



Micro-Finance in Pakistan: Institutional Practices, Challenges and Way Forward

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ABSTRACT

During the last five years, size of Pakistan’s microfinance sector got double in terms of its gross loan portfolio (GLP) of PKR 703 billion. Despite the hundred percent increase in the GLP, the fact that serving only 12 million borrowers out of a potential 40 million transpires that a significant inclusion gap still persists. This research uses the qualitative and quantitative data to find the existing gaps between the supply and the demand sides. This research study utilizes Chi-square analysis to quantify the qualitative survey results. Comparative analysis of different institutional practices, lending methodologies and products guides the research to find out the challenges and to recommend the strategic interventions for improvement. The study, after the analysis, identifies several critical barriers including high operational costs, scarcity of inexpensive credit lines and stringent regulations which fail to reduce the existing gaps between both sides and thus threaten financial sustainability. Furthermore, Microfinance Banks (MFBs) provide microloans on high interest rates (25–30%), while the borrowers, particularly in agriculture, struggle with increased default risks due to climate-induced shocks. Other operational challenge like limited staff capacity and very low digital literacy among the borrowers further hinder growth. The study recommends that in order to reduce the gap between the demand and supply of MF services, the sector requires structural reforms, including the availability of inexpensive and low-cost equity, regulatory reform regarding deposit-taking licenses for MFIs and enhanced digital integration among the borrowers. Introduction of large-scale safety nets for the borrowing farmers besides training the relevant human resource in MF services are very important steps for shifting microfinance from a means of survival to a plausible cause of sustainable and inclusive economic growth in Pakistan. Bilateral Contract Market (CTBCM) to induce competition for better performance and service delivery. For resilient financial sustainability of power sector in long term, competitive market with modernized grid infrastructure, integration of renewable/distributed generational sources and professional cadre management shall be essential.

Keywords:

Bilateral Contract Market, financial sustainability gross loan portfolio Microfinance Banks.

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1. INTRODUCTION

1.1. Background

State Bank of Pakistan (2025) defines microfinance as “the provision of financial services including credit, savings, insurance etc. to those sectors of economy, which are not serviced by traditional formal financial institutions. Microfinance caters to the financial services’ needs of the poor and micro enterprises and is normally collateral-free shortterm facility whereas the commercial banks generally deal with corporate clients, SMEs and individuals with larger income levels and extend financing facilities primarily based on collaterals and borrowers’ capacity to repay”.

The concept of MF is relatable to the Poverty Graduation theory that explains the process, in which extremely poor households come out of poverty, through a periodic series of step-wise activities, designed to build sustainable livelihoods. This idea became popular through the work of BRAC (Bangladesh Rural Advancement Committee) in Bangladesh, which devised and experimented with the “Graduation Approach” in the early 2000s (Hashemi & de Montesquiou, 2011). The theory explains that extremely poor persons mostly suffer from multi-faceted poverty owing to lack of assets, skills, access to funds and lack of opportunity to earn which hampers them to take advantage of the conventional microfinance programs (Banerjee et al., 2015). According to the Poverty Graduation theory, first of all, the beneficiaries receive consumptive financial aid to fulfill their basic necessities of life including food, providing sustenance. Later, they are provided with productive assets (such as livestock or equipment) and skill through technical training to earn their living in regular manner. With passage of time, they are given access to MF services like savings, microcredit and insurance, besides mentoring for their social inclusion (de Montesquiou & Sheldon, 2014). Thus, the wholesome support enables them to “graduate” from extreme poverty to a level of self-adequacy and economic stability.

In Pakistan, the Microfinance sector consists of Microfinance Banks (MFBs) regulated by State Bank of Pakistan (SBP) and Microfinance Institutions (MFIs) regulated by Securities Exchange Commission of Pakistan (SECP). MFBs largely operate through Branchless Banking (BB), which has the potential for increasing outreach through BB Agents, mobile wallets etc. across the country. Most MFBs have partnered with

telecom operators to increase their footprints and serve as a key driver for improving financial inclusion (State Bank of Pakistan, [2025](#)).

1.2. Legal Frameworks and Policies on Microfinance in Pakistan

a) Regulatory Bodies and Governance

State Bank of Pakistan acts as an umbrella regulator of microfinance sector. It regulates the operations and commands the compliance from all the microfinance banks (MFBs) and microfinance institutions (MFIs). Under the SBP, Microfinance Regulatory Authority regulates the microfinance banks and ensures their compliance in accordance with operational guidelines of the SBP (Rasheed et al., [2021](#)).

b) Microfinance Institutions Ordinance (2001)

The Microfinance Institutions Ordinance (2001) serves as the cornerstone of Pakistan's microfinance legal framework. It lays out clear guidelines about how microfinance institutions (MFIs) are licensed and regulated ensuring that these entities operate in a sound and transparent manner. The ordinance outlines the key responsibilities of MFIs, emphasizing adequate capital, healthy loan portfolios, and strong consumer protection measures. SBP regulates the interest rates, checks borrowers' exploitation and monitors the financial sustainability of the sector (State Bank of Pakistan, [2025](#)).

c) The Prudential Regulations for Microfinance Banks (MFBs)

Besides the Microfinance Institutions Ordinance (2001), the prudential regulations (updated in May, 2025) guide about maintaining the operational standards for microfinance banks (MFBs) in Pakistan. The areas included for standardized operations are loan disbursement, repayment mechanisms and risk management practices. Particular emphasis remains on good governance, transparency, and accountability ensuring that MFBs function appropriately through their robust internal controls and effective risk management. The compliance of these regulations enable a stable and responsible microfinance environment for the MFIs as well as for the borrowers (Maenuddin et al., 2024).

d) The Pakistan Microfinance Investment Company (PMFIC) & Pakistan Microfinance Network (PMFN)

PMFIC was incorporated on August 10, 2016 under the Companies Ordinance, 1984 (now the Companies Act, 2017). It is licensed to operate as a Non-Banking Finance Company (NBFC), authorized to provide

investment finance services (Pakistan Microfinance Investment Company, [2025](#)). The PMFIC was established by the government of Pakistan through its Poverty Alleviation Fund (PPAF). In 2016, PPAF deliberately invested its microfinance operations into Pakistan Microfinance Investment Company (PMFIC) in collaboration with the State Bank, to develop the MF sector in the country, with an equity share of 49% (Pakistan Poverty Alleviation Fund, [2024](#)). The purpose was to develop the equity pool for MF sector in partnership with private sector. PPAF has share of 49% equity in the PMFIC while the rest of share in equity is contributed by the DFID through KarandaaZ Pakistan with 37.8% share and KfW (German Development Bank) with 13.2% share. The PMFIC started from a portfolio of 12 billion rupees in 2016 which has increased up to 34 billion rupees (S. Siddiqui, personal communication, September 7, 2025). Pakistan Microfinance Network (PMFN) was registered in 2001 under Section 42 of Companies Act 1984 (Companies Act, 2017 now) plays an important role in fostering collaboration among all the registered microfinance providers and advancing microfinance policies for enhancing their scale, quality of service, diversity of portfolio and financial sustainability in order to achieve inclusive services (Pakistan Microfinance Network, [2025](#)).

e) National Financial Inclusion Strategy (NFIS) 2020-2025

The SBP introduced the National Financial Inclusion Strategy (NFIS) in 2020 which provides a roadmap to broaden access to financial services across the country. Its primary focus is women, young people, and rural communities. The objective behind this strategy is to raise the overall rate of financial inclusion and ensure that low-income households can access credit, savings, insurance, and other essential financial products of microfinance institutions. The NFIS sets clear objectives to strengthen the microfinance sector by promoting financial system through expansion of digital services and mobile banking. A key objective is to make digital platforms central to microfinance that helps to lower the transaction costs and improve access for people in rural areas. The strategy promotes gender equality, women's financial empowerment and opportunities for small farmers and entrepreneurs (State Bank of Pakistan, [2025](#)).

