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The Effect of Character, Capacity, and Collateral on Causing Non-Perfoming Loans in Banking in Indonesia

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Abstract: This research seeks to analyze, identify, and assess the impact of character, capacity, and collateral on the factors leading to non-performing loans in the city of Cirebon, using banks as the analytical unit. A non-performing loan refers to credit that is overdue for a specific duration, typically exceeding 90 or 180 days. Such loans arise when the borrower fails to meet their repayment obligations as per the terms agreed upon by both parties. Non-performing loan denotes a situation where a client is unable to settle their debts with the bank punctually. This study employs a quantitative approach to select the sample, which consists of 48 bank employees in Cirebon, analyzed through classical assumption methods to test the research hypothesis. The statistical analysis indicates that the character variable significantly influences the incidence of non-performing loans, the capacity variable has a notable influence on the occurrence of non-performing loans, and the collateral variable also significantly impacts the occurrence of non-performing loans.

Keywords: Non-Performing Loan, Character, Capacity, Collateral.

INTRODUCTION

Non-performing loan is a serious problem that has a huge impact on economic stability and the financial system. In Cirebon City, the phenomenon of non-performing loan created various challenges for Banks or Financial Institutions. Cirebon City as one of the strategic economic centers in West Java, Indonesia, has many loan programs, financing, Bank Perkreditan Rakyat (BPR) and other financial institutions to support financing needs for many levels of society. However, Otoritas Jasa Keuangan (OJK) of Cirebon City reported that the non-performing loan rate or loans included in the failed category in Cirebon City reached 12%, this figure is higher than the national average. In addition, BPR Bank Cirebon experienced very large losses due to the large number of bad loans recorded up to IDR 30 billion (izan Khaerul, 2022). The high number of non-performing loan is a structural problem whose impact is greater than expected and requires serious attention.

Based on data from the Financial Services Authority (OJK) and Bank Indonesia (BI), the percentage of non-performing loans has increased quite significantly over the past few years

but then decreased again in 2022 after COVID-19 as in the table below, this shows that the Indonesian economy is recovering from the pandemic downturn.

Table 1. Average percentage data of bad credit in Indonesia from 2017-2022.

Tahun	Non-Performing Loan
2017	2,9%
2018	2,8%
2019	2,7%
2020	3,3%
2021	3,1%
2022	2,9%

Source: OJK & BI

The increasing non-performing loan are caused by many factors, mainly due to the economic crisis during the COVID-19 Pandemic, the COVID-19 Pandemic has had a very significant impact on the economy throughout the world, especially developing countries like Indonesia, although the Minister of Finance said that Indonesia did not experience a significant impact from the economic contraction that occurred during COVID-19. The Minister of Finance said that the main factor in Indonesia's survival during the pandemic was MSMEs, MSMEs greatly influenced the survival of the economy by covering 61% of the National GDP and absorbing more than 97% of the workforce (Andrianto Robertus, 2024). However, in practice, COVID-19 has worsened the economic conditions for many parties including MSMEs, the Covid pandemic has resulted in many mass layoffs and has also had an impact on MSMEs which are the horns of the country's economy and cannot maintain profitability. The impact of this Covid has had a long and sustainable effect, countless companies, startups and MSMEs have experienced a significant decline in income to bankruptcy and are unable to meet their credit payment obligations, Covid is a crucial factor in the surge in non-performing loan cases.

Unfair regulations for Banks and Financial Institutions are also an important factor in why non-performing loan are a continuing problem. In November 2024, the Indonesian government signed a new regulation on the removal of the Blacklist or Amnesty for 6 million business actors, farmers, fishermen and MSMEs who cannot fulfill their payment obligations that have been released or have been considered a burden of loss by the bank (Octaviano Adrianus, 2024). This regulation actually indirectly supports an unhealthy credit system and increases the risk of credit evasion, creditors who do not comply with paying their obligations will easily hide behind regulations to support their bad behavior. The Indonesian government is recorded as having carried out credit restructuring during the COVID Pandemic in 2021 (Rika Hesti, 2021).

