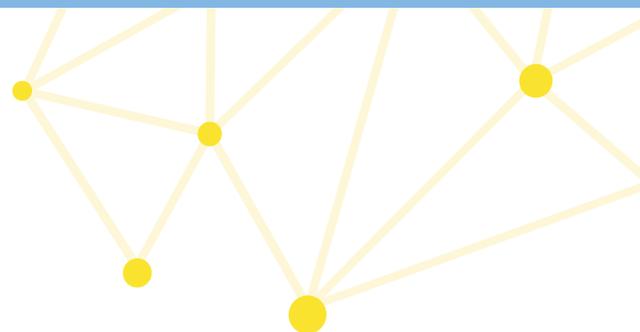


# EU Policy and the Lebanese Protests: Filling the Gap

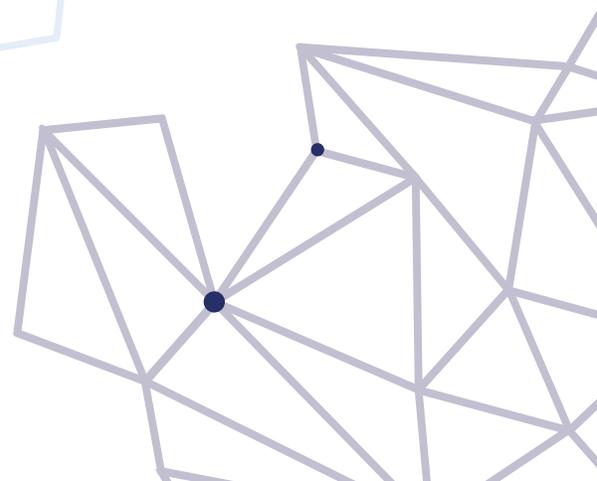


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# EU Policy and the Lebanese Protests: Filling the Gap

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## Key statement

As the Lebanese political crisis enters a new round, the EU should follow a dual objective of (1) helping Lebanon avoid defaulting and halting currency depreciation while at the same time (2) rendering financial aid conditional on the new government ensuring accountability and inclusion of protestors' demands. The current situation—where Prime Minister-to be Hassan Diab has on the one hand gained his position mainly through Hezbollah and Amal support (weakening the country's position in the face of the International Monetary Fund (IMF), the World Bank, and more generally the US-dominated macro-economic institutions), but on the other has vowed to form a technocratic government in conversation with civil society—has produced workable conditions for such a EU strategy. Indeed, should PM Diab comply with conditions, the resulting technocratic, civil society-supported government could advance the agenda of democratisation (including electoral reforms already stipulated in the 2018 Action Plan, such as residence voting, and a move away from sectarian gerrymandering). Should he however refuse to comply, a default of the country would be interpreted as a failure of the “old elite”—and not of civil society—which would, in turn, keep the “playing field” open. At any rate, the EU should take recent Internal Security Forces (ISF) and Army mistreatment of peaceful protestors (both in terms of excessive force, arbitrary arrests, and allegations of torture) seriously, and suspend aid to Lebanese security forces until convincing investigations have been launched and guarantees are in place that inhibit such events from occurring again.

