positive and statistically significant effect on economic growth, while the cash reserve ratio showed a non-statistically significant effect. However, the monetary policy rate had a negative effect on economic growth before the banking sector reforms. Based on it, this study develops the following hypothesis:

H_3: There is a positive relationship between banking sector growth and economic slowdown.

Credit demand

Credit demand refers to the desire or need of individuals, businesses, or governments to borrow money from financial institutions or other lenders to finance their activities, investments, or expenditures. The relationship between credit growth and economic growth in emerging market economies like India is complex. Demand-side factors, such as lower investment demand and global supply bottlenecks, have negatively impacted credit growth. This slowdown can hinder economic growth by restricting access to financing and hindering investment and consumption activities. Strong policy support is needed to uphold credit demand and stimulate economic activity. Understanding these factors can help policymakers implement targeted interventions for economic stability and development Gosh (2023). Balke & Zeng (2012) explored the impact of credit demand, financial intermediation, and funds on economic activity and credit conditions. The study revealed that changes in financial intermediation and credit demand significantly influence interest rate spreads and credit quantity. However, economic downturns can disrupt financial intermediation

processes, leading to a decline in credit availability and economic activity. Understanding these drivers can help policymakers implement measures to mitigate the adverse effects of economic downturns and promote financial stability. Based on it, this study develops the following hypothesis:

H_4: There is a negative relationship between credit demand and economic growth.

Interest rate policies

Interest rate policies are deliberate actions by central banks or monetary authorities to set and adjust interest rates to achieve economic objectives like controlling inflation, stimulating growth, or stabilizing financial markets. Thimmavajjala (2020) the study discussed the role of monetary policy, particularly interest rate policies, in addressing the economic slowdown in India. Khodary (2024) found that interest rates significantly impact economic growth in Morocco. Increased money supply stimulates economic activity, while higher interest rates dampen downturns. Inflation positively influences short-term growth, although high rates may lead to long-term instability. Gong (2024) investigated the influencing factors of interest rates in China, focusing on inflation, liquidity demand, and economic growth. It revealed a significant impact of social financing growth rate on interest rates, suggesting changes in credit availability can influence interest rates. The study emphasized the role of supply and demand dynamics in determining interest rates, offering valuable insights for policymakers and economists managing economic downturns in China. Based on it, this study develops the following hypothesis:

H_5: There is a positive relationship between interest rate policies and economic slowdown.

Consumer confidence

Consumer confidence is the optimism or pessimism consumers have about their economic situation and future prospects, influencing spending, economic activity, and inflation. High confidence leads to increased spending, while low confidence may result in reduced spending. Cofnas (2015) study showed consumer Confidence data significantly influences market movements, with positive growth indicating economic expansion, while a decline signals economic slowdown. Understanding these indicators is crucial for traders to develop effective trading strategies, as unexpected data releases can significantly impact market movements. Matsusaka & Sbordone (1995) showed Consumer confidence has a positive relationship with economic fluctuations, with higher confidence levels indicating increased economic activity, while lower confidence levels may contribute to economic slowdowns. Based on it, this study develops the following hypothesis:

H_6: There is a positive relationship between consumer confidence and economic slowdown.

3. Results and discussion

Correlation analysis

On analysis of data, correlation analysis has been undertaken first and for this purpose, Kendall's Tau correlation coefficients along with mean and standard deviation has been computed and the results are presented in Table 1.

Table 1

Kendall's Tau correlation coefficients matrix

This table presents Kendall's Tau correlation coefficients between dependent and independent variables. The correlation coefficients are based on 130 observations. The dependent variable is ES (Economic slowdown). The independent variables are GP (Government policies), ERV (Exchange rate volatility), BSG (Banking sector growth), CD (Credit demand), IRP (Interest rate policies), and CC (Consumer confidence).