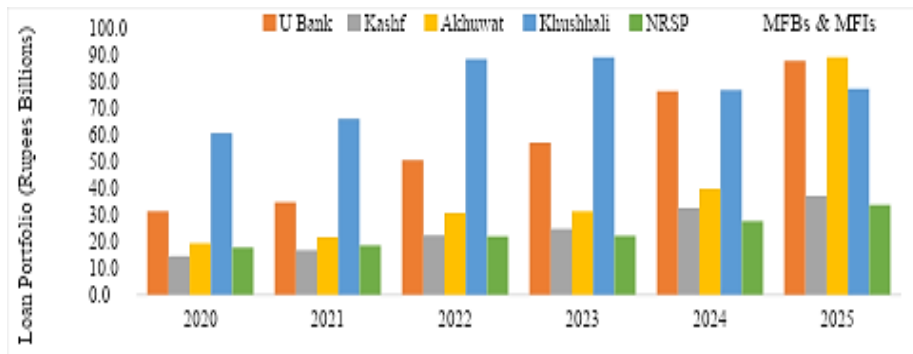
1.3. Microfinance in Pakistan: History

The origins of microfinance in Pakistan can be traced back to the cooperative experiments initiated under the Comilla Model in the late 1950s by Dr. Akhter Hameed Khan in the then East Pakistan. Although

initially designed as a rural development program, this model provided the conceptual foundation for small-scale credit and community-based lending in South Asia (Khan, 1979; Robinson, 2001). In Pakistan, the sector took more formal shape during the 1990s with the establishment of dedicated institutions such as the Kashf Foundation (1996), which pioneered women-focused microcredit (Zafar, 2002) and the Khushhali Bank (2000), the country's first licensed microfinance bank under the Microfinance Institutions Ordinance of 2001, supported by ADB (Montgomery, 2006). Pakistan Poverty Alleviation Fund, (2024) has served as an umbrella institution for community-driven local development in the country which got registered in February 1997 under Section 42 of the Companies Ordinance 1984 (Companies Act, 2017 now) as a not-for-profit company. It formally started its functions in 2000 to support people living in multi-dimensional poverty by providing an array of financial and non-financial services. Another milestone was the creation of the Akhuwat Foundation, (2001), which introduced an interest-free lending model (Qarz-e-Hasna) (Akhuwat Islamic Microfinance, 2025).

Figure 1

Loan Portfolio of Major MFBs & MFIs from 2020-2025



Note. Loan portfolio of U Bank, Kashf Foundation (2020), Akhuwat Islamic Microfinance, Khushhali Bank and of National Rural Support Program from Pakistan Microfinance Network (2025)

1.4. Growth Trajectory

In Pakistan, during the last decade, microfinance sector experienced extraordinary growth and the number of active borrowers nearly doubled, rising from around 2 million in 2012 to more than 4.6 million by 2016. During the same period, the gross loan portfolio expanded rapidly to PKR 136.9 billion from PKR 33.1 (Malik, 2022) along with unprecedented

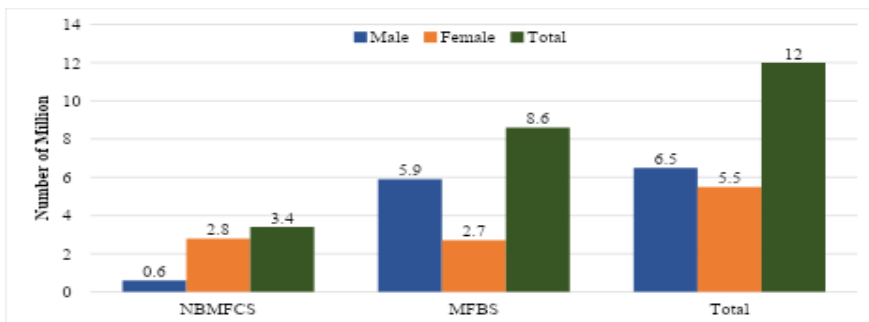
success to access the depositor, with the client base growing from 1.6 million in 2012 to over 20 million by 2016 (State Bank of Pakistan, 2020). The MFIs, and MFBs promoted financial inclusion, through branchless banking and digital financial services (State Bank of Pakistan, 2020), and social capital in rural areas of Pakistan. Most microfinance beneficiaries are women from rural areas (Khan et al., 2016). It has been observed that microfinance significantly lowers poverty, increases household income, and promotes women empowerment, for instance the Kashf Foundation and Akhuwat have played a particularly influential role by prioritizing gender-inclusive lending, enabling women to start small businesses and uplift their socio-economic standing (Rehman et al., 2020).

1.5. Current State

By July 2025, Pakistan’s microfinance sector has grown significantly, reaching 12 million active borrowers (Pakistan Microfinance Network, 2025). This expansion has been supported by 46 microfinance providers including 12 MFBs, 33 MFIs, 1 RSP group and a broad network of branches and agents. The gross loan portfolio also saw remarkable growth, reaching around 703 billion rupees by July 2025, from 323 billion rupees in 2020 with women nearly 46% and 54% men (Pakistan Microfinance Network, 2025). Moreover, while the sector has made strides, there is still a long way to go in achieving full financial inclusion. Current reports indicate that only 12 million people are provided MF facility while the estimated 40 million of the potential market remains underserved by the MF sector in Pakistan (A. Basharat, personal communication, September 7, 2025). The following graphs illustrate the number and gross loan portfolio of the sector’s active borrowers indicating the gender as well (Pakistan Microfinance Network, 2025).

Figure 2

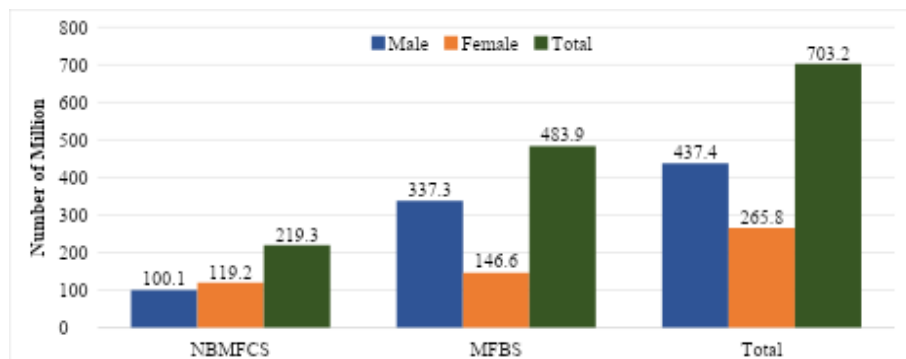
Active Borrowers of NBMFCs & MFBs Gender-wise (July, 2025)



Note. Active Borrowers including male and female for the NBMFCs and MFBs from Pakistan Microfinance Network ([2025](#))

Figure 3

Gross Loan Portfolio of NBMFCs & MFBs (Gender-wise) in billion



Note. Gross loan portfolio of NBMFCs and MFBs gender-wise from Pakistan Microfinance Network ([2025](#))

Figure 2 illustrates that out of 12 million active borrowers, 6.5 million are males while 5.5 million are female. The MFBs have highest number of borrowers (8.6 million) out of which male borrowers are 5.9 million while females are only 2.7 million. The NMFBCs have only 3.4 million borrowers in which 82% (2.8 million) are females with only 18% (0.6 million) males. Figure 3 illustrates that the MFBs have highest loan portfolio of 483.9 billion rupees (69%) of the total combined gross loan portfolio while the share of NMFBCs is nearly 31% with 219.3 billion rupees.

1.6. Statement of Problem

Around 12 million borrowers were served by Microfinance Institutions and Microfinance Banks up to July, 2025. Pakistan has reportedly about 40 million financially excluded adults, including low-income households, who still remain underserved despite increased MF interventions through public sector and non-governmental institutions (Pakistan Microfinance Network, [2025](#)). The outreach of the MF sector is constrained by non-availability of low-cost credit lines, high operational costs, stringent regulations, limited use of digital MF services and low financial literacy. These challenges significantly impede the progress of microfinance towards its core objectives of financial inclusion and economic elevation.

1.7. Research Questions

What institutional practices and systemic challenges are limiting the effectiveness of MF services in Pakistan? What strategies can be implemented to enhance the role of Microfinance in promoting financial inclusion and economic elevation?

1.8. Aims and Objectives of Research

This study aims at investigating the microfinance practices which are prevalent in Pakistan including the MFBs and MFIs. The main objective of this study is to examine the MF practices and explore systemic challenges which are limiting the effectiveness of the MF sector in Pakistan. The other objective of this study is to highlight the strategies which can be implemented to enhance the role of MF sector in promoting financial inclusion and economic elevation.

1.9. Significance and Scope of Research

The MF sector in Pakistan has been serving for the past 25 years now with a steady increase in the gross loan portfolio as well as in the number of active borrowers but still the total number of borrowers served in Pakistan through its entire MF sector (12 million) is almost equal to number of borrowers being served by only Grameen Bank in Bangladesh (Tung, 2024) which identifies a huge gap of supply and demand as well as highlights the potential of the MF sector in Pakistan. Therefore, this research study is very important to comprehend the reasons behind this gap and to recommend way forward for improving the effectiveness of microfinance in Pakistan. The scope of this study is strictly confined with MF institutional practices and procedures. Data shall be used of last five years for studying and analyzing different factors of microfinance. Primary data collection through survey is limited to one MFI, for individual lending model, only.

