

LEBANON THIS WEEK

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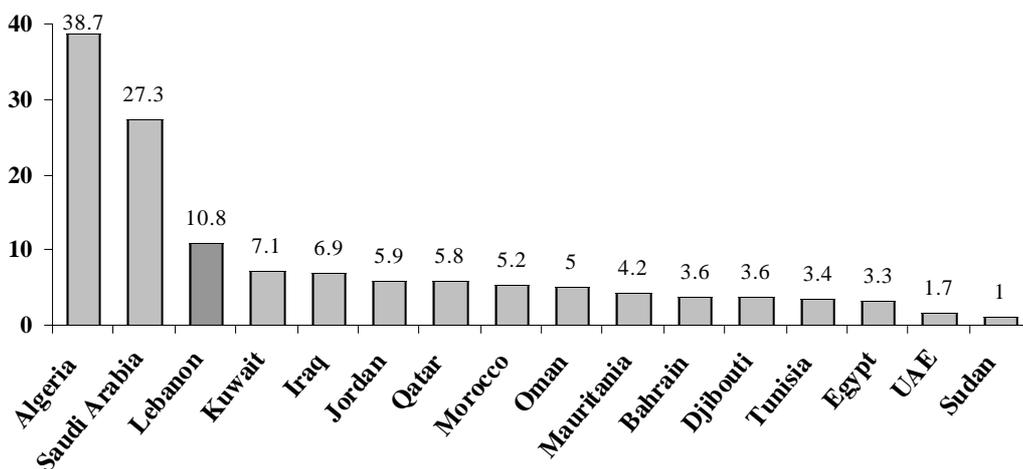
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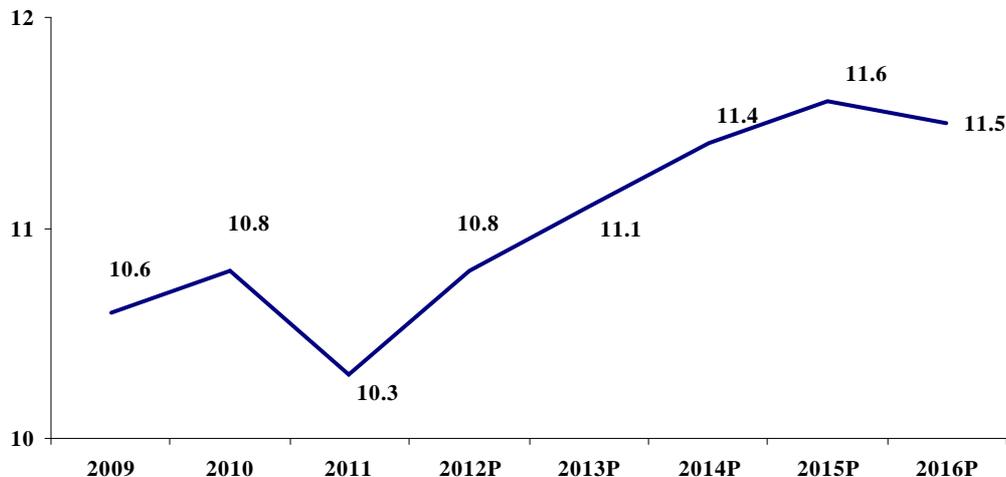
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Charts of the Week

Projected Foreign Currency Reserves at Arab Central Banks
(in months of next year's imports of goods & services)



Projected Foreign Currency Reserves at the Central Bank of Lebanon
(in months of next year's imports of goods & services)



Source: IMF, IIF, Credit Suisse, Byblos Research

Quote to Note

"The inclusion of these receipts in the budget figures is somewhat controversial, given that the actual cash does not reach the Ministry of Finance until the end of the year, and only after certain deductions have been made."

Citigroup, on the practice by the Finance Ministry to include estimates of telecom receipts in its monthly results even though they remain in the Telecom Ministry's account till the end of the year.

Number of the Week

87.2%: Urban population in Lebanon as a percentage of the total population, compared to the global average of 50.7%, according to the World Bank

Economic Indicators

| \$m (unless otherwise mentioned) | 2010 | Mar 11 | 2011 | Jan 12 | Feb 12 | Mar 12 | % Change* |
|---|-------------|---------------|-------------|---------------|---------------|---------------|------------------|
| Exports | 4,256 | 354 | 4,276 | 348 | 429 | 377 | 6.50 |
| Imports | 17,956 | 1,631 | 20,170 | 1,454 | 2,799 | 1,723 | 5.64 |
| Trade Balance | (13,700) | (1,277) | (15,894) | (1,106) | (2,370) | (1,346) | 5.40 |
| Balance of Payments | 3,326 | 270 | (1,996) | (290) | (134) | 51 | (81.11) |
| Checks Cleared in LBP | 13,519 | 1,301 | 14,251 | 1,246 | 1,152 | 1,192 | (8.38) |
| Checks Cleared in FC | 53,925 | 4,798 | 57,852 | 4,665 | 4,272 | 4,844 | 0.96 |
| Total Checks Cleared | 67,444 | 6,099 | 72,103 | 5,911 | 5,424 | 6,036 | (1.03) |
| Budget Deficit/Surplus | (2,894) | (548) | (2,342) | (176) | (181) | (312) | (42.99) |
| Primary Balance | 1,231 | (120) | 1,662 | 33 | 11 | 133 | (210.84) |
| Airport Passengers | 5,512,435 | 344,024 | 5,596,034 | 424,741 | 374,252 | 438,570 | 27.48 |

