

## LEBANON THIS WEEK

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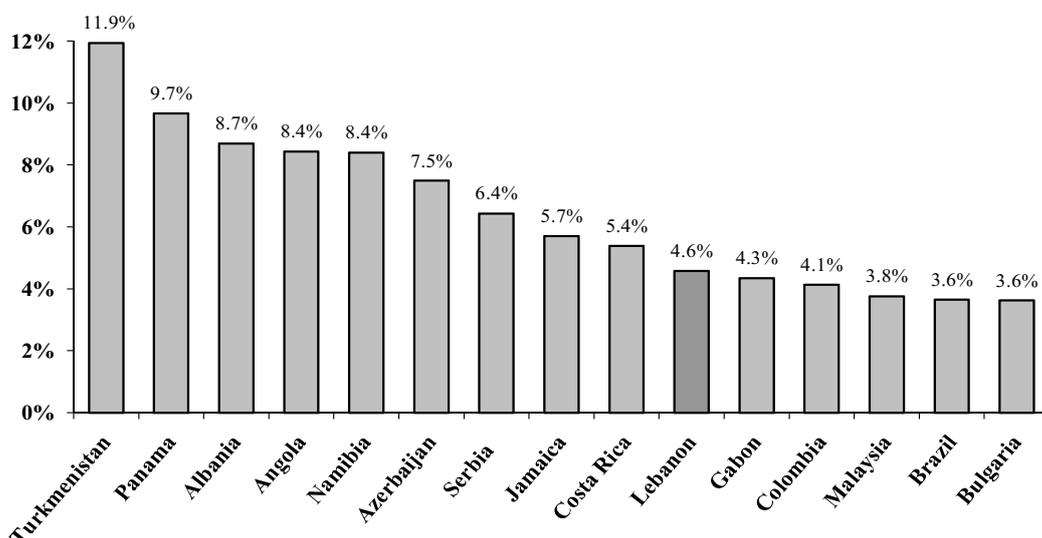
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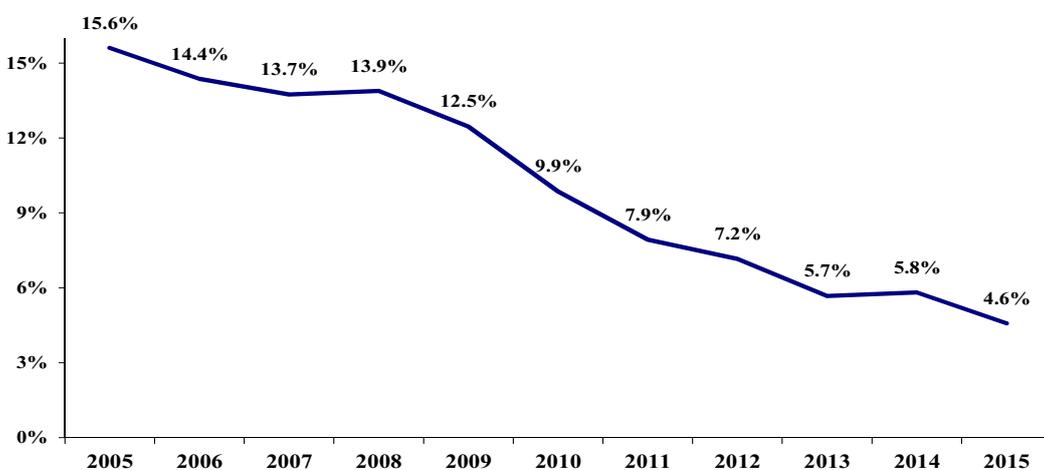
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### Charts of the Week

Largest Recipients of FDI among Upper Middle-Income Countries\* in 2015 (% of GDP)



Foreign Direct Investment Inflows to Lebanon (% of GDP)



\*countries with a GDP of \$10bn or more

Source: UNCTAD, IMF, Byblos Bank

### Quote to Note

"Further narrowing of the fiscal deficit is unlikely without policy reforms."

*Barclays Capital, on the urgent need to implement structural reforms*

### Number of the Week

**42:** Number of times since May 2014 that the Lebanese Parliament convened and failed to elect a President

## Lebanon in the News

\$m (unless otherwise mentioned)	2015	Mar 2015	Dec 2015	Jan 2016	Feb 2016	Mar 2016	% Change*
Exports	2,952	257	236	186	228	220	(14.40)
Imports	18,069	1,509	1,841	1,494	1,377	1,750	15.97
Trade Balance	(15,117)	(1,252)	(1,605)	(1,308)	(1,149)	(1,530)	22.20
Balance of Payments	(3,354)	(417)	(372)	(719)	363	(228)	(45.32)
Checks Cleared in LBP	18,714	1,579	1,709	1,709	1,538	1,609	1.89
Checks Cleared in FC	50,845	4,322	4,265	4,065	3,988	3,983	(7.84)
Total Checks Cleared	69,559	5,901	5,974	5,774	5,526	5,592	(5.24)
Budget Deficit/Surplus	(3,952)	(506.29)	(711.58)	(214.00)	(513.56)	(713.34)	40.90
Primary Balance	724.40	(22.84)	(338.61)	32.08	(276.67)	(156.28)	584.20
Airport Passengers***	7,241,463	478,284	616,249	546,609	442,212	534,954	11.85

\$bn (unless otherwise mentioned)	2015	Mar 2015	Dec 2015	Jan 2016	Feb 2016	Mar 2016	% Change*
BdL Gross FX Reserves	30.64	34.53	30.64	31.64	31.42	30.37	(12.05)
<i>In months of Imports</i>	20.35	22.88	16.64	21.18	22.82	17.35	(24.16)
Public Debt	70.31	69.44	70.31	70.62	71.22	71.04	2.31
Bank Assets	185.99	176.95	185.99	186.20	186.59	187.66	6.05
Bank Deposits (Private Sector)	151.59	145.46	151.59	151.50	151.42	152.44	4.80
Bank Loans to Private Sector	54.22	51.14	54.22	54.39	54.56	55.06	7.65
Money Supply M2	52.15	49.44	52.15	52.24	52.29	52.52	6.23
Money Supply M3	123.62	118.06	123.62	123.26	123.49	124.51	5.47
LBP Lending Rate (%)	7.45	6.94	7.45	8.28	8.18	8.62	168bps
LBP Deposit Rate (%)	5.56	5.57	5.56	5.52	5.57	5.59	2bps
USD Lending Rate (%)	7.06	7.16	7.06	7.34	7.31	7.36	20bps
USD Deposit Rate (%)	3.17	3.12	3.17	3.22	3.22	3.27	15bps
Consumer Price Index**	(3.75)	(3.38)	(3.40)	(3.16)	(2.94)	(3.57)	(19bps)

