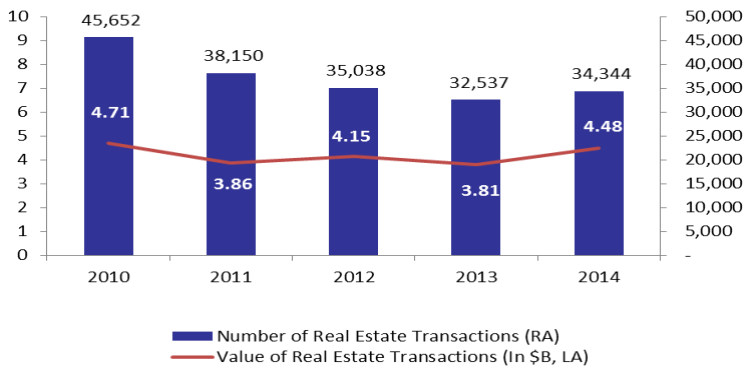
Slight Progress of the Real Estate Market in H1 2014

BLOMINVEST BANK

Value and Volume of Real Estate Transactions by June



Source: Cadastre

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With the beginning of 2014, activity in the Lebanese real estate market got little breathing space despite the escalating challenges that were undergoing in Lebanon and the region. Investors revealed optimistic prospects about the year and translated their hopes in both the construction and real estate markets. Yet, the sector remained wobbly and characterized by a mismatch between the purchasing power, the supply and the tenacious pricing system. Developers were also facing the scarcity in land, volatility in workforce availability, lower demand from GCC residents who switched to more secure areas, financial sustainability concerns, legal and logistic delays in delivery, and construction material price sensitivity.

The Mismatch of Demand and Supply Kept Prices Depressed

2007-2011 was a booming period for the Lebanese real estate market characterized by a pent-up demand outpacing supply levels. Supply remained low over the mentioned period as projects need time to be constructed and the majority takes more than a year to be done. Consequently, real estate prices went up after being well below the regional market.

However, real estate demand was hindered starting late 2011 by pressures from the war in Syria and the fragile domestic situation that continued through 2013. The period 2011-2013 can be described by an improving supply that took time to adapt to demand levels.

In 2014, real estate supply rose at a faster pace than demand with prices stagnating at their previous levels. This increase in supply can be explained by the considerable number of empty flats following the shift in demand.

Improving Demand in the First Half of 2014

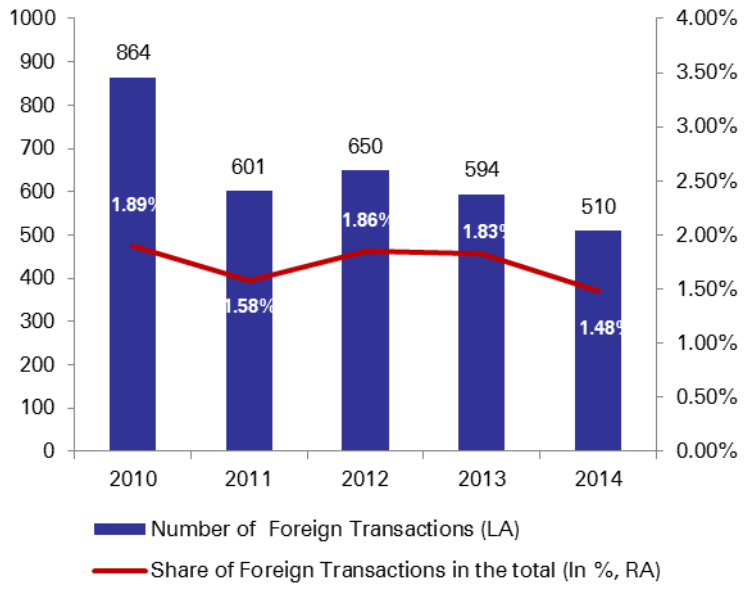
Demand in the Lebanese real estate sector saw three years of respective declines as political and economic instabilities weakened investors' appetite. Noting that Foreign Direct Investments' (FDI) inflows to Lebanon are still highly focused on the real estate market, they dropped to $2.83B in 2013 or 6% of FDI inflows into West Asia, down from $3.67B or 8% of FDI inflows into West Asia in 2012. Lebanon also lost some of its appeal for foreign investors as Greenfield investments into the country were slashed by almost half from $201M in 2012 to $104M in 2013. As a result, real estate transactions deteriorated by 7.1% year-on-year (y-o-y) in the first half of 2013 to 32,537, down by yearly 14.7% and 28.7% from 2011 and 2010.

