Asset-based microfinance for microenterprises:
Evidence from Pakistan

Faisal Bari 1 2 3 4
Kashif Malik 1 2 3
Muhammad Meki 1 2 3
Simon Quinn 4

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Abstract

We conduct a field experiment offering graduated microcredit clients the opportunity to finance a business asset worth four times their previous borrowing limit. We implement this using a hire-purchase contract; our control group is offered a non-interest loan. We find large, significant and persistent effects from asset finance contracts: treated microenterprise owners run larger businesses and enjoy higher profits; consequently, household consumption increases, particularly on food and children’s education. A dynamic structural model with non-concave capital adjustment cost rationalisation not only yields the potential for welfare improvements through large capital injections that are financially sustainable for microfinance institutions.

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2 Lahore University of Management Sciences: bari.faisal@lums.edu.pk.
3 Lahore University of Management Sciences: meki.muhammad@lums.edu.pk.
4 University of Oxford: Department of International Development and Centre for Islamic Studies: quinn.simon@economics.ox.ac.uk.
Asset-based Microfinance for Microenterprises: Evidence from Pakistan

We conduct a field experiment offering graduated microcredit clients the opportunity to finance a business asset worth four times their previous borrowing limit. We implement this using a hire-purchase contract; our control group is offered a zero-interest loan. We find large, significant and persistent effects from asset finance contracts: treated microenterprise owners run larger businesses and enjoy higher profits; consequently, household consumption increases, particularly on food and children’s education. A dynamic structural model with non-convex capital adjustment costs rationalizes our results; this highlights the potential for welfare improvements through large capital injections that are financially sustainable for microfinance institutions.

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