\* Year-on-Year \*\* Year-on-Year percentage change

\*\*\*includes arrivals, departures, transit

Note: bps i.e. basis points

Source: Association of Banks in Lebanon, Banque du Liban, Ministry of Finance, Central Administration of Statistics, Byblos Research

## Capital Markets

Most Traded Stocks on BSE	Last Price (\$)	% Change*	Total Volume	Weight in Market Capitalization	Sovereign Eurobonds	Coupon %	Mid Price \$	Mid Yield %
Byblos Common	1.64	(0.61)	1,199,285	5.31%	Mar 2017	9.00	103.13	4.20
Audi Listed	6.20	(0.16)	309,857	22.31%	Nov 2018	5.15	100.13	5.09
BLOM GDR	10.05	0.00	100,300	6.68%	May 2019	6.00	101.25	5.52
Solidere "A"	9.69	0.00	92,272	8.72%	Mar 2020	6.38	102.13	5.72
Audi GDR	6.20	0.00	51,462	6.42%	Apr 2021	8.25	109.00	6.03
BLOM Listed	9.95	0.40	21,740	19.26%	Oct 2022	6.10	99.25	6.25
Solidere "B"	9.47	1.07	19,787	5.54%	Jun 2025	6.25	97.25	6.66
Byblos Pref. 09	100.10	(0.10)	3,189	1.80%	Nov 2026	6.60	98.75	6.77
Byblos Pref. 08	100.30	0.00	1,855	1.81%	Feb 2030	6.65	97.75	6.91
HOLCIM	14.50	1.33	730	2.55%	Nov 2035	7.05	99.85	7.06

Source: Beirut Stock Exchange (BSE); \*Week-on-week

Source: Byblos Bank Capital Markets

	July 11-15	July 4-8	% Change	June 2016	June 2015	% Change
Total Shares Traded	1,831,833	223,719	718.81	2,859,053	5,436,086	(47.41)
Total Value Traded	\$7,883,444	\$2,206,225	257.33	\$22,365,431	\$49,874,049	(55.16)
Market Capitalization	\$11.11bn	\$11.08bn	0.24	\$11.03bn	\$11.56bn	(4.55)

Source: Beirut Stock Exchange (BSE)



### Lebanon ranks 122nd globally, 14th in MENA region in country risk

In its quarterly survey of the country risk level in 186 countries, the Euromoney Group ranked Lebanon in 122nd place worldwide and in 14th place among 22 countries in the Middle East & North Africa (MENA) region in the second quarter of 2016. Also, Lebanon came in 38th place among 50 upper middle-income countries (UMICs) included in the survey. Lebanon's global rank improved by one spot from 123rd place in the first quarter of 2016 and regressed by three spots from 119th place in the second quarter of 2015. Lebanon's regional rank has not changed since the fourth quarter of 2013. The survey evaluates individual country risk by assigning a weighting to six categories that cover Political Risks, Economic Performance, Access to Bank Finance & Capital Markets, Debt Indicators, Credit Ratings, and Structural Assessments.

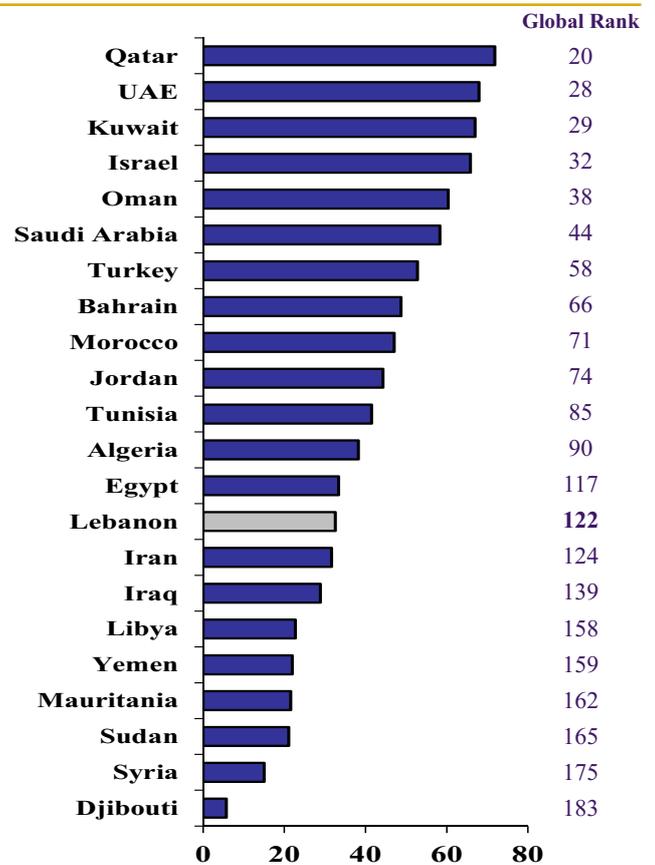
Globally, Lebanon had a lower country risk level than Iran, Mozambique and Pakistan, and a higher risk level than Greece, Egypt and Jamaica among economies with a GDP of \$10bn or more. It also ranked ahead of Iran and behind Jamaica among UMICs. Lebanon's global rank improved by three spots on the Credit Ratings category and by two spots on the Economic Performance category. In contrast, Lebanon's rank was unchanged from the preceding quarter on the Political Risks category, the Structural Assessments factor, the Debt Indicators category and the Access to Bank Finance & Capital Markets category.