| \$bn (unless otherwise mentioned) | Dec 2010 | Mar 11 | Dec 11 | Jan 12 | Feb 12 | Mar 12 | % Change* |
|--|-----------------|---------------|---------------|---------------|---------------|---------------|------------------|
| BdL FX Reserves | 28.60 | 28.54 | 30.82 | 30.74 | 30.76 | 30.99 | 8.58 |
| <i>In months of Imports</i> | <i>19.46</i> | <i>17.40</i> | <i>18.51</i> | <i>21.14</i> | <i>10.99</i> | <i>17.99</i> | <i>3.37</i> |
| Public Debt | 52.59 | 52.59 | 53.64 | 53.65 | 53.94 | 54.08 | 2.83 |
| Net Public Debt | 45.01 | 45.61 | 46.35 | 46.54 | 46.74 | 46.91 | 2.85 |
| Bank Assets | 128.93 | 132.49 | 140.58 | 142.85 | 144.11 | 144.73 | 9.24 |
| Bank Deposits (Private Sector) | 107.20 | 108.15 | 115.72 | 116.69 | 117.42 | 118.22 | 9.31 |
| Bank Loans to Private Sector | 34.93 | 36.43 | 39.38 | 40.51 | 40.45 | 41.00 | 12.54 |
| Money Supply M2 | 39.40 | 37.14 | 38.90 | 39.09 | 39.46 | 40.04 | 7.81 |
| Money Supply M3 | 92.15 | 92.76 | 97.23 | 97.49 | 98.13 | 98.94 | 6.66 |
| LBP Lending Rate (%) | 7.91 | 7.73 | 7.38 | 7.19 | 7.07 | 7.16 | (57b.p.) |
| LBP Deposit Rate (%) | 5.68 | 5.63 | 5.63 | 5.60 | 5.47 | 5.46 | (17b.p.) |
| USD Lending Rate (%) | 6.74 | 7.24 | 7.02 | 6.99 | 7.13 | 7.06 | (18b.p.) |
| USD Deposit Rate (%) | 2.80 | 2.82 | 2.83 | 2.87 | 2.87 | 2.83 | 1b.p. |
| %* Change in CPI** | 6.19 | 6.94 | 4.27 | 4.47 | 3.71 | 4.40 | (254b.p.) |

* Year-on-Year; ** Consumer Price Index

Note: b.p. i.e. basis point

Sources: ABL, BdL

Capital Markets

| Most Traded Stocks on BSE | Last Price (\$) | % Change* | Total Volume | Weight in Market Capitalization |
|----------------------------------|------------------------|------------------|---------------------|--|
| Solidere "A" | 13.48 | 2.35 | 79,194 | 13.07% |
| Solidere "B" | 13.32 | 2.38 | 32,889 | 8.40% |
| Byblos Common | 1.48 | (1.33) | 56,907 | 5.16% |
| Byblos Pref. 08 | 100.00 | 0.00 | 250 | 1.94% |
| Byblos Pref. 09 | 100.30 | 0.00 | 3,084 | 1.95% |
| BLOM GDR | 7.75 | 0.65 | 351,076 | 5.55% |
| BLOM Listed | 7.40 | 0.00 | 0 | 15.43% |
| Audi GDR | 6.24 | 1.46 | 14 | 6.06% |
| Audi Listed | 5.70 | 0.71 | 51,020 | 19.32% |
| HOLCIM | 17.74 | 5.60 | 2,800 | 3.36% |

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

| Sovereign Eurobonds | Coupon % | Mid Price \$ | Mid Yield % |
|----------------------------|-----------------|---------------------|--------------------|
| Sep. 2012 | 7.750 | 100.13 | 2.32 |
| June 2013 | 8.625 | 104.00 | 5.55 |
| Apr. 2014 | 7.375 | 105.00 | 4.33 |
| Jan. 2015 | 5.875 | 103.00 | 4.54 |
| Apr. 2015 | 10.00 | 114.13 | 4.91 |
| Jan. 2016 | 8.500 | 112.00 | 5.16 |
| Mar. 2017 | 9.000 | 115.38 | 5.00 |
| Nov. 2018 | 5.150 | 99.75 | 4.58 |
| Apr. 2021 | 8.250 | 116.00 | 5.27 |
| Nov. 2026 | 6.600 | 101.00 | 5.83 |

Source: Byblos Bank Capital Markets

| | July 2-6 | June 25-29 | % Change | June 2012 | June 2011 | % Change |
|------------------------------|-----------------|-------------------|-----------------|------------------|------------------|-----------------|
| Total Shares Traded | 601,825 | 4,299,484 | (86.00) | 6,244,741 | 2,792,846 | 123.60 |
| Total Value Traded | \$5,253,187 | \$41,368,850 | (87.30) | \$60,044,046 | \$34,880,478 | 72.14 |
| Market Capitalization | \$10.31bn | \$10.07bn | 2.40 | \$10.07bn | \$11.33bn | (11.14) |

Source: Beirut Stock Exchange (BSE)



Lebanon ranks 92nd globally in FDI potential, net FDI inflows at \$2.3bn in 2011

Figures released by the United Nations Conference on Trade and Development (UNCTAD) show that foreign direct investment (FDI) in Lebanon totaled \$3.2bn in 2011, constituting a decrease of 25.2% from \$4.3bn in 2010. FDI inflows to Lebanon totaled \$4.8bn in 2009, \$4.3bn in 2008 and \$3.4bn in 2007. The UNCTAD indicated that flows to Lebanon were affected by the slowdown in the Lebanese real estate sector, which is the most important recipient of FDI, due to the adverse spillovers of both the global financial crisis and regional unrest.

Lebanon was the third largest recipient of FDI in nominal terms among 19 Arab countries, the sixth largest among the 22 economies of the MENA region, and the fourth largest in West Asia in 2011. Also net FDI inflows to Lebanon totaled \$2.3bn in 2011, making the country the third largest destination of net inflows in the Arab world.

Also, Lebanon posted the seventh steepest drop in FDI among Arab countries and in the MENA region last year. Lebanon was one of 10 Arab and MENA countries that saw a fall in FDI inflows in 2011. In comparison, FDI to Arab economies declined by 35.6% year-on-year, contracted by 11.4% to MENA countries and dropped by 16.3% to West Asia; while FDI to developing economies grew by 11% and global FDI rose by 16.5%. In parallel, Lebanon ranked in 10th place globally and was the only Arab economy among the top 10 worldwide on the Inward FDI Attraction Index, while it ranked in 92nd place globally and in 14th place in the Arab world on the Inward FDI Potential Index.