Another factor is the character of the debtor, the character of the debtor in question is the attitude, behavior, and morality that affect his ability to fulfill credit obligations. Debtors with less disciplined and irresponsible characters tend to be at higher risk of experiencing bad credit due to a lack of commitment in themselves.

Capacity is also an important factor in the occurrence of non-performing loan, in this case the borrower's financial capacity and how they manage it greatly determines whether they can repay the credit given, although in practice some debtors who have adequate management capabilities and financial capacity still have the possibility of experiencing bad debts due to moral hazard or already having bad intentions to repay even before receiving credit. Capacity refers to the ability of prospective debtors to repay their obligations.

Collateral is the next factor that is very likely to influence the occurrence of non-performing loan, this happens because many cases of collateral given by debtors to banks do not have clear legality and some of them even violate the law, some others occur because the collateral given by the debtor is collateral that is difficult to resell, so that the debtor has a

mindset to release the collateral to get credit quickly and does not want to pay it back because the debtor realizes that the collateral given is collateral that is difficult to resell.

Due to the high level of non-performing loan, this affects access to financing for many parties who do not have sufficient resources to convince the bank that they are worthy of credit. Even so, easy access to financing should encourage a more conducive economy, but because of limited access due to the large number of non-performing loans that occur, it results in a greater domino effect such as a lack of lower and unstable economic turnover. In developing countries including Indonesia, access to credit financing is the main and most vital determinant of the ability of entrepreneurs and MSMEs to expand employment, develop economic growth and also determine the development of a country.

Addressing the problem of non-performing loan requires a holistic and collaborative approach. Regulators, local governments, and financial institutions must improve their systems and regulations to strengthen risk management and financial literacy so that all levels of society, including entrepreneurs and MSMEs, can maintain their credibility properly. Regulators and local governments must also ensure transparency in credit management so that it is not intervened by other parties and avoid conflicts of interest. In addition, economic policies and credit amnesty or restructuring policies need to be reviewed to maintain a healthier banking environment. Technical support for business actors and MSMEs affected by the pandemic is one example of an action that can help restore their ability to meet credit obligations without harming financial institutions, technical support can also encourage more sustainable economic growth.

The use of optimal accounting and management systems also helps to reduce cases of non-performing loan by taking more accurate information from debtors. If the management accounting system can be used optimally, it will affect the quality of the management information taken, which ultimately results in better quality management accounting information and a more appropriate decision-making process by managers (Wahdiat et al., 2019).

This study aims to analyze, identify and evaluate the influence of character, capacity, and collateral on the causes of non-performing loans in the city of Cirebon using banks as the unit of analysis. Based on the results of previous research on cooperatives conducted by (Putri & Widyari, 2024), character, capacity, and collateral have a significant influence in determining non-performing loans. However, research in the context of banking is still very limited due to the difficulty of obtaining information.

This study is expected to help banks in the city of Cirebon or banks in Indonesia to minimize the occurrence of non-performing loans by improving more effective policies, internal controls and improving better risk mitigation. This study is also expected to be an insight for business actors and MSMEs about the importance of character, collateral submitted to banks and financial institutions is also expected to be a guide in better financial management so as to make it easier to get access to credit in the future.

METHOD

This research employs a quantitative approach to identify the sample size, which consists of 48 banking staff members located in Cirebon City. The study focuses on three independent variables: character (X1), capacity (X2), and collateral (X3), along with the dependent variable of non-performing loans (Y). The data utilized in this research is primary data, gathered via a questionnaire method. The primary data consists of answer ratings distributed directly to bank employees in Cirebon City. The analysis employs multiple linear regression tests, a widely used statistical technique to explore the connections between dependent variables and one or more independent variables (Muthiaur, 2024).