In parallel, Lebanon received a score of 32.55 points, almost unchanged from 32.6 points in the first quarter of 2016 and from 32.58 points in the second quarter of 2015. Lebanon's score came below the global average score of 42.7 points, the UMICs' average of 39.6 points and the MENA average of 40.8 points. Also, its score came below the Arab average of 39.4 points and the Gulf Cooperation Council (GCC) countries' average score of 62.4 points, but was above the average score of non-GCC Arab countries of 28.8 points.

Lebanon's score regressed by a marginal 0.3% on the Political Risks category, by 0.2% on the Structural Assessments factor and by 0.1% on the Economic Performance category. Its scores on the Debt Indicators, Credit Ratings and Access to Bank Finance & Capital Market categories were unchanged from the first quarter of 2016.

Lebanon ranked ahead of Cameroon and behind Guatemala globally, while it came ahead of Mauritania and behind Algeria regionally on the Political Risks category. Also, it ranked ahead of Bangladesh and behind Kenya worldwide, and came ahead of Libya and behind Iraq regionally in terms of Economic Performance. Further, Lebanon came ahead of Morocco and behind Panama globally, and ranked ahead of Morocco and behind Bahrain regionally on the Structural Assessment category. Finally, Lebanon ranked ahead of Cambodia and behind Albania globally, and came ahead of Iraq and behind Jordan regionally on the Debt Indicators category.

**MENA Countries Rankings & Scores in Second Quarter of 2016**



Source: Euromoney Group, Byblos Research

**Country Risk Indicators for Lebanon - Second Quarter 2016**

	Weighting (%)	Score	MENA Rank	Global Rank	MENA Avg Score	Global Avg Score
Political Risk	30	10.30	14	131	12.15	13.73
Economic Performance	30	12.39	14	112	13.31	13.35
Structural Assessments	10	5.08	9	66	4.34	4.03
Debt Indicators	10	2.27	16	164	4.47	4.71
Credit Rating	10	1.04	12	111	2.94	3.09
Access to Bank Finance & Capital Market	10	1.50	15	122	3.63	3.80

Source: Euromoney Group, Byblos Research



### **Stable currency and interest rate markets**

In the monthly meeting between the Central Bank and the Association of Banks in Lebanon (ABL), Governor Riad Salamé indicated that the currency market is stable, which is a positive signal. He added that interest rates have been stable, given the common interest between all involved parties to preserve rate stability, especially that the Central Bank's recent operations with Lebanese banks have increased liquidity in Lebanese pound. The Central Bank sold Treasury bills from its portfolio to Lebanese banks, and the banks bought Eurobonds from the Central Bank's portfolio. Governor Salamé noted that banks have already re-invested about 50% of the liquidity generated from these operations, and that the Ministry of Finance is considering a new issuance of long-term Treasury bonds in order to absorb the remaining liquidity. In addition, he indicated that the Central Bank's recent operations with banks have provided them with funds to help them meet the new international accounting standard requirements under IFRS9, which will come into force by 2018. He said that the Banking Control Commission of Lebanon (BCCL) is currently studying the IFRS9 standards and principals that banks need to apply this year, in order to ease the financial burden that they would incur from the introduction of these standards. Governor Salamé noted that, in case the banks' generated funds from their recent operations with the Central Bank exceed the amount required to meet the IFRS9 standards, then they can allocate the remaining funds toward their profits. He considered that the Central Bank's recent measures have supported the stability of the Lebanese pound without any of the involved parties incurring additional costs.

In parallel, Governor Salamé indicated that Lebanon should move forward with the proper implementation of the exchange of tax information with other jurisdictions, in order to avoid being included in the list of non-cooperative countries. He noted that the required amendments to the related laws should at least be ratified by the concerned parliamentary committees, in case authorities do not ratify them. Further, he said that the Central Bank can issue a circular related to Law 44 about fighting money laundering and terrorist financing that already considers tax evasion as a financial crime, in case Parliament fails to convene and ratify the relevant laws. He pointed out that the Central Bank's circular would allow cooperation with the international community on foreign requests related to tax evasion. He added that the automatic exchange of information would require Lebanon to join the related international treaty in order to be able to receive and provide tax information automatically. In addition, he said that the outflow of information covered by the Lebanese banking secrecy law can be processed through the Special Investigation Commission against money laundering and terrorism financing. He noted that the incoming information should be centralized in a secured database in order to avoid any negative impact on the capital and financial inflows to the country.

In parallel, Governor Salamé called on banks to resort to Basic Circular 135 about debt restructuring in order to limit the rise of non-performing loans in their loan portfolios that have been materializing since 2015. However, he indicated that the BCCL has not yet received any file related to the circular.

### **Compensation of public-sector personnel up 8% in first 11 months of 2015, absorbs 35% of fiscal spending**

Figures issued by the Ministry of Finance show that the compensation of public-sector personnel totaled \$4.2bn in the first 11 months of 2015, constituting an increase of 8.2% from \$3.9bn in the same period of 2014. Salaries, wages and related benefits accounted for 66.1% of the total in the first 11 months of the year, followed by retirement benefits (24.8%), transfers to public institutions to cover salaries (4.7%) and end-of-service indemnities (4.4%). The increase in the compensation of public-sector personnel reflects an annual rise in salaries, wages and related benefits, retirement benefits, transfers to public institutions and end-of-service indemnities. The compensation of public-sector personnel represented the largest component of total primary spending and accounted for 67% of such expenditures in the first 11 months of 2015 compared to 57% in the same period of 2014. The compensation of public-sector personnel absorbed 35% of total fiscal spending in the covered period, up from 31% in the same period of 2014.

In parallel, salaries, wages and related benefits paid to public-sector employees totaled \$2.8bn in the first 11 months of 2015, constituting an increase of 4.6% from the same period of 2014. This category includes basic salaries, employment benefits, allowances, contributions to civil servants' cooperatives, as well as contributions to other mutual funds providing health insurance for specific categories of civil servants, mainly judges, religious judges and employees at the Parliament.