FDI inflows to Lebanon accounted for 8% of total FDI in Arab countries and for 4.4% of inflows to the MENA region in 2011, compared to 6.8% in the Arab world and 5.3% regionally in 2010. They also represented 6.6% of total flows to the 13 countries that form West Asia, 0.5% of FDI inflows to developing countries, and 0.2% of global foreign direct investment in 2011.

Further, FDI flows to Lebanon were equivalent to 8.2% of GDP in 2011, highest in the Arab world, and were equivalent to 26.7% of gross fixed capital formation, the highest such ratio in the region. In comparison, FDI flows as a percentage of gross fixed capital formation were equivalent to 9.1% in West Asian economies, 8.5% in developing economies and 9.2% on a global basis in 2011.

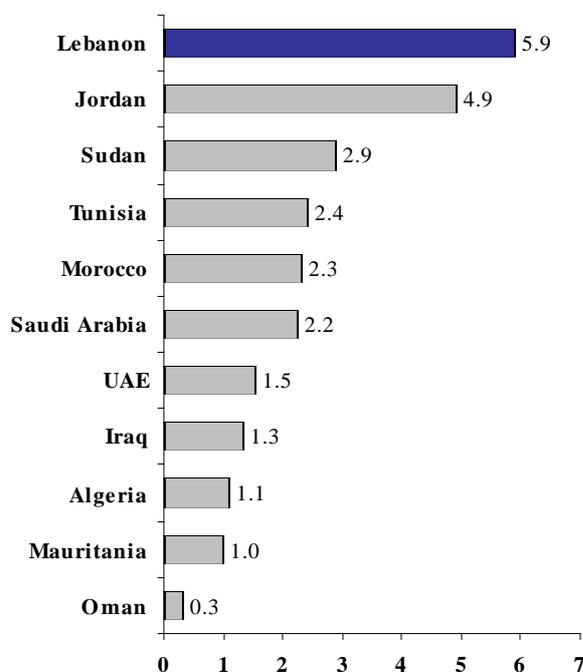
In addition, net cross-border M&A purchases in Lebanon reached \$834m in 2011 compared to a zero value of purchases in 2010, \$283m in 2009 and -\$233m in 2008, reflecting the differential between the acquisition price of companies abroad by Lebanon-based entities and the value of sales of foreign affiliates of locally-based entities. Lebanon was the source of four cross-border M&A purchases in 2011. Further, The UNCTAD did not record any net cross-border M&A sales in Lebanon in 2011, while such sales reached \$642m in 2010.

Further, there were eight Greenfield FDI projects in Lebanon in 2011 relative to 19 in 2010. In comparison, Lebanon was the source of 27 Greenfield FDI projects in 2011 relative to 31 projects in 2010. Global FDI reached \$1,524bn, while FDI inflows to developing economies totaled \$684.4bn in 2011.

| Foreign Direct Investment in Arab Countries (\$m) | | | |
|---|---------------|---------------|---------------|
| | 2011 | 2010 | Change (%) |
| Saudi Arabia | 16,400 | 28,105 | (41.6) |
| UAE | 7,679 | 5,500 | 39.6 |
| Lebanon | 3,200 | 4,280 | (25.2) |
| Algeria | 2,571 | 2,264 | 13.6 |
| Morocco | 2,519 | 1,574 | 60.1 |
| Sudan | 1,936 | 2,064 | (6.2) |
| Iraq | 1,617 | 1,396 | 15.8 |
| Jordan | 1,469 | 1,651 | (11) |
| Tunisia | 1,143 | 1,513 | (24.4) |
| Syria | 1,059 | 1,850 | (42.7) |
| Oman | 788 | 1,142 | (31) |
| Bahrain | 781 | 156 | 401 |
| Kuwait | 399 | 319 | 25.1 |
| Palestine | 214 | 180 | 18.8 |
| Djibouti | 78 | 27 | 191 |
| Mauritania | 45 | 131 | (65.4) |
| Qatar | (87) | 4,670 | - |
| Egypt | (483) | 6,386 | - |
| Yemen | (713) | (93) | - |
| Total | 40,615 | 63,112 | (35.6) |

Source: UNCTAD, Byblos Research

Net FDI inflows in 2011 (% of GDP)



Source: UNCTAD, Byblos Research

Lebanon ranks 61st globally, 9th among Arab countries in terms of innovation

INSEAD's Global Innovation Index (GII) for 2012 ranked Lebanon in 61st place among 141 countries around the world and in ninth place among 15 Arab countries. Lebanon also came in 18th place among 40 upper-middle income countries (UMICs) included in the survey. Lebanon ranked in 49th place globally among 125 countries in 2011, in fifth place among 15 Arab countries and in seventh place among 30 UMICs. The index measures innovation in a broad sense to include social and business innovations, as well as scientific innovation. It rates the innovation level of each country on a scale from zero to 100, with a score of 100 reflecting the most innovative economy. The index is a composite of 84 variables that are grouped in two sub-indices that are the Innovation Input Sub-Index and the Innovation Output Sub-Index. It covers an economy's institutions, human capital & research, infrastructure, market and business sophistication; as well as its knowledge & technology, and creative outputs. The countries included in the index represent 95% of the world's population and 99.4% of the world's GDP.

Globally, Lebanon ranked ahead of Macedonia, Ukraine and India, and came behind Brazil, Tunisia and Costa Rica. Regionally, it came ahead Morocco, Egypt and Algeria and ranked behind Tunisia, Jordan and Kuwait. It also ranked ahead of Macedonia and behind Costa Rica among UMICs. Lebanon received a score of 36.21 points, down 2.4% from 37.11 points in 2011, which constitutes the smallest decline among the seven Arab economies whose innovation level regressed year-on-year. Also, Lebanon's score came lower than the global average of 36.81 points, but is higher than the UMIC's average of 35.24 points, the MENA average of 34.24 points and the Arab average of 33.26 points.

Lebanon ranked ahead of Georgia, Tunisia and Serbia, and came behind Thailand, Russia and Kuwait on the Innovation Input Sub-Index. This category covers the elements of the national economy that enable innovative activities, such as institutions, human capital and research, infrastructure, market sophistication, and business sophistication. Regionally, Lebanon ranked ahead of Morocco, Jordan and Tunisia, and came behind Kuwait, Oman, and Saudi Arabia. It also ranked ahead of Serbia and behind Russia among UMICs.

