



How Europe Can Help Lebanon Overcome Its Economic Implosion

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Principal Findings

What's new? The devastating blast in the Beirut port on 4 August 2020 was only the latest, and most terrifying, sign of the political bankruptcy of Lebanon's ruling elites. These politicians have driven the country to the brink of ruin, as the banking sector collapses and COVID-19 spreads faster.

Why does it matter? Lebanon's donors cannot countenance the country becoming a failed state. Yet their calls on Lebanese elites to undertake thoroughgoing economic and political reforms have gone unheeded, accelerating the downward trend. The U.S. "maximum pressure" campaign against Iran, which also targets Hizbollah, is further complicating matters.

What should be done? Even as it conditions funding of major development projects on substantive IMF-proposed reforms, Europe should expand urgently needed humanitarian aid, seek to improve transparency and civil society involvement in its projects, and urge the U.S. to lessen pressure on Hizbollah while trying to engage the movement in the reform agenda.

Executive Summary

Lebanon's post-war political order may have reached its limit as its economy implodes. Its elites have yet to chart a way out of a crisis that they created themselves over the years. Their failures have provoked popular, occasionally violent, protests that have continued despite the COVID-19 pandemic. Lebanon's main donors, especially in Europe, are keen to see the country recover but, conscious of its poor record of instituting reforms, have attached strings to assistance beyond emergency humanitarian aid. Donors have told the government and ruling elites that they must first reach a deal with the International Monetary Fund (IMF) and carry out reforms in accordance with past commitments. French President Emmanuel Macron's visit following the 4 August blast in the Beirut port, which destroyed part of the city and caused over 200 deaths, conveyed a similar message. The European Union and member states should stick to this line, agreeing to resume non-humanitarian assistance only once the Lebanese authorities launch genuine reforms that benefit the country as a whole, not just the privileged few.

In the face of economic collapse, Lebanon's political leaders are looking for ways to fill the country's yawning financial gap, including by soliciting support from international financial institutions, but they resist taking the steps that those institutions request in return. Each leader is blaming another for standing in the way of reforms that put the public good ahead of political and private interests. Donors are disinclined to throw good money after bad, especially when the "bad" is a gigantic Ponzi scheme of elite self-dealing. International financial institutions and governments concerned about Lebanon's welfare and stability have insisted on structural and sectoral reforms since at least 2018, making them a condition for further financial assistance.

Lebanese leaders have dragged their feet, perhaps hoping that donors would show flexibility out of an overriding interest in the country's stability in a turbulent region. The protests that broke out in October 2019, triggered by yet another attempt to raise revenues from the population (a fee on the use of WhatsApp for voice calls), showed that this ploy was not working, bringing down the government of Prime Minister Saad Hariri. After January 2020, the replacement government of Prime Minister Hassan Diab made no headway in instituting reforms, either. The tragic 4 August explosion in the port of Beirut, apparently the result of years of official negligence and incompetence, forced his government to resign.

Today, little has changed. Macron launched an initiative that promised a way out of the crisis, but Lebanese leaders have yet to take a concrete step. A newly appointed prime minister, Mustapha Adib, promptly resigned after failing to form a government; negotiations with the IMF are at a standstill; and protests continue, with activists calling for greater transparency and better governance, and demanding that Lebanon's international supporters refrain from bailing out the country's elites without first securing meaningful reforms. Hariri, who was again named premier on 22 October, faces tasks no easier than those that confounded Adib.

The EU and European governments have long been among Lebanon's principal donors. France, in particular, has hosted numerous donor conferences, and President Macron has pledged to mobilise additional support. For a long time, such assis-

tance came with no or few conditions attached, despite obvious flaws in the country's governance and economic model. Short-term stability seemed to be the main concern. That appears to have changed, as donors more recently have tied major investments in the country's infrastructure to substantial sectoral and structural reforms, and then refrained from releasing funds as the Lebanese government failed to improve its practices.

The stalemate is compounded by the U.S. "maximum pressure" campaign against Iran, which has affected Iran's Lebanese ally, Hizbollah. While endorsing the European demand for reforms, U.S. officials accuse Hizbollah of blocking progress and object to Macron's decision to invite Hizbollah, along with all other parties, to participate in the reform effort. Instead, Washington has slapped sanctions on the Lebanese movement's allies in an effort to isolate it. This U.S. policy, European officials say, is hampering their effort to pull Lebanon out of the pit.

Yet these donors now face a dilemma: while they do not want the country to become a failed state that spawns a severe humanitarian crisis, they also do not wish to rescue elites whose track record suggests they are capable of taking Lebanon over the precipice. They therefore try to calibrate their aid policy by responding to acute short-term needs with emergency humanitarian aid while keeping their projects for basic infrastructure operational and tying pledges of more substantial aid to the launch of genuine reforms.

It remains unclear whether this approach will bear fruit. European donors' ability to help Lebanon confront its long-term challenges is inherently linked to its political leaders' will to act. Little may change, therefore, in the short to medium term. Yet donors can nevertheless use the current moment to clarify their thinking and messaging, and also to set the bottom-line standard for future aid.

They should stress that their diplomatic position is not part of or aligned with the U.S. "maximum pressure" campaign against Iran, and that their demand for fundamental reforms is aimed at putting Lebanon back on track, not at clipping a particular political party's wings. They should also reaffirm that no Lebanese political leader can expect to receive a free pass solely for being Western-aligned, and that the entire political class will have to make concessions. And, consistent with their global policy, they should insist on minimal standards of transparency and accountability within Lebanon's public institutions and judiciary.

Finally, they should define benchmarks tied to the different stages of projects they intend to support, including by sequencing reforms in the concerned sectors; make efforts to improve transparency and public access to their own project monitoring and evaluation; find ways to better integrate civil society-based expertise in decision-making about externally funded projects; and explore ways to support a dialogue between political forces and civil society organisations to jointly tackle institutional obstacles to reform.

Beirut/Brussels, 30 October 2020

How Europe Can Help Lebanon Overcome Its Economic Implosion

I. Introduction

Lebanon is in desperate need of emergency aid, with the Lebanese pound having lost 75 per cent of its value since October 2019, more than half the population living below the poverty line, 35 per cent of the work force unemployed, and nine in ten Syrian and Palestinian refugees food-insecure.¹ While the first wave of the COVID-19 pandemic that broke out in March was contained by an effective, if economically costly, three-month lockdown, a second wave hit the country with full force in August.² This dire situation was compounded by the 4 August blast in the Beirut port, which killed over 200 people, destroyed large parts of the city and left some 300,000 people homeless.³

Despite several European initiatives, spearheaded by France, Lebanese political leaders have failed to satisfy donor conditions for reforms that would help put the economy back on track. As a result, the European Union (EU) and European governments have disbursed no significant funds over the past couple of years, except for humanitarian aid and money for projects already underway. The ruling elites' inability to reach an agreement with the International Monetary Fund (IMF) and implement necessary reforms – the first steps to unlocking more substantial foreign aid – is pushing the country closer to the edge.⁴

This report addresses the question of what Europe should do when it does not want its Mediterranean basin neighbour Lebanon to disintegrate, yet also does not wish to perpetuate, much less deepen, the economic malaise by continuing to indulge, and thus further entrench, the Lebanese ruling elite. Research consisted of some 70 in-person and telephone interviews between March and September 2020 with Lebanese activists, NGO representatives, economic experts, EU and European government officials and diplomats, U.S. and Canadian diplomats, officials of Lebanon's main donors and international aid organisations (the World Bank, UN and Organisation for Economic Co-operation and Development), and representatives of development agencies in Beirut and the main European capitals.

¹ See the data on Lebanon compiled by the Economist Intelligence Unit. The UN Food and Agriculture Organization (FAO) defines food insecurity as occurring when “people are unable to meet their minimum food requirements over a sustained period of time”. See “An Introduction to the Basic Concepts of Food Security”, FAO, 2008.

² “Lebanon imposes night curfew, closes bars as COVID-19 patients exceed 53,000”, *Arab News*, 12 October 2020. The health sector has been especially hard hit by the combined effects of the pandemic and port explosion. “The Beirut blast left Lebanon's health system badly shaken”, ReliefWeb, 13 October 2020.

