

LEBANON THIS WEEK

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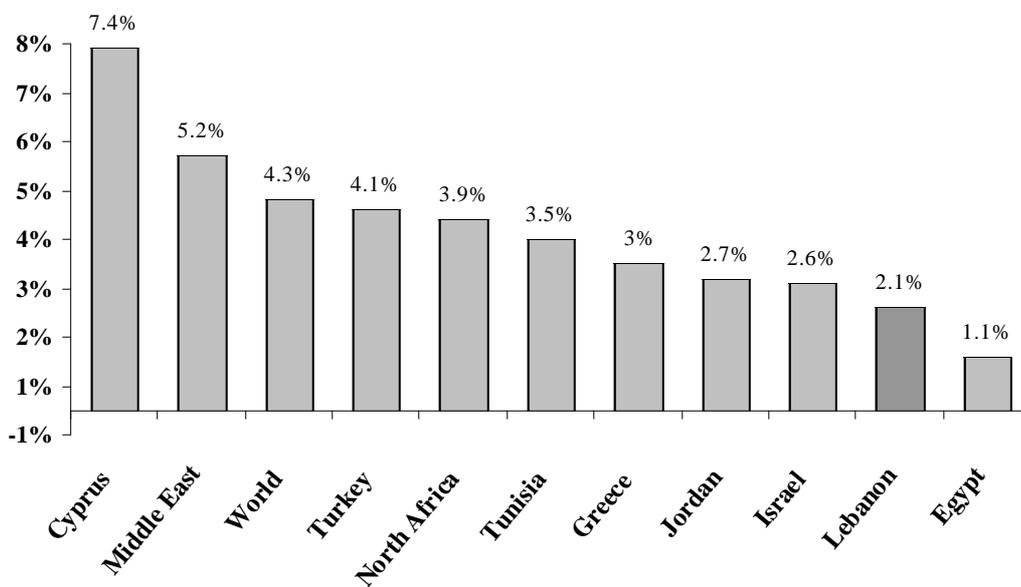
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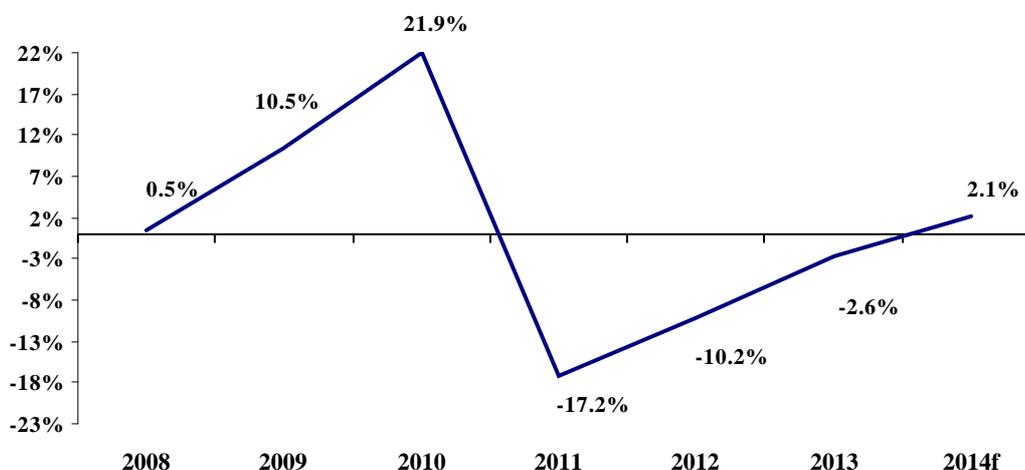
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Charts of the Week

Projected Travel & Tourism's Total Contribution to GDP in 2014 (% real growth)



Travel & Tourism's Total Contribution to GDP in Lebanon (% real growth)



Source: World Travel & Tourism Council, Byblos Bank

Quote to Note

"The banking system's solid liquidity buffers and depositor-based funding will continue to support stability over the outlook period."

Moody's Investors Service, on the stabilizing role of the Lebanese banking sector

Number of the Week

629: Number of medicines whose retail price will be reduced by an average of 20% starting on April 15, 2014, according to the Ministry of Health

Economic Indicators

| \$m (unless otherwise mentioned) | 2012 | Dec 12 | Sep 13 | Oct 13 | Nov 13 | Dec 13 | % Change* |
|---|-------------|---------------|---------------|---------------|---------------|---------------|------------------|
| Exports | 4,486 | 381 | 288 | 391 | 263 | 243 | (36.22) |
| Imports | 21,281 | 1,871 | 1,565 | 1,757 | 1,772 | 1,797 | (3.96) |
| Trade Balance | (16,795) | (1,490) | (1,277) | (1,366) | (1,509) | (1,554) | 4.30 |
| Balance of Payments | (1,538) | 312 | 504 | (794) | (192) | 534 | 71.15 |
| Checks Cleared in LBP | 14,976 | 1,337 | 1,473 | 1,516 | 1,451 | 1,562 | 16.83 |
| Checks Cleared in FC | 56,044 | 4,670 | 4,513 | 4,698 | 4,584 | 4,728 | 1.24 |
| Total Checks Cleared | 69,787 | 6,007 | 5,986 | 6,214 | 6,035 | 6,290 | 4.71 |
| Budget Deficit/Surplus | (3,925) | (132.36) | (668.16) | (228.92) | (126.15) | (137.58) | 3.94 |
| Primary Balance | (109.87) | 134.56 | (262.33) | 233.07 | 340.22 | 171.23 | 27.26 |
| Airport Passengers | 5,960,414 | 495,760 | 539,297 | 524,741 | 407,869 | 510,367 | 2.95 |

