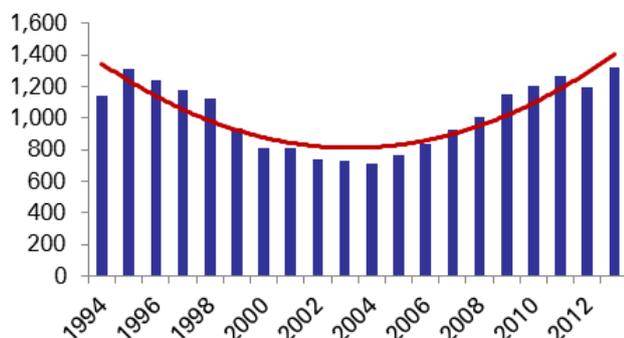




Cement Consumption per Capita (In kg/capita)



Source: Banque du Liban, World Bank

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2013 was one of the most challenging years of the Lebanese cement industry's 80-Year of history. Domestically, numerous gridlocks painted the political scene and several security incidents have shaken investment appetite. Regionally, the 3-Year ongoing war in the neighboring Syria kept on hindering the overall economic performance of the country with the International Monetary Fund (IMF) anticipating Lebanon's real GDP growth at a marginal 1% in 2013.

Contrarily to expectations, the cement sector showed a 9.8% yearly growth in the number of cement deliveries to 5.83M tons despite the slowdown in real estate and construction activities. This is probably explained by higher public spending, previously licensed projects and illegal construction.

Despite the several challenges faced over 2013, the sector was one of the few industries able to survive thanks to the strong fundamentals and the high level of expertise. Total production capacity hovered around 6.47Mt in 2013, compared to 6.32Mt recorded in 2012.

Cement Market Suppliers

The Lebanese cement market is fully dependent on local production. Due to the high cost of cement shipment, international firms find it more profitable to build new plants in the targeted countries which help them in reducing their costs and achieving their diversification strategy.

The cement market in Lebanon is oligopolistic in structure. Cement supply is provided by 3 main cement plants: Cimenterie Nationale S.A.L. grasps the biggest market share, accounting for 41.7% of total cement sales in 2013 and producing grey cement only. HOLCIM (Liban) stands in the second place with a 36.9% stake and offering both types of cement, grey and white, as well as ready mixed concrete. Finally, Ciment de Sibline S.A.L posted a 21.4% market share in 2013 and produces only grey cement.

HOLCIM saw its market share decrease in 2013 following faster increases in the yearly sales of its 2 main competitors: Cimenterie Nationale and Ciment de Sibline. In details, Cimenterie Nationale's sales for 2013 reached 2.40Mt, up by 14.3% from 2012's level. As for Ciment de Sibline, sales went up by an annualized 8.8% to 1.23Mt by the end of 2013. Finally, HOLCIM's aggregate sales, combined with its subsidiary Société Libanaise des Ciments Blancs (SLCB), totaled 2.12Mt in 2013, up from 2.00Mt recorded a year ago.

Accordingly, sales to production ratio ranged between 80% and 100% pointing to the fact that the majority of the Lebanese cement supply was liquidated. This can be considered as a healthy sign for the industry's perseverance and productivity.

Contrasting with the improving local demand, Lebanese cement exports were cut in half in 2013. Lebanon exports cement to a number of Arab states, namely Syria. Accordingly, the Syrian war heavily hit Lebanese exports that tumbled 44% to 285,205Mt in 2013, as compared to 509,488Mt in 2012. Cimenterie Nationale exported in 2013 a marginal stake of its production to Syria, Libya and Egypt. HOLCIM also revealed minimal export activity to Syria and northern Cyprus, where the company took over Bogaz Endustri Madencilik (BEM). However, Ciments de Sibleine mainly focused in 2013 on satisfying the local demand.

Despite the negative performance of cement exports in 2013, local producers managed to liquidate their production in the domestic market. This helped them in maintaining their profits given that local price is almost the double of export price. Worth noting that cement exports have a much lower value than locally sold products as the big volume of exports helps in reducing the marginal cost.

Pillars of Demand in the Cement Industry: Real Estate and Construction

Cement is at the heart of construction and real estate activities. Accordingly, any increase in the number of construction permits should lead to a rise in the demand for cement. Worth noting that permits are usually issued at least six months after applications are filed. Additionally, investors' appetite in owning Lebanese properties can be measured thanks to the variation of real estate transactions.

First, the real estate sector showed a slowdown in 2013. A weak investment sentiment was coupled to a frailer demand from GCC countries as the latter switched to more secure areas. The property sector recorded a 7.9% y-o-y slip in the total number of real estate transactions to reach 70,476 in 2013, compared to 75,954 transactions in 2012. Foreign demand also tumbled with the volume of sales to foreigners decreasing over the same year by an annual 7.7% to 1,278 transactions. In addition, total value of property sales transactions retreated by 2.6% y-o-y to reach \$8.71B by 2013, up from \$8.94B in 2012.