³ See “Beirut Explosion Situation Report #4, August 25, 2020”, UN Office for the Coordination of Humanitarian Affairs, 25 August 2020.

⁴ For background to the crisis, see Crisis Group Middle East Report N°214, *Pulling Lebanon out of the Pit*, 8 June 2020; and Crisis Group Middle East Briefing, *Lebanon: Keeping Hizbollah in the Fold*, forthcoming.

II. A New Aid-with-Strings-Attached Strategy

Lebanon's economic decline has been long in the making and its causes have been plain for all to see. European governments, especially the French, have launched a series of initiatives in the past two years that sought to reverse the downward trend by mobilising international assistance on the explicit condition that Lebanese leaders institute sweeping reforms. This insistence came with the recognition that support provided through donor conferences held between 2000 and 2007 had failed to address substantial flaws in Lebanon's governance.

A. *The 2018 CEDRE Donor Conference*

In April 2018, states that had been supporting Lebanon's post-civil war recovery organised a donor conference in Paris, the *Conférence économique pour le développement par les réformes et avec les entreprises (CEDRE)*.⁵ They billed it as an initiative "to support the development and the strengthening of the Lebanese economy as part of a comprehensive plan for reform and for infrastructure investments".⁶ Unlike earlier donor conferences, CEDRE focused solely on projects, mainly in infrastructure development; was based on soft loans, grants and private investment; and, most importantly, conditioned its aid on the government carrying out both sectoral and structural reforms.⁷ CEDRE's main objective was to stimulate productivity and sustainability in the medium to long term at a time when Lebanon's economic and financial system's failures had become increasingly apparent. A European diplomat said:

CEDRE was conceived in 2017 as a plan to put the Lebanese economy back on track. We had to restore balance in our relationship with the government [ie, no longer giving it a blank check], and do what the IMF [normally] does but without the IMF [being involved]. The situation had degenerated at the time but could still be controlled. Yet we all saw the iceberg coming. CEDRE was the conference

⁵ The CEDRE donors are France, Germany, the Netherlands, Italy, the UK, the U.S., Saudi Arabia, Kuwait, Qatar, Turkey, the EU, the European Investment Bank, the European Bank for Reconstruction and Development, the World Bank, the Arab Fund for Economic and Social Development, and the Islamic Development Bank.

⁶ "CEDRE – Joint Statement", France Diplomatie, 6 April 2018. The Lebanese government presented a Capital Investment Plan outlining 269 projects in all major infrastructure sectors and received funding pledges amounting to \$11.06 billion (\$10.2 billion in loans and \$860 million in grants).

⁷ Sectoral reforms would focus on electricity, water and waste management; structural reforms centred on fighting corruption and strengthening governance and accountability, including in public finance and investment management. By contrast, donors at the Paris I (2001) and II (2002) conferences pledged only budget support. At the Paris III conference (2007), they additionally introduced conditional loans for projects. Eventually, some of these loans were cancelled because Lebanon failed to satisfy the conditions. Crisis Group telephone interview, French economic expert, April 2020. See also, "CEDRE – Joint Statement", op. cit. A European diplomat said, "CEDRE was created in opposition to Paris I and II, when donors provided budgetary support – untraceable by definition – following external shocks. We were in a different context then, a post-[civil] war period with reconstruction needs". Crisis Group interview, February 2020.

of last resort. To implement its recommendations would have been much less painful for Lebanon than implementing an agreement with the IMF will be.⁸

CEDRE donors' insistence on conditionality derived primarily from economic considerations and the realisation they could no longer avert their eyes from a situation they had been ignoring. They saw that bilateral and multilateral assistance disbursed in the framework of earlier such exercises – Paris I (2001) and Paris II (2002) – had failed to generate economic development, concluding that anything beyond humanitarian aid would be a lost investment.⁹ At the time, Lebanon also had become a lesser priority – compared with crises elsewhere – for its traditional donors. Donors appeared to consider their approach to Lebanon increasingly self-defeating: in order to prop up leaders deemed “Western-aligned”, they had been keeping the money flowing despite the country's failure to move forward on its reform commitments. A French-Lebanese economic expert said:

Traditional political calculations have somehow caught up with economic considerations. Donors like France, some of which faced budgetary constraints, simply had grown tired of the Lebanese political elite's way of doing things, which blocked all progress, while their relationship with Lebanon, which had always been based on personal ties, had become less solid than in the 1990s and 2000s. Moreover, Lebanon was no longer their first priority compared to other crises, such as Syria, Libya and the Sahel.¹⁰

If Western governments viewed CEDRE as the better way to help stop Lebanon's economy from imploding, Lebanese civil society organisations saw it quite differently. They denounced CEDRE as a politically driven process aimed at giving further legitimacy to the political class responsible for the country's fiscal and economic mismanagement. A Lebanese NGO representative said:

We lost two years with CEDRE. It was obvious that the traditional political class would not carry out any reforms. With CEDRE, donors continued to pretend that the problem in Lebanon was only economic and budgetary. You had to be naïve, or no one had an interest in dropping their masks. Everyone participated in the charade.¹¹

Most of Lebanese civil society actors additionally viewed CEDRE as unacceptable interference in Lebanon's internal affairs in support of Prime Minister Saad Hariri's then-outgoing government, given the event's timing just ahead of the May 2018 legislative elections. A Lebanese economic expert said:

CEDRE took place just one month before the elections. This was clearly a political decision. This was flagrant partisanship with the political class: CEDRE was a great gift to the outgoing government's electoral campaign, which thus found itself cleared of responsibility for the terrible economic and financial situation. It is one

⁸ Crisis Group telephone interview, European diplomat, June 2020.

⁹ Crisis Group telephone interviews, February-March 2020.

¹⁰ Crisis Group telephone interview, March 2020.

¹¹ Crisis Group interview, Beirut, March 2020.

thing for donors to provide ineffective aid, but quite another to get in the way of building a more democratic society.¹²

This critique echoes the analysis of some European diplomats and other important donors, who considered it a mistake to put the outgoing government in charge of the CEDRE process and argued that the conference should have taken place after the elections. A European diplomat said:

For the Europeans, Hariri was CEDRE's entry point, but that strategy failed. CEDRE was a project to support Hariri after his kidnapping in Saudi Arabia, to give him back legitimacy. It was a French-driven process that nobody dared to oppose. It would have been better if the conference had taken place after the elections, because this [ie, holding it beforehand] obscured CEDRE's relevance for the Lebanese political class and civil society [namely that, for the first time, donors had expressly made all aid conditional on reforms].¹³

CEDRE's timing was inauspicious also from a pragmatic point of view. After the 6 May 2018 parliamentary elections, government formation took nearly nine months. The national unity government led by Saad Hariri that was confirmed on 31 January 2019 was riddled with divisions and unable to make sufficient headway on the reform agenda. By 31 October, when Hariri resigned under pressure from nationwide street protests, donors had released none of the funds pledged at CEDRE.

The new government of Prime Minister Hassan Diab promised to do better. Diab approved a reform plan on 30 April that included deficit reduction through expenditure caps and new fiscal policies, debt restructuring, banking and financial sector reform, and steps promoting economic growth.¹⁴ It billed the plan as a "starting point" to secure external funding.¹⁵ On 1 May, it officially asked the IMF for \$10 billion in aid.¹⁶ Two weeks later, Diab organised the CEDRE follow-up committee's first meeting, noting afterward, in a speech marking his hundredth day in office, that donor country ambassadors attending it "felt our seriousness". In the speech, Diab said Lebanon was "on the right path toward operationalising the CEDRE Conference decisions".¹⁷ Over the next two months, he repeatedly stressed reform efforts he said the government was making.¹⁸

¹² Crisis Group telephone interview, April 2020.

¹³ Crisis Group interview, Beirut, March 2020. On 2 November 2017, Hariri was summoned to Saudi Arabia, where he was reportedly forced to read a resignation speech, which was televised on 4 November. "Exclusive: How Saudi Arabia turned on Lebanon's Hariri", Reuters, 11 November 2017.

¹⁴ "The Lebanese Government's Financial Recovery Plan", 30 April 2020.

¹⁵ "Lebanon government approves financial economic plan", Al Arabiya, 30 April 2020.

