

Lebanon: beyond tomorrow

With falling domestic consumption and foreign direct investment offering limited demand at home and the Syrian war disrupting regional export routes, Lebanon's cement producers are cutting costs and reducing output. However, the long-term scenario offers improved opportunities both within and beyond the country's borders.

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As local demand weakens and foreign direct investment falls, Lebanon's cement producers look to the medium- to long term for a pick-up in domestic cement consumption



Since 2011 the Lebanese economy has been burdened by regional and local instabilities. The Syrian crisis and an extended political deadlock that has left a vacant presidential seat for over two years have had a significant impact on the country.

Lebanon's real GDP growth took a sharp turn away from the high 8-10 per cent seen between 2007-10 to a meagre range of 0.9-2.8 per cent between 2011-14 (see Figure 1). The activity of vital economic sectors such as construction and real estate receded as foreign investments shrank

and local demand weakened. The tourism sector no longer thrives on heavy spending by tourists from Gulf Cooperation Council (GCC) countries as several and repeated travel bans issued by GCC governments prevented their nationals from visiting Lebanon.

This extended period of distress leaves growth expectations very low with real GDP estimates of one per cent for 2015-16 and two per cent for 2017.

Lebanon is not only affected by the decrease in the number of tourists but also by the drop in foreign direct

investment (FDI) and remittances from GCC countries. Low oil prices have squeezed the budgets of oil-exporting countries, compelling them to lower spending and cut investments abroad. The drop in FDI from oil-exporting countries into Lebanon is expected to translate into a loss for the real estate sector as this sector absorbs more than half of the inflows. Furthermore, the fall in oil prices is predicted to lead to a decline in remittances in the case of Lebanon. Oil exporters have postponed or cancelled large government projects forcing companies to cut costs and lay off employees, many of which are Lebanese expatriates.

Recent times have seen few building permits issued as real estate stagnates



Lebanese cement companies have focussed on reducing production costs



Holcim Liban has worked on the installation of a hot gas system this year



Construction challenges

Real estate/housing construction

The construction and real estate sectors have seen demand drop with few building permits issued (see Figures 2 and 3) in the past six years. The real estate sector remains stagnant with developers having a hard time selling their large stock of real estate units. These stockpiled after 2012 when demand for large, expensive real estate from wealthy Gulf investors, Lebanese expatriates and resident Lebanese eroded. Even the big real estate developers, who were the only ones to sustain the sour turn of conditions on the market, are now compelled to offer 10-20 per cent discounts on their listed prices.

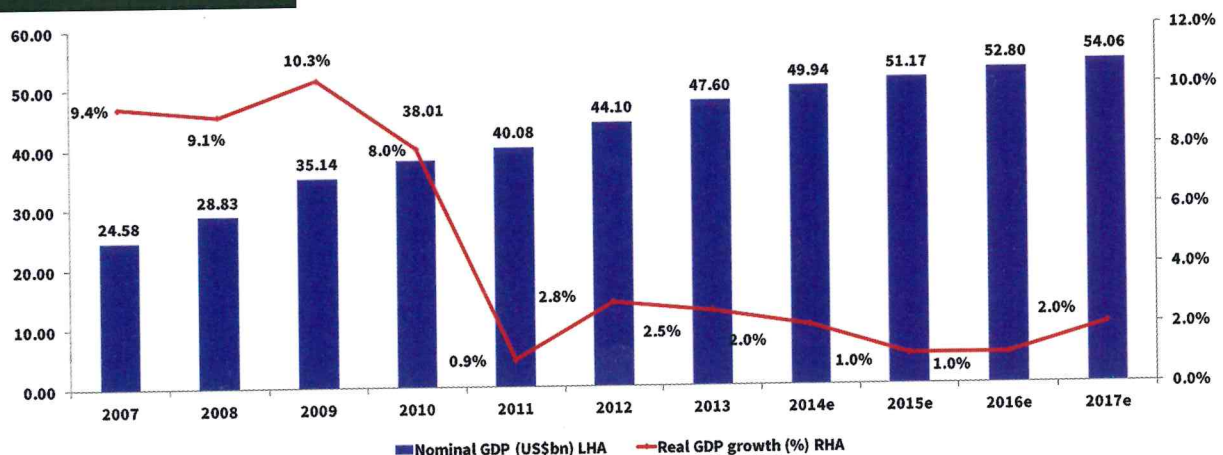
In the residential market, the few new projects consist only of small-sized apartments of around 140m², since that is where the new demand lies. The average construction area authorised per permit fell from 995.38m² in 2010 to 754.78m² in June 2016.