Global Innovation Index 2012

| | Score | Arab Rank | Global Rank |
|----------------|--------------|-----------|-------------|
| Qatar | 47.74 | 1 | 26 |
| UAE | 41.99 | 2 | 34 |
| Jordan | 38.43 | 3 | 41 |
| Bahrain | 37.80 | 4 | 46 |
| Lebanon | 37.11 | 5 | 49 |
| Kuwait | 36.64 | 6 | 52 |
| Saudi Arabia | 36.44 | 7 | 54 |
| Oman | 35.51 | 8 | 57 |
| Tunisia | 33.89 | 9 | 66 |
| Egypt | 29.21 | 10 | 87 |
| Morocco | 28.73 | 11 | 94 |
| Syria | 24.82 | 12 | 115 |
| Yemen | 20.72 | 13 | 123 |
| Sudan | 20.36 | 14 | 124 |
| Algeria | 19.79 | 15 | 125 |

Source: INSEAD, Byblos Research

Components of the Global Innovation Index

| | Global Rank | Arab Rank | UMIC Rank | Lebanon Score | Global Ave Score | Arab Ave Score | UMIC Ave Score |
|--------------------------------|-------------|-----------|-----------|---------------|------------------|----------------|----------------|
| Innovation Input | 62 | 7 | 18 | 41.82 | 42.27 | 40.07 | 40.80 |
| Institutions | 75 | 9 | 25 | 53.90 | 58.07 | 54.80 | 55.57 |
| Human Capital & Research | 57 | 7 | 12 | 39.40 | 36.53 | 38.57 | 35.09 |
| Infrastructure | 72 | 9 | 27 | 33.50 | 35.76 | 34.39 | 35.15 |
| Market Sophistication | 90 | 7 | 28 | 34.00 | 40.41 | 34.05 | 38.80 |
| Business Sophistication | 33 | 3 | 4 | 48.30 | 40.60 | 38.53 | 39.37 |
| Innovation Output | 63 | 8 | 18 | 30.60 | 31.35 | 26.45 | 29.68 |
| Knowledge & Technology Outputs | 48 | 1 | 10 | 33.90 | 30.28 | 23.07 | 27.38 |
| Creative Outputs | 93 | 9 | 33 | 27.30 | 32.42 | 29.81 | 31.98 |

Source: INSEAD, Byblos Research

European Union supports innovation in manufacturing

The European Union and the Lebanese Center for Innovation and Technology launched the Innovation Voucher project with the aim of reinforcing the competitiveness of the Lebanese private sector and supporting the country's socio-economic development and economic growth. The project, which is funded by the European Union and the Industrial Research Institute, will promote technological innovation in the manufacturing industry. The project will grant up to €10,000 to at least 20 Lebanese small- and medium-sized enterprises for the purpose of research and innovation in their products and services. In parallel, the Italian government extended a €14m soft loan to the Council for Development & Reconstruction for the construction of two wastewater treatment plants and new sewage networks in the Keserwan region.

Sovereign risks higher than market perception, fiscal deficit to widen on extra-budgetary expenditures

Citigroup indicated that sovereign risks in Lebanon remain elevated, and that the risks are not fully reflected in the spreads on Lebanese sovereign bonds compared to other emerging markets with a similar credit risk profile. It attributed this trend to the strong liquidity in the domestic banking sector, which is the primary buyer of Lebanese Eurobonds. It pointed out that the performance of the Eurobonds was weak recently, with some bondholders selling their holding in the past few weeks. It considered that fears of spillovers of the Syrian crisis after the recent rise in violence in parts of the country, as well as the government's plan to issue \$2bn in government debt, may have caused the sell-off. It noted that the effect of these two factors is likely to subside in the coming weeks, which would lead to a reversal in the recent underperformance of the bonds. Also, it did not anticipate the bond issuance to be the start of a borrowing cycle by the government, and expected Eurobonds to become scarce again once the new issuance is absorbed by the highly liquid banking sector.

In parallel, Citigroup did not expect the revised 2012 draft budget to be ratified into law, especially with all the tax increases and new taxes that the Finance Ministry has proposed. It said these measures are facing strong resistance in light of their negative impact on the already fragile economy. But it did not anticipate the tax measures to be implemented given wide expectations that the budget is not going to be ratified anyway. It added that the Cabinet has requested Parliament's approval for \$7.6bn in extra-budgetary expenditures for 2012 to be financed through Treasury bills and loans. It said that the spending would be earmarked to cover budgets of state institutions until the end of the year, as well as development projects in Tripoli. However, it pointed out that the deal failed to gain parliamentary approval and that President Michel Suleiman could use his presidential privileges to sign it into law, a move he had previously resisted. Citigroup expected the rise in public expenditures to exceed the growth in revenues if the spending bill is approved, and forecast Lebanon's budget deficit to widen to 7.9% of GDP this year from 6.8% of GDP in 2011.

Political uncertainty and economic slowdown unlikely to affect currency stability and debt servicing

HSBC Bank revised marginally its real GDP growth forecast for Lebanon to 2.4% in 2012 from a previous estimate of 2.3%, and compared to growth of 3.7% for the Middle East & North Africa and of 2.4% for the region's non-oil producers. Lebanon's projected growth rate for 2012 would make it the third slowest economy among 14 countries in the MENA region, after Jordan at 2.1% and Egypt at 1.8%. It said that the conflict in Syria is imposing a heavy economic cost on Lebanon. It added that political uncertainty, perceived security risks, and warnings from GCC states for their nationals to avoid traveling to Lebanon will have an impact on tourism and the construction sector and, in turn, on economic growth. But it noted that this is unlikely to undermine Lebanon's ability to service its debt or maintain the stability of its currency, provided that there is no outflow of deposits from its liquid banking system. It pointed out that the Lebanese economy continues to outperform regional oil importers according to several indicators. It also expected the fiscal deficit to remain stable at 5.9% of GDP in 2012, mainly due to the drop in oil prices during the second quarter of the year.