¹⁶ See "Lebanon's economic rescue plan 'good starting point': IMF spokesperson", Al Arabiya, 21 May 2020.

¹⁷ "PM Speech Marking 100 Days since Government Confidence Vote", Prime Minister's Office, 21 May 2020 (Arabic).

¹⁸ During French Foreign Minister Jean-Yves Le Drian's visit to Lebanon from 23-24 July, for example, Diab declared that his government had accomplished numerous reforms, including establishing an inter-ministerial commission to implement CEDRE, completing an audit of the Banque du Liban and installing X-ray screening at border crossings. "Diab reçoit Le Drian : 'Je suis confiant que la France ne lâchera pas le Liban aujourd'hui'", *L'Orient-Le Jour*, 23 July 2020.

Diab may have been betting that reactivating CEDRE would help Lebanon reap quick benefits from the government's rescue plan, as he suggested, while continuing to negotiate with the IMF.¹⁹ But his reform plan encountered ever stronger backlash, including from politicians supporting the government, and negotiations with the IMF stalled.²⁰ In response, Lebanon's principal donors insisted that they would still need to see reforms before agreeing to make funds available for other than humanitarian purposes.²¹ Putting a positive spin on events, they cited the follow-up committee meeting as progress, saying it had produced a more specific list of reforms as well as a calendar for making them; but they also warned that "time [had] come for the government to take political decisions that will have concrete results".²² A European diplomat listed the priorities:

The government needs to legislate and implement a national anti-corruption strategy. It has been slow to adopt or even put on the agenda other draft legislation, such as the laws on public procurement, the independence of the judiciary, illicit enrichment and the recovery of diverted assets. The government could also initiate Lebanon's accession process to the 1997 OECD convention. Instead, it continues to send bad signals, such as blocking appointments to the High Council of Justice. The same goes for the electricity sector: the government has taken no positive steps, quite the contrary.²³

International donors and Lebanese civil society organisations consider reform of the electricity sector one of the country's top priorities. The financial and economic crisis cannot be solved without this step – the state-owned power utility's accumulated deficit equals 43 per cent of Lebanon's public debt – and moves to fix the electricity sector will be a critical test of the government's will to launch reforms.²⁴

¹⁹ See "PM Speech Marking 100 Days since Government Confidence Vote", op. cit.

²⁰ A dispute between the government, the central bank and the private banking sector over who should bear the brunt of the losses in the financial sector – banks, depositors, taxpayers – stalled negotiations with the IMF and eventually led to their breakdown. "Why are Lebanon's negotiations with the IMF deadlocked?", *Commerce du Levant*, 11 July 2020.

²¹ Crisis Group telephone interviews, European diplomats, May-July 2020. During his July visit to Lebanon, the French foreign minister said the government had not yet undertaken the expected reforms, including under CEDRE. "Conférence de presse de M. Le Drian à Beyrouth", France Diplomatie, 23 July 2020. After Le Drian had left, Diab declared that his visit "brought nothing new, and the French minister lacks information regarding the government's path of reform in Lebanon". Quoted in "Diab speaks of international decision not to support Lebanon", *The Daily Star*, 28 July 2020.

²² Crisis Group telephone interview, European diplomat, June 2020. In the meeting, which included the CEDRE participants, the government introduced a roadmap comprising: next steps for implementing the follow-up mechanism, including setting up a dedicated, publicly accessible monitoring website (announced for mid-June) and an inter-ministerial committee positioned within the prime minister's office (supported by the United Nations Development Programme); a start to prioritising the Capital Investment Plan's infrastructure projects (selecting 138 projects of an initial 285); and updating the implementation of sectoral reforms, including anti-corruption, the judicial sector, public procurement and fiscal governance (with the completion of the anti-corruption strategy and the creation of a national anti-corruption agency).

²³ Crisis Group telephone interview, European diplomat, June 2020.

²⁴ Problems in the electricity sector remain unresolved. The country suffers from chronic power shortages, which force people to use costly private generators. Power generation relies on imported,

The state of the electricity sector is emblematic of the extent to which patronage and vested interests have blocked reform, preventing the country from having functioning public services while increasing the budget deficit.²⁵ Donors and Lebanese civil society actors say the only way to move forward would be to establish solid governance and transparency mechanisms and adopt a strategy based on cost efficiency and environmental-cost planning.²⁶ Most important will be creating an independent regulatory authority removed from political decision-making and partisan agendas.²⁷ Other sectors struggle with similar problems and require similar solutions.²⁸

Before any substantial reform, however, must come a rescue of the country's financial system, along with stabilisation of the currency and state budget. To the Europeans, the top priority is therefore for the Lebanese government to reach an agreement with the IMF.²⁹ Such a deal and attendant reforms could then open the door to additional development aid and project investment, including CEDRE funds currently locked up.³⁰

B. *The Macron Initiative*

The 4 August port explosion precipitated the Diab government's resignation, following angry protests. It also generated fresh international efforts to support Lebanon, first by providing emergency humanitarian aid and then by pushing anew to put the

expensive and pollutant-heavy fuel and diesel oil. Losses, both technical and non-technical (such as illegal connections or unpaid bills), are estimated at 36-40 per cent of production. Jessica Obeid, "Lebanon's Power Sector: Making Reforms Work", Lebanese Centre for Policy Studies, June 2020; and "Why Lebanon's electricity crisis is so hard to fix", *Arab News*, 15 June 2020.

²⁵ Crisis Group interviews, European diplomats, Beirut and by telephone, March-June 2020.

²⁶ They criticise the government not only for continuing to issue contracts without public tenders and failing to address the lack of transparency in procurement, but also for including in its plan the construction of a third new power plant in Selaata, in the north, which they claim would be for the political benefit of the leader of the Free Patriotic Movement Jibril Bassil, who is also the son-in-law of the party-founder, Lebanese President Michel Aoun, despite studies showing its cost inefficiency and failure to meet technical and environmental criteria. Crisis Group telephone interviews, civil society representative and European diplomats, April-July 2020. See also "Why Lebanon's electricity crisis is so hard to fix", *op. cit.*

²⁷ Jessica Obeid, an expert on the Lebanese energy sector, said, "In 2002, Law 462 established an independent regulatory authority with full mandates, including the authority to issue and cancel licenses and restructure the power utility. This law was never implemented. Until today, successive governments have constantly tried to amend the law to dilute the regulatory authority's role in favour of the energy minister by making it more of an advisory body". Crisis Group telephone interview, July 2020. See also Jessica Obeid, "Lebanon: The 3-Decade Impossible Power Sector Reforms", Istituto per gli Studi di Politica Internazionale, March 2020.

²⁸ Crisis Group telephone interviews, civil society representatives and European diplomats, April-July 2020. A European diplomat said, "The sticking points and needed reforms are the same, regardless of the sector. There may be good laws on the books, but they are not being implemented. Political leaders keep trying to empty the laws of substance". Crisis Group telephone interview, July 2020.

²⁹ A European diplomat said, "As long as there is no agreement with the IMF, there will not be a framework for financial restructuring, and that means that no investment will be sustainable". Crisis Group telephone interview, June 2020.