The neighboring war in Syria also took its toll on real estate activity sending construction permits, an indicator of future demand for cement, down by 12.0% year-on-year (y-o-y) to 12.92M square meters¹ (sqm). According to the latest data released by the Orders of Engineers in Beirut and the North, the number of issued permits declined from 18,193 in 2012 to 16,724 in 2013. Worth noting that the average area per permit has also decreased by approximately 11.0% to 775 sqm/permit in 2013, as developers were more twisted towards smaller plot projects alluding to a smaller consumption of cement derivatives.

Yet, the Ministry of Interior and Municipalities (MOIM) announcement by mid-2013 boosted construction in several regions without permits. In details, MOIM handed over the crackdown of illegal construction activity to the municipalities. Given the lack of authority within municipalities, illegal activity surged for almost 3 months when the MOIM intervened again to suppress illegal projects.

Though, construction loans went up by 12.8% y-o-y to \$9.18B in 2013 following the stimuli of Banque du Liban and the financial sector to boost demand and consecutively economic growth.

Government Infrastructure: Another driver of cement industry

New governmental projects were almost inexistent especially with the political divide that marked 2013 and the Cabinet formation dilemma that persisted for more than 10 months. This directly impacted infrastructure projects as public works were automatically postponed waiting for a political breakthrough.

¹ Construction permits reflects the investors' expectations of real estate activity in the coming 6 months

However, an ongoing expansion and restoration project at the Port of Beirut took place over 2013. It has definitely contributed in the cement deliveries yearly growth. HOLCIM won the tender and immediately positioned a mobile plant at the site and took immediate action.

Stagnant cement prices amid slowing property sector

Despite the slowdown in real estate activity, cement prices preserved their average prices supported by the Lebanese government. The price of cement remained almost fixed, with a slight uptick of 2% to \$94 per ton - without VAT - for the grey cement, and almost a 3% slip for the white cement to average \$173 per ton - without VAT-.

Cement prices stood unchanged in 2013 despite the decreasing cost of energy. Prices in the cement sector go hand on hand with energy prices given that cement production is one of the most energy intensive industries². Accordingly, any variation in the prices of energy products will be highly reflected in the upcoming trends of cement prices and vice versa. In 2013, energy prices revealed a declining trend that should have triggered down Lebanese cement prices. Thus, cement production variable cost dropped by an average of 12% y-o-y to settle around \$39. According to HOLCIM, the total cost of production in 2013 has increased, despite the downtick in variable costs, which could be partly explained by respective hikes in raw materials' prices, wages and salaries or even due to inflation.

Average Price of Cement in Selected Countries

Country	Price (In \$ per ton)
Egypt	105
Jordan	99
Lebanon	92
Kuwait	70
Qatar	70
Oman	69
KSA	64

Source: BLOMINVEST compilation

The Lebanese cement companies managed to maintain prices reasonable when comparing to other regional countries that profit from subsidized energy products and cheaper working force. Prices hover around \$105 per ton in Egypt, \$95 per ton in Turkey, \$99 per ton in Jordan and \$64 per ton in Saudi Arabia. This reflects that any overflowing supply of Lebanese cement can be easily exported to Arab countries in shortage with cement supply. Dubai can be a potential client in the coming period with the booming real estate projects related to the 2020 World Expo.

Local cement suppliers profit from the government regulation related to cement imports that aim to protect the locally produced cement from foreign competition. In details, the government has not granted cement import licenses since 2001 and has imposed prohibitive tariffs on imports of cement derivatives that can reach up to 75% for grey cement, clinker and related products and 25% for white cement. The government decision is explained by the fact that the local supply exceeds by far the local consumption making imports unnecessary.

² Each tone of cement produced requires 60 to 130 kilograms of fuel oil or its equivalent, depending on the cement variety and the process used, and about 110 KWh of electricity

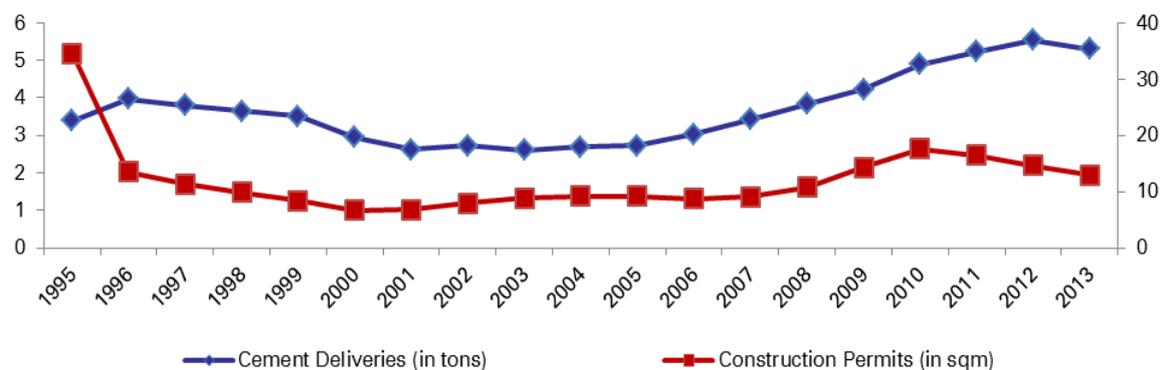
Performance of the industry over the past 2 decades

Activity on the Lebanese cement market floated over the past 20 years relatively to the country's economic and political position.

