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HIDDEN OPPORTUNITIES IN THE LEBANESE ECONOMIC SECTORS

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I. Agro-Industry in Lebanon: Looming Potential Restrained by Numerous Deficiencies

Combining agricultural and industrial techniques, agro-industry in Lebanon is a developed sector with promising outlooks. The sector encompasses several sub-industries of which olive oil, spirits, dairy products, canned vegetables, confectionery, juices etc... Several opportunities reside within this sector as the latter is almost immune to the local and regional uprisings. Despite the negative spill overs of the Syrian war on the overall Lebanese economy, agricultural products' manufacturing posted satisfactory performance. First, the interruption of exports' transportation through the Syrian border did not negatively impact agro-industrial external activity as some importing markets of Syrian food products shifted their demand to neighboring countries such as Lebanon to compensate for the decrease of Syrian exports. Second, the Syrian crisis attenuated the Syrian competition in the Lebanese market and boosted Syrian refugees' demand for the Lebanese goods. Great potential for development resides within the agro-industrial activity, yet more investments are needed to realize economies of scale thus boosting productivity and reducing costs.

- Agro-industry is the largest industrial sector in Lebanon and the one that employs the most
- Around 54% of production goes to domestic consumption, while the rest is exported.
- Lebanon's food manufactured products are attracting foreign demand more than the country's raw agricultural products thus gathering higher revenues.
- Cheap skilled-labor is available in Lebanon, which renders Lebanon to be more competitive on the regional level
- Presence of backward linkages with a solid and diversified agricultural sector
- Institutional support from the government: Institutions available for testing and R& D (including 3 Labs) and a vocational school specialized in food industries
- Presence of an internationally recognized Lebanese cuisine

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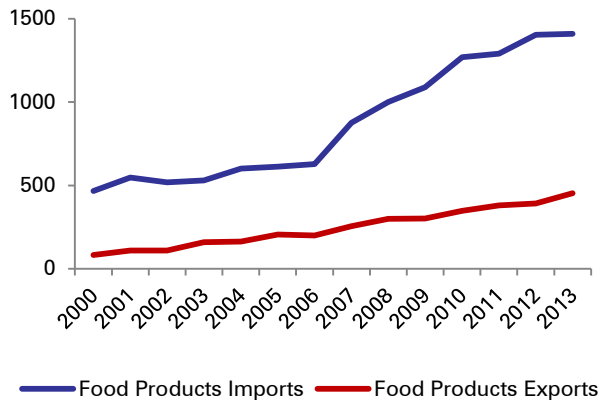
Agro-Industry in Lebanon: Looming Potential Restrained by Numerous Deficiencies

Food Manufacturing External Activity since 2000



Source: The Syndicate of Lebanese Food Industrialists

Total Industrial Exports (In $M)

Source: Ministry of Industry

Agro-Industry Overview

Combining agricultural and industrial techniques, agro-industry in Lebanon is a developed sector with promising outlooks. Despite its several competitive advantages, the sub-sector, that is mainly based on food production and processing, needs rehabilitation and support.

Agro-Industry in Lebanon benefits of a significant economic standing since it is the largest industrial sector. Regardless of the timid 2.2% share in 2011's Gross Domestic Product[1] (GDP), the sector almost contributed to 26.3% of the industrial sector's value added over the same year. Additionally, the food processing sector had an estimated workforce[2] of 20,607 in 2007, constituting the highest share of the industrial sector total workforce at 25%.

Even though the sector revealed a positive economic performance, agro-industrial activity remained sluggish. While the CAGR of GDP stood at 9.1% between 2004 and 2011, the sector broadened at a CAGR of 4.2% with a value added hovering around $1.13B in 2011 compared to $814M registered in 2004.

Despite the negative spillovers of the Syrian war on the overall Lebanese economy, agricultural products' manufacturing posted satisfactory performance. First, the interruption of exports' transportation through the Syrian border did not negatively impacted agro-industrial external activity as some importing markets of Syrian food products shifted their demand to neighboring countries such as Lebanon to compensate for the decrease of Syrian exports. Second, the Syrian crisis attenuated the Syrian competition in the Lebanese market and boosted Syrian refugees' demand for the Lebanese goods.

Agro-Processed Food Prices in Lebanon

Prices in the agro-food industry were mainly following international trends and partly influenced by the domestic and regional developments. The Food and Agriculture Organization's (FAO) annual Food Price Index indicated that 2008 and

[1] According to CAS National Accounts of 2011
[2] According to the Ministry of Industry , The Lebanese Industrial Sector Facts & Findings 2007

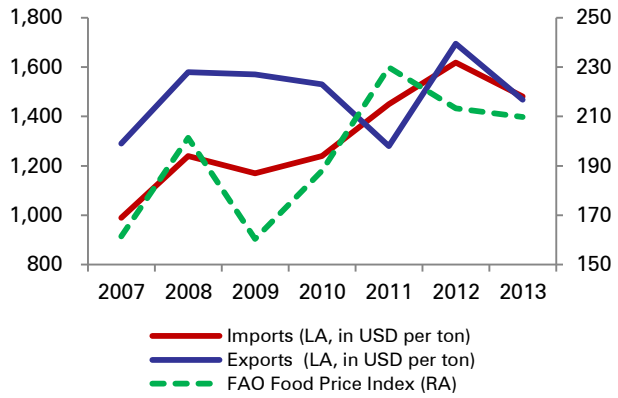
2011 were 2 years of noticeable worldwide increases in food prices by 25% and 22%, respectively. In Lebanon, this was translated by respective 22% increase in export prices in 2008 to $1,580 per ton. In contrast, 2011 saw an opposite path with food prices slipping by 16% to $1,280 per ton. This could be explained by the Arab spring emergence in 2011 that heavily influenced Arab demand for the Lebanese agro-industrial products, sending their prices down despite the global growth.

On a comparable scale, Lebanese food products struggle to remain competitive. First, several regional countries heavily subsidize the majority of their exported goods or their production costs (marketing, internal transport, freight and oil costs). This could have a distorting effect when world prices are already low which will worsen prices. This is explained by the over-production in those countries resulting from the subsidies. Accordingly, not all free trade agreements are beneficial to Lebanon but in contrast could cause severe damages to the sector when the cost of production in Lebanon is higher than that in some other countries.

Food Products' Price per ton (in USD)

	Imports	Exports
2007	990	1,290
2008	1,240	1,580
2009	1,170	1,570
2010	1,240	1,530
2011	1,450	1,280
2012	1,618	1,695
2013	1,481	1,468

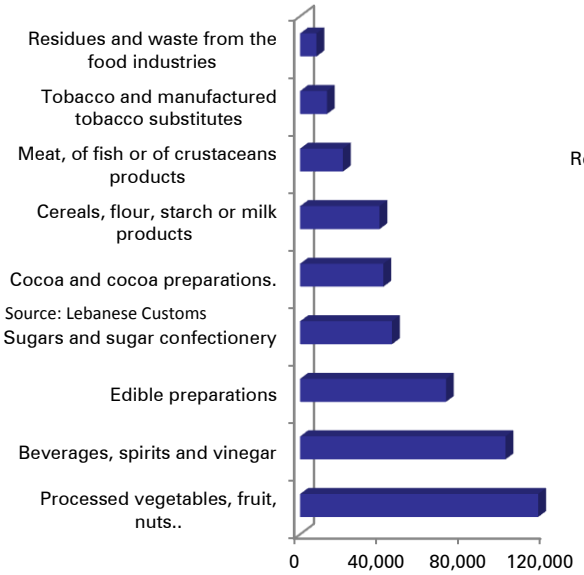
FAO Food Price Index and Lebanon's Food Imports and Exports Prices



Source: The Syndicate of Lebanese Food Industrialists, FAO, BLOMINVEST Research Department

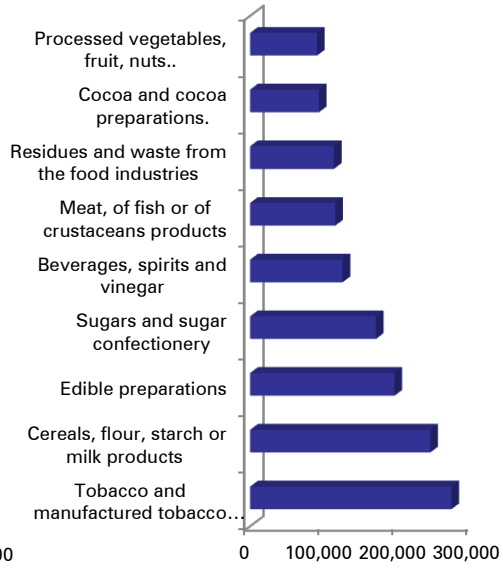
Agro-Industrial Products in 2013 (In Thousands of USD)

Total Exports



Source: Lebanese Customs

Total Imports



Source: Lebanese Customs

Production within the Agro-Industrial Sector

The Lebanese food industry provides its production to both local and foreign markets. Food products exported in 2013 amounted to $452.80M, almost 46.0% of the year's total estimated production. This leaves the remaining 54% of 2013's estimated production for domestic consumption.

Lebanon's food manufactured products are attracting foreign demand more than the country's raw agricultural products thus gathering higher revenues. While the Lebanese agricultural exports almost constituted 0.5% of 2013's estimated GDP and 5.5% of the year's total exports, agro-industrial products posted a higher 1.0% stake of the same year's GDP and 11.4% of 2013's total exports.

The main exported products were preparations of vegetables, fruits, nuts (25.6% of total agro-industrial products) followed by the Beverages, spirits and vinegar category (22.1% of the total). Edible preparations (including soups, syrups. ice cream, and extracts, essences and concentrates of coffee, tea or mate etc...) came third revealing a 15.7% stake.

Arab countries remain the main importers of Lebanon's agro-industrial products. Saudi Arabia topped the list with a total value of $69.00M in 2013 compared to $62.93M in 2012. Syria came second at $55.02M, up from $51.64M in 2012 mainly due to the disruption of agro-industrial activity in the war-ridden country. Iraq and the United Arab Emirates (UAE) respectively imported $51.44M and $25.59M in 2013. The former revealed a 146.8% upsurge in value and 257.9% in volume, while the latter saw a 40.5% in value and 27.5% in volume. This alludes to the mounting number of trade ties between Lebanon and Iraq as well as the UAE.

In line with the improving status of exports, food imports were also on the rise. While 2013's value of imports barely inched up by a 0.5% year-on-year (y-o-y) to $1.40B, the volume of processed food imported to Lebanon saw a 9.8% y-o-y growth to 866,795 tons. Accordingly, imported food products saw their average price decrease from $1,618 in 2012 to $1,481 in 2013. This was mainly due to the annual 21% similar drop in the average price of beverages, spirits and vinegar as well as sugars and sugar confectionery to $454 per ton and $670 per ton, respectively.

Accordingly, the agro-industrial external activity improved in 2013 yet remains deficient. Food manufacturing external trade deficit stood at $957.39M in 2013, tightening from 2012's deficit of $1.01B. The imports cover ratio stood at 32.1% in 2013 improving from the 28.0% recorded in 2012. In addition, the average price per ton of Lebanese exports dropped by 13.4%, while that of the Lebanese imports fell at a slower pace of 8.5% y-o-y.

Given the modest size of the Lebanese agro-industry, diversity and volume of food production are impressive. The sector encompasses several sub-industries of which olive oil, spirits, dairy products, canned vegetables, confectionery, juices etc...

Olive Oil Industry

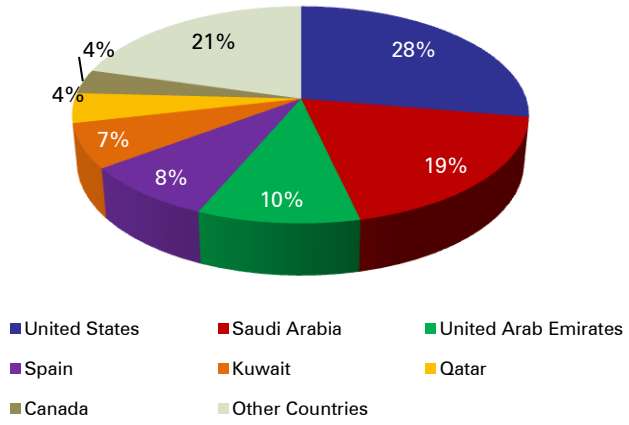
Olive oil, one of the promising agro-industries in Lebanon that is still not up to potential, is gaining more ground on both domestic and international markets. According to IDAL, total olive oil production reached 90,307 tons in 2011, nine times higher than 2000's production.

On the external front, total exports of olive oil surged by 70% y-o-y in 2013 to hit 7,085 tons worth $22.45M compared to 4,163 tons worth $15.24M in 2012. The top 3 importers of the Lebanese olive oil are the United States of America (USA) with a 28% share followed by Saudi Arabia (19%) and the UAE (10%). This is mainly explained by the proliferation of the Lebanese diaspora that heavily uses olive oil as one of its typical ethno-culinary habits.

On a different note, the average price of olive oil slipped in 2013 by 13.5% y-o-y to $3,168 per ton, considerably higher than the average price of imported olive oil that hovered around $2,000 per ton. However, the high level of olive oil local consumption forced Lebanon to import in 2013 additional volumes of olive oil products that reached 5,428 tons worth $10.87M, noting that 98% of the total was imported from Syria.

Worth mentioning that olive oil is one of the few agro-industries to post an external trade surplus in 2013. The mounting status of the Lebanese sub-industry in the markets abroad helped olive oil trade surplus to broaden from $10.16M in 2012 to reach $11.58M by the end of 2013.

Top Importers of Lebanon's Olive Oil in 2013



Source: Lebanese Customs

Despite the noticeable improvement of the sector, olive oil production in Lebanon keeps on facing several difficulties, of which the high cost of production, the inadequate quality as well as the existing competition with imported olive oils that tend to be cheaper.

On a positive note, the trade agreement between Lebanon and the European Union (EU) had a positive impact on Lebanon as olive oil products gained access to the European market besides the regular Arab markets. In details, the agreement allows Lebanon to export 1,000 tons of extra-virgin olive oil to the EU duty-free while allowing the country to impose a 70 per cent tariff rate on EU olive oil.

Numerous projects were initiated to support the promising sub-industry, of which CEDARSplus program (2006-2008) funded by the Cooperative Housing Foundation (CHF) in cooperation with the United States Agency for International Development (USAID). The program promotes the production and marketing of olive oil to meet the increasing demand of international markets.

Another initiative was launched by USAID and LIVCD (Lebanon Industry Value Chain Development) in May this year to develop a seal to certify the quality and origin of Lebanese olive oil. The project will improve the penetration of Lebanese olive oil suppliers into international markets along with rising consumer confidence in the purchased products.

Dairy Products

The Lebanese dairy market is a viable and competitive sector struggling to maintain its vibrant trend. The sub-sector, that remained immune to the ongoing local and regional developments, benefits from a stable to increasing demand for dairy products. This is due to the classification of dairy products as primary goods in the Lebanese culture. However, the sector suffered earlier this year a scandal related to the use of Natamycin[3] by some local producers, a banned substance according to the standards of LIBNOR[4].

[3] Food additive acting as an antifungal agent
[4] Lebanese Standards Institution affiliated with the ministry of Industry

Production within the sector is divided between large scale industrial plants, small scale firms and several rural communities. Taanayel Les Fermes almost grasps half of the local market demand, standing as a top provider of the Lebanese dairy products. Dairy Khoury comes second, followed by Libanlait and Dairyday.

However, a fierce competition takes place among the existing suppliers as the Lebanese market size is relatively small. Marketing strategies and new lines of ice cream and specialized yogurt are implemented to maintain the same level of profit.

Besides local production, external trade within the sector witnessed a strong deficit. Exports barely represented 3% of total dairy imports in 2013. On a positive note, and after 2 consecutive years of declines, exports of dairy products improved by an annual 5.2% to $9.39M in 2013.

The existing players should target markets where labor costs are significantly higher than in Lebanon. However, the critical expiry of such products renders the expansion of export activity riskier.

Several projects were initiated by international entities to support the sub-industry, of which FAO and USAID. In 2011, the LRF-21 dairy project "Recovery and Rehabilitation of Dairy Sector in Bekaa Valley and Hermel – Akkar Uplands" was funded by the Lebanon Recovery Fund (LRF) and executed by the Food and Agriculture Organization (FAO) with direct collaboration and cooperation of the Lebanese Ministry of Agriculture (MOA). The project aimed the sustainability of milk production and the improvement of food safety standards within the dairy industry in specific Lebanese regions.

Another $6.9M program was funded by the USAID renowned as "The Action for Sustainable Agro-Industry in Lebanon" (ASAIL). The project provided extensive technical assistance, marketing, business development and access to finance by Small Medium Enterprises (SME).

Spirits Industry

Winemaking in Lebanon dates back several thousands of years as the country tend to be ideal for industry growth with an estimated market size at $26.4M for 2012. FAO estimated wine production to be near 14,200 tons of wine in 2011, ranking it as the 45th largest wine producer in the world with 0.05% of global supply.

Yet, and contrary to global trends, Lebanon has been paying less for greater quantities of wine. The reason behind this drop is attributed to the decrease in taxes levied on imported wines through Lebanon's adoption of the Euromena Accords. The agreement which aims at the reciprocal phasing out of taxes imposed on wine between Lebanon and Europe has granted the latter easier access to Lebanese markets.

Lebanon exports the majority of its wine to Europe, primarily UK and France. Local wineries should capitalize on trade agreements such as those signed with Europe to penetrate foreign markets at competitive prices. In an attempt to cement their presence in the global wine market, 33 Lebanese wineries participated in Berlin during May this year in the presentation of their wines to distributors and importers from central Europe.

The future success of the Lebanese wine industry dictates a shift in production towards high quality wines. Despite the high entry costs, operating production costs are relatively low (10-25% of retail value), making the investment appealing in the long run. Unable to compete in mass production, Lebanon should establish itself as a niche market catering to wine consumers.

Looking at the Lebanese *beer* market, consumption in Lebanon is estimated at 29M liters annually, placing the country in the 90th position internationally from a basket of 123 countries on a per capita basis. Almaza, the market leader, accounts for 74% of the local market, or 21.7M liters.

The costs associated with the business are discouraging, especially since most of beer key ingredients are imported. Shipping costs are thus added into the equation, along with high electricity bill, customs and taxes that can significantly hurt

the bottom-line. Even bottles are imported as the glass industry, an energy-intensive business, suffers from high utility costs in Lebanon which can only be forwarded to the end-buyer.

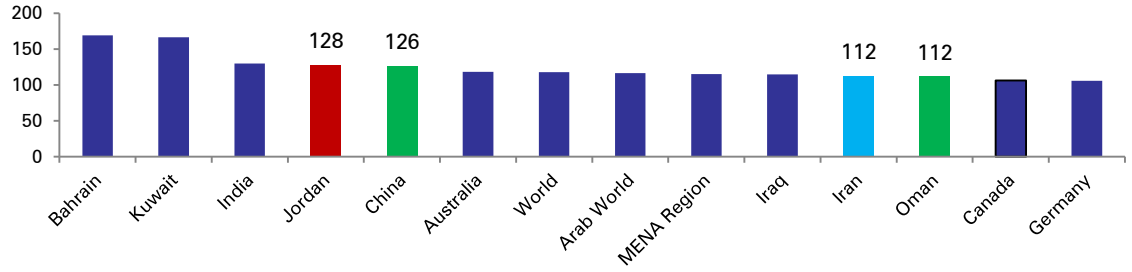
Exports constitute a significant part of the Lebanese brewing business. We estimate Almaza to export roughly 10%, or 2.33M liters annually, to various destinations such as Syria, United States, Turkey, and UAE. Exports allow better profitability since companies are able to charge much more internationally.

When it comes to *Arak*, Lebanon's national drink, assessing the market in Lebanon is almost impossible as the majority of productions is made by individuals. Total production of Arak is estimated to be around 5M to 6M bottles annually[5], with 50% exported abroad. Arak is one of the few products not imported to Lebanon which appears to be a competitive advantage for the country as it could focus on bolstering, besides its local supply, the export activity of its traditional alcoholic drink.

Other problems related to the costs of production, lack of government regulation and illegal competition hinders the sub-sector performance. First, high costs encounter Arak's production as the manufacturing process is long and complex (Arak is triple distilled for better quality). Second, the absence of regulation encourages the proliferation of the arak "baladi" that often does not respect the standards of production, opening doors to imbalanced competition. And third, an intense competition exists with the different types of spirits such as wine and beer and the international drinks such as whiskey, vodka, etc...

As shown by the aforementioned examples, production in the Lebanese agro-industrial sector faces several challenges that keep its evolution below the potential. According to the World Bank, the food production index of Lebanon stood in 2012 at 102, up by 3.9% from 2011 but remaining below the world index of 118 and the 117 of the Arab World. Noting that imports almost constitute 45% of the Lebanese demand for manufactured food products, several opportunities exist and numerous areas of investments are compelling.

Food Production Index in 2012



Source: World Bank

Al Wadi-Al-Akhdar, the canned food giant, managed to bolster its sales thanks to the introduction of a large variety of new differentiated products. The food company is never resting on its laurels but aiming to spread its brand on the global scale mainly where the Lebanese diaspora resides. The leading food brand offers a wide range of Middle Eastern and international food products that can be found all over Europe, Asia, Australia and America.

LibanJus, a market leader in both the juice and ice cream markets, is always upgrading and expanding its business model to boost sales. The firm sequentially introduced Iceberg in 1991, Maccaw in 1999, Uno in 2003 as well as Iceberg milkshake in 2005.

