LEBANON REAL ESTATE SECTOR

A WEAKENING DEMAND IN A BUYER'S MARKET

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- **Residents almost exclusively driving a slower market**

The Lebanese real estate sector has lately been witnessing an accentuated slowdown in activity against the backdrop of heightened political bickering and still elevated realty prices on the internal front, and the repercussions of the ongoing war in Syria on investor and buyer confidence on the external front. Lebanese resident buyers are keeping the market afloat, with the more limited financial means they have compared to Gulf nationals or even Lebanese expatriates meaning less space is being bought. Property sales value trends perfectly reflect a lower number of sales transactions, with the latter diving by 13.4% in the first seven months of 2015.

- **Developers adapting to new trends by offering smaller units**

Quite a few developers have had to adapt to this new reality, and have started to construct smaller properties in the hope of capturing new demand. Construction permits edged 18.5% lower in the first seven months of 2015. Forthcoming projects will be fewer in Beirut than they used to be a few years ago to the advantage of Mount Lebanon and the South. The share of Beirut out of total permits moved down to just 8% in 2014. A slowing property market yet does not mean activity is non-existent. It just obeys to the overall politico-security mood and buyer sentiment. And since locals are the ones driving the market nowadays, sales in the small to mid-size property market are the ones shaping supply trends.

- **BDL stimulus package a breath of fresh air to the market**

With prices still high in practically all residential areas, a persistent gap between property prices and the income per capita of Lebanese residents has been more or less plaguing sales, regardless of the overall buyer mood. This is where BDL has been injecting a breath of fresh air into the market, launching a welcome initiative by all stakeholders concerned a couple of years ago, consisting of an economic stimulus package of which a non-negligible chunk allocated to housing and aiming to boost economic growth amidst currently prevailing difficult conditions. BDL recently announced yet another round of stimulus measures for 2016 amounting to a record high US$ 1.5 billion (of which a significant portion of housing loans), which is expected to extend the win-win situation for all parties involved in the realty market.

- **Commercial realty similarly impacted by economic slowdown and political uncertainties**

The retail market remains influenced by the accentuated economic slowdown and volatility of politico-security conditions, with consumption spending slowing down and reflecting on buyers' appetite across retail stores. Supply of retail space exceeded demand thus leading to downward price pressures across retail areas. In parallel, the office market performance remained sluggish for the same reasons. Office rents in Lebanon witnessed declines on the overall in the past year as local businesses are postponing new investment plans until there is more stability in the country. The office market has been mostly stagnant and the stock of new supply has pushed the overall market supply to exceed demand.

- **A buyer's market eagerly awaiting sustainably positive domestic and regional signals**

The local realty market outlook is strongly tied to the evolution of domestic and regional conditions. If the situation stays the same or somehow worsens, buyer mood will remain quite sluggish, perhaps even more so. But the price side of the equation would not be very much affected due to the end-user nature of demand, low developer leverage and limited available-for-sale land plots, and the sales and transactions side is likely to take the bigger hit. Should there be sustainably positive signals, higher sales activity would gradually erode the excess market supply, though this could take some time given the accumulated large stock of unsold properties. At a later stage, mainly in a regional settlement scenario, upward price pressures could start making a comeback. Today, the Lebanese real estate market is more than ever a buyer's market. Buyers well acquainted with local pricing dynamics and seeking a residence have all the bargaining power they need, and choice of residences they can think of not to mention financing options available, to make a good buy today, awaiting to reap the benefits sometime in the future.

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RESIDENTIAL MARKET TRENDS

Resident demand keeping the market afloat …

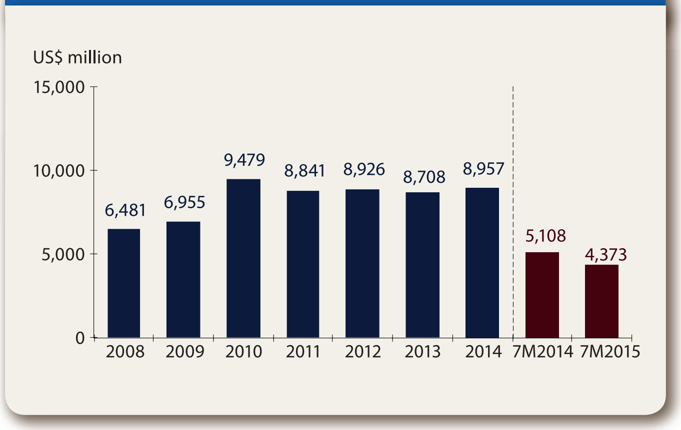
The Lebanese real estate sector has lately been witnessing an accentuated slowdown in activity against the backdrop of heightened political bickering and still elevated realty prices on the internal front, and the repercussions of the ongoing war in Syria on investor and buyer confidence on the external front. There is a quasi-paralysis of the State's institutions, from the vacant Presidency to the stagnant Parliament and to the frozen Council of Ministers. At the same time, the civil war in Syria and regional tensions have pushed foreign investors unto the backseat, as these now await to have a clearer idea of how the regional/domestic situation is going to evolve and how events will unfold, before possibly making a forceful comeback to the domestic realty scene. Recent mass demonstrations across Lebanon on the back of a trash crisis have exacerbated further the prevailing gloominess and added to the cautiousness of the investment mood.

It is within this delicate context that the domestic real estate sector entered into a fifth year of slowdown, an era that started with the popular uprisings in neighboring Arab States that took their toll on investor confidence and discouraged wealthy Gulf nationals, who once were active realty investors in Lebanon, to park their funds elsewhere and focus on other areas of investment. Non-Lebanese foreign investors are practically out of the local realty market, as only a very limited number of them are still active in Lebanon, and probably will not be coming back unless they see solid signs of amelioration in the regional situation.

Lebanese expatriates might be enquiring, and few pursuing a transaction to its end, especially the ones who have their direct family here and work abroad, but some are refraining from making a buy as long as they do not have to. Some of them already have acquired a foothold in the country in the so-called boom years of 2007-2010, and some are just not willing to invest in a country they do not live in given the prevailing conditions and the uncertain investment climate. It is Lebanese resident buyers who are keeping the market afloat, with the more limited financial means they have compared to Gulf nationals or even Lebanese expatriates.