On a positive note, the first half of 2014 was promising and boosted by a recovering local demand. The long awaited Cabinet formation by Mid-Feb 2014 sent the total number of real estate transactions (local and foreign transactions) 5.5% higher in H1 2014 to 34,344 compared to 32,537 in H1 2013. Total value of property sales transactions surged 17.6% y-o-y from $3.81B in 2013 to reach $4.48B by June 2014. Local demand for real estate projects improved in H1 2014 mainly on high hopes of a possible breakthrough in the pending political impasse. In this context, the number of real estate transactions sold to Lebanese nationals added 5.9% y-o-y to 33,834 in the first half of 2014, grasping 98.5% of total transactions.

Despite the improving status of the overall investment sentiment, the Lebanese property market kept on undergoing the significant decrease in foreign demand mainly stemming from GCC countries. In details, sales

to foreigners were following a sluggish trend since 2010 with the exception of 2012 when the displaced Syrians enhanced foreign demand in the Lebanese real estate market. However, sales to foreigners went from 594 by June 2013 to 510 by June 2014. This constitutes a 14.1% yearly drop from 2013 and a 41.0% y-o-y slump from the first half of 2010.

Foreign Demand Evolution and Share by June



Source: Cadastre

Lebanon's real estate projects are further losing foreign investors' appeal over the years, noting that the share of real estate sales to foreigners is minimal at 1.5% compared to 1.8% and 1.9% in 2013 and 2012, respectively. This was mainly due to the repeated warnings from GCC governments calling their citizens to avoid Lebanon due to the high degree of political uncertainty and security developments.

Regions' preference changed in 2014 following a shift in buyers' perspective. Despite the absence of security that governed the Northern part of Lebanon in 2013, the gradual yearly decline in prices and the newly formed Cabinet security strategy managed to boost the number of real estate transactions in the district that grasped 26% in H1 2014 compared to 16% in H1 2013. Baabda came second with a 20% stake of total transactions after being the most preferred Lebanese region in 2013 and was followed by Metn in the 3rd place (11%). Zahleh and Keserwan shared the 4th rank with 10% of total real estate sales while the South region and Nabatieh took the 5th standing with a similar 8% stake. As expected, Beirut was the biggest loser (6% of the total) given the scarcity of land and the highly priced apartments.

Real Estate Supply on the Rise in H1 2014 Outpacing the Slight Increase in Demand