³⁰ Crisis Group interviews, European diplomats, Beirut, March 2020.

country on the reform track.³¹ The French president, Emmanuel Macron, staked his reputation on success, visiting Beirut in the immediate aftermath of the blast and launching an initiative to help the Lebanese through emergency assistance. He indicated that he was prepared to enter dialogue with the full range of Lebanon's political forces, as the crisis implicated all of them. And he reiterated that donor pledges under CEDRE remained in force but that the time had come for the Lebanese authorities to make substantial reforms.³²

The French government detailed the way forward in a roadmap document at the end of August, which it transmitted to Lebanese political leaders just prior to Macron's second visit to Beirut, on 1 September. The plan's first step was the requirement that the newly appointed prime minister, Mustapha Adib, form an "independent" government, backed by the political parties and comprising "competent personalities", within fifteen days.³³

Macron underlined that his initiative would not be a "blank check; on the contrary", and he specified the reforms the new government would have to undertake within a specified timeline. These reforms, which partly overlapped with those demanded by the IMF, included resumption of the stalled negotiations with the IMF; a capital control law; a complete audit of the accounts of Lebanon's central bank, the Banque du Liban; reform of the electricity sector, with the establishment of a National Electricity Regulatory Authority based on Law 462 (2002) and cancellation of the Selaata power plant project; judicial reform through passage of an independence of the judiciary law; implementation of an anti-corruption strategy; and adoption of the draft Public Procurement Law.³⁴ Macron also promised to host a future donor conference if he saw initial progress on these reforms.³⁵ He agreed to hold meetings with Lebanese political leaders to address substantial issues related to Lebanon's political system.³⁶ And he warned that this initiative would be "the last chance for this system".³⁷

Officials of other European governments welcomed the French initiative, viewing it as consistent with reforms they had been demanding for years.³⁸ If they sounded a note of disagreement, it was merely about Macron's unilateral approach.³⁹ Yet they also said they had not seen the slightest evidence of progress or inclination on Leba-

³¹ On 9 August, the French president and UN Secretary-General co-hosted an international conference on "support to Beirut and the Lebanese people" to address immediate needs following the explosion. See "International Conference on Assistance and Support to Beirut and the Lebanese People", Elysée, 9 August 2020. See also "Lebanon is on track to become a failed state", Al Jazeera, 7 August 2020.

³² "Conférence de presse du Président de la république depuis Beyrouth", Elysée, 6 August 2020.

³³ "French President Macron says Lebanon has promised to form cabinet within two weeks", France 24, 1 September 2020.

³⁴ Crisis Group telephone interviews, European diplomats, Beirut, September 2020.

³⁵ "Conférence de presse du Président de la république à la Résidence des Pins", Elysée, 1 September 2020.

³⁶ "Emmanuel Macron au Liban : éviter les dangers de l'aventure solitaire", *Le Monde*, 2 September 2020.

³⁷ Quoted in "Macron warns Lebanese politicians of 'last chance'", *Arab News*, 2 September 2020.

³⁸ Crisis Group telephone interviews, September 2020.

³⁹ Crisis Group telephone interviews, European diplomats, September 2020. Others said, to the contrary, that the emergency required a unilateral approach and that only the French were in a position to take the lead. Crisis Group telephone interviews, European diplomats, September 2020.

nese leaders' part to contemplate concrete reforms.⁴⁰ In their view, these leaders are either still underestimating the challenges at stake or betting that European governments will relax their demands because they do not want to see another failed state in the Mediterranean. A European diplomat said:

Because of the blank check attitude before CEDRE, our aid policy may have a credibility problem. But international donors have reversed that approach, as we have illustrated by not disbursing any funds under CEDRE. Yet it's not clear whether political leaders in Lebanon have understood this, and it may be that they will continue to play the game of which [of the donors] will crack first. If so, they are making a big mistake: European consensus is solid and there is no one else ready to invest, even among traditional donors such as the Gulf states.⁴¹

Some civil society activists blame Macron for repeating the mistakes they accuse him of making at CEDRE. In betting on the traditional political leaders to carry out the necessary reforms, they say, France once again is encouraging a deal with the same old system that has dragged Lebanon into the crisis, giving that system a political reprieve and boosting what remains of its legitimacy.⁴² An activist with a pro-reform NGO explained:

The French roadmap includes necessary reforms that we agree with. But it focuses only on technical issues and ignores the real political issues that explain how we got there. Without addressing the political side, we sustain a dysfunctional system that will be unable to implement an economic recovery program the way it should. We can't put the cart before the horse.⁴³

C. *Regional Interference*

The stalemate has deepened due to the difficulty of keeping all the donors at the table. While tensions between donors and Lebanese authorities are not new, the U.S. and its Gulf Arab partners became even more reluctant with the appointment of the Diab government, which they viewed as heavily influenced by Hizbollah and its allies.⁴⁴

⁴⁰ A European diplomat said, "When the Diab government resigned, we turned to the status quo ante. Parliament could have agreed to a deal with the IMF, but it didn't. Political leaders, and I mean all of them, don't want reforms or change". Crisis Group telephone interview, 15 September 2020.

⁴¹ Crisis Group telephone interview, 17 September 2020.

⁴² Crisis Group telephone interviews, September 2020. See also "Une véritable transition suppose de s'émanciper de la Constitution", *L'Orient-Le Jour*, 12 September 2020.

⁴³ Crisis Group telephone interview, 25 September 2020.

⁴⁴ "Wary of Iran, Gulf Arab states seen shrugging off new Lebanese government", Reuters, 27 January 2020. U.S. Secretary of State Mike Pompeo said, "We are fully prepared to support a government that conducts real reforms and operates in a way that is not beholden to Hizballah. When that comes, when the government demonstrates – whoever that is – demonstrates their willingness and capacity to do that, I think not only the United States but the whole world will move in to assist the Lebanese Government, get its economy back on its feet". "Secretary on the Release of the 2019 Country Reports on Terrorism", U.S. Embassy in Lebanon, 24 June 2020. The U.S. remains Lebanon's principal donor, providing \$751.3 million in 2019 alone: \$345 million in humanitarian aid, \$117.5 million for economic development and \$221 million in military assistance. Crisis Group telephone interview, U.S. diplomat, March 2020.

The U.S. has repeatedly reaffirmed the need for reforms but, unlike European governments, sees Hezbollah as the main obstacle.⁴⁵ A European diplomat said at the time of the Diab government, “U.S. maximum pressure on Iran complicates the situation here in Lebanon. Washington and its Gulf partners are overly cautious in engaging with the Diab government. This is not our position. We are ready to engage constructively”. But, he added, “for now, despite our differences, the U.S. is not looking to undermine our efforts; they seem to be taking a wait-and-see approach instead”.⁴⁶

This attitude seemed to harden at the beginning of September, while the French initiative was starting to move forward and Macron obtained an agreement from all political leaders, including Hezbollah, on his proposed roadmap.⁴⁷ Only a few days later, the U.S. imposed sanctions for the first time against senior political figures allied with Hezbollah; a second instalment of sanctions announced a week later targeted companies allegedly linked to the party, along with a member of its executive committee.⁴⁸ Moreover, while affirming that the U.S. supports the French reform initiative in general, U.S. officials said Washington disagrees with the expressly stated French approach to include Hezbollah at the negotiating table along with all other Lebanese political parties. U.S. officials, along with their Saudi counterparts, ramped up their anti-Hezbollah rhetoric.⁴⁹

⁴⁵ U.S. Assistant Secretary of State for Near East Affairs David Schenker accused Hezbollah of attempting to “acquire the Lebanese financial system. ... [The U.S.] repeats the call for the Lebanese government to undertake serious reforms and fight corruption ... but [it] has not made any serious attempt yet to do so. ... We know that Hezbollah will not abide by any of these steps, but we still hope that the government will fulfil its obligations”. Quoted in “More US sanctions will target Hezbollah: Schenker”, *Daily Star*, 23 June 2020. According to Hezbollah broadcast media, its Secretary General Hassan Nasrallah advised Washington to abandon its policy to besiege Lebanon, warning that such behavior won’t weaken Hezbollah but will strengthen it. Nasrallah also said Lebanon must not just rely on the outcome of the talks with the IMF, stressing the importance of looking for other choices. Quoted in “Sayyed Nasrallah announces new front: reviving agricultural, industrial sectors in Lebanon”, *Al-Manar*, 10 July 2020.

⁴⁶ Crisis Group telephone interview, June 2020. In February 2020, French Economy Minister Bruno Le Maire declared that support for Lebanon’s economic recovery should be delinked from U.S.-Iran arm wrestling. “Il ne faut pas mélanger le rétablissement économique du Liban et la question de l’Iran, déclare Le Maire”, *L’Orient-Le Jour*, 23 February 2020.

⁴⁷ “Conférence de presse du Président de la république à la Résidence des Pins”, op. cit.

⁴⁸ “Lebanese Hezbollah and allied parties condemn U.S. sanctions on former ministers”, Reuters, 15 September 2020; “U.S. blacklists Hezbollah official, Lebanon-based companies”, Reuters, 17 September 2020.