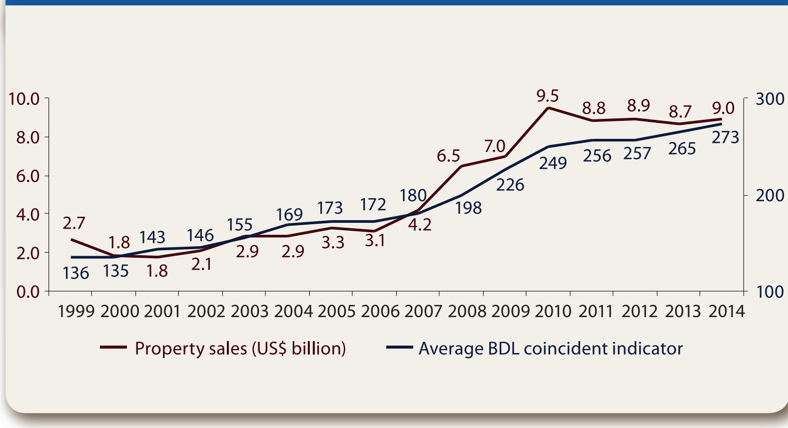
The residential market, traditionally accounting for the wide majority of real estate activity in the country, reflects this slowdown phase the most. Official market-wide statistics reveal that the total value of real estate sales in the country plunged anew over the first seven months of this year (-14.4%), reflecting a mismatch between demand and supply in some areas according to Plus Properties. One must not forget that the total value of transactions remains one of the most adequate gauges of market activity on the demand side given its very high correlation with the BDL's average coincident indicator, a synthetic index mirroring economic activity in the country. Our regression analysis linking the latter to the transactions value over the past decade and a half, shows a very high correlation of about 96% between the two variables.

PROPERTY SALES TRANSACTIONS VALUE



Sources: Real Estate Registry, Bank Audi's Group Research Department

PROPERTY SALES V/S AVERAGE BDL COINCIDENT INDICATOR



Sources: Real Estate Registry, BDL, Bank Audi's Group Research Department

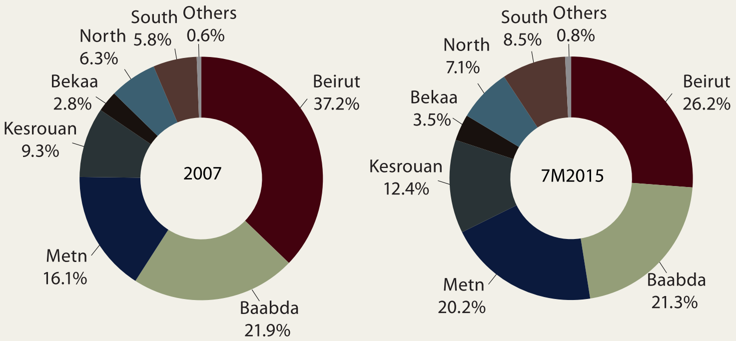
Property sales value trends perfectly reflect a lower number of sales transactions in the market, the latter diving again this year (-13.4% in the first seven months). The similar evolution of total market sales figures gives an idea about how stable prices have been in recent times in the property market. It is yet worth noting that the number of sales to foreigners, after four consecutive years of decline, has increased by 36.6% so far this year. But this does not lead us to believe that foreigners are back on the market as they were prior to the Arab Spring, rather this is likely to reflect recent demand on behalf of some Syrians and Iraqis fleeing their country. We believe this is a slight increase from a historically low base attained so far this decade. As a matter of fact, year-to-date sales to foreigners remain 26% lower than they were in the first seven months of 2010, i.e. prior to the regional turmoil.

… and going for more affordable smaller properties

Obviously, a slower realty market activity almost exclusively driven by locals means less space is being bought, with Lebanese residents increasingly going for smaller sized flats or residences. This is because prices are hovering near highs attained in 2010, thus rendering the purchase of an apartment quite expensive. As a result, large sized flats are much less demanded nowadays, and sales in the higher end segment of the market are more or less frozen, a few exceptions aside. This does not mean that the smaller sized flats are selling like hotcakes. These are actually also feeling the pinch of the local market slowdown, with buyers less in a hurry to close a sales deal and developers suffering quite a bit to sell their growing stock of apartments. But at least smaller sizes are more appealing and more likely to be sold than others. Those are the apartments that are demanded and sought after, as they are simply more affordable.

The still elevated prices are pushing some young newlyweds to move to a smaller, less expensive flat that they can at least afford, albeit for a few years only until their income generation power increases. Some others prefer to directly opt for three-bedroom units and settle in from the start, but the fact remains that even these are now aware that the less than 250 sqm apartments are probably going to be the ones that they can afford, be it in the capital city or in the immediate and less immediate trendy residential suburbs. Long gone are the days where the large sized flats were synonym of good or frequent buys, and small sized flats are the segment that is being the most resilient to the slowdown the market has been forced into a few years ago.

PROPERTY SALES TRANSACTIONS VALUE BY REGION



Sources: Real Estate Registry, Bank Audi's Group Research Department

SEASONALITY ANALYSIS: PROPERTY SALES BY QUARTER

	Q1	Q2	Q3	Q4	Total
2008	16.3%	23.7%	29.4%	30.6%	100%
2009	14.5%	20.4%	26.5%	38.6%	100%
2010	22.3%	27.4%	23.7%	26.6%	100%
2011	20.5%	23.1%	24.7%	31.8%	100%
2012	21.9%	24.6%	24.3%	29.2%	100%
2013	17.4%	26.4%	25.6%	30.7%	100%
2014	22.9%	27.1%	24.4%	25.5%	100%
Total	**19.7%**	**24.9%**	**25.3%**	**30.1%**	**100%**

Sources: Real Estate Registry, Bank Audi's Group Research Department

Developers adapting and responding by building smaller units

Quite a few developers have had to adapt to this new reality, and have started to construct smaller properties in the hope of capturing new demand. This has been the most frequent case in the capital city where prices are the highest anyways, with some areas already boasting new projects offering residences with size of less than 200 sqm and even less than 100 sqm, be they studios or small flats. It seems Beirut will more and more catch up with modern European capital cities boasting small flats to cater to new social dynamics and capture as much demand as feasible given sticky-on-the-downside prices.