Salaries and benefits of military personnel reached \$1.8bn and accounted for 62.9% of salaries, wages and related benefits paid in the public sector in the first 11 months of 2015, followed by educational personnel with \$588.4m (21%), civil staff with \$272m (9.7%), the government's contribution to the employees' cooperative with \$154.6m (5.5%) and customs employees with \$22.6m (0.8%). Also, the Lebanese Army's salaries totaled \$1.1bn in the first 11 months of 2015 and represented 64.4% of military personnel's salaries and benefits. The salaries of the Internal Security Forces followed with \$473m (26.9%), those of the General Security Forces with \$121.4m (6.9%) and the State Security Forces with \$32.5m (1.8%).

The overall increase in salaries, wages and related benefits paid to public-sector employees reflects an expansion of \$90.2m in basic salaries, an increase of \$40.5m in allowance and a rise of \$4.6m in employment benefits, which was partly offset by a drop of \$8m in other payments given to non-military bodies, such as bonuses. The increase in allowances was allocated almost in full to military personnel. Overall, basic salaries grew by 4.6% year-on-year to \$2.1bn in the first 11 months of 2015, allowances increased by 11.4% to \$395.4m and employment benefits rose by 3.7% to \$128.7m, while other payments disbursed to non-military bodies decreased by 4.3% to \$191.7m.



### Merrill Lynch upgrades Lebanon's external debt to Marketweight, debt posts 7th lowest return in emerging markets

Figures issued by Merrill Lynch indicate that Lebanon's external debt posted a return of 2.59% in the first half of 2016, constituting the fourth lowest return among 41 markets in the Central & Eastern Europe and the Middle East & Africa (CEEMEA) region, as well as the seventh lowest return among 72 emerging markets included in Merrill Lynch's External Debt EM Sovereign Index. Lebanon underperformed the overall emerging markets' return of 9.07% during the covered period. Further, Lebanon's external debt posted the second lowest return among 24 countries in the Middle East & Africa region in the first half of the year, ahead of only Mozambique (-11.8%).

In parallel, Merrill Lynch tactically upgraded its recommendation for Lebanon's external debt to "Marketweight" from "Underweight" in its emerging markets portfolio of external debt. It noted that Lebanese Eurobonds have been extremely stable due, in large part, to support from the local banks. It added that the recent underperformance could represent a reasonable opportunity for international investors to cover some of their Underweight positions. Merrill Lynch's recommendation on Lebanese Eurobond had been "Underweight" since April 28, 2016.

Also, Lebanon's external debt posted a return of -0.95% in June 2016, constituting the second lowest return in the CEEMEA region and the fourth lowest in emerging markets during the covered month. Lebanon underperformed the emerging markets' return of 3.07% in June 2016.

Further, Lebanon's external debt posted the second lowest return in the Middle East & Africa region in June 2016, ahead of only Mozambique (-5.38%). It underperformed Zambia (+6.33%), Ghana (+5.27%), Iraq (+5.16%), South Africa (+4.48%), Cameroon (+3.86%), Turkey (+3.83%), Gabon (+3.75%), Senegal (+3.48%), the Ivory Coast (+3.42%), Namibia (+3.34%), Bahrain (+2.3%), Qatar (+2.13%), the UAE (+2.05%), Nigeria (+1.96%), Angola (+1.71%), Morocco (+1.69%), Egypt (+1.61%), Kenya (+1.6%), Israel (+1.57%), Tunisia (+0.81%), Jordan (+0.71%) and Rwanda (+0.07%).

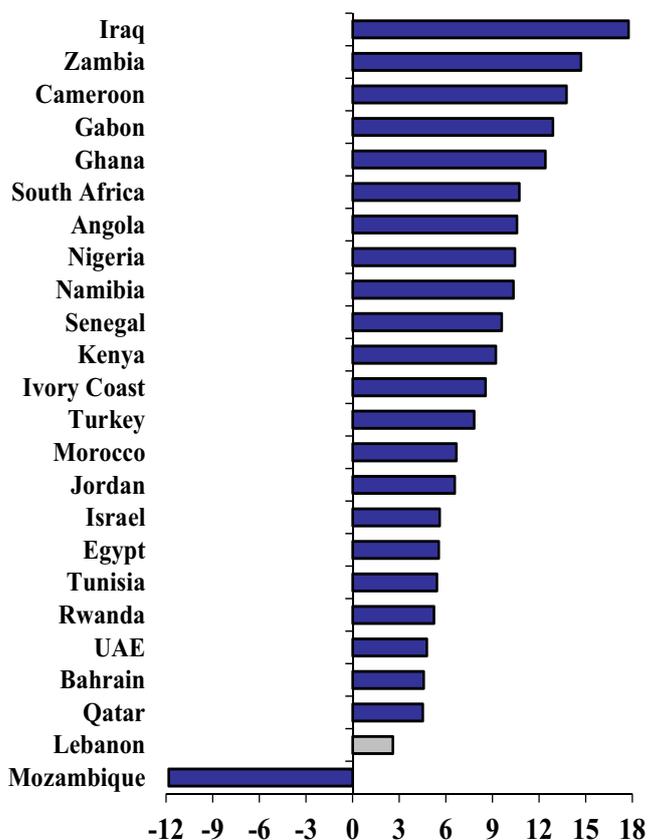
In parallel, Merrill Lynch indicated that the option-adjusted spread on Lebanese Eurobonds was 532 basis points at the end of June 2016 compared to 386 basis points a year earlier, constituting the 17th widest spread in the CEEMEA region and the 25th widest among emerging markets. It was wider than the emerging markets' overall spread of 333 basis points at the end of June 2016. Lebanon has a weight of 2.85% on Merrill Lynch's External Debt EM Sovereign Index, the fifth largest weight in the CEEMEA universe and the 11th largest among emerging economies. Lebanon accounted for 5.5% of allocations in the CEEMEA region.

### Revenues through the Port of Beirut up 4% to \$102m in first five months of 2016

Figures released by the Port of Beirut show that the port's overall revenues reached \$101.5m in the first five months of 2016, constituting an increase of 4.4% from \$97.2m in the same period of 2015. The Port of Beirut handled 3.66 million tons in freight in the first five months of 2016, up by 14.6% from 3.19 million tons in the same period in 2015. Imported freight amounted to 3.26 million tons in the covered period and accounted for 89.2% of aggregate freight, while the remaining 396,000 tons, or 10.8%, consisted of export cargo. A total of 885 ships docked at the port in the covered period compared to 704 vessels in the first five months of 2015.