Ghandour is another example. The enduring firm in confectionery and food products is facing international competition mainly from Turkey as the latter's products are relatively cheaper. The company is mainly focusing on penetrating new markets hand on hand with plans to improve its brand image by spreading their marketing campaigns, extending their product lines and remodeling their existing brands such as Dabké, Unica, Pik One, Tarboosh etc...

[5] According to L'Orient le Jour "L'arak : un marché bien portant malgré les defis"

Another big investment was initiated by Kassatly Chtaura, a leading drinks manufacturer that is behind Buzz alcohol drinks and, since 2005, the wine Chateau Ka. Kassatly is to invest up to $15M, through a loan backed by the Central Bank, in the production of 20M liters of beer a year, close to the amount Almaza produces.

When performing well, the Lebanese agro-industrial sector is a promoter of job creation. Several opportunities reside within the sector as the latter is almost immune to the local and regional uprisings. The decision of the Lebanese government to reduce the tax on industrial export profits by 50% will definitely have a positive impact on the external trading activity of the sector.

Finally, great potential for development resides within the agro-industrial activity, yet more investments are needed to realize economies of scale thus boosting productivity and reducing costs.

II. Lebanese Wineries Filling Glasses and Welcoming Tourists

Lebanese wine has been considered an adequate ambassador to Lebanon in foreign countries. Owing to its ideal Mediterranean climate and its varied topography, Lebanon has been a fruitful land for wine-making. With vineyards covering around 2,000 hectares growing more than 21 varieties of grapes, Lebanon produces 8,000,000 bottles of wine annually. This production is divided equally between domestic and foreign consumption. The main destinations of Lebanese wine are UK, France and the US. As for local demand for wine bottles, it stands at 6,000,000 bottles annually, with 33.3% being satisfied by imports. Besides benefiting from the government of agriculture's and Union Vinicole du Liban's (UVL, Lebanon's official association of wine producers) help, most Lebanese wineries, especially the ones having a restaurant, gain from wine tourism.

- Lebanon has been a net exporter of wine in the past 4 years, with a surplus amounting to $4M, in 2014.
- Exports have been increasing in the past 4 years with a compounded annual growth rate of 5.8%.
- Wine imports to Lebanon are subject to a L.P 200/litre alcohol excise and a custom duty of 15% if it is sparkling and 70% if it is still wine.
- The government is planning a new tax reform on exported wine where the government will pay back 50% of the profit tax and the L.P 200/litre alcohol excise on exported wines
- UVL aims at promoting Lebanon as a wine producing country, highlighting its proud history, and promoting its potential.
- Other than the availability of adequate land, the wine industry has no barriers to entry.
- The Lebanese Ministry of Agriculture endorses the wine sector by allocating a slightly higher budget each year. The targeted budget in 2015 is $132,000.
- To promote the Lebanese wine abroad, the Ministry of Agriculture has been holding exhibitions in major cities around the world, under the name of "Lebanese Wine Day"

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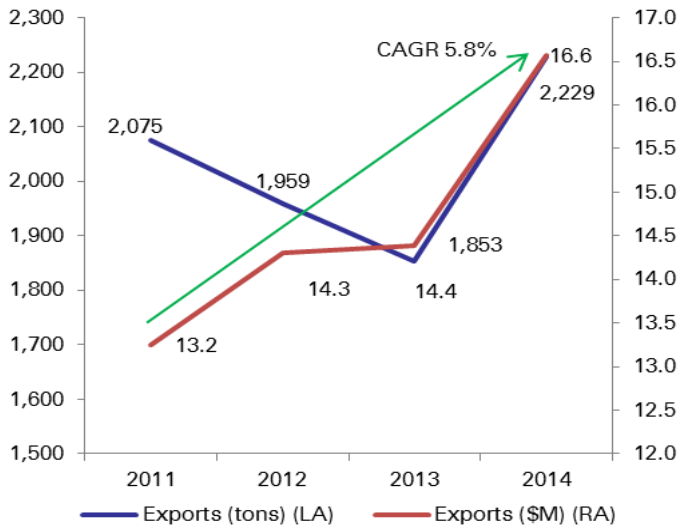
Lebanese Wineries Filling Glasses and Welcoming Tourists

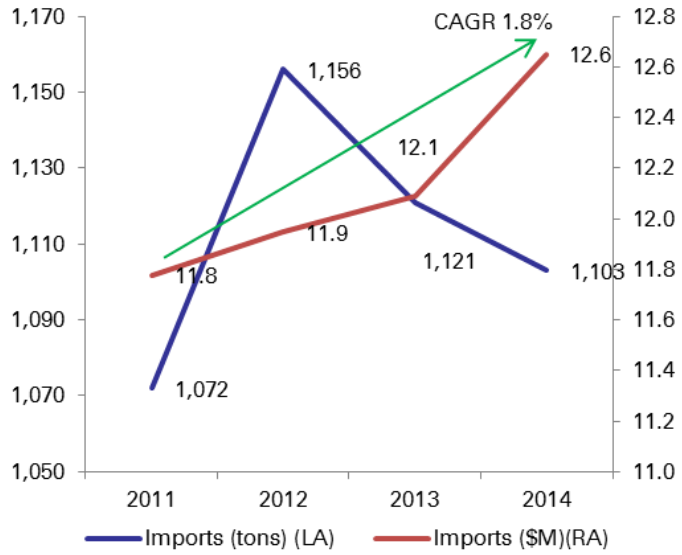
Wine Exports



Source: Customs

Endowed with the ideal Mediterranean climate and a diverse landscape of a sun-drenched waterfront, looming summits and desiccated valleys, Lebanon has long been prolific terrain for vineyards. More than 5000 years ago, the Phoenicians were making wine in Lebanon and trading it throughout the Mediterranean and Europe. The Temple of Bacchus, the Roman God of Wine, in Baalbek stands in testimony to the history of wine in the Bekaa valley. Moreover, it is believed that Christ's first public miracle, where he transformed water into wine, occurred in Cana, South Lebanon.

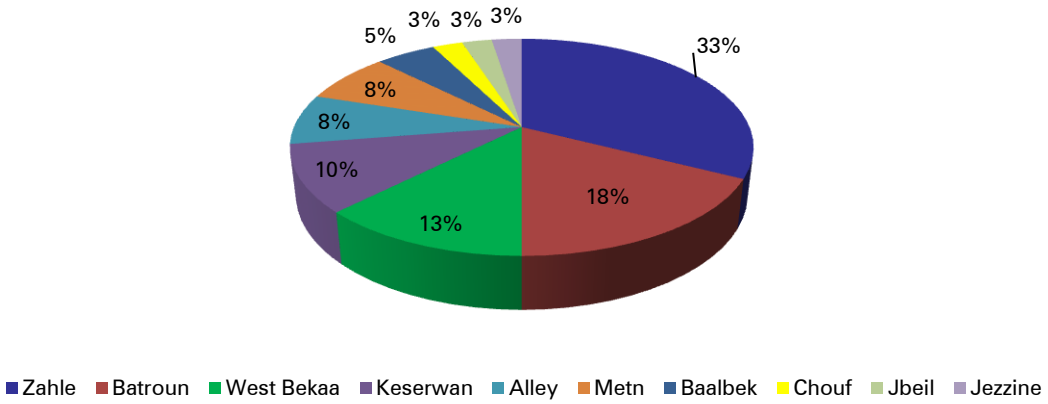
Wine Imports



Source: Customs

The number of wineries in Lebanon has increased sharply since the end of the Civil War, reaching 40 wineries in 2015, compared to only 5 after the war. 33% of the wine producers, or 13 wineries, are located in Zahle, due to the district's suitable "teroire" for wine making.

Distribution of Wineries across Lebanese Districts



Source: BLOMINVEST Research Department

Of the 40 wineries, 19 are members of the "Union Vinicole du Liban" (UVL), Lebanon's official association of wine producers. The prime aim of the UVL is "to consolidate and build on Lebanon's image as a wine producing country by highlighting its proud history and promoting its potential." It deals with governmental and economical institutions when needed to ease wineries' participation in international fairs. With the collaboration of Lebanese embassies abroad, the UVL is participating in international wine events, in which Lebanese wineries exhibit together under the name of 'Lebanese Wine', instead of each individual brand alone.

Lebanese vineyards cover around 2,000 hectares, producing 8,000,000 bottles of wine annually. According to UVL, Chateau Ksara produces around 37.5%, equivalent to 3,000,000 bottles; followed by Chateau Kefraya with 1,500,000 bottles, Chateau Musar with 600,000, Clos St Thomas with 400,000 bottles and 300,000 for each of Chateau Ka and Chateau Massaya. According to chief executive manager of Chateau Kefraya, Emile Majdalani, Ksara and Kefraya are the top providers in the Lebanese market with almost 30% market share each. Mr. Issa, partner at Domaine des Tourelles, stated that his winery grabs 3-4% of the local market.

The following table summarizes the different varieties of grapes grown in Lebanon and used in winemaking:

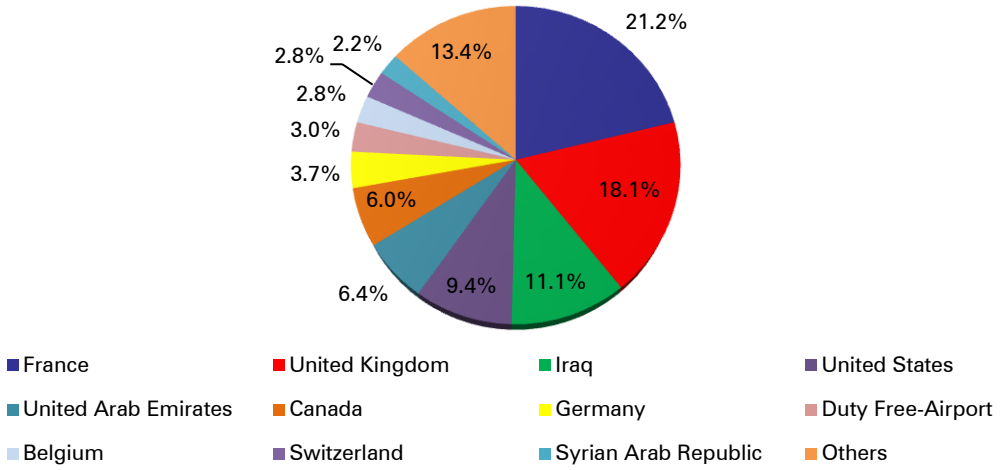
REDS	WHITES
Cabernet Franc is a red grape variety planted in Bordeaux and the Loire Valley that is also popular among the wine makers of north east Italy. A new grape to Lebanon, it is planted both in the Bekaa and in Bhamdoun.	**Chardonnay** is a relatively new arrival to Lebanon but has thrived in the Bekaa terroir.
Cabernet Sauvignon has, in the past twenty years, become Lebanon's most widely planted grape (500 hectares – a quarter of the total area under wine grape vine – were planted between 2000 and 2005) and comprises roughly 40% of the country's wine grapes under vine. It is used by all the major Lebanese wineries in blends and can be found as varietal in its own right.	**Gewürztraminer** is used in Lebanon in extremely limited quantities
Carignan has been used for decades in Lebanon, where, local producers say, it performs better than in France. It gives a beautiful dark hue, good acidity and high alcohol. It is used to structure reds that are destined for ageing as well as rosé wines.	**Clairette** has been a popular grape but is used less these days.
Cinsault has been used to make wine for 150 years in Lebanon and today makes up nearly 35% of Lebanon's total wine grapes.	**Merweh** is a white Lebanese cultivar used in wines and arak.
Gamay is planted in extremely limited quantities for nouveau wines.	**Muscat** is a white grape planted in limited quantities in Lebanon, where it is blended with other varieties.
Grenache is widely used by Lebanese producers, for whom it can give wines with a high alcoholic content.	**Obeidy** is a white Lebanese cultivar used in wines and arak.
Merlot is a popular and important grape in the majority of upper and mid-range wines.	**Sauvignon Blanc** is a versatile, highly acidic, grape used extensively in Lebanese white wines.
Mourvèdre is popular with a few Lebanese producers, who value its ability to contribute to well-structured wines.	**Semillon** is planted in limited quantities in Lebanon.
Petit Verdot is used in limited quantities by those wineries who appreciate that it can contribute significantly to a wine's ageing potential because of its high tannin content.	**Ugni Blanc** was one of the earliest imported white grapes used in Lebanon, where it was used for wines, arak and other eaux de vie.
Syrah is a favourite with Lebanese producers, who value its longevity as well as its aromas and flavours of prunes, spices and berry fruits.	**Viognier** is recent arrival in Lebanon, where it has been blended successfully with Chardonnay, Sauvignon Blanc and Muscat to make premium whites.
Tempranillo is arguably the most important Spanish grape variety and one that is popular with a few Lebanese producers.	

Source: Union Vinicole du Liban

Customs data show that Lebanon has been a net exporter of wine in the past 4 years, with a trade surplus amounting to $4M in 2014. Wine imports and exports have been gradually increasing, however at different paces, where exports recorded a 15.3% increase from 2013's value while imports edged up by only 4.1%.

Of the 8M bottles that Lebanon's wineries produce, 50% are exported, worth $16.6M, at an average price of $4.2/bottle. The major 3 destinations are UK (30.5%), France (15.0%), and the US (11.3%). In terms of tonnage, France imports 21.2% of the 2,229 tons that Lebanon exports, followed by UK and Iraq with respective shares of 18.1% and 11.1%. Worth noting that in 2011, Syria was the third major destination for Lebanese wine, importing 206 tons worth $748,000. Exports to Syria plummeted to 49 tons worth $128,000 in 2014.

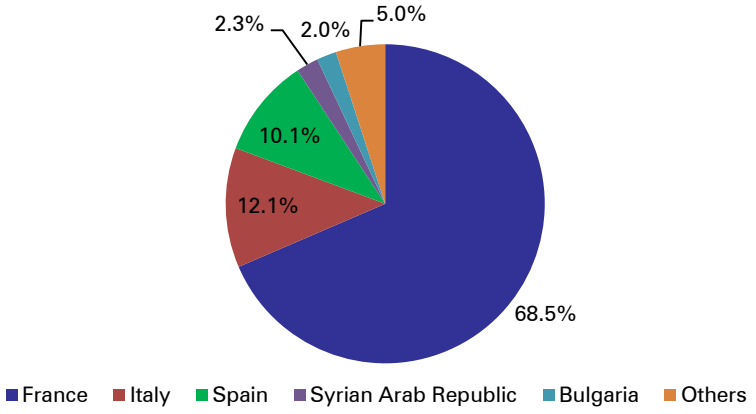
Top Wine Exporters (In terms of tonnage)



Source: Customs

Lebanon consumes 6M bottles of wine yearly, where 33.3% or 2M bottles are imported with an average price of $6.3/bottle. Wine imports, which amount to $12.6M, consist of 65.2% still wine and 34.8% sparkling. 83% of total wine imports, or $10.5M, is imported from France, 8.6% ($1.1M) from Italy, and 2.3% ($294,000) from Spain. In terms of tonnage, Lebanon imports 1,103 tons of wine, of which 68.5% came from France, 12.1% from Italy, and 10.1% from Spain. Worth mentioning that in 2012, Lebanon used to import 38 tons of wine worth $126,000 from Syria. This number plunged to 0 in 2013 and picked up to 25 tons or $72,000 in 2014.

Top Wine Importers (In terms of tonnage)



Source: Customs

The wine industry in Lebanon has no barriers to entry, besides the availability of adequate land. However, Ghida Kassatly Boulos, marketing manager at Chateau Ka, pointed out that even though the market has no barriers to entry, a prospective château faces a huge initial investment and high costs of production. According to several wineries, return on investment in wine production is not achieved before 10-20 years, as it takes almost 5 years to produce the first bottle. Besides the high cost of land and labour, the main burden that wineries endure is the high costs of equipment, barrels, bottles, labels, and cork-stoppers, all of which are imported (due to bad or non-existent local production) and are subject to VAT (10%) and Customs (5%).

The major obstacle that Lebanese wineries face is competition from imported wine. Imported wine holds an advantage over local wine across different consumer preferences. Foreign wine benefits from greater brand recognition and customer appeal. People who are price-oriented would still prefer the foreign wine because it is cheaper than its local counterpart. This was aided by the gradual reduction of customs on European imports until it was completely cancelled in 2014. According to UVL, French wines were the greatest beneficiaries of this customs reform. Therefore, European wine is preferred regardless of price.

Moreover, according to Mr. Issa, small wineries and potential entrants face aggressive competition as powerful wineries dominate the local market rendering an imbalance of visibility. He states: “Small wineries will face difficulties entering the market in the presence of exclusivity and money power.”

Another impediment that Lebanese wineries have been facing is the spill-over effects of the Syrian Civil war. As previously mentioned, wine exports to Syria and other regional markets decreased substantially from 2011 to 2014, partly due to land freight interruption. Furthermore, tourists have been reluctant to visit Lebanon, which in turn led to the decrease in wine consumption.

Lebanon’s wine sector was also affected by the recent European crisis. As the euro depreciated against the U.S. dollar, Lebanese wines became more expensive in the European markets and European wines were cheaper locally. Therefore, Lebanese wine became less competitive.

Despite these hurdles, Lebanese wineries are strengthened by wine tourism. According to its PR manager, Rania Chammas, Chateau Ksara was ranked the 5th touristic sight in Lebanon, as it is the oldest winery in Lebanon and has natural caves. In 1898, Ksara discovered an extensive Roman cave system underneath the winery, which was expanded and repaired to become Lebanon’s only natural cellar system. Other wineries that gain from wine tourism are those with restaurants, such as Chateau Kefraya, Massaya, Domaine des Tourelles and Ixir. Noting that due to the clashes in the Bekaa region, tourists have been reluctant to visit the chateaux there and are showing a greater preference to those in Batroun, as the area is considered more secure. For instance, in its golden years, Chateau Ksara received 75,000 tourists annually who visited its natural caves; this number has dropped to around 25,000 after the security instability.

Furthermore, the Lebanese Ministry of Agriculture endorses the wine sector by allocating a slightly higher budget each year. The targeted budget this year is $132,000, compared to $105,000 last year. To advertise Lebanese wine abroad, the Ministry has been holding exhibitions in major cities around the world under the name of “Lebanese Wine Day”. The first fair took place in Paris in 2013, and was followed by one in Berlin in 2014. This year the “Lebanese Wine Day” exhibition is planned to take place in New York. In addition, one winery mentioned that to increase wine exports, the government is planning a new tax reform on exported wine where the government will pay back 50% of the profit tax and the L.P 200/litre alcohol excise on exported wines. However, this has not yet been put into effect.

Nevertheless, to further promote Lebanese wine, a system, like the one used in France that identifies the originating region of the grapes used in each kind of wine, should be adopted. This is because each kind of grape is influenced by different climate conditions and natural resources which bestow them with a specific taste, characteristics, reputation and quality that are distinct from the ones grown in other regions. This would offer vineries, cultivating their grapes in conditions suitable for growing vines, market recognition and often higher prices.

For instance, France applies the “Appellation d’Origine Controlee” (AOC, translation: “controlled designation of origin”) system on its wines, which is a set of very strict rules on the types of grapes grown in each wine region. The set includes restrictions as to the specific geological area where the fruit is grown and the wine was made, along with the type of

allowable grape variety planted in the vineyard. There are also specific, agreed upon production methods, minimum levels of alcohol, vine age and required minimum vineyard planting densities. There are also rules for harvesting and wine-making techniques in place along with restrictions on where the cellars must be located. The reason behind the AOC system is that it is the place where the product is produced that gives the wine its unique character and style.

Lebanese wineries have been trying to find new ways to improve their produce. In 2015, a new wine recipe made solely from purely Lebanese "Obeidy" grapes was launched by local wineries, to create a distinct image for Lebanese wine. In addition, Chateau Wadih was the initiator of the probiotic wine, red wine with probiotic substance that protects the liver from the effects of alcohol and stimulates the immune system, without affecting the wine's taste. Outside Lebanon, only one winery produces a probiotic blend, which learned the method from Dr Bou Younes, owner of Chateau Wadih.

Finally, all wineries agree that before endorsing Lebanese wine in foreign markets, Lebanese citizens should have a stronger national feeling and consider their country's wine as a national pride. Lebanese wine has been considered as an adequate ambassador to Lebanon in foreign countries. However it is time for Lebanese wineries and their products to achieve similar levels of acknowledgement and recognition inside their own country's borders.

III. Olive Oil: The Bittersweet Taste of Lebanon

Olive trees occupy an area of 56,300 ha in Lebanon, growing 10 varieties of olives. Olive orchards extend from North to South of Lebanon, with 41% of olive oil production taking place in the North, 21% in Nabatieh, 15% in the South, 13% in Bekaa, and 10% in Mount Lebanon. Each region offers its produce a special taste native to the specifics of its land. Olive trees do not need a lot of care as they are mostly rain-fed, and rainfall is relatively abundant in Lebanon. 70% of olive production is destined to the production of olive oil, while the remaining is destined to the production of table olives. The productivity of Lebanese olives ranges from 18-25%. The Lebanese olive oil market is highly competitive with 544 registered oil mills and 110,000 olive farmers and growers. Demand for olive oil in Lebanon is estimated to be around 4.5 kg/person/year, which amounts to 18,000 tons per year. This is serviced predominantly by Lebanese oil, which is sold at premium prices. There are growth opportunities in the olive oil sector due to higher awareness that will attract customers towards high-end product.