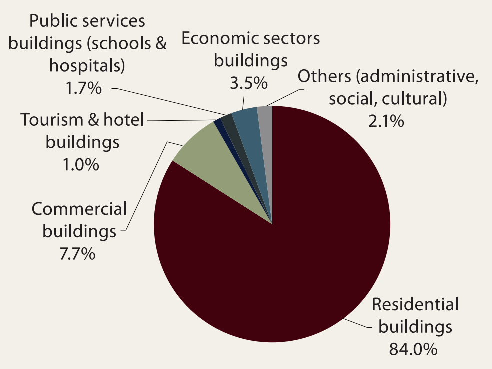
Outside Beirut, developers are only starting to launch smaller projects as buyers who can not afford a Beirut flat anymore generally opt for peripheral or suburban areas that are less expensive but where they could at least afford the buy. Usually, these come in sizes of less than 250 sqm as opposed to 250 sqm-350 sqm before the Arab Spring. Some projects propose flats of less than 200 sqm as those areas have become trendy and prices were also riding the same rising price wave Beirut properties were prior to the Arab Spring. With Beirut becoming more or less saturated in terms of available land plots, suburbs such as Hazmieh, Horch Tabet, Mar Takla (and lately New Mar Takla given the progressive saturation in the former area), Baabda, Yarze, Jamhour, Fanar, Mansourieh, Bchamoun, Naame, Naccache, Rabieh, and Bayada to name only a few started bustling with projects in the past decade. These are now much more densely populated than before, with prices closer than any time before to those of the capital city.

The breakdown of property sales value by area mirrors new demand patterns. Beirut's share out of the total decreased from 37.2% in 2007 (just before prices in the capital city started becoming quite high for new buyers not to actively consider suburban areas) to 26.2% in the first seven months of 2015. Practically all other regions saw their share increase, with Metn (now accounting for 20.2% of the total) and Kesrouan leading the pack (now accounting for 12.4% of the total).

Supply-side figures reflect not only the slowdown but also the smaller size-oriented activity in the market. Official figures show that construction permits, mostly an indicator of forthcoming activity (as they can be secured today for projects in the future), followed demand trends quite closely. They edged 18.5% lower in the first seven months of this year.

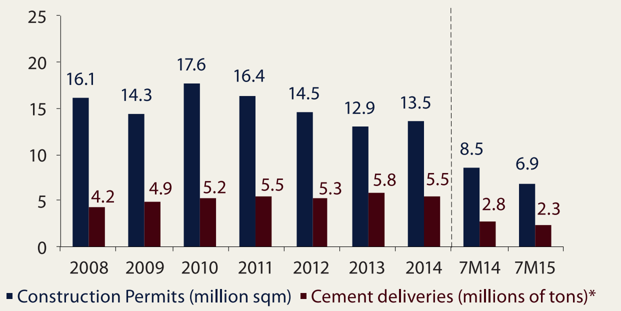
The breakdown of construction permits by area shows that forthcoming projects will be fewer in Beirut than they used to be in 2007 (just at the start of the boom era) to the advantage of Mount Lebanon and the South. The share of Beirut out of total construction permits moved from 20.3% in 2007 to 8.4% in 2014, while that of the broad Mount Lebanon slightly inched up to reach 56.0%, and that of the South including

CONSTRUCTION PERMITS (AREA) BY USAGE PURPOSE (2014)



Sources: Order of Engineers of Beirut, Bank Audi's Group Research Department

CONSTRUCTION PERMITS & CEMENT DELIVERIES



* Cement deliveries data cover the first six months of the years 2014 and 2015

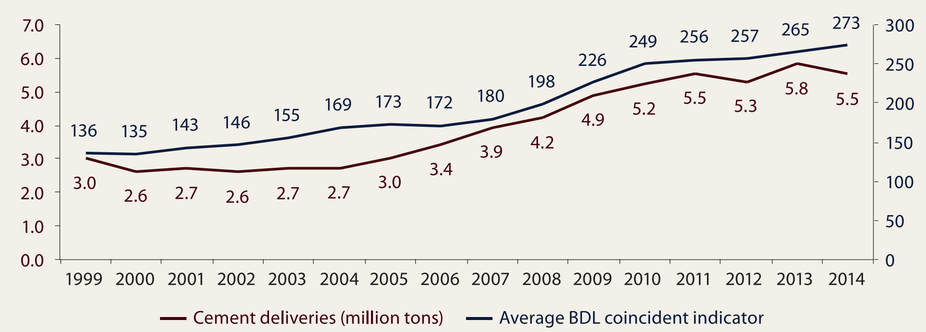
Sources: Order of Engineers of Beirut and Tripoli, BDL, Bank Audi's Group Research Department

Nabatiyeh soared. Furthermore, the Building Promoters Federation of Lebanon said that developers are currently building around 17,000 housing units per annum instead of the 25,000 a few years ago, noting that they are not taking into account anymore the 9,000 or so units that used to be demanded by non-GCC foreigners, Gulf nationals or even Lebanese expatriates.

Similarly, cement deliveries, a coincident indicator of construction activity, declined by a further 18.7% so far this year. Cement deliveries are also very highly correlated with overall economic activity in the country, with our regression analysis run over the past decade and a half between cement deliveries and BDL's average coincident indicator showing a 95% correlation between the two variables.

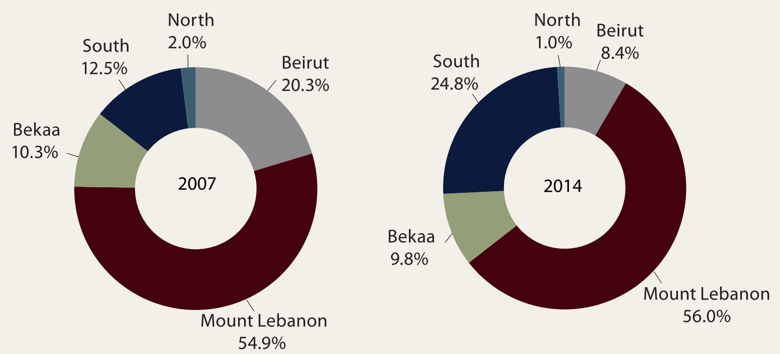
As real estate activity was mostly characterized by a further slowdown in demand domestically, construction costs stood almost still both last year and over the first seven months of 2015. Our compiled construction cost index for Lebanon, including various materials and labor prices, merely edged up by 0.5% in the first seven months of this year, mirroring a tiny 0.6% rise in materials costs amidst a nil change in labor cost. This actually reflects the overall market mood in a much calmer realty sector than during the pre-Arab Spring years. Besides, the large inflow of Syrian workers refugees willing to work for lower wages provides competition to Lebanese workers and puts adverse pressure on labor costs.