⁴⁹ “Pompeo says Hezbollah weapons risk torpedoing French efforts in Lebanon”, Reuters, 15 September 2020. In an op-ed published on the occasion of his visit to Paris, U.S. Secretary of State Mike Pompeo wrote that “Hezbollah has been the predominant political actor in that country for roughly three decades, and today in Beirut, corruption abounds, a broken financial and political system barely functions, and young Lebanese chant ‘Iran, get out!’ in the streets”. “France should stand with freedom, not Tehran”, *Le Figaro*, 14 September 2020. Saudi King Salman bin Abdulaziz blamed the “humanitarian catastrophe” in Lebanon on Hezbollah’s control of decision-making “by force of arms”. “Hezbollah has destroyed Lebanon, must disarm: Saudi Arabia’s King Salman”, *Al Arabiya*, 23 September 2020.

Many European officials view this external pressure upon Hizbollah as counter-productive.⁵⁰ The sanctions, announced on 9 September, came as the clock ticked on Macron's fifteen-day deadline for Prime Minister-designate Adib to form a government. The sanctions, together with more aggressive U.S. rhetoric echoed by its allies such as Saudi Arabia and former Prime Minister Hariri's growing influence over the formation of Adib's supposedly independent cabinet, led to a hardening of Hizbollah's position and contributed to the failure of the negotiations and ultimately to Adib's resignation.⁵¹ Some European diplomats interpreted Hizbollah's tactics as designed to signal to the Europeans that it would end its cooperation in the political process altogether if the U.S. persisted in placing sanctions on the party.⁵²

The stalemate exposes a critical limit of Europe's ability to use its economic heft as leverage. The EU and some of its member states may have a supply of economic incentives to nudge the Lebanese elite into agreeing to reforms, but they have no control over the heavy sticks that the U.S. and some of its allies are wielding against Hizbollah and those who align with it. Insofar as Hizbollah and its allies are firmly entrenched in Lebanese political institutions, the resulting polarisation is likely to block and derail the reform process. A European diplomat said:

Europe has no leverage over U.S. sanctions policy, and this discredits Europe's posture in Lebanon. But, in the meantime, Hizbollah knows that Europeans, and mainly France, are the only ones to talk to, the only partner for an exit from the crisis. Some in Hizbollah may have the idea that the political stakes are bigger, meaning that it will depend on what will happen between the U.S. and Iran after the U.S. elections. What we are saying from the European side is: let's try to dissociate the current crisis in Lebanon from the regional context, because the crisis is hitting the population very hard, and it affects the entire Lebanese political class.⁵³

On 22 October, Hariri was charged with forming a cabinet under his leadership. His reappointment as prime minister did little to allay concerns that he would follow in the footsteps of his immediate predecessor: he received even fewer votes in parliament than Adib and faces the same political constraints.

⁵⁰ A European diplomat said, "Europe has a different perspective than the U.S. in certain ways. Europe is a facilitating partner, trying to enable the political leaders to find a consensus. We want to focus on the domestic agenda. Our analysis is that we should try to keep all the regional issues outside of the country. The only way to avoid chaos is for Lebanon to reach an agreement with the IMF and get governance reforms right. It would be naïve to ignore the U.S. rhetoric, its political pressure and sanctions against Hizbollah. But at the end of the day, we have to work to shield Lebanon from the international rivalry and keep its political leaders focused on domestic issues. The U.S. cannot do that. This is our added value". Crisis Group telephone interview, 21 September 2020.

⁵¹ "Pompeo says Hezbollah weapons risk torpedoing French efforts in Lebanon" and "Hezbollah has destroyed Lebanon, must disarm: Saudi Arabia's King Salman", both op. cit. As Hizbollah and Amal were demanding to choose the finance minister, Hariri appeared to oppose them, announcing that he would "ingest the poison" and "help Adib name an independent Shiite finance minister". "Hariri: I've decided to help Adib name an independent Shiite finance minister", Naharnet, 22 September 2020.

⁵² Crisis Group telephone interviews, September 2020.

⁵³ Crisis Group telephone interview, 16 September 2020.

III. A Dilemma for European Aid Policy

No matter who leads the next Lebanese government, Lebanon's donors face a difficult dilemma. Should they throw the country's elites a lifeline – beyond emergency humanitarian relief – by saving them from hyper-inflation and state bankruptcy, lest Lebanon become one more failed state in an already floundering region? Or should they try to induce fundamental reforms by holding firm on their conditions for providing development assistance, but risk failure in view of the elites' resistance to such changes, and as a result potentially see the country slide into the abyss?

A. *A Governance Gap*

Despite its upper middle-income status, Lebanon remains largely dependent on international Official Development Assistance (ODA) for investments in basic services and infrastructure.⁵⁴ The bulk of the state budget is allocated to public-sector salaries, while the country's private sector is dominated by a financial sector directed toward rent seeking – in particular, investment in high-yielding government debt – rather than productive investment. Non-ODA foreign income, such as remittances and foreign direct investment, has been directed mostly toward private consumption and real estate development.⁵⁵

Still, Lebanon receives less ODA than other countries in its income range, or any other Middle East country, for economic infrastructure such as transport and energy, or for productive sectors such as agriculture and industry.⁵⁶ An official in an international economic cooperation organisation suggested that the low amount is likely the result of “donor mistrust and even more the government's inability to agree on common-good projects”.⁵⁷ Donors often fail to spend their budget for Lebanon because of its low absorptive capacity. This problem, he noted, comes not from technical capacity (as it does in many other ODA-recipient countries), which is comparatively high in Lebanon, but primarily from political blockages and pervasive corruption.⁵⁸

⁵⁴ See “Transition Finance Country Study Lebanon – Global Public Goods and the Response to Adverse Shocks: The Case of Lebanon”, Organisation for Economic Co-operation and Development (OECD), 11 June 2019; and the OECD's “Creditor Reporting System”. Relative to its upper middle-income status, Lebanon receives a large share of ODA, even if this amount represented only 10 per cent of total external income between 2012 and 2016, far behind the share of remittances (approximately two thirds) and foreign direct investment. Lebanon's ODA is intended mainly to help it respond to the Syrian refugee crisis; it increased from \$277 million in 2011 to \$977 million in 2018. It consists of short-term humanitarian assistance (\$470 million in 2018) and funding for mid-term projects in the education, health and water sectors serving both Syrian refugee and Lebanese host communities (\$364 million in 2018).

⁵⁵ OECD, “Transition Finance Country Study Lebanon”, op. cit.

⁵⁶ Ibid.

⁵⁷ Crisis Group telephone interview, April 2020.

⁵⁸ He said, “In Lebanon, everything is blocked. The ODA absorption capacity is quite low while the technical capacities are there (not like in some African countries); the problem is corruption. Without this, Lebanon could receive more ODA than it does today”. Crisis Group telephone interview, April 2020. According to Transparency International, Lebanon ranks 137th of 180 countries on the index that measures how corrupt a country's public sector is perceived to be by experts and business executives. “Corruption Perceptions Index”, Transparency International, 2019.

European development officials habitually complain about Lebanese elites' lack of interest in fostering development projects.⁵⁹ As long as the government fails to hold officials accountable for their use of public finance and institutions, the Europeans say, these elites will keep placing personal interest ahead of the public good. A Lebanese expert explained:

The Lebanese political system is based on capturing public resources – where public money is available for personal enrichment and to feed patronage networks. Lebanese elites spend their time negotiating how to share the cake, to the detriment of the projects' technical or financial relevance. In all areas, public policy is guided by only one factor: the potential contracts and commissions they will be able to acquire.⁶⁰

Lebanese government officials with decision-making power over a project often disagree over how to share the dividends. As a result, donors may have to delay or cancel projects financed through grants or concessional loans, even if they have already funded assessment studies. A European Development Agency official offered the example of a project to build new public service infrastructure, entirely based on a European grant to the Lebanese government; ultimately, the donor had to transfer the project to local NGOs, as the relevant authorities could not agree among themselves on where the project should be located and who should supervise it.⁶¹ Likewise, the ability of each person involved in decision-making to block a project may also cause interruptions midway or just before it comes online.