- Oil cooperatives offer milling services to farmers at 10-20% reduction in price compared to private service mills.
- Cooperatives succeeded in attracting foreign funds to the olive oil sector.
- Lebanon has been a net exporter of olive oil for more than 5 years, with a surplus in the trade balance of $8.99M in 2014.
- Olive oil imports from countries other than the Arab market are subject to a 70% custom duty and a minimum fee of L.P. 6,000 per litre. Imported olive oil from the EU is still exposed to this tariff, even after the removal of custom duties on European imports
- Lebanon can export to the EU up to a quota of 1,000 tons with a 100% reduction on custom duty and ad valorem tax. However, exports of Lebanese olive oil to the EU are much less than 1,000 tons. Hence the opportunity to export more.
- Demand for high quality extra virgin olive oil increased throughout the years due to higher consumer awareness regarding positive attributes of extra virgin olive oil
- The hike in the price of olive oil encouraged olive oil suppliers to take better care of their orchards and increase their production.

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Olive Oil: The Bittersweet Taste of Lebanon

Main Types of Olives Grown in Lebanon

Soury/Souri/Sourani	**Found primarily in the North and in the Mount Lebanon area with a medium and alternate productivity**
	Used for producing good quality oil
	Characterized by its medium to high oil yield
Samakmaki	Grown in the South
	Distinguished by its small sized fruit that ripens late
Airouni/Ayrounis/Little Soury	Very widespread
	Characterized by its small fruits which give a very low yield of peppery oil
Baladi	Found extensively in the North
	Mistaken for the Soury
Chami	Originated in Damascus
	Characterized by its early ripening which is suitable for table olives
Edlebis	Originated from the region of Edleb in Syria

Source: USAID Report

Spirituality appears to flow through the branches of the olive tree. It has been used as a religious symbol of peace, life, fertility, and renewal. In ancient Greece, courageous soldiers were honored with a crown made of olive twigs. The first Olympic torch was a burning olive branch. Romans used this branch as a symbol of peace and the tree was considered so sacred that those found guilty of cutting one down were condemned to death or exile. In the temples of Baalbek, in Lebanon's Bekaa Valley, olive oil was offered to the gods at the end of a good harvest to give thanks. Moreover, in 2000, olive groves were planted right up the barbed wire border with Israel, after the latter withdrew from Southern Lebanon, after an 18-year occupation. Liberation, rebirth, renewal, and peace can be symbolized by the olive tree.

Lebanon is renowned for its opulent olive orchards dating back centuries. The northern villages of Amioun and Bshaale are home to some of the oldest olive trees in the world, many of which date back at least 1,500 years. Although the origin of the olive tree is still unidentified, some theories suggest that the olive was first cultivated on the shores of the Mediterranean along the coasts of Lebanon and Palestine, and the Phoenician settlements were the first to domesticate and adapt the wild olive tree to cultivation. As far back as 1600 BC, Phoenicians introduced the olive tree to Greece and then to Italy, France, Spain and finally North Africa.

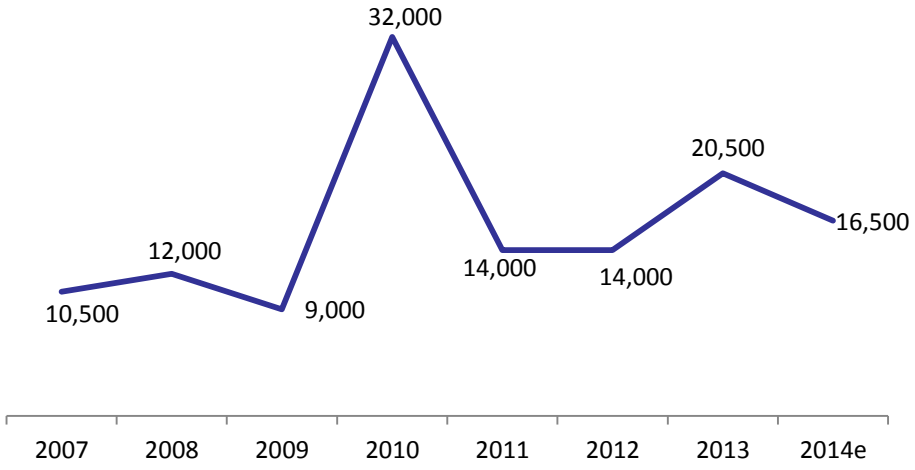
Olive trees occupy an area of 563 km^2 (56,300 ha) in Lebanon, which represents 5.4% of the country's territory, or 8% of total agricultural lands. Olive groves are grown in 6 major regions, extending from North to South: Batroun, Koura, Zgharta, Akkar, Rashaya el Foukhar, and Hasbaya, in addition to several other subordinate areas. More specifically, around 41% of olive oil production takes place in the North, followed by Nabatieh with 21% of total production, 15% in the South, 13% in the Bekaa, and 10% in Mount Lebanon. Each region offers its produce a special taste native to the specifics of its land. There are about ten olive varieties grown in Lebanon, which produce high quality, flavorful oil.

Lebanon's olive trees are on average 150 years old and are mostly rain-fed. Only 8% of the olives cultivated area is irrigated. This is mainly due to the fact that rainfall is relatively abundant in the country at an average of 2.2B m^3 per year. Around 70% of the olive production is destined to the production of olive oil, and the remaining is destined to the production of

table olives. The oil productivity of Lebanese olives ranges from 18-25%. Additionally, as a rule of thumb olives harvested in October and November produce higher yields than those harvested earlier or later in the season. The milling process also affects yields: modern mills extract between 8-12% more oil from the olive at each stage, including oil that must be refined, and pomace oil.

Lebanon's olive oil industry is worth $70M, with an average annual production estimated to be around 20,500 tons. This market is highly competitive, with around 544 registered oil mills in Lebanon, and 110,000 olive farmers and growers. However, full-time farmers, whose only occupation is cultivating olive trees, are only 340. Many families own a small piece of land of at least 1,000 sqm, and use it to cultivate oil for extra revenues.

Yearly Olive Oil Production in Lebanon (in tons)



Source: International Olive Oil Council

There has been an evolution in the production of the Lebanese olive oil throughout the years. Between 1990 and 2007, olive oil production range between 2,000 tons and 8,000 tons. It began rising starting 2007, with an observable jump in 2010, reaching 32,000 tons. This hike was mainly due to the increased tourism activity that Lebanon experienced through that year, which was satisfied by locally produced olive oil and foreign olive oil bottled in Lebanon. Olive oil production remained growing in the past 4 years, due to the increase in demand and price. As consumers are now more informed about the benefits of organic and extra virgin olive oil, demand for this commodity increased. Moreover, the hike in the price of olive oil encouraged olive oil suppliers to take better care of their orchards and increase their production.

There are many estimates of the olive oil production in Lebanon with a large discrepancy between different sources. In particular, the quantity produced in 2010 shows the largest divergence. While the International Olive Oil Council states it to be 32,000 tons, FAO estimates it at 20,000 tons and the US Department of Agriculture approximates it at 14,000 tons.

Olive oil production varies from one year to another, due to the variability of the productivity by nature of the crop, as well as the current practices of the farmers. In high production years, olive trees can yield around 22,000-23,000 tons. This number drops to 18,000-19,000 tons in low production years.

According to Mr. Sleiman Daher, President of the Olive Producers Cooperative in Zgharta, the variability of olive oil production from year to year is due to the fact that olive trees are rain-fed. According to a study done by him, the yield of the olive tree would increase by more than 10 times, from 7 kg to 100 kg, if the tree was irrigated instead of only depending on rain.

Different qualities of olive oil can be produced, the best being extra virgin olive oil. Extra virgin olive oil should be produced by olives that are free of any disease, harvested at the right time, and processed immediately. If the olives are picked from the ground instead of the tree, the quality of the final oil is compromised. No chemicals should be added to the oil, and the final oil has to pass a large number of tests and meet a range of strict standards, to be considered extra virgin.

Qualities of oils Derived from Olives

	Origin	Oleic Acid	Peroxide Content
Extra Virgin Olive Oil	Zero defects, derived from olives using only mechanical process - no solvents	less than 0.8g/100g	less than 20
Virgin Olive Oil	derived from olives using only mechanical process - no solvents	0.8-2g/100g	less than 20
Blended Olive Oil	Blended virgin and refined olive oil	2-3.3g/100g	less than 15*
Refined Olive Oil	Oil obtained from low quality virgin olive oil through refining process	0.3/2g/100g	less than 5*
Olive Pomace Oil	Extracted from olive husk after milling. Inedible oil.	1g/100g	less than 15

*Refined oils and oils blended with refined oil have a lower peroxide content due to the refining process
Source: International Olive Oil Council

Olive oil producers in Lebanon vary in size. The smaller the size of the land is the more the practices adopted are traditional, leading to lower efficiency and productivity.

Around 77% of olive producers are small growers, managing olive orchards of 5,000 sqm or less. These producers usually work on their own land, and follow traditional production and orchard management practices. Their produce is mainly consumed by the households and sometimes distributed to friends. In some cases, excess oil is sold to mills or other customers and suppliers.

Medium growers have larger orchards between 6,000-10,000 sqm. Farmers in this category implement better agricultural practices and professionally manage their land, incurring a higher production cost per hectare. A fraction of growers do not actually work on the land themselves, and instead hire people to manage all phases of production up to harvesting. After their household consumption is removed, medium producers have significant surplus production. Part of it is sold through their personal network of family and friends. What is left is stored for a significant period of time, leading to a degradation of its quality. Unlike many wines, which improve with age, extra virgin olive oil is perishable: like all natural fruit juices, its flavor and aroma begin to deteriorate within a few months of milling, a decline that accelerate when the oil is bottled. This is then sold in larger volumes to olive oil traders or commercial bottlers at a relatively low price.

Large growers, who own fields greater than 10,000 sqm, represent 9% of Lebanese olive farms. The largest areas are owned by large families, religious institutions, or major oil bottlers and traders. These institutional growers are usually highly efficient in managing their orchards. They own machinery and harvesting equipment that reduces their unit cost and increase productivity. Because of their greater efficiency, these large growers produce more than half of total oil produced in Lebanon. Their sales strategies are almost the same as medium farmers: a small initial amount is sold at high prices directly to households with the remainder being sold to traders or bottlers at much lower prices.

Very few large producers have made the required investments in milling technology, bottling, effective branding, and distribution to operate as fully integrated olive production, milling, and bottling enterprises. They apply better and more efficient farming practices; their production is entirely channeled to their own milling and bottling operations, which may also involve purchasing olives from other farmers for milling, as well as olive oil for bottling.

Instead of farming their own orchards, growers or owners have the option to sell their potential harvest to a middleman prior to the actual harvest season. This is known as “Daman”. There are two types of Daman: the middleman does all the necessary work and get the harvest, as if he is renting the land with the olive trees in it. The other type of middleman agrees to purchase the olives on the tree from landowners 1-2 months prior to harvest. If the production is high, the middlemen have more power and can negotiate to pay back one-third of the harvested olive or oil to the farmer. In low

productive seasons, the farmer has the upper hand and can command a higher share of almost 50%, since his product is in higher demand. Harvesting middlemen are necessary actors especially for farmers who cannot afford harvesting and transportation costs that account for up to half the total production costs of olive oil.

After harvesting the olives, the crop is sent to mills. Most of these mills are traditional and privately owned by individuals and companies. If paid in-kind, mills keep 10% of the oil produced. Some farmers or middlemen allow the mill to trade their oil, as the mills are usually important selling points of unbranded oil to urban clients that trust and recommend particular mills.
Cooperatives also offer milling services to farmers for a 10-20% reduction in price compared to private service mills. They do not serve as important loci of olive oil sales, however, as members prefer to sell on their own rather than through a cooperative. This reflects the hesitancy of members to mix their own oil with that of other members and the fact that small producers are able to sell oil at extremely attractive prices through personal and family relationships. Worth mentioning that cooperatives succeeded in attracting foreign funds to the olive oil sector, such as that of the USAID and of the Italian government.

The supply chain is completed with the bottlers and exporters. In addition to bottling their own olive oils, market players at this stage also provide bottling and branding services of oils from other farmers. Then the bottles are sent to for domestic consumption and part is exported. However, due to the lack of regulation and to decrease their costs, some bottlers mix the Lebanese olive oil with cheaper oil imported from Syria or Tunis.

The Lebanese market is divided into 3 main parts: direct sales from farmer to consumer, HORECA, and retail. Around a quarter of total olive oil production is estimated to be sold through direct sales to households. The demand on high quality extra virgin olive oil increased throughout the years due to higher consumer awareness regarding positive attributes of extra virgin olive oil. The overall consumption did not really change though.

The domestic market for olive oil is serviced predominantly by Lebanese oil, much of which is sold at premium prices directly from the producer to the consumer. Demand is estimated to be around 4.5 kg/person/year, which amounts to about 18,000 tons in total per year. Lebanese consumers have a distinct preference for locally produced oil, and tend to buy olive oil in bulk from trusted family or neighbors with whom they have an established relationship.

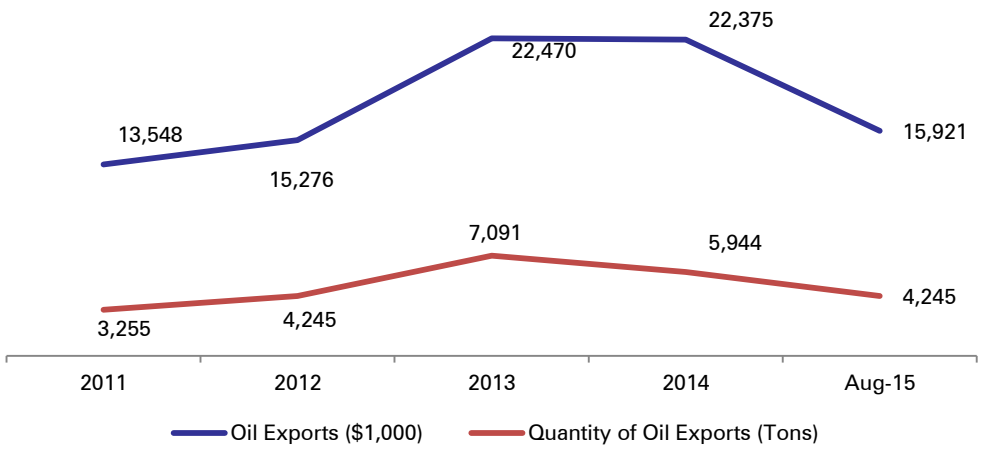
The demand of hotels, restaurants, and catering services is a major one, however it varies greatly from year to year as it is highly affected by tourism. This demand is satisfied either through direct sales channels or by olive oil traders who specialize in lower quality oil.

Finally, the retail market is generally accessed either through distributors or through the brand owner's own contracts. Profit margins ranges between 20-25% for supermarkets and up to 50% for traditional neighborhood shops and grocery stores, which are easier to access.

On the international front, Lebanon has been a net exporter of olive oil for more than 5 years, with a surplus in the trade balance of $3.03M, up to August 2015. Olive oil trade balance stood at $8.99M in 2014, 22.47% lower than its value in 2013.

Lebanon exported 4,245 tons of olive oil by August 2015, worth $15.92M. In 2014, olive oil exports stood at 5,944 tons worth $22.38M, compared to 7,091 tons worth $22.47M tons in 2013. In 2014, 28.34% of Lebanese olive oil exports were sent to Saudi Arabia, 16.63% to the United States, and 10.08% to the United Arab Emirates.

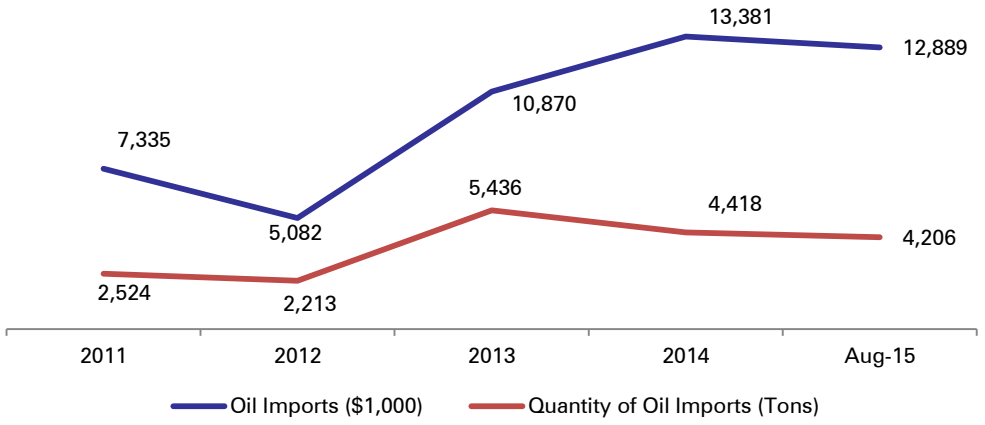
Olive Oil Exports



Source: Customs

As for imports, they reached 4,206 tons worth $12.89M in the first 8 months of 2015. In 2014, Lebanon imported 4,418 tons worth $13.38M, compared to 5,436 tons worth $18.87M in 2013. 50.74% were imported from Syria, 46.21% from Tunis, and 1.02% from Saudi Arabia.

Olive Oil Imports



Source: Customs

The reason for the dominance of Arab olive oil importers is the free trade agreement between Arab countries. Under the Greater Arab Free Trade Area (GAFTA) Agreement, and starting in January 2005, all agricultural products follow a zero-tariff regime. However, some exceptions still hold under the Lebanese-Egyptian Trade Agreement, whereby olive and olive oil from Egypt is not permitted to enter the Lebanese market.

As for olive oil imports from other countries, they are subject to a 70% custom duty and a minimum fee of L.L. 6,000 per liter. Imported olive oil from the European Union is still exposed to this tariff, even after the removal of custom duties on European imports.

In the case of Lebanon exporting olive oil to the EU, it can sell up to a quota of 1,000 tons with a 100% reduction on custom duty and ad valorem tax. However, exports of Lebanese olive oil to the EU are much less than 1,000 tons, due to the high

regulations and qualifications imposed by the EU. It is a bit hard for Lebanon to increase its olive oil exports because it produces a small quantity, and cannot guarantee the same quality each year.
The olive oil sector in Lebanon is facing many challenges leading local producers to have a surplus of around 4,000 tons to 5,000 tons per year. This is due to many reasons, mainly lower local demand and fierce competition from foreign olive oil.

In the 1960s, demand for olive oil was much higher, at 10kg/person. The decrease in demand results from the difference in lifestyle people follow, in which they do not buy anymore a big quantity of olive oil and store them in pantries as their ancestors used to do. In addition, due to the high price of olive oil, people are substituting it for other cheaper types of oil such as soy, vegetable, or canola.

Moreover, Lebanon's olive oil has been threatened as cheaper foreign products are being allowed to flood the domestic market. Lebanon has seen a decrease in demand for local olive oil over the years due to high cost of production, making way for imported products to sway consumers. According to Mr. Daher, Lebanese olive oil is being sold between L.L. 150,000-200,000 per tank (15-16.5 kg). A Syrian tank, however, costs only $45.

According to Mr. Youssef Fares, general manager of Olive Trade, the main challenge facing the olive oil market in Lebanon is the lack of authenticity control, meaning the absence of official characterization whether the olive oil is genuinely of Lebanese origin. Lebanon's high cost of olive production has negative consequences for its competitiveness in the domestic and international markets. To compensate for this constraint, Lebanon imports inexpensive oil from other Mediterranean olive oil producing countries, where the cost of production is much lower. Such imports profit bottlers, who mix lower priced imported oil with Lebanese oil to reduce costs and sell into both domestic and international markets. Lebanon does not impose any traceability or labeling requirements with regards to origin, making it easier to blend oil imported from abroad that may be lower in quality.

Another impediment facing Lebanese olive oil farmers is the lack of help from the public sector. For instance, plans to construct dams (Darb Ashtar and Bshenin) to irrigate the olive orchards have been in place since the 1960's, however they have not been built yet. The government should give financial support since turning a traditional mill into an automated one can constitute a hefty investment depending on the capacity and sophistication. Moreover, the government should help farmers prevent their olive trees to be contaminated by a fungal disease called "peacock's spots".

To overcome these hindrances and improve this sector, authenticity control programs that would characterize the Lebanese olive oil should be established. "Protected Designation of Origin" (PDO) certification, similar to the Appellation d'Origine Contrôlée designation in French wines and extra virgin olive oil, should be launched to distinguish Lebanese olive oil from imported oil that is bottled in Lebanon.

The quality of olive oil should be tested, to educate the consumer on the product being bought. Although the first Lebanese National Laboratory for Olive Oil Testing was inaugurated in June 2014 in Kfarshima by the Agriculture Ministry, in line with a project funded by the Italian Embassy in Beirut. Mr. Daher said that this laboratory is not being used. Moreover, an organoleptic panel of tasters should be accredited to ascertain the quality of olive oil.

As with wine, olive oil should be marketed so as each style would fit a certain type of meal. A powerful oil, described as "robust," "early harvest" or "full-bodied", could accompany foods with strong or distinctive flavors, such as meat and salads. A milder oil, often called "mild," "delicate fruit," or "late harvest", could be chosen for foods like fish, chicken or potatoes.

There are growth opportunities in the olive oil sector due to higher awareness that will attract consumers towards high-end product. For instance, productions of extra virgin olive oil and organic growth hold favorable prospects and have a growing export potential. Currently, around 300 km^2 of land is dedicated to the production of organic olive oil.

Olive oil is amongst the most prominent Lebanese signature agro-industrial products, and a proud part of the country's history and culinary tradition. Lebanon's diverse topography, fertile soil, microclimates, and olive varieties allow farmers to produce uniquely flavored products. This sector should be regulated and standards should be elevated in order for the olive oil to reflect an image of Lebanon being specialized in high-end products to justify higher price tags.