RESULTS AND DISCUSSION

Researchers use the classical assumption method to determine the hypothesis of the study. The initial stage is carried out by testing the validity of reliability, then continued with the normality test. The next stage, the researcher conducted a multicollinearity test which was then reprocessed through the heteroscedasticity test. The final stage, the researcher conducted an F test to determine the error in drawing conclusions and a T test as a measuring tool to determine the hypothesis.

Tabel 2. Validity Reability Test Result.

Variables	Items	Pearson Corellation	Cronbach Alpha
Character (X1)	A1	0,818	0,923
	A2	0,871	
	A3	0,869	
Capacity (X2)	B1	0,841	0,816
	B2	0,883	
	B3	0.852	
Collateral (X3)	C1	0,674	0,899
	C2	0,704	
	C3	0,630	
Non-Performing Loan (Y)	D1	0,903	0,902
	D2	0,915	
	D3	0,926	

Source : Data Processing Results (2025)

Based on the results of the validity and reliability tests conducted by the researcher, it shows that each item tested has a correlation value above 0.6 where each question item in the questionnaire has been tested and shows that all items significantly measure the intended construct, it is concluded that the instrument used by the researcher is valid and reliable for use as a research instrument.

The normality test was conducted using the Kolmogorov-Smirnov method by considering a significance value of 0.05. If the significance of the results is greater than 0.05, then the data is normally distributed, but if the results are not normally distributed, then the data is not suitable for use in research or further testing is needed (Putri & Widyari, 2024).

Tabel 3. Normality Test Result

Kolmogorov smirnov	Asymp. Sig	criteria	information
0,053	0,200	0,05	Normally distributed

Source : Data Processing Results (2025)

Based on the results of the Kolmogorov Smirnov test, the significance value is 0.200, which is greater than the alpha value (0.05). Through these results, it can be concluded that the residual values are normally distributed and suitable for use as further research data.

Tabel 4. Multicolleniarity Test Result

Variable	Tolerance	VIF	Information
Character	0,861	1,161	No Multicollinearity
Capacity	0,669	1,495	No Multicollinearity
Collateral	0,690	1,450	No Multicollinearity

Source : Data Processing Results (2025)

Based on the multicollinearity test analysis contained in the table, all tolerance values for variables are more than 0.10 and VIF values are below 10, therefore it can be concluded that the model does not experience multicollinearity problems. Multicollinearity testing is carried out using the tolerance and VIF (Variance Inflation Factor) methods, where the common limit values used to indicate multicollinearity are tolerance values ≤ 0.10 and VIF values ≥ 10 (Putri & Widyari, 2024).

Tabel 5. Heteroscedasticity Test Result

	Unstandardized Coefficients		Standardized Coefficients		
Model	B	Std. Error	Beta	t	Sig.
(Constant)	.937	.732		1.280	.207
Character	.065	.040	.251	1.620	.112
Capacity	-.043	.040	-.191	-1.088	.283
Collateral	-.044	.062	-.122	-.706	.484

Source : Data Processing Results (2025)

Based on the table of test results conducted by the researcher, it shows that each variable has a significant value above 0.05, so it can be concluded based on the heteroscedasticity test, in this model it means that the homoscedasticity assumption is met or the regression estimation results are accurate and reliable, so that the results of this test can be used for research and do not require further improvement.

Tabel 6. F Test Result

Model	Sum of Squares	Df	Mean Square	F	Sig
Regression	124.174	3	41.391	52.295	0,000[b]
Residual	34.826	44	.792		
Total	159.000	47			

Source : Data Processing Results (2025)

Based on the results of ANOVA (Analysis of Variance) attached to the table above, it shows that the calculated F value is 52,295 which indicates that the proposed model has high significance. This is reinforced by the significance result of 0.000b which is smaller than 0.05 or smaller than the commonly used tolerance limit. In the calculation results, this research model has a coefficient of determination (R^2) of 0.781, which means that 78.1% of the variability of bad credit can be explained by the variables of character, capacity, and collateral.

Meanwhile, the significance value of 0.000b indicates that the error in drawing conclusions is very small.