2. LITERATURE REVIEW

The concept of microfinance was utilized by Dr. Muhammad Yunus, a Bangladeshi economist, way back in 1970 with the idea of microcredit when small loans were given to poor individuals to help them start or grow their businesses. Initially, Dr. Yunus provided a small loan of \$27 to 42 women in a rural village of Bangladesh for purchasing raw materials to make bamboo furniture. The successful implementation of that initiative laid the foundation for Grameen Bank in 1983, which became the very

first formal microfinance bank (Hulme, [2009](#)). Later, the MF model of Bangladesh became an international phenomenon, with network of MFIs and MFBs offering multiple financial services to the poor as per their specific needs in other countries. While the concept remains the same, various microfinance models have emerged, including Self-Help Groups (SHGs) in India, Village Banks in Latin America, and the Grameen Bank model in Bangladesh ([Bayulgen, 2008](#)).

Microfinance in Pakistan has continued to evolve from small, informal credit provision into a more diversified sector that includes deposit-taking microfinance banks, non-bank microfinance companies, Islamic/interest-free lenders, and product innovations (e.g., asset-based financing). Contemporary research examines both supply-side institutional practices and demand-side welfare impacts, while also investigating structural constraints to expansion and sustainability (Azam et al., [2024](#); Bari et al., [2024](#)). A major strand of recent work documents institutional experimentation with loan design to improve productivity and welfare.

Bari et al. ([2024](#)) report results from a randomized field experiment in Pakistan showing that asset-based microfinance contracts (hire-purchase-style financing for productive assets) produce larger and more persistent gains in microenterprise size, profits, and household consumption than conventional small cash loans. His research finds that offering larger, asset-linked finance along with flexible repayment schedules can lead to expansion of businesses and investment in human-capital (e.g., spending on education). This research study highlights a robust institutional practice (asset-based loans) with strong empirical support for economic growth of the borrowers' enterprises.

However, Azam et al. ([2024](#)) finds that though the expansion does relate to active borrowers and disbursement, but still the growth gets affected by certain dynamics like types of loan portfolio and capacity limits which can restrain the sustained growth. This identifies those structural challenges due to which the increased number of borrowers does not always reflect increases in loan portfolios or institutional stability.

Bari et al. ([2024](#)) find that traditional microloans tend to bring only modest improvements in people's lives, and these benefits are not shared equally. Borrowers who already have some business experience or access to larger, asset-building loans tend to gain the most. When MFIs rely on small, short-term loans, the poverty reduction gets constrained. Findings

of Bari et al. (2024) claim that the real issue lies in disconnect between the loan amount and the real needs of an enterprise.

Beyond structural loan designs and asset-based contracts, the integration of digital financial services (DFS) has emerged as a transformative force in the Pakistani microfinance landscape. Recent evidence suggests that the adoption of mobile banking and digital wallets mitigates the high transaction costs traditionally associated with rural lending (Mersland et al., 2023). By leveraging financial technology, microfinance institutions (MFIs) can bypass geographical barriers, thereby enhancing the "outreach" dimension that remains a challenge in conventional models. However, the shift toward digitization introduces a new layer of complexity regarding digital literacy among marginalized borrowers. As noted by Kiva and Morduch (2024), while fintech accelerates disbursement speeds, the lack of human intermediation may inadvertently weaken the social ties—often referred to as social capital—that traditionally ensured high repayment rates in the original Grameen model.

Furthermore, the tension between achieving financial self-sufficiency and fulfilling a social mission remains a central theme in contemporary scholarly discourse. While Bari et al. (2024) emphasize the necessity of enterprise-specific lending, other researchers argue that the long-term viability of the sector depends on "double bottom line" reporting (Serrano-Cinca & Gutiérrez-Nieto, 2023). This perspective posits that institutional stability is not merely a byproduct of loan portfolio growth but is deeply rooted in the ability of MFIs to adapt to macroeconomic volatility and inflationary pressures. Consequently, the contemporary literature increasingly advocates for a shift from a "one-size-fits-all" credit approach toward a more nuanced, holistic financial inclusion strategy. This strategy integrates insurance, savings, and tailored business training to protect borrowers against the "debt traps" often exacerbated by modest, short-term liquidity injections (Hossain et al., 2024).

3. SECTION II: RESEARCH METHODOLOGY

3.1 Research Design

A mixed method research design has been selected for this research. This research study is conducted through qualitative and quantitative data collection followed by descriptive and evaluative analyses, as well as Chi-Square analysis.

3.2 Research Data, Sample Size and Sampling Technique

The quantitative data has been collected from the secondary resources through annual reports and articles. The qualitative data has also been gathered by using primary resources through personal communication with representatives from MFBs, MFIs, PMFIC, PMFN and PPAF (list of respondents is annexed in Appendix as Annexure-I). The stratified random sampling method was used to select sample population from AIM beneficiaries across the country. This technique ensured a diverse sample, providing a balanced view from various regions of Pakistan including both genders. A structured questionnaire comprising ten questions was prepared with questions regarding awareness about the MF facility, level of satisfaction in receiving the MF service, degree of accomplishment of purpose behind getting the loan, degree of financial inclusion, range of loan amount received, status of utilization of loan and extent of economic elevation. The data was collected from beneficiaries of microfinance served by Akhuwat Islamic Microfinance (AIM), through a structured questionnaire (annexed in Appendix as Annexure-II), using a survey technique. A total of 732 questionnaires were distributed and all were returned, duly filled in. The data has been collected at national level including all the four provinces besides ICT, AJK & GB. It was cross-sectional and was collected over a period from 1st week of August to 1st week of September, 2025. Randomly selected respondents were those beneficiaries of microfinance (microloans) who have received loans and utilized them for their enterprises/businesses' growth. The qualitative data collected from the beneficiaries of AIM (MFI) was converted into quantitative data to apply the Chi-square test. The data was tested between the null and alternate hypothesis to ascertain the strength of association between different variables, formed through the questionnaire.

3.3 Data Analysis

3.3.1 Descriptive Analysis of Sample Size, Gender Distribution & Marital Status

Out of total 732 beneficiaries, 377 are male members while 355 are female members. The pie chart indicates their marital status showing majority of them i.e. 609 are married with families, the unmarried persons are 99 while the number of widows is 23 and 1 widower. The graphs represent a very important ground reality that beneficiaries who have families are found in higher number who avail the MF loans for improving their economic status as compared to single persons.

Figure 4
Total Beneficiaries Surveyed

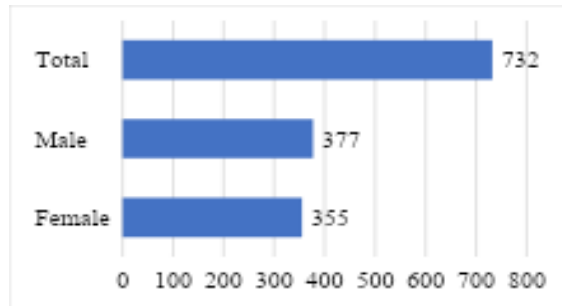
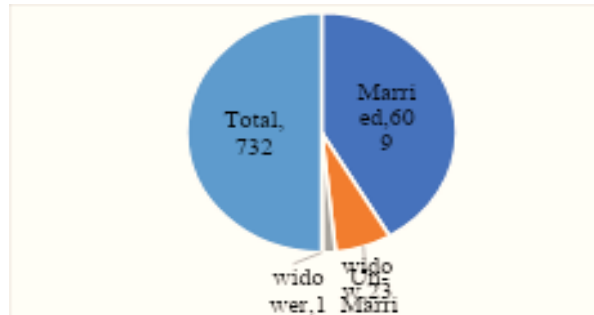


Figure 5
Marital Status



Note. Author’s own survey findings on total number of beneficiaries and their marital status

3.3.2 Descriptive Analysis of Age Ranges & Area-wise Distribution

Figure 6:
Age Ranges

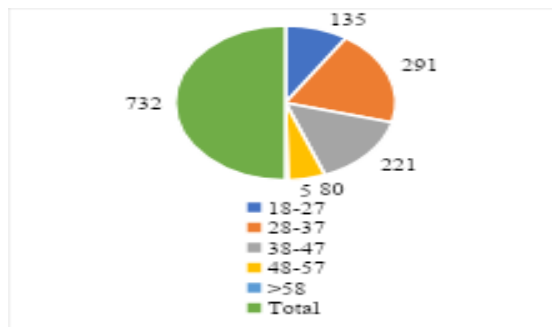
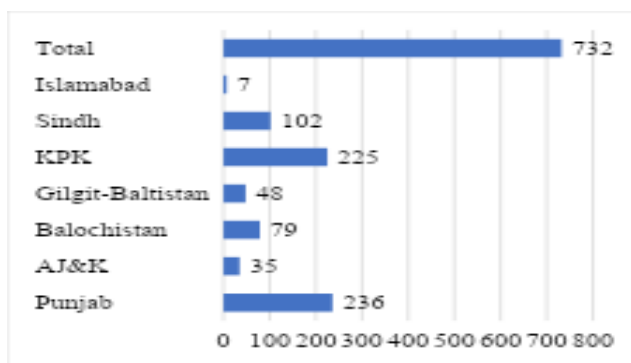