Variables	Mean	S.D.	ES	GP	ERV	BSG	CD	IRP	CC
ES	3.34	0.64	1						
GP	3.52	0.71	-0.315**	1					
ERV	3.34	0.68	0.331**	0.379**	1				
BSG	3.52	0.67	-0.254**	0.153*	0.464**	1			
CD	3.65	0.70	-0.327**	0.210**	0.514**	0.556**	1		
IRP	3.71	0.71	0.353**	0.424**	0.312**	0.331**	0.399**	1	
CC	3.51	0.57	-0.503**	0.558**	0.614**	0.470**	0.540**	0.562**	1

Notes: The asterisk signs (**) and (*) indicate that the results are significant at one percent and five percent level respectively.

Table 1 shows that government policies are negatively correlated to economic slowdown. It indicates that supportive governmental actions or regulations leads to reduce economic slowdown. Similarly, exchange rate volatility is positively correlated to economic slowdown. It indicates that frequent fluctuations in currency values can disrupt trade, investment, and overall economic stability, leading to an increase in the pace of economic slowdown. Likewise, banking sector growth is negatively correlated to economic slowdown. It indicates that higher the banking sector growth, lower would be the economic slowdown. Further, credit demand is negatively correlated to economic slowdown. It indicates that higher the credit demand, lower would be the economic slowdown. In addition, interest rate policies are negatively correlated to economic slowdown. It indicates that central bank of Nepal should adopt accommodative interest rate policies, such as lowering interest rates during economic downturns to encourage borrowing and spending. Moreover, consumer confidence is also negatively correlated to economic slowdown. It indicates that pessimistic consumer sentiment can contribute to reduced spending and investment, thereby dampening economic activity.

Regression analysis

Having indicated the Kendall's Tau correlation coefficients, the regression analysis has been carried out and the results are presented in Table 2. More specifically, it shows the regression results of government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, and consumer confidence on economic slowdown.

Table 2

Estimated regression results of government policies, exchange rate volatility, banking sector growth, credit demand, interest rate policies, and consumer confidence on economic slowdown.

The results are based on 130 observations using linear regression model. The model is $ES = \beta_0 + \beta_1 GP + \beta_2 ERV + \beta_3 CD + \beta_4 BSG + \beta_5 IRP + \beta_6 CC + e$, where the dependent variable is ES (Economic slowdown). The independent variables are GP (Government policies), ERV (Exchange rate volatility), BSG (Banking sector growth), CD (Credit demand), IRP (Interest rate policies), and CC (Consumer confidence).

Model	Intercept	Regression coefficients of						Adj. R_ bar2	SEE	F-value
		GP	ERV	BSG	CD	IRP	CC			
1	1.283 (7.340)**	-0.668 (13.006)**						0.566	0.375	169.151
2	1.388 (8.402)**		0.604 (13.142)**					0.571	0.373	172.724
3	1.111 (8.763)**			-0.720 (19.356)**				0.743	0.288	374.648
4	1.063 (7.182)**				-0.720 (19.356)**			0.688	0.318	285.179
5	0.943 (7.361)**					-0.243 (12.853)**		0.764	0.277	418.440
6	0.947 (7.079)**						-0.243 (12.853)**	0.748	0.286	383.024
7	0.572 (3.971)**	-0.449 (10.496)**	0.514 (10.631)**					0.768	0.274	215.693
8	0.407 (3.801)**	-0.326 (9.724)**	0.182 (5.091)**	-0.413 (10.483)**				0.875	0.201	302.968
9	0.138 (1.862)	-0.243 (10.496)**	0.175 (7.413)**	-0.262 (9.138)**	-0.305 (12.738)**			0.945	0.13335	558.590
10	0.017 (0.488)	-0.188 (16.771)**	0.220 (19.389)**	-0.130 (8.705)**	-0.175 (13.601)**	-0.243 (12.853)**		0.988	0.06281	2101.980
11	0.076 (1.869)	0.076 (1.869)	0.179 (12.577)**	-0.193 (10.997)**	-0.243 (12.853)**		-0.243 (12.853)**	0.984	0.07289	1554.273

Notes:

i. Figures in parenthesis are t-values
ii. The asterisk signs (**) and (*) indicate that the results are significant at 1 percent and 5 percent level respectively.
iii. Economic slowdown is dependent variable.