CEMENT DELIVERIES V/S BDL AVERAGE COINCIDENT INDICATOR



Sources: BDL, Bank Audi's Group Research Department

CONSTRUCTION PERMITS BY AREA



Sources: Order of Engineers of Beirut, Bank Audi's Group Research Department

A slowing property market yet does not mean activity is non-existent. It just obeys to the overall politico-security mood and buyer sentiment. And since locals are the ones driving the market nowadays, sales in the small to mid-size property market are the ones shaping trends. With prices still high in practically all residential areas, a persistent gap between property prices and the income per capita of Lebanese residents has been more or less plaguing sales in the market, regardless of the overall buyer mood.

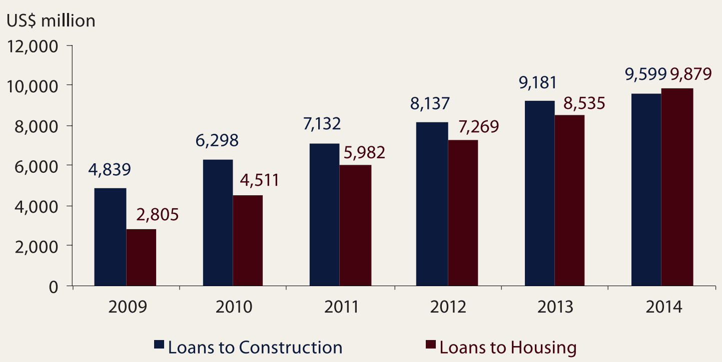
BDL stimulus packages a breath of fresh air to the market

This is where Banque du Liban has been injecting a breath of fresh air into the market. BDL indeed launched a welcome initiative by all stakeholders concerned a couple of years ago, implementing an economic stimulus package of which a non-negligible chunk has been allocated to housing, in order to boost economic growth in the face of the currently prevailing difficult conditions. As such, the past couple of years have seen BDL provide banks with subsidized loans to re-lend to the productive sectors of the economy. Envelopes of funds have thus helped local buyers acquire a permanent home while discouraging further speculating investors. Those housing loans are adequately targeting residents who actually buy a home to live in it, rather than selling it shortly after in the hope of making a quick buck, as there is a seven-year timeframe during which borrowers cannot make an early settlement of their loans without a penalty, and this is likely to discourage non end-user buyers.

BDL housing loan schemes allow buyers to benefit from funds over 20 or 30 years and are helping bridge this wide gap between their purchasing power and high realty prices. Since they are capped at around LP 800 million, these adequately cater to the current demand revolving around smaller sized flats on behalf of Lebanese residents. While boasting a floating rate tied to Lebanese Treasury bills and thus quite advantageous at lows persistent in post-global crisis outburst era, these are affordable and also somewhat allow developers to get some return on their investment. Amidst the lingering political deadlock in the country and tough regional conditions, BDL recently announced yet another round of stimulus measures for the year 2016 amounting to a record high US$ 1.5 billion (of which a significant portion of housing loans), which is expected to extend the win-win situation for all parties involved in the domestic realty market.

Total housing loans outstanding actually exceeded for the first time last year the outstanding stock of loans to the construction sector. Housing loans reached US$ 9.9 billion at end-2014, growing by 15.8% from the previous year and by 33.3% on average per annum since 2007 (i.e. when the market started booming), as per BDL statistics. Loans to the construction sector slowed down last year (+4.6%), likely

BANK LOANS TO CONSTRUCTION AND HOUSING



Sources: BDL, Bank Audi's Group Research Department

PROPERTY SECTOR FINANCING

US$ million	2008	2009	2010	2011	2012	2013	2014
Property sales transactions	6,481	6,955	9,479	8,841	8,926	8,708	8,957
o.w. Built property estimate	3,318	3,367	4,542	4,089	4,219	4,191	4,352
Housing loans portfolio	1,768	2,805	4,511	5,982	7,269	8,535	9,879
New housing loans	446	1,037	1,706	1,471	1,287	1,266	1,344
Avg lending ratio	13.4%	30.8%	37.6%	36.0%	30.5%	30.2%	30.9%
Avg self financing ratio	86.6%	69.2%	62.4%	64.0%	69.5%	69.8%	69.1%

Sources: Real Estate Registry, BDL, Bank Audi's Group Research Department reflecting slower construction activity, and reached US$ 9.6 billion at end-2014. We estimate the self-financing (i.e. non-bank debt financing) in the market, derived from new housing loans extended and an estimated percentage of built properties out of total sales, at close to 70% throughout the past couple of years. Although declining from levels exceeding 80% in 2007-2008 due to the expansion in banks' housing loans portfolios, the self-financing ratio remains quite high by international standards.

Price more or less still resilient to sales downturn

A curious phenomenon that has long shaped Lebanese residential realty is that despite the consecutive slowdown years the market has been going through, prices are sticky on the downside. They have only slightly nudged from their 2010 peaks, notwithstanding some mild discounts granted by some developers upon actually sealing a sales deal, and continue to be a major burden for prospective buyers/ boon for property owners.

The reasons behind the sticky prices are three-fold. First and foremost, the profile of buyers has a big role in shaping the stickiness or resilience of prices. These consist mostly of locals seeking to buy a property to live in it, rather than invest for a relatively short period of time and make an exit to cash in some gains. It is widely estimated that speculators do not account for more than 20% of total market activity on the overall, and thus have a limited role in shaping market pricing. Speculators are also discouraged by the stringent BDL measures aimed at keeping them away as much as possible from affecting price and activity dynamics to shield the market from investor mood swings to a large extent.

Second, property developers themselves are not heavily indebted towards banking institutions when it comes to their construction projects. While some do resort to banks to fund their building activity, the majority relies on self-financing rather than bank debt, otherwise on pre-sales which help them finance projects by injecting future residents' funds. This does not force developers to rush into sales at whatever cost just to reimburse bank dues. Instead, developers can allow themselves to sleep on their stock of apartments for a while as they wait for better days to come. Sometimes they even slow down the pace of construction activity which lengthens the time needed to complete a project, aiming to minimize costs in slow periods.