IV. Investing in the Real Estate Sector: It's All about Timing

As it has been the case in the past decades, the Lebanese real estate sector has been well recognized for its staircase movements whereby declines are more or less restrained. Despite the heavy impact of political and security situations on the Lebanese property market, real estate earned its title as an attractive and safe source of income return even in the darkest times. These highly tangible assets allow investors to diversify their portfolios and can open doors to a variety of sub-sectors such as investing in the residential or retail markets or even buying lands or commercial offices.

Given that the past four years were not the best of times for real estate activity, projects kept on taking place and adjusting to the new realities:

- Project opportunities outside Beirut are prospering including the opening of new malls and new residential and commercial projects.
- Real estate prices reached relatively low levels given the mismatch between demand and supply, which turned the market into a buyer's one where developers are willing to discount their prices.
- The emergence of specialized real estate services, which are provided through financial institutions with high expertise in terms of sponsoring, structuring and managing.
- The steady demand for small apartments from Low- and Middle– Income Households was supported by BDL housing incentives, thus resulting in housing loans edging up by a yearly 8.8% in 2014.
- Lower global construction prices following the depreciation of the euro (down by a yearly 12% in 2014) and the considerable decrease in construction materials' prices (MSCI World Construction Materials Index down by a yearly 13.6% in 2014).

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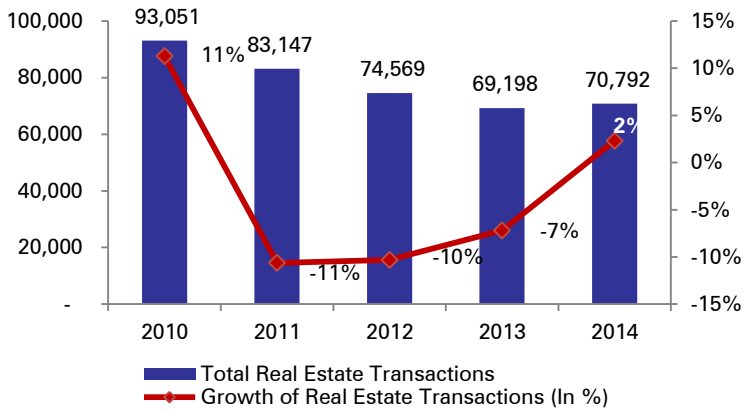
Real Estate Activity in 2014: Sluggish Performance amid Intensifying Challenges

Evolution of Total Real Estate Transactions



Source: Cadastre

As the old saying goes, "after the storm, comes the rainbow". Lebanon's real estate sector showed solid performance relatively to the circumstances that were taking place in the country in the past few years. In fact, the Israeli war in 20016 has cost Lebanon a substantial destruction of its infrastructure and real estate projects hand in hand with paralyzing its economic activity. However, the period that followed between 2007 and 2011 was booming and characterized by a pent-up demand outpacing supply levels. This is one more proof showing the ability of real estate in Lebanon to rise up from the ashes and to survive the political and security shocks. Thus, and even though the performance of real estate in Lebanon relies on healthy drivers, the economic slowdown that hit the country starting 2011 failed to turn into a severe stoppage of real estate activities regardless of the downside risks.

For too long, real estate sector in Lebanon remained one of the core sectors to assess the economic health of the country and determine its forthcoming standing. The undeniable importance of real estate activity is reflected by the sector's substantial contribution to the country's Gross Domestic Product (GDP) which was estimated around 14% by 2013[6]. Yet, the lack of data in the sector undermines the valuation of real estate demand and supply. The size of current local demand cannot be assessed accurately as updated income distribution and housing ownerships are not available, noting that remittances from the large Lebanese diaspora contribute substantially to the uphold of domestic demand as well as the growth potential for the real estate.

As a matter of fact, and similarly to the majority of Lebanon's economic sectors, real estate remained highly dependent on the country's political and security conditions. For instance, total real estate transactions (local and foreign) during 2010-2013 slumped 25.6% to 69,198. Actually, 2013's political factors have sent the "Political Stability and Absence of Violence" (PSAV)[7] index for Lebanon to the 14th lowest level among 214 countries. Lebanon's index kept revealing very low figures over the past 8 years, hovering between a lower band of 3 Percentile Rank (PR) in 2007 and a higher band of 8 PR in 2009 alluding to the country's persistent instability. The latest index of 2010 stood at 6 and steadied at this level till 2013. Worth mentioning, the index scores the variation of political stability in a country correspondingly to the occurring incidents and

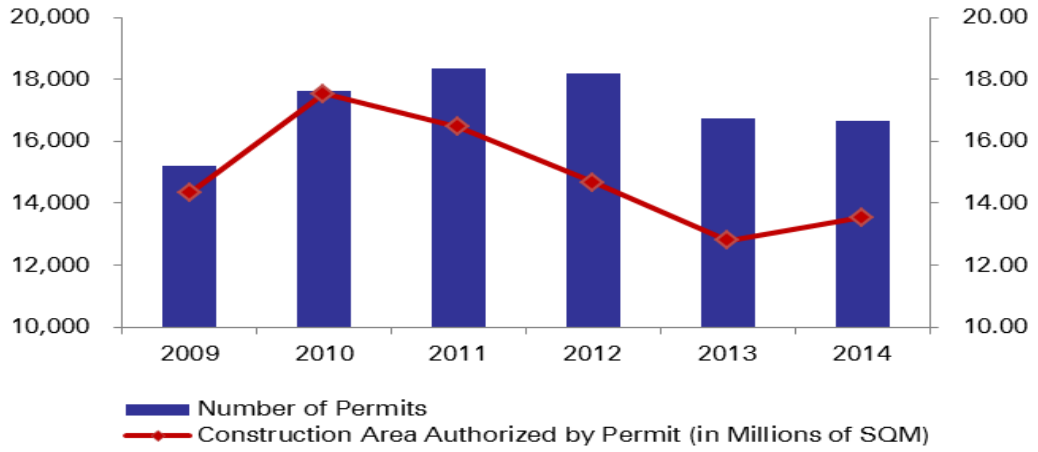
[6] According to the national accounts of the Central Administration of Statistics (CAS)

[7] Index introduced by the World Bank, as a part of the yearly Worldwide Governance Indicators. It is defined as a tool to measure the "likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically motivated violence and terrorism."

their weight as a Percentile Rank (PR) among all countries from 0 (lowest political stability) to 100 (highest political stability).

In 2014, mixed political signs shaped the local demand for real estate. In the first half of the year, 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. This resulted from the long-awaited Cabinet formation in February along with a firm security plan that managed to reduce security incidents in several Lebanese regions. However, the presidential vacuum that started by the end of May painted the second half of the year and was coupled with series of security incidents topped by the hostage of Lebanese soldiers by militants in Arsal in the first week of August.

Evolution of Construction Activity



Source: Orders of Engineers in Beirut and the North

Construction Activity retreats in 2014 despite Global Economic Turmoil

The international bearish trend in oil prices, that reached in 2014 one of their lowest levels since 2010, could have significantly triggered down transportation costs in the construction industry especially when developers' projects are located far from the providers of construction materials.

In addition, construction costs were partly impacted by the Euro's depreciation. Noting that Lebanese developers heavily rely on the European building materials for design and decoration purposes (such as ceramic and marble rom Italy and Spain), their imports from the Euro Zone became cheaper. Worth mentioning that, the European official currency almost saw a 12% yearly slump, by the end of 2014, from €/$ 1.37 to €/$ 1.21. In fact, the MSCI World Construction Materials Index reflected as well the situation and dropped 13.6% y-o-y, which could explain the potential drop in Lebanon's construction costs as the global decline of construction prices was imported to Lebanon.

Besides the repercussions of the Syrian crisis on the Lebanese real estate sector, contractors benefitted from the cheaper Syrian labor force. As several Syrian citizens were fleeing the country for employment at low wages, the local workforce was facing fierce competition while real estate developers were enjoying cheaper labor costs and fewer obligations (when it comes to social security), which contributed in decreasing their construction costs even more.

Yet, Lebanese developers witnessed several challenges in 2014 of which the changing demand, the scarcity of land, the volatility of workforce availability and the economic slowdown. Choosing the location for their units amid ongoing security developments across the country and centralization of projects in the capital was another burden for real estate suppliers. Several developers failed to survive the economic slowdown and were forced to exit the market. This has partly left room to the remaining players, which were mainly the biggest developers.

Cement deliveries, which are one of the earliest barometers of construction activity, posted a 7.0% y-o-y decline by November 2014 to 5.07M tons. Similarly, 2014 saw the number of authorized construction permits slightly slid by a yearly 0.36% to 16,663. However, the number of construction permits is not reflective of the precise volume of real estate supply in a specific time as applications are filed 6 months earlier and the execution of a permit is valid up to eight years from the date of issuance. Still, permits can disclose contractors' sentiments and expectations for the coming period.

Real Demand Remains Stagnant in 2014 despite Increasing Real Estate Transactions

According to official data, the total number of real estate transactions (foreign and local) went up by 2.3% y-o-y by the end of 2014 to 70,792. Even though 2014's yearly increase followed 3 years of continuous drops, the total number of transactions remained well below 2011's and 2012's respective levels of 83,147 and 74,569. This explains that demand did not really improve in 2014 but slightly recovered from the very low base reached a year earlier. In addition, the number of real estate transactions reveals when ownership of the sold entities is recorded with the Cadastre in the Registrar of Deeds. In reference to an interview with the Executive magazine, Mr. Jihad Ibrahim, general manager of Jamil Ibrahim Establishment, stated that the number of real estate transactions does not show when the transaction really took place as the time frame to handover a residential unit requires at least 3 years and the majority of sales happen during or before the project is initiated. Thus, the increase in the average value per transaction by the end of 2014 does not necessarily indicate a growing demand or even an increase in the prices of real estate projects.

In effect, 2 main types of apartments characterize the Lebanese real estate market: luxurious flats and affordable apartments that each had a divergent path in 2014.

1. Luxurious and Spacious Apartments Went Hand in Hand with Fading Foreign Demand

Wealthy Lebanese citizens and Arab nationals were renowned for their consistent demand for luxurious spacious flats in Lebanon. Those apartments are usually above 220 Square Meters and are very well located, mainly in the capital Beirut.

However, the fact that the small Mediterranean country has a strategic location in the Middle East makes real estate demand for expensive apartments vulnerable to the slightest regional tensions that can upsurge. In fact, sales to foreigners slumped by a yearly 6.4% to 1,196 in 2014, the lowest level in 6 years.

Noting that GCC citizens constitute a substantial stake of the demand for luxurious apartments in Lebanon, their demand kept on dwindling following repeated warnings from their governments to avoid Lebanon due to the high degree of political uncertainty and security developments. Correspondingly, Lebanon's real estate projects were further losing foreign investors' appeal over the years, noting that the share of real estate sales to foreigners in 2014 stood at 1.7% compared to 1.8% and 1.9% in 2013 and 2012, respectively.

Lebanese suppliers were more cautious when initiating large-scale deluxe projects and preferred serving the existing local demand. On the other hand, the Syrian war also took its toll on the real estate developers that feared a probable extension of the conflict to Lebanon that could affect their projects and sales.

Even though several Syrian citizens flew their country heading to Lebanon, their demand was mainly concentrated in rentals and not real estate purchases. This can be explained by the fact that the wealthy Syrians leaving their country were looking for more secure countries, none of which was Lebanon. Thus, the ones targeting Lebanon were the middle-range families and those expecting to go back to Syria when the situation improves. Those could not afford buying real estate units in Lebanon, but rather rented apartments.

Thus, and with supply outpacing the demand for luxurious and spacious apartments, the latter's prices went down around 20% as buyers gained more freedom and time to negotiate their purchases. 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.

2. Small Flats: Steady Demand from Low- and Middle – Income Households

In 2014, demand for real estate was mainly restricted to basic housing on the expense of luxurious accommodation. With local demand being the one to rise over the year and with the majority of spacious apartments remaining unsold, local consumers were looking for small affordable houses. In fact, 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.

In addition, the subsidy that BDL provides to commercial banks for housing encourages demand for small apartments with area not exceeding 150 Square Meters (SQM). Accordingly, Lebanese buyers are looking for smaller flats that they can afford with their relatively low income. Thus, demand for such apartments is growing and was mainly behind the uptick of housing loans distributed in the financial sector that rose 8.8% y-o-y in H1 2014 to reach $8.53B.

The rising number of unsold apartments made suppliers more cautious and alert about a potential mismatch between the existing demand and supply. Accordingly, and before initiating any new project, in-depth studies of the market are conducted to avoid any risk that could restrain developers from liquidating their projects. Defining the needs of real estate buyers became more essential in 2014 which have turned investments towards small and affordable apartments.

Given the scarcity of land and its effect on prices, developers were looking for new areas for their investments where they can benefit from larger plots thus reducing their costs. Despite the slump in the number of construction permits, the construction area authorized by permits (CAP) increased by a yearly 5.8% to reach 13,545,707 SQM in 2014. The increase in the CAP should not be regarded as an improvement in the construction sector but rather as a partial recovery from 2013's levels when it had shrunk by an annual 13%. In fact, developers became more oriented towards new type of projects to serve the changing demand. Given that only big contractors survived the economic slowdown, they became more interested in large scale projects (as they are built over large plots of land) featuring small apartments with numerous facilities at an affordable price.

Real estate contractors also tried in 2014 to spread their projects over new geographical areas where land is more abundant and less expensive to serve a more selective demand. Mount Lebanon kept on capturing the lion's share (48.9% of total permits) in terms of geographical distribution of projects given its relative proximity to the capital and thus the slightly lower prices in terms of land. However, the number of projects in Mount Lebanon area slightly slipped by 0.7% y-o-y in 2014 to 7,248 permits. Furthermore, the rising clashes in the Bekaa area (10.9% of total projects in 2014) and North of Lebanon region (14.4%) were behind the downturn in the number of projects from 1,776 and 2,196 to 1,617 and 1,984, respectively. Meanwhile, Beirut, that showed the lowest number of permits (given the scarcity of land) with a slight stake of 5.6% of the total, saw a 6.2% yearly rise in the number of construction permits to 839.

Additionally, the falling construction costs facilitated prices' decline of small apartments. Therefore, many developers were more open for price negotiations with some of them willing to offer approximately 10% to 15% of discount.

What about the Commercial Market in 2014?

While maintaining their high levels, commercial rentals in Lebanon showed substantial declines in 2014. In details, and amid a slowdown in the residential market, investors were more oriented towards commercial projects. Those investments have become more income appealing in terms of sales and rents given the shortage in stock.

Cushman & Wakefield annual report showed that retail rents in the main Lebanese locations hovered between $500 - $1,600 per SQM/Year and considerably declined during 2014 around 15%-30%, partly on dropping investment sentiment. However, ABC Centre Achrafieh, which was 2014's most expensive retail location in Lebanon, preserved 2013's level of $1,583 per SQM/Year. The Lebanese mall ranked 37th among 64 countries and stood just after Biblioteksgatan - Sweeden ($1,636 per SQM/Year) and Rue Neuve - Belgium ($1,750 per SQM/Year). ABC Achrafieh rental was higher than that of Grand Rue – Luxembourg ($1,500 per SQM/Year) and Shopping Centre - Kazakhstan ($1,330 per SQM/Year).

On the local front, Beirut Central District and Rue Verdun rental prices followed ABC Centre Achrafieh at respective prices of $792 per SQM/Year (a 16.7% yearly decline) and $633 per SQM/Year (a 20.0% y-o-y drop). Rue Hamra and Kaslik ranked fourth in Lebanon with similar rental price of $554 per SQM/Year.

Finally, assessing real estate prices and the trend they followed in 2014 remains challenging on insufficient existing data that could be misleading. Despite the economic slowdown, the substantial decline in construction costs and the complications on the Syrian front that kept on weakening investors' confidence, property prices went in the same direction. Though, the decline in the prices of luxurious flats certainly took place at a faster pace than that of affordable apartments.

Real estate and construction activities have been struggling for several years to preserve their leading positions as core sectors in the Lebanese economy. Following 2008-2009 booming period, real estate was hindered starting late 2011 by pressures from the war in Syria and the fragile domestic situation. However, the strong fundamentals of the sector managed to slow down the retreat in activity up until 2014 when indicators began to stabilize.

V. Knowledge Economy on a Fast Growth Track

A knowledge economy is an economy where information is leveraged for the creation and the enhancement of high-value added products and services such as mobile applications, technological gadgets, software…etc. The potential for growth in this field is huge because these knowledge-based products and services can be exported to any country and are not confined to Lebanon or the region. Moreover, growth in the knowledge economy is not linked to the overall economic growth; even if a country is in recession, it can still harbor growth in the knowledge economy.

The talented Lebanese labor force is combined with favorable developments in the field of knowledge economy. The Central Bank of Lebanon unlocked $400M worth of investment capital to be deployed in that domain. According to Circular #331, commercial banks can provide equity financing for Lebanese startups, venture capital firms, accelerators and incubators. The bank's exposure would be limited to 25% as the Central Bank covers up to 75% of the banks' participation.

- Lebanon houses an educated and qualified labor force. Lebanon ranked 28th out of 144 countries for the quality of the educational system and 5th for the quality of math and science education according to the World Economic Forum.

- Venture capitalism has been growing in Lebanon despite the economy's setbacks since 2011. Lebanon ranked 59th out of 144 countries in terms of venture capital availability in the 2014-2015 edition of the World Economic Forum's Global Competitiveness Index up from the 62nd place in the 2013-2014 edition.

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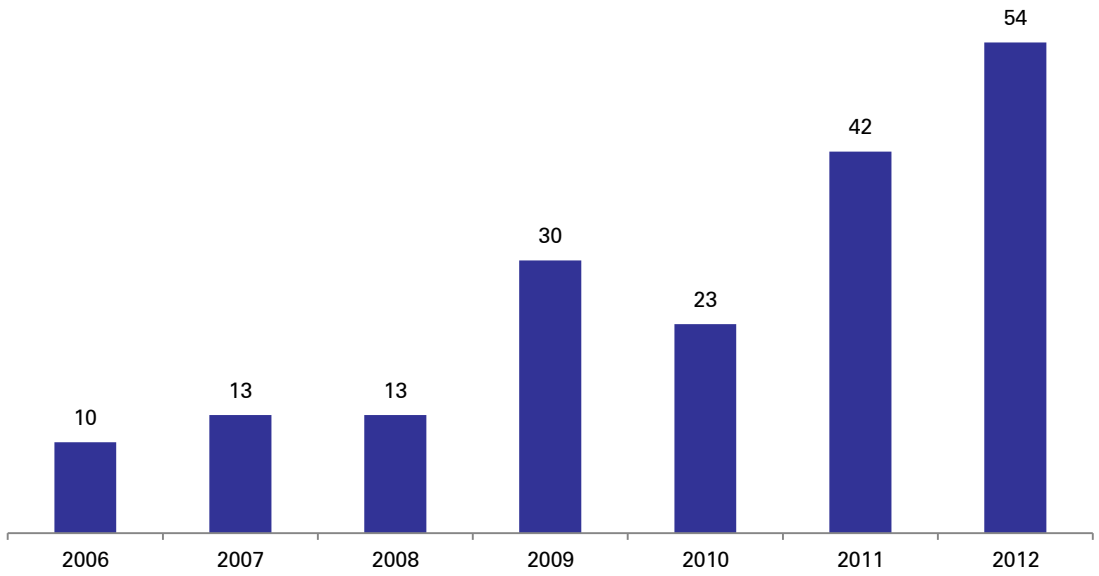
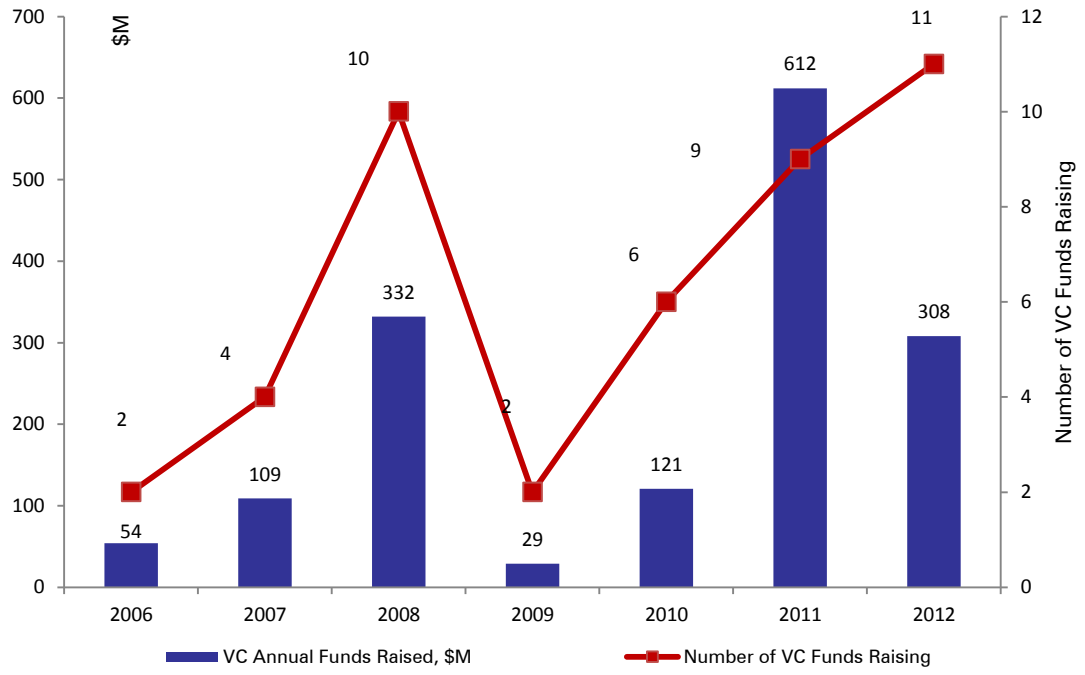
Lebanon Taps into the Potential Lying in Innovation and Entrepreneurship