In parallel, HSBC expected household consumption in Lebanon to grow by 3% in 2012, up from 2.7% in 2011. It said that Lebanon would post the eighth highest growth in household consumption in the region, tying with Morocco and Tunisia. Also, it expected Lebanon to post a gross saving ratio of 9.7% of GDP this year, up from 7.6% of GDP, but still the lowest such ratio in the region and relative to a ratio of 20% of GDP for non-oil producers in the region. It also projected Lebanon's total investment to decrease by 1% in 2012, relative to a contraction of 2% in 2011, and to post the steepest drop in the region. It forecast real private sector credit growth in Lebanon at 1.5% in 2012 relative to a growth rate of 9.8% in 2011 and compared to a contraction of 0.6% for the region's non-oil producers. Further, it forecast the Central Bank's reserves to reach 15.1 months of imports in 2012, down marginally from 15.3 months of imports in 2011, and to post the fourth highest level in the region behind Algeria at 36 months of imports, Saudi Arabia at 34.3 months of imports and Iraq at 21.7 months of imports.

Economic activity to slow down in coming quarters

Standard Chartered projected Lebanon's economic growth at 3.5% in 2012 relative to 1.5% in 2011, and considered that the main risk to the outlook relates to the possibility of further spillovers of the Syrian conflict into Lebanon. It said spreads on Lebanese Eurobonds and on five-year Credit Default Swaps have widened in recent weeks due to heightened regional political risks as well as increased market-wide risk aversion. It expected spreads to tighten once the overall risk environment improves. It added that the economy is rebounding based on indicators covering the first four months of the year, but cautioned that the figures are inflated due to a low base effect. However, it pointed out that the latest available data does not reflect the impact on the economy of the recent security deterioration in several parts of the country. It noted that the components of Lebanon's GDP are highly volatile and that trends can reverse abruptly. As such, it expected economic growth to slow down in the coming quarters.

In parallel, Standard Chartered said that the banking sector's deposit growth rate constitutes one of the key risk indicators. It pointed out the strong link between bank lending and bank deposits, and the stronger relationship between lending and economic activity. It added that these links highlight the significance of foreign deposit inflows for lending and economic activity. It said that the sector's private-sector deposits grew by 2.6% in the first four months of this year and by 8% year-on-year. In parallel, Standard Chartered projected the fiscal deficit at 7% of GDP this year relative to 7.5% of GDP last year. It forecast Lebanon's current account deficit to narrow to 16% of GDP in 2012 from 17.5% of GDP in 2011. It anticipated the inflation rate at 4.8% this year, relative to 5% in 2011.



Fitch affirms sovereign ratings at 'B', main risk to ratings is outflow of deposits

Fitch Ratings affirmed Lebanon's Long-term foreign and local currency Issuer Default Ratings (IDR) and Short-term foreign currency IDR at 'B', with a 'stable' outlook. It also affirmed the Country Ceiling at 'B'. The agency attributed its decision to the fact that Lebanon's substantial foreign exchange reserves, lower debt levels and reduced debt servicing costs relative to the previous decade, mitigate the downside risks to political stability, growth and public finances in 2012. It said the low ratings incorporate a degree of tolerance for political volatility, but it warned that they would come under negative pressure in case of internal strife or a spillover of tensions from Syria. It added that the economic impact of increased political tensions has been felt so far in lower growth, and expected economic activity to slow further this year given that the summer season will be adversely affected by travel advisories announced by a number of Gulf Cooperation Council (GCC) countries and that activity in the property sector has stagnated. It noted, however, that key financial variables such as foreign currency reserves and banking system deposits continue to rise.

Fitch considered that the primary risk to Lebanon's sovereign ratings consists of a sustained outflow of deposits that would reduce the banks' deposit base and the Central Bank's foreign currency reserves. It added that previous instances of deposit outflows were triggered by political instability and were temporary, and that deposits continue to grow currently. It noted that non-resident deposits grew by 15% last year growth due to attractive interest rate differentials and the formation of a new government in June. It added that overall bank deposits posted annual growth of 8% in April 2012 and non-resident deposits continue to increase at last year's pace.

In parallel, Fitch expected the fiscal deficit to exceed 9% of GDP and for the debt to stabilize at 135% of GDP in 2012, and for the debt ratio to remain broadly stable over the next two years. It noted that the debt level is the third-highest among all Fitch-rated sovereigns after Japan and Greece, despite its decline by 45% of GDP in the past five years. It added that the debt's sustainability remains supported by the size and depth of the local banking sector, which is the main holder of government securities. The agency indicated that the government has submitted an expansionary budget for this year that included a rise in wages and a marked increase in capital spending. It noted, however, that the draft budget is unlikely to be approved due to sharp political differences, just like in the previous six years. It added that, as a result, the deficit will widen, but not to the extent planned, as spending commitments will not be implemented.

Central Bank foreign assets up 9.2% to \$35.2bn in first half of 2012

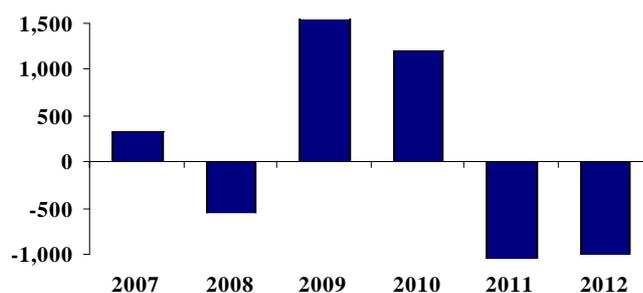
The Central Bank's interim balance sheet reached \$74.4bn at the end of June 2012 compared to \$70.3bn at the end of 2011 and to \$66.1bn at end-June 2011. Assets in foreign currencies increased by 9.2% in the first half of the year to \$35.2bn from \$32.2bn at the end of 2011. Assets in foreign currencies increased by \$2.29bn in June, \$615.5m in April, \$141.5m in March and by \$118.8m in February; while they declined by \$122.75m in May and by \$72.6m in January 2012. This resulted in an aggregate increase of nearly \$3bn in the first half of the year, with increases of \$187.6m in the first quarter and of \$2.79bn in the second quarter of 2012. Further, assets in foreign currencies rose by \$5.4bn, or 18%, year-on-year. The rise of foreign assets in June is due to the issuance by the Finance Ministry of three new Eurobonds totaling \$2bn that were used for early redemption and cancellation of Lebanese pound-denominated Treasury bills held by the Central Bank.