There are other reasons as well why projects may be postponed or fail to become operational once completed, for example if the government neglects to make a budgetary allocation for maintenance. Several European-funded projects have suffered this fate.⁶² Procedural obstacles and lack of administrative and management capacity also can cause interminable delays.⁶³

Lebanese NGO representatives and civil society activists characterise the problem differently. They blame the international community for basing its aid policy on a short-term vision of stability at the expense of improving governance. They say the

⁵⁹ A European Development Agency official said, "Lebanon is a typical case of a country whose political elite is not concerned with the country's sustainable development. You don't develop a country from the outside. The aid should support an indigenous development dynamic, but this is absent in Lebanon". Crisis Group telephone interview, June 2020.

⁶⁰ Crisis Group telephone interview, April 2020.

⁶¹ Crisis Group telephone interview, January 2020. The official added, "This project was based on a grant. But loan-based projects can also be cancelled or delayed. In that case, the price of the loan may rise with the delays. But the authorities do not care".

⁶² For example, solid waste and waste water management projects – considered highly lucrative sectors – have not always become operational, despite funds having been disbursed and even, in some cases, the project having been completed. Some European agencies today refuse to operate in these sectors because of such problems. Crisis Group telephone interviews, European diplomats and development agency officials, March-June 2020.

⁶³ A European development official said, "There are a lot of procedural problems in Lebanon. Parliament authorises negotiating a project; the Council of Ministers validates the project; then parliament must ratify the project again. The problem is that these projects are systematically at the bottom of parliament's priorities, due to the successive crises the country is going through". Crisis Group interview, Beirut, March 2020.

governance components in externally funded projects tend to be diluted, if not totally absent, when they should be an essential part. Pointing to the protests that broke out in October 2019, they contend that the only way out of the crisis would be to build a state apparatus that replaces the patronage networks that have hijacked governing institutions.⁶⁴ An NGO representative said:

The current crisis in Lebanon has two drivers: political and economic. The Europeans, like other Western donors, believed that the only issue for stability in Lebanon was Hizbollah and its weapons, and thus they misjudged the magnitude of the disaster that was coming. They were convinced that a badly governed Lebanon is an acceptable price for a stable Lebanon. It is time they understand that governance and stability are inextricably linked.⁶⁵

Lebanese critics blame Europe for perpetuating a failed system by not conditioning aid on improvements in governance.⁶⁶ An NGO representative said, “Aid has helped our political class stay in power; it has not contributed to developing the country. As long as European money goes to the political class, we don’t want it”.⁶⁷

Finally, NGOs and civil society organisations complain about the lack of access to information regarding externally funded projects, despite the 2017 Access to Information Law, complicating their oversight role. European donors, the EU in particular, come in for similar criticism. NGO representatives say they do not have systematic access to European monitoring and evaluation of its bilateral projects.⁶⁸

Despite some criticism of donors’ interference in Lebanese internal affairs through CEDRE and the latest French initiative, NGO representatives and civil society activists say they welcome the fact that international donors have signalled their willingness to change the rules of the game by conditioning part of their aid on sectoral and structural reforms. They say the new rules should apply to all donor funding (apart from humanitarian aid), beyond projects endorsed by CEDRE. They further stress that donors should use the financial and economic crisis as an opportunity to push for such reforms. They want donors to be uncompromising regarding implementation, not to lessen their demands. A French-Lebanese economic expert said, “We cannot ask the Europeans to carry out these reforms for the Lebanese, but we can ask them to take steps to ensure their money is well spent”.⁶⁹

European officials say they agree with the Lebanese NGOs’ demand for “no aid – apart from humanitarian aid – without reforms”, and that this position, as CEDRE

⁶⁴ Crisis Group interview, Lebanese governance NGO representative, Beirut, March 2020.

⁶⁵ Crisis Group telephone interview, May 2020.

⁶⁶ Crisis Group interviews, March–June 2020. A Lebanese NGO representative said, “The international community cultivated politically the idea of a Lebanese miracle. It was blindness. Lebanese politicians are experts when it comes to fooling donors”. Crisis Group interview, Beirut, March 2020.

⁶⁷ Crisis Group telephone interview, April 2020.

⁶⁸ Crisis Group interviews, Lebanese NGO representatives and civil society activists, March–April 2020. A Lebanese NGO representative said, “The problem in Lebanon is that we don’t have access to information. So, we can’t go to court. Even if we had a very good law on access to information, the problem is that there is no law enforcement. We always come back to the central problem of the need for an independent judiciary. Without it, nothing will change, no matter how many laws we pass”. Crisis Group interview, Beirut, March 2020.

⁶⁹ Crisis Group telephone interview, March 2020.

and the French initiative illustrate, is the pillar of their policy. Beyond not wanting to throw money into a bottomless pit, they say the protesters' growing criticisms of external aid policy have strengthened their resolve in this respect.⁷⁰ This new determination appears to have survived the COVID-19 crisis, with its disastrous impact on the economy, and the 4 August blast, events to which European donors have responded exclusively through humanitarian aid, which has been substantial.⁷¹

B. *Conditionality vs. Stability*

Yet European donors acknowledge that they face an unescapable reality: if Lebanese elites fail to deliver, there does not appear to be a viable alternative. To confront the predicament of needing first to see fundamental change, lest they throw good money after bad, while the economy is in a free fall threatening the livelihoods of millions (including Syrian refugees), European donors are trying to stabilise the country through a range of short- and long-term aid packages. They differentiate humanitarian aid, which is non-conditional, from the promise of more substantial, conditional long-term support aimed at improving infrastructure, economic viability and state functioning. A European diplomat said:

There is no plan B. The alternative to successful economic recovery is only pure humanitarian aid, which requires no conditions, and we will adjust our support to the circumstances on the ground. This is clearly a scenario that we would like to avoid. But any substantial investment that goes beyond humanitarian aid will be tied to conditions.⁷²

At this stage, European donors are continuing to fund infrastructural projects for basic services already under way.⁷³ Although European funding for new projects is

⁷⁰ A European diplomat said, "Even if we wanted to engage with Lebanon without reforms, which we don't, we wouldn't be able to: pressure from civil society is strong and they are watching us". Crisis Group interview, Beirut, February 2020.

⁷¹ See "Lebanon: EU Delivers Additional Emergency Assistance Following the Explosion in Beirut", press release, European Commission, 31 August 2020. A European diplomat said, "The COVID-19 crisis will not make us more flexible regarding sectoral and structural reforms. It is almost the other way around. The COVID-19 crisis has severely affected European economies. Some countries will become even more careful with their money. There will be no free gifts. We have always said to the Lebanese authorities, 'Be careful, because we don't know what the future will bring'". Crisis Group telephone interview, June 2020.

⁷² Crisis Group telephone interview, September 2020.

⁷³ Crisis Group telephone interviews, April, June and July 2020. Some donors are also giving more non-financial technical assistance, consisting mainly of information and expertise sharing and skills training, rather than investing in new infrastructure, or have reoriented their programming toward Lebanese NGOs. A European Development Agency official said, "A lot of us decided to shift to technical assistance in order not to run into the constant obstacles of project implementation in Lebanon. But if everybody does that, how do you address the needs?" Crisis Group interview, Beirut, March 2020. Such an approach also can delay the challenge of rebuilding a more accountable and more sustainable state apparatus. A European Development Agency official stressed that directing funding to Lebanese NGOs is a short-term solution only: "Lebanon needs a functioning state above all. But for now, NGOs are more accountable and more efficient in implementing projects". Crisis Group telephone interview, May 2020.

on hold for now, some European diplomats intimate that their governments may not necessarily condition future aid upon reforms if, for example, it concerns low-scale basic-services projects.⁷⁴ They reject the notion that change will come only once the situation is at its worst, because refusing aid to basic services will compound economic hardship just when more than half the population is living below the poverty line. A European aid agency official said:

If international aid is cut, public services will collapse even more rapidly. The Lebanese political system will be exposed for what it is if we disengage. But such an approach would have a seriously negative impact on the population. In the current crisis, the state will fail to keep many public services afloat. For example, it won't be able to ensure sewage treatment and the water supply. This will create an environmental, humanitarian and health problem. So, what is the responsible approach for donors? We have decided to continue to keep our projects for basic services afloat for the coming months in order to prevent a catastrophe.⁷⁵

No European government wants Lebanon to become a failed state. What they want most is to maintain stability in what Europe considers its immediate neighbourhood – in line with EU neighbourhood policy – and to preserve its long-term partnership with Lebanon developed in numerous fields (education, military, economic).⁷⁶ Another major interest is to prevent a new wave of refugees coming to the continent. If the economic crisis in Lebanon continues, more and more people will feel pressure to emigrate, whether legally or otherwise, to escape mounting hardships. It is not clear that humanitarian aid will be enough to stop them.⁷⁷

Ultimately, if the Europeans wish to stay on the straight and narrow path of conditionality vis-à-vis a political system that has shown itself to be incapable of delivering reform, they may find themselves playing a high-stakes game that runs the risk of further destabilising the country.⁷⁸ A European diplomat said:

Europeans must walk a delicate path in Lebanon. On one side, how much can we expect from any government in Lebanon? This situation may lead us to a discussion about how far we can go regarding demands for reform. Then again, concrete reforms are needed for any sustainable way out of the crisis, and the population is clamouring for them. This is about our own credibility as well.⁷⁹

⁷⁴ Crisis Group telephone interviews, European diplomats, September 2020.