Number of VC Transactions in the MENA Region



VC Annual Funds Raised in the MENA Region



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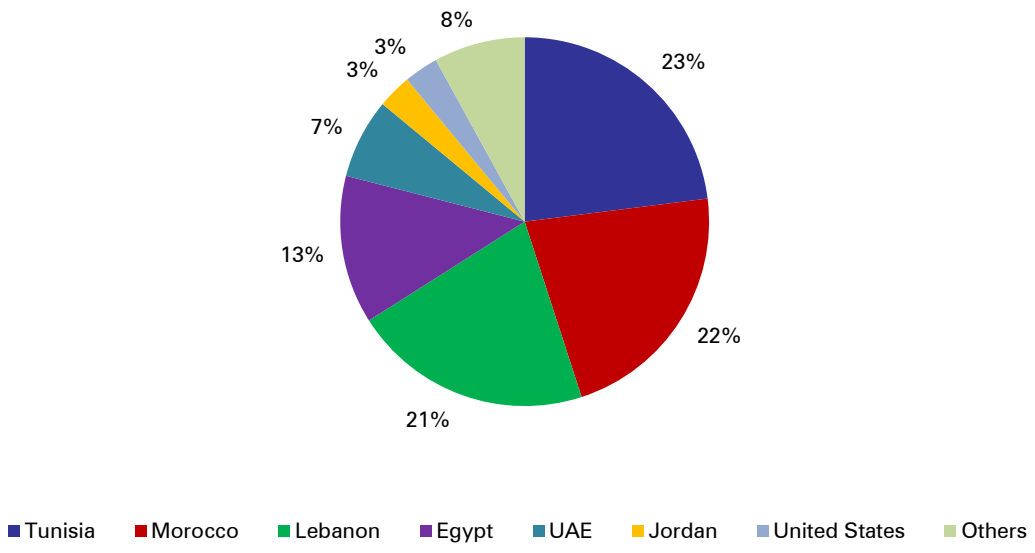
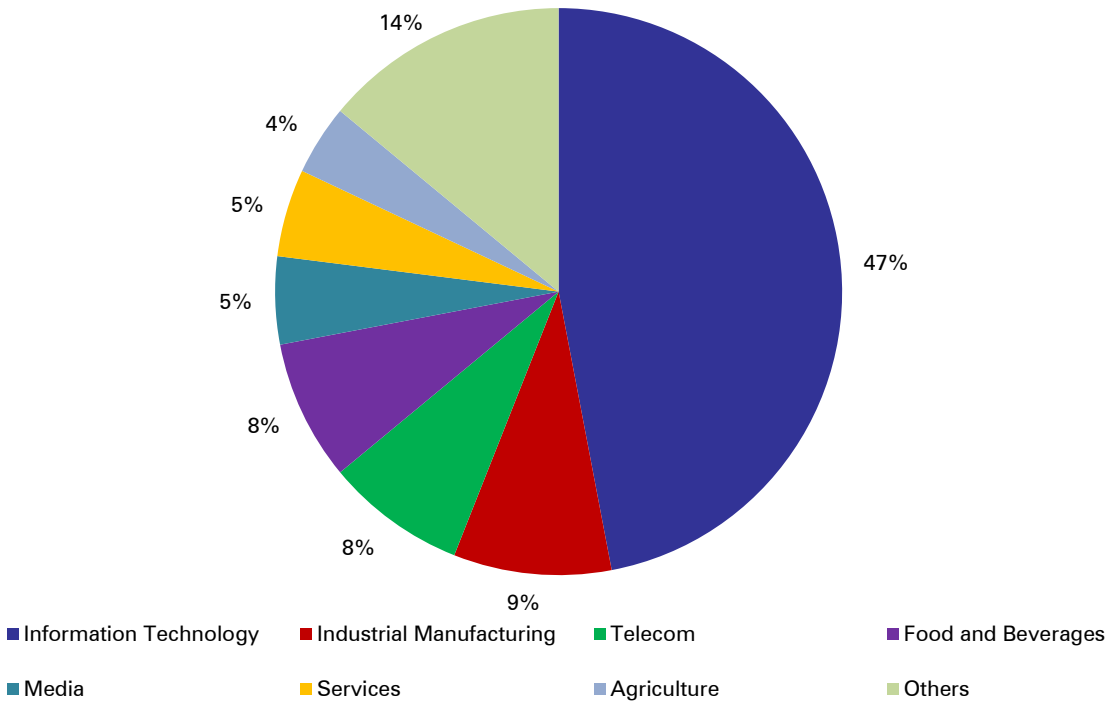
Country Concentration of VC Deals by Volume, 2010-2012



Sector Concentration of VC Deals by Volume, 2010-2012



Source: Zawya Private Equity Monitor

Embracing Innovation and Venture Capitalism

Lebanon is now unlocking the potential economic benefits held in innovative entrepreneurship, a pillar of growth and development. This truly counts as a budding cultural shift, one that can only be successful if entrepreneurs with new-ideas believe Lebanon is an innovation hotbed and if angel investors, venture capitalists, and most recently commercial banks set the right backdrop to making it one, by rendering equity financing available.

The desire to promote and encourage innovation goes hand in hand with the growth of Venture Capitalism in Lebanon. Venture Capitalists' major role is scanning a large pool of start-ups, detecting the ones with the most solid business model and growth-potential, assisting them in their early- stage growth period and propelling them into long-term growth. VC assistance is not limited to financing but also entails sharing expertise and contact networks which allow the start-ups to adapt to the fast track business environment.

A start-up must be prepared before approaching venture capitalists. The first phase in the start-up's financing cycle is delicate since all there is on the table is a budding idea and financing is limited to "love money" i.e. Friends, family or angel investors providing seed capital to kick-start the business rather than reap high returns on their investment. At this stage, referred to as "the valley of death", there is no steady or significant revenue stream, the entrepreneur incurs many initial costs and the valuation is subjective and minimal. The challenge therefore lies in surviving until the start-up is ready to successfully approach a VC.

After VCs are approached, the entrepreneur often opts for several rounds of financing. As they gather funds through multiple rounds, entrepreneurs are fine-tuning their product/service and growing their structure while being in touch with the market. In this process, if the product/service is gaining traction, the value of the company is technically increasing and allowing the entrepreneur to gather more funds in the coming round with minimum dilution of ownership.

What VCs have to Offer…

A developed VC industry has the potential to generate a slew of positive effects on Lebanon's economy such as job creation and higher competitiveness across various industries, both leading to higher overall growth. Essentially, VC would give the economy a sense of rejuvenation. The fresh Lebanese graduates will be able to steer away from the traditional career paths of medicine, engineering, law or stable high-growth jobs and explore the idea of becoming innovative entrepreneurs. As the VC space grows stronger and more organized, accessing finance to turn an idea into a profitable and scalable business becomes more of an achievable goal.

VC activity also encourages entrepreneurs of all stages to invest in Research and Development (R&D). R&D allows the future entrepreneur to learn all there is to know on the sector he is looking to tap, and gives the established entrepreneur the ability to understand and even anticipate the dynamics at play in his/her market. Awareness in regard of the benefits of R&D is yet to be raised in Lebanon, which ranked 127th out of 144 countries in terms of company spending on R&D by the World Economic Forum (WEF).

What Lebanon has to Offer...

A robust educational system is essential for the innovation landscape as it molds the country's future entrepreneurs. Lebanon has no shortcomings on this front, ranking 28th out of 144 countries for the quality of the educational system and 5th for the quality of math and science education according to the World Economic Forum. However, Lebanon is not fully reaping the rewards of this qualified pool of labor and that due to the "brain-drain" phenomenon. The qualified men and women are being drawn to grow their business or career abroad. An essential infrastructure reform and enhancement, particularly electricity and internet, is required to keep the technical innovators interested in Lebanon.

Lebanon and VCs: Strong Match even in Tough Times

Lebanon has had a challenging economic landscape since 2011 till this day but still witnessed a steady growth in venture capitalism activity. An unstable local and regional security situation along with numerous political deadlocks have had wide-reaching consequences on the Lebanese economy, subduing the core sectors of construction, real estate, and tourism. In spite of this backdrop, Lebanon ranked 59th out of 144 countries in terms of venture capital availability in the 2014-2015

edition of the World Economic Forum's Global Competitiveness Index up from the 62nd place in the 2013-2014 edition. The rise of VC availability can be explained by the fact that venture capitalists are risk takers who back entrepreneurs in "sickness and in health". VC is even a gateway for a country to regain economic strength through higher competitiveness and reduced unemployment.

Central Bank Gives the Knowledge Economy a Boost

It's precisely because the economy is in need of a boost that the central bank (Banque du Liban, BDL) issued circular #331, allowing the banks to be not only lenders but also investors in the knowledge economy. One of a kind in Lebanon, this circular stipulates that commercial banks now have the chance to finance startups, venture capital firms, accelerators, incubators, all part of the knowledge economy, through equity.

The circular has already been perceived as promising by banks, VCs and startups alike. After concluding around 15 investments in technology startups, Berytech, aiming for an average of $30M for its second fund Berytech Fund II, has already gathered funds from Lebanese commercial banks, including Blom Bank. Blom Bank, along with Bank Audi, Bank Med, Banque Libano-Francaise and a few others have also pledged funds for Middle East Venture Partners' (MEVP) new $50M fund. Hala Fadel, fund manager at Comgest, along with entrepreneurs Henri Asseily and Herve Cuviliez are also setting up a fund under Leap Ventures with a target of $100M and an initial objective of $50M, to be gathered from banks mostly and from some of the partners' own investments. Al-Mawarid Bank and Beirut Angels set the #331 circular in motion by offering more than $300,000 to Presella, an online tickets and events reservation application. Beirut Angels is a local business angels' network launched in 2013 by former Minister of Telecom Nicolas Sehnaoui, Hala Fadel, Chairperson of the MIT Enterprise Forum and Louay Al Kadri, co-founder and CEO of Presella.

All stakeholders in the knowledge economy which are operating under the wing of BDL's circular must be careful not to over-supply the market. With new money coming in, equilibrium must be struck between supply and demand especially that new demand for money needs time to materialize. With all the VCs that have embarked on the #331 journey planning to invest over a span of around four years, pumping $30M each year would be an acceptable deployment of funds that the market can absorb.

Different scenarios might play out when the new funds are deployed on the market. If VCs have too much money on their hands that they need to invest while the market has very few attractive opportunities, the startups might benefit from overvaluations.

However, if the new money creates a "VC oligopoly", the VCs get the upper hand. When only a few VCs control the market, startups might not have a vast array of choices and will find themselves compelled to select one of the key market players to access funding and technically lose ground in terms of negotiations.

The funds to be deployed under circular #331 might also incite other venture capital firms to enter the market or simply create a healthy competition amongst existing VCs which would then be a win-win situation for both parties. Prior to the circular, the market was characterized mostly by small funds and ticket-sizes, much co-investing and deal-sharing. This situation is likely to change once competition on the market heats up with larger funds and more proprietary deals emerging.

According to Mr. Omar Christidis, founder and CEO of ArabNet, an events and media company for the Arab digital industry, in order to gain a competitive edge, VCs must show that they can add value beyond money or/and seek to be the most visible and the most accessible on the market, which allows them to gather a substantial flow of deals. He also stressed on the fact that VCs must be keen on preserving a sound market reputation, as this element is a heavy-weight in the start-up community.

What Needs To Be Done?

With large sums of money in the VC pipeline, a higher deal flow is needed. This deal flow needs to be generated by accelerators and incubators that foster the creation of start-ups. Accelerators and incubators offer early-stage entrepreneurs the mentorship and the training they need to transform a mere idea into a viable product that can garner success when it's launched and that can attract VCs. However, Lebanon needs more of these "start-up" generators today to

increase the deal flow and allow the money in the VC pipeline to be utilized in worthy-investments. Hence, it goes without saying that the VC world and the accelerator and incubator ecosystem are complementary.

Setting the innovative entrepreneurship on a growth path requires better communication channels amongst all stakeholders. Entrepreneurs, Accelerators & Incubators, Venture capitalists and most recently Lebanese banks have to embrace the approach of continuous learning to keep up with the ever-evolving start-up world.

In order to foster innovation, efforts to enhance intellectual property protection must be on Lebanon's to-do-list. An innovator needs to make sure that his product is protected by the rule of law. Lebanon must increase efforts on this front as the World Economic Forum (WEF) ranked it 139th out of 144 countries in terms of intellectual property protection. However, in terms of capacity for innovation, Lebanon climbs in the ranking all the way up to the 54th spot, meaning that potential exists but simply needs to be nurtured.

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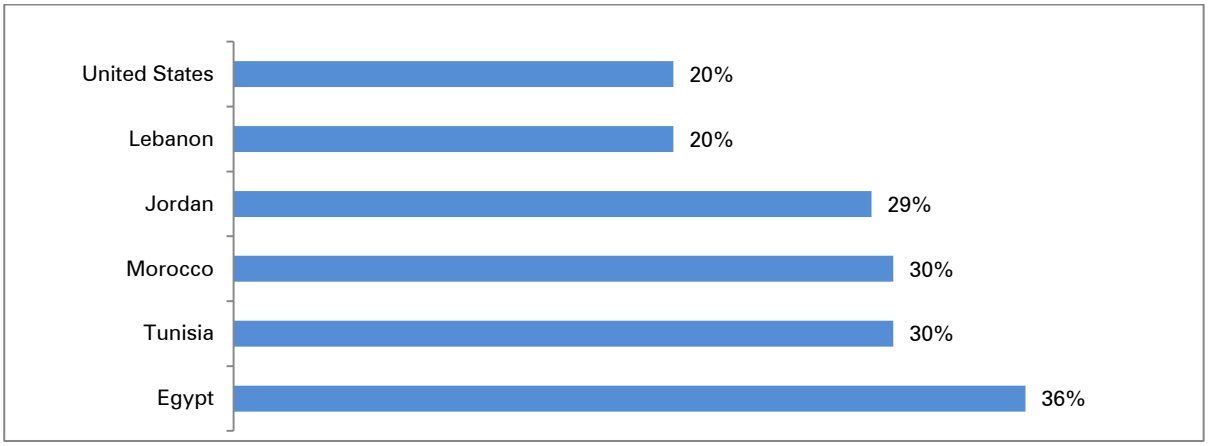
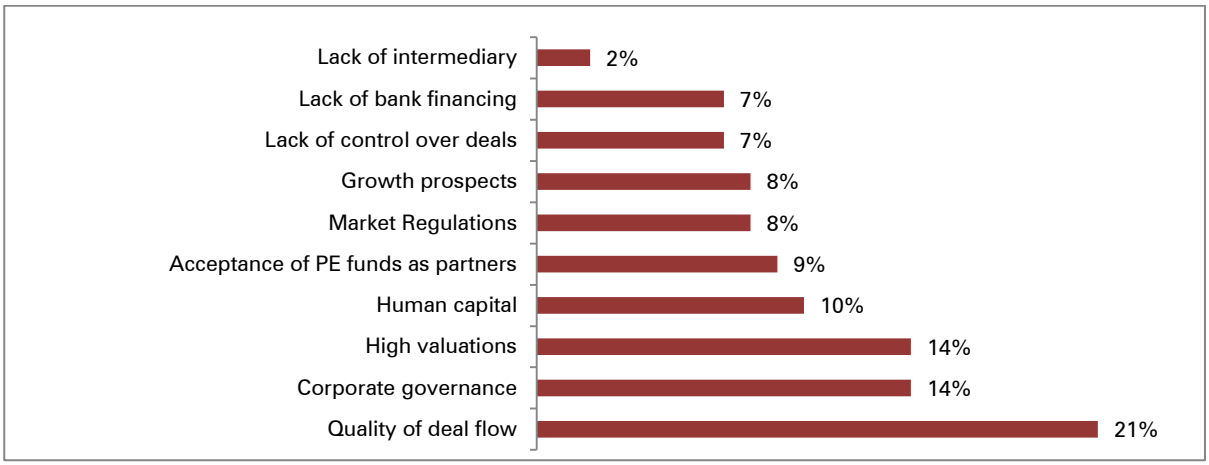
New Angel Investors for Tech Startups: the Lebanese Banks

Value Added of Information &Technology to GDP, 2012



Source: world Bank data

Main Challenges for Private Equity Investments



Source: Survey by Zawya focusing on General Partners in the MENA region, during Q1 of 2013

Amidst tighter economic conditions, an innovative financial service consented by the BdL introduced a new financing option to the Lebanese startups. A new Circular (#331, available on BdL's website) licensed the stepping in of banks to finance startups, venture capital firms, incubators and accelerators working in the knowledge economy, not through the usual debt, but this time through equity.

In essence, the move complements past initiatives to subsidize companies working in various economic sectors, and aims at boosting the economic cycle through domestic lending and job creation. Meanwhile the unconventional part allowing equity investment in startups builds on further market characteristics.

Tech startup firms are especially appreciated for their job creation benefits and resilience to the economic downturns when fixed jobs are less available and entrepreneurship becomes more tempting. Yet, they are the ones facing most difficulties when it comes to financing. Their current options were limited to private equity and some products of Islamic banking, while the commercial banks were only involved through debt offering, provided that it is guaranteed by Kafalat and only for a ceiling of $400k per company.

The BdL's move thus reshuffled some of the financing options for both banks and startups. Building on the continuous growth of bank deposits which advanced at an annual pace of 10% by July, much faster than the economy's growth, Lebanese banks preserved the best position to provide capital for the private sector, as the BdL governor puts it. On the other hand, their lending portfolio to the private sector reached around $39.7 billion, almost 94% of the country's GDP, representing a high leverage ratio for companies and limiting the growth of debt-driven investments capabilities, hence the benefits of switching to equity.

But does the circular offer enough incentives for banks to make use of it? A review of its clauses and conditions reveal interesting opportunities, and quite some challenges.

The circular allows investments up to 7 years in startup companies, incubators, accelerators and venture capital firms working in the knowledge economy field, as long as they are a Lebanese joint stock company and not working offshore.

The returns are tempting. The circular stipulates that BdL will finance 75% of the bank's investment in these firms. Banks would receive zero-interest loans from BdL, and invest them in treasury bills. The invested loans will be calculated in a way to generate interest equivalent to 75% of the bank's participation in the firm, therefore limiting the banks' exposure to 25%.

Total investable amounts in these firms are also limited. Only 3% of the bank's capital can be used, out of which a maximum of 10% is allowed in a single company. To put this into perspective, the largest banks such as BLOM and Audi can individually invest up to $50 million and $66 million in the field, respectively, and given the offered hedge from BdL, the direct exposure won't exceed $12.5 million for BLOM and $16 million for Audi. Investments in a single company would also be limited to $5million from BLOM and $6.6 million from Audi. Whilst this is minimal on a large bank's balance sheets, it is very advantageous for firms, as most current investments are concentrated below the $2 million bar.

For reference, Lebanese Business Angels and Cedrus Ventures offer to finance companies with a budget going from $50k to $500k. Venture capital funds like Berytech's and Middle East Venture Fund invest up to $2 million, and only the International Finance Corporation (IFC) and Riyada Enterprise Development (RED) participate with more than $2 million. Now, and as a result of the new circular, the Lebanese banks would make around $385 million available to fund startups in the knowledge economy.

The 10% rule also highlights the need for diversification and entails investment in 10 different companies. The reason is that despite their unlimited upside potential, startup companies have a low survivorship rate of around 20% during the first 3 years. In this area, incubators and accelerators play a significant role as they increase the chances of hosting successful companies. For instance, Seeqnce reported that 10 of 22 of their graduated tenants are fully active.

The offered hedge by BdL against the banks' investments therefore looks appealing. Some aspects remain to be cleared though. One is the method that will be used to calculate the interests to be received by banks, or more accurately whether the bank's initial investment would be matched by interests based on its present or future value. Another question for banks would be the risk-weighted assets required for such investments. Basel II stipulates a risk weighted allocation of 100% for exposures to equity investments, while Basel III can go up to 400% for exposures to not publicly traded equity investments and 600% for certain investment funds.

But aside from the risks and returns, many challenges await the implementation of this circular.

Certainly, the regular channels of commercial banks' credit are not best suited to advise on equity financing opportunities, but most of the Lebanese banks have an investment arm and are not short of skilled investment teams. Many banks are also already indirectly engaged in the private equity world. Blominvest bank, alongside 5 other banks[8,] holds a share in the Building Block Equity Fund which has a capital of $7.3 million and is managed by Middle East Venture Partners (MEVP). The fund had made successful investments in 3 companies (shahiya.com, shawarmanji and cedar books). Audi Saradar investment bank is also a partner in Berytech. The question remains whether banks' participations in these funds and firms

[8] *Fransabank, Bank Audi, BankMed, BLF, Crédit Libanais*

would benefit from BdL's facilities, given that the majority are not limited to tech companies and many have the legal form of a limited partnership or registered offshore.

The circular also notes an active role for banks in the development of the firm's business, which might be of concern to both banks and startups. The screening and selection of successful startups is an enormous effort and the continuous counseling and follow up require a mobilization of dedicated teams. To note the difficulty of having companies in the pipeline, it suffices to see that many of the funds' available capital are still not allocated. Incubators and accelerators remain the first place where investment funds look as they have developed considerable experience in screening companies and fostering their development. Berytech, the pioneer incubator in Lebanon graduated over 60 tenants during the past decade. In this context, banks might opt for investments in funds at the expense of direct investing in companies if they represent less of a hassle.