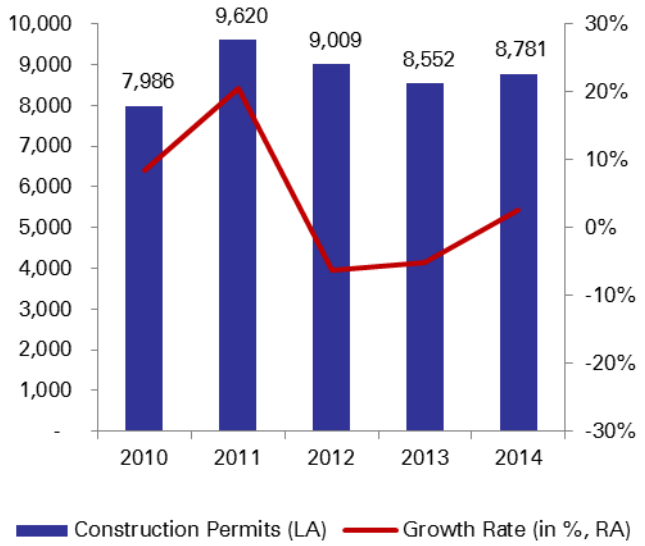
The first half of 2014 unveiled a rising demand in the real estate market hand-on-hand with a progressing supply. Yet, the increase in supply of real estate projects went at a faster pace than that of demand. In details, many elements backed real estate supply to catch up and rise. First, and after demand went down due to the amplified prices reached by the end of 2010, prices stabilized and stocks of supply increased. Those existing real estate stocks accumulated with other old stocks resulting of the inadequacy of demand with the available supply. The situation worsened for the Lebanese suppliers after foreign demand was hit by the repeated warnings form GCC governments calling their citizens to avoid Lebanon due to the high degree of political uncertainty and security developments.

As supply outpaced the improving demand, buyers gained more freedom and time to negotiate their purchases. Therefore, many developers are currently more open for price negotiations with some of them willing to offer approximately 10% discount. Worth mentioning that the time needed to sell an apartment has prolonged lately as buyers have the option to choose from the overflowing number of unsold apartments and negotiate for their own best interest.

Supply activity in H1 2014 can be measured by the construction sector's performance. Given its vital role in propelling the expansion of local economy, construction represented a 4% share of the Gross Domestic Product (GDP)[1]. In 2014, construction activity was buoyant mirroring investors' optimism about 2014 and the possible breakthroughs on both the security and political fronts. Correspondingly, construction loans also went up by 6.4% y-o-y to $9.04B in May 2014.

Cement deliveries, which are one of the earliest barometers of construction activity, revealed improving performance. Accordingly, cement deliveries maintained the upward trend that started in 2013 and posted a 7.4% y-o-y growth by May 2014 to 2.26M tons compared to 2.11M by May 2013.

Construction Permits by June



Source: Orders of Engineers in Beirut and the North

Another sign of increasing supply was translated by a higher number of construction permits in the first half of 2014. The number of construction permits posted a 2.7% yearly rise to 8,781. Worth mentioning that construction permits reflect the market's envisioning of real estate activity in the previous 6 months. Thus, the improvement in H1 2014 reveals the hopeful expectations of contractors when it comes to the country's security, economic and political stability in the coming year 2014.

The Orders of Engineers in Beirut and the North data revealed that Mount Lebanon kept the top location for new constructions in H1 2014 capturing 43.3% of total activity in terms of projects number, while the lowest was Beirut reporting 5.0% of total projects. South Lebanon, Nabatiyeh, North Lebanon and Bekaa showed respective stakes of 16.8%, 12.6%, 12.4% and 9.9% by the end of June 2014.

Furthermore, the Construction area Authorized by Permit (CAP) jumped 16.1% y-o-y to 7.27M Square Meters (SQM) in the first six months of 2014. This would imply the spreading of projects over high-end investments, and the shift of supply to serve a more selective demand. Accordingly, the average area per permit has widened by 13.1% to 827.45 SQM/permit by June 2014 compared to 731.87 SQM/permit recorded in H1 2013.

The mismatch between demand for and supply of apartments following the change of type of demand and the bigger supply was spread all over the Lebanese regions. However, and given the lack of data for other regions, we tried to analyze the consequences of the disproportion between the demand and supply on the real estate market of Beirut.

[1] *Central Administration of Statistics (CAS) 2011 National Accounts.*

Beirut: a Sample of Mismatching Demand and Supply

The divergence between demand and supply on the real estate market and the domestic and regional uprisings severely hit the property sector demand since 2011. Given the lack of data about 2014, real estate consultant, RAMCO, stated that Beirut residential projects completed in 2013 showing that 277 new apartments remained unsold in 2013 compared to 217 units completed during the course of 2012. Unsold apartments in 2013 represented an 81,773 SQM of built-up residential area worth $437.58M.