Figure 7

Area-wise Distribution



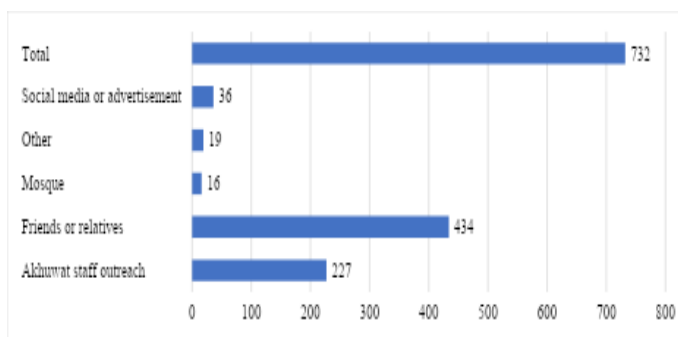
Note. Author's own survey findings on age ranges of beneficiaries and their area wise distribution

Out of the total sample size, the highest number of persons is 291 who fall within the age range of 28-37, while the second highest number is 221 who fall within the age range of 38-47. Secondly, the majority of persons out of the sample size of 732 belongs to Punjab with 236. The smallest number 7 represents the ICT. The graphical illustration of the age ranges and area-wise distribution identifies another very important ground reality that the MFIs provide loan to majority of people belonging to most productive age range and lesser to those who are beyond the age of 48 and above.

3.3.3 Descriptive Analysis of Answers on Q1 & Q2 (Awareness & Level of Satisfaction)

Figure 8

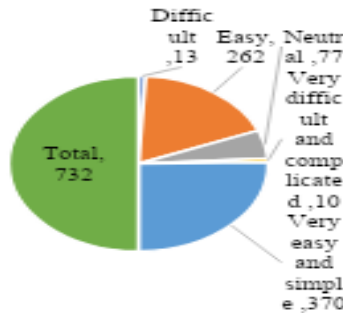
Responses for Q1. How did you come to know about Akhuwat's Microfinance Facility?



Note. The survey item read as follows: “How did you come to know about Akhuwat’s microfinance facility?”

Figure 9

Responses for Q2. How would You Describe the Loan Approval Procedure?



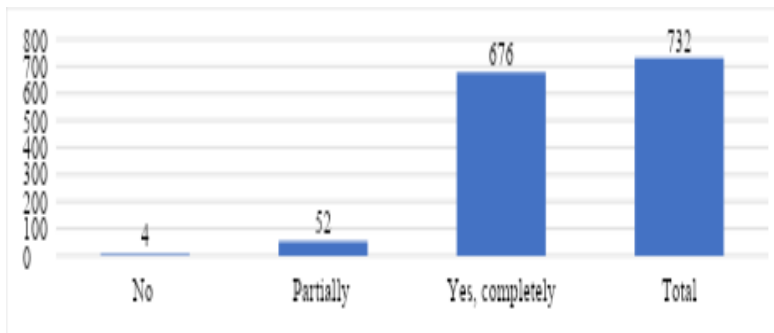
Note. The survey item read as follows: “How would you describe the loan approval procedure?”

Regarding the questions on knowledge about the MF facility and ease of getting it, both of the graphs illustrate that majority referred to their friends and families for seeking knowledge as well as majority of the persons termed the process very easy and simple.

3.3.4 Descriptive Analysis of Answers on Q3 & Q4 (Degree of Accomplishment of purpose)

Figure 10

Responses for Q3. Were You Able to Use the Loan Amount for your Business as Planned?

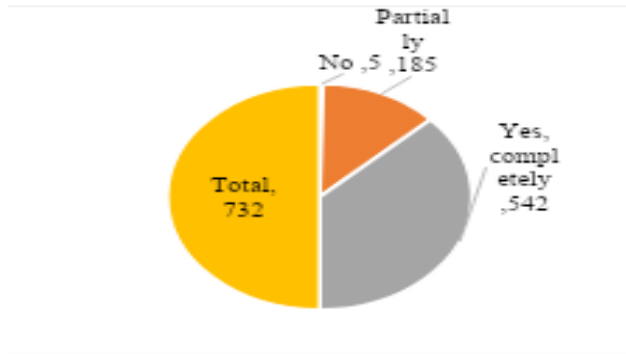


Note. The survey item read as follows: “Were you able to use the loan amount for your business as planned?”

Majority of the beneficiaries responded in affirmation on being able to utilize the loan amount fully however only 52 persons could utilize it partially for reasons to be analyzed during the section of findings through qualitative data analysis.

Figure 11

Responses for Q4. Did the Loan Amount Fulfill Your Purpose?



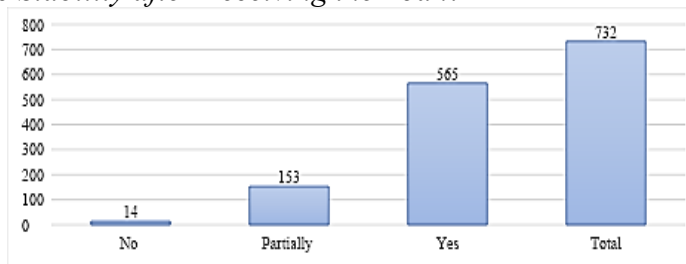
Note. The survey item read as follows: “Did the loan amount fulfill your purpose?”

On the fulfillment of purpose behind getting the loan, majority of respondents (542) said that their purpose was fully accomplished. However, 185 said that purpose was fulfilled partially but here the number of partial accomplishments is higher as compared to the same in past question. Only 5 could not utilize the loan amount as planned.

3.3.5 Descriptive Analysis of Answers on Q5 & Q6 (Financial Inclusion)

Figure 12

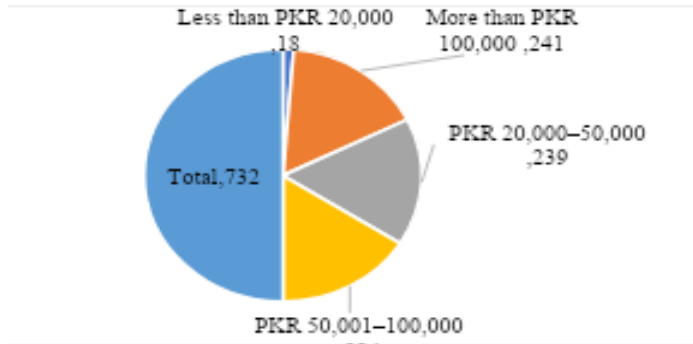
Responses for Q5. Do You Consider Yourself Successful in Achieving Economic Stability after Receiving the Loan?



Note. The survey item read as follows: “Do you consider yourself successful in achieving economic stability after receiving the loan?”

Figure 13

Responses for Q6. What was the Loan Amount You Received?



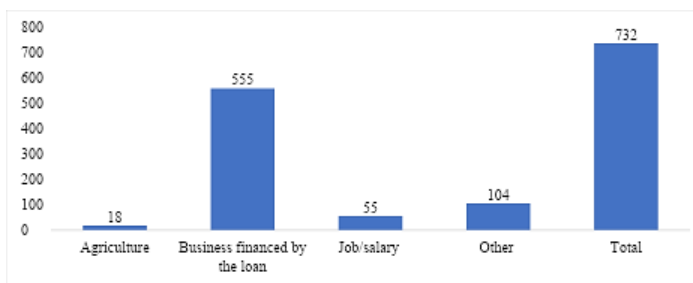
Note. The survey item read as follows: “What was the loan amount you received?”

The majority of respondents (565) consider themselves to be economically stable after receiving the loan amount while 153 do so partially. Only 14 respondents do not think so. The majority of the respondents have received loan amount of more than 100,000 rupees. While 234 of them have received between 50,000 to 100,000 rupees, 239 received between 20,000 to 50,000 rupees and only 18 have received less than 20,000 rupees. Here another very important factor gets highlighted that receiving an amount of loan between 50,000 to more than 100,000 rupees contributed to fulfilling borrowers’ purpose successfully and the borrowers became economically stable after that.

3.3.6 Descriptive Analysis of Answers on Q7 & Q8 (Loan Utilization & Economic Elevation)

Figure 14

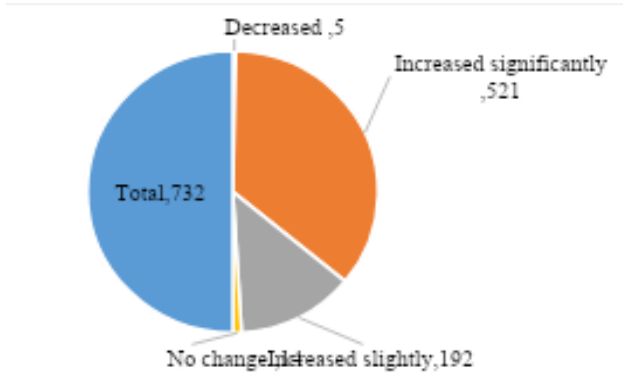
Responses for Q7. What is your Main Source of Income Now?