In parallel, revenues generated through the Port of Tripoli reached \$6.9m in the first five months of 2016, constituting a rise of 21.2% from \$5.7m in the same period of 2015. The Port of Tripoli handled 739,392 tons of freight in the covered period, representing an increase of 15.2% from 641,568 tons in the same period of 2015. Imported freight amounted to 556,300 tons and accounted for 75.2% of the total, while the remaining 183,092 tons, or 24.8% of the total, were export cargo. A total of 2,133 vessels docked at the port in the first five months of 2016, constituting a drop of 0.7% from 2,148 ships in the same period of 2015.

### External Debt Performance in the Middle East & Africa in First Half of 2016 (%)



Source: Merrill Lynch, Byblos Research

### **Fitch downgrades Lebanon's sovereign ratings to 'B-', outlook 'stable'**

Fitch Ratings downgraded Lebanon's long-term foreign and local currency Issuer Default Ratings (IDRs) from 'B' to 'B-' and revised the outlook on the IDRs from 'negative' to 'stable'. It also lowered the Country Ceiling and the ratings on Lebanon's senior unsecured foreign and local currency bonds from 'B' to 'B-', while it affirmed the short-term foreign currency IDR at 'B'. It attributed the downgrades to the sustained political risks that have deteriorated due to the ongoing conflict in Syria, as well as to the country's weak public finances and low economic performance. It noted that negative spillovers from the Syrian conflict have gradually weighed on the country's economy and political environment, which has increased the pressure on the sovereign's creditworthiness. The sovereign downgrade aligns Fitch's new 'B-' rating with Standard & Poor's current rating of 'B-' for Lebanon.

First, the agency indicated that political risks remain elevated, given the 26-month vacuum at the presidential level, the paralysis in decision-making within the government and Parliament, and the deterioration in public services. It considered that the prospects of a substantial improvement in the domestic political environment are linked to a resolution to the Syrian conflict. Second, it pointed out that Lebanon's public finance dynamics are not improving, as the public debt level, estimated at 136.7% of GDP in 2015, is the third highest among Fitch-rated sovereigns. It noted that the high debt level has resulted in elevated and rising debt servicing costs that absorbed about 42% of the government's revenues during the 2013-15 period. It anticipated the wide structural fiscal deficits to persist in coming years due to the lack of fiscal reforms and the elevated current expenditures, which, along with subdued economic activity, would increase the public debt stock during the 2016-18 period. It estimated that the financing of the government's needs has been resilient but is coming under increasing pressure. It noted that the banking system is attracting sufficient deposits to meet the government's financing requirements and to ensure a moderate growth in lending to the private sector. However, it considered that the growth in the banks' deposits has decelerated so far this year. Third, Fitch pointed out that spillovers from the Syrian conflict have significantly affected Lebanon's economic performance and prospects. It projected Lebanon's real GDP growth to remain below 2% in 2016, despite the positive impact of the drop in global oil prices and the Central Bank's economic stimulus packages.

In parallel, the agency indicated that Lebanon's IDRs reflect the country's strong external liquidity buffers despite the wide current account deficit that it estimates at 17% of GDP in 2015. It pointed out that the country's foreign currency reserves remain at a high level. Further, it indicated that the ratings take into account Lebanon's GDP per capita and broader human development indicators, which are well above similarly-rated peers and that are more in line with the median of 'BBB'-rated sovereigns. Also, it noted that the government has a perfect track record of public debt repayment.

### **Association of Banks amends reference rates on US dollar and Lebanese pound lending**

The Association of Banks in Lebanon (ABL) recommended to its member banks to reduce the Beirut Reference Rate (BRR) in US dollars to 6.3% starting in August 2016 from 6.34% in July. The rate, considered as the reference rate for lending in foreign currency, replaced the London Interbank Offered Rate (LIBOR) in 2009, as the ABL considered that the LIBOR does not reflect the cost of funding and lending in Lebanon. Additionally, the ABL recommended to its member banks to decrease the BRR in Lebanese pounds to 8.67% in August from the July rate of 8.7%. The BRR in US dollars and Lebanese pounds were adopted in March and May 2009, respectively. The ABL considers that the BRR does not replace the Beirut Prime Lending Rate in each currency, but constitutes the basis to calculate the prime rate after adding the cost of liquidity and refinancing, credit risk and the profitability of banks to the prime lending rate.

### **Real estate prices vary significantly across Beirut**

Figures released by property advisory firm RAMCO show that the asking price for first floor apartments in buildings under construction in Beirut ranges from a low of \$2,148 per square meter (sqm) in the Basta area to a high of \$8,500 per sqm in the Manara area.

The asking price for first floor apartments in buildings under construction in Beirut is the highest in the Manara area, followed by Wadi Abou Jamil (\$7,500 per sqm), Saifi Village (\$7,133 per sqm), Minet El Hosn (\$7,017 per sqm), the Foch/Allenby street (\$7,000 per sqm), the Grand Serail area (\$6,250 per sqm), Ramlet el Baida (\$6,200 per sqm), Ain el Mreisseh (\$5,880 per sqm), Raouché (\$5,430 per sqm), Saifi (\$5,120 per sqm), Ain el Tineh (\$5,067 per sqm) and Sursock (\$5,000 per sqm). In contrast, the asking price for first floor apartments in buildings under construction in Beirut is the lowest in Basta, followed by Rawas (\$2,150 per sqm), Noueiri (\$2,170 per sqm), the Beirut Arab University area (\$2,180 per sqm), the Salim Salam area (\$2,200 per sqm), Borj Abi Haidar (\$2,282 per sqm), Makassed (\$2,286 per sqm), Hamad (\$2,304 per sqm), Barbour (\$2,315 per sqm) and Karantina (\$2,345 per sqm). The survey covered 348 buildings that are currently under construction in 72 neighborhoods in Beirut.

RAMCO indicated in its 2016 survey that the asking price for first floor apartments in buildings under construction fell in 52% of Beirut's neighborhoods from the preceding year, while it rose in 41% of them and was unchanged in 6% of the capital's neighborhoods.



