

# THE LEBANON BRIEF

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# FINANCIAL MARKETS

## Equity Market Stock Market

	21/09/12	14/09/12	% Change
BLOM Stock Index*	1121.81	1121.67	0.01%
Average Traded Volume	82,102	54,683	50.14%
Average Traded Value	531,932	494,162	7.64%

\*22 January 1996 = 1000



## Banking Sector

	Mkt	21/09/12	14/09/12	% Change
BLOM (GDR)	BSE	\$7.70	\$7.65	0.65%
BLOM Listed	BSE	\$7.40	\$7.40	0.00%
BLOM (GDR)	LSE	\$7.75	\$7.85	-1.27%
Audi (GDR)	BSE	\$5.73	\$5.71	0.35%
Audi Listed	BSE	\$5.55	\$5.50	0.91%
Audi (GDR)	LSE	\$5.54	\$5.60	-1.07%
Byblos (C)	BSE	\$1.49	\$1.50	-0.67%
Byblos (GDR)	LSE	\$79.00	\$79.00	0.00%
Bank of Beirut (C)	BSE	\$19.00	\$19.00	0.00%
BLC (C)	BSE	\$1.90	\$1.90	0.00%
Fransabank (B)	OTC	\$28.00	\$28.00	0.00%
BEMO (C)	BSE	\$1.99	\$1.99	0.00%

	Mkt	21/09/12	14/09/12	% Change
Banks' Preferred Shares Index *		\$105.66	\$105.41	0.24%
BEMO Preferred 2006	BSE	\$100.00	\$100.00	0.00%
Audi Pref. D	BSE	\$10.00	\$10.00	0.00%
Audi Pref. E	BSE	\$100.00	\$100.00	0.00%
Audi Pref. F	BSE	\$100.00	\$100.00	0.00%
Byblos Preferred 08	BSE	\$102.30	\$101.80	0.49%
Byblos Preferred 09	BSE	\$103.10	\$102.80	0.29%
Bank of Beirut Pref. D	BSE	\$26.00	\$26.00	0.00%
Bank of Beirut Pref. E	BSE	\$25.80	\$25.80	0.00%
BLOM Preferred 2011	BSE	\$10.17	\$10.17	0.00%
Bank of Beirut Pref. H	BSE	\$26.10	\$26.10	0.00%

\* 25 August 2006 = 100

The BLOM Stock Index (BSI), Lebanon's leading index, barely increased by 0.01% this week to reach 1,121.81 points, resulting in a 4.66% loss since year start. Market capitalization grew by \$1M to \$8.87B while the average daily traded volume was 82,102 shares worth \$531,932 higher than last week's 54,683 shares valued at \$494,162.

The Lebanese benchmark failed to beat the Morgan Stanley (MCSI) Emerging Index which rose by 1.66% to 998.27 points. It also lagged behind the S&P Pan Arab Composite LargeMidCap Index and the S&P AFE40 index that increased by 0.48% and 0.91% to 111.67 and 54.39 points respectively. Egypt and Dubai's stock exchanges were the best performers recording respective growth levels of 2.93% and 1.98% while Tunisia's bourse was the worst performer declining by 3.29%.

The banking sector dominated the market accounting for 61% of total value traded while the real estate sector captured the remaining share. BLOM and Audi GDRs rose by 0.65% and 0.35% to reach \$7.70 and \$5.73 respectively. Audi Listed stock added 0.91% to close at \$5.55 while Byblos Bank ended the session with a 0.67% decrease settling at \$1.49. On the other hand, the preferred shares index rose by 0.24% to 105.66 points characterized by the 0.49% and 0.29% increase of Byblos Bank Preferred 08 and 09 shares to \$102.30 and \$103.10 correspondingly. On the London Stock Exchange, BLOM and Audi GDR both slipped by 1.27% and 1.07% to end the week at \$7.75 and \$5.54 respectively. Byblos GDR remained flat at \$79.

As for the real estate sector, Solidere class A shares retreated by 0.16% at \$12.82 as its class B shares also declined by 1.32% to \$12.67. In London, Solidere GDR edged up by 0.4% to \$12.5.

In the industrial sector, Holcim Liban climbed 0.33% to settle at \$15.36.

Elsewhere, RYMCO fell by 3.93% to reach \$2.20.