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## Part I : State of Play

### *The Lebanese Crisis at the coming of Hassan Diab*

As of the 19th of December 2019, the Lebanese political crisis has entered a new stage: after weeks of postponements, parliament has recommended Prof. Hassan Diab—engineer, academic, and ex-minister of education under the Mikati government of 2011-2014—to become Prime Minister; a decision which was subsequently approved by President Michel Aoun. The 69 MPs which decided in Diab’s favour stemmed from the Shia Hezbollah/Amal camp and the Maronite Free Patriotic Movement, with only 7 Sunni MPs voting in his favour. As such, Diab’s designation is considered a win for the Hezbollah dominated March 8 alliance over the Future Movement dominated March 14 alliance, even Diab himself asseverates to be an independent candidate (i.e., independent from the political establishment). Diab has vowed to follow protestors’ demands for a technocratic government aimed at safeguarding Lebanon from economic collapse, and bringing overdue reforms pertaining to accountability and transparency. Yet, following the announcement of his designation, protestors took to the street accusing Diab to be part of the establishment. Furthermore, stories of alleged abuses of power (such as [exerting pressure on a medical doctor to employ his son](#)) the designee’s allegedly high degrees of vanity (publishing a 1000 page book on his achievements as a minister, and having the printing costs billed to the ministry; his 192 page long CV), as well as accusations of stealing his student’s work for publication dominated in anti-establishment cyberspace. In short, it appears as if firstly, Diab represents the farthest March 8 is willing to go when it comes to an “independent, technocratic” executive, but secondly, his reputation in wider society renders this alleged independence insufficient. **This dynamic, in interplay with the deteriorating economic situation of the country, represents a highly volatile yet promising situation—and opens up a valid space for productive EU foreign policy intervention, both in the interest of Lebanese national stability, and the normative goal of democratization in the EU neighbourhood.**

### *The Lebanese Economy on the Brink*

With 2019 coming to an end, Lebanon is facing an increasing risk of sovereign debt default and/or currency devaluation, with disastrous effects on the import-dependent, services-dominated and low-production economy – expressed by the World Bank forecasting a 0.2% contraction of Lebanese GDP in 2020. The issue at the heart of this crisis lies at the nexus of fraudulent financial engineering of the Central Bank, misuse of public funds, and the strong relationship between national financial sector and government.

By 2019, Lebanon has amassed a staggering 90 billion USD of sovereign debt, translating to the 3rd highest debt-to-GDP ratio in the world, estimated at 157%. In current estimations, debt servicing makes for 32% of Lebanese public expenditure. Yet, the current crisis presents the peculiar characteristics of a twin sovereign debt crisis: With 60% of total obligations denominated in dollars, and the lion’s share of debt held by Lebanese commercial banks, **Lebanese public spending has essentially sponsored a small group of rich account holders, who profited from high interests rates on their dollar denominated savings**, and whose outward spending (in the form of imports and/or spending in foreign countries) forced Banque du Liban (the Lebanese Central Bank, BDL) to burn through its foreign currency reserves. In order to uphold the peg of 1500 LBP to a dollar, the Lebanese central bank thus “polished” their balance sheets through seigniorage declared as revenue (a practice allowed for in BDL regulations), essentially “creating” dollars for Lebanon’s economy. The practice, fuelled by highly attractive interest rates on dollar denominated deposits of the Lebanese diaspora was described by commentators as a Ponzi scheme, and has given rise to the ridi-

culing definition of these funds as “lollars”, or Lebanese dollars that are nothing but numbers on sovereign and commercial banks’ balance sheets. According to current estimates, there are around 129 billion of these “lollars” spooking Lebanese accounts.

With the surge of protests, which dampened already low levels of productivity in the country, the instable non-equilibrium essentially came close to tipping over: with major parts of the country under effective lockdown, businesses are forced to close, employees are being laid off in droves, and importation has been decimated. The causal relationship here is unclear, as Lebanon’s economic situation was precarious already before protests commenced – in fact, it was one of the salient grievances that brought people to the streets. Yet, the protests have supercharged the downwards trajectory of the economy even further due to their disruptive strategies. **At any rate, the Central Bank continues to refuse emergency measures: neither did it ask for formal currency controls to be installed, nor did it propose a restructuring of debt** (in the form of a haircut to the aforementioned high earner accounts which had profited from artificially high interest rates), **nor did it allow the exchange rate to float.** BDL governor Riad Salameh continues to claim that reserves are plentiful, and that his institution has the means to keep up both peg and debt servicing. Recent estimates from Goldman Sachs claim that Lebanon’s foreign reserves now lie at a 28 billion USD, which would mean that the country likely faces default in early 2020.

