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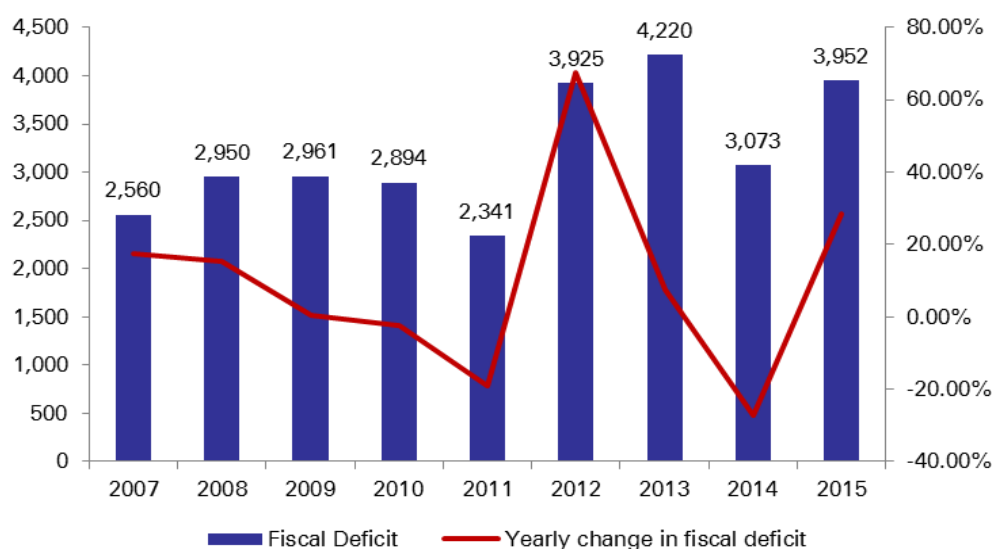
Contact Information

Research Assistant: Lana Saadeh
lana.saadeh@blominvestbank.com

Head of Research: Marwan Mikhael
marwan.mikhael@blominvestbank.com

Research Department
Tel: +961 1 991 784

Yearly Fiscal Deficit (in \$M) and Percentage Change



Source: Ministry of Finance

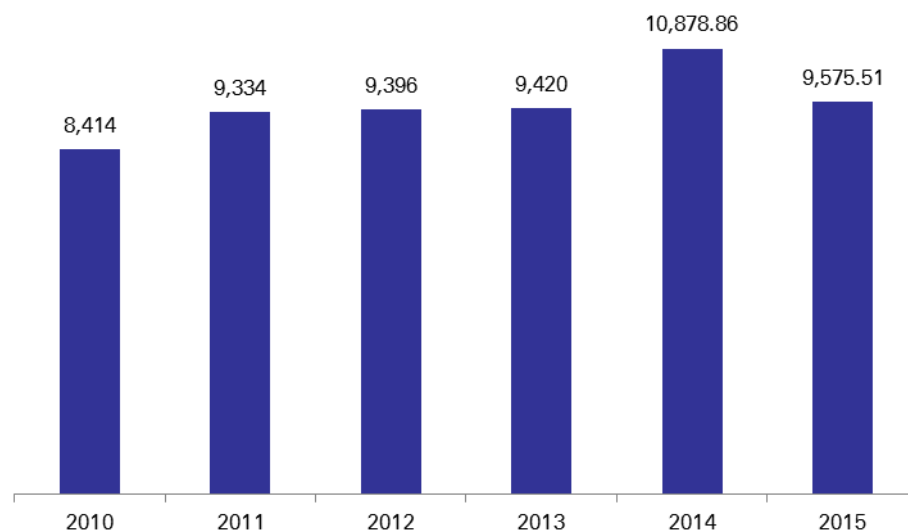
Lebanon has been recording a fiscal deficit for more than 9 years, reaching a maximum of \$4.22B in 2013. The deficit narrowed by 27.18% in 2014, then deteriorated again in 2015.

The slowdown in economic growth, as shown by real Gross Domestic Product (GDP) growth that declined from 1.8% in 2014 to 0.5% in 2015, and the political uncertainties contributed to the 28.62% year-on-year (y-o-y) widening in fiscal deficit to \$3.95B in 2015. In fact, total revenues declined by 11.98% to \$9.58B, despite the 3.04% drop in total expenditures to \$13.53B. Therefore, the fiscal deficit-to-GDP ratio reached 7.80% in 2015, compared to a lower ratio of 6.31% in 2014.