The regression result shows that the beta coefficients for government policies are negative with economic slowdown. It indicates that government policies have negative impact on economic slowdown. This finding is not consistent with the findings of Carless (2004). Likewise, the beta coefficients for exchange rate volatility are positive with economic slowdown. It indicates that exchange rate volatility has a positive impact on economic slowdown. This finding is consistent with the findings of Schaufeli and Leiter (2001). In contrast, the beta coefficients for banking sector growth are negative with economic slowdown. It indicates that banking sector growth has a negative impact on economic slowdown. This finding is not consistent with the findings of Amaegberi and Krokeyi (2023). Similarly, the beta coefficients for credit demand are negative with economic slowdown. It indicates that credit demand has a negative impact on economic slowdown. This finding is not consistent with the findings of Pearson (2000). Likewise, the beta coefficients for interest rate policies are positive with economic slowdown. It indicates that interest rate policies have a positive impact on economic slowdown. This finding is consistent with the findings of Ashforth, (1989). Further, the beta-coefficients for consumer confidence are negative with economic slowdown. It indicates that consumer confidence has a negative impact on economic slowdown. This finding is not consistent with the findings of Jiang *et al.* (2009).

4. Summary and conclusion

Liquidity gluts and credit crunches are critical factors during economic slowdowns. A liquidity glut, which provides an excess supply of money, can help stimulate economic activity by making borrowing easier. However, if not properly managed, it can lead to inflation or asset bubbles. Conversely, a credit crunch restricts access to loans and credit, which can worsen economic downturns by limiting investment and spending. Balancing

these conditions is essential; sufficient liquidity supports economic activity, while avoiding excesses prevents instability. Effective management of liquidity and credit can mitigate the impacts of economic slowdowns and support recovery.

This study attempts to examine the liquidity glut and credit crunch in the face of economic slowdown: Perspective of Nepalese stakeholders. The study is based on primary data of 130 respondents.

The major conclusion of this study is that government policies, credit demand, banking sector growth, interest rate policies, and consumer confidence have negative impact on economic slowdown. However, exchange rate volatility has a positive impact on economic slowdown. It indicates that frequent fluctuations in currency values can disrupt trade, investment, and overall economic stability, leading to an increase in the pace of economic slowdown. The study also concludes that banking sector growth is most significant factor followed by interest rate policies that determines the change in the economic activities that directly affects the economic growth.

References

Abbas, F., S. Iqbal, & B. Aziz, 2019. The impact of bank capital, bank liquidity and credit risk on profitability in postcrisis period:ⁿA comparative study of US and Asia. *Cogent Economics & Finance* 7(1), 26-39.

Ahmed, H. M., S. I. El-Halaby, & H. A. Soliman, 2022. The consequence of the credit risk on the financial performance in light of COVID-19: Evidence from Islamic versus conventional banks across MEA region. *Future Business Journal* 8(1), 1–22.

Alwadeai, A., N. Vlasova, & H. Mareeh, & N. Aljonaid, 2024. Beyond traditional defenses: Unraveling the dynamics of reserves and exchange rate volatility in the face of economic sanctions. *Russian Journal of Economics* 10(1), 1-19.

Amaegberi, M., & W. Krokeyi, 2023. Banking Sector Reforms and Economic Growth in Nigeria. *Mediterranean Journal of Social Sciences* 14(3), 25-39.

Balke, N., & Z. Zeng, & R. Zhang, 2021. Identifying credit demand, financial intermediation, and supply of funds shocks: A structural VAR approach. *The North American Journal of Economics and Finance* 56(5), 39-45.

Baral, K. J., 2005. Health check-up of commercial banks in the framework of CAMEL: A case study of joint venture banks in Nepal. *Journal of Nepalese Business Studies* 2(1), 41-55

Boffey, R., & G. N. Robson, 1995. Bank credit risk management. *Managerial Finance* 21(1), 66-78.

Campbell, J. Y. and J. F. Cocco, 2007. How do house prices affect consumption? evidence from micro data. *Journal of Monetary Economics* 54(3), 591-621.

D, G., 2019. Savings and Liquidity Gluts and the American Long-Term Interest Rates Before the Great Financial Crisis. *Zarządzanie Publiczne* 12(5), 63-82.

