



Capital market imperfections and the incentive to lease ☆

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Abstract

This paper evaluates the influence of financial contracting costs on public corporations' incentives to lease fixed capital. We argue that firms facing high costs of external funds can economize on the cost of funding by leasing. We construct several measures of leasing propensity, plus some *a priori* indicators of the severity of financial constraints facing firms. We find that the share of total annual fixed capital costs attributable to either capital or operating leases is substantially higher at lower-rated, non-dividend-paying, cash-poor firms — those likely to face relatively high premiums for external funds.

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