The rising number of unsold apartments does not reflect a slowing demand, but a changing one. Demand for apartments remains high as revealed by the rising number of housing loans that reached $9.08B by May 2014, up by a yearly 18.1% thanks to Banque du Liban's (BDL) incentive program[2].

Yet, buyers' purchasing power is far below the offered prices. Besides wealthy buyers, the average income of a Lebanese employee is relatively low and the maximum payment that the latter can settle is one third of its monthly income[3]. In addition, the subsidy that BDL provides to commercial banks for housing encourages demand for small apartments with area not exceeding 150 SQM. Accordingly, Lebanese buyers are looking for smaller flats that they can afford with their relatively low income.

Given the shift of demand towards smaller apartments, Beirut real estate suppliers adjusted their projects' size. A recent study[4] revealed that 17 out of 24 neighborhoods showed reduction of apartments' space even in the most luxurious regions. Setting an example, Sursock apartments posted a 36.5% decline in the projects' area from 392 SQM to 287 SQM. The same case can be seen in the coastal neighborhoods such as Aïn el-Mreisseh (-4,1%), Manara (-20.8%) and Ramlet el Baïda (-14.0%). Saifi (-22.1%), Mar Mikhaël (-11,5 %), Sodeco (-3.8%), Gemmayzé (-3.6%) and Hamra (-1.8%) followed the same trend as well. However, apartments in Beirut's Downtown area revealed a 2.2% increase in the average area per project from 344 SQM to 352 SQM as well as Clemenceau (+1.6%), Koraytem (+1%) and Furn el-Hayek (+2.2%).

Real Estate Prices: New Formation Process Coherent to the Changing Demand

Even with the economic slowdown and the complications on the Syrian front that kept on weakening investors' confidence, property prices remained steady and not dictated by the fluctuating demand. However, the average value per transaction edged up by 10.5% y-o-y in the first half of 2014 to $129,409 compared to $117,098 recorded in the same period last year. Besides the scarcity of land that remained the first price influence, the Syrian crisis has also cast a multitude of consequences on demand, as citizens fleeing their country were looking for purchases or rents thus helping to maintain prices.

As for the geographical breakdown, the average value per transaction altered in H1 2014 relatively to changes in demand or projects' sizes, the intensification of security uprisings in some regions as well as the scarcity of land in others. The capital Beirut kept on posting the highest average value per transaction at $538,694 by June 2014, up by 23% from the same period in 2013. The South region saw the highest yearly growth of 29% to $76,664 mainly due to the relatively stable security environment that is actually reigning. In contrast, the prolonged clashes in Tripoli worsened the average value per transaction in the North district by 44% y-o-y to $30,589. The average value per transaction in Nabatieh, Zahleh, Baabda and Keserwan rose by nearly 16%, 12%, 4% and 3% y-o-y to $46,120, $41,224, $123,347 and $125,080, respectively.

Given that the average value per transaction rose by the end of June 2014 compared to 2013's level, this does not necessarily indicate an increase in the prices of real estate projects. Yet, the parallel growth of the average area per construction permit over the same period can, to a certain extent, point to a potential increase in the average size of projects build by contractors.

2 In the beginning of 2013, BDL placed $1.46B at the disposal of banks at 1% interest so commercial banks can increase loans to institutions and households at reduced interest. BDL mainly aimed the expansion of lending and demand for housing loans (56% of total placement) for low and medium income households.