| \$bn (unless otherwise mentioned) | Dec 2012 | Dec 12 | Sep 13 | Oct 13 | Nov 13 | Dec 13 | % Change* |
|--|-----------------|---------------|---------------|---------------|---------------|---------------|------------------|
| BdL FX Reserves | 29.97 | 29.97 | 32.03 | 31.86 | 31.78 | 31.70 | 5.77 |
| <i>In months of Imports</i> | 16.02 | 16.02 | 20.47 | 18.13 | 17.93 | 17.64 | 10.13 |
| Public Debt | 57.69 | 57.69 | 62.39 | 62.44 | 63.26 | 63.46 | 10.01 |
| Net Public Debt | 49.12 | 49.12 | 52.15 | 52.50 | 52.75 | 53.18 | 8.28 |
| Bank Assets | 151.88 | 151.88 | 159.26 | 160.63 | 161.92 | 164.82 | 8.52 |
| Bank Deposits (Private Sector) | 124.99 | 124.99 | 131.26 | 132.10 | 133.15 | 136.21 | 8.97 |
| Bank Loans to Private Sector | 43.45 | 43.45 | 45.88 | 46.50 | 46.81 | 47.38 | 9.05 |
| Money Supply M2 | 43.17 | 43.17 | 44.49 | 44.72 | 45.05 | 45.60 | 5.63 |
| Money Supply M3 | 104.01 | 104.01 | 108.49 | 109.02 | 109.34 | 111.16 | 6.87 |
| LBP Lending Rate (%) | 7.07 | 7.07 | 7.36 | 7.59 | 7.01 | 7.29 | 22b.p |
| LBP Deposit Rate (%) | 5.41 | 5.41 | 5.37 | 5.44 | 5.47 | 5.44 | 3b.p |
| USD Lending Rate (%) | 6.87 | 6.87 | 6.95 | 6.85 | 6.88 | 6.88 | 1b.p |
| USD Deposit Rate (%) | 2.86 | 2.86 | 2.91 | 2.94 | 2.97 | 2.95 | 9b.p |
| %* Change in CPI** | 4.68 | 4.68 | 4.81 | 5.04 | 4.96 | 3.89 | (79b.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" | 12.89 | (1.15) | 44,946 | 11.50% |
| Solidere "B" | 12.76 | (2.22) | 17,712 | 7.40% |
| Byblos Common | 1.70 | 1.80 | 1,120,602 | 5.45% |
| Byblos Pref. 08 | 101.50 | 0.00 | 0 | 1.81% |
| Byblos Pref. 09 | 103.10 | 0.00 | 0 | 1.84% |
| BLOM GDR | 9.20 | 0.00 | 0 | 6.07% |
| BLOM Listed | 9.05 | 0.56 | 1,500 | 17.36% |
| Audi GDR | 6.45 | 0.78 | 3,000 | 5.90% |
| Audi Listed | 6.41 | 0.00 | 274,770 | 20.00% |
| HOLCIM | 14.50 | 0.00 | 0 | 2.52% |

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

| Sovereign Eurobonds | Coupon % | Mid Price \$ | Mid Yield % |
|----------------------------|-----------------|---------------------|--------------------|
| Apr. 2014 | 7.375 | 100.20 | 1.34 |
| Jan. 2015 | 5.875 | 101.94 | 3.35 |
| Apr. 2015 | 10.000 | 107.25 | 3.03 |
| Jan. 2016 | 8.500 | 107.75 | 3.99 |
| Mar. 2017 | 9.000 | 112.00 | 4.62 |
| Nov. 2018 | 5.150 | 100.00 | 5.15 |
| Apr. 2021 | 8.250 | 113.00 | 5.96 |
| Nov. 2026 | 6.600 | 100.25 | 6.57 |

Source: Byblos Bank Capital Markets

| | Mar 24-28 | Mar 17-21 | % Change | Feb 2014 | Feb 2013 | % Change |
|------------------------------|------------------|------------------|-----------------|-----------------|-----------------|-----------------|
| Total Shares Traded | 1,485,282 | 4,276,599 | (65.27) | 6,037,763 | 1,491,134 | 304.91 |
| Total Value Traded | \$4,913,405 | \$26,612,700 | (81.54) | \$43,140,999 | \$12,994,109 | 232.0 |
| Market Capitalization | \$11.21bn | \$11.21bn | (0.01) | \$11.30bn | \$10.94bn | 3.30 |

Source: Beirut Stock Exchange (BSE)



Beirut ranks 43rd globally in house prices and 55th in rental yield, property remains overvalued

The Global Property Guide's annual report on real estate investment trends around the world indicated that Beirut ranked in 43rd place among 94 markets globally in 2013 and in second place in the Arab world in terms of the price of a 150 square meter (sqm) apartment. The average price of a 150sqm apartment in Beirut was \$3,693 per sqm, higher than prices in the Bahamas, in Antigua and in Saint Kitts, and lower than those in Kiev in Ukraine, in Sao Paulo in Brazil and in Malta's Valletta. When excluding microstates and small islands, Beirut ranks in 36th place with an average price higher than in Ljubljana in Slovenia, in Bangkok and in Bucharest. The Guide noted that property demand in Beirut, especially from foreigners and non-residents, has fallen sharply due to domestic political tensions and regional unrest.

The report offers the tools needed by foreign and non-resident investors to buy income-generating property overseas. It said that only resale apartments and houses are included in the survey. The properties surveyed have to be in excellent condition, have good facilities, and have been refurbished or redecorated within the past five years. The Global Property Guide's valuation data is based on upper-end apartments in prestigious areas that appeal to foreign investors or renters. It said that figures for Beirut cover the areas of Achrafieh, Ain El Mreisseh, Ain El Tineh, Clemenceau, Hamra, Manara, Raouche, Sanayeh, the Beirut Central District, Ramlet El Baida, Verdun and Saifi.

Beirut ranked in 55th place in 2013 among 84 markets globally and in last place among five Arab markets in terms of Gross Rental Yield (GRY), which is the annual rent relative to the house price. Beirut would have the 50th highest GRY globally when excluding microstates and small islands. The survey said the GRY is the return-on-investment before taxes, maintenance fees and other costs, and is a key figure for investors. Globally, Beirut's GRY was higher than that in Serbia, in Berlin and in Brussels, and lower than that in Sophia in Bulgaria, in Kuala Lumpur and in Sydney. Beirut's GRY was 4.51% in 2013, significantly lower than the Arab average of 6.86%. The survey upgraded Lebanon's GRY to the 'poor' category in 2013 from the 'very poor' category in 2012. It was the only Arab market in this category.

Further, Beirut ranked in 30th place among 84 markets globally and in first place in the region in terms of the price of an apartment relative to its rent, or the Price-to-Rent ratio. Beirut's Price-to-Rent ratio would be the 26th highest globally when excluding microstates and small islands. The ratio reflects the years of rent that are required to recover the cost of buying a property, and is typically used for measuring the undervaluation or overvaluation of real estate prices. Globally, Beirut had the same ratio as Sydney and Kuala Lumpur, had a higher ratio than Sophia, Sao Paulo and Bermuda, and a lower ratio than New York City, Lisbon and Brussels. Lebanon's Price-to-Rent ratio was 22 times, higher than the Arab average of 15.8 times, and indicating that it takes 22 years of rent to recover the purchase price of a 150sqm apartment in Beirut.