Tabel 7. T Test Result

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig
	B	Std. Error			
(Constant)	.599	1.219		.491	.626
Character	.267	.067	.304	3.992	.000
Capacity	.443	.066	.578	6.696	.000
Collateral	.276	.104	.225	2.654	.011

Source : Data Processing Results (2025)

Based on the findings of the multiple linear regression analysis listed in Table 7, it is known that the variables of character, capacity, and collateral have a significant effect on the emergence of bad debts. This can be seen in the table above which shows that the significance value (Sig.) for the character variable is 0.000, for capacity 0.000, and for collateral 0.011, all of which are below the significance value of P of 0.05. Thus, it can be concluded that the variables of character, capacity, and collateral have a statistically significant effect on the possibility of bad debts. This finding is supported by research conducted by (Saputra et al., 2020), (Firdaus & Rajiantara, 2022) and (Somashekar Vichitra & Reddy K. Gayathri, 2022) which also explain that character, capacity, and collateral have a significant effect on the occurrence of bad debts..

Discussion

The results of the character variable assessment conducted by the researcher show that debtor behavior greatly influences the factors causing non-performing loan in banking. If the debtor has a bad character, the possibility of the debtor defaulting will be greater.This is because the lifestyle, characteristics and bad intentions of the debtor have a very high potential to result in non-performing loan payments. This study refines the findings of (Saputra et al., 2020) who in their research revealed that character does not have a significant effect on the occurrence of non-performing loan.

The findings from the capacity variable assessment carried out by the investigator indicate that a borrower's ability influences significantly the factors leading to non-performing loans in banking sector. When a debtor exhibits inadequate financial management, inefficient fund allocation, and lacks sufficient financial capability for repayment, the likelihood of encountering non-performing loan defaults escalates substantially. This analysis is corroborated by research carried out by (Somashekar Vichitra & Reddy K. Gayathri, 2022) who in their research revealed that capacity has a significant effect on the occurrence of non-performing loan.

The findings from the collateral variable analysis performed by the researcher indicated that the borrower's collateral significantly impacted the factors leading to non-performing loans in banking sector. If the borrower possesses collateral with questionable legality, lacks easy resell potential, and is embroiled in legal disputes, there is an exceptionally high risk of resulting in non-performing loan defaults. This study is corroborated by research carried out by (Putri & Widyari, 2024) which in its research revealed that collateral has a significant effect on the occurrence of non-performing loan.

Borrower character is one of the key elements taken into account in credit evaluation. Where, positive characters, such as integrity and responsibility, can reduce the risk of non-

performing loans. In addition, the borrower's financial capacity, which includes income and ability to pay, plays an important role in determining the borrower's ability to meet their credit obligations. Solid capacity tends to reduce the possibility of non-performing loans. On the other hand, collateral or collateral deposited by the borrower is also an important factor. Collateral with high value provides additional protection for the bank, thus minimizing the risk of non-performing loans. Through a comprehensive data analysis, it was found that character, capacity, and collateral significantly affect the risk of non-performing loans. Case studies involving various types of borrowers and banking institutions showed that borrowers with good character, strong financial capacity, and adequate collateral tend to have a lower risk of non-performing loans. The findings of this study are expected to provide insight for banks in improving more efficient credit policies and practices, as well as reducing the level of non-performing loans in the future.

CONCLUSION

This study examines the influence of character, capacity and collateral on the causes of non-performing loan in banking in Cirebon City. Unlike several studies conducted by previous researchers who placed cooperatives as the analysis unit, the researcher tried to use a new technique by placing banks as the unit of analysis and bank employees as respondents. Although in this study, the researcher experienced many limitations, one of which was the difficulty of accessing information due to the strict regulations applied by banking. The researcher tried to use a new perspective by making Cirebon City a case study, where Cirebon is one of the cities with the highest non-performing loan in 2024. The results of the data analysis found that the variables of character, capacity and collateral each had an effect on the occurrence of non-performing loan.

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