**In the absence of formal government responses to the crisis, The Association of Banks has acted as the de facto monetary authority.** When the initial reaction of banks threatened by the possibility of runs on their dollar denominated accounts, i.e. closure of branches, proved unsustainable, the Association reacted by imposing informal capital controls and withdrawal limits. The non-official nature of these controls has, conversely, lead to the non-effectiveness of the policy: as it is widely reported, nothing impedes the aforementioned holders of high level dollar accounts—a class of account holders tightly linked, if not supposable with the political class—to move their deposits out of the country, due to the pressure they can exert on banks and employees. As recent reports suggest, an estimated [\\$2 billion](#) were wired from a number of Lebanese politician’s accounts to Switzerland in the days following the announcement of Diab’s premiership. It is thus primarily import oriented business, and medium earners that are affected.

**In short, the economic situation of Lebanon is highly instable, and the absence of informed, crisis-averse policy decisions contributes to its further demise.** While thus far BDL claims the peg to be intact, informal exchange rates vary between 2500 and 2000 LBP to a dollar; and a wide range of business owners adapt their wages accordingly—a possibility in conditions of complete absence of labour regulations, and a predominance of informal labour. At any rate, the situation has specifically aided the traditionally nepotistic political class in keeping the lowest strata of society from joining the protests, especially with Hezbollah, who regularly circulates videos of piles of cash in order to maintain its support base by stylizing itself as the only guarantee of Shia prosperity. **The master theme of Lebanese politics stands: hardship strengthens partisan cohesion.** In the current state of affairs, Lebanese accounts are in desperate need of foreign aid—a need that, given the political equilibrium arising from Hassan Diab’s nomination, seems impossible. In the meantime, President Aoun has vowed that the economic crisis can be averted by exploiting the oil and gas resources of Lebanon – a claim that leading experts deny.

### ***The Political Situation***

**Hassan Diab’s designation as PM represents a desperate attempt by the March 8 alliance to, on the one hand, ensure the continuation of the political establishment’s control over the country, while**

**on the other hand taking a step towards satisfying the protestors' demands.** While it appears for now as if neither objective has been ensured, his agenda gives rise to the notion that Diab might indeed be the right choice for a third objective: averting economic collapse.

While Diab is a Sunni ex-minister, the Hariri dominated March 14 alliance has voiced its concerns over the former's proximity to Hezbollah, Amal and the Free Patriotic Movement who sponsored his ascension. The dynamic's immediate effect has been a surge of rioting from Future Movement supporters which form a parallel protest movement to the now established civil society "revolutionaries". While Diab is an academic with what he claims to be a proven record of managerial skills in the public sector, protestors question his "technocratic nature" and assume him to be a member of the political establishment, citing stories of corrupt behaviour and unprofessional hubris. Diab himself, on the other hand, claims to be the independent technocrat that the protestors have been waiting for—and indeed, what is known of his project speaks in his favour: as a first in Lebanese post-war government, he has vowed to reduce the total number of ministers to 20 (the traditional number lies closer to 40); to appoint only experts with proven records of excellence to his cabinet; and to do so in close cooperation with civil society. Lastly, and perhaps most importantly, **Diab has outspokenly supported the possibility of accepting an international financial institution's intervention in the national economy—and has expressed himself favourably to receiving an international credit line under conditionality of revamping public spending, fighting corruption, and generally "regain-[ing the trust of the international community](#)".** All claims stand in direct conflict with his parliamentarian supporters, President Aoun, Speaker of Parliament, and Hezbollah Leader Nasrallah, who have expressed wishes to install a "hybrid" techno-political government of usual numbers, while ensuring that no foreign help is needed, and thus refusing structural reforms. Diab has given himself six weeks to prove his agenda.

In addition to this shift in the highest echelons, the reality on Lebanese streets seems to be transforming too: December has shown increased levels of violent repression, arbitrary arrests and persecution of protestors. Notably, the violent repression of demonstrations in Nejmeh and Martyrs' squares two nights prior to the announcement of Diab's ascension to PM, where ISF and Parliamentary Police used extensive amounts of teargas, rubber projectiles and generally physical violence to disperse protestors, has sparked calls from the UN to a [formal investigation](#).