Infrastructure

Policy inertia and the lack of financial resources are preventing much-needed infrastructure investment in Lebanon. Without a budget for more than a decade, the absence of fiscal policy left the country with a deficit of US\$3.95bn at the end of 2015. The fiscal mismanagement also resulted in the concentration of government spending at more than 90 per cent on current expenditure such as personnel costs, transfers to the state-owned electricity company EDL and debt servicing, while capital expenditure that is needed for infrastructure development is left behind (see Table 1).

However, the influx of refugees has increased the urgency of tending to Lebanon's infrastructure requirements.

Figure 1: Lebanon GDP, 2007A-17E



Source: IMF

Lebanon is now hosting over 1.5m Syrian refugees, an influx that is weakening an already decaying infrastructure. According to the World Bank, an estimated US\$246-

\$525m was needed over the 2013-14 period for additional road maintenance and expansion of the public transportation systems. Therefore, the majority of current

cement demand stems from the private sector (malls, complexes, residential buildings).

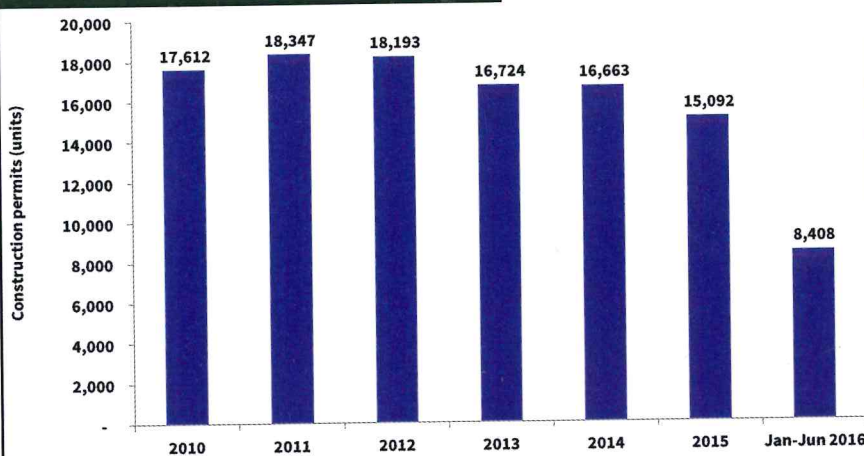
Shifting rather than growing cement demand

Domestic cement deliveries fell from 5.5Mt in 2014 to 5Mt in 2015. In 1H16 they recorded double-digit YoY growth of 10 per cent to reach 2.5Mt, according to the Central Bank of Lebanon.

However, this increase is the result of a set of exceptional factors, says Adib Hachem, marketing and sales director at Cimenterie Nationale and chairman/general manager of Sabeh Beton: "Candidates running for the municipality elections engaged in public projects ahead of the election that took place in May. In addition, Lebanon saw fewer rainy and snowy days in 1H16 and that helped shift demand that would have normally taken place in the second half of the year to the first half of the year. Moreover, an anticipated surge in steel prices, which later failed to materialise, encouraged builders to speed up their construction works. The procedures to obtain construction permits for areas smaller than 150m² were eased."