## Real Estate

	Mkt	21/09/12	14/09/12	% Change
Solidere (A)	BSE	\$12.82	\$12.84	-0.16%
Solidere (B)	BSE	\$12.67	\$12.84	-1.32%
Solidere (GDR)	LSE	\$12.50	\$12.45	0.40%

Finally, political tensions have resurfaced but the security situation is improving and will most likely shape the trend of the market for the coming week.

## Manufacturing Sector

	Mkt	21/09/12	14/09/12	% Change
HOLCIM Liban	BSE	\$15.36	\$15.31	0.33%
Ciments Blancs (B)	BSE	\$3.50	\$3.50	0.00%
Ciments Blancs (N)	BSE	\$3.05	\$3.05	0.00%

## Funds

	Mkt	21/09/12	14/09/12	% Change
Beirut Preferred Fund	BSE	\$102.80	\$102.80	0.00%
BLOM Cedars Balanced Fund Tranche "A"	-----	\$6,682.86	\$6,676.45	0.10%
BLOM Cedars Balanced Fund Tranche "B"	-----	\$5,065.00	\$5,060.75	0.08%
BLOM Cedars Balanced Fund Tranche "C"	-----	\$5,075.68	\$5,070.81	0.10%
BLOM Bond Fund	-----	\$9,788.90	\$9,788.90	0.00%

## Retail Sector

	Mkt	21/09/12	14/09/12	% Change
RYMCO	BSE	\$2.20	\$2.29	-3.93%
ABC (New)	OTC	\$16.50	\$16.50	0.00%

## Tourism Sector

	Mkt	21/09/12	14/09/12	% Change
Casino Du Liban	OTC	\$565.00	\$565.00	0.00%
SGHL	OTC	\$4.50	\$4.50	0.00%

## Foreign Exchange Market

### Lebanese Forex Market

	21/09/12	14/09/12	%Change
Dollar / LP	1502.50	1503.50	-0.07%
Euro / LP	1966.23	1965.18	0.05%
Swiss Franc / LP	1622.71	1616.62	0.38%
Yen / LP	19.27	19.35	-0.41%
Sterling / LP	2457.98	2441.25	0.69%
NEER Index**	102.88	102.92	-0.04%

\*Close of GMT 09:00+2

\*\*Nominal Effective Exchange Rate; Base Year Jan 2006=100

\*\*The unadjusted weighted average value of a country's currency relative to all major currencies being traded within a pool of currencies. The NEER represents the approximate relative price a consumer will pay for an imported good.

### Nominal Effective Exchange Rate (NEER)



The exchange rate between the Lebanese Pound and the US dollar narrowed on the local exchange market this week to \$/LP 1,501 - \$/LP 1,504 with a mid-price of \$/LP 1,502.5, from \$/LP 1503.5 last week. Foreign assets (excluding gold) at the Central Bank increased by a monthly 0.6% to \$35.27 billion by the end of August 2012, while the dollarization rate of private sector diminished to 64.7% by the end of July 2012, down from 65% in the previous month and 66% in December 2011.

In international markets, the US dollar and the euro continued to fluctuate ending this week with no significant change. The former climbed on its safe haven status but edged back due to monetary easing measures in the US while the latter continued to see easing short positions against after last week confidence boost. By Friday September 21, 2012, 12.30 pm Beirut time, the euro had inched up 0.05% from the previous week to €/ \$ 1.3043 causing the dollar-pegged Lebanese Pound to depreciate to €/LP 1966.23, from €/LP 1965.18. The Nominal effective exchange rate (NEER) diminished by 0.04% to 102.88 points.

## Money & Treasury Bills Markets

### Money Market Rates

	21/09/12	14/09/12	Change bps
Overnight interbank	2.75	2.75%	0
BDL 45-day C	3.57%	3.57%	0
BDL 60-day CD	3.85%	3.85%	0

Broad money M3 increased by LP84B (\$55.72M) during the week ending September 6 to reach LP154,375B (\$102.4B). Accordingly, M3 increased by 7.47% y-o-y and 5.32% from end of December 2011. M1 climbed during the week by LP110B (\$72.97M) due to a LP222B (\$147.26M) increase in money in circulation, while demand deposits declined by LP112B (\$74.3M). Total deposits (excluding demand deposits) fell by \$17.05M as term and saving deposits in LP increased by \$9.95M, whereas deposits denominated in foreign currencies fell by \$27M. As for the dollarization rate of broad money, it edged down by 6 basis points on a weekly basis to 58.2%. The overnight interbank rate on funds in LBP stood at 2.75% during the month of July, according to the Association of Lebanese Banks.