Similarly, Amnesty International has [called for](#) the immediate release of imprisoned protestors. The surging violence represents a shift from the political establishment's prior strategies of (1) attempting to co-opt the protests, (2) attempting to instil sectarian divisions, and (3) blaming economic hardship on protestors in order to move popular support away from civil society organisations (CSOs). The "new" strategy is much more direct: state-sponsored repression of peaceful mobilizations.

In short, the situation is highly ambiguous. Diab's nomination is directly linked to March 8 Alliance's clinging to power, and internationally and locally perceived as such. **This allows to firstly assume that the international community will refuse to assert its full cooperation, as Hezbollah (as March 8's main component) is still considered a terrorist organisation by US and EU; and to secondly assume that protests will continue.** Yet, his agenda appears to favour at least some of civil society's demands, and furthermore appears to give hope when it comes to averting economic disaster through prudential policy. It yet remains to see what Diab's position is towards more structural demands of civil society – such as the reform of the electoral system towards less sectarianism (to be achieved by allowing for residence voting and an end to sectarian gerrymandering), and the installation of a comprehensive anti-corruption agenda. At any rate, the playing field resulting from this dynamic is one where his commitment to reform can be encouraged by

promising comprehensive aid in his real commitment of averting the crisis. To conclude, **it remains to say that the current state of affairs appears to be a situation of “last resort”, where another failure to form a government might invariably lead to economic collapse, a spiral of violence between protesters and security forces, or a direct political takeover of the party that manages to rally the most effective support.**

## Part II : EU Policy

### *An EU foreign policy losing ambition*

The European Neighbourhood Instrument (ENI) represents the key and broadest supportive financial and technical scheme between the EU and Lebanon. Operationally, ENI is framed as a multi-annual program whose focuses, and priorities are defined by a Single Support Framework (SSF) annually channelled into the Action Plan. Furthermore, the EU is engaged with Lebanon with targeted funding to the private sector provided by the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD) and as a primary donor in CEDRE conference. As far as ENI is concerned, for the period 2017-2020 the EU has allocated between €186.5 million-€227.9 million to promote growth and job creation, to foster local governance and socio-economic development and strengthen the Rule of Law with enhanced security. The three-folded multi-annual scheme constitutes the current paradigm of EU intervention under the frame of European Neighbourhood Program (ENP), as other examples in the region could prove (see [EU Joint Strategy 2017-2020 in support of Palestine](#)).

Overall, the EU has been setting its priorities bearing in mind security concerns posed by the Syrian refugee crisis and the growing importance of Hezbollah in the regional political arena. As a matter of fact, the EU has given great attention to lower social strata of the Lebanese population dwelling in sensitive areas of the North East and South with two main objectives: improving living conditions and economic activities and strengthening local governance (particularly municipal units) in order to offset Hezbollah's influence actively promoted by welfare provisions. **In doing so, the EU has broadly relied on Lebanese traditional powers, such as the financial sector and the political leadership who have failed and refrained to provide an alternative economic and political model as the current crisis has shown.**

As mentioned above, ENI is operatively implemented through the Annual Action Plan. In 2019, the document (formally approved by the Commission in mid-October) envisages three main actions in line with the multi-annual priorities of SSF and it establishes a €32 million budget financed by the general budget of the Union for 2019 and 2020.

1. The first project identified in the document aims at strengthening the business outlook and the local institutional capacity of the North-Eastern Bekaa Valley. Regarding the latter, the EU acknowledges that government institutions involved in local development have unclear or conflicting mandates and distribution of responsibilities, a situation that significantly contributes to inadequate central management and weak fiscal capacity. As such, the EU by investing in agriculture and local economy aims at generating sufficient income to upscale the coordination capacity of local actors encouraging the involvement of civil society organizations as well as reducing crime rate. The financial allocation consists in €11 million disbursed through grants. Under the responsibility of the Commission's authorising officer responsible, the grant may be awarded without a call for proposals to a Consortium led by the European NGO We-

World-GVC, which is currently running other three humanitarian projects in the region; one, financially supported by ECHO. **The underlying assumption is that the political and security conditions of the country remain stable.**