### **World Bank to focus on service delivery and job creation in Lebanon in coming six years**

The World Bank Group indicated that it approved the Country Partnership Framework (CPF), or business plan, for Lebanon for the 2017-22 period. It said that the CPF focuses on two priority areas that consist of improving the access to and the quality of service delivery, as well as on expanding economic opportunities and developing human capital. It considered that the two focus areas would help Lebanon adapt to the economic and social impact of the Syrian crisis, safeguard the country's development gains, address the country's structural vulnerabilities, and enhance the prospects for stability and development in the coming years.

In terms of expanding the access to and the quality of service delivery, the Bank indicated that the CPF will help alleviate infrastructure constraints where possible and will encourage greater private sector participation in areas where there is potential for substantial impact, where the government is ready to engage, and where there is interest from the private sector. It said that the Bank, along with the International Finance Corporation, its private sector arm, would support select infrastructure investments, including investments in the water sector aimed to improve service delivery and strengthen the Beirut & Mount Lebanon Water Authority operation. It considered that investments in the environmental sector would help reduce industrial, hazardous and wastewater pollution, while investing in the transportation sector would support countrywide connectivity and increase rural and urban accessibility. It added that investments at the level of municipalities would address the service needs of a rapidly growing urban population. In addition, the Bank said that it will continue its dialogue with all stakeholders about the energy sector in order to reach a consensus about it.

In terms of expanding economic opportunities and developing human capital, the Bank pointed out that it will promote the creation of jobs by improving the country's investment climate, by increasing financial inclusion, as well as by developing skills and improving the delivery of education and health care services.

### **Industrial exports down 13% to \$634m in first quarter of 2016**

Figures released by the Ministry of Industry show that industrial exports totaled \$633.9m in the first quarter of 2016, constituting a decrease of 12.8% from \$727.2m in the same quarter of 2015. Industrial exports totaled \$211.6m in March 2016, down by 5% from \$222.8m in the preceding month and by 14.1% from \$246.5m in March 2015. The decline in industrial exports over the first quarter of the year was due to the increasing cost and challenges faced by land and maritime exporters, as well as to lower demand from Lebanon's key export markets. Exports of machinery & mechanical appliances totaled \$167.9m and accounted for 26.5% of aggregate industrial exports in the first quarter of 2016, followed by prepared foodstuffs with \$111.8m (17.6%), chemical products with \$93.1m (14.7%), base metals with \$64.5m (10.2%), and plastics & articles with \$33.3m (5.3%). Arab countries were the destination of 56.7% of Lebanese industrial exports during the first quarter of 2016, followed by European economies with 16.5%, African countries with 14.1%, Asian economies with 7.9%, countries in the Americas with 2.8% and markets in Oceania with 0.5%. On a country basis, Saudi Arabia was the main destination of Lebanese industrial exports and accounted for 14.1% of the total in the first quarter of 2016, followed by the UAE with 11.3%, Iraq with 8.9%, Syria with 5.9% and Jordan with 3.9%. During the first quarter of 2016, 19 African countries, 17 Arab states, 15 European economies, seven Asian countries, three economies in the Americas and one country in Oceania imported \$1m or more each in industrial products from Lebanon. Overall, Lebanon exported its industrial products to 43 European economies, 38 African countries, 22 Asian economies, 19 countries in the Americas, 19 Arab economies and three markets in Oceania during the first quarter of 2016.

In parallel, industrial imports reached \$67.7m in the first quarter of 2016, up by 7% from \$63.2m in the same quarter of 2015. Italy was the main source of such imports and accounted for 22.7% of the total in the first quarter of 2016, followed by China with 21.8% and Germany with 15.7%. Further, imports of industrial equipment and machinery reached \$25.1m in March 2016, increasing by 22.5% from the same month of 2015. Italy was the main source of imports of industrial equipment in March and accounted for 28.1% of the total, followed by China with 17.3% and Canada with 13.6%.



### New car sales up 2% in first half of 2016

Figures released by the Association of Automobile Importers in Lebanon (AIA) show that dealers sold 18,444 new passenger cars in the first half of 2016, constituting an increase of 2.2% from 18,047 cars sold in the same period of 2015. Consumers purchased 2,411 new cars in January, 2,793 automobiles in February, 2,786 cars in March, 3,109 vehicles in April, 3,165 automobiles in May and 4,180 cars in June 2016. Japanese automobiles accounted for 37.2% of total sales in the first half of 2016, followed by Korean cars with a 35.6% share, European automobiles (20.4%), American vehicles (6.1%) and Chinese cars (0.7%). The sales of new American vehicles increased by 20.5% year-on-year in the first half of the year, those of European automobiles rose by 4.5% and sales of Korean cars grew by 2.3%; while the number of Chinese cars sold dropped by 3.2% year-on-year and those of Japanese cars regressed by 1.4%. Kia is the leading brand in the Lebanese market with 3,628 vehicles sold in the first half of 2016, followed by Hyundai with 2,911 in new car sales, Toyota (2,572), Nissan (1,876), Renault (886) and Mitsubishi (756). In parallel, 1,305 new commercial vehicles were sold in the first half of 2016, up by 16.1% from 1,124 vehicles sold in the same period of 2015. Overall, car dealers sold 19,749 new passenger automobiles and commercial vehicles in the first half of 2016, constituting a rise of 3% from 19,171 cars sold in the same period of 2015.

The AIA indicated that 90% of new cars sold were small-engine automobiles with a low selling price. It added that the trend of the market toward buying small cars is due to the absence of an adapted and structured public transportation system, as well as to the drop in the purchasing power of consumers.

In parallel, the number of new vehicles sold by Lebanon's top five distributors reached 13,606 in the first half of 2016 and accounted for 68.3% of new car sales. NATCO sal sold 3,628 vehicles, equivalent to 18.4% of the total, followed by Century Motor Co. sal with 2,960 (15%), Boustany United Machineries sal with 2,887 vehicles (14.6%), Rasamny Younis Motor Co. sal with 2,282 (11.6%) and Bassoul Heneiné sal with 1,849 (9.4%).