### Treasury Yields

	21/09/12	14/09/12	Change bps
3-M TB yield	4.39%	4.39%	0
6-M TB yield	4.87%	4.87%	0
12-M TB yield	5.08%	5.08%	0
24-M TB coupon	5.84%	5.84%	0
36-M TB coupon	6.50%	6.50%	0
60-M TB coupon	6.74%	6.74%	0

On September 13, the Ministry of Finance (MoF) raised LP177.48B (\$117.73M) through the issuance of Treasury Bills. The 6M paper took 65.95% of total subscriptions, while the 60M and 3M papers captured 30.11% and 3.95% of total demand respectively. The average discount rate for the 3M and 6M papers were unchanged at 4.39% and 4.87% respectively, with the average coupon rate for the 60M paper also steady at 6.74%. Moreover, the MoF managed to issue worth LP1,367.1B (\$907.26M) Treasury Bills during the TBs auction held on September 20. Demand was mainly observed on the first 10-year TB paper issued by the Lebanese government which captured LP1,149B (\$762.19M) or 84.08% of total subscription. The 36M paper accounted for 15.82% of total demand, while the 24M and 12M papers captured less than 1%. During the auction, the average discount rate for the 12M paper and the average coupon rate for the 10Y, 24M, and 36M papers stood at 5.08%, 8.24%, 5.84% and 6.5% respectively. To note that the MoF continues to undertake all accepted bids.

## Eurobond Market

## Eurobonds Index and Yield

	21/09/12	14/09/12	Change	Year to Date
BLOM Bond Index (BBI)*	108.570	108.310	0.24%	-2.14%
Weighted Yield**	5.22%	5.34%	-12	44
Weighted Spread***	456	473	-17	50

\*Base Year 2000 = 100; includes US\$ sovereign bonds traded on the OTC market

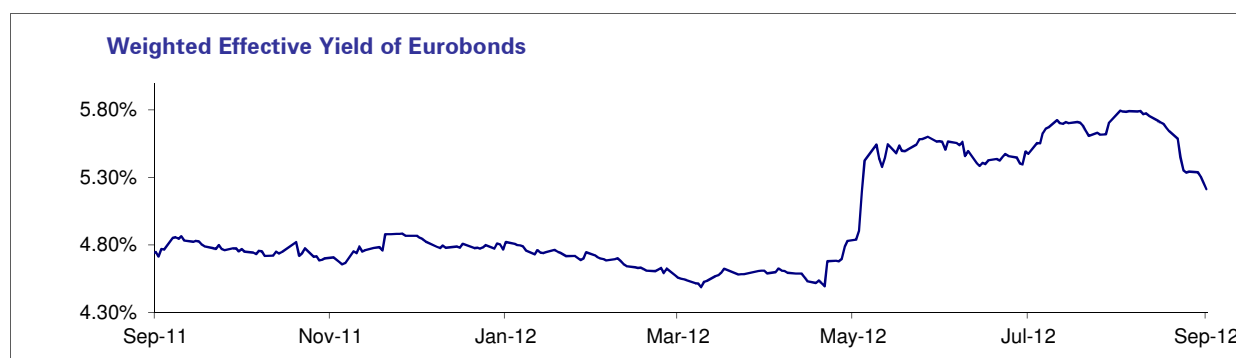
\*\* The change is in basis points

\*\*\*Against US Treasuries (in basis points)

## Lebanese Government Eurobonds

Maturity - Coupon	21/09/12 Price*	14/09/12 Price*	Weekly Change%	21/09/12 Yield	14/09/12 Yield	Weekly Change bps
2013, Mar - 9.125%	102.75	103.13	-0.36%	3.08%	2.55%	52
2013, Jun - 8.625%	103.75	104.25	-0.48%	3.40%	2.87%	52
2014, Apr - 7.375%	105.25	105.25	0.00%	3.85%	3.89%	-4
2014, May - 9.000%	107.75	107.75	0.00%	3.95%	4.01%	-6
2015, Jan - 5.875%	104.13	104.00	0.12%	3.98%	4.05%	-7
2015, Aug - 8.500%	112.25	111.94	0.28%	3.93%	4.06%	-14
2016, Jan - 8.500%	112.25	112.13	0.11%	4.48%	4.54%	-6
2016, May - 11.625%	122.00	123.13	-0.91%	4.92%	4.65%	27
2017, Mar - 9.000%	115.25	115.75	-0.43%	5.15%	5.05%	10
2018, Nov - 5.150%	99.44	99.50	-0.06%	5.26%	5.25%	1
2020, Mar - 6.375%	103.75	103.50	0.24%	5.75%	5.79%	-4
2021, Apr - 8.250%	114.75	115.25	-0.43%	6.02%	5.95%	7
2022, Oct - 6.100%	101.75	101.75	0.00%	5.87%	5.87%	0
2024, Dec - 7.000%	106.13	106.25	-0.12%	6.27%	6.26%	1
2026, Nov - 6.600%	101.63	102.15	-0.51%	6.42%	6.37%	6