3 As per BDL regulations

4 Conducted by L'orient le Jour in cooperation with RAMCO

Selected World's Most Expensive Cities

Ranking	Country	Buying Price ($/SQM)
1	Monaco	53,026
10	Japan, Tokyo	11,466
20	China, Shanghai	6,932
43	Lebanon, Beirut	3,693
75	Morocco, Marrakesh	2,015

Source: Global Property Guide

Buyers wishing to acquire an apartment in Beirut need to be wealthy while those with low to middle income are forced to buy in areas outside the capital. According to Global Property Guide's survey, Beirut-Lebanon stood at the 43rd place among 94 countries with a buying price of $3,693/ SQM for an apartment of 120 SQM in Beirut. Worth mentioning, that the asking value for an apartment in Beirut ranges between $1,925 and $7,647 per SQM.

Selected Countries Real Estate Prices and GDP per Capita

Country	Buying Price ($/SQM)	GDP per Capita	Ratio
Italy, Rome	8,355	34,619	24.1%
Denmark, Copenhagen	5,310	58,930	9.0%
Lebanon, Beirut	**3,693**	**9,928**	**37.2%**
Mexico, Mexico City	2,635	10,307	25.6%
Jordan, Amman	1,283	14,760	8.7%

Source: Global Property Guide

The ratio (buying price over GDP per capita) can easily illustrate the considerable burden of real estate prices in Beirut for the Lebanese resident. The ratio registered a 37.2% stake in Beirut compared to 24.1% in Rome and 8.7% in Amman.

The Residential Market in Lebanon:

RAMCO released a research publication early in 2014 about residential prices of neighborhoods through the capital. The study, which enclosed 382 buildings under construction across Beirut, revealed that an adjustment phase in the residential market started in 2013 after several years of price increases. Property owners have finally started to adapt to the financial capabilities of people who buy out of income and used to be priced out of the market (despite being the largest share of buyers).

Average Price of an Apartment under Construction in Municipal Beirut

Location	BCD	Achrafieh	Western Beirut	Municipal Beirut
Average Price (USD/SQM)	8,156	4,204	4,143	**4,331**
Average Size (in SQM)	323	248	240	**252**
Average Budget (in $)	$2,634,388	$1,042,592	$994,320	**$1,091,412**

Source: RAMCO

The study revealed that the value of an average apartment excluding negotiation margins is $1.09M. Worth mentioning that the average apartment according to the study has 3 bedrooms, located on the 6th floor and measures 252 SQM. Accordingly, the average price per SQM of an apartment under construction in Municipal Beirut hovered around $4,331. RAMCO declared that the average apartment size has declined over the past 4 years by 18% or 58 SQM confirming the investors' shift towards smaller plot projects. The geographical prices breakdown of the surveyed apartments showed that the highest average price (53% higher than municipal Beirut's average) was recorded in BCD at $2.63M for a size of 323 SQM. Ashrafieh followed with an average budget of $1.04M for a size of 248 SQM, while Western Beirut average apartment price stood at $994,320.

In details, prices in Ashrafieh reached their highest levels at the top of the neighborhood's hill in the area of Rizk Tower and declined gradually as they reach the Port of Beirut and the south-eastern hills that oversee Nahr Beirut. As for the Western half of Beirut, prices hovered according to their proximity to the seashore line. This means that asking sales prices are the highest along the seashore and decrease progressively as they go inland. Also, the central neighborhoods located between the western and eastern Beirut posted the lowest residential prices.

However, the three most expensive areas in Beirut were BCD ($7,647 per SQM), Ain el Mreisseh ($7,000 per SQM) and Raouche ($6,557). In contrast, the cheapest three neighborhoods across Beirut were Noueiri ($1,925 per SQM), Tarik Jdideh ($2,101 per SQM) and Bachoura ($2,200 per SQM).