The value of the Central Bank's gold reserves increased by 0.6% in the first half of 2012 and by 4% year-on-year to \$14.5bn, compared to the peak of \$16.7bn reached at end-August 2011. Its securities portfolio dropped by 4.2% in the first half and by 1.3% annually to \$11.1bn. Further, deposits of the financial sector rose by \$3.5bn, or 7.2%, in the first half of the year and by \$7.3bn or 16.2% annually to \$52.5bn; while deposits of the public sector increased by 15.7% year-to-June and by 16% year-on-year to \$6.1bn. Assets in foreign currencies increased by \$1.6bn in 2011, \$2.3bn in 2010, \$8.3bn in 2009, and \$7.3bn in 2008.

Balance of payments posts deficit of \$998m in first five months of 2012

Central Bank figures show that Lebanon's balance of payments posted a deficit of \$997.7m in the first five months of 2012 compared to a deficit of \$1bn in the same period last year. The balance of payments posted a deficit of \$81.5m in May compared to a deficit of \$543m in April 2012 and a deficit of \$445.2m in May 2011. The May 2012 deficit was caused by a deficit of \$65m in the net foreign assets of banks and financial institutions and a deficit of \$16.2m in those of the Central Bank. The cumulative deficit over the first five months of 2012 was caused by a surplus of \$895.8m in the Central Bank's net foreign assets and a deficit of \$1.9bn in those of banks and financial institutions. The balance of payments posted a deficit of \$2bn in 2011 and surpluses of \$3.3bn in 2010, \$7.9bn in 2009 and \$3.5bn in 2008.

Balance of Payments* (US\$m)



* in the first five months of each year

Source: Central Bank of Lebanon

Net public debt at \$47bn at end-May 2012

Lebanon's gross public debt reached \$55.1bn at the end of May 2012, constituting a rise of 2.7% from the end of 2011 and an increase of 4.5% from end-May 2011. Domestic debt reached \$33.9bn at end-May, up by 3.8% from end-2011 and by 6.5% annually, while external debt stood at \$21.2bn, up by 1.1% from end-2011 and by 1.6% from a year earlier. Local currency debt accounted for 61.6% of gross public debt at end-May 2012 compared to 60.5% a year earlier, while foreign currency-denominated debt represented 38.4% of the total at the end of May relative to 39.5% a year earlier. The weighted interest rate on outstanding Treasury bills was 6.64%, while the weighted interest rate on Eurobonds was 6.98% at the end of May. Further, the weighted life on Eurobonds was 5.64 years, while that on Treasury bills was 943 days.

Commercial banks accounted for 48.3% of the local public debt at the end of May 2012 compared to 52.7% a year earlier. They were followed by the Central Bank with 36.1%, up from 31% at end-May 2011; while public agencies, financial institutions and the general public accounted for 15.6% of local debt compared to 16.4% in May 2011. Eurobond holders, foreign private sector loans and special T-bills in foreign currencies accounted for 88% of the external debt, followed by multilateral institutions with 6.3%, foreign governments with 4.8%, and Paris II loans with 0.9%. Net public debt, which excludes the public sector's deposits at the Central Bank and at commercial banks from overall debt figures, increased annually by 3.2% to \$47.2bn. In parallel, the gross market debt accounted for about 62% of total public debt. Gross market debt is the total public debt less the portfolios of the Central Bank, the National Social Security Fund, bilateral and multilateral loans, as well as Paris II and Paris III related debt.

Agriculture Ministry takes measures to support exports

The Ministry of Agriculture announced a series of measures to help Lebanese farmers export their products. It indicated that several agricultural exporters are shipping their products by sea. But it noted that each vessel does not carry less than 4,500 tons of goods, or around 200 containers, which necessitates coordination between exporters. As such, the ministries of agriculture and transportation, along with the Investment Development Authority of Lebanon (IDAL), launched a special operations room to assist exporters with maritime transport, and created a hotline service in order to facilitate their transactions. Further, it said that Lebanese Customs have stepped up their activities to prevent smuggling and the flooding of agricultural products into the Lebanese market, as they have banned the entry of agricultural trucks that do not meet local quality and packaging specifications. In parallel, the Agriculture Ministry agreed with IDAL to introduce amendments to the Agri Plus program, constituting the fourth amendment in six months to the program of subsidies to agricultural exporters. Also, the ministry encouraged farmers to increase their exports to Iraq, Libya, Egypt, and the Gulf Cooperation Council markets, especially in light of the unstable situation in Syria. Lebanon exports about 500,000 tons of vegetables and fruits per year and imports about 180,000 tons.

Corporate Highlights

Eight Lebanese banks among Top 1000 banks in the world, Byblos Bank posts highest Tier One-to-capital ratio

In its 2012 survey of the Top 1000 commercial banks in the world, *The Banker* magazine included eight Lebanese banks on the list, down from nine banks last year, none of which ranked among the top 25 banks in the Middle East. The rankings are based on Tier One capital at year-end 2011 as defined by the Basel Bank for International Settlements. *The Banker* said the definition is stricter than total shareholders' equity and covers only the core of a bank's strength, namely the shareholders' equity available to cover actual or potential losses.

Byblos Bank's Tier One capital reached \$1.42bn at the end of 2011. It ranked ahead of Parsian Bank in Iran and International Bancshares Corp in the U.S., and was preceded by Banco de Occidente in Colombia and China's Bank of Dalian. Byblos Bank's Tier One capital rose by 5.5% in 2011. As a result, Byblos Bank posted the highest rise in Tier One capital in 2011 among Lebanese banks whose Tier One capital exceeds \$1bn, and the third highest rise among the eight Lebanese banks included in the rankings.