• Mid Prices ; BLOMINVEST bank



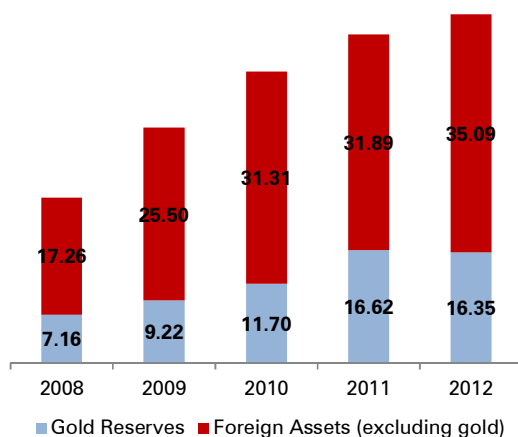
The Eurobond market kept its uptrend this week as the BLOM Bond Index (BBI) climbed 0.24% to 108.57 points. Investors regained some confidence in Lebanon's sovereign debt by the end of the week, after the government successfully issued a 10 year Treasury Bill, worth more than LP 1 trillion and yielding 8.24%. Correspondingly, the yield on the 10-year Eurobond was 5.99% by the end of this week, while the BBI's average weighted yield was 5.22% 12 basis points (bps) lower than last week. The spread between average Eurobond and US Treasury yields narrowed 17 bps to 456 bps. In comparison, the JP Morgan emerging markets' bond index took a break this week sliding by 0.15%.

Lebanon's credit default swap for 5 years (CDS) was last quoted between 440-475 bps. In regional economies, Dubai and Saudi Arabia 5-year CDS quotes ended the week at 276-286 bps and 84-93 bps respectively. In emerging Turkey and Brazil, 5-year CDS quotes closed at 152-155 bps and 103-106 bps respectively.

## ECONOMIC AND FINANCIAL NEWS

### BdL Foreign Assets and Gold Reserves

By mid-September



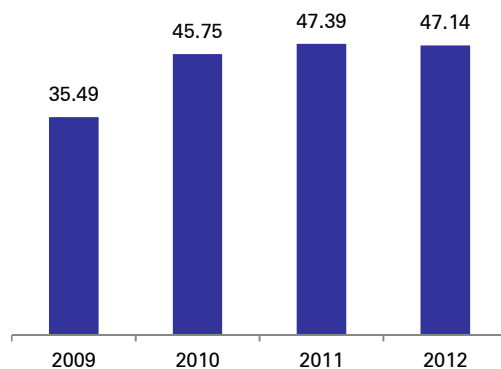
Source: BdL

### BdL Assets Reach \$77 billion by mid-September Supported by International Gold Prices

In the period between 15 August and 15 September 2012, total assets at Lebanon's Central Bank (BdL) climbed by 3% to a new record of \$77.2 billion, 9.8% above their value in December 2011. This expansion was mostly due to a 9.8% jump in the value of BdL's gold reserves to \$16.35 billion, but also as a result of a 3.77% increase in the Central Bank's Securities portfolio to \$11.46 billion. The international price of gold had appreciated to \$1772 per ounce by September 14, from \$1603 per ounce a month earlier. BdL's foreign assets remained unchanged from a month earlier at \$35.09 billion. With regards to BdL's liabilities, financial sector deposits increased by 1.84% m-o-m to \$54.13 billion, while public sector deposits dropped 5% m-o-m to reach \$5.76 billion. Currency in circulation outside of BdL inched up by 0.35% to \$2.19 billion.