Note. The survey item read as follows: “What is your main source of income now?”

Figure 15

Responses for Q8. How has Your Income Changed After Receiving the Loan?



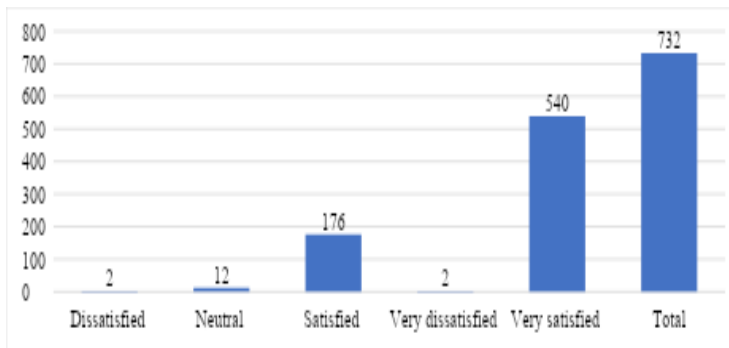
Note. The survey item read as follows: “How has your income changed after receiving the loan?”

The majority of respondents (555) replied that their current business is funded by the loan and majority with almost same number of respondents (521) have agreed that their income has significantly increased after receiving the loan, while 192 stated that their income has slightly increased. Only 14 could not find any change in their income level and for 5 respondents, there was no success rather it decreased.

3.3.7 Descriptive Analysis of Answers on Q9 & Q10 (Satisfaction & Referral)

Figure 16

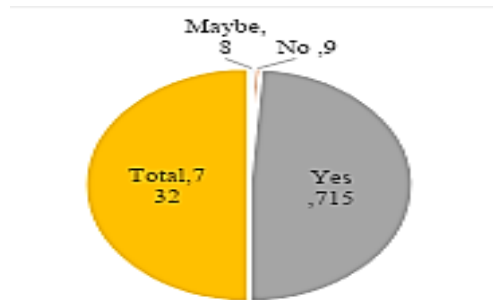
Responses for Q9. How Satisfied are you with Akhuwat’s Services Overall?



Note. The survey item read as follows: “How satisfied are you with Akhuwat’s services overall?”

Figure 17

Responses for Q10. Would you recommend Akhuwat’s microfinance to others?



Note. The survey item read as follows: “Would you recommend Akhuwat’s microfinance to others?”

The majority of respondents have expressed their satisfaction on AIM’s services and similarly majority (715) also chose to recommend AIM to others.

4. SECTION III: INSTITUTIONAL PRACTICES OF MF SECTOR IN PAKISTAN

4.1 Financial Products and Services in Microfinance Sector in Pakistan

Microfinance institutions (MFIs) and microfinance banks (MFBs) in Pakistan provide multiple financial products and services to fulfill the needs of individuals who are poor and excluded from formal banking due to non-availability of collateral (SBP, [2025](#)). These products are designed to support targeted people to promote their economic activities, financial inclusion, and poverty alleviation. The key financial products and services offered by microfinance sector are as follows:

4.1.1 Microcredit (Micro-Loan)

Microcredit also known as microloan is a prime financial product offered by all the MFIs and by the MFBs in Pakistan (Khan & Sulaiman, [2015](#)). These loans are traditionally of less amounts and serve persons who do not have access to traditional banks and collateral-based lending. The main purpose of microcredit is to support low-income entrepreneurs by providing the funds required to start or expand their businesses of small scale.

a) Loan Size and Purpose

Microloans in Pakistan generally range from PKR 10,000 to PKR 100,000 and are offered to support income-generating activities in sectors such as retail, agriculture, livestock and services (SBP, [2025](#)). This limited financial support however, helps micro-entrepreneurs to survive and to stabilize their livelihoods.

b) Repayment Terms

The plan for repayment is designed to adapt as per the borrowers' cash flow patterns. The repayment is structured usually to be made on a weekly, bi-monthly or monthly basis, keeping in view the borrowers' income cycle, for having flexibility and to reduce the risk of default (Pakistan Microfinance Network, [2025](#)).

c) Collateral Requirements

The MF lending largely relies on social collateral rather than physical assets in contrast with the conventional banks. Group members, community leaders, or notables who guarantee for the repayment, support the borrowers based on their mutual trust and social bonding. This system of social collateral enables the low-income individuals to have credit in absence of any tangible assets (SBP, [2025](#)).

4.1.2 Qarz-e-Hasna (Interest-Free Loans)

Akhuwat Islamic Microfinance provides Qarz-e-Hasna (loan to be repaid) with zero interest in compliance of the Islamic principle of taking no interest on repayment of loan's principal amount (Ansari et al., [2019](#)). This model is developed to support needy people who are financially vulnerable and excluded from conventional credit systems due to non-availability of collateral. People usually apply for Qarz- e Hasna to meet urgent needs like medical expenses, emergencies, or to finance small business activities. Only principal amount is due on the borrowers without any interest rate which eases the financial pressure on low-income households. Most important feature of Qarz- e Hasna is mutual trust and support which makes it highly effective in building social capital (Akhuwat Islamic Microfinance, [2025](#)).

4.1.3 Micro-Savings

Micro-savings products are designed for individuals who have low income. This is a safe way to secure a small amount of money for those who have limited financial means. Micro saving account can be opened

with a very little amount with flexible withdrawal options. It makes easier for people to save some money for important future needs. Micro-savings accounts promote saving culture among the people who are unable to open an account in formal banking system. A significant benefit of these accounts is their ability to strengthen financial security, help individuals and provide them opportunity to manage and grow their savings in a safe environment. This product is provided by the MFBs only (SBP, [2025](#)).

4.1.4 Micro-Insurance

Micro-insurance products are designed to protect the clients from business loss, health issues, loss of life, and loss to asset like crop and livestock. The main purpose of micro-insurance is to save low income households from financial shocks activated by medical emergencies, death, or natural disasters. The defining property of these products is their low cost, minimum premium which makes them affordable for low income group to save their livelihood from unexpected emergencies (SBP, [2025](#)).

4.1.5 Micro-Entrepreneurship Loans

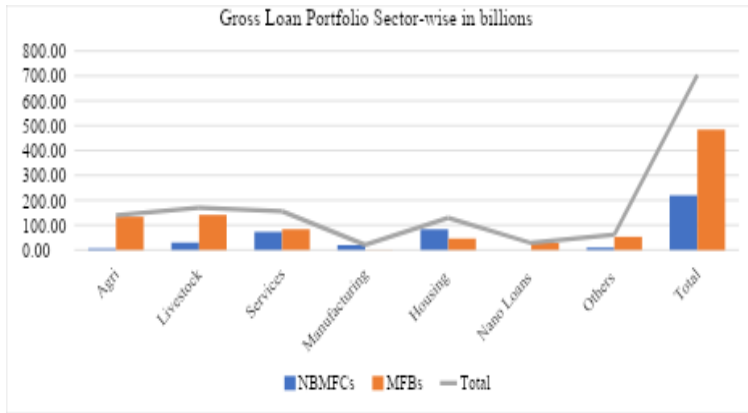
Micro-entrepreneurship loans are created to support individuals who want to start or grow their small businesses. This loan can be used for buying equipment, stocking up on raw materials, or building inventory. These loans enable people to get the tools they need to keep their businesses running smoothly (Pakistan Microfinance Network, [2025](#)). Owing to flexible repayment schedule, these loans are very convenient which are adjusted according to the borrowers' cash flows thus providing ease to borrowers to pay back with no stress (SBP, [2025](#)).

4.1.6 Agriculture Financing

These loans serve the small farmers and facilitates them to procure necessary equipment and seeds. The farmers who cannot access the conventional loans from the banks get benefit from this type of financing which provides the critical funds required to sustain and increase their agricultural productivity. By bridging this financing gap, these loans help farmers to enhance the crop yields, buy better quality agriculture-products, earn more and play their role for food security (SBP, [2025](#)).

Figure 18

Gross Loan Portfolio Provided by NBMFCs and MFBs Sector-wise



Note. Gross loan portfolio of NBMFCs and MFBs sector-wise from Pakistan Microfinance Network ([2025](#))

The figure 18 above shows that the highest gross lending by MFBs is being done for Livestock/Poultry (140.85 billion), followed by Agriculture (133.14 billion) and then by Trade/Services (83.14 billion). However, the highest gross lending by NBMFCs is being done for Housing (82.85 million) followed by Trade/services (72.69 million). Small farmers face huge challenges in repaying the Microloans due to unpredictable crop patterns and decreased crop yields owing to frequent climatic changes, therefore, climate change is an emerging challenge towards loan defaults especially for the agricultural loans (S. Siddiqui, personal communication, September 8, 2025).