The primary balance, representing fiscal balance excluding debt service, posted a surplus of \$724.40M compared to a higher surplus of \$1.31B in 2014. Hence, the primary balance grasped a 1.43% share of GDP in 2015, compared to a higher share of 2.68% in 2014.

The Contracting Lebanese Economy Took its Toll on Government Revenues

Yearly Government Revenues



Source: Ministry of Finance

Government revenues failed to maintain its uptrend, dropping from \$10.88B in 2014 to \$9.58B in 2015. This was mainly due to lower revenues from Value-added Taxes (VAT), taxes on property, and telecoms.

The depreciating Euro against the dollar-pegged Lebanese pound caused total tax revenues to decrease slightly by 0.56% yearly to stand at \$6.85B. The Euro depreciated by 10.22% during 2015 making Europeans imports relatively cheaper. Hence, taxes on domestic goods and services, representing the highest share of 35.98% of tax revenues, dropped 2.48% y-o-y to \$2.47B in 2015. VAT revenues (84.99% of taxes on goods and services) lost 4.34% to \$2.10B, due to the 49.71% yearly plunge in the price of Brent Crude oil in 2015, exceeding the 5.71% y-o-y increase in volume of mineral products to 5.99M tons in 2015.

Income tax, constituting a 27.95% share of tax revenues, was mainly pulled up by the resilience of the Lebanese banking system. Total income tax added 3.29% annually, to stand at \$1.92B in 2015. The 5% interest income tax on banks increased by 7.90% to \$508.65M, as loans to the private sector inched up 6.53% to \$54.22B. Similarly, taxes on wages and salaries and capital transfer taxes grew 3.81% and 8.23% to \$442.61M and \$187.67M, respectively. Meanwhile, taxes on profits dropped 1.46% to \$731.37M, due to the contracting economy as reflected by the Purchasing Managers' Index (PMI) that remained below the 50 mark, separating contraction and expansion, at an average of 48.4 points in 2015.

Although liberalized trade agreement between Lebanon and the EU was fully implemented in the second half of 2014, and should have pushed down custom duties, these revenues revealed a slight increase in 2015. Custom duties (19.98% of tax revenues) added 1.07% to \$1.37B, in 2015. This might be due to the volume of imports to Lebanon which increased by 1.60% to 15.70M tons.

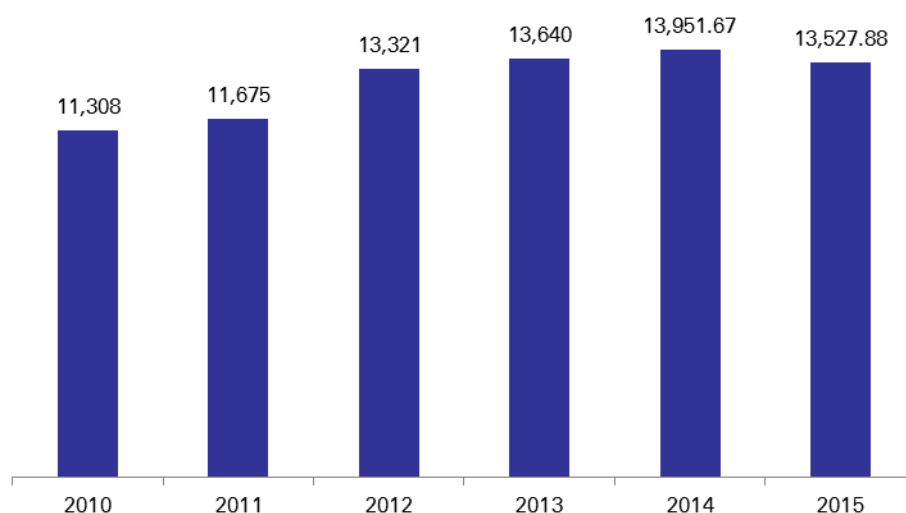
Taxes on property (11.42%) lost 5.26% to 782.25M, due to the lackluster performance of the real estate sector. The geo-political developments and the local political stalemate kept on hindering activity on the realty market. As a result, the contracting number of real estate transactions pushed down taxes collected on property. In fact, total real estate transactions, recorded a 5.40% yearly decline to 82,790, leading to a 10.72% slump in real estate registration fees to \$513.07M, in 2015.