### Value of Cleared Checks

Up to August (\$B)

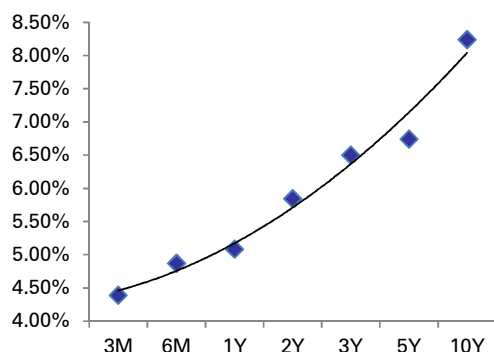


Source: ABL

### Cleared Checks Reach \$47.14B up to August 2012

The value of checks cleared by Banque du Liban continued its downward trend affected by the current Lebanese political situation and the persistent political instability in the region. The number of cleared checks reached 8.65M valued at \$47.14B in the first eight months of 2012 compared to a total of 8.57M checks worth \$47.4B registered a year earlier. Checks denominated in foreign currencies dropped by 1.48% y-o-y to \$37.38B, while the value of checks denominated in Lebanese pounds increased 3.27% to \$9.77B. The dollarization rate of checks stood at 79.28% compared to 80.04% recorded in August 2011. Moreover, the value of returned checks declined by 4.58% y-o-y to \$1.04B, representing 2.18% of the total value of checks. For the month of August alone, the value of cleared checks dropped for the second consecutive month, falling by 3.73% from August 2011 to reach \$5.89B as the value of checks denominated in foreign currencies retreated by 7.18% to \$4.66B, its lowest level in four months. Checks denominated in LP advanced by 11.99% y-o-y to \$1.23B.

### Lebanon's Public Debt

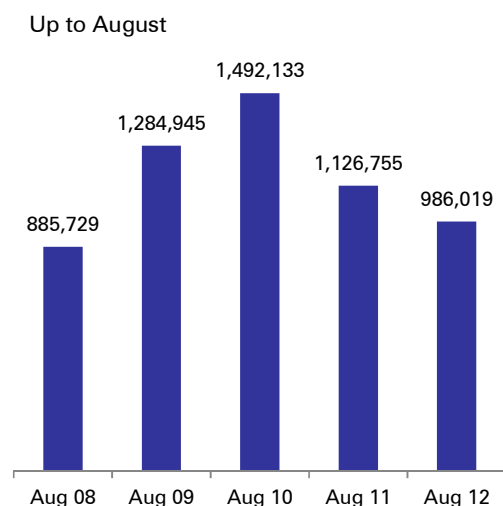


Source: Reuters

### Finance Ministry Raises LP 1 Trillion in 10 Year Treasury Bill Sale

Lebanon successfully sold its first 10 year Treasury bill despite turmoil in Syria and escalating domestic political tensions, indicating confidence in Lebanon's economy and currency, according to Central Bank Governor Riad Salameh. The sale brought in more than LP 1 trillion or \$700 million for the Lebanese government, and will pay out an interest rate of 8.24%. Lebanese banks had been asking for yields that are higher than those currently being offered on short and medium TBs. Governor Salameh added that the Lebanese currency is not at risk, as market demand has held up well against political concerns, explaining the success of the TB sale. Moreover, BdL currently holds a record of \$35 billion in foreign reserves, which constitute a buffer against shocks.