In all cases, the potential remains huge, especially for technology and information startups. Software and online products and solutions can reach a huge consumer base and need not be capital intensive. The MENA region alone has a population of over 350 million people, a third of which are under the age of 15, eager for connectivity and smart devices. Some of the MENA countries also rank well on the list of highest GDP/Capita in the world. In Lebanon, around 1 million are subscribed to 3G services and around 2.6 million use internet through their fixed lines. The penetration rate for mobiles is also projected to exceed the current 93% as Lebanon remains one of the few countries with a less than 100% rate.

Private equity remains subdued in the MENA region, with total investments representing 0.05% of its GDP in 2012, well below the US' 0.86% and the UK's 1.05%. However information and technology gained special focus earning it the largest share of 40% of the total investment volume made in the MENA region (excluding Israel) during 2012. This is one sector where a small population is not an impediment. The 7million+ population of Israel recorded around 3,500 startups solely focused on tech during 2012. Its dubbed "Silicon Wadi" is the second largest concentration of high tech industries after US' "Silicon Valley".

With low liquidity needs, high expected returns and a hedged risk, funding the tech startups though equity represents a worthy opportunity. The legendary entrepreneurial spirit of the Lebanese might find more reasons to hold on to the country and help pull the economy out of stagnation and debt. Certainly, the accompanying infrastructure and mechanics need to follow, but it is still a milestone that was achieved by the Central bank and to be followed by the financial sector, hoping it will encourage talent to uncover and multiply.

VI. Lebanese Plastic Industry: High Standards and Steady Growth

Lebanon is home to plastic importers and manufacturers meeting the highest internationally-recognized standards. In fact, high-quality plastic products are the most appealing for investment in the Lebanese plastic industry because that is where our competitive advantage is the strongest. The mark of quality is what allowed Lebanese plastic manufacturers to successfully tap into foreign markets such as MENA countries, Gabon, Niger, Holland, Belgium, Luxembourg and many others.

The plastic industry in Lebanon spans across a large pool of products: food packaging, pipes, agricultural plastic products. The Lebanese plastic industry is one of the few industries that have been shielded from the morose economic environment. The Syrian crisis, which had ripples on key sectors of the Lebanese economy such as real estate, construction and tourism, did not affect the Plastic industry. In fact, Lebanese plastic companies have their established export markets and local clientele to rely on in addition to numerous industry-related strengths.

- Demand for plastic is inelastic since there is no available substitute for plastic
- There is no expiry date on plastic products, so manufacturers do not face any pressure regarding inventory piling up and can even hold on to stock until selling prices are higher
- Lebanese companies are environmentally conscious as many of them recycle and reuse plastic and as some are running their factories on renewable energy
- The machines needed to manufacture plastic are highly affordable
- Current developments on the forex market and the energy market open a great window of investment in the Lebanese plastic industry. In fact, the era of weak euro and cheap oil automatically translate into a smaller price tag on raw materials and alleviates manufacturing costs.
- The average mark-up on the market is 17%
- Lebanon's net exports of raw materials for plastic manufacturing amounted to $353.73M in 2014
- Lebanon's net exports of finished plastic products amounted to $211.96M in 2014

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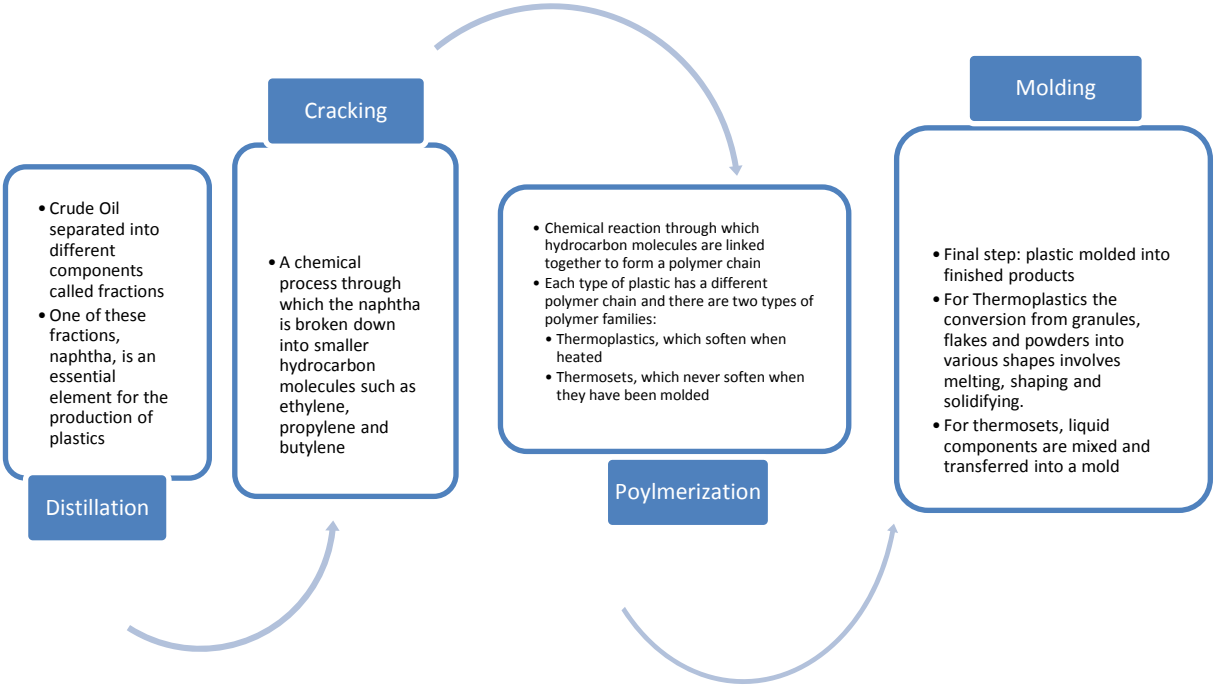
The Lebanese Plastic Industry: Leveraging its Strengths Locally and Abroad

The Lebanese plastic industry is one of the few industries that have been shielded from the morose economic environment. The Syrian crisis, which had ripples on key sectors of the Lebanese economy such as real estate, construction and tourism, did not greatly affect the Plastic industry. In fact, Lebanese plastic companies have their established export markets and local clientele to rely on in addition to numerous industry-related strengths.

How is Plastic made?



Source: Association of Plastic Manufacturers Plastics Europe

The Lebanese plastic industry is one of the few industries that have been shielded from the morose economic environment. The Syrian crisis, which had ripples on key sectors of the Lebanese economy such as real estate, construction and tourism, did not greatly affect the Plastic industry. In fact, Lebanese plastic companies have their established export markets and local clientele to rely on in addition to numerous industry-related strengths.

The Lebanese plastic industry holds much strength that certainly outweighs its weaknesses. First and foremost, there is no expiry date on the plastic products. Therefore companies feel no pressure when and if their inventory builds up as they can liquidate their stock at a higher price in the future. Moreover, companies benefit from the fact that all of the scrap plastic is recycled. Most importantly, demand for plastic is highly inelastic and no other substitute is available. For plastic manufacturers, the cost of the needed machines is very affordable and averages $15,000.

Strengths and Weaknesses of the Lebanese Plastic Industry

Strengths	Weaknesses
• No Available Substitute for Plastic	• Unlawful competition (reported in food packaging segment)
• No expiry date on plastic products	• New Law on Syrian Labor
• Plastic can be recycled and reused	• High Energy Costs
• Demand for Plastic is inelastic and is mostly insensitive to downturns in the economic cycle	• -
• Low cost of machines needed to manufacture plastic	• -
• Recent drop in oil prices reduced costs of raw materials	• -

A sample based on 51 plastic companies registered at the Association of Lebanese Industrialists (ALI) reflects on the product segmentation of the sector. The biggest number of companies are specialized in food packaging (plastic cups, salad boxes, plastic, and cutlery) followed by containers and bottles (water bottles, detergent bottles, water container), next in line are pipes, home furniture, raw materials, agricultural materials, bags, hospital materials and industrial materials. It is worth mentioning that by raw materials we are referring to companies that collect and then recycle scrap from restaurants, garbage…etc.

Product Segmentation in the Lebanese Plastic Industry

Type of Plastic Product	**Number of Registered Companies**
Food Packaging: Plastic cups, salad boxes, plastic cutlery	11
Containers and Bottles: water bottles, detergents, water containers	9
Pipes	8
Home Furniture	7
Raw Materials: collecting scrap from restaurants, garbage and then recycling	6
Agricultural Materials	5
Bags	3
Hospital Materials	1
Industrial Materials	1

Source: Association of Lebanese Industrialists

Types of materials used in plastic manufacturing depending on final use of plastic product

Type of Plastic Product	Materials
Food Packaging: Plastic cups, salad boxes, plastic cutlery	Polyethylene terephthalate (PET), Low density Polyethylene (LDPE), Polypropylene (PP),Polystyrene (PS)
Containers and Bottles: water bottles, detergents, water containers	High Density Polyethylene (HDPE)
Pipes	PVC Polyvinyl chloride
Home Furniture	PVC Polyvinyl chloride
Agricultural Materials	PVC Polyvinyl chloride, Low density Polyethylene (LDPE)
Bags	Low density Polyethylene (LDPE)
Hospital Materials	High Density Polyethylene (HDPE)

Source: Etablissement Fawzi Haddad

The Lebanese market holds both plastic manufacturers and plastic importers and distributors. According to Lebanese customs, in 2014, Lebanon imported $695.01M worth of raw materials needed for the manufacturing of plastic and finished products. On the other hand exports of both raw materials and finished products totaled $130.59M.

The plastic market is large in Lebanon if nothing but our net exports of raw materials and finished products totaled $565.69M. In 2014, the net exports of raw materials amounted to $353.73M while the net exports of finished products amounted to $211.96M.

The major imported items in the plastic category are raw materials. The polymers of ethylene and propylene, which are used across all segments of plastic manufacturing as shown in the table above, hold the largest combined share of 28% in total imports with a value of $203.12M. 57.82% or $92.69M of the ethylene polymers originated from Saudi Arabia in 2014 while 14.27% or $22.88M were imported from Qatar. Saudi Arabia is also the main import source of propylene polymers accounting for 64.57% or $27.64M of total propylene imports while 23.30% or $9.97M originated from the UAE.

In 2014, the finished articles of conveyance and packing of goods also hold a sizeable 8% share in total plastic imports with a value of $57.19M. The main import sources for those articles are Jordan with a 14.45% share or $8.26M, China with a share of 13.77% or $7.88M and Turkey with a share of 13.59% or $7.77M.

As for tubes, hoses and pipes, they constituted 6% or $44.66M of total plastic imports in 2014. 23.41% or $10.45M of those items originated from Italy while 15.95% or $7.12M originated from Turkey.

Meanwhile, the main exported plastic items in 2014 were articles for the conveyance or packing of goods. Their total value amounted to $29.49M in 2014, representing 23% of total exports. Interestingly, the main export market was Syria with a 15% share in the total or $4.35M, followed by 12% or $3.55M for Saudi Arabia and 12% or $3.48M for Jordan.

The second largest exported items are tableware, kitchenware and other household articles with a share of 9%in total exports. Exports of these items registered a value of $12.08M in 2014. 16% or $1.94M were sent to Iraq and 11% or $1.38M were sent to Saudi Arabia.

Elements on the global markets such as the exchange rate of the euro and oil prices greatly affect the cost structure of Lebanese Plastic companies. If the euro is weak and oil prices are low, the cost of raw materials for manufacturers and the cost of finished product for importers and distributors are pushed downwards.

However, costs are pushed upwards by the hefty spending on energy. The plastic industry is an energy intensive industry especially given the high conversion costs of raw materials into finished plastic products. A recent labor law has also weighed on the costs of plastic factories. As of 2014, companies were compelled to guarantee each Syrian worker they employ. The guarantee costs around $1,000/year/worker and must be renewed each year.

Although the plastic industry benefits from much strength, it suffers from the unlawful competition on the Lebanese market. According to a market source, certain plastic factories infiltrated the market and lowered prices as they were not paying their taxes. This compelled legal factories to secure a proper mark-up by tapping into foreign markets. Companies such as Etablissement Fawzi Haddad tapped into Gabon, Niger, Ivory Coast and the Democratic Republic of Congo. The company states that one of the benefits of tapping into foreign markets is the fact that no sales on credit occur.

In the biggest segment of the industry, which is food packaging, the biggest players are General Packaging Industries (GPI), Bekaplast and Somoplast. The market's dynamics between these players are smooth. According to a market source, each plastic company on the Lebanese market has its own known-clients and operating strategy. The pricing system is highly dependent on the quality of the offered product and on the targeted clientele. It has been reported that the average mark-up on the market is around 17%. The pricing also varies whether or not intermediaries are involved. The price is surely lower when intermediaries are involved to guarantee profit for the middle-man.

As for the market of plastic pipes in Lebanon, different companies meet the demand of different areas on the Lebanese territory. Dagher Plast covers the demand for pipes in Mount Lebanon, Beirut, and the north while Haykal Plast and Plastypipe cover the regions of Bekaa and the south. A prominent leader in this market is Advanced Plastic Industries (API) a manufacturer of high quality polypropylene (PP-RCT) pipes and fittings which has acquired numerous international certifications and that meets internationally recognized standards.

The large-sized plastic pipe companies in Lebanon import raw materials and then manufacture the pipes at home and even supply the smaller companies with the finished pipes. The most important raw material that is imported is PVC resin, to which are added pigments and additives in the manufacturing process. The source of the PVC resin differs from one company to the other. Per example, Dagher Plast imports PVC resin from Europe and China while Haykal Plast acquires the raw material from the United States, The Kingdom of Saudi Arabia and France. Interestingly, the United States became the top provider of PVC resin instead of the Kingdom of Saudi Arabia after the Syrian crisis disrupted land trade routes.

PVC pipes have multiple uses and different clienteles. According to market sources, the pipes can be used for drainage and sewage, water conveyance, soil and waste discharge within the building structure. There are also PVC accessories such as PVC fittings which constitute sockets for the PVC pipes. The main clients for these products are construction sites and public works. Market sources have also noted that demand for these products has remained robust and on an upward trend despite the overall economic downturn due to the inelastic and un-substitutable nature of plastic pipes' demand.

The pricing on the market is dependent on the thickness of the pipes. For a 6 meter-long pipe with a thickness of 2.4 mm the price is at $6 while for a 6 meter-long pipe with a thickness of 7.7 mm the price surges to $115.

For plastic food packaging companies and plastic pipe companies alike, oil prices and the exchange rate of the euro hold a great influence on costs and profits. Plastic pipe companies benefit in the cases where the purchase of raw materials has been made with a devalued euro and where the selling of the goods on the local market occurs when the euro has appreciated and vice-versa. Pipe manufacturers have also confirmed the positive influence lower oil prices had on their costs but no figures were released for confidentiality purposes.

Lebanese plastic pipe manufacturers have tapped into foreign markets. Per example, Dagher Plast mainly exports PVC accessories such as PVC fittings and most recently tapped into the Iraqi market. Meanwhile, Haykal Plast reported exports to African countries.

For polyethylene agricultural films, the largest manufacturer in Lebanon is Masterpack, member of Indevco Group. Masterpack holds 90% of the Lebanese market and estimates the size of the market to be between $10M to $12M. Masterpack imports polyethylene resin in order to manufacture the agricultural films in Lebanon. The main import source is

the Saudi Arabian company SABIC. Commenting on the effect of lower oil prices, a source from Masterpack highlighted that although lower oil prices meant lower prices of raw materials it also meant that the selling prices of the finished films had to be lower in order to "follow the market". The price of agricultural films ranges from $2 per kg to $3.5/$4 per kg and is considered to be competitive. It's this competitiveness that allows Masterpack to export 70% of its annual turnover or around 23,000 MT to over 68 countries in the Middle East, Europe, Asia, Australasia and Africa.

VII. The Lebanese Jewelry Sector: Success Story, Locally and Abroad

According to the Syndicate of Expert Goldsmiths and Jewelers in Lebanon (SEGJL), Lebanon stands out as a leader in jewelry and gold production in the Middle East, employing 8,000 people with 2,000 qualified jewelers at around 60 main workshops. This industry grew in a way to become heavily dependent on regional sales, either through exports or targeting Gulf tourists. The president of the Lebanese Syndicate of Goldsmith and Jewelers estimates exports to the Gulf to account for about 50% of total gold sales. Also, Swiss jewelry brands are importing unfinished products to Lebanon and using the cheaper and highly skilled craftsmanship here to turn them into finished products and export them back to Switzerland.

- The jewelry sector contributes to around 16% of Lebanon's GDP
- Lebanese jewelry market offers products ranging from fashion or costume jewelry to high-end jewelry.
- Estimates for sales of jewelry reveal that 10% of Lebanese jewelry is sold locally while 90% is exported and sold abroad.
- Lebanon possesses a comparative advantage in the industry, enjoying highly-skilled and experienced low-cost craftsmen
- Lebanon is home to an annual exhibition, "the International Jewelry and Watches" Exhibition that ranked among the Middle East's most prestigious jewelry exhibitions. Wholesales and high end brands from around the globe participate to showcase their finished and variety of stones.
- Global diamond demand projected to grow more than 6% per year through 2020.
- Jewelers in Lebanon are not subject to custom duties on raw material or unfinished products.
- Imported finished jewels are subject to a 25% custom duty, in addition to the 10% VAT.
- Other than having the know-hows, there are no barriers to enter the jewelry market in Lebanon.
- The presence of international brands in the local market does not threaten the business of local jewelers as they offer products of a quality that competes with that of international product and at more affordable prices.

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Lebanese Jewelry Industry: Radiant yet Opaque

Jewelry has been lustrous, having unfathomable significance in different cultures. It has been cherished not only for its ornamental worth, but also for its use as a form of wealth, expression, and body modification. Besides, precious stones and gems were worn as amulets to ward off negative energy.

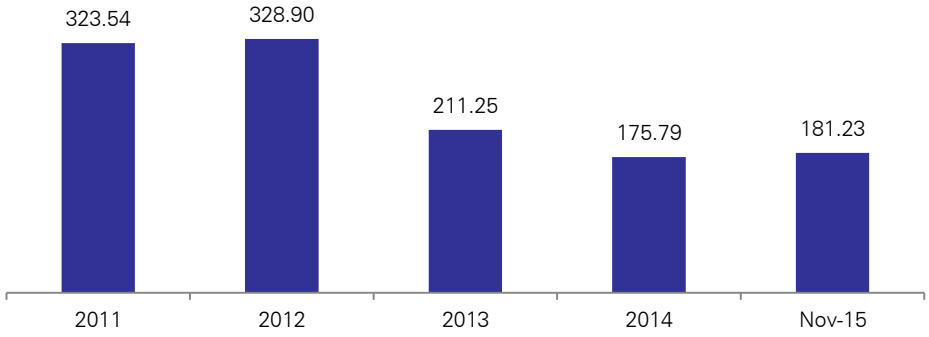
The jewelry industry has a long history in Lebanon. Jewelry designers have been passing their know-how from one generation to the next, engraving their names around the globe. Lebanese jewelers have thrived throughout the world, becoming the country's ambassadors. Not only do international celebrities wear Lebanese jewelry, but also, the Princess of Monaco, Charlene Wittstock, was adorned on her wedding day in a bespoke necklace made of rose gold set with diamonds and pearls designed by House of Tabbah.

The jewelry market in Lebanon is a large and competitive one, with few names leading the market. The size of the Lebanese jewelry market is estimated at $600M, fragmented to 3 groups, each targeting a specific clientele. Some of them are very active in the low end segment of the market, others in the medium segment, with only few jewelers targeting the high-end.

Secrecy dominates over the jewelry industry. This industry has always been opaque, with an unidentifiable accurate size of the market and a high level of confidentiality within companies in the industry. However, Nada Le Cavelier estimates that 75% of the jewelry market is locally produced, with the remaining 25% being imported.

" Pearls, precious stones and metals" exports are considered the second main exports of Lebanon, with a share of 15%, or $407.26M in the first 11 months of 2015. However, 56% ($226.02M) of this value consists of gold ingots. 22% ($87.91M) consists of finished diamonds for nonindustrial use. The major markets for Lebanese exports of "pearls, precious stones and metals" are South Africa (44%), United Arab Emirates (25%), Switzerland (13%), Saudi Arabia (5%) and Hong Kong (3%). In fact, exports are largely underestimated as a large part of Arab buyers purchase jewelry when they are in Lebanon. In 2014, "pearls, precious stones and metals" dropped in value by an annual 29.63% to $541.66M, however at a volume of 39.34% higher than the previous year, at 85 tons. Worth noting that according to the European Ministry of Foreign Affairs, Lebanon is the 5th largest exporter of jewelry to Europe, with a 4% share in 2014, up from a share of 0.4% in 2013.

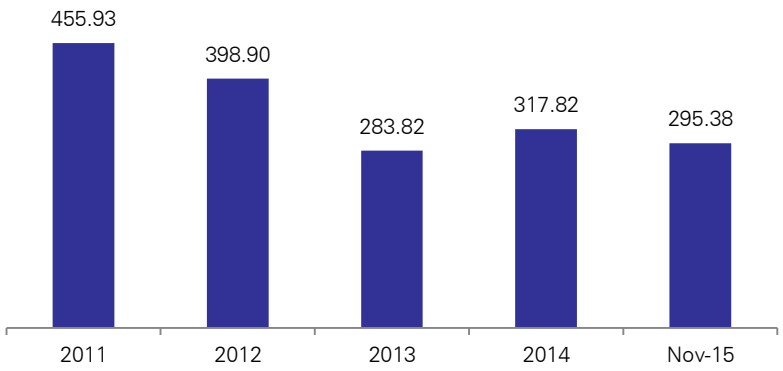
Lebanon's Pearls, Precious Stones and Metal Exports Excluding Gold Ingots ($M)



Source: Customs

As for imports, they stood at $738.03M by November 2015, 60% of which are gold ingots with a value of $442.65M. 25% of "pearls, precious stones and metals" consist of diamonds for nonindustrial use, having a value of $185.39M up to November 2015. The major jewelry importers to Lebanon are Switzerland (24%), Togo (20%), Belgium (15%), United Arab Emirates (12%) and Benin (4%).

