Lending Activity in Lebanon : Q1 2018

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The economic slowdown of the Lebanese economy has persisted for several years with marginal growth in GDP levels, and the beginning of 2018 was no different. In fact, the private sector's business conditions kept on deteriorating as depicted by Lebanon's Purchasing Managers' Index (PMI) that averaged 46.9 points in the first quarters of 2018, compared to 47.4 during the same period in 2017, standing well below the 50-points mark, separating economic growth from contraction.

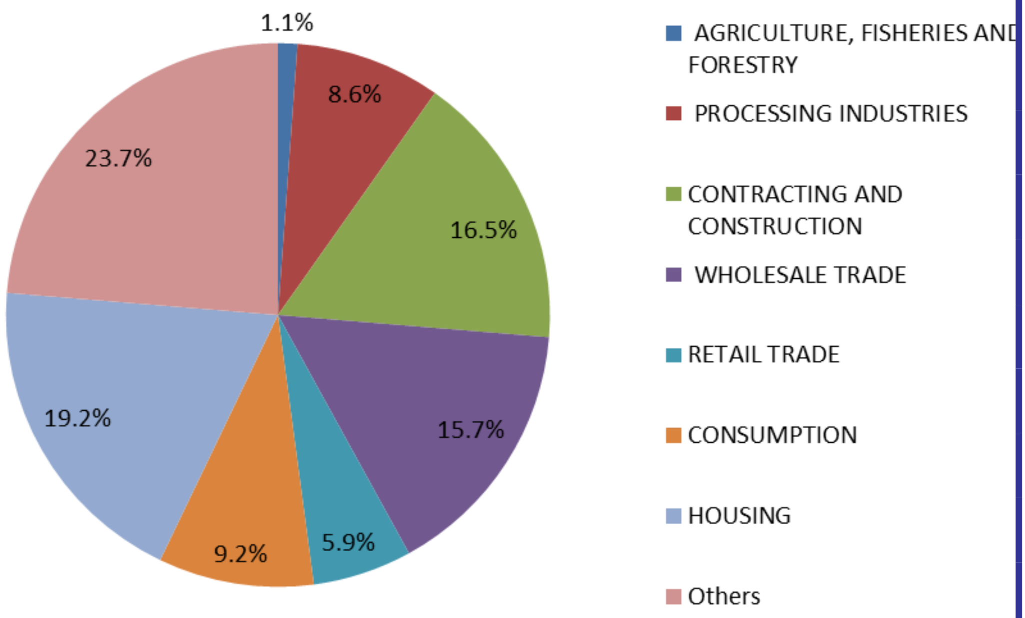
Despite severe economic conditions in the previous years, the Lebanese banking sector proved its robustness and resilience; however, escape was inevitable for this sector during the first quarter of the year. Loans granted by the Lebanese banks have witnessed a compounded annual growth rate (CAGR) of 8.9% during the past 5 years, yet recorded a marginal drop of 0.04% in Q1 2018. According to the Central Bank's latest data, the total value of credit provided by the Lebanese banks to the economic sectors excluding those to the financial intermediation reached $65.01B by March 2018 standing at 121% of 2018's IMF estimated Gross Domestic Product (GDP).

Moreover, to further depict the weakening of the economy, banks' gross nonperforming loans (NPL) have recorded a 3.51% uptick since year start. In details, NPLs of 2 major categories, contracting and construction and wholesale trade, constituted 25.62% and 19.73% of total NPLs.

Nonetheless, individuals and businesses still rely heavily on loans because it's an easy way access to money and is considered a safer strategy for firms. The composition of credit loans have been maintained for the past several years. Individual loans, which include housing, consumption and car loans, grasped the largest share of the total at

31.8% followed by contracting and construction loans (16.51% of the total) and wholesale trade loans and retail trade loans (15.69% and 5.89% of the total, respectively).