### Number of Visitors up to August



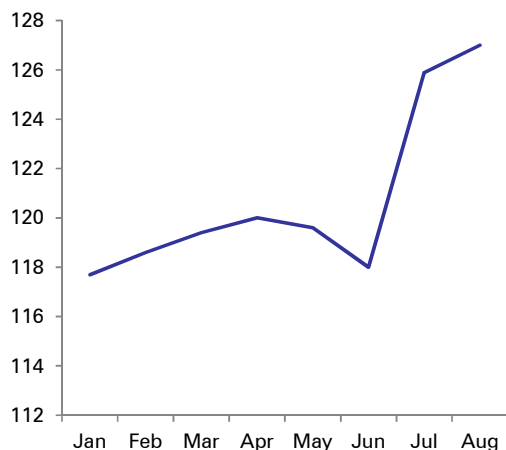
Source: Ministry of Tourism

### Visitors of Lebanon decrease by 12.5% by August

114,929 tourists visited Lebanon during the month of August, a 26.88% drop compared to July, according to statistics published by the ministry of Tourism, noting that Ramadan fell in the first part of the month. The annual decline during 2012 is so far 12.49% with a total of 986,019 visitors entering the country compared to 1,126,755 visitors recorded by August 2011. Better expectations are set for September's figures following the Pope's visit to Lebanon. In details, visitors from Europe ranked first during August with 44,464 arrivals, i.e. 39% of all comers, with the single highest entrances being from France at 14,498 visitors. People from Arab countries came second at 26.83% of total registries with 30,839 visitors of which 11,966 were from Iraq. Visitors from Americas represented 19.72% with 22,661 recorded arrivals. Over the 8 months span of 2012, the declining trends were noticed among visitors from the Arab countries (-9.41%), Europe (-5%) and Asia (-51%) with the only increase being among visitors from the American continent (+2.75%).

## Inflation at 0.9% in August

## Consumer Price Index in 2012

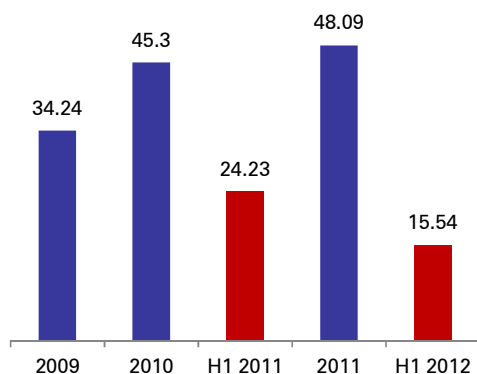


Source: CAS

Lebanon's consumer price index picked up a 0.91% monthly increase in August, landing its annual increase at 9.32%; to note that the annual change in CPI also includes the 44.1% surge in housing from July 2009, when the previous survey on rentals was conducted by the Central Administration of Statistics. The slight change during August was mainly driven by the 3.48% rise of transportation costs which weigh 12.3% in the index, noting that compared to August 2011, transportation costs are less by 0.53%. Also the utilities sub-index weighted 9.5% in the CPI (water-electricity –gas& fuel), inflated a further monthly 3% after its 5.9% jump in July, as a direct consequence of increasing electricity shortage and higher fuel prices which had led households to use costly alternative power supplies. Food and non-alcoholic beverages augmented by a monthly 0.27% and an annual 5.49%, noting that they account for 19.9% of the CPI. Health sub-index rose by a slight 0.36% m-o-m sustained by the status-quo of the negotiations between the hospitals and the NSSF.

## CORPORATE DEVELOPMENTS

### BLC's Net profit (\$M)



Source: Company Reports

### BLC's net profit drops by a yearly 35.88% in H1 2012

BLC Bank's net profit fell by 35.88% to \$15.54 million in the first half of 2012, compared to last year's \$24.23 million during the same period. This decline is characterized by the 89.06% yearly drop in gains on disposal of property and equipment, down from \$9.11 million to \$1 million and the 10.37% annual increase in staff costs to \$24.07 million. On the other hand, the bank's net interest income increased by 43.46% to \$46.63 million while net fees and commission income recorded \$9.29 million. The bank's consolidated assets grew by 5.39% to \$4.65 billion compared to \$4.42 billion by the end of 2011. Finally, customer deposits jumped by 8.56% to \$3.92 billion while loans and advances rose by 8.86 percent to \$1.67 billion.

### Alpha Banks

Bank Audi Sal - Audi Saradar Group	Bank of Beirut Sal
BankMed Sal	Française -Banque Libano Sal
BBAC Sal	BLOM Bank Sal
Byblos Bank Sal	Crédit Libanais Sal
First National Bank Sal	Sal Fransabank
IBL Bank Sal	Société Générale de Banque au Liban Sal - SGBL

Source: Bankdata Financial Services

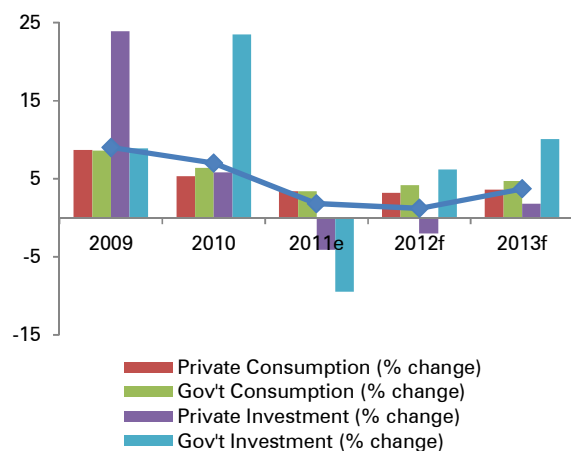
### Alpha banks' total assets reach \$146.72B in H1 2012