Pearls, Precious Stones and Metal Imports to Lebanon Excluding Gold Ingots ($M)



Source: Customs

Unlike the rest of the economic sectors, the jewelry industry preserved its shine, with its sales remaining resilient in the face of the global economic and political upheavals. Demand has been shifting towards diamond and other precious stones in the past 8 years, as it has become more fashionable than only gold medallions. George Kazazian from HIMO jewelry and Nada Le Cavelier both estimate that demand is divided equally between gold alone and gold with diamonds and precious stones.

Other than being a tradition to offer jewelry for many occasions, the robustness of the industry is derived from various factors. First and foremost, Lebanon has a comparative advantage in producing jewelry compared to the European countries. Lebanon enjoys highly-skilled and experienced low-cost craftsmen. One labor hour in the jewelry industry in EU costs €100, whereas in Lebanon 8 labor hours cost $500, equivalent to $62.5/hour. Moreover, EU jewelers pay high marketing costs to promote their products. Finally, there is a higher multiplier effect in Europe compared to Lebanon; Lebanese items come straight from the manufacturer to the retailers. In contrast, the jewelry passes through many intermediaries in Europe before reaching the retailer. In addition, Rosy Zaarour from Zoughaib jewelry states that gold produced in Lebanon is of a more refined quality than that of the EU and the US. Most of the gold in Lebanon has a purity of 18 carats or 21 carats, compared to 9 carats and 14 carats in the EU and US. In addition, the high competition in the Lebanese market results in relatively lower prices. Furthermore, unfinished precious stones and metals imported are free from any tax.

Another reason for the buoyancy of this industry is the wide and disparate customer base. According to George Kazazian, 70% of sales are to local customers, while 30% are sold to foreigners. Lebanese jewelers have diversified their income sources, decreasing fluctuations in their sales, by opening in the Arabian Gulf, Paris, London, Geneva, New York, and

beyond. Not forgetting to mention that most of the clients of this industry come from the middle and upper classes, which are less affected by the economic disturbances.

Furthermore, jewelry, gold in specific, is considered as a safe haven. According to Rosy Zaarour, many people bought gold coins and gold jewelry when gold price dropped in the past year, in anticipation of making a profit when its price increase again. George Kazazian stated that people prefer buying jewelry since it retains more than half of its price.

Jewelers were affected differently by the Arab spring and the decrease in tourism. According to Zoughaib, the Syrian war only interrupted the shipping process but had no effect on sales. Vending to foreigners persisted via online demand. On the scope of outlets however, their branch in the airport saw a decrease in sales. Yeprem jewelry states that demand was not affected. In contrast, other jewelers were positively affected as rich refugees in Lebanon, from Iraq and Syria, pushed demand up. Hence, one source revealed that its turnover increased by an annual 15% in 2015. However, due to the global recession and political problems, exports to Ukraine, Africa, and Dubai decreased. HIMO pointed out that January used to be one of the high seasons for jewelry as most expats and Gulf nationals used to spend New Year's Eve in Lebanon. This has not been the case for the past two years.

Most market players in the jewelry industry claimed that they were not affected by the volatility in gold prices, and hence do not adopt any hedging strategy. This comes from the fact that jewelers set their prices in relation to the items' weight. Zoughaib mentioned that they experience a lower turnover when gold prices increase since their products are more concentrated on gold. Jewelers specialized in diamonds and precious stones are affected the least, since gold is used only as a support for the gems and constitutes a maximum of 10% of the item's value. One jeweler indicated that when gold prices fluctuate, the price per ounce of gold charged is the average weighted price over a certain period.

Due to all these advantages, Lebanese jewelers face no competition from the presence of international jewelry brands in the local market. In spite of this, jewelers from the high-end segment encounter rivalry with these brands as they have the same taste and price range and target the same clientele of high-income earners.

Nonetheless, all that glitters is not gold. The Lebanese jewelry industry is highly unregulated and lacks transparency. A few jewelers mix diamond with zircon and sell the item as if it were made of only diamonds. Moreover, they sell diamonds to clients with a certificate indicating that its size is bigger than it actually is. In addition, as there are no barriers to entry, people with no prior education or experience concerning jewelry and the quality of precious stones, can join the market. As a consequence the Lebanese jewelry industry is being flooded by copied items or by poorly manufactured trinkets, with sometimes fake stones. Some of the market players suggest that the Lebanese Syndicate of Jewelers creates a laboratory where clients can be reassured of the quality of ornaments they are buying.

Competition from the Asian manufacturers also constitutes a challenge to the Lebanese jewelry industry. Some Lebanese jewelers have established factories in Asia and taught artisans the trade. These new craftsmen are sought after by the West, due to the cheaper labor costs.

Laws should be implemented to eliminate unhealthy competition and keep the market clean. Independent laboratories to ensure stones' quality and protect consumers would enhance transparency.

However, one main forte for Lebanese jewelers is being proactive, owning a talent for design innovation, and remaining up-to-date. These qualities were the main reasons that burnished the Lebanese jewelry industry, leading designers to bourgeon globally.

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VIII. Lebanese Eurobonds and Treasury Bills, Reliable and Profitable

Through its economy's many ups and downs, Lebanon has never defaulted on its debt. The Ministry of Finance holds regular and successful Treasury Bills (T-Bills) auctions in which new subscriptions exceed maturing T-bills often. Lebanon recently completed the largest Eurobonds issuance in its history with a value of $2.2B that was largely oversubscribed with demand reaching $4.9B. Despite a tough operating environment, both local and foreign investors subscribed to the Eurobonds issuance.

Lebanese Treasury Bills offer attractive yields when compared to the MENA region…

Percentage Yields of Government Bonds in the MENA Region

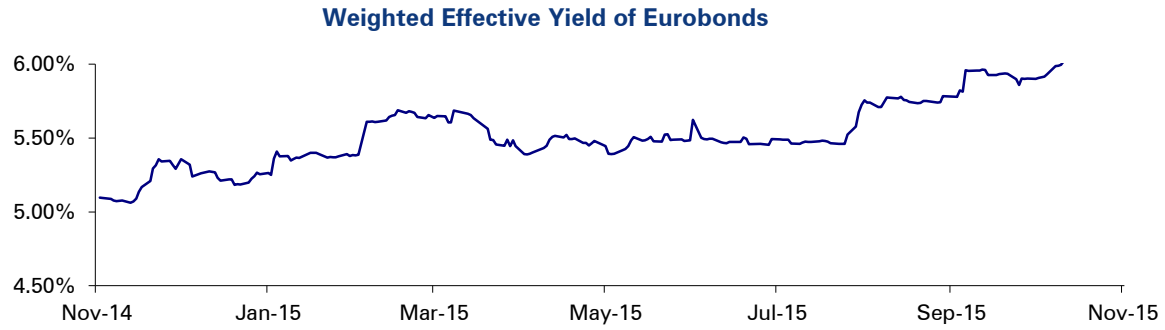
Maturity	Jordan	Qatar	Saudi Arabia	Bahrain	Lebanon's Treasury Bills in LBP
3 Months	2.35	1.27	1.12	0.723	4.44
1 Year	2.545	-	1.36	1.255	5.35
2 Years	2.765	2.25	1.26	2.42	5.84
5 Years	3.928	2.39	-	4.2	6.74

Source: Reuters, Banque du Liban

Face Value of Lebanese Treasury Securities in October 2015

Outstanding Lebanese Treasury Securities Denominated in LBP	42.22 Billion USD
Outstanding Lebanese Treasury Securities Denominated in FC	23.50 Billion USD

Source: Association of Lebanese Banks



Source: Blominvest Research Department

Yield on Selected Maturities of Lebanese Eurobonds

5Y	6.48%
10Y	6.88%
15Y	7.27%
20Y	7.34%

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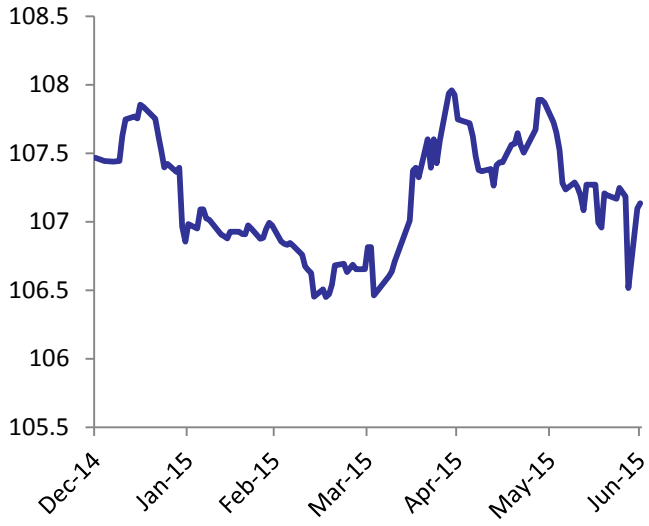
Lebanese Eurobonds Still Benefitting from Investor Confidence in H1 2015

Performance of the BLOM Bond Index (BBI) in H1 2015



Source: Blominvest Research Department

The year 2015 still portrayed key problems for Lebanon on the political and economic fronts. Parliamentary sessions for the election of a new President were and, are still, regularly postponed, rendering legislation and decision making ever more difficult. On the economic front, external and fiscal deficits have persisted, pushing the public debt further up.

The performance of the Lebanese Eurobonds' market in the first six months of 2015 was rather subdued, but remained relatively resilient in the face of the sour economic and political scenes. In fact, the BLOM Bond Index (BBI) ended the first half of 2015 at 107.13 points, down by 0.31% year-to-date and down by 0.89% year-on-year. The weighted average yield of Lebanese Eurobonds, which is in an inverse relationship with the price, rose in H1 2015. After ending the year 2014 at 5.24%, the weighted yield surged to 5.49% at the end of June 2015.

The subdued performance of the BBI mainly came about due to lower demand for shorter term maturities as demand for medium and long-term maturities seemed to have been strong in H1 2015. The yields on the Lebanese Eurobonds maturing in 5 Years and 10 Years declined from 5.30% and 6.16% at the end of 2014 to 5.20% and 6.06% at the end of June, respectively.

In spite of Lebanon's economic issues, investors are still confident as shown by the successful Eurobonds issuance in February. In February, the Ministry of Finance launched a Eurobond issuance of $2.2B, the largest in history, with BLOM Bank, Citi, and Société Générale des Banques au Liban (SGBL) as lead managers. The issue was divided into two categories: the: $800M of 10Y Eurobonds maturing in 2025 and yielding 6.20%, and $1.4B of 15Y Eurobonds yielding 6.65%.

The issuance was successful with strong appetite from both local and foreign investors. The issuance was 5 times oversubscribed with bids hovering around $4.9B. International orders were promising as they were around 15%, which could be partly due to the overflowing cash in the global financial markets following the decreasing oil prices.

Details of Lebanon's Largest Eurobonds Issuance

	$800M Issuance	$1,400M Issuance
Issuer	Republic of Lebanon	Republic of Lebanon
Type	Bond	Bond
Coupon	6.65%	6.20%
Maturity Date	2030	2025

The ministry of Finance however noted that the amount of Eurobonds it is entitled to issue falls short of its 2015 needs. Parliament authorized only a $2.5B Eurobonds issuance for 2015, leaving the Ministry with leeway to issue only $300M worth of Eurobonds in 2015. However, the foreign financing needs of the government for the remainder of the year are at $2.2B.

In the US, the treasuries' market has proven its resilience even as an increase in federal fund rates looms ahead. The US Treasury Bond Index compiled by Bloomberg ended the year 2014 at 114.77 point, only to increase by 5.23% to 120.87 at the end of June 2015. The yield on the US Treasury notes maturing in 5 years slid from 1.68% at the end of 2014 to 1.63% at the end of June 2015. However, the yield on the benchmark 10 Year notes increased from 2.20% to 2.35% over the same period, indicating lower demand for those papers.

The US Treasury market continues to benefit not only from uncertainties regarding the date of the hike in interest rates but also from "worrisome" factors in the global economy. In fact, the Federal Reserve had initially announced that the interest rate liftoff would take place in June 2015 only to postpone that event to September 2015. Even for September, some market participants remain skeptical which in turn preserves the "safe asset quality" offered by US treasuries and keeps demand for them robust. Second, the "zero-risk" aspect of holding US treasuries continue to be appealing amidst global headwinds such as the Greek crisis and the economic slowdown in China in addition to the strong U.S. Dollar.

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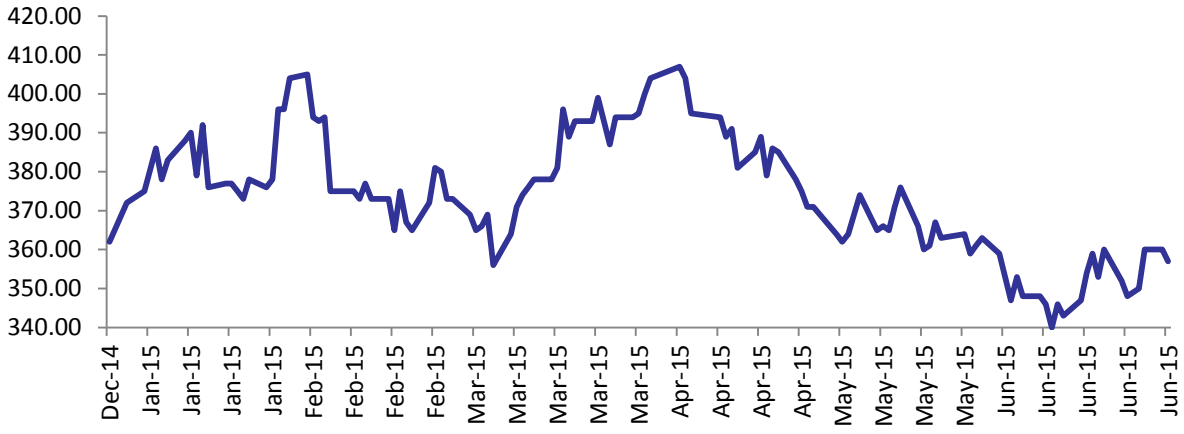
Major Foreign Holders of Treasury Securities, In Billions of US Dollars

Country/Date	Jun-15	Dec-14	Jun-14
China, Mainland	1,271.20	1,244.30	1,268.40
Japan	1,197.10	1,230.90	1,219.30
Caribbean Banking Centers	318.50	272.40	250.60
Oil Exporters	296.70	285.90	262.10
Brazil	256.30	255.80	253.70
Ireland	217.70	202.00	177.10
Switzerland	217.10	190.10	175.90
United Kingdom 2/	214.70	188.90	173.60
Belgium	207.70	335.40	364.10
Luxembourg	184.00	171.80	145.30
Hong Kong	181.30	172.60	157.60
Taiwan	175.60	174.40	179.40
India	117.00	83.00	72.90
Singapore	113.70	110.00	98.10
Mexico	86.30	84.80	72.80
Korea	76.70	68.30	57.50
Turkey	75.80	77.00	52.80
Germany	75.30	72.70	68.00
Russia	72.00	86.00	113.90
Canada	68.60	69.00	66.20
France	67.80	79.20	63.10
Norway	66.10	81.60	87.10
Sweden	40.00	39.60	34.90
Philippines	39.90	40.60	34.60
Colombia	37.80	34.70	33.50
Netherlands	36.80	36.20	36.30
Australia	34.10	34.50	35.30
Italy	33.00	31.90	31.30
Spain	31.60	27.70	23.20
Thailand	31.40	33.20	41.30
Chile	29.00	25.50	27.20
Kazakhstan	28.40	31.60	35.10
Poland	28.20	27.70	29.50
Israel	20.00	25.20	26.10
Denmark	17.10	16.70	16.00
Vietnam	13.60	14.00	14.40
Peru	11.60	10.90	12.80
All Other	185.70	189.90	208.20
Grand Total	6,175.20	6,156.00	6,018.70

Source: Department of the Treasury/Federal Reserve Board

Despite the ongoing political deadlock, investors' confidence in Lebanon's fixed income papers seems to have strengthened, which could be due to the stable security situation. The spread between the yield on the 5 Year Lebanese Eurobonds and their US comparable narrowed from 362 basis points (bps) at the end of December 2014 to 357 bps at the end of June 2015. The same goes for the 10 Year spread, which narrowed from 396 at the end of December 2014 to 371 bps at the end of June 2015.

5Y Spread between Lebanese Eurobonds and their US Comparable



Source: Blominvest Research Department

The notion of confidence and resilience on the Lebanese Eurobonds market is cemented further by the narrowing of the country's 5 Year Credit Default Swaps (CDS) quotes. The 5 Year CDS quotes, which reflect how investors perceive the government's risk of default, narrowed from 362-396 bps with a mid-price of 379 bps at the end of 2014 to 352-378 bps with a mid-price of 365 bps at the end of June 2015. This sign of increased confidence may have been brought about as the security situation in 2015 remained under control.

However, when compared to regional economies, Lebanon's CDS quotes remains quite high. At the end of June 2015, the 5Y CDS quote of Saudi Arabia stood at 58.04 bps, that of Dubai at 319.04 bps and that of Egypt at 303.67 bps.

When benchmarked against the emerging bonds market, the BBI was outperformed by the JP Morgan Emerging Markets Bond Index. The latter registered a 2.53% year-to-date increase to reach 674.99 points at the end of June 2015. As long as the low-interest rate environment persists, emerging bond markets will remain attractive to investors. Moreover, fears of any future volatility have been eradicated by some market players which believe that the outflows that could have been brought about by a potential Fed rate hike have already retreated from the market. According to the International Institute of Finance's Emerging Market (EM) Portfolio Flows Tracker, "EM Bond flows rose marginally to $1.2 billion in June, continuing a five month streak of subdued inflows (averaging $2 billion per month, compared to $15 billion per month in 2012-2014)."

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IX. The Beirut Stock Exchange, Undervalued Market Place with Future Potential

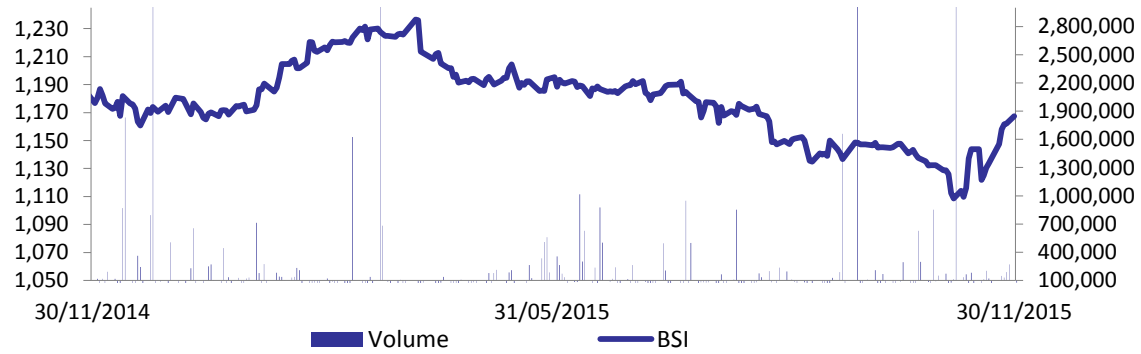
The Beirut Stock Exchange is home to banking stocks, real estate stocks, retail stocks and industrial stocks. Top Lebanese commercial banks have listed both common and preferred shares on the Beirut Stock Exchange. The Lebanese bourse is an undervalued market place and is therefore an attractive investment option. When it comes to the banking sector in particular, stocks are largely undervalued and banks offer relatively high dividend yields.

Through its laws and close monitoring, the Capital Markets Authority (CMA) is actively acting towards increasing the transparency and the depth of the Beirut Stock Exchange.

BSE Figures as at 30/11/2015

Number of Listed Stocks	29
Market Capitalization	9.7 billion USD
Banking sector, % share in total traded value	83%
Real estate sector, % share in total traded value	16%
Industrial sector, % share in total traded value	1%
Retail sector, % share in total traded value	0.04%

Performance of the BLOM Stock Index



Source: Blominvest Research Department

Ratios for the Top Three Lebanese Banks (Bank Audi, BLOM Bank and Bank Byblos)

Average Price to Book	0.8
Average Dividend Yield	7.7%

Source: Reuters

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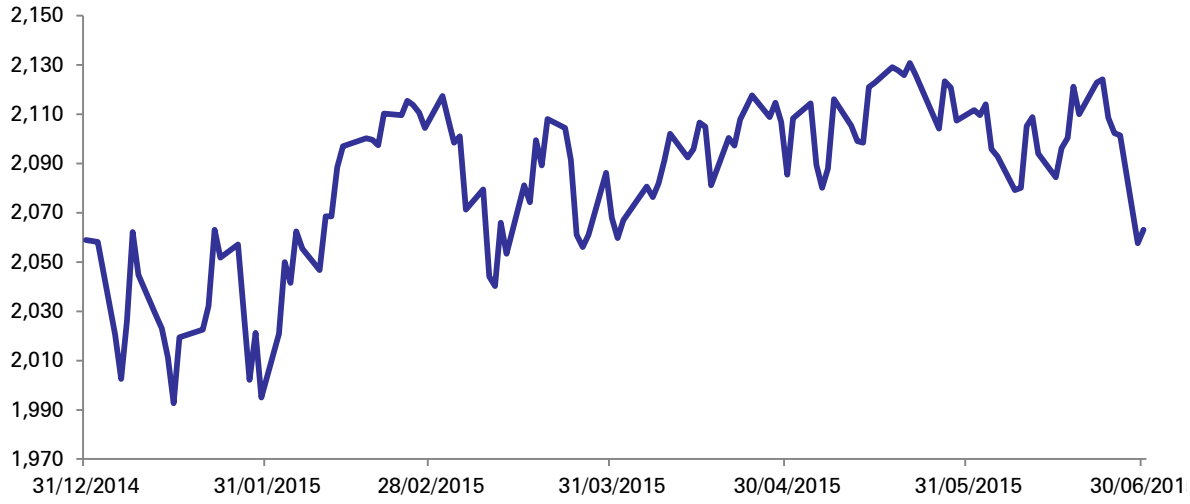
Beirut Stock Exchange: H1 2015 Performance Review

While major financial markets today are considered to be free-floating, dictated almost unconditionally by demand and supply, there exists ample evidence of monetary authorities playing primary roles in swaying market activity. The stand-out economic factor influencing global markets this year has been the bearish trend in oil prices. On the other hand, central banks play their part in market manipulation via monetary policy decisions. Divergent central bank monetary policies yield varying results on their respective markets. Currently, the U.S. looks toward interest rate policy normalization, Europe and Japan advance their quantitative easing (QE) programs, and many emerging markets lower interest rates to stimulate growth.