⁷⁵ Crisis Group telephone interview, May 2020.

⁷⁶ A European diplomat said, "To preserve our traditional link with the Christian communities and to preserve the Lebanese model of coexistence between communities is an additional motivation for us [Europeans]". Crisis Group telephone interview, September 2020.

⁷⁷ "Surge in deadly sea crossings from Lebanon to Cyprus as economic crisis pushes hundreds of thousands more children into poverty", Save the Children, 14 October 2020.

⁷⁸ Crisis Group telephone interviews, European diplomats, March-June 2020.

⁷⁹ Crisis Group telephone interview, July 2020.

IV. What Should Europe Do?

Even as the economic and financial crisis deepens, Lebanese political leaders have yet to endorse a strategy on how to move forward. Their internal disagreements over an IMF deal – European donors’ fundamental precondition for providing aid – will likely drag out, with new negotiations remaining on hold as long as no new government is formed.⁸⁰ In the face of this deadlock, Lebanon’s economic and social crisis could lead to widespread food insecurity and further deterioration of state capacity to provide basic services, such as health and education. This outcome is not in the interest of either the Lebanese or the Europeans.

The EU and European governments cannot force the Lebanese authorities to carry out the reforms needed to secure external funding. But they can expand their humanitarian support as long as current political blockages persist to prevent a more serious humanitarian crisis. They should continue their assistance for impoverished communities (including refugees) and support for infrastructure and basic services at a small and local scale. Donors should also explore expanding existing programs that seek to create jobs for Lebanese and refugees alike by improving local infrastructure and agricultural production in peripheral areas, as these places will likely be the first to experience food insecurity and the failure of already feeble state services and control.

In the meantime, and with a longer-term perspective, donors should continue to explore how they can further help Lebanon, through diplomatic tools and assistance policy, in finding a sustainable exit from the crisis once a deal with the IMF is in place. Even then, they will have to maintain substantial humanitarian aid for the foreseeable future, as economic consolidation will require time and poverty rates will remain high.

The EU and France, in particular, appear best placed to convince Lebanese political groups of the inevitability of change. They have the ability to talk to all sides and, perhaps most importantly, appear to prioritise rescuing Lebanon rather than serving larger strategic agendas. European donors should make clear that they do not support the U.S. “maximum pressure” campaign against Iran as it affects Lebanon. Instead, they should reiterate that they have no hidden agenda to promote or shunt aside a particular political side or party. Instead, they should stress that they see every party as crucial to finding a way out of the crisis and that all political actors will have to relinquish some of the patronage networks they have spun in state institutions. Furthermore, European donors should remind the Trump administration and its Gulf allies of the risk their approach to Lebanon entails for the country’s stability and ask that they refrain from obstructing European efforts.

European donors should stick to their line that they are looking to resume major non-humanitarian assistance only once the Lebanese authorities begin the process of genuine reforms after reaching an agreement with the IMF. These should aim at building an independent judiciary; strengthening accountability by implementing the anti-corruption law; adopting a law on transparency and its translation into concrete actions; and modernising the public procurement system.

⁸⁰ See fn 20 above. “Statement by IMF Managing Director Kristalina Georgieva on the International Conference on Support to Beirut and the Lebanese People”, IMF, 9 August 2020.

In addition, European donors should make clear to Lebanese leaders that they expect certain minimum standards of transparency and accountability in public institutions to govern their development aid. One of these standards could be, for example, transparency evaluations carried out by the EU itself or its international non-governmental partners.

The EU should also keep encouraging collective action at the member state level to ensure common objectives and coherence of projects, even if some member states, like France, at times favour a more unilateral approach. Any development project, currently under way or set to take place outside of CEDRE, should be assessed based not only on Lebanon's needs but also on review of past experience for pitfalls specific to the Lebanese context that could compromise its chances for success. Furthermore, European donors should specify and incrementally link reform steps, such as the establishment of proper legal and regulatory frameworks (like an independent regulatory authority for the electricity sector) and transparent procurement, recruitment and planning procedures, in the sectors they fund to a project's successive stages (conception, planning, disbursement and implementation), in order to clarify to Lebanese authorities what steps are required.

Alongside these measures, Europeans should improve their own transparency regarding the projects they fund, including through systematic public access to project monitoring and evaluation. Too, Europeans should be more direct about who is to blame in case a project is delayed or fails, as it would make the responsible persons or institutions accountable vis-à-vis the Lebanese population and help in identifying the obstacles.

Finally, with regard to civil society, Europeans should consider how they can better engage with its representatives in their development cooperation policy. They are civil society's biggest donors, but they could improve the quality and efficiency of their support, especially where political leaders are actively resisting carrying out reforms. By establishing greater transparency regarding their own project development and evaluation, Europeans can empower civil society to force greater accountability on the Lebanese government and thus become a more effective watchdog. Europeans could also explore ways to establish a more systematic consultative process with civil society for defining, implementing and evaluating their programs.