Alpha banks', the top 12 largest Lebanese banks, consolidated total assets grew by 8.4% y-o-y to stand at \$146.72B in June 2012 according to the latest report by Bankdata. This increase is mainly driven by the 52.46% surge in cash and balances with the Central Bank that recorded \$28.22B. Net loans and advances to customers rose by a yearly 12.60% to \$41.41B. On the liabilities side, deposits from customers grew by 8.63% to reach \$120.48B. Moreover, the consolidated net profit reached \$836M, up by 7.67% from the same period in 2011. Net interest income drove profits up as it climbed by a yearly 13.21% to \$1.36B. BankMed Sal led the group in terms of asset growth as it surged 11.84% to \$13.19B from year start, followed by First National Bank growing by 10.36% to \$3.11B. Furthermore, IBL Bank Sal topped the group in terms of YTD loans and advances growth with an increase of 30.67% to \$828.47M. Finally, Bank Audi, BLOM Bank and Byblos Bank remained the market leaders in terms of total assets making a cumulative share of 47% of total consolidated assets.

## FOCUS IN BRIEF

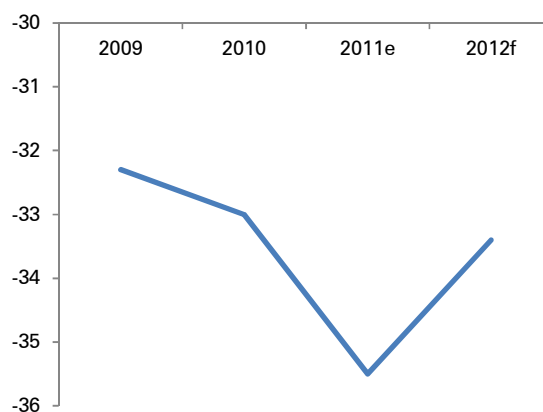
IIF, "Turmoil in Syria Dims Economic Prospects", Overview

Real GDP by Expenditure Components



Source: IIF

Net Export (% GDP)



Source: IIF

### Selected CDS Spreads

(basis points, 5 year maturities)

	31-Dec-10	30-Dec-11	28-Jun-12	7-Sep-12
<b>Lebanon</b>	<b>305</b>	<b>475</b>	<b>488</b>	<b>492</b>
Egypt	243	640	640	440
Dubai	415	445	365	283
Tunisia	120	268	285	305
Bahrain	186	383	350	278
Morocco	126	268	282	213
Saudi Arabia	75	129	129	96
Turkey	141	291	260	154

Source: IIF

### Lebanon: Selected Vulnerability Indicators

	2009	2010	2011e	2012f
Current Account Balance, % GDP (- = Deficit)	-19.5	-20.1	-25.6	-27.7
Nonperforming Loans, % Total Loans	6.0	4.3	3.8	4.0
Government Debt, % GDP	147.6	141.7	136.9	138.6
Fiscal Balance, % GDP	-8.5	-5.7	-6.0	-8.9

Source: IIF

The IIF issued a research note on economic growth and political risks in Lebanon, titled "Lebanon: Turmoil in Syria Dims Economic Prospects". Below is an overview of the study.

The IIF perceives the economic activity in Lebanon in 2012 strongly restrained by ongoing events in Syria but positions the country as relatively resilient to shocks. GDP growth is estimated to have slowed from 7% in 2010 to 1.8%<sup>1</sup> in 2011 (Blominvest estimates GDP growth at 3% in 2011) and is projected to remain positive but to decelerate to 1.2% in 2012. The IIF observes that the intensification of social upheaval in Syria reflects itself heavily on the Lebanese territory mostly through kidnapping and fighting in the north area of the country. While this is pulling down the economic activity through lower transit trade, a fall in tourism activity, and weak investments, the resiliency that the local economy has to shocks is being backed by a strong banking system and continuous remittances and deposits coming in from the Lebanese Diaspora.