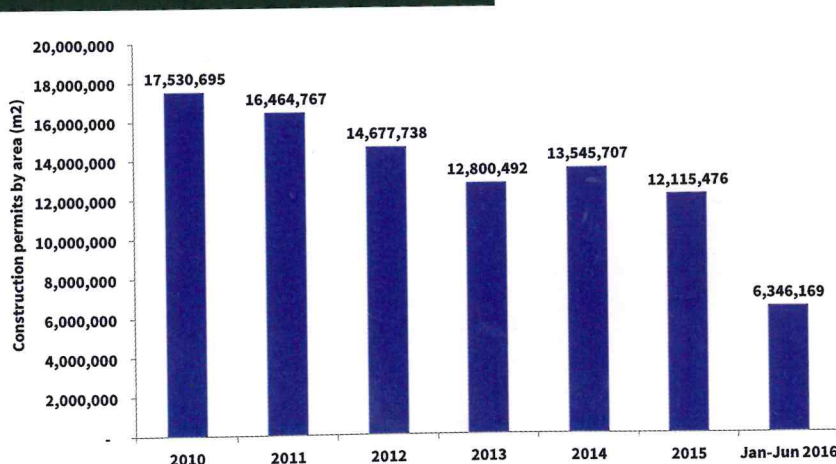
"In the 1H16 domestic cement deliveries recorded a double-digit YoY growth due to exceptional factors rather than consumption growth."

Figure 2: number of construction permits, 2010-2016



Source: Order of Engineers and Architects in Beirut and Tripoli

Figure 3: construction permits by area, 2010-2016



Source: Order of Engineers and Architects in Beirut and Tripoli

Table 1: current vs capital expenditure in Lebanon, 2008-14

Expenditure type	2008	2009	2010	2011	2012	2013	2014
Current expenditure (US\$bn)	7.09	8.37	8.58	10.52	11.78	11.92	12.29
Capital expenditure (US\$bn)	341	364.553	458.183	448.142	504.133	654.780	585.995

Source: Lebanon Ministry of Finance

Table 2: total installed capacity of Lebanese cement producers

Company	Clinker production capacity (Mta)	Cement production capacity (Mta)
Cimenterie Nationale	2.5	3.0
Holcim Liban	1.8	2.2
Ciment de Sibline	1.1	1.3
Total	5.4	6.5

Source: Cimenterie Nationale

Developments in the market have also impacted on domestic cement prices. The price of grey cement in bags and delivered to construction sites, including VAT, reached US\$105/t in 1H16, unchanged from 2015 but around US\$8 down from 2014. The factory price (excluding VAT) stood at US\$85 in 1H16. The evolution in the price of white cement is generally parallel to that of grey cement.

Access to export markets cut

In addition to domestic consumption lagging behind, access to profitable export markets has been completely cut off for grey cement producers and significantly reduced for white cement producers.

Syria and Iraq were the most lucrative markets for exports of Lebanese cement since their proximity allowed Lebanese manufacturers to reap the benefits of the cost-effective land transport. However, the Syrian war has disrupted land trade routes and shipments by sea are too costly. Therefore, exports of grey cement to Syria, Iraq, and even Egypt and Libya are currently halted.

In addition, war-ridden Syria has issued three consecutive bans on imports of Lebanese grey cement since 2013, making access to Syria impossible. In 1H16 US\$1.609m or 14,700t of Lebanese white cement were exported to Syria.

This situation is further exacerbated by Lebanon's location next to two of the largest cement-producing and exporting countries in the world: Iran and Turkey. The combination of significantly more competitive prices and excess supply in these two nearby countries represent

solid barriers to entry for Lebanese cement producers. In addition, Egypt is a large market with plenty of potential opportunities, but it is also a country mired in political instability where interest rates are exorbitantly high to reflect the country's risk and where the Egyptian pound has suffered a severe devaluation.

Cement production

Lebanon's total installed cement capacity is 6.5Mta while its total clinker capacity reaches 5.4Mta.

The country is home to three cement producers – Cimenterie Nationale, Ciment de Sibline and LafargeHolcim Group-owned Holcim Liban. All three manufacturers produce grey cement, but Holcim Liban also produces white cement through its subsidiary Société Libanaise des Ciments Blancs SAL (SLCB). However,

white cement volumes on the Lebanese market represent less than one per cent of grey cement volumes.

Cimenterie Nationale is the biggest player with a market share of 43 per cent in July 2016 while Holcim and Ciment de Sibline account for 38 and 19 per cent, respectively.

With both the domestic and export markets presenting challenges to Lebanon's cement producers, the operating environment has been detrimental to business success since 2011, and proved exceptionally difficult in 2015 and the opening months of 2016. With limited sales options both in Lebanon and beyond, Lebanese cement companies can only resort to cost-cutting and reducing production.