"Up and Coming Cities for the Rich" Report's Breakdown

Rank	City	Price of a two-bedroom apartment
1	Beirut, Lebanon	$180,000-$500,000
2	Cape Town, South Africa	$110,000-$370,000
3	Chennai, India	$40,000-$160,000
4	Chicago, U.S.	$250,000-$700,000
5	Dublin, Ireland	$210,000-$560,000
6	Istanbul, Turkey	$125,000-$280,000
7	Jakarta, Indonesia	$90,000-$260,000
8	Lagos, Nigeria	$70,000-$300,000
9	Melbourne, Australia	$320,000-$675,000
10	Miami, U.S.	$275,000-$900,000
11	Panama City, Panama	$200,000-$500,000
12	Tel Aviv, Israel	$500,000-$1,450,000

Source: CNN Money

According to a new report carried by CNN Money and entitled "Up and Coming Cities for the Rich"[5], Beirut ranked first among 12 countries as the best destination for risk-taking real estate investors. The report announced that Beirut is one of the best countries for real estate investors to create wealth and best returns in the coming period as it is also recognized as a regional financial hub. In addition, the report concluded that

5 Report compiled by Savills World Research, Candy & Candy and Deutsche Asset & Wealth Management

real estate investments in Lebanon are reasonably priced compared to the international standards. Beirut toped each of Cape Town- South Africa, Chennai-India, Chicago-U.S.A, Dublin-Ireland and Istanbul-Turkey.

The report considered that a two-bedroom apartment in Beirut ranges in price from $180,000 to $500,000, depending on the location. Prices for a two-bedroom apartment in Jakarta-Indonesia and Lagos-Nigeria range $90,000-$260,000 and $70,000-300,000, respectively. Currently, a two-bedroom apartment in Beirut is lower priced than that in Melbourne-Australia ($320,000-$675,000) and Miami-USA ($275,000-$900,000).

The Office and Land Markets' Standing in the Sector

Offices and raw land are other market segments within the real estate sector. On a global view, both sections showed steady performance despite the slackening economic situation of the country. However, the lack of data in both segments undermines evaluation possibilities of the changes in demand.

The slowdown in the residential market, amid a mismatch between demand and supply, pushed investors towards commercial projects that are more income appealing; given the shortage in stock within the market. Real estate consultant RAMCO released a survey by the end of 2013 showing that 32 office projects are actually taking place in Beirut totaling 147,871 SQM. Out of those projects, eight are residential towers offering office floors on the lower levels.

As for the projects' geographical distribution, Ashrafieh captured the bulk with 18 projects of 97,491 SQM. New offices selling prices are estimated at $3,500 per SQM in average relatively to the project location. Ras Beirut followed with 10 office projects representing a total of 25,307 SQM. Two of those projects are mainly located near medical centers in the area with a supply average price between $5,000 and $ 5,500 per SQM. BCD came in the third place with 4 projects of 25,073 SQM approximately an equal area to Ras Beirut location. In BCD, the majority of projects aren't meant to be sold but to be offered on the rental market. Worth noting that, the average sales price stands actually around $7,000 per SQM for a first floor core and shell. The main clients for new small projects are self-employed persons such doctors and lawyers in addition to local firms.

A Challenging Outlook for the Second Half of 2014 amid Persisting Instabilities

Up until now, investors in the real estate market have been optimistic and eager for a brighter political outlook in the coming period. It was obvious in the first half of 2014 when the long awaited Cabinet formation took place and the security plan imposed by the latter stabilized the quavering situation. Even though security stability reigned for a limited time, June was mostly branded by a presidential vacuum, several wage-hike strikes, and security disruptions. This led the total number of real estate transactions to drop in June by 4.1% y-o-y.

The real estate sector in Lebanon witnessed in 2013 sluggish activity due to the local and regional political uprisings as well as the inconsistent market conditions reflected by a dwindling demand, incompatible supply and stagnant prices. Accordingly, the unsold supply stock witnessed continuous rises especially with a slackening demand from Lebanese expatriates, foreign nationals, and Syrian refugees, insufficient to absorb all the stock available on the market.

Therefore, real estate in Lebanon is going through a period of stagnation despite the positive signals revealed in the beginning of 2014 or the negative ones recorded a year earlier. The intensification of security developments in the country in addition to the ongoing domestic political deadlock concerning the presidential elections would weigh on the economy and particularly on real estate.

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