When considered on the global scale, the moderate recession in the Euro Area is not expected to affect much the Lebanese economy, contrary to developments in the MENA countries. Trade between Lebanon and the Euro Area is limited with exports to the latter making up about 8% of total exports in 2011 and tourists' arrivals from the Euro Area accounting for 24% of the total. However the bulk of Lebanon's trade and financial linkages are with MENA countries, the GCC in particular where economic growth reveals promising prospects for the Lebanese economy. The IIF predicts workers remittances to Lebanon, standing at 14% of GDP, to remain stable as most of them originate in the GCC countries, Australia, North America, and Sub-Saharan Africa, where the economic activity is expected to remain robust in 2013.

According to the IIF measure, Lebanon's GDP growth reached 2.5% in the first quarter of 2012, and contracted by 0.3% in the second quarter, driven down by social upheaval in Syria and the consequential political tensions it brought in to Lebanon. Most proxy indicators of economic activity used by the IIF have declined over the second quarter of the year, driving the former result. While the volume of total imports of goods rose sharply in light of weakening demand, the IIF linked the increase to the rise in imports of petroleum products in the first quarter of 2012 which was perceived through the surge in purchases for electricity production. Also, the robust rise in VAT reflects, according to the IIF, the rise in imports of petroleum products that led to higher VAT collection at customs.

Looking forward into the third and fourth quarter of the year, the IIF estimates a small contraction over the former quarter as a result of a worried security situation, driving the Lebanese economy into a recession over 2012<sup>2</sup>. Hotels witnessed more than a 30% cancellation rate as a result of the series of kidnapping targeting Syrians and people with a few other nationalities. Adding to that, the embassies of Saudi Arabia, Qatar, the UAE, and Kuwait advised their citizens to leave Lebanon, which impacted directly and heavily the trade and tourism activities in the country, dragging down the economy. As a result, the IIF estimated a 0.5% contraction in GDP growth over the third quarter of 2012 and projects a 3% positive GDP growth over the fourth quarter on the recent improved security situation after the Lebanese Army was able to contain the fighting in Tripoli and free four kidnapped Syrians.

The financial markets in Lebanon have also showed sign of slowdown, especially when compared to regional markets. The Beirut stock market price index fell by 4.3% from end of 2011 to end of August 2012, compared to a rise of 14.4% in Dubai and a rise of 4% for the emerging market index. Also, CDS spreads, the cost of insuring Lebanon's debt against default went up by 187 basis points since end of 2010 to 492 basis points as of September 7th, 2012, and this ranks the highest among MENA emerging economies. Yet on the positive side, Lebanon's bond yields benefit from being held by domestic banks, which are highly liquid and continue to attract significant deposits from the Lebanese Diaspora.

In spite of rising risks threatening the Lebanese economy, the country is endowed with strong buffers with its significant official reserves and strong banking system. The central bank showed consistency over time in exercising effective regulation and supervising the banking system through a conservative approach to its funding practices. For instance, only 26% of total deposits are handed as private sector loans, keeping high capital liquidity cushions. This has insured a strong confidence in the Lebanese Pound and led to a rise in foreign assets held by the Central Bank to a new peak of \$35.3 billion as of end of August 2012.

<sup>1</sup> The IIF's quarterly real GDP growth figures for Lebanon are based on 12 proxy economic activity indicators compiled monthly and converted to real terms: registered tourist arrivals, airport arrivals, electricity production, cement deliveries, capital goods imports, petroleum products imports, the value of cleared checks and ATM withdrawals, total deposits, private sector credit, VAT, exports of goods, and imports of goods

<sup>2</sup> Recession is when GDP growth is negative for two consecutive quarters or more

As much as Lebanon's monetary management strongly supports the economy, improvements are required in other areas to withstand internal and external risks. Lebanon faces the major challenge of debt management. Although the debt is mostly held in local currency and financed by the banking system which is consistently being liquid and profitable, the widening current account and fiscal deficit makes it vital for the country to bring in significant inflows of foreign capital<sup>3</sup> to finance both deficits. And for that to materialize, stability should be ensured for the political and security situation of the country. Also, structural reforms should be implemented to enhance Lebanon's poor infrastructure and for that a budget should be approved to allocate spending across ministries, and the private sector role should be stronger in providing the investment for which the government lacks the mean.

Under the assumption of an enhancement in the security situation along with the initiation of the implementation of structural reforms, the IIF projects real GDP growth to accelerate to 3.7% in 2013 and 4.5% in 2014, driven by a recovering tourism sector and private investment. This will bring in a reduction in the debt-to-GDP ratio and reduce risk premia

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<sup>3</sup> Mostly in the form of FDI and nonresident deposits in the banking system

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