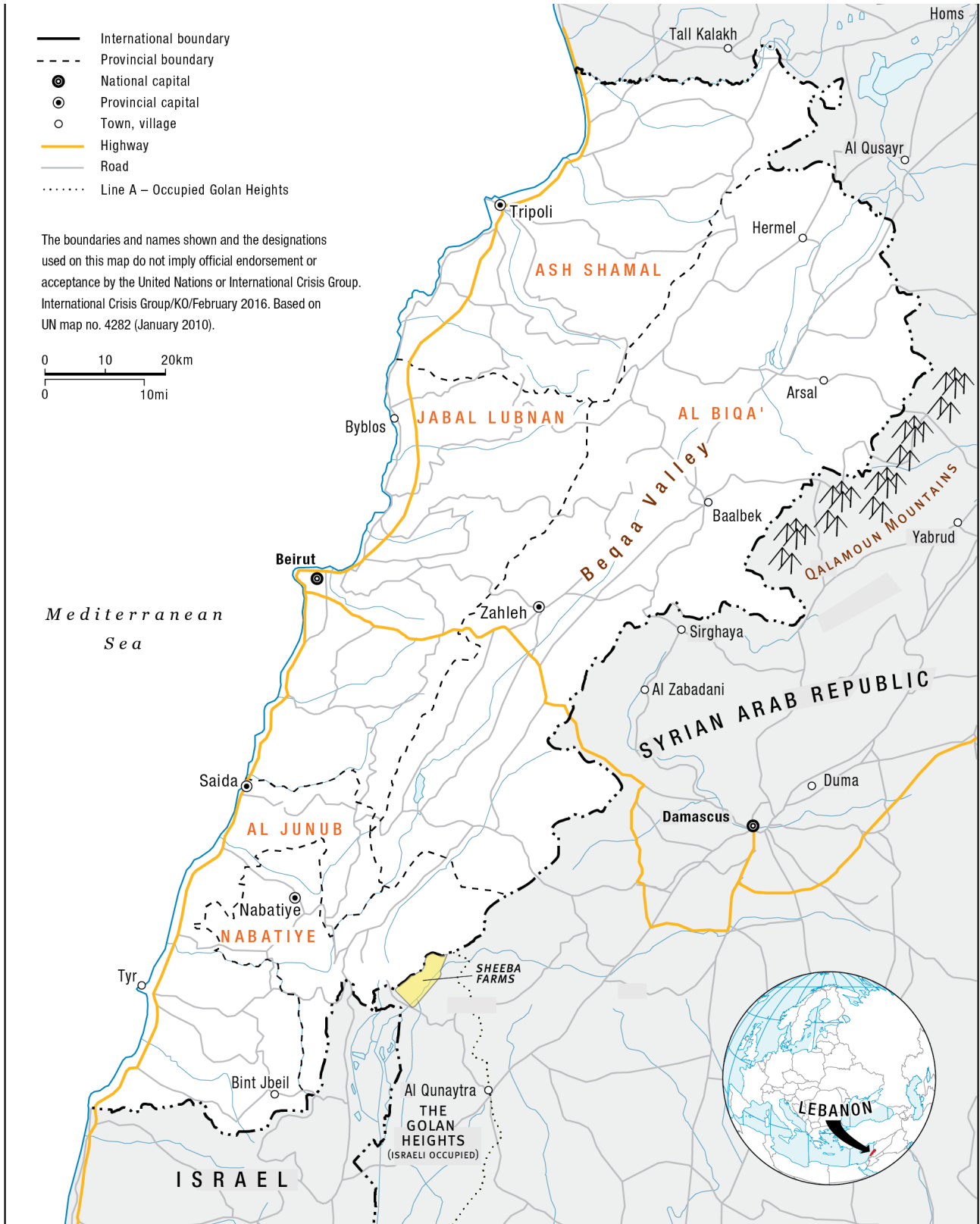
V. Conclusion

Lebanon's political leaders are fiddling while the country smoulders, threatening a multi-level crisis from which it will be increasingly difficult to recover. European donors, with France in the lead, stand at the ready to help their Mediterranean neighbour reverse course. Their approach, since the 2018 CEDRE donor exercise, has pointed in the right direction. Europeans ought to stay the course, despite the port calamity in August and the real possibility that Lebanon will become a failed state.

The only realistic way out of the crisis is for the EU and European governments to keep insisting that Hariri and his fellow politicians form a new government as soon as possible, and that this government strike a deal with the IMF and immediately launch a series of major institutional reforms as a condition for disbursement of significant external funding for infrastructure and development. The Europeans should also urge the U.S. to reduce its pressure on Hizbollah and its Lebanese allies in order to enable a new government to form. At the same time, the Europeans should actively encourage, through funding and diplomatic support, the involvement of Lebanese civil society actors, working in cooperation with political leaders, in the search for solutions to Lebanon's accumulated problems.

Beirut/Brussels, 30 October 2020

Appendix A: Map of Lebanon



Appendix B: About the International Crisis Group

The International Crisis Group (Crisis Group) is an independent, non-profit, non-governmental organisation, with some 120 staff members on five continents, working through field-based analysis and high-level advocacy to prevent and resolve deadly conflict.

Crisis Group's approach is grounded in field research. Teams of political analysts are located within or close by countries or regions at risk of outbreak, escalation or recurrence of violent conflict. Based on information and assessments from the field, it produces analytical reports containing practical recommendations targeted at key international, regional and national decision-takers. Crisis Group also publishes *CrisisWatch*, a monthly early-warning bulletin, providing a succinct regular update on the state of play in up to 80 situations of conflict or potential conflict around the world.

Crisis Group's reports are distributed widely by email and made available simultaneously on its website, www.crisisgroup.org. Crisis Group works closely with governments and those who influence them, including the media, to highlight its crisis analyses and to generate support for its policy prescriptions.

The Crisis Group Board of Trustees – which includes prominent figures from the fields of politics, diplomacy, business and the media – is directly involved in helping to bring the reports and recommendations to the attention of senior policymakers around the world. Crisis Group is co-chaired by President & CEO of the Fiore Group and Founder of the Radcliffe Foundation, Frank Giustra, as well as by former UN Deputy Secretary-General and Administrator of the United Nations Development Programme (UNDP), Lord (Mark) Malloch-Brown.

Crisis Group's President & CEO, Robert Malley, took up the post on 1 January 2018. Malley was formerly Crisis Group's Middle East and North Africa Program Director and most recently was a Special Assistant to former U.S. President Barack Obama as well as Senior Adviser to the President for the Counter-ISIL Campaign, and White House Coordinator for the Middle East, North Africa and the Gulf region. Previously, he served as President Bill Clinton's Special Assistant for Israeli-Palestinian Affairs.

Crisis Group's international headquarters is in Brussels, and the organisation has offices in seven other locations: Bogotá, Dakar, Istanbul, Nairobi, London, New York, and Washington, DC. It has presences in the following locations: Abuja, Addis Ababa, Bahrain, Baku, Bangkok, Beirut, Caracas, Gaza City, Guatemala City, Jerusalem, Johannesburg, Juba, Kabul, Kiev, Manila, Mexico City, Moscow, Seoul, Tbilisi, Toronto, Tripoli, Tunis, and Yangon.

Crisis Group receives financial support from a wide range of governments, foundations, and private sources. Currently Crisis Group holds relationships with the following governmental departments and agencies: Australian Department of Foreign Affairs and Trade, Austrian Development Agency, Danish Ministry of Foreign Affairs, Dutch Ministry of Foreign Affairs, European Union Emergency Trust Fund for Africa, European Union Instrument contributing to Stability and Peace, Finnish Ministry of Foreign Affairs, French Development Agency, French Ministry of Europe and Foreign Affairs, Global Affairs Canada, Iceland Ministry for Foreign Affairs, Irish Department of Foreign Affairs, Japan International Cooperation Agency, the Principality of Liechtenstein Ministry of Foreign Affairs, Luxembourg Ministry of Foreign and European Affairs, Norwegian Ministry of Foreign Affairs, Qatar Ministry of Foreign Affairs, Swedish Ministry of Foreign Affairs, Swiss Federal Department of Foreign Affairs, United Nations Development Programme, UK Foreign, Commonwealth and Development Office, and the World Bank.

Crisis Group also holds relationships with the following foundations and organizations: Adelphi Research, Carnegie Corporation of New York, Facebook, Ford Foundation, Friedrich-Ebert-Stiftung, Global Challenges Foundation, Henry Luce Foundation, John D. and Catherine T. MacArthur Foundation, Open Society Foundations, Ploughshares Fund, Robert Bosch Stiftung, Rockefeller Brothers Fund, and Stiftung Mercator.

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Appendix C: Reports and Briefings on the Middle East and North Africa since 2017

Special Reports and Briefings

Counter-terrorism Pitfalls: What the U.S. Fight against ISIS and al-Qaeda Should Avoid, Special Report N°3, 22 March 2017.

Council of Despair? The Fragmentation of UN Diplomacy, Special Briefing N°1, 30 April 2019.

Seven Opportunities for the UN in 2019-2020, Special Briefing N°2, 12 September 2019.

Seven Priorities for the New EU High Representative, Special Briefing N°3, 12 December 2019.

COVID-19 and Conflict: Seven Trends to Watch, Special Briefing N°4, 24 March 2020 (also available in French and Spanish).

Israel/Palestine

Israel, Hizbollah and Iran: Preventing Another War in Syria, Middle East Report N°182, 8 February 2018 (also available in Arabic).

Averting War in Gaza, Middle East Briefing N°60, 20 July 2018 (also available in Arabic).

Rebuilding the Gaza Ceasefire, Middle East Report N°191, 16 November 2018 (also available in Arabic).

Defusing the Crisis at Jerusalem's Gate of Mercy, Middle East Briefing N°67, 3 April 2019 (also available in Arabic).

Reversing Israel's Deepening Annexation of Occupied East Jerusalem, Middle East Report N°202, 12 June 2019.

The Gaza Strip and COVID-19: Preparing for the Worst, Middle East Briefing N°75, 1 April 2020 (also available in Arabic).

Gaza's New Coronavirus Fears, Middle East Briefing N°78, 9 September 2020 (also available in Arabic).

Iraq/Syria/Lebanon

Hizbollah's Syria Conundrum, Middle East Report N°175, 14 March 2017 (also available in Arabic and Farsi).

Fighting ISIS: The Road to and beyond Raqqa, Middle East Briefing N°53, 28 April 2017 (also available in Arabic).

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