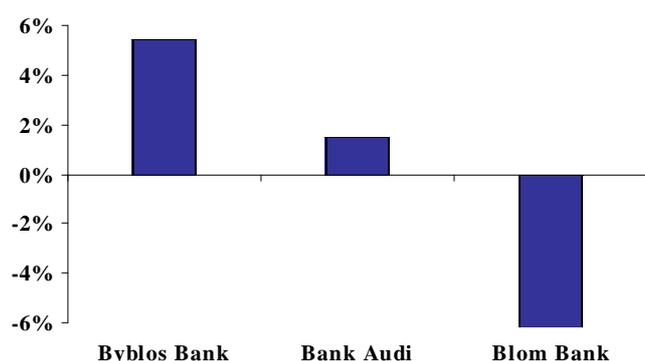
Further, Byblos Bank's Tier One capital-to-assets ratio reached 8.58% at end-2011, posting the highest such ratio among all Lebanese banks. It was followed BLOM Bank (7.39%), Banque Libano-Française (7.16%), Bank Audi (6.59%), Fransabank (6.2%), Bank of Beirut (6.15%), BankMed (6.07%), and Crédit Libanais (5.7%).

None of the Lebanese banks improved their ranking in the 2012 survey. Among the top three banks, BLOM Bank's rank regressed by 49 notches to 411th place and that of Bank Audi dropped by 33 places (288th), while Byblos Bank's rank declined by 22 spots to 470th place and posted the smallest year-on-year drop in the standings among the top 3 banks and the fourth lowest among the Lebanese banks included in the survey. Beyond the top 3 banks, Bank of Beirut fell by 120 spots to 753rd place and posted the worst decline among the eight banks, BankMed regressed by 22 notches (681st), Crédit Libanais decreased by 15 spots (874th), Fransabank fell by seven places (616th), and Banque Libano-Française dropped by two spots (674th).

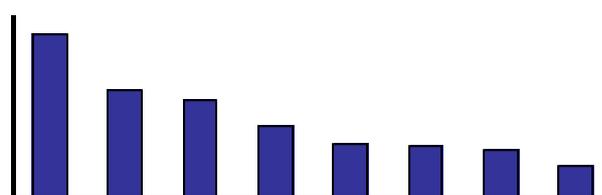
Overall, Fransabank's Tier One capital increased by 9.9% year-on-year, followed by Banque Libano-Française with a rise of 8.6%, Byblos Bank with a jump of 5.5%, Crédit Libanais with growth of 5.3%, BankMed with a 4.2% improvement, and Bank Audi with a rise of 1.5%. In contrast, BLOM Bank's Tier One capital contracted by 6.3% and that of Bank of Beirut fell by 19.6%.

The aggregate Tier One capital of the eight Lebanese banks totaled \$8.36bn at end-2011, constituting an increase of 1% from end-2010 and compared to a 5.7% rise in the Tier One capital of the Top 1000 banks. Further, the profits-to-Tier One capital ratio of the Lebanese banks reached 20.4% in 2011 compared to 12.2% for the Top 1000 banks. Lebanon had the 24th highest return on capital worldwide in 2011, as the return on capital of the eight Lebanese banks was 20.4% last year. The eight Lebanese banks accounted for 0.14% of the Tier One capital of the Top 1000 banks, for 0.11% of their total assets and for 0.24% of their aggregate pre-tax profits. They also accounted for 3.9% of the Tier One capital of the 93 Middle Eastern banks included in the Top 1000, for 5.6% of their total assets and for 5.2% of their aggregate pre-tax profits.

Rise in Tier One Capital of Top 3 Banks in 2011 (%)



Tier One Capital-to-Assets Ratio in 2011 (%)



Source: *The Banker* magazine, Byblos Research

Commercial banks' assets reach \$145bn at end-May 2012

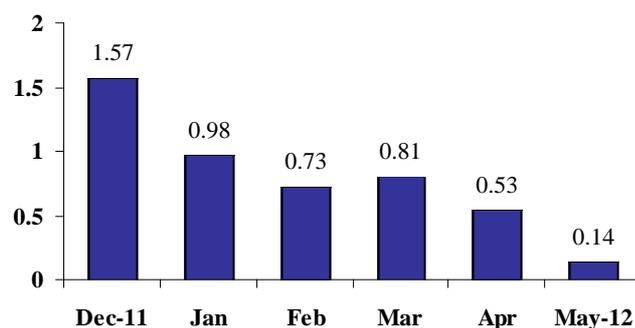
The consolidated balance sheet of commercial banks operating in Lebanon shows that total assets reached \$144.9bn at the end of May 2012, constituting an increase of 3.1% from end-2011 and a rise of 8.1% from end-May 2011. Private sector deposits totaled \$118.9bn, increasing by 2.8% from end-2011 and rising by 7.6% from a year earlier. Deposits in Lebanese pounds reached \$41.7bn, up by 5.8% from end-2011 and by 12.6% year-on-year; while deposits in foreign currencies totaled \$77.2bn, rising by 1.2% from end-2011 and by 5.1% from end-May 2011. Non-resident foreign currency deposits totaled \$18.6bn at end-May 2012, unchanged from end-2011, and grew by 9.2% from a year earlier. Total non-resident deposits reached \$21.6bn at end-May 2012 and grew by 1.7% from end-2011 and by 11.4% from a year earlier. Total private sector deposits increased by \$141m in May, \$533m in April, \$806m in March, \$725m in February and by \$976m in January 2012, compared to a rise of \$539m in May, \$1.8bn in April, \$1.3bn in March, \$673m in February and a decline of \$1.1bn in January 2011. In parallel, deposits of non-resident banks reached \$6.5bn in May, as they increased by 11.4% from end-2011 and by 4% year-on-year. The dollarization rate of deposits reached 64.9% at the end of May, down from 66.4% a year earlier. Further, the average deposit rate in Lebanese pounds reached 5.49% in May relative 5.64% a year earlier; while the same rate in US dollars was 2.83%, down from 2.84% in May 2011.