4.1.7 Group Lending

In this lending, each member of the group guarantees the individual loan repayment ([Besley & Coate, 1995](#)). This model is helpful in the societies where people are unable to provide collateral or do not have credit history so they cannot access formal banking system. The main objective of group lending is to encourage social cohesion and mutual support within the community, and reduce risk of nonpayment of loan through the group's collective responsibility (Kashf Foundation, 2018).

4.1.8 Digital Financial Services

In this era of digitalization, microfinance institutions and banks offer a variety of digital financial services like mobile money products, digital loans, and mobile wallets which provide financial assistance to the needy

people at their doorstep (Manzoor et al, [2021](#)). The main objective of mobile wallets and mobile saving is to provide opportunities to individuals who do not have access to traditional formal banking services. These mobile financial services provide easy access to rural population and they can obtain loan by using mobile phones (Pakistan Microfinance Network, [2025](#)).

Figure 19

Sector-wise lending Portfolio shares

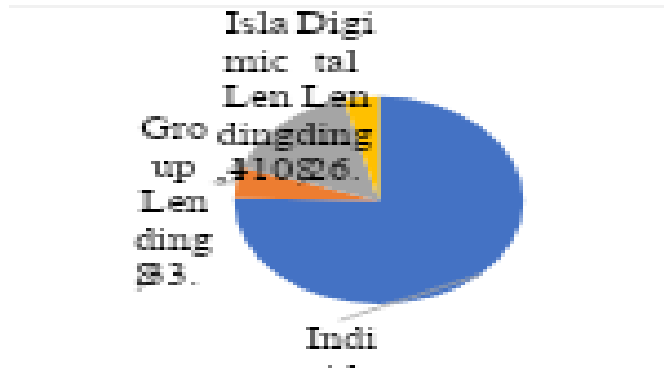


Table 1

Portfolio Share in Bn (%)

Type of Lending	Share in Bn (%)
Individual Lending	521.6 billion (75%)
Islamic Lending	110.4 billion (16%)
Group Lending	33.8 billion (5%)
Digital Lending	26.8 billion (4%)

Note. Sector wise lending portfolio shares from Pakistan Microfinance Network ([2025](#))

The Pie-chart shows the volume in terms of funds (billion rupees) and percentages of four different types of lending including Individual at the top, followed by Islamic, group at third position while the digital with only 4 % share among rest of lending methodologies.

4.2 Interest Rates and Fees in Microfinance in Pakistan

Microfinance can be used as a vibrant tool that helps low-income individuals especially in rural areas and enables them to have access to financial services. However, interest rate and fee of microfinance loan affect affordability and accessibility while the type of loan, institutional policies, and borrower demographics characteristics determine the interest rate and fee of financial loans. Usually, there is huge difference between the cost of microfinance loan and traditional commercial loans. As a matter of fact, the cost of microfinance loan is higher than the cost of commercial bank's loan due to the former's sustainability. In Pakistan, MFBs normally charge interest rates ranging from 25% to 30% annually to cover the cost of small loans thereby, borrowers are liable to pay higher interest rate because they obtain loan without any collateral or have no credit history (A. Basharat, personal communication, September 7, 2025).

4.3 Comparing Microfinance and Traditional Bank Interest Rates

Commercial banks charge 15% to 20% interest rate annually on personal loans while MFBs charge 25% to 30%, several factors operate behind this difference in the cost of borrowing. First, MF sector receives funds from either the PMFIC or from the commercial banks with interest rates and charges the same from the borrowers including their administrative costs that makes it expensive (S. Siddiqui, personal communication, September 7, 2025). Second, MF serves high-risk borrowers because they are unable to produce collateral and do not have any credit history. Third, Microfinance serves in remote areas where the cost of establishing a branch is high, so to cover operational and transactional costs, they charge higher rates (Shankar, [2007](#)). Therefore, higher interest rates and fees restrict the financial inclusion which is the main objective of Microfinance.

4.4 Repayment Terms and Collection Practices in Pakistan's MF Sector

Effective repayment terms and collection practices play a significant role in making the MFIs and MFBs financially viable and sustainable, so they can foster financial inclusion in Pakistan, particularly among low-income populations who are unable to access traditional banking systems (Kamran & Uusitalo, [2024](#)).

4.4.1 Collection Practices in Microfinance

Microfinance institutions adopt a range of effective collection practices such as weekly collection visits, mobile and digital payments, group lending payments, late payment and default fees, and community-based collection models.

a) Weekly Collection Visits: The concerned person regularly visits the borrower in person to collect the repayment. The regular visits not only regularize the repayment but also enable the monitoring of borrower's business besides providing him/her the necessary support to avoid default. This practice is particularly effective for small business borrowers because MFI officers' regular engagement with small-scale enterprises improves borrower's capacity to repay (Kashf Foundation, 2018).

b) Mobile and Digital Payments: Mobile banking and digital payment platforms such as Easypaisa and Jazz Cash were introduced to facilitate the borrowers and to reduce cost involved in physical collection visits. These digital collection modes facilitate the backward rural areas where physical branches of MFBs are limited (Pakistan Microfinance Network, [2025](#)).

c) Group Lending Collections: In group lending models, a loan is issued to a group and all members of the group are responsible for repayment of loan, so borrowers are held accountable by their peers which reduce the risk of default. Group leaders coordinate with members of the group and guarantee the compliance of the loan as per repayment schedules (Kashf Foundation, 2018).

d) Community-Based Collection Models: Community representatives are responsible for loan repayment process. These representative individuals have greater knowledge about the local context and have contact with borrowers at personal level, so they ensure the 100 % repayments through relationship with community and reduce the risk of default (Akhuwat Islamic Microfinance, [2025](#)).

4.5 A Comparative Analysis of Microfinance Institutional Practices, Lending, Methodologies, and Repayment Systems in India, Pakistan and Bangladesh

In South Asia, microfinance emerged as a significant tool to overcome poverty and gender inequality. It serves marginalized and underserved populations, which serves to enhance financial inclusion and poverty alleviation. In India, Pakistan, and Bangladesh, MFIs and MFBs have

adopted various institutional frameworks, lending methodologies, and repayment systems that are well suited to their local population according to their socio-economic conditions.

4.5.1 Institutional Framework and Regulatory Environment

In India, microfinance institutions operate under the regulatory oversight of the Reserve Bank of India (RBI), which governs Non-Banking Financial Company–Microfinance Institutions (NBFC-MFIs), alongside the Ministry of Rural Development, which manages the Self-Help Group (SHG) model. In contrast, Pakistan’s microfinance sector is regulated by the State Bank of Pakistan (SBP) which supervises MFBs and the Securities and Exchange Commission of Pakistan (SECP), which oversees MFIs. Renowned stakeholders in Pakistan’s microfinance sector include Khushhali Microfinance Bank and Akhuwat Islamic Microfinance. Majority number of the borrowers from these MF facilities are rural (SBP, 2025). The MF sector in Bangladesh is predominantly prevailing by institutions including Grameen Bank and BRAC. The Grameen Bank is termed as a founder MF bank globally especially in the group lending methodology. Microcredit Regulatory Authority (MRA) in Bangladesh regulates this sector which functions under the supervisory control of Bangladesh Bank. The purpose is to ensure financial discipline, transparency, and greater outreach to low-income communities (Grameen Bank, 2020).

4.5.2 Lending Methodologies

The lending methodologies are offered in different countries in unique manner to cater to the distinct challenges of providing micro loans to poor populations. The most popular models are the Self-Help Group (SHG) and Joint Liability Group (JLG) models which are offered in India. SHGs are small, mostly composed of women, who save the funds together and provide loans to one another thus ensuring availability of loans besides the building the social capital. The second model is offered to agricultural and small business borrowers, in which the group members provide guarantees for each other’s debts. This replaces the physical collateral with the social collateral (Microfinance India, 2020). Apart from this, lending on individual level has also grown very fast in India, focusing the SMEs and enterprises run by women.

In Pakistan, although the MF services for group lending are available but the sector puts more focus for the individual lending, especially for people in small businesses and agriculture (Pakistan Microfinance

Network, [2025](#)). A unique service in Pakistan's microfinance landscape is the provision of interest-free lending model (Qarz-e-Hasna) which is introduced by the MF institutions like the Akhuwat Foundation, which targets the promotion of economic empowerment and poverty alleviation through interest free loans (Shariah-compliant debts).

4.5.3 Repayment Terms and Collection Practices

The repayment mechanism in India, are made in monthly cycles, although agricultural loans have more flexible payment schedules linked with the income cycle of the borrowers (RBI, 2020). The MF sector of Pakistan also provides flexible repayment schedules, with provision of paying back on any of the option including weekly, fortnightly or on monthly basis, depending on the borrowers' budget. Mostly borrowers including the farmers are provided a grace period up to three months, so that they can repay after the harvesting of crops (Pakistan Microfinance Network, [2025](#)). The repayment conditions in Bangladesh require paying back weekly or monthly, though the Grameen Bank has set the standard for weekly repayments for its group lending model. The bKash mobile payment system is used as a major tool for repaying the loans particularly in rural areas (Grameen Bank, [2020](#)). The mobile repayment platforms such as Paytm and Bharat Pay have become very popular for being user friendly. Pakistan has also introduced the cellular transactions through Easy paisa and Jazz Cash by mobile phones (Pakistan Microfinance Network, [2025](#)).