Third, with Lebanon being a small country with a more and more limited number of virgin plots available for sale, the cost of land is certainly not on its way down. This implies a structural support for flat prices. The latter consists of three main components, namely the cost of land purchased by the developer for the project, the construction costs, and the developer's margin. With the first component not likely to go down, and the second one not easy to squeeze for discounts, the developer's margin remains the only option to play around with in order to possibly move prices down in the current situation.

But with low leverage, developers have not been encouraged to sacrifice much of their margin. At the same time, since the domestic/regional situation has not really improved in last few years, the stock of apartments for sale has grown. Projects that were kicked off before 2010/2011 and consisting of larger sized apartments are quite tough to sell, while those of smaller size are, as mentioned already, faring better these days. Ramco Real Estate Advisers recently estimated in a study of 56 projects completed in 2014 and spread over 51 neighborhood in Municipal Beirut that 83,976 sqm of residential area completed last year have not been sold, representing 271 new apartments equivalent to a value estimated at close to half a billion dollars.

Within this context, developers wanting to get some liquidity or at least progressively sell some flats in their projects have started granting some mild discounts to serious enquirers. The reality is that those discounts, while limited in value and usually proportional to the size of the apartment, are getting more frequent than before. This does not mean that all developers are granting discounts. But when some do, price discounts hover around 10% and can reach up to 20% in some cases.

It is worth noting that there is a difference between the asking sales price and the actual sales price. The latter is usually the one post-mild discounts, as the former has not really seen much of a change. Asking prices have maintained their high levels despite the sharp slowdown in activity, with sticky prices ruling the market and occasional though increasingly frequent discounts remaining quite limited in value. We are talking about discounts and not price declines per se, only in the aim of giving a boost to a tough market for sellers nowadays.

For instance, and in the absence of official or comprehensive country-wide figures, Ramco Real Estate Advisers lately announced that the prices of apartments under construction in Beirut edged down by a mere 0.7% in 2014. This study tracks the evolution of asking sales prices (per sqm, and not final ones) on the first floor during 2014 across 249 residential buildings under construction in 67 neighborhood across Municipal Beirut. In August, the same source revealed that a spring study covering 345 residential buildings under construction across the same areas reveals that the average value of a first floor apartment declined by a small 4% between 2014 and 2015 over a twelve-month period. One must bear in mind this 4% drop combines both a lower surface on the market and a slightly inching down price per square meter, and thus differs from the previous study covering 2014. Had it not been for those factors shaping the sticky-on-the-downside feature of realty prices in the country, the market would have likely seen sharper price declines. It is worth adding that those negotiations always took place and are not restricted to the slowdown phase. It is just that in the slowdown phase, actual discounts granted are likely to be higher than in the pre-Arab Spring days.

To sum things up, property prices in Lebanon take the form of an ascending staircase. They stay more or less stable for a while under economic slowdowns, then go up in an upward adjustment phase similar to the one we witnessed in the 2007-2010 period economic boom. But they never really go down, at least tangibly. At best, some mild discounts are granted but on the overall, their value remains pretty much the same, making it a sought-after safe haven for investors in Lebanon.

Rents following sales market trend but supported by Syrian demand and high selling prices

Against the backdrop of such high prices, and regardless of those discounts, some residents have been turning towards rentals rather than buys. Some are also concerned about the domestic situation, and have decided to adopt a wait-and-see attitude before deciding to go for a buy. Some others, and those are mainly Syrian refugees, have directly opted to rent awaiting the outcome of the war in their country. Those three market players' profiles have helped the rental market, traditionally less vigorous than the sales market, regain some momentum. Rentals are the most frequent in the capital city, though suburbs are also sought after on behalf of locals and some expatriates working temporarily in Lebanon (diplomatic missions, multinational agencies, etc).

At the same time, the supply in the rental market is not tight either. Some Lebanese now working abroad have decided to put their flats for rent, and a few others, who had made an investment in the country or inherited a property, are renting it out either to yield a return or awaiting the next wave of price appreciation in order to make gains on their investment.

As such, demand is more or less healthier in the residential rental market relatively to a few years back mostly owing to the Syrian factor, and supply is quite ample, which fact also keeps room for some discounts in specific cases. Usually, since the rental period is relatively limited in time and the amount less sensitive than in the case of a buy, the negotiation process can be less problematic and more flexibility is shown from both sides. But on the overall, the same trends shaping sales prices are leaving their imprints on the rental market, and some landlords are finding it difficult to find tenants.

Within the context of high property prices, Beirut's annual rental yields (pre-tax, maintenance fees and other costs and excluding newly built properties) remain relatively low and below those of peers in the MENA region, as per the latest available figures released by Global Property Guide. The latter puts the average rental yield in Lebanon's Beirut (150 sqm flats) at around 4.5% (and this goes down to close to 3.5% for apartments of 250 sqm and above), against higher averages in the 5%-11% range for premier city centers of the UAE, Morocco, Egypt and Jordan, in ascending order, and reaching 6.1% for emerging markets.

It is worth noting that the new rental law (also governing pre-1992 contracts) voted last year was supposed to take effect in late 2014. But the Constitutional Council decided to send it back to the Parliamentary commission in charge requesting a few amendments. The latter decided to enlarge the amendment scope so as to place tenants in a better position yet without compromising owners' position, and sent it to the Parliament for approval. With the Parliament's activity currently blocked, the new amended Law has yet to be voted. Anyhow, one of the amendments stipulates that the new annual rent would constitute 4% rather than 5% of the current value of the apartment. Another of the amendments revealed by the committee would make longtime tenants whose salaries are up to five times the minimum wage have their rent liberated after the twelfth rather than ninth year. Among other amendments, the fund created by authorities to help lower income people would pay the full increase in rent for tenants whose salaries are less than three times the minimum wage and 80% of the increase for those whose salaries range between three and five times the minimum wage.

With residential realty bearing the brunt of the economic slowdown and delicate local and regional politico-security conditions, some developers have turned to commercial real estate development, namely office and retail property construction, believing they could achieve faster and lucrative sales there.

RETAIL MARKET TRENDS

Further slowdown in retail market activity but prime F&B hotspots buck the trend

The Lebanese retail property market remains influenced by the accentuated economic slowdown and volatility of politico-security conditions, with consumption spending slowing down and reflecting on buyers' appetite across retail stores. As a result, supply of retail space exceeded demand thus leading to downward price pressures across retail areas.