Also, Beirut ranked in 30th place among 84 markets globally and in second place among five Arab markets in terms of the Rent-per-Month of a 150sqm apartment. Beirut would rank in 25th place globally on this indicator when excluding microstates and small islands. Globally, monthly rents in Beirut were more expensive than in Bangkok, in Buenos Aires and in Mexico City, and were less costly than in the Philippines' Metro Manila area, in Warsaw, and in Cape Town in South Africa. Beirut's rent-per-month was \$2,082 for a 150sqm apartment compared to the Arab average of \$1,715 per month.

Further, Lebanon ranked in fourth place among nine Arab markets in terms of Round-trip Transaction Cost, which reflects all costs of buying and reselling a residential property, expressed as a percentage of the property value. Such costs include registration costs, real estate agents' commissions, legal fees and sales and transfer taxes. Roundtrip transaction costs in Lebanon reached 11.57% compared to the regional average of 8.1%. The cost of buying a property in Lebanon was lower than that in Jordan (12.9%), Egypt (12.3%) and Morocco (12.1%), but came higher than that in the UAE (9%), Tunisia (7.1%), Bahrain (5%), Oman (3%) and Qatar (zero).

Finally, Lebanon ranked in second place among five Arab countries in terms of the cost of a typical upscale housing unit of 100sqm relative to the country's GDP per capita, or the house Price-to-Income ratio. The price of a 100sqm upscale apartment in Lebanon is equivalent to 35.26 times the country's GDP per capita, which is higher than in Egypt (28.44 times), Jordan (28.23 times) and the UAE (7.56 times), and is only lower than in Morocco at 63.73 times. In comparison, the region's average house Price-to-Income ratio is 32.64 times.

| City | Gross Rental Yield (%) | Price-to-Rent ratio | Buying Price* US\$/sqm | Rent* US\$/month | Roundtrip Cost (%) |
|---------------|------------------------|---------------------|------------------------|------------------|--------------------|
| Cairo | 9.40 | 11 | 831 | 977 | 12.30 |
| Amman | 8.53 | 12 | 1,282 | 1,367 | 12.94 |
| Marrakesh | 6.04 | 17 | 2,015 | 1,217 | 12.13 |
| Dubai | 5.82 | 17 | 5,037 | 2,932 | 9.01 |
| Beirut | 4.51 | 22 | 3,693 | 2,082 | 11.57 |

**150sqm apartment*

Source: Global Property Guide, Byblos Research



Multiple Cabinet changes would prevent economic and fiscal reforms

Barclays Capital projected Lebanon's real GDP growth at 1.5% in 2014, similar to its estimated growth rates for 2012 and 2013. It attributed its forecast to the uncertain domestic political outlook and to the deteriorating situation in Syria, which continue to weigh on Lebanon's economic activity. It said that growth dynamics are not likely to improve significantly this year, as the expected multiple changes in Cabinets would prevent the implementation of reforms that aim to stimulate growth. It noted that the successful election of a President by the constitutional deadline of May 25, 2014 would lead to the formation of a new Cabinet, whose term will end after the Parliamentary elections that are scheduled for November 2014. As such, it considered that the uncertain outlook at the institutional level would leave the current and incoming governments with limited opportunities to improve economic conditions this year. It pointed out that either the Lebanese Parliament would elect a new president by the constitutional deadline, or the country will face a vacuum at the presidential level, similar to that seen in 2007.

In parallel, it considered that the expected multiple Cabinet changes would delay fiscal reforms, which would worsen the public debt's dynamics. It forecast the fiscal deficit to widen to 10.5% of GDP in 2014 from 9.3% of GDP in 2013, as the stagnation in economic activity would weaken revenue generation and as the rising number of Syrian refugees would continue to weigh on public spending. It said that the government would continue to rely on the banking sector to finance its estimated \$4.8bn fiscal deficit for 2014 and to rollover maturing Eurobonds. It projected the public debt level to rise to 154% of GDP in 2014 from 146% of GDP in 2013.

Surveyed economists expect real GDP growth at 2% in 2014

Bloomberg's survey of economists and analysts about the outlook on the Lebanese economy indicates that real GDP growth is expected to reach 2% on average in 2014, and to rise to 3% in 2015 and 3.6% in 2016. The individual forecasts of growth rates for 2014 ranged between 0.9% and 2.6%. The consensus forecast among 60% of participants is that real GDP would grow by 2% or above this year. The survey's results displayed a median real GDP growth figure of 2.1% for this year. The survey's results are based on the opinions of 10 economists and analysts based in Lebanon and abroad. Bloomberg conducted the poll during the March 16-19, 2014 period and will update it on a quarterly basis.

Also, participants forecast Lebanon's inflation rate at 3.8% on average for 2014, and to reach 4.2% in 2015 and 3.3% in 2016. The opinions of polled economists differed drastically on the direction of consumer prices in 2014 with expectations ranging between 1.7% and 7.5%; while 80% of participants agreed that the inflation rate will come between 3% and 4% this year. The poll's results revealed a median inflation rate of 3.6% for 2014.

In addition, surveyed economists forecast Lebanon's fiscal deficit at 10.4% of GDP on average this year, and to narrow to 10.3% of GDP in 2015 and 9.1% of GDP in 2016. All participants expected the fiscal deficit to remain above 9% of GDP this year, with opinions ranging between deficits of 9.2% of GDP and 14% of GDP. Also, half of participants projected a double-digit fiscal deficit and the other half expected a deficit between 9.2% of GDP and 9.5% of GDP in 2014. The median for the fiscal deficit came at 9.8% of GDP for this year.

Further, polled economists projected the current account deficit at 9.9% of GDP, on average, this year and to reach 8.7% of GDP in 2015 and 9.1% of GDP in 2016. Also, one-third of those polled expect the current account deficit to be in double-digits in 2014, with expectations ranging from deficits of 5.3% of GDP to 16.7% of GDP this year. The poll's results show that the median current account deficit would be 8.5% of GDP in 2014.

In parallel, respondents assigned an average probability of 33% for Lebanon to enter a recession in the next 12 months. The opinions of four surveyed economists differed significantly with probabilities ranging between a low of 10% and a high of 50%. The poll's results indicated a median recession probability of 35% for 2014.

