

High-rising prices

Wage hikes and slowing demand raise the pressure for developers

By Jeff Neumann

If you have read this far through our special report, you probably have a good idea of the challenges faced by the real estate sector over the past year. Data shows that demand for residential property is weakening across Lebanon and developers are coping with higher operating costs than before. How they adapt will determine how well they weather what some expect to be a prolonged downturn.

Overall construction costs in Lebanon were up in the first few months of 2012, due in part to the

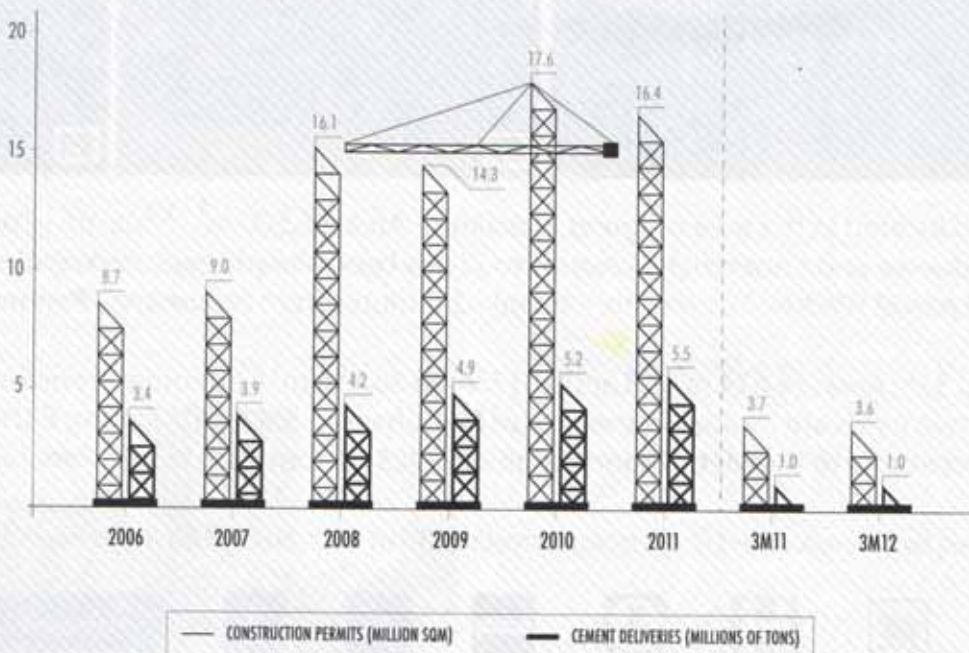
mandatory wage increase approved by the government in March. However, material costs have for the most part stayed at the same levels through the first five months of 2012. For instance, steel in Lebanon has remained at \$750 per ton through June; Portland cement cost \$102 per ton over the same time period.

Shaving the fat

When asked about what is being done to cut costs, most developers declined to go into detail. The one exception, Karim Bassil, founder of BREI Real Estate Investment, offered a brief insight into

BUILDING BASICS

CONSTRUCTION PERMITS & CEMENT DELIVERIES



Source: Order of Engineers of Beirut and Tripoli, Banque du Liban, Bank Audi's Research Department



Stable prices of steel are one less thing to keep developers up at night

his company's operations. "The main thing is we're reducing our overhead, we're reducing our margins. We have already reduced our margins by 50 percent this year," he says, describing the return generated from new income on a project. "We're just not making the same kind of money that we were making before," adds Bassil. "In Lebanon, when you plan something for, let's say, 30 percent ARR (average rate of return), you end up with 20 percent of 70 percent ARR."

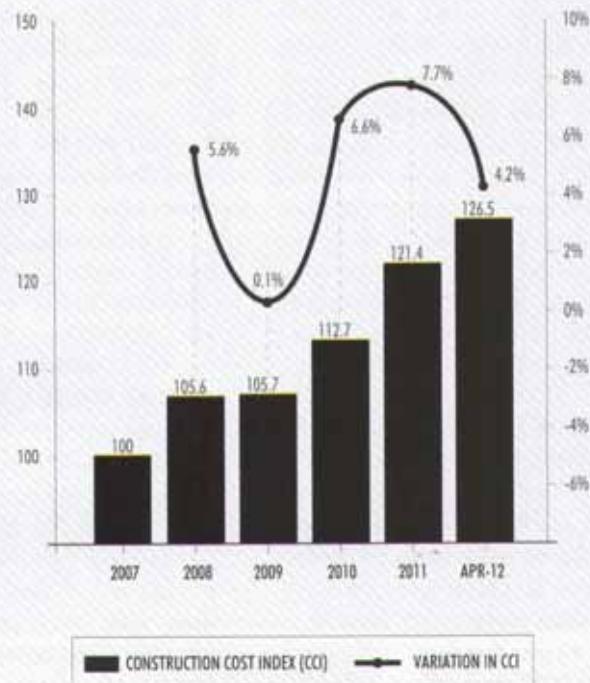
Cement deliveries are also down this year by 4.2 percent — another obvious indicator of a slowdown in construction. This stings developers even more due to the fact that between 2005 and 2010, average annual deliveries increased by 11.2 percent. As an example of the many factors listed coming to a head, Bassil says that "on one of my projects in Beirut, instead of putting it around 20 percent ARR, we put it at 8 percent. This is because of politics, war and project delays — they all play a role in [reducing ARR]."

Through May, the total number of construction permits issued in Lebanon was down 9.3 percent from May 2011, according to data compiled by InfoPro. Also of note, construction area authorized by permits were down 12.5 percent from the same time last year.

Indeed, times are tight for the sector, forcing developers and contractors to consider all options. As Bassil puts it, "Personally, we're doing everything to keep our business alive for better days to come."

THE BILL ON BUILDING

CONSTRUCTION COST INDEX



Source: Davis Langdon, Infopro, Bank Audi's Group Research Department