Composition of Total Loans Granted in Q1 2018



Source: BDL

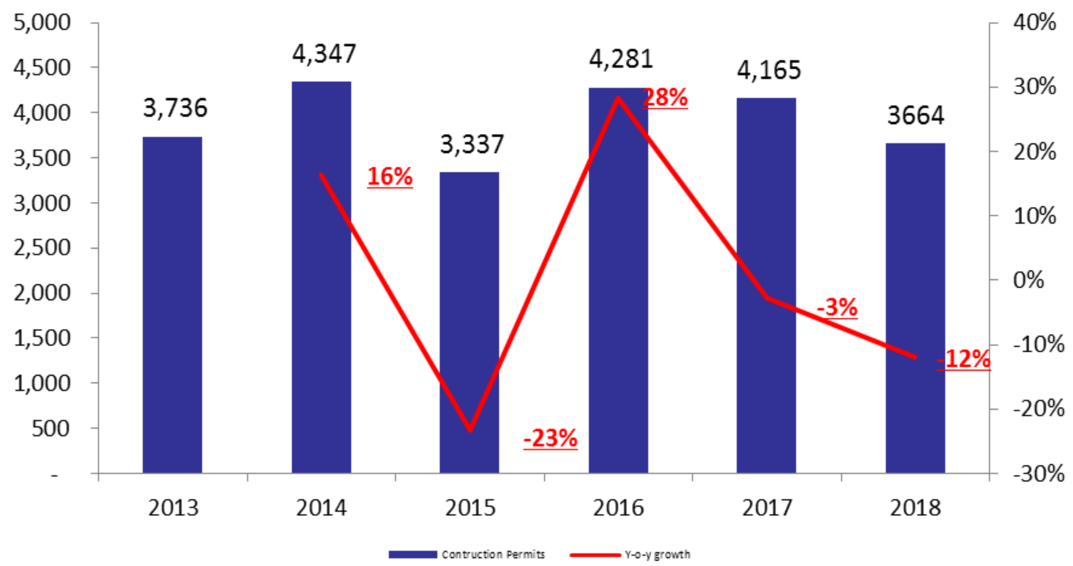
The value of individual loans is still the highest amongst loan categories, especially housing loans. Individual loans amounted to $21.57B, of which housing totaled $13.51B. Compared to the end of 2017, housing loans saw a 0.91% yearly growth however that growth is much slower than the 10.5% registered during 2017. The large increase in value during 2017 can be justified by the Banque du Liban's (BDL) Circular #473 that was released in October 2017 as well as the drop in interest rates on subsidized loans. Based on the circular, the ceiling on the amount of subsidized housing loans has been upped from a previous LBP 800 million (around $530,679) to LBP 1.2 billion ($796,020).

However, in the first quarter of 2018, the Central Bank issued a banking circular that entailed significant amendments to the government's subsidized loan program. Under the terms of the circular, the Housing Bank raised its interest rate from 3% by 75 bps to 3.75%, and decreased the amortization schedule from 30 years to 20 years, thus significantly tightening the terms of the loan. As such, these procedures have taken their toll on the banking sector, hence increasing housing NPLs by 16.23% y-t-d. In the upcoming period, markets are expected to adapt to this change to pre-2012 levels, hence resulting in lower real estate prices.

On a different note, car loans and credit cards witnessed deterioration in the first 3 months of the year. Given that the car market has been suffering for the past few years, car loans went down by 1.9% to $1.16B. Moreover, credit cards fell by 1.36% to $690.84 despite the fact that the number of outstanding credit cards grew by 3 % in 2017 to reach 571,366.

In terms of the real estate sector, the feeble demand resulted in a drop of construction loans, which fell by 1.17% to $11.32B, with 20% of these loans considered to be NPLs. Hence, banks are mostly taking precautions and decreasing the credit allocated to this sector. Moreover, as a further confirmation of the weakness of this sector by the first quarter of 2018, construction permits plunged by 12.03% y-o-y drop in total number of construction permits over the same period that confirm the lack of investment appetite, bearing in mind that permits are usually issued at least 6 months after applications are filed and the execution of a permit is valid up to five years from the date of issuance. Furthermore, according to the data from the General Directorate of Land Registry and Cadastre (LRC), the number of RE transactions which may include one or more realties, reached 14,181 transactions by March 2018, down from 17,081 in Q1 of 2017. In its turn, the value of total RE transactions stood at $2.01B, also contracting by 14.03% year-on-year (y-o-y).

Construction Permits in Q1



Source: Order of Engineers

According to the Central Bank, contracting and construction loans represented the second largest share of loans in total loans granted in the sector with a share of 16.51% up to March 2018. Loans for General and commercial contractors, with respective shares of 33.8% and 32% of total contracting and construction loans fell by 0.20% and 2.5% year-to-date to reach $3.83B and $3.62B up to March 2018.

Worth mentioning, loans for large projects have increased since the beginning of the year. In more details, loans for the construction of stadiums, sport centres and tourism complexes rose by 2.7% to $95M and loans for the construction of slaughterhouses, mills and plants went up by 19.8% y-t-d to $19M by March 2018. However, loans for the construction of factories and laboratories declined by 5.4% since year start to $53M Wholesale trade, the third largest category in loans granted, wasn't affected by the slowdown in the lending activity. In fact, loans grew at 3.72% y-t-d to reach $10.76B. In details, foodstuffs and beverages, one of the top exported products of Lebanon, constituted the largest share of this category and surged by 8.7% to $2.39B. In addition, given the 27% rise in oil prices, loans or oil and oil products witnessed a 10.5% increase to $1.41B.

The lending activity in Lebanon has slowed down during the first three months of the year, and this trend is expected to persist in the near future. However, more regulated capital markets; a rise in foreign investments, and new reforms to adapt to the new housing loans crisis could boost the Lebanese economy and hence release the pressure from the banking sector.

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