Coincident Indicator continues to reflect economic stagnation

The Central Bank's Coincident Indicator, an index of economic activity in Lebanon, reached 280.3 points in January 2014 compared to 267.9 in December 2013 and 263.9 in January 2013. The Coincident Indicator, an average of 8 weighted economic indicators, rose by 4.6% month-on-month and by 6.2% year-on-year in January 2014. The indicator averaged 266.1 in the 12 months ending January 2014, compared to 264.7 in the 12 months ending December 2013 and 257.7 in the 12 months ending January 2013. As a result, the average coincident indicator rose by 0.5% month-on-month and by 3.2% year-on-year, which continues to reflect economic slowdown. In parallel, the indicator improved 11 times and regressed 10 times in the month of January since 1993. It averaged 264.7 points in 2013, 256.6 in 2012, 255.7 in 2011, 249.5 in 2010 and 225.9 in 2009.

Central Bank lifts secrecy on 17 cases suspected of money laundering

The Special Investigation Commission (SIC) against money laundering and terrorism financing issued its 13th annual report detailing its activities in tracing dirty money in Lebanon in 2013. Established by the Central Bank of Lebanon as an independent legal entity, the commission's mandate is to investigate suspected money-laundering operations and monitor compliance with the rules and procedures of Law 318, an anti-money laundering law passed in April 2001 by the Lebanese Parliament.

The report indicated that the SIC received 301 suspected cases in 2013, of which 189 cases, or 62.8%, were local cases and 112 cases, or 37.2%, were referred from abroad. The SIC referred 137 suspected cases to the judicial authorities, while 46 cases are still pending and the remaining 118 cases did not fall within the framework of Law 318. As a result, authorities lifted the banking secrecy on 17 cases, of which one case was referred from foreign governments and organizations and 16 cases from domestic sources. The SIC investigated a total of 191 out of 284 cases in 2012, 285 out of 335 cases in 2011, 189 out of 245 cases in 2010, 77 out of 202 suspected cases in 2009, 67 out of 226 cases in 2008, 54 out of 234 cases in 2007 and 70 out of 185 cases in 2006. Counterfeiting and forgery accounted for 14.5% of reported cases, followed by embezzlement of private funds with 7.9%, terrorism & transfer of funds with 6.2%, embezzlement of public funds with 5%, organized crimes with 2.5% and narcotics trade with 2.1%, while the remaining 61.8% of cases were not categorized. In cases related to terrorism, local sources provided five names (three cases), the United Nations supplied 11 names (eight cases), and financial investigative units provided 36 names (four cases). Further, Europe was the main source of requests to Lebanese authorities, as it accounted for 53.8% of total requests of assistance, followed by North America (13.8%), the Middle East & the Arabian Gulf (9.2%), the United Nations (7.7%), Africa (6.2%), Asia (3.8%), Latin America (3.2%) and Australia (2.3%).

Also, the SIC examined a number of institutions to ensure their compliance with Law 318. It covered 205 money dealers, equivalent to 58.6% of total reporting money dealers in Lebanon, 21 financial institutions (38.2%), 27 banks (37%), three brokerage firms (25%) and 12 insurance companies (23.1%).

Telecom Minister announces reform measures

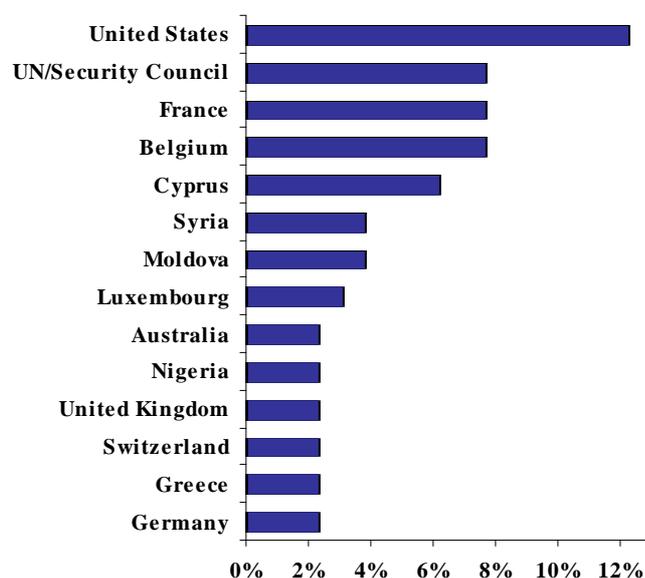
Telecommunications Minister Boutros Harb launched a series of initiatives to reform the telecom sector. He intends to implement the reforms within the coming two months, or before the end of the current Cabinet's mandate.

First, he aims to reduce the rates charged on international phone calls by up to 50%, as well as to reactivate the sale and use of prepaid cards, such as 'Telecards' and 'Kalam', and to reduce their prices by 30% to 50%. In addition, he intends to cancel the LBP50,000 (\$33.2) fixed fee for newly-installed landlines and to reduce the fixed monthly fee paid on landlines from LBP12,000 (\$8) to LBP8,000 (\$5.3). Also, he will study a plan that would offer Internet subscribers the option to enroll in an unlimited usage plan. Further, he said that the Telecom ministry will release the telecom revenues owed to municipalities. The revenues include LBP257bn (\$170.4m) from the mobile phone network for the 2010-13 period, and LBP65bn (\$43.1m) from landline receipts from the second, third and fourth quarters of 2013. He pointed out that the funds would benefit 900 municipalities across Lebanon.

Second, the minister aims to expand Internet access and DSL services to remote areas and to raise the speed of the service. Also, he intends to introduce a credit card payment system for bill settlements. Minister Harb indicated that Law 431, which aims to liberalize the telecom sector, has not been applied in previous years and affirmed that he intends to implement it.

In parallel, the Ministry of Telecommunications plans to extend the management contracts of Orascom Telecom and Zain, which operate the state-owned mobile phone networks Mobile Interim Company 1 (MIC 1) and Mobile Interim Company 1 (MIC 2), respectively, until the end of June 2014. The decision would constitute the sixth contract extension since early 2013. It indicated that it successfully negotiated an agreement with the two companies to reduce their operating fees by around \$5.5m in the next three months, while it also saved the Treasury an additional \$5.5m in the first quarter of the year. As such, savings to the Treasury are estimated at \$11m in the first half of 2014.