4.5.4 Outreach and Client Base

India's MF sector reaches over 78 million active borrowers, with a significant portion of clients from rural areas. Women account for the majority of borrowers, reflecting the country's emphasis on gender-inclusive financial products (Microfinance India, 2024). Pakistan's MF sector has active borrowers of about 12 million with 46% of which women, primarily from rural regions (Pakistan Microfinance Network, [2025](#)). The agriculture sector is a key focus in Pakistan, with institutions like Khushhali Bank reaching small-scale farmers (SBP, [2025](#)). Bangladesh, with its pioneering MFB, Grameen Bank, has a client base of over 12 million borrowers alone, with 80% of these borrowers being women from rural areas out of its total 32.18 million MF borrowers (Tung, [2024](#)). Both Grameen Bank and BRAC have extensive outreach programs that focus on empowering rural women through microcredit and social development programs (Grameen Bank, [2020](#)). One very important reason

for Pakistan having less outreach and client base in MF sector is limited availability of low cost wholesale financing/ credit lines which limit the number and outreach of MFIs (S. Siddiqui, personal communication, September 8, 2025). Besides MF, government reaches out the poor for their sustenance through cash transfers by different Federal and Provincial agencies particularly to quote example of Benazir Income Support Program (BISP), wherein the funds are provided for the consumptive/non-productive usage of the beneficiaries (M. Saqib, personal communication, September 6, 2025). The volume of current allocation for BISP has reached a record high level of about 716 billion rupees (The Nation, [2025](#)).

Table 2

Comparison of different MF Indicators for Pakistan, India & Bangladesh

Countries	Pakistan	India	Bangladesh
Regulator	SBP for MFBs & SECP for MFIs	Reserve Bank of India (RBI)	Bangladesh Bank
GLP (PKR)	703 billion	13.97 trillion	4.3 trillion
No. of MF Providers	46	194	731
Borrowers (M)	12	78+	32+
Portfolio-at-Risk >30 days	6.38%	2.3%	1-2 %

Note. Comparison of different MF indicators for Pakistan, India and Bangladesh indicating their regulators, gross loan portfolios, MFPIs, total number of borrowers and Portfolio at risk: Pakistan Microfinance Network ([2025](#)), Microfinance India (2024), Microcredit Regulatory Authority ([2024](#)) & (Grameen,[2018](#))

4.5.5 Poverty Graduation Approach of PPAF

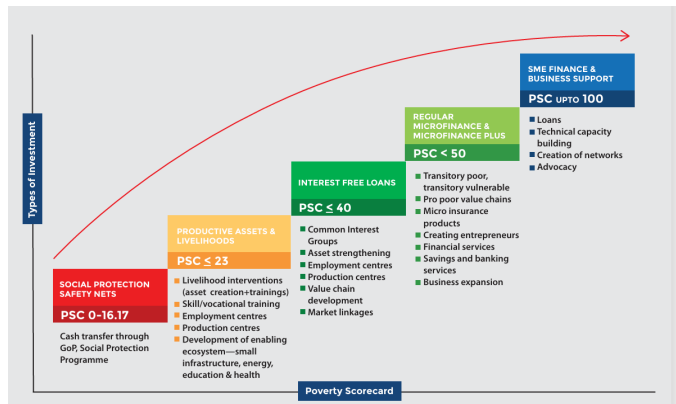
Validating the theory of Poverty Graduation elaborated in Section 1.1, PPAF's interventions target to enable the households graduate out of poverty, reducing their dependence on the government's social protection grants/cash transfers. The poverty graduation model of PPAF is steered by evidence, with outcomes also verified by a global research study published in the May 2015 issue of Science. The study gathered evidence from randomly selected six graduation programs (in Ethiopia, Ghana, Honduras, India, Pakistan, and Peru) between 2006 and 2014.

The Poverty Graduation Arc in Figure 20 demonstrates the Graduation model, making progress through consumption support, skills enhancement, asset transfer, saving, access to finance and business

support, ultimately leading to sustainable livelihoods. Distinct and well-thought-through interventions are tailored to each poverty band to ensure that appropriate combination of tools is used to effectively graduate people to a higher score on the Poverty Score Card (PSC). With this approach, PPAF actually provides an exit strategy from the government’s social protection, non-productive/consumptive initiatives (PPAF, 2025). It is pertinent to mention that the MF loans are for productive usage therefore, government may consider re-directing some share from the huge allocations from government’s social protection programs, diverting the non-productive usage to productive usage for the MF sector in line with the Poverty Graduation approach of PPAF (Z. Azad, personal communication, September 17, 2025).

Figure 20

Poverty Graduation Approach/ Model Adopted by PPAF



Note. Poverty Graduation Approach model adopted by Pakistan Poverty Alleviation Fund demonstrating Poverty Graduation Arc under the Graduation model, making progress through consumption support, skills enhancement, asset transfer, saving, access to finance, and business support, ultimately leading to sustainable livelihoods (PPAF, 2024).

5. SECTION IV: FINDINGS –CHALLENGES FACED BY MF SECTOR IN PAKISTAN ON BASIS OF DESCRIPTIVE AND EVALUATIVE ANALYSES

5.1 Chi-Square Analysis of Data Collected through Questionnaire

Table 3
Chi-Square Matrix

Hypothesis	Chi-Square Test		Decision (Status of Hypothesis)	Value	Decision (Strength Level)
	DF	Statistical Significance			
Association between use of loan as planned and change in income (data collected from answers of Q3 & Q8)	3	.000	Accepted	.454	Moderate
Association between loan fulfilling the purpose and client satisfaction (data collected from answers of Q4 & Q9)	4	.000	Accepted	.225	Weak
Association between loan amount received and economic elevation (data collected from answers of Q6 & Q5)	6	.044	Accepted	.133	Weak
Association between current source of income and change in income (data collected from answers of Q7 & Q8)	6	.000	Accepted	.292	Weak

For the Chi-Square test, if statistical significance is less than .05 then researcher's alternative hypothesis is acceptable as is the case in all four hypotheses mentioned above. For gauging the strength of the association, it is tested that if the value is between 0 and 0.3, then association is considered weak; for value range between 0.31 to 0.5, it is considered moderate; for value range between 0.51 to 0.7, it is considered as good; and for 0.71 onward, it is considered highly strong (McHugh, [2013](#)).

For the first hypothesis, it is evident from the Chi-Square test that there lies a moderate association between use of loan amount as planned by the borrower and change in income after utilization of the MF. This moderate association is interpreted to link the utility of loan with impact on income level meaning that MF facility does have a positive impact on borrowers' economic status.

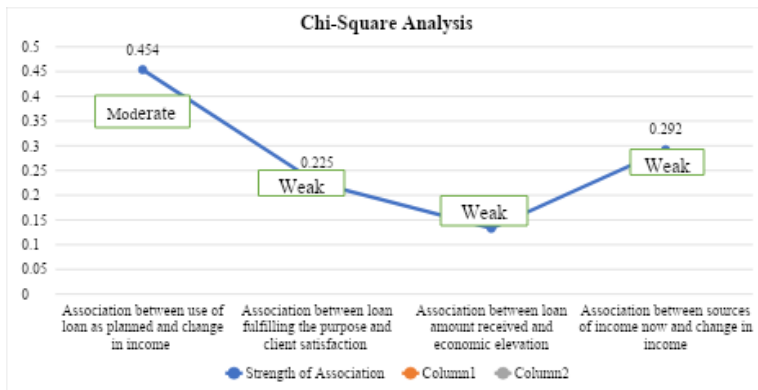
For the second hypothesis, there lies a weak association between MF fulfilling the purpose of borrower and his/her satisfaction on MF facility. The weak association is interpreted to link the fulfillment of purpose of loan and level of satisfaction of the borrower owing to lesser amount of loan received or unsustainable loan.

For the third hypothesis, the association between loan received and economic elevation is also weak depicting the fact that there are other external factors too beyond the MF which affect the economic stability of the borrower and these factors are not controlled by the borrowers.

For the fourth hypothesis, similarly just like the last two cases, the association is weak between the current source of income and change in income which also identifies the existence of factors other than the MF facility, beyond the control of the borrowers.