Excise taxes added 5.81% to \$899.09M in 2015. Excise taxes on fuel grew 22.80% to \$417.26M, as a decline in price caused an increase in consumption of fuel. Excise on cars increased 12.60% to \$316.24M, as the number of newly registered commercial and passenger cars in 2015 increased by 3.78% to 41,654 cars. The improvement experienced in the car market is the result of price reductions, aggressive promotional campaigns and after-sale services carried out by importers. The progress was also the result of depreciations in the euro, the yen and the decline in oil prices. In contrast, excise on tobacco lost 28.14% to \$158.34M. The volume and value of tobacco decreased 21.20% and 21.42% to 13,891 tons with a value of \$176.88M, in 2015.

Similarly, non-tax revenues dropped 24.09% compared to 2014 to stand at \$2.19B in 2015. Telecommunication Service Revenues declined 38.67% to \$1.13B. This resulted from the Ministry of Telecoms' decision, which was implemented in June 2014, to reduce internet and mobile tariffs. Revenues from the Casino and the National lottery decreased 6.03% and 10.06% to \$72.87M and \$39.44M, respectively. Meanwhile, Revenues from Beirut International Airport and Port of Beirut grew 55.52% and 42.15% to \$63.28M and \$77.42M, respectively. Administrative Fees and Charges added 17.51% \$525.89M.

Government Expenditures Decreased for the First Time in More than 4 Years

Government Yearly Expenditures



Source: Ministry of Finance

Although the slump in oil prices caused EdL transfers to decline, the upturns in interest payments and public sector wages led public expenditures to registering a slight downturn from \$13.95B in 2014 to \$13.53B by the end of 2015.

Expenditures are mainly disbursed for interest payments that constitute 32.96% of total government expenditures. Interest payments grew by an annual 6.45% to \$4.46B in 2015. This was mainly due to the 9.98% increase in interest payments on domestic debt to \$2.87B and the smaller 0.62% uptick in that on foreign debt to \$1.59B. The value of debt in domestic currency registered a 5.58% yearly increase to \$43.25B by December 2015. As for debt in foreign currency, it increased by 5.72% on a y-o-y basis to reach \$27.06B in December 2015.

Interest payments on both domestic and foreign debt increased, as the Ministry of Finance is trying to lengthen the maturities of government bonds. Longer debt maturities are serving the debt management strategy of the government that wants to lock interest rates for longer maturities before the Federal Reserve's interest rates hike that occurred in December 2015. The average maturity of Lebanon's Treasury-bills' portfolio was extended from 1,193 days end of 2014 to 1,222 days by December 2015.

The international slump in oil prices was manifested in lower transfers to EDL. Transfers to EDL, which constituted 8.39% of government expenditures in 2015, plunged 45.81% to \$1.13B.

Public sector wages grew 8% by August 2015. The Ministry of Finance states that this consistent upward trend in public salaries is the result of the increased hiring of military personnel and of lower base in current primary expenditures which fell by 14% from 2013 to 2015.

Public Debt Stood at \$70.3B in 2015

The fiscal deficit led gross public debt to grow by 5.63% to \$70.3B or 138.71% of GDP in 2015. Net public debt, which excludes public sector deposits at commercial banks and at the Central Bank, increased by 7.39% y-o-y to 61.54B by December 2015.

Lebanese commercial banks remained the top holders of Lebanon's public debt denominated in local currency with a share of 45.8%, followed by a stake of 37.3% for the Central Bank of Lebanon and a 16.9% share for the non-banking sector.

Worth noting, Lebanon successfully sold \$2.2B of Sovereign Eurobonds in February 2015. The debt issuance enclosed 2 new categories: \$800M of 10Y Eurobonds maturing in 2025 and yielding 6.20%, and \$1.4B of 15Y Eurobonds yielding at 6.65%. The settlement date of the issuance was set on February 26, 2015 with lead managers being: BLOM Bank, Citi, and Société Générale des Banques au Liban (SGBL). Besides the strong demand from Lebanon's local banks, Banque du Liban (BdL) also took a share of the new issuance. Finally, international orders were promising as they hovered around 15% which could be partly due to the overflowing cash in the global financial markets following the decreasing oil prices.

For your Queries:

BLOMINVEST BANK s.a.l.

Research Department
Bab Idriss, Weygand Str.
POBOX 11-1540 Riad El Soloh
Beirut 1107 2080 Lebanon

Lana Saadeh, Research Assistant
Tel: +961 1 991 784
lane.saadeh@blominvestbank.com

Marwan Mikhael, Head of Research
marwan.mikhael@blominvestbank.com
+961 1 991 782

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