The development of the industry started in 1995 when demand for cement witnessed considerable growth reflecting a growing urbanization. Large-scale reconstruction projects were initiated after the Lebanese war such as buildings and infrastructure. Lebanon had a considerably high level of cement consumption per capita at 1,309 kg/person compared to lower levels of 900 kg/person in Saudi Arabia, 620 kg/person in Jordan and 313 kg/person in Egypt³. Cement companies saw their total production absorbed by local market with cement deliveries rising by 17.1% y-o-y in 1995 to 3.97Mt, up from 3.39Mt in 1994.

When closely monitoring the period 1996-2000, cement producers suffered repetitive Israeli attacks on the Lebanese lands especially "Operation Grapes of Wrath" in 1996 that targeted south Lebanon and the Bekaa. Hundreds of Lebanese were displaced after their homes were completely ruined and their lives became in danger. New real estate projects were canceled as investment sentiment touched its lowest levels given the high degree of insecurity that overshadowed the period. Construction permits revealed their steepest yearly decline of 61% from 34.53M sqm in 1995 to 13.49M sqm in 1996. Local demand for cement followed the same path, yet at a slower path. Cement deliveries went down from 3.81Mt in 1996 to 2.62Mt in 2000. Cement consumption per capita drastically decreased by 34.7% in 2000 to reach a low of 810 kg/person.

Cement Deliveries and Construction Permits



Source: Banque du Liban, Blominvest Bank- Research Department

Construction activity started recovering in 2001 on improving political stability and despite the persisting economic difficulties. The Lebanese government was finding it difficult to finance its deficit as the balance of payments turned negative, and gross international reserves declined. In addition, Lebanon faced over the same period a fiscal deficit of \$2.8B (16% of GDP) as well as a vicious cycle of rising national debt and dwindling economic activity. However, the political stability and especially the withdrawal of Israeli troops from Southern Lebanon led reconstruction and restoration activities in the South and Bekaa to boom. Meanwhile, the reigning security over the period helped local and foreign contractors resuming their projects and initiating new plans widely diversified across the country.

The industry gained momentum during 2002-2006 revealing a 3.9% CAGR in cement deliveries. The unsustainable economic situation in Lebanon was reversed by Paris II conference in November 2002, which gave a boost of energy to the cement industry. Cement deliveries and construction permits went up by respective 3.8% and 11.5% in 2003.

³ Flemings, 1996

The 3Y period going from 2007 to 2010 reflected the prosperous period that emerged after the Israeli war of 2006 and the withdrawal of Syrian troops in April 2005. Demand for cement surged following the boom in real estate projects. Cement companies delivered in 2010 more than 5.20Mt of cement in the local market, up from 3.83Mt in 2007. As for the consumption per capita, it surged by 30.0% over the 3Y time frame to hit 1,205 kg/person.

The eruption of Arab Spring did not fully impact cement deliveries in 2011, while the Syrian war weighed over the sector's performance in 2012. In details, cement deliveries rose by 6.1% y-o-y in 2011, yet at a much slower pace than years earlier. Exports to Syria were almost cut in half over the same period at 222,065 tons compared to 464,201 tons in 2010. This was due to the emergence of war in Syria by mid-2011. Spillovers of the Syrian war on the Lebanese economy in 2012 sent cement deliveries down by a yearly 4.3% by the end of 2012 to 5.31Mt. However, the cement industry's resiliency and strong fundamentals helped the sector recovering in 2013.

Prospects of Growth

According to Cimenterie Nationale, the Lebanese cement sector will remain highly impacted by the economic and political situation of the country. As for 2014, the total production of the sector is projected to settle around 5.88Mt. Medium term prospects appear to be gloomy over the coming five years and total production of cement may witness a slip to 4Mt, unless smuggling to Syria resumed. Activity in the industry will probably pick up over the long term as the settlement of the Syrian situation as well as infrastructure projects such as dams and road networks may boost the sector's performance. Lastly, Cimenterie Nationale intends to boost its production capacity by 2Mt by 2017.

HOLCIM Liban is currently postponing any future plan of expansion as the company is waiting for its recently-announced merger with Lafarge to be completed early 2015, noting that the latter is operating in the neighboring Syria since 2010.

Meanwhile, Ciment de Sibline upgraded its production line in 2013 by increasing the production capacity from 30 tons per hour to 40 tons per hour.

When considering the whole cement sector in Lebanon, the market is expected to maintain strong footing. Projections remain strong about a flourishing Lebanese building materials industry once the war in Syria ends and the reconstruction phase begin. According to the UN's Economic and Social Commission for Western Asia forecasts, the demand for cement in Syria will hover around 30Mt per annum, or 3 times the level of demand prior to the conflict. This demand will be satisfied by imports from the neighboring countries, mainly Lebanon and Jordan.

Finally, the industry has strong basics but still needs to invest in more efficient production capacities in order to meet the growing competition on the markets.

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