Dermine, J., 1986. Deposit rates, credit rates and bank capital: The Klein-Monti model revisited. *Journal of Banking & Finance* 10(1), 99-114.

Diamond, D. W., & R. G. Rajan, 2000. A theory of bank capital.*The Journal of Finance* 55(6), 2431-2465

Mohammed, E. K., 2024. The impact of money supply, interest rate and inflation rate on economic growth: A case of Morocco. *Journal of Economics, Finance and Accounting Studies* 6(2),

132-142.

Gong, P., 2024. Main influencing factors of interest rates in china and empirical research. Finance & *Economics* 1(6), 1-5.

Hanipah, H., P. Sugiartini, & I. M. Maula, 2023. Analysis of the impact of government fiscal and monetary policies on economic growth in Indonesia: Government Economic Approach. *Journal of Social Research* 2(11), 3867-3871.

Heise, M., R. Schneider, D. F. Milleker, & C. Broyer, 2005. Global liquidity glut: problem or growth driver?. *Economy and Markets* 47(7), 1-18.

Hessou, H., 2018. Basel III capital buffers and Canadian credit unions lending: Impact of the credit cycle and the business cycle. *International Review of Financial Analysis* 57(8), 23-39.

Kesraoui, A., M. Lachaab, & A. Omri, 2022. The impact of credit risk and liquidity risk on bank margins during economic fluctuations: Evidence from MENA countries with a dual banking system. *Applied Economics* 54(35), 4113-4130.

Kluza, K., 2014. Impact of the economic slowdown on local government investments, debt and productivity in the EU countries. *Journal of Economics and Management* 18(6), 26-39.

Madugu, A. H., M. Ibrahim, & J. O. Amoah, 2020. Differential effects of credit risk and capital adequacy ratio on profitability of the domestic banking sector in Ghana. *Transnational Corporations Review* 12(1), 37-52.

Matsusaka, J. G., & A. M. Sbordone, 1995. Consumer confidence and economic fluctuations. *Economic Inquiry* 33(2), 296-318.

Ajayi-Nifise, A. O., S. T. Tula, O. F. Asuzu, N. Z. Mhlongo, F. O. Olatoye, & C. V. Ibeh, 2024. The role of government policy in fostering entrepreneurship: a USA and Africa review. *International Journal of Management & Entrepreneurship Research* 6(2), 352-367.

Niyonsaba, B., 2023. Nexus between Exchange Rate Volatility and Economic Growth: A Theoretical Review. *International Journal of Research Publication and Reviews* 4(3), 4675-4684.

Nor, A. H. S. M., M. Kogid, T. Sarmidi, & Z. Isa, 2012. Kesan Kemeruapan Kadar Pertukaran ke atas Pasaran Saham di Malaysia. *Jurnal Ekonomi Malaysia* 46(2), 141-157.

Omar, W. A. W., N. O. Al-Towati, & H. Amlus, 2020. The impact of the credit crunch and shadow economy on economic growth in Libya: Evidence from ARDL. *Saudi Journal of Economics and Finance* 1(1), 49-63.

Porath, D., 2006. Estimating probabilities of default for German savings banks and credit cooperatives. *Schmalenbach Business Review* 58(7), 214-233.

Rifqah Amaliah, S., & H. H. Hassan, 2019. The relationship between bank's credit risk, liquidity, and capital adequacy towards its profitability in Indonesia. *International Journal of Recent Technology and Engineering (IJRTE)* 7(5), 225-237.

Shair, W., N. Ahmad, M. Tayyab, & I. Ishaq, 2023. Effect of economic policy uncertainty on exchange rate volatility in Pakistan. *Bulletin of Business and Economics (BBE)* 12(4), 33-44.

Shrestha, B. P., 2012. Impact of liquidity on profitability of commercial banks in Nepal. Nepal *Journal of Management* 5(1), 27-38

Tang, Y., H. Chen, B. Wang, M. Chen, & X. Yang, 2009. Discriminant analysis of zero recovery for China's NPL. *Journal of Applied Mathematics and Decision Sciences* 4(6), 1-16.