### Contract for electricity-generating ships in Lebanon extended until 2018

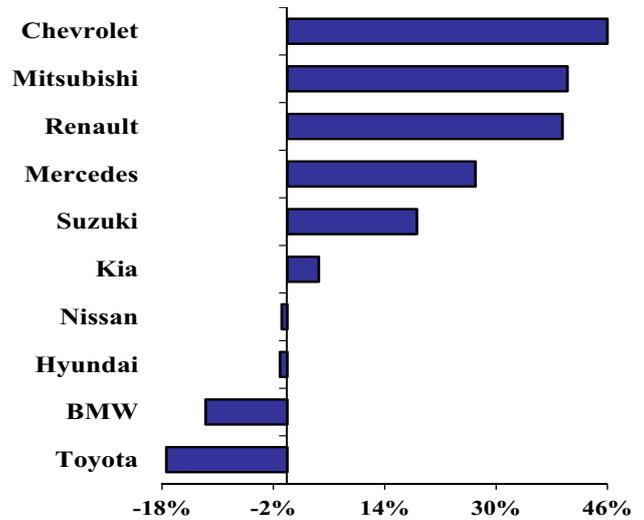
The Ministry of Energy & Water announced that it has extended until the end of September 2018 the contract of Turkish firm Karadeniz Holding for the leasing of two electricity-generating ships. The agreement will provide Lebanon with electricity supply of about 380 megawatts. The ministry added that the ships would produce electricity at a rate of 5.85 US cents per kilowatt hour relative to 5.95 US cents per kilowatt hour in the past three years, which is significantly lower than the average cost of 18 US cents per kilowatt hour for the power that Electricité du Liban produces.

The ministry initially signed the agreement in February 2012 for a period of three years in order to offset the planned suspension of production at the Jiyeh and Zouk Mikael power plants during their rehabilitation process. The ministry had the option to renew the contract for two additional years. However, the ministry indicated that maintenance work has yet to start, even after the arrival of the ships in April 2013. Instead, authorities used the power generated by the two ships to cover the wide gap between local electricity generation and domestic demand. Lebanon's current electricity production stands at around 1,500 megawatts, while demand exceeds 3,000 megawatts.

### Initiative to promote industrial sector in Lebanon

The United Nations Industrial Development Organization (UNIDO), along with the Ministry of Industry, inaugurated the "Creative Lebanon" initiative in Beirut, which is a boutique where small Lebanese producers showcase their new innovative products. The initiative is a joint venture between two of UNIDO's existing projects, the Development of Clusters in Cultural and Creative Industries in the Southern Mediterranean project (CCI) that is funded by the European Union and the Italian government, and the Community Empowerment and Livelihoods Enhancement Project (CELEP) that is financed by Italy. It allows firms that are part of the CCI's jewelry cluster in the Bourj Hammoud area and the furniture cluster in Tripoli to display their products at the boutique. The latter also includes goods produced by Lebanese SMEs and cooperatives that include handmade handicrafts, organic foodstuff, syrups, wine, traditional Lebanese food, compotes, and agro-foods, among other Lebanese-made merchandise. The "Creative Lebanon" initiative aims to promote inclusive and sustainable industrialization in Lebanon. The three phases of the CELEP aim to support the manufacturing capacities of Lebanese SMEs and cooperatives to enhance the production possibilities of the refugee host communities. The objective of the CELEP project is to strengthen the formal private sector and to promote regional cooperation among Southern Mediterranean countries, including Lebanon.

Sales of Top 10 Car Brands in First Half of 2016 (% change\*)



\* from the same period of 2015

Source: AIA, Byblos Research

### **Moody's maintains 'negative' outlook on banking sector**

Moody's Investors Service maintained its 'negative' outlook on Lebanon's banking system for the next 12 to 18 months due to the subdued economic activity in the country that would slow down lending growth and increase the pressure on the banks' asset quality, as well as because of the banks' high and growing exposure to the Lebanese sovereign, which leaves their capital buffers vulnerable to sovereign event risk.

Moody's expected Lebanese banks to face difficulties from the challenging domestic operating environment. It anticipated the domestic political deadlock and regional instability to result in subdued domestic economic activity and lower lending growth. As such, it expected nominal credit growth to decelerate from 7% in 2015 to below 6% in 2016, compared to an annual credit growth rate of 24% during the 2007-10 period. It noted, however, that lending activity in the country would be supported by the Central Bank's fourth economic stimulus package. Further, it pointed out that compliance practices have become more demanding, which would increase operating costs and could cause banks to become more risk averse and forgo legitimate business opportunities. It noted that the cost of compliance would have a bigger impact on smaller banks. However, it considered that Lebanese banks are accustomed to operating in an uncertain environment and that they have shown exceptional resilience under previous periods of severe stress.

In terms of asset risks and capital, Moody's indicated that the banks' high exposure to sovereign risk constitutes their main credit risk, as it links their creditworthiness to that of the Lebanese government. It said that the banking sector's aggregate exposure to the government and to the Central Bank reached \$86bn in March 2016, equivalent to 46% of total assets and to over five-times the banks' Tier-One capital. It noted that the banks' exposure to the government has been broadly stable between 2013 and 2015, but that their exposure to the Central Bank grew by 41% during the same period. It added that the Central Bank has taken a greater role in financing the government, as its holdings of government securities grew by 25% annually since 2013.

In parallel, it anticipated the banks' asset quality to moderately deteriorate over the coming 12 to 18 months, with most of the pressure coming from the banks' large exposure to the real estate sector and to retail lending. It projected the non-performing loans ratio to exceed 5% in 2016 and expected loan-loss provision expenses to be equivalent to about 1% to 1.5% of gross loans. Further, the agency anticipated the banking sector's capital level to be stable over the coming 12 to 18 months, supported by limited asset growth, profit retention and the full implementation of Basel III capital regulations. It forecast total shareholders' equity to be equivalent to 9% of the sector's assets at the end of 2016. It considered that the Lebanese banks' capital adequacy ratios are inflated, as the regulatory zero risk-weight that is applied to local currency-denominated securities understates the risk-weighted assets.