Cimenterie Nationale reported that it is operating at only 60 per cent of its

Table 3: Lebanese cement and clinker exports to selected destinations, 2012-1H16

Country	Exports (US\$'000)				
	2012	2013	2014	2015	1H16
Syria	31,892	4753	1952	2484	1609
Egypt	-	1759	4895	1101	-
Cyprus	3267	3573	-	450	663
Congo	-	24	-	-	-
Greece	249	-	-	-	-
Spain	858	853	-	-	-
Italy	1094	-	-	-	-
Libya	-	4099	-	-	-
Jordan	-	904	896	64	-
Total	37,378	17,439	7817	4147	2275

Source: Lebanon Customs

New hot gas system for Chekka coal mill



Integrated hot gas duct

In December 2015 LafargeHolcim awarded Intercem the contract for the turnkey supply of a hot gas system for its coal mill in Chekka, Lebanon. The project will help the cement plant reduce energy costs and optimise specific labour.

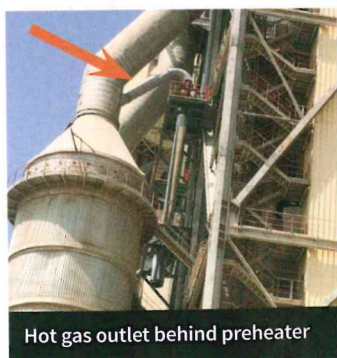
The new hot gas system connects the preheater with the coal mill and comprises a $\phi 900\text{mm} \times 360\text{m}$ hot gas duct. The process data of the hot gas outlet of the heat exchanger are of $18,500\text{Nm}^3/\text{h}$ at 400°C .

Besides diverse ducts, a cyclone, process fan and several control dampers, compensators, complete instrumentation and automation as well as a new recirculation duct with two control dampers at the existing vertical coal mill were supplied.

The turnkey scope of supply and services includes:

- project management
- as-built-survey of the existing plant using 3D-Laser scanning
- review of the statics of the existing steel structure and concrete construction
- process- and detail engineering
- supply of the mechanical equipment, including steel structure
- coordination of the locally-produced components
- supply of the electrical equipment, including clarification of connections and integration into the existing control systems
- execution of the complete foundation works
- transport management
- electrical and mechanical assembly of the plant
- commissioning of the hot gas system
- training of the operating team.

The project is expected to be commissioned in 4Q16.



Hot gas outlet behind preheater



Connection of hot gas ducts

capacity, with two out of three kilns being stopped several months a year. The company also noted that the collection of receivables has lengthened by 20 days every six months for the past year and a half.

Meanwhile, Holcim says in its 2015 annual report: "The slowdown in the real estate market has impacted the liquidity flow negatively. Efforts to collect cash and limit the credit risk have been a priority for the company."

Holcim Liban saw sales of white and grey cement decrease by 11.6 per cent and 10 per cent to 59,400t and 1.864Mt, respectively, in 2015.

Furthermore, as cement manufacturing is an energy-intensive industry, low oil prices would appear beneficial for cement producers. However, Holcim Liban reports that "the low oil prices have a positive effect on energy costs – but the main type of fuel used in cement production is petcoke and there is no perfect correlation between petcoke prices and oil prices. In fact it has substantially increased again in the second half of 2016."

Outlook

Looking ahead, cement market prospects are tightly linked to positive political shocks in Lebanon and Syria. Cement deliveries are expected to remain around 5.2Mt in 2016, according to Cimenterie Nationale.

In Lebanon the current waste crisis and the ensuing need for the construction of garbage disposal and sorting facilities will generate demand for cement as will several public projects such as dams in the regions of Beqaata, Balaa, Msaylha, Kaysamany and Besri and a large tunnel between the regions of Wardaniyeh and Khaldeh. These projects will require around 600,000t of cement over a period of 4-5 years, with a peak expected in 2018.

As for long-term opportunities abroad, Syria remains the most attractive export market due its geographic proximity with Lebanon and its potential reconstruction needs.

Future cement demand in Syria is estimated to vary between 15-20Mt, about 3-4 times Lebanon's current cement deliveries. Even with all plants in Syria operating at normal production levels, the country would still need to import around 12Mta of cement over five years with deliveries expected mainly from neighbouring Lebanon, Jordan and Turkey. ■