Demand remains concentrated in mall shops and local branded stores outside malls across several areas, noting that the retail market continues to see considerable demand revolving around the food and beverages sector. While Mar Mikhael and Badaro, two of the capital city's vibrant nightlife hubs and offering a wide array of food and beverages services, continued to buck the overall retail market trend, several areas such as Hamra, Verdun, Gemmayzeh and Maarad, which were once flourishing, have been encountering a downturn, among others.

In details, Maarad Street had lost its vibe against the backdrop of the unstable political situation in the city's capital and the repetitive protests in addition to the tourism activity slowdown in recent years. Several retail units and restaurants closed, leading to an increase in the units supplied in the market, and exerting downward pressure on rents. Gemmayzeh has seen a good deal of competition, especially in the food and beverages segment whereby the spotlight gradually shifted to various areas like Mar Mikhael, Hamra and Uruguay Street. Accordingly, demand was shyer in the area and with a number of restaurants shutting down and the stock of vacant units rising, pushing down rental prices. Alongside, some areas in Hamra encountered downward rental price pressures despite their diversified retail market space that encompasses both local brands shops in addition to food and beverages units. It is worth noting that amidst the currently prevailing conditions, the decline in rents has not been sufficient to attract further demand which is awaiting an improvement in the overall investment climate and an upturn in the economic cycle.

Opposing the trend, retail demand in Mar Mikhael has been outpacing existing supply. This is leading to upward pressures on rental prices. Alongside, Badaro is also faring well. With the relatively more expensive rents in Mar Mikhael and the dimming vibe of Gemmayzeh, Badaro, which remains a relatively affordable area, is an emerging commercial address and seeing healthy demand. The area seems to be offering opportunities for companies operating in the food and beverages sector, with some available supply, and easy access from both within and outside the capital city's major arteries. Badaro is a conveniently located residential and commercial office area providing prospective tenants with a non-negligible potential client base.

Within this context, the latest Cushman & Wakefield global survey of the prime retail locations around the world covering the 12 months to September 2014 shows that Beirut's prime locations rents declined by 11.6% on average relative to the previous survey (covering the 12 months to June 2013). This reflects declining rents across prime retail hubs in the country.

The survey shows that Beirut's prime retail locations rent stand below those of all other regions. The MENA countries' prime retail spots surveyed by Cushman & Wakefield boast average rents 63% above those of Beirut's prime retail locations. Furthermore, rents of the emerging markets' prime retail spots stand 45% above those of Beirut's and the global average is almost 1.5 times that of Lebanon's capital city prime retail spots.

It is worth noting that a number of retail arcades and shopping centers are opening in once virgin areas away from the capital to cater to the needs of the resident populations in these areas. Such retail units are opening in several areas across Mount-Lebanon, the South, the North and the Bekaa, allowing the retail market offering to develop and expand in more remote zones.

Without a tangible improvement in the local political and security climate, the retail landscape in Lebanon is likely to continue experiencing a downturn. In the end, demand is quite linked to the economic cycle and to a certain extent to purchases on behalf of foreigners, and thus tied to tourism activity. However, the foreign component of demand is only likely to be fully encouraged by a wide scale amelioration in regional security conditions, especially those wealthy Gulf tourists who like to shop and spend big bucks while on holidays in Lebanon.

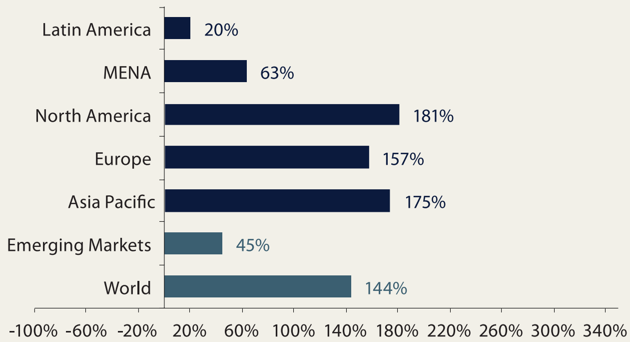
OFFICE MARKET TRENDS

Economic slowdown and political uncertainty weighing on demand for office space

The performance of the office market remained sluggish over the covered period, amidst political and security uncertainties, not to mention their impact on economic conditions and business activity. Office rents in Lebanon witnessed declines on the overall in the past year as local businesses are postponing new investment plans in the market until there is more stability in the country. The market has been mostly stagnant and the stock of new supply has pushed the overall market supply to exceed demand on the overall.

Office space remains mostly concentrated around the Beirut Central District (BCD), Achrafieh, Hamra and Verdun areas, noting that some areas outside Beirut have recently been the focus of developers (Sin el Fil, Dbayeh, etc). BCD has been the prime office destination in Lebanon. In fact, the area that falls within the perimeter of Solidere boasts around 150 dedicated office buildings, making it a business hub with the largest concentration of office buildings in the country. According to Ramco Real Estate Advisers, the BCD has been the traditional market leader in terms of pricing, and it is also the benchmark for quality amongst office stock in other parts of Beirut.

RETAIL RENTS 12 MONTHS TO SEPTEMBER 2014 RELATIVE TO PRIME BEIRUT RENTS



Sources: Cushman & Wakefield, Bank Audi's Group Research Department

Rental values in BCD have been on a downward trend over the covered period and prospecting tenants can currently negotiate office spaces at double-digit discounts, as per the same source. In recent weeks, the wave of popular protests across major BCD arteries has been affecting traffic and activity in these areas, and this is likely to hinder demand for office space until the situation is resolved. Areas outside the BCD in the capital city remained stagnant and a few minor discounts here and there could sometimes be observed.

This has yet not prevented the Lebanese market from witnessing the kickoff of new projects in recent times. As a matter of fact, some developers opted to turn to office projects as an alternative to residential projects in light of waning demand, and as some land plots are located along noisy areas and would not attract many residential buyers in the first place. The office market in Beirut boasts 37 projects currently under construction in Municipal Beirut, representing 195,694 square meters of office space, as per the same source's study dated February 2015. It is worth noting that out of the total number of projects under construction, 29% are part of mixed-use projects that offer offices on the lower floors and residential apartments on the upper floors. The office stock under construction has increased by 32% in February 2015 from their previous survey dated September 2013.