Loans to the private sector totaled \$41.9bn at end-May, constituting an increase of 6.4% from end-2011 and a rise of 11.9% from a year earlier. Lending to the resident private sector totaled \$35.9bn and increased by 4.8% from end-2011, while lending to the non-resident private sector reached \$6bn and rose by 17% from end-2011. The dollarization rate in private sector lending reached 78.3% in May compared to 79.8% a year earlier. The average lending rate in Lebanese pounds was 7.34% in May 2012 compared to 7.67% a year earlier, while the same average in US dollars was 7.12% compared to 7.04% in May 2011. In addition, claims on non-resident banks reached \$12.6bn at end-May, posting a decrease of 13.8% from end-2011. Claims on the public sector stood at \$29.2bn, up 2.9% year-on-year but down 0.2% from end-2011. The ratio of private sector loans-to-deposits in foreign currencies stood at 42.5%, well below the Central Bank's limit of 70%, and compared to 40.7% a year earlier. In parallel, the same ratio in Lebanese pounds was 21.7%, up from 20.4% a year earlier. The ratio of total private sector loans to deposits was 35.2% compared to 33.9% a year earlier. The banks' aggregate capital base stood at \$11.6bn, up by 11.1% from \$10.5bn in May 2011.

CMA CGM sells assets as part of restructuring plan

Lebanese-owned and France-based container shipping group CMA CGM sold its stake in French cruise shipping operation La Compagnie du Ponant to private equity firm Bridgepoint. The transaction is part of the group's restructuring plan. CMA CGM's founding family, the Saadé family, has a 50% stake and CMA CGM holds a 40% share in La Compagnie du Ponant. Last month, Standard & Poor's downgraded the long-term corporate credit rating of the CMA CGM to 'CCC+' from 'B-'. It also lowered to 'CCC-' from 'CCC' the company's €325m and \$475m worth of senior unsecured notes that mature in 2019 and 2017, respectively. It kept the company's ratings on CreditWatch with negative implications. It attributed the downgrades to the company's deteriorating liquidity position due to negative operating cash flow in the first quarter of 2012 and continued depletion of available cash. S&P expected CMA CGM's liquidity position to remain under strain over the coming months due to delays in corrective actions. It noted that the firm is unlikely to complete the amendments to its debt amortization profile and to its financial covenants by June 30, 2012; and could take longer than expected to receive \$250m from the issuance of redeemable bonds to the Turkish Yildirim Group.

Private Sector Deposit Change (\$bn)



Source: Association of Banks in Lebanon

Ratio Highlights

| (in % unless specified) | 2009 | 2010 | 2011 | Change* |
|-----------------------------------|--------|--------|--------|---------|
| Nominal GDP ⁽¹⁾ (\$bn) | 34.7 | 37.1 | 39.1 | |
| External Debt / GDP | 61.3 | 55.4 | 53.5 | (190) |
| Local Debt / GDP | 86.0 | 86.3 | 83.7 | (260) |
| Total Debt / GDP | 147.2 | 141.8 | 137.2 | (460) |
| Total External Debt / GDP | 176.1 | 167.0 | 163.2 | (380) |
| Trade Balance / GDP | (36.8) | (36.9) | (40.7) | (380) |
| Exports / Imports | 21.5 | 23.7 | 21.2 | (250) |
| Budget Revenues / GDP | 24.3 | 22.7 | 22.7 | (5) |
| Budget Expenditures / GDP | 32.8 | 30.6 | 27.2 | (342) |
| Budget Balance / GDP | (8.5) | (7.9) | (6.0) | 191 |
| Primary Balance / GDP | 3.1 | 3.2 | 4.3 | 105 |
| BdL FX Reserves / M2 | 74.0 | 77.1 | 78.8 | 172 |
| M3 / GDP | 236.5 | 248.4 | 248.7 | 30 |
| Bank Assets / GDP | 332.1 | 347.5 | 359.5 | 1,200 |
| Bank Deposits / GDP | 276.0 | 289.0 | 296.0 | 695 |
| Private Sector Loans / GDP | 81.8 | 94.2 | 100.7 | 650 |
| Dollarization of Deposits | 64.5 | 63.2 | 65.9 | 270 |
| Dollarization of Loans | 84.0 | 80.3 | 78.4 | (190) |

* Change in basis points 10/11

(1) Based on Ministry of Finance Estimations and the International Monetary Fund

Source: Association of Banks in Lebanon, Byblos Research Calculations

Note: M2 includes money in circulation and deposits in LBP, M3 includes M2 plus Deposits in FC and bonds

Risk Outlook

| Lebanon | Dec 2010 | Nov 2011 | Dec 2011 | Change* | Risk Level |
|-----------------------|----------|----------|----------|---------|------------|
| Political Risk Rating | 58.5 | 55.0 | 54.5 | ▼ | High |
| Financial Risk Rating | 28.5 | 35.0 | 35.0 | ▲ | Low |
| Economic Risk Rating | 32.5 | 34.0 | 34.0 | ▲ | Moderate |
| Composite Risk Rating | 59.7 | 62.0 | 61.7 | ▲ | Moderate |

| Regional Average | Dec 2010 | Nov 2011 | Dec 2011 | Change* | Risk Level |
|-----------------------|----------|----------|----------|---------|------------|
| Political Risk Rating | 64.5 | 60.2 | 60.6 | ▼ | Moderate |
| Financial Risk Rating | 42.2 | 42.3 | 42.2 | ↔ | Very Low |
| Economic Risk Rating | 38.0 | 36.2 | 36.6 | ▼ | Low |
| Composite Risk Rating | 72.3 | 69.3 | 69.7 | ▼ | Low |

*year-on-year

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 | B1 | NP | Stable | B2 | | Stable |
| Fitch Ratings | B | B | Stable | B | | Stable |
| Standard & Poor's | B | B | Negative | B | B | Negative |
| Capital Intelligence | B | B | Stable | B | B | Stable |

Source: Rating agencies

| Banking Ratings | Banks' Financial Strength | Banking Sector Risk | Outlook |
|-----------------|---------------------------|---------------------|----------|
| Moody's | E+ | | Negative |
| EIU | | B | Stable |

Source: Rating agencies



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