Main Sources of Foreign Request of Assistance*



*% of total foreign requests

Source: Special Investigation Commission, Byblos Research

Primary deficit widens to 0.5% of GDP in 2013

Figures released by the Ministry of Finance show that the fiscal deficit widened to 9.3% of GDP in 2013 from 9.1% of GDP in 2012. The fiscal deficit widened by 7.5% last year due to a 2.4% increase in spending and almost flat overall revenues. Aggregate public spending was equivalent to 30.2% of GDP in 2013 compared to 31% of GDP in 2012; while total public revenues were equivalent to 20.8% of GDP last year relative to 21.9% of GDP in 2012. Also, the primary budget deficit widened from 0.3% of GDP in 2012 to 0.5% of GDP in 2013, constituting the second consecutive annual deficit. The deterioration in Lebanon's public finances continued to reverse the public debt dynamics, as the debt level increased from 134.3% of GDP in 2012 to 140.5% of GDP in 2013, constituting the second consecutive annual increase. On the revenues side, tax receipts regressed from the equivalent of 15.7% of GDP in 2012 to 14.9% of GDP in 2013; while non-tax revenues declined from 5.1% of GDP to 4.8% of GDP in 2013. Also, Treasury receipts rose marginally from 1.1% of GDP in 2012 to 1.2% of GDP in 2013. On the spending side, current expenditures fell from the equivalent of 27.4% of GDP in 2012 to 26.4% of GDP in 2013; Treasury spending remained almost unchanged at 2% of GDP; and capital outlays increased from 1.2% of GDP in 2012 to 1.4% of GDP in 2013.

In parallel, current expenditures increased by 1.2% to \$11.9bn in 2013, Treasury spending rose by 2% to \$882.9m, capital outlays grew by 30% to \$654.7m, and budget advances rose by 7.8% to \$154.6m. Excluding debt servicing, current expenditures fell by \$23.9m, or by a marginal 0.3%, to \$7.9bn during 2013. The decrease mainly reflects a \$233.5m fall in transfers to Electricité du Liban (EdL), a \$165.8m decline in personnel cost and a \$57.7m drop in transfers to the Higher Relief Council (HRC). The decline was partly offset by a \$100.2m increase in materials & supplies, a \$99.5m rise in transfers to the National Social Security Fund, a \$65m expansion of other current spending, a \$45.8m increase in contributions to the non-public sector and a \$38.5m transfer to the Special Tribunal for Lebanon. Overall, salaries & wages decreased by 3% to \$2.8bn, transfers to EdL fell by 10.3% to \$2bn, retirement & end-of-service compensations dropped by 4.5% to \$1.2bn, and transfers to the HRC regressed by 44.8% to \$71.6m.

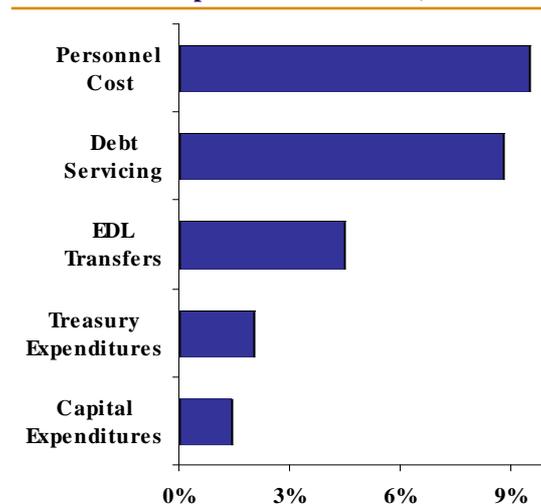
Further, capital expenditures grew by \$150.6m as payments for the maintenance of roads increased by \$78.3m and those to the Council for Development & Reconstruction rose by \$70.3m. Also, the distribution of Treasury spending shows that municipalities represented 44.4% of the total, followed by VAT refunds (22.6%), payments to public entities (12%) and guarantees (7%). Treasury spending rose by \$17.9m mainly due to a \$41.1m, or 26% rise in VAT refunds, a \$35.2m (50%) growth in payments to public entities and to a \$23.9m (63.8%) increase in guarantees, that were partly offset by a \$51.7m or 11.7% fall in payments to municipalities.

Public-sector salaries and benefits down 3% in 2013

Figures issued by the Ministry of Finance show that salaries, wages and related benefits paid to public-sector employees totaled \$2.8bn in 2013, constituting a decrease of 3% from 2012. They represented the largest component of total primary spending and accounted for 29.4% of such expenditures in 2013 compared to 30.8% in 2012. The figures include basic salaries, indemnities, 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 Parliament employees. The payments exclude retirement and end-of-service indemnities as well as salaries, wages and benefits of employees at public institutions. Salaries and benefits of military personnel reached \$1.7bn and accounted for 61.3% of the total, followed by educational personnel with \$622.9m (22%), civil staff with \$446.4m (15.7%), and customs employees with \$29.2m (1%). The distribution of military personnel salaries and benefits shows that the Lebanese Army's salaries totaled \$1.1bn in 2013 and represented 63.5% of the military personnel's salaries and benefits. They were followed by salaries of the Internal Security Forces with \$506.8m (29.2%), General Security Forces with \$94.9m (5.5%), and State Security Forces with \$32.5m (1.9%).

The ministry attributed the decrease in salaries, wages and related benefits paid to public-sector employees to a decrease of \$84m, or 2.6%, in basic salaries that reached \$2.1bn. The breakdown of basic salaries shows a decline of \$76m in outlays to educational personnel, an increase of \$26m in payments to military personnel, and a decrease of \$34m in payments to civil personnel. Also, indemnities rose by 11.3% to \$150.6m year-on-year; while allowances declined by 2.4% annually to \$384.7m and other expenses, mainly composed of payments to employees of the Civil Servants Cooperative, fell by 16.2% year-on-year to \$165.2m.

Main Public Expenditures in 2013 (% of GDP)



Source: Ministry of Finance, Byblos Research

Central Bank launches modernization plan

The Central Bank of Lebanon launched a comprehensive modernization plan that aims to develop a new generation of banking services that include programs and initiatives relevant to financial institutions. The plan coincides with the launch of other programs at the Banking Control Commission, the Special Investigation Commission and the Capital Markets Authority. The implementation of the modernization plan is expected to take about two years and would allow the Central Bank and governing bodies to implement their responsibilities more efficiently and promote a merit-based culture. The execution of the plan has begun in several areas, such as the institutionalization of the supervision of the stability of the banking and financial sector. It incorporates developing and integrating solutions and mechanisms of macro- and micro-prudential systems that include the latest stress-testing measures, early warning systems and risk classification.