The Beirut Central District witnesses more than 43 thousand square meters of office space under construction. Some of this stock would be offered on the rental market, which leaves slightly more than 80% of office space available to the sales market, the bulk of which would be delivered between 2016 and 2017, as per the same source.

On the Western side of Beirut, only 21,611 square meters of offices are under construction, mainly in Hamra, Bachoura, and UNESCO. It is yet worth noting that a number of offices in Hamra have been devoted to the area's medical profession. The proximity of some of the largest hospitals nearby (AUBMC, CMC, among others) warrants the presence of office clinics in the area.

But the largest stock of new offices remains in the Achrafieh area, with two thirds of the total upcoming office stock in the capital city, in particular Corniche el Nahr, Adlieh, and Badaro. These areas are the most active, mainly along the axis that links the National Museum to the area of Fiat. In the next couple of years, the south-eastern part of Achrafieh is poised to become an important business destination, as new stock is in the pipeline and would by then come to the market. Moreover, these areas are easily accessible and have a strategic location at the crossroads of major arteries linking the capital city to suburban areas.

Sin El Fil and Dbayeh are also emerging as prominent office spots due to their strategic location between the North of the country, Metn and Beirut. Sin el Fil in particular seems to be imposing itself as an area providing high quality offices, with an ability to compete with more traditional office hubs such as downtown, Ras Beirut, Charles Malek and Adlieh areas. Some companies are thinking in terms of renting relatively larger and more modern office space outside Beirut with better parking amenities.

While rather steady demand for office space was just about met by supply in the past few years, the ongoing projects remain apt to modernize the office stock in the country. However, the pace at which demand would follow the increase in supply of dedicated office space is likely to be determined by the evolution of the political situation and its impact on the business climate in the country.

CONCLUDING REMARKS: PROPERTY MARKET OUTLOOK

The Lebanese property market is continuing to experience an activity slowdown nowadays, and is mostly operating on the flat side of the price staircase. This means that prices have been mostly resilient to the activity slowdown. Indeed, some mild discounts have been granted to residents serious about buying a residential property for their own use. The big question on the minds of investors and buyers alike, be they residents, expatriates or foreigners, is what happens next? Where is the local realty market heading? Are there going to be further discounts or some sort of price declines? Or on the contrary is the market on the verge of seeing a new wave of price appreciation?

While there are many unknowns here, one thing is certain: the outlook of the local realty market is strongly tied to the evolution of the domestic and regional politico-security situation. In the event the situation stays the same or somehow worsens, buyer mood will remain quite sluggish, perhaps even more so. But one must not forget that there is an incompressible number of housing units demanded every year, within the context of a Lebanese population growth above 1% creating more than 10,000 new households per annum. Newlyweds cannot indefinitely postpone their purchase, and renting over the long run can prove quite costly as there can not be a return on investment for the tenant. There is likely to be some demand for residential realty, albeit at a possibly slower pace. BDL schemes would once again prove as handy as needed and would facilitate some transactions. It would be interesting to see how much developers would be still willing to wait, and if they would think of sacrificing a bit more of their margins. With the current low leverage and end-user demand dynamics prevailing in the country, adding to upward land price pressure, prices are still not likely to decline tangibly. At best, some additional and at least more frequent discounts could be registered. The price side of the equation would not be very much affected, but the sales and transactions side is likely to take the bigger hit.

In the event the situation improves, things could be quite different. Should buyers perceive sustained signs of amelioration, the market is likely to see improved investor sentiment lead to more sales, and developers would then gradually be less inclined to grant discounts. Sufficient sales would at first give them less reasons to be flexible as is the case presently. Buyers would gradually lose their proudly acquired bargaining power and prices would stabilize around current asking price levels in the first phase. Should the positive signals prove sustainable, i.e. the resumption of cabinet action and election of a President and normalization of the domestic political situation, the sales activity would gradually erode the excess supply in the market and the demand/supply mismatch would gradually be reduced, though this could take some time given the accumulated large stock of unsold properties.

This would give the time for buyers and prospective investors to further digest new price dynamics (relative to pre-boom era) and slowly turn realty activity back into a seller's market, be it at the level of residential or commercial realty, though in order for that to fully happen, clearer visibility on the Syria front might be required. At a later stage, mainly in the event of a regional settlement scenario, upward price pressures could start making a comeback. Locals might be generating sufficient demand in the lower to mid-sized flat segment, and might even not be the only market players active then. Expatriates who are keeping a close eye on their home land and are looking for the right time to gain a foothold or vacation residence might turn from occasional enquirers to actual buyers. Same goes for foreigners, especially Arab nationals, who like to spend time in the country and choose it as one of their preferred travel destinations.

A much better visibility on the regional security front would encourage them to return to the market after years of absence. One must not forget that the foreigners were the ones who, along with well-off expatriates, contributed to raising price levels by adding to resident demand and creating a strong buying momentum. Hopefully by then the domestic economic activity would have started improving in a way that alleviates the purchasing power/realty prices gap, though the latter is likely to persist for quite a while and somewhat restrict the majority of local demand to the smaller flats.

This is especially valid if the dust settles on the neighboring Syrian ground, with all positive spillovers it holds for the Lebanese investment climate in general, and realty market in particular. While things are quite uncertain and complicated for the time being, this remains a longer term scenario that can certainly not be ruled out, notwithstanding potentially lucrative opportunities for Lebanese developers who could participate in the reconstruction of some of the neighboring country's torn buildings. But meanwhile, the region continues to be meddled into what appears to be a persisting state of uncertainty and violence, and Lebanon's realty activity continues to be hindered by political bickering and paralysis. The way things are right now, the Lebanese real estate market is definitely a buyer's market, today more than ever. In this sense, the many buyers or investors well acquainted with the local market pricing dynamics and seeking a residence in the country have all the bargaining power they need, and choice of residences they can think of not to mention financing options available, to make a good buy today, awaiting to reap the benefits sometime in the future.

APPENDIX: SOLIDERE POSTS FURTHER INCREASE IN NET REVENUES IN 1H2015 FOLLOWING STRONG 2014 UPTURN

Solidere, the largest Lebanese real estate developer, recently issued its first half 2015 financial performance results, posting consolidated total revenues of US$ 57.8 million, up by 48% from US$ 39.0 million in the same period of 2014. This follows a 47% annual increase in total revenues to reach US$ 239.0 million in 2014, mostly owed to a higher number of sales contracts.