The U.S. stock market took a breather relative to most global peers while still posting positive returns. U.S. stocks displayed modest gains as investors struggled with uncertain global growth, oil price volatility and the timing of the Federal Reserve's impending interest rate hike. The Standard and Poor's 500 Index (S&P 500) ticked up marginally by 0.20% since year-start, to 2,063.11 points end of June 2015, compared to 2,058.90 points end of 2014. The dollar strength in the face of monetary easing elsewhere in the world helped keep a lid on U.S. share prices.

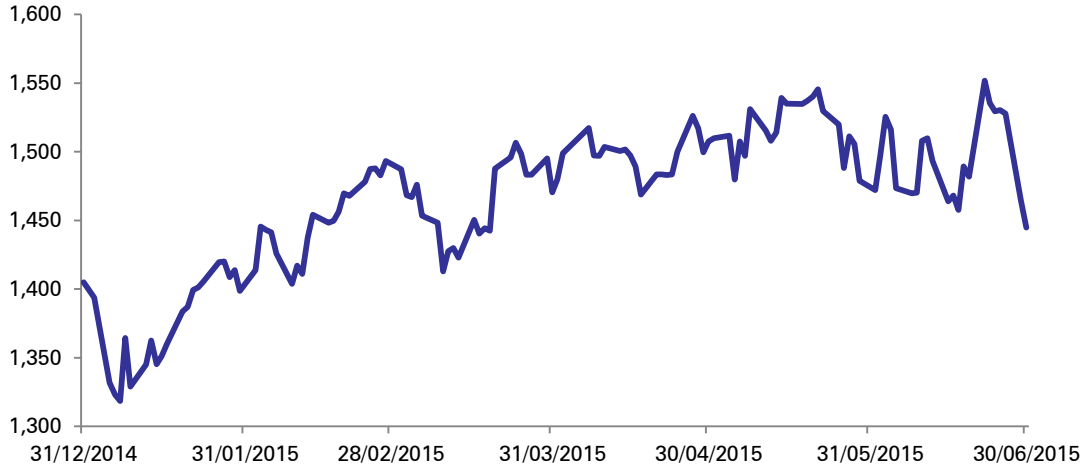
S&P 500 Index



Source: Reuters

European stocks powered ahead, boosted by improving economic data, falling oil prices and an aggressive new stimulus program launched by the European Central Bank. Signs of a brighter economic outlook emerged in the form of accelerating retail sales, rising export activity and improved credit availability for businesses and households. Much of the optimism was attributed to the start of the ECB's €60B/month bond-buying initiative, which is designed to encourage lending and stimulate economic growth. Despite renewed strains emanating from Greece that it might exit the Eurozone, the Euro Stoxx 50 Index enjoyed double-digit y-t-d gain, increasing 10.25% from 3,146.43 points end of 2014, to 3,468.90 points in June 2015. The drop in the euro over the past few months has helped fuel appetite for European stocks, as investors bet the lower currency will spark a corporate resistance after years of stagnating profits.

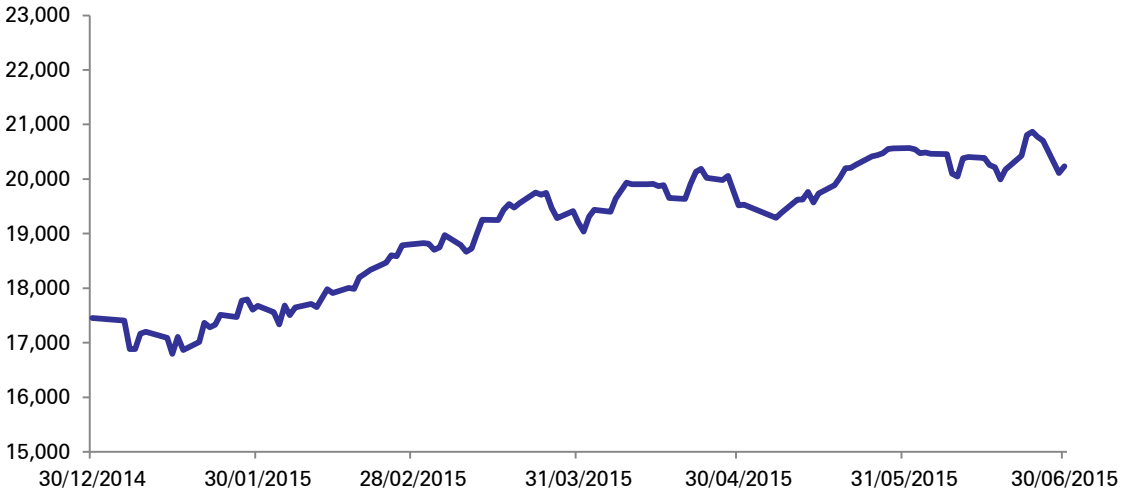
Euro Stoxx 50 Index



Source: Reuters

Similarly, equities rallied in Japan, bolstered by Bank of Japan's unconventional monetary policy. Supported by the QE-induced fall of the Yen, the Nikkei 225 Index swelled 15.96% y-t-d to 20,235.73 points end of H1 2015, relative to 17,450.77 points end of 2014. Strong corporate earnings and optimism that companies would begin raising dividends also contributed to the improvement of stocks in Japan.

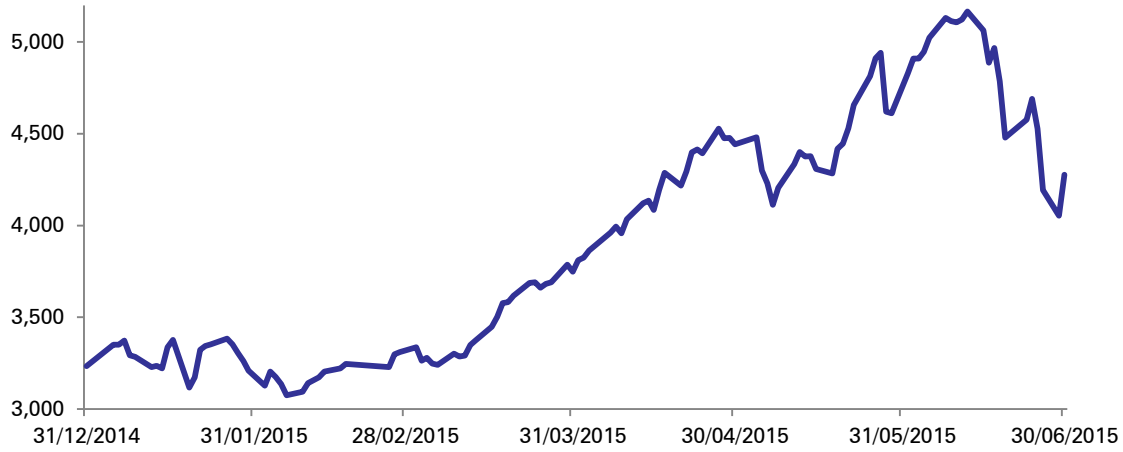
Nikkei 225 Index



Source: Reuters

Despite the shock that the Chinese stock market faced in mid-June 2015, the Shanghai Composite Index managed to post a 32.23% y-t-d growth to 4,277.22 points end of H1 2015. Weak economic conditions did not deter investors from pumping their money in the bourse, until the index reached its 52-week high of 5,166.35 points on the 12th of June, thereby causing China's asset bubble to burst. This resulted in the 29% decrease in the gauge from the peak on the 12th of June to end July at 3,663.73 points.

Shanghai Composite Index



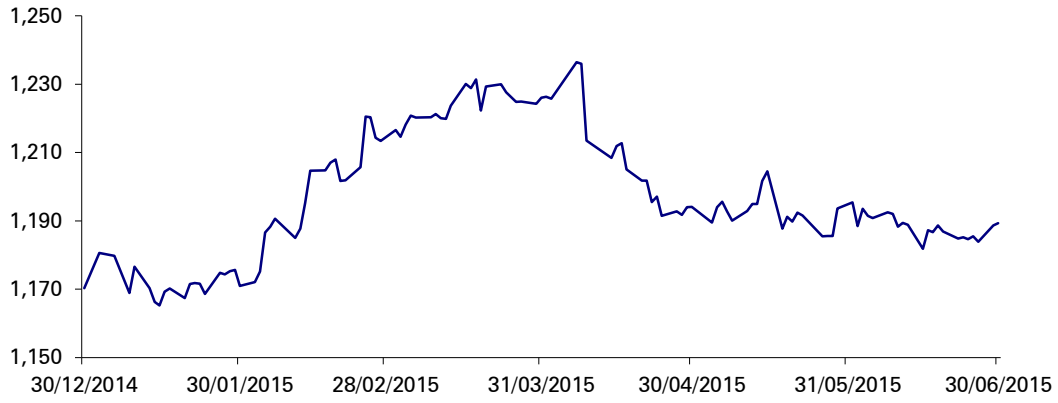
Source: Reuters

In the Arab world, Tunisia's Stock Exchange was in the lead, with a 12.36% gain since year-start. Four years after Tunisia sparked off the Arab spring uprisings, the country's stock market is reaping the benefits of political stability, steps toward reform, and declining oil prices. In 2013, Tunisia signed a 2-year deal with the IMF, agreeing to follow certain economic policies such as keeping its deficit under control, making its foreign exchange market more flexible.

On the other hand, the Egyptian Bourse recorded the biggest y-t-d decline. The decision of postponing the application of the 10% capital gains tax for 2 years and its positive vibes on the Egyptian stock market failed to boost the performance of the country's benchmark index. In fact, the security turbulences that the country encountered drove the EGX30 down by 6.22% y-t-d in the first six months of 2015. However, to improve the benchmark index, the Egyptian bourse stated a plan to reduce the required free float for new companies to be listed on EGX30, starting August 1. In details, the new equal-weighted index will include the top 50 listed companies in terms of liquidity.

As for Lebanon, the Beirut Stock Exchange (BSE) showed a mild recuperation, as the political and security situation acted as a headwind on investors' sentiment. The BLOM Stock Index (BSI) gained 1.63% y-t-d to end H1 2015 at 1,189.31 points, compared to 1,170.26 in December 2014. The volume of traded shares dropped from 28.10M shares worth $173.73M in H1 2014, to 25.72M shares, however at a higher value of $220.83M.

BLOM Stock Index



Source: BLOMINVEST Research Department

30 stocks were listed on the BSE, end of H1, 2015 with the number of outstanding shares edging up 3.86% y-o-y to 1.56M shares. This was due to the listing of 50M Audi common shares in September 2014, 4,762,000 Bank of Beirut (BoB) Priority 2014 shares in October 2014, and 3M BoB Preferred shares class "J", in February 2015.

Of the total traded value, the banking sector grasped the lion's share of 79.29%, followed by the real estate sector and the industrial sector, with respective stakes of 20.59% and 0.12%. RYMCO, the only listed company belonging to the retail sector, witnessed no trades in 2015.

The top performing shares in the banking sector were BLOM common shares, whose price surged 11.36% since the end of 2014, to $9.80. The common shares of BEMO and of Audi followed, recording rises of 8.57% and 3.83% y-t-d to $1.90 and $6.23, respectively.

On the other hand Audi GDR shares and BLC preferred shares class "A" were the worst performers in the banking sector, shedding 8.50% and 2.91% to $6.03 and $25.5, respectively. In addition, Bank of Beirut Preferred shares classes "E" and "H" lost 2.86% each, to end H1 2015 at the same price of $25.5.

In the real-estate sector, Solidere shares classes "A" and "B" gained 1.41% and 0.53% to $11.48 and $11.40, respectively.

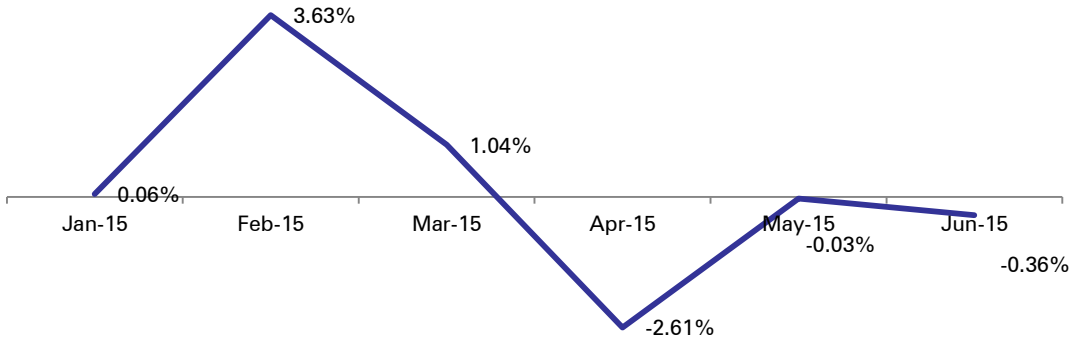
In the industrial sector, HOLCIM shares and Ciments Blancs bearer shares dropped 0.33% and 19.47% to $15.20 and $3.02, respectively. Ciments Blancs nominal shares were not traded in 2015.

Regarding the preferred shares, the BLOM Preferred Shares Index (BPSI) lost 1.15% to end H1 2015 at 104.71 points. BEMO preferred shares 2013 were the only preferred shares to record a gain since the beginning of 2015, adding 1.20% to $101.20. The preferred shares of Audi class "E", of BLC classes "B" and "C", and that of Bank of Beirut preferred "J" saw no change in their prices.

Looking at the monthly performance, the BSE fared better in the first quarter of 2015 than in the second quarter. In details, the BSI saw monthly gains of 0.06%, 3.63%, and 1.04%, in January, February, and March, respectively. Optimistic expectations tend to prevail at the start of a calendar year, and can explain the slight upturn in market performance over the first month. Moreover, security stability and the positive earnings results of listed banks for 2014 allowed the BSI to stay on its bullish trend. In addition, the CMA announced during Q1, that it will authorize the launching of an electronic market for digital trading. This electronic exchange will be run by the BSE if the government privatizes the bourse. If not, the online bourse will be independent and owned by the private sector.

Market conditions soured in April due to significant political and security turbulences. As a result of more increased focus on developments in Qalamoun (region on the border between Lebanon and Syria) between Syrian government forces and rebel factions, the BSI witnessed a 2.61% decrease in April. The downward trend continued in May and June, though at a slower pace, declining by 0.03% and 0.36%, respectively.

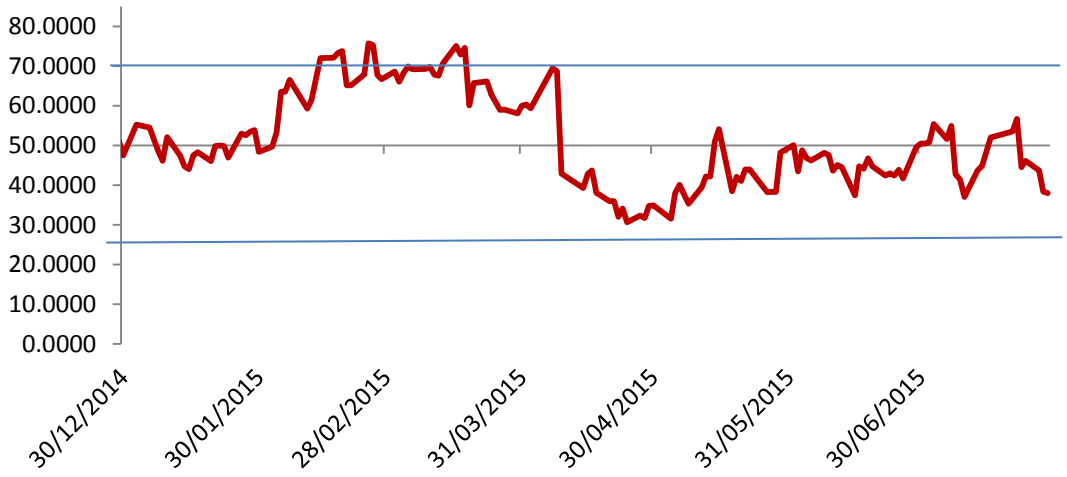
BLOM Stock Index Monthly Performance



Source: BLOMINVEST Research Department

Looking forward, the BSI is expected to improve slightly at the end of July, if listed banks released positive financial results for H1 2014. However, this progress would not last, unless solutions emerge on the political front. Another way to predict the trend of the BSI for the rest of the year is examining the Relative Strength Index (RSI). The RSI, a momentum indicator measuring the speed and change of price movements, shows when the index is overvalued (when it hits the 70-mark) or undervalued (when it hits the 30-mark). In Q1 2015, the RSI surpassed the 70-mark, after banks recorded positive financial performance for fiscal year 2014. In April, the RSI hit the 30-mark, however without crossing it, due to security uprisings. In the coming months, the BSI is expected to continue its sideways movement, unless developments concerning the presidential vacuum emerge, boosting investors' sentiment.

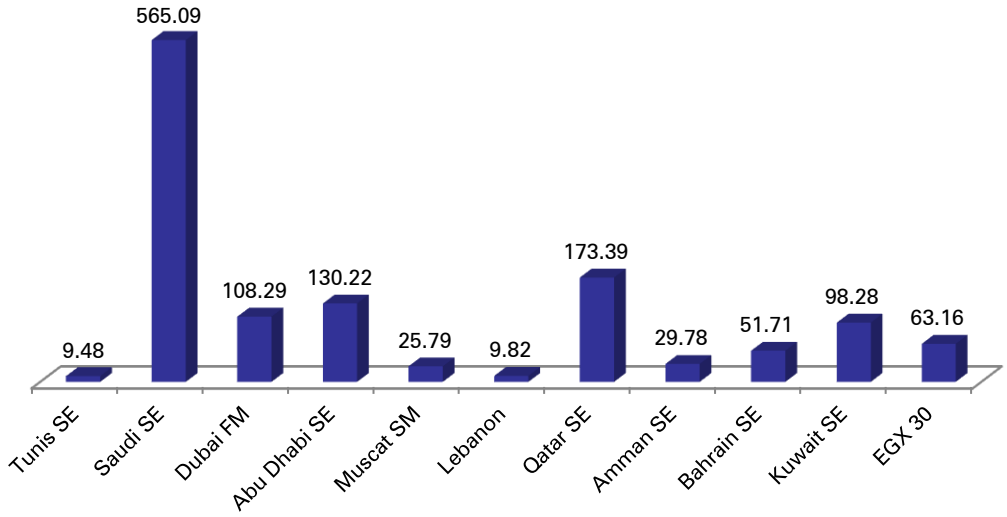
RSI for the BSI



Source: BLOMINVEST Research Department

Looking at the market capitalization of the BSE compared to the MENA region, it is the smallest after Tunis, at $9.82B.

Market Capitalization ($B, as of end July 2015)



Source: Zawya, BLOMINVEST Research Department

Many steps can be taken to improve the Liquidity of the BSE. For instance, privatizing the Beirut Stock Exchange would provide incentive for the shareholders to increase activity because it would be run as a for-profit business. Turning the BSE into a privately held company would make it more efficient in attracting local and regional companies to list on the BSE.

Other options to increase supply on the stock exchange include listing government-owned companies, as well as creating incentives for family-owned companies to list. This could be done through tax incentives, such as providing a tax waiver.

Moreover, there is a need to change an entrenched culture which is focused on short-term financing secured by banks. This would in no way adversely affect the work of commercial banks. In fact, well-developed capital markets would complement and support the activities of banks and vice versa.

Laws and regulations should change to encourage the creation of pension funds, which are the major investors in most stock exchanges.

Separating the stock exchange management and the regulating authority on one hand, and privatizing the stock exchange on the other, would have a great importance on Lebanon's Bourse. Splitting regulation from management reinforces market transparency and widely opens the market to institutional investors especially when the control is performed by an independent administrative authority with undisputed credibility. As for handing the market management to the private sector, it certainly develops the market activity by increasing the number of issuers and diversifying the financial instruments. Moreover, corporatization brings in new technologies such as stock trading on electronic communication networks, provides a level playing field, thereby encouraging competition and facilitates mergers with other exchanges reinforcing the market capitalization.

In this context, the creation of the CMA was an important step towards developing and regulating the stock exchange. The CMA has started to issue regulations aimed at increasing transparency and protecting investors. But more is awaited regarding the issuance of circulars aimed at developing the stock markets in capitalization and depth.

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