Commercial activity declines in third quarter of 2013

The Central Bank's quarterly business survey of opinions indicated that the volume of commercial sales decreased during the third quarter of 2013 and remained low relative to historical levels, with the balance of opinion standing at -11 compared to -6 during the same quarter of 2012. But the balance of opinion has modestly improved from -17 in each of the first and second quarters of last year. The business survey reflects the opinions of enterprise managers about their business activity in order to depict the evolution of a number of key economic variables. The balance of opinions was the lowest in the North at -25, followed by Beirut & Mount Lebanon (-18), the Bekaa (+4), and the South (+27). The survey shows that the balance of opinions for the sales volume of food items was +8 in the third quarter of 2013 relative to -5 in the preceding quarter and compared to +11 in the same quarter of 2012. The balance of opinions for the sales of inter-industrial goods was -9 in the third quarter relative to -19 in the preceding period and compared to -1 in the third quarter of 2012; while it was -21 for non-food products relative to -23 in the second quarter of 2013 and down from -18 in the same quarter of 2012. Also, the balance of opinions for inventory levels in all commercial sub-sectors was -3 in the third quarter of 2013 compared to -4 in both the preceding quarter and the third quarter of 2012. Opinions about the level of inventories were the highest in the Bekaa where they reached +7, followed by Beirut & Mount Lebanon (+2), the South (-7), and the North (-26). The balance of opinions is the difference between the proportion of surveyed managers who consider that there was an improvement in an indicator and the proportion of those who reported a decline in the same indicator.

| Commercial Activity: year-on-year evolution of opinions | | | | |
|---|------------------------|-------|-------|-------|
| Aggregate results | Q3-10 | Q3-11 | Q3-12 | Q3-13 |
| Sales volume | 16 | -12 | -6 | -11 |
| Number of employees | 12 | 0 | -2 | -6 |
| Inventories of finished goods | 11 | 4 | -4 | -3 |
| Q3-13 Regional results | Beirut / Mount Lebanon | North | South | Bekaa |
| Sales volume | -18 | -25 | 27 | 4 |
| Inventories of finished goods | 2 | -26 | -7 | 7 |

Source: Central Bank Business Survey for third quarter of 2013

Rafic Hariri International Airport is ninth best in the Middle East

Skytrax World Airport Awards for 2014 ranked the Rafic Hariri International Airport in ninth place on its list of the top 10 airports in the Middle East, down one spot from eighth place in the 2013 and 2012 lists. The results are based on the answers of 12.85 million travelers from 110 different nationalities, and cover more than 410 airports worldwide. Skytrax is a consultancy firm based in the United Kingdom. The Rafic Hariri International Airport received more votes than only Queen Alia International Airport in Amman. The Abu Dhabi International Airport was voted the best airport in the Middle East, followed by the Dubai International Airport, Bahrain International Airport, Muscat International Airport, Doha International Airport, the Ben Gurion Airport in Tel Aviv, King Khalid International Airport in Riyadh and Kuwait International Airport. The Changi Airport in Singapore was voted the best airport in the world.

In parallel, O. R. Tambo International Airport in Johannesburg was voted the best airport in Africa; Changi Airport in Singapore was the best in Asia; Auckland International Airport was found to be the best in Australia & the Pacific region; and Munich Airport was considered to be the best in Europe. Also, Delhi's Indira Gandhi International Airport was considered the best airport in India & Central Asia; Mauritius International Airport was voted the best airport in the Indian Ocean; and Moscow's Domodedovo International Airport was the best in Russia & Commonwealth of Independent States. Further, Panam's Tocumen International Airport received the largest number of votes in Central America & the Caribbean; Vancouver International Airport was selected the best in North America; and Jorge Chavez International Airport in Lima was considered the best in South America.

Customs receipts down 11% to \$216m in first two months of 2014

Figures released by the Customs Directorate indicate that customs revenues reached \$216.1m in the first two months of 2014, constituting a decrease of 11% from \$243m in the same period last year. The Port of Beirut continues to be the main point of customs receipts, as it accounted for 88% of the total in the first two months of 2014, and was followed by the Hariri International Airport with 8.1%, the Port of Tripoli with 2.8%, the Port of Saida with 0.6% and the Masnaa crossing point with 0.5%. Customs receipts from the value added tax totaled \$220.7m in the first two months of 2014, up 3.9% from \$212.4m in the same period of 2013. The Port of Beirut accounted for 83% of such receipts, and was followed by the Hariri International Airport with 10.5%, the Port of Tripoli with 3.8%, the Masnaa crossing point with 2%, the Port of Saida with 0.5% and the crossing point of Abboudieh with 0.1%. As such, overall customs receipts reached \$436.8m in the first two months of 2014, with the Port of Beirut accounting for 85.5% of the total, followed by the Hariri International Airport with 9.3%, the Port of Tripoli with 3.3%, and the Masnaa crossing point with 1.2%. In addition, other entry points represented the balance, with the port of Saida accounting for 0.6%.

Advances against real estate account for 32% of bank credits, share of trade & services at 35% of utilized credits at end-September 2013

Figures issued by the Central Bank about the distribution of bank credits by type show that advances against real estate totaled \$16.6bn, and accounted for 32.2% of total private sector credits at the end of September 2013. They were followed by overdrafts with \$14.7bn (28.6%), advances against personal guarantees \$9.6bn (18.6%), advances against cash collateral or bank guarantees \$6.3bn (12.2%), advances against other real guarantees \$3bn (5.8%), and advances against financial values \$1.4bn (2.6%). In parallel, utilized credits by the private sector totaled \$51.52bn at end-September 2013, with the trade & services sector accounting for \$17.9bn, or 34.8% of such credits. It was followed by personal credits with \$14.1bn (27.5%), construction with \$9bn (17.5%), industry with \$5.8bn (11.3%), financial intermediaries with \$2.7bn (5.2%) and agriculture with \$546m (1.1%), while other sectors accounted for the remaining \$1.4bn (2.7%). Also, wholesale trade represented 43.1% of trade & services credits, followed by real estate services with 20.3%, retail with 16.6%, hotels & restaurants with 8.5%, transport & storage with 8.3%, and educational services with 3.2%. Personal credits attracted 77% of loan beneficiaries, followed by trade & services with 12.5% of beneficiaries, industry with 3.3%, construction with 1.7%, agriculture with 0.9%, financial intermediaries with 0.7%, while other sectors attracted the remaining 3.9%. Further, the aggregate number of loan beneficiaries grew by 8.4% year-on-year to 461,664, while 78.1% of beneficiaries had loans ranging from LBP5m to LBP100m by end-September 2013. Beirut and its suburbs accounted for 78.1% of bank credits and for 53.5% of beneficiaries. It was followed by Mount Lebanon with 10.6% of credits and 16.7% of beneficiaries; South Lebanon with 4.4% of credits and 8.8% of beneficiaries; North Lebanon with 3.9% of credits and 14.2% of beneficiaries; and the Bekaa with 3.1% of credits and 6.8% of beneficiaries.