Figure 21

Chi-Square Analysis for Strength of Association from survey responses on MF



Note. Results of Chi-Square Test - Analysis showing strength of association between different variables from survey responses

5.2 Challenges Identified

5.2.1 Operational Efficiency, Financial Sustainability and Stringent Regulations

Despite reasonable growth in Pakistan’s MF sector, the MFBs and MFIs continue to face serious challenges, particularly in terms of operational efficiency and financial sustainability. One of the major issues confronted is operational efficiency in providing loans to a large number of borrowers which ordinarily requires regular monitoring, executing the repayment

collections and travelling for field visits. These activities raise the cost of operation, which in turn reduces efficiency and the MFIs operate below their optimal capacity. Alongside operational issues, financial sustainability is another pressing challenge. In Pakistan, due to stringent regulations, the MFIs are barred from receiving deposits/savings from their clients and they have to depend largely on either the grants or the wholesale funds provided by the PMFIC or Commercial banks with interest rate ranging from 15 to 20 %. The loans are thus charged at higher interest rates making them expensive for the poor borrowers besides the limited equity also causes financial sustainability issues over long run (M. Saqib, personal communication, September 6, 2025). Research indicates that larger institutions are more likely to attain financial stability because of economies of scale as these facilities have a large clientele. They get better repayment charges and thus attract investments more frequently (Ngo, Mullineux, & Ly, 2014). Smaller MFIs, on the other hand, often struggle to cover administrative costs and rely on external subsidies, raising doubts about their long-term viability (Purohit & Saravanan, 2018).

5.2.2 Challenges of High Interest Rates by MFBs and Lesser Share by MFIs in MF Sector

The data on gross loan portfolio for July 2025 demonstrates that 69% of this portfolio is provided by the MFBs while hardly 31% is being provided by the NBMFCs. Another huge challenge is identified by analyzing the data on the contributory share by both sectors. The banks of MF sector provide loans on an average interest rate of 25 to 30% while the MFIs which charge relatively lesser interest rates are able to serve only about 30% of the total borrowers. This means that loan portfolio is inclined towards MFBs which are more costly MF providers as compared to the MFIs. The lesser share of MF sector by the MFIs identifies the associated challenge of limited and low-cost credit lines (A. Basharat, personal communication, September 6, 2025).

5.2.3 Loan Default, Risk Management and Impact of Climate Change (External Factors) on MF Sector

Another persistent challenge confronting microfinance institutions (MFIs) is the problem of loan default, which directly threatens both operational sustainability and financial stability. Climate change has emerged as one of the most pressing challenges for economy of Pakistan as well as for its MF sector. Particularly for agriculture loans, the ability of growers and

small-scale borrowers to repay their loans is severely affected, and they cannot improve their economic conditions either (S. Siddiqui, personal communication, September 8, 2025). Owing to reduced yields affected by climatic changes, the poor farmers are likely to default and thus become risky clients for the MF sector which ultimately reduces MF service availability due to risk management concerns under a stringent regulatory regime (Pakistan Microfinance Review, 2025).

5.2.4 Lack of Trained Human Resource and Capacity Building of Clients

Human resource capacity and training play a central role in shaping the effectiveness and sustainability of MFBs and that of MFIs. Although MFIs are widely recognized for their contribution to financial inclusion and economic elevation of the borrowers, their long-term success largely depends on the strength of their human resource systems and the quality of training provided to clients. Research shows that MFIs often struggle with issues such as high staff turnover, lack of professional development, and the demanding nature of fieldwork, all of which weaken institutional capacity ([Das, Newton-Lewis, Khalil, Rajadhyaksha, & Nagpal, 2022](#)) Developing the capacity is a very important aspect of sustainable microfinance. Sapovadia ([2007](#)) refers to it as a “pillar of microfinance,” with focus on the strengthening of the staff as well as that of the clients in terms of the required skills of financial literacy, transparency, and long-term institutional growth. In Pakistan, institutions such as the National Rural Support Programme (NRSP) and Akhuwat Islamic Microfinance (AIM) do provide technical and business development trainings to their borrowers which helps them to increase their productivity and scale up their businesses. However, this challenge still remains there owing to their comparatively smaller share of about 3.4 million active borrowers only out of a national total of around 12 million.

5.2.5 Challenges of Technology Adoption and Digitalization in Microfinance Institutions

Recent data from the Pakistan Microfinance Network ([2025](#)) indicates that systemic hurdles continue to stifle the momentum of digital adoption within Microfinance Institutions (MFIs). A primary deterrent is the intensive capital requirement for digitalization; many MFIs operate under tight fiscal constraints, making the procurement and maintenance of sophisticated digital architecture nearly prohibitive. Beyond internal finances, external environmental factors play a critical role. Research from

emerging markets suggests that even when upfront investment is secured, success is often thwarted by inadequate physical infrastructure, such as inconsistent power supplies and limited internet coverage in rural locales (Rozzani et al., 2013). Furthermore, there is a significant "digital readiness" gap among the target demographic. Effective online transition assumes a level of hardware access and digital competency that many low-income borrowers simply do not possess (Yousry Fattouh & Sobhi Makhoulouf, 2024). The impact of these barriers is quantifiable: digital lending currently accounts for a mere 4% of the sector's total portfolio (roughly PKR 26.8 billion). This disparity emphasizes that for digital transformation to be truly inclusive, it must be accompanied by robust infrastructure and comprehensive client education.

6. CONCLUSION

This study demonstrates that the microfinance sector is deeply embedded in essential industries like agriculture, livestock, and small-scale manufacturing, serving as a lifeline for those marginalized by commercial banking. However, while the sector currently supports 12 million clients, this is notably small when compared to a neighbor like Bangladesh, where a single institution can serve a similar number. With an estimated 40 million potential borrowers still lacking access, the "untapped potential" is vast. Realizing this growth requires addressing structural weaknesses, such as high funding costs and rigid regulatory environments. By shifting toward poverty graduation models and technological scaling, the sector can transition from a short-term relief mechanism to a foundational pillar of national economic elevation.

7. SECTION V: WAY FORWARD FOR MICROFINANCE IN PAKISTAN

The following actionable strategic recommendations are proposed to convert the existing challenges into future opportunities for the growth of Pakistan's MF sector:

A. Operational Efficiency, Financial Sustainability, and Stringent Regulations

- **Targeted fiscal support:** Implement performance-linked subsidies to assist smaller MFIs in managing high overheads.
- **Liquidity optimization:** Collaborate with Development Finance Institutions (DFIs) to secure low-interest credit lines for the PMFIC.

- **Strategic fund allocation:** Redirect a portion of BISP funds (approximately 10%) toward poverty graduation initiatives managed through MFIs.
- **Regulatory flexibility:** Reform policies to allow stable MFIs to accept deposits, thereby diversifying their funding sources.
- **Resource pooling:** Utilize shared digital platforms and monitoring systems to minimize redundant operational costs.

B. Loan Default, Risk Management, and Climate Change

- **Develop weather-indexed** crop insurance and micro-insurance schemes tailored for small farmers.
- **Establish risk-sharing** funds between government, donors, and MFIs/MFBs to absorb shocks during climate-related disasters.
- **Train borrowers** in climate-smart farming practices to reduce vulnerability and improve repayment capacity.

C. High Interest Rates and Limited Share of MFIs

- **Encourage blended finance models**, combining concessional donor funds with commercial investment to reduce lending costs and increase the outreach of MFIs.
- **Provide targeted credit lines** to MFIs through the PMFIC at subsidized rates.
- **Encouraging partnerships** between MFBs and MFIs to extend affordable credit into underserved rural areas and reduce their dependence on commercial debts.
- **Fixing responsibility** with facility - linking the licenses of the MFIs and MFBs with increase in borrowers' base with clear yearly targets by SECP and SBP respectively.

D. Trained Human Resource, Capacity Building & Facilitation of Clients

- Provision of short training programs for staff in financial management, digital tools, and client engagement in collaboration with team of PPAF.
- Introduction of retention incentives and linking career growth with performance to reduce high staff turnover.

- Preparing and training the borrowers' education modules on financial literacy & business modeling and link the same with loan disbursement.
- According to the survey results, the importance of personal trust and word-of-mouth needs to be built upon by interactive community programs where satisfied clients should share their experience with others to spread awareness and enhance outreach.
- The highest number of borrowers, in survey results, are between 28 & 45 years, while younger and older people are fewer. Introduction of youth micro-loans with training support and adaptable productive loans for older borrowers will extend services to their age groups.
- The survey results showed that micro-loans ranging Rupees 20,000 - 50,000 was very impactful on increase in income. Availability of such middle range loans with flexible repayment plans and stepwise increase in loan amount, according to enterprises' needs for growth, be ensured to facilitate the borrowers.

E. Technology Adoption and Digitalization

- Create partnerships between MFIs and Commercial Banks/Fintech to capitalize on their digital infrastructure for provision of digital MF services in rural areas.
- Deploy low-cost digital solutions (USSD codes & agent banking) for clients without smartphones or internet.
- Provide digital literacy training for clients and frontline staff to bridge the "last mile" gap in adoption for digitalization.

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