In terms of profitability and efficiency, Moody's expected the sector's profitability to come under pressure from elevated provisioning requirements, and as the decline in new business opportunities limits net interest income growth and fee income generation. It indicated that loan-loss provisioning costs remain elevated and have absorbed an estimated 13% of pre-provision income in 2015 compared to about 6% in 2010. It added that the slowdown in lending activity and the disruption of overland routes through Syria will continue to weigh on income from credit-servicing and trade-finance activity, which usually provide a significant share of the banks' fee and commission income.

In terms of funding and liquidity, Moody's pointed out that the banking sector benefits from solid liquidity buffers and deposit-based funding, which support the system's overall stability. It projected private sector deposit growth at about 5% in 2016, supported by remittance inflows from Lebanese expatriates. It noted that the banks' deposits have been resilient to previous crises and periods of high domestic instability.

### **Top five freight forwarders' import activity up 6% in first five months of 2016, exports up 17%**

Figures released by the Port of Beirut show that overall import shipping operations by the top five freight forwarders through the port reached 145,763 20-foot equivalent units (TEUs) in the first five months of 2016, constituting an increase of 6.1% from 137,392 TEUs in the same period of 2015. The five freight forwarders accounted for 88.2% of imports to the Lebanese market and for 61.4% of the total import freight forwarding market during the covered period. Mediterranean Shipping Company (MSC) handled 47,561 TEUs in imports in the first five months of 2016, equivalent to a 20% share of the total freight forwarding import market. Metz Group followed with 28,518 TEUs (12%), Merit Shipping with 27,603 TEUs (11.6%), Sealine Group with 24,953 TEUs (10.5%) and Gezairy Transport with 17,128 TEUs (7.2%). Further, Gezairy Transport registered a year-on-year increase of 45.4% in import shipping, the highest among the top five freight forwarders, while Sealine Group posted the only decline at 20.1%.

In parallel, export shipping operations by the top five freight forwarders through the Port of Beirut reached 33,517 TEUs in the first five months of 2016, constituting an increase of 16.7% from 28,728 TEUs in the same period of 2015. The five freight forwarders accounted for 98% of exported Lebanese cargo and for 14.2% of the total export freight forwarding market in the first five months of 2016. Merit Shipping handled 15,230 TEUs of freight in the covered period, equivalent to 44.5% of the Lebanese cargo export market. Sealine Group followed with 7,865 TEUs (23%), Metz Group with 6,827 TEUs (19.9%), MSC with 2,051 TEUs (6%) and Gezairy Transport with 1,544 TEUs (4.5%). Further, Merit Shipping registered the only year-on-year rise of 62.5% in export shipping among the top five freight forwarders, while Gezairy Transport posted the steepest decline at 8.7%.



## Ratio Highlights

(in % unless specified)	2013	2014	2015	Change*
Nominal GDP (\$bn)	47.2	49.4	50.9	
Public Debt in Foreign Currency / GDP	55.3	51.9	53.2	134
Public Debt in Local Currency / GDP	79.1	83.0	85.0	203
Gross Public Debt / GDP	134.4	134.8	138.2	337
Total Gross External Debt / GDP**	163.8	165.1	162.4	(270)
Trade Balance / GDP	(36.6)	(34.8)	(29.7)	512
Exports / Imports	18.5	16.2	16.6	41
Fiscal Revenues / GDP	19.9	22.0	18.8	(322)
Fiscal Expenditures / GDP	28.9	28.3	26.6	(167)
Fiscal Balance / GDP	(8.9)	(6.2)	(7.8)	(154)
Primary Balance / GDP	(0.5)	2.6	1.4	(122)
Gross Foreign Currency Reserves / M2	69.5	66.5	58.7	(780)
M3 / GDP	235.4	238.4	243.0	462
Commercial Banks Assets / GDP	349.0	355.9	365.6	968
Private Sector Deposits / GDP	288.4	292.6	298.0	540
Private Sector Loans / GDP	100.3	103.1	106.6	348
Private Sector Deposits Dollarization Rate	66.1	65.7	64.9	(83)
Private Sector Lending Dollarization Rate	76.5	75.6	74.8	(73)

\* Change in basis points 14/15

\*\*Includes portion of public debt owed to non-residents, liabilities to non-resident banks, non-resident deposits (estimated by the IMF), Bank for International Settlements' claims on Lebanese non-banks

Source: Association of Banks in Lebanon, Institute of International Finance, International Monetary Fund, World Bank, Byblos Research Estimates & Calculations  
Note: M2 includes money in circulation and deposits in LBP, M3 includes M2 plus Deposits in FC and bonds

## Risk Metrics

Lebanon	Oct 2014	Sep 2015	Oct 2015	Change**	Risk Level
Political Risk Rating	52.0	54.5	54.5	▼	High
Financial Risk Rating	38.0	39.0	39.0	▼	Low
Economic Risk Rating	27.0	33.0	33.0	▼	Moderate
Composite Risk Rating	58.5	63.25	63.25	▼	Moderate

MENA Average*	Oct 2014	Sep 2015	Oct 2015	Change**	Risk Level
Political Risk Rating	57.1	57.6	57.7	▼	High
Financial Risk Rating	40.6	39.2	39.3	▲	Low
Economic Risk Rating	35.6	31.3	31.2	▲	Moderate
Composite Risk Rating	66.6	64.0	64.1	▲	Moderate

\*excluding Lebanon

\*\*year-on-year change in risk

Source: The PRS Group, Byblos Research

Note: Political & Composite Risk Ratings range from 0 to 100 (where 100 indicates the lowest risk)

Financial & Economic Risk ratings range from 0 to 50 (where 50 indicates the lowest risk)

## Ratings & Outlook

Sovereign Ratings	Foreign Currency			Local Currency		
	LT	ST	Outlook	LT	ST	Outlook
Moody's	B2	NP	Negative	B2		Negative
Fitch Ratings	B-	B	Stable	B-		Stable
Standard & Poor's	B-	B	Negative	B-	B	Negative
Capital Intelligence	B	B	Negative	B	B	Negative

Source: Rating agencies

Banking Ratings	Banks' Financial Strength	Banking Sector Risk	Outlook
Moody's	E+		Negative



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