Subsidized interest loans at \$415m in first nine months of 2013

Figures released by the Central Bank show that the amount of subsidized interest loans to productive sectors in Lebanon reached \$415.3m in the first nine months of 2013. The industrial sector accounted for \$212.9m, or 51.3% of the total, followed by tourism with \$150.4m (36.2%) and agriculture with \$52.1m (12.5%). Subsidized interest loans extended in 2012 totaled \$695.8m relative to \$923.2m in 2011, \$727.6m in 2010 and \$490.7m in 2009. The cumulative amount of subsidized interest loans to productive sectors in Lebanon reached \$5.43bn between 1997 and September 2013.

Subsidized medium & long-term loans reached \$332.3m in the first nine months of 2013, equivalent to 80% of the total. Industry accounted for 51.7% of total subsidized medium & long-term loans, followed by tourism with 40% and agriculture with 8.3%. The program was established in the first quarter of 1997 and consists of a 5% to 7% subsidy on the interest for loans extended in foreign currencies to productive sectors.

Also, subsidized interest loans guaranteed by the Kafalat Corporation totaled \$77m, or 18.5% of the total. Industry accounted for 46.1% of Kafalat-backed subsidies, followed by agriculture with 31.7% and tourism with 22.3%. Kafalat provides financial guarantees for loans of up to \$400,000 for small and medium-sized enterprises in productive sectors. Further, subsidized interest loans granted by leasing companies totaled \$5.5m in the first nine months of last year, or 1.3% of the total, and were extended in full to the industry sector. In addition, subsidized interest loans granted by the International Finance Corporation amounted to \$0.5m, or 0.1% of the total, and were extended in full to the tourism sector.

Amendments to capital adequacy ratios' computation compliant with Basel III standards

In the monthly meeting between the Central Bank and the Association of Banks in Lebanon (ABL), Governor Riad Salamé indicated that the monetary situation in Lebanon is stable and that the balance-of-payments posted a surplus of \$140m in the first two months of the year due in part to the Bank's foreign operations. He said that the sovereign's financing needs in foreign currency will be met through the issuance of Eurobonds to replace those maturing in April and May 2014. He hoped that banks would subscribe to the issuances given their good liquidity level in foreign currency, adding that the subscriptions would not crowd-out lending to the private sector.

In parallel, Governor Salamé indicated that the modifications that the Bank introduced to the computation of capital adequacy ratios for banks in Lebanon are compliant with Basel III standards. He also said that the Central Bank places domestic banks' reserve requirements in foreign currency at foreign banks or at other central banks, which reflects risks equivalent to the Lebanese banks' direct placements with foreign banks. He stressed that the Central Bank does not utilize these deposits, as per the Code of Money and Credit, and that it plays an intermediary role. As such, he indicated that regulators are allowed to allocate to these placements a weight of 20%, similar to that allocated to the banks' direct placements with foreign banks. He noted that, in the case of Lebanon, the Central Bank chose a median weight of 50%.

In parallel, Governor Salamé encouraged banks to invest in the knowledge economy and to promote technology as per Circular 331. He said that banks could invest in local venture capital funds that would, in turn, invest in start-up companies. Further, the ABL indicated that it is in the process of preparing and signing Memorandums of Understanding with several regulatory authorities around the world, such as in Cyprus, Belgium and the United Kingdom.

Banque Libano-Française posts profits of \$100m in 2013

Banque Libano-Française sal, one of Lebanon's top 10 banks, posted unaudited consolidated net profits of \$100.2m in 2013, constituting an increase of 14.4% from 2012. Net operating income rose by 9.8% year-on-year to \$230.9m, with net interest income decreasing by 2.6% to \$164m and net fees & commissions receipts rising by 8.7% to \$41.8m. Non-interest income accounted for 32.3% of total income, up from 30.7% in 2012; with net fees & commissions accounting for 51% of non-interest earnings. Further, the bank's interest margin was 1.64% in 2013 relative to 1.71% in 2012; while its net spread decreased marginally to 1.6% from 1.66% in 2012. Total operating expenditures grew by 6.3% year-on-year to \$119.8m in 2013, with staff expenses increasing by 7.8% to \$72.9m. Also, the bank's return on average assets reached 0.93% in 2013, relative to 0.85% a year earlier; while its return on average equity was 11.53% relative to 10.68% in 2012. The bank's cost-to-income ratio increased to 47.2% in 2013 relative to 45.6% in 2012.

In parallel, total assets reached \$11.1bn at end-2013, constituting a 5.8% rise from end-2012, while loans & advances to customers, excluding loans & advances to related parties, rose by 8.1% year-on-year to \$3.6bn. Also, customer deposits, excluding deposits from related parties, totaled \$9.3bn at end-2013, constituting an increase of 5.7% from a year earlier. The loans-to-deposits ratio rose to 38.8% at end-2013 from 37.9% at end-2012. In parallel, the bank's shareholders' equity rose by 6.6% from end-2012 to \$896.7m at end-2013.