Solidere has three business segments consisting of real estate sales, real estate rental and rendered services, and hospitality. The breakdown of revenue by segment shows that land sales revenues attained US$ 26.4 million in the first six months of 2015, surging from US$ 6.4 million in the first half of 2014. Revenues from rented properties registered US$ 28.2 million in the first six months of 2015, up by 2.7% year-on-year. In contrast, revenues from rendered services dropped from US$ 3.6 million in the first half of 2014 to US$ 2.9 million in the corresponding period of this year. Revenues from hospitality declined to US$ 0.3 million in the first six months of 2015, from US$ 1.5 million in the same period of 2014. Solidere's total cost of revenues reached US$ 21.8 million in the first half of 2015, against US$ 18.0 million in the same period of last year.

As a result, the company's net revenues from operations reached US$ 37.2 million in the first six months of 2015, against US$ 23.6 million in the corresponding period of 2014. This outpaced the variation in general and administrative expenses, which edged up by 0.3% year-on-year in the first half of 2015 to reach US$ 18.7 million.

While Solidere's net revenues from operations posted a further increase so far this year and the company benefited from an 84% increase in the share of results of associates and joint ventures, it recorded a net loss during the first six months of 2015. In fact, Solidere set up a provision for the probable loss on a previously executed sale contact in the amount of US$ 50.5 million. The contract value amounted to US$ 59.8 million with an outstanding receivable of US$ 44.8 million (excluding interest) as at end-June 2015.

Solidere reported a net loss of US$ 28.7 million in the first half of 2015, with the company's real estate sales segment posting the largest loss. The latter recorded a net loss of US$ 45.3 million in the first half of 2015, on the back of the US$ 50.5 million provision for loss on a contract. Solidere's hospitality segment also reported a narrow net loss over the same period. On the other hand, the real estate rental and rendered services segment posted net profits of US$ 13.3 million in the first half of 2015.

On another note, the company's consolidated financial statements showed that Solidere's assets amounted to US$ 2.9 billion at end-June 2015, slightly inching down from US$ 3.0 billion at end-2014. Inventory of

SOLIDERE SELECTED FINANCIAL INDICATORS

US$ million	2008	2009	2010	2011	2012	2013	2014	1H 2015
Revenues from land sales	256.6	305.1	337.2	241.7	49.6	94.9	169.5	26.4
Revenues from rented properties	21.7	27.3	41.2	49.9	54.3	54.9	61.5	28.2
Net revenues from operations	206.1	234.1	272.5	227.9	71.4	112.8	180.6	37.2
General and administrative expenses	19.4	26.2	42.7	38.2	36.7	30.9	34.3	18.7
Net profits	182.7	189.2	195.5	158.8	17.2	42.6	113.7	-28.7
Total assets	2,454	2,399	2,600	2,769	2,836	2,873	2,964	2,906
Total equity	1,860	1,810	1,838	1,935	1,908	1,951	2,065	2,036
ROAA	7.3%	7.8%	7.8%	5.9%	0.6%	1.5%	3.9%	-
ROAE	9.9%	10.3%	10.7%	8.4%	0.9%	2.2%	5.7%	-

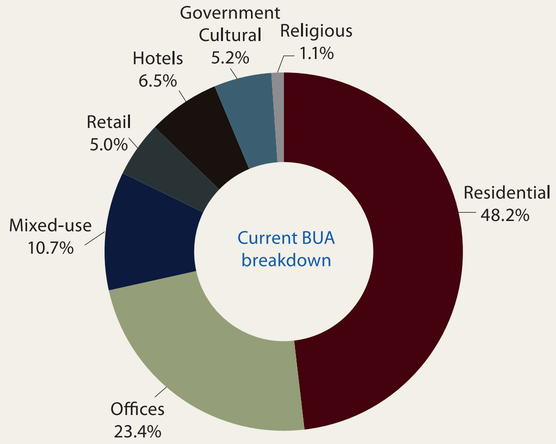
Sources: Solidere, Bank Audi's Group Research Department land and projects in progress stood at US$ 1.1 billion at end-June 2015, nearly unchanged from end-2014. Cash and bank balances declined from US$ 158.7 million at end-2014 to a still comfortable US$ 108.8 million at end-June 2015 (due to lower short-term deposits balance), thus bearing witness to a still healthy overall liquidity position. Cash and bank balances include US$ 73.4 million as of June 2015 representing current bank accounts with a local bank that is a significant but minority shareholder of the Group.

Solidere's total equity stood at US$ 2.0 billion at end-June 2015, slightly down from US$ 2.1 billion at end-2014, and accounting for a large chunk of the company's funding side of the balance sheet (70% at end-June 2015). As a matter of fact, the company's leverage remains low as reflected in the debt-to-equity ratio, which reached 32.1% at end-June 2015. Furthermore, the adequate liquidity position of the company helps alleviate even further the leverage ratio. The net debt-to-equity ratio reached 26.7% at end-June 2015.

The shareholders of Solidere decided in their ordinary general assembly that the company would distribute dividends amounting to US$ 52.9 million for the financial year 2014, noting that the previous year did not see any distribution of dividends. Each of the Class (A) and Class (B) shares would entitle to US$ 0.1 (10 cents) in cash dividend per share for a total of US$ 16.0 million. Moreover, one share of Class (A) or Class (B) shares would be offered for every 50 Class (A) or Class (B) shares from the Treasury shares for a total of US$ 36.9 million. It is worth recalling that Solidere registered net profits of US$ 113.7 million in 2014, surging by 2.6x from those registered in 2013. The dividends distribution comes within the context of sluggish equity price performance on the Beirut Stock Exchange and very low total market share turnover ratio as a percentage of market capitalization (4.1% in the first half of 2015 and 5.9% in full-year 2014) relative to regional and global benchmarks (70% and 160% respectively).

Given current macroeconomic conditions, Solidere is taking a more prudent approach to ensure that company resources are used more cautiously and at the opportune time. It has worked on prioritizing and rescheduling real estate projects, streamlining operations, decreasing overhead expenses, and preserving the solid capital structure. In line with market conditions and to boost the momentum of investment in the area, Solidere has introduced a set of favorable and competitive terms including flexible financial conditions with regard to land purchases. The company is focusing on completing the infrastructure in the reclaimed area.

SOLIDERE LAND USE



Sources: Solidere, Bank Audi's Group Research Department

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