Lebanese Eurobonds' Performance H1 2016

BLOMINVEST BANK

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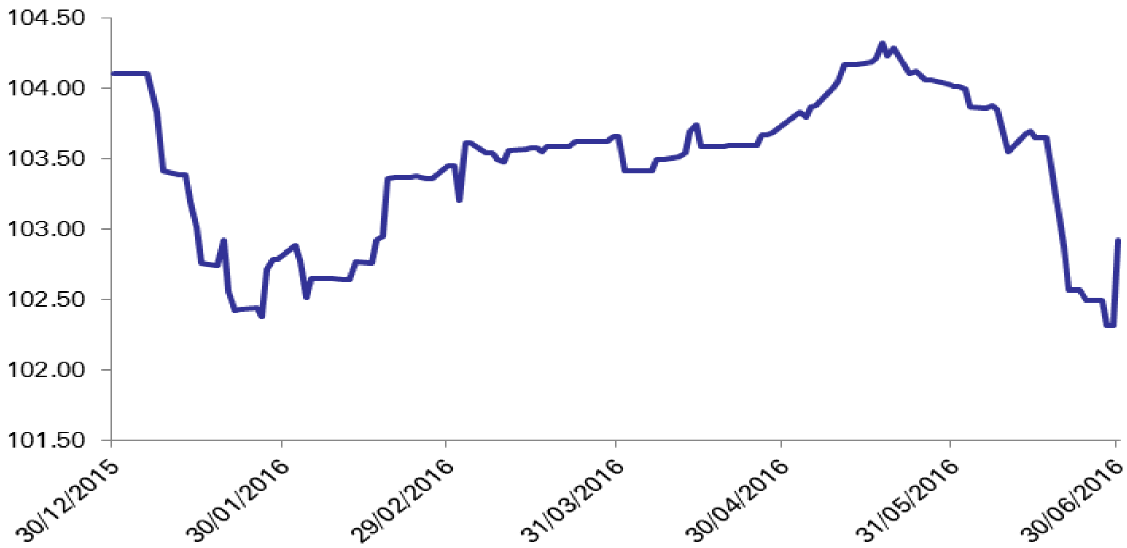
Performance of BBI in H1 2016



Source: BLOMINVEST Research Department

The first half (H1) of 2016 was marked by unstable geopolitical dynamics and a continuing political stalemate, with almost 26 months of political vacuum. In the beginning of 2016, GCC countries (Bahrain, Kuwait, Qatar, and Saudi Arabia) warned their citizens from travelling to Lebanon. This occurred after Saudi Arabia halted $4B in aid to the Lebanese Armed Forces in response to diplomatic differences with the Lebanese government, in January. Moreover, a bombing exploded next to BLOM Bank headquarters in June.

These events enervated the performance of the Lebanese Eurobonds Market, as reflected by the BLOM Bond Index (BBI) that reached its lowest level in more than 7 years at 102.31 points on the 29th of June 2016.

In fact, the BBI ended H1 2016 at 102.93 points, 3.93% lower than its value a year ago, and dropping by 1.14% since the beginning of the year. The weighted average yield of Lebanese Eurobonds, which is inversely related to the price, increased from 6.14% end of 2015 to 6.38% on the 30th of June 2016.

The decline in the BBI mostly came as a result of frail demand for medium- and long-term Lebanese Eurobonds. The yields on the 5Y and 10Y Lebanese Eurobonds increased from 6.10% and 6.67%, end of 2015, to 6.31% and 6.67% end of H1 2016, respectively.

Despite the market's feeble performance, the Lebanese government successfully completed a new Eurobonds issuance in April, for 2 tranches: 8Y (April 2024) and 15Y (April 2031). The size of the 8Y issue was $700M, while that of the 15Y issue was $300M. Both tranches were oversubscribed; hence the allocation for the 8Y was 80%, and that of the 15Y was 70%. The coupon rates for the 8Y and 15Y maturities stood at 6.65% and 7%, respectively, paid semi-annually. Foreign participation was around 7.5%. The lead managers of this issuance were BLOM Bank S.A.L, Byblos Bank S.A.L, and Deutsche Bank.

Details of April 2016 Lebanese Eurobonds Issuance

	8Y	15Y
Issuer	Lebanese Republic	Lebanese Republic
Type	Eurobond	Eurobond
Coupon	6.65%	7%
Maturity Date	April 2024	April 2031
Issue Size	$700M	$300M

Source: BLOMINVEST Bank Research Department

In the US, demand for treasuries increased as the US Treasuries Index, compiled by Bloomberg, grew 5.43% year-to-date (y-t-d) to 129.55 points. Global economic worries and negative yields in Europe and Japan helped drive demand for US Treasuries. Moreover, slow growth in China and other emerging countries disrupted markets and pushed investors towards low-risk investments.

Hence, the yield on US treasuries maturing in 5 years decreased from 1.8% end of 2015 to 1.01% end of June 2016. Similarly, the yield on US Treasuries maturing in 10 years declined from 2.31% to 1.49%, during the same period.

Due to the diverging trends followed by Lebanese Eurobonds and US treasuries, the spreads between the 5Y and 10Y yields on Lebanese Eurobonds and their US counterparts widened from 430 basis points (bps) and 436 bps, end of 2015, to 530 bps and 545 bps, respectively, end of H1 2016.

Similarly, the 5Y Credit Default Swaps quote, which reflect how the government's risk of default is perceived, broadened from 416-436 bps, with a mid-quote of 426 bps, end of 2015 to 457-467 bps with a mid-quote of 467 bps, end of June 2016.

As for bonds of the emerging markets, they saw a surge in their demand, reflecting a renewed appetite for risk among investors. The JP Morgan Emerging Bond Index hiked 10.90% y-t-d to 743.81 points in June 2016. This was bolstered by Brazil, after major economic reforms in Brazil pushed up demand for Brazilian Eurobonds.

Despite the renowned low risk of default of the Lebanese government and its high yielding debt, demand for Lebanese Eurobonds remained low. Any improvement experienced on the political or security front would allow Lebanon's Eurobonds market to regain investors' confidence.

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