EFG Hermes' net losses at \$49m in 2013

Regional investment bank EFG Hermes declared consolidated net losses of EGP335m, or around \$48.8m, in 2013, compared to net profits of EGP211.1m in 2012. But EFG Hermes posted normalized net profits of EGP427m or \$62.1m last year if adjusted for the one-off charges and gains undergone by the investment bank during the year. The profits were mainly impacted by non-cash goodwill impairment charges and non-cash change in the fair value of investment property of EGP605m. Investment banking operations generated net losses of EGP786m, while commercial banking activity by Crédit Libanais posted net profits of EGP451m in 2013. Total operating revenues reached EGP2.17bn in 2013, up 18.4% annually. EFG said that commercial banking revenues increased by 17.7% annually to EGP1.3bn, while those of investment banking improved by 19.6% year-on-year to EGP830m. It noted that revenues generated from capital markets and treasury operations increased by 63.7% year-on-year to EGP167m, while income from the asset management division rose by 71% to EGP207m. In parallel, EFG Hermes indicated that total consolidated assets reached EGP67.4bn, or \$9.7bn at the end of 2013; relative to EGP59.4bn at end-2012. It added that Crédit Libanais accounted for 61.7% of consolidated operating revenues in 2013.

EFG Hermes Holding SAE holds a 65% stake in Crédit Libanais sal and has a call option for an additional 25% interest in the bank. Crédit Libanais posted net profits of \$68.6m in 2013, constituting an increase of 12.3% from 2012. The bank's return on average assets reached 0.8% in 2013, unchanged from a year earlier; while its return on average equity was 12.1% relative to 12.9% in 2012. The cost-to-income ratio dropped to 57.5% in 2013 from 60.1% a year earlier. Its total assets reached \$8.36bn at end-2013, constituting a 5.2% increase from end-2012; while its loans to customers stood at \$2.6bn at end-2013, up 16.3% from end-2012. The bank's deposits totaled \$7.16bn at the end of 2013 and increased by 2.8% from a year earlier. The loans-to-deposits ratio rose to 36.3% at end-2013 from 32.1% a year earlier.

CreditBank's net profits at \$19m in 2013

CreditBank sal announced unaudited consolidated net profits of \$18.7m in 2013, up by 14.8% from 2012. Net operating income grew by 9.8% year-on-year to \$72.9m, with net interest income rising by 23.6% to \$52m and net fees & commissions receipts increasing by 11.5% to \$15.6m. Non-interest income accounted for 31.65% of total income, down from 40.4% in 2012 with net fees & commissions accounting for 64.8% of non-interest earnings up from 49.1% in 2012. Further, the bank's interest margin rose to 2.22% in 2013 relative to 2.13% a year earlier, and its spread increased to 2.14% from 2.05% in 2012. Total operating expenditures increased by 7% to \$49.9m, with staff expenses growing by 6.4% to \$28.1m. Also, the bank's return on average assets reached 0.77% in 2013, compared to 0.79% a year earlier; while its return on average equity was 9.88% relative to 10.15% in 2012. The cost-to-income ratio was 65.64% in 2013 compared to 66.15% in 2012.

In parallel, total assets reached \$2.6bn at end-2013, constituting a 19.1% rise from a year earlier; while loans & advances to customers, excluding loans & advances to related parties, rose by 20.8% from end-2012 to \$1.3bn. Also, customer deposits, excluding deposits from related parties, totaled \$2.3bn at end-2013, reflecting growth of 20.1% from end-2012. The loans-to-deposits ratio was 57% at end-2013, almost unchanged from 56.8% a year earlier. In parallel, the bank's shareholders' equity rose by 22.5% from end-2012 to \$207.8m at end-2013.

Ratio Highlights

| (in % unless specified) | 2011 | 2012 | 2013 | Change* |
|--|--------|--------|--------|---------|
| Nominal GDP (\$bn) | 40.1 | 42.5 | 44.3 | |
| Public Debt in Foreign Currency / GDP | 52.2 | 57.4 | 59.0 | 160 |
| Public Debt in Local Currency / GDP | 81.6 | 78.4 | 84.4 | 600 |
| Gross Public Debt / GDP | 133.9 | 135.7 | 143.4 | 770 |
| Total Gross External Debt / GDP | 169.0 | 169.9 | 172.7 | 280 |
| Trade Balance / GDP | (34.7) | (34.6) | (32.8) | 180 |
| Exports / Imports | 27.9 | 27.6 | 27.0 | (60) |
| Fiscal Revenues / GDP | 23.3 | 22.1 | 20.9 | (120) |
| Fiscal Expenditures / GDP | 29.1 | 31.4 | 32.1 | 70 |
| Fiscal Balance / GDP | (5.9) | (9.3) | (11.2) | (190) |
| Primary Balance / GDP | 4.1 | (0.3) | (2.5) | (220) |
| Gross Foreign Currency Reserves / M2 | 79.2 | 69.4 | 70.6 | 120 |
| M3 / GDP | 242.5 | 244.7 | 248.9 | 420 |
| Commercial Banks Assets / GDP | 350.6 | 357.4 | 372.4 | 1,500 |
| Private Sector Deposits / GDP | 288.6 | 294.1 | 307.7 | 1,360 |
| Private Sector Loans / GDP | 98.2 | 102.2 | 107.0 | 480 |
| Private Sector Deposits Dollarization Rate | 65.9 | 64.8 | 66.1 | 130 |
| Private Sector Lending Dollarization Rate | 78.4 | 77.6 | 76.5 | (110) |

* Change in basis points 12/13

Source: Institute of International Finance, Association of Banks in Lebanon, International Monetary Fund, Byblos Research Estimates & Calculations

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

Risk Outlook

| Lebanon | July 2012 | June 2013 | July 2013 | Change* | Risk Level |
|-----------------------|-----------|-----------|-----------|---------|------------|
| Political Risk Rating | 53.5 | 53.0 | 53.0 | ▼ | High |
| Financial Risk Rating | 35.0 | 33.5 | 33.5 | ▼ | Moderate |
| Economic Risk Rating | 34.0 | 28.5 | 28.5 | ▼ | High |
| Composite Risk Rating | 61.2 | 57.5 | 57.5 | ▼ | High |

| Regional Average | July 2012 | June 2013 | July 2013 | Change* | Risk Level |
|-----------------------|-----------|-----------|-----------|---------|------------|
| Political Risk Rating | 59.8 | 58.4 | 58.3 | ▼ | High |
| Financial Risk Rating | 41.9 | 41.0 | 41.3 | ▼ | Very Low |
| Economic Risk Rating | 37.2 | 36.7 | 36.6 | ▼ | Low |
| Composite Risk Rating | 69.4 | 68.0 | 68.1 | ▼ | Moderate |

*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 | Negative | B1 | | Negative |
| Fitch Ratings | B | B | Negative | B | | Negative |
| 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 | | CCC | |

Source: Rating agencies

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