2. The second pillar of the 2019 Action Plan stems from the broad security priority envisaged by the EU. As a matter of fact, the Commission has invested €15 million to strengthen the capacity of municipal police and to foster the Internal Security Forces' accountability with respect to human rights. Regarding the latter, the EU has undertaken several initiatives to include CSOs in the program. However, the 2019 Action Plan allocates only one fifth of its €15 million to human rights monitoring, and only a share of this to promote CSOs inclusion in the process. Furthermore, after the Law No.62 of October 2016 provided for the establishment of a National Human Rights Commission (NHRC) and a National Preventive Mechanism (NPM), the EU has supported the inclusion of the two bodies in its own strategy. However, besides acknowledging the lack of willingness of the ISF to cooperate with the two bodies as high/medium risk to the program, **the EU seems to forget that Lebanese authorities have consistently failed to implement the national anti-torture law (Law No. 65 of October 2017)** and that the government has not yet issued the decree to operationalize the NPM nor it assigned a budget. The working assumption is the persistency of relative political stability in Lebanon and the region.
3. The third objective of the 2019 Action Plan is to support local stakeholder to promote a more transparent and accountable electoral process, involving CSOs and political parties in order to strengthen public confidence in the democratic consolidation of the country. In 2005 and 2009 the EU Election Observation Missions (EUEOMs) recommended among others: a non-confessional electoral system, the setting of the minimum voting age at 18 (currently at 21, when the age of legal majority is 18), implementation of an out of country voting mechanism, enhanced women's representation (Lebanon has of the lowest rates in the world, at 3.1% far less than the regional Arab average of 12%) and transfer of voter registration to the actual place of residence. So far, none of the aforementioned recommendations has been implemented. Furthermore, **the current Action Plan avoids mentioning any structural reform of the electoral system**, posing its exclusive attention to transparency and capacity building in coordination with UNDP and the Minister of Interior and Municipalities (MoIM). UNDP will be later responsible for sub-grants' awards to civil society organisations to which one third of the budget (€2 million) will be allocated.

**The 2019 Action Plan, contrary to its predecessor, does not mention any commitment or conditional criteria expressed in the strategic CEDRE Conference** (March 2018), where the EU announced a package of up to €150 million, conditional to reforms, which could be extended up to €1.5 billion loans until 2020. Several CSOs have affirmed the need for more transparency and clarity during the monitoring and implementation of CEDRE funds, and more consistency on conditional criteria demanded by donors. As the Lebanese Government resulted negligent regarding such requests, the EU, as have other donors, has delayed the funds' disbursement diverging their attention to security issues and capacity building. As a matter of fact, the three actions defined in the 2018 Action Plan, supposedly in line with CEDRE's outcomes, were national infrastructure and governance reforms and clean energy transition fostered by an audacious investment plan and job creation for the private sector.

**Such actions have been financially supported by credit facilities provided by the EIB and the EBRD for respectively €818 million, and around €700 million, whose main direct beneficiaries are local commercial banks, Électricité du Liban (Lebanon's national electricity company, EdL) and Lebanon's Council of Development and Reconstruction (CDR).** As part of the global strategy outlined above, that seeks

to support the current traditional power forces, the EBRD has approved on March 26, 2018 an equity investment for approximately 2.51% of Bank Audi SAL's total common shares outstanding. Bank Audi, which is the largest bank in Lebanon for assets share (20% of the total in 2014), is predominantly owned and managed by Politically Exposed People (PEPs) part of the Hariri family or strongly associated with it.

Concerning the improvement of Syrian refugees' living conditions and the support to low-income strata of Lebanese population affected by the crisis, **the EU has spearheaded the international response with over €10.6 billion mobilised so far by both the EU and its Member States.** As per the EU only, the total amount disbursed at June 2019 stands at around €770 million, channelled through EU Regional Trust Fund in Response to the Syrian Crisis (Madad Fund). Of this amount €521 million has been allocated to Lebanon in line with the adoption of the EU-Lebanon Compact (2016-2020). Signed in 2016, the document focuses on three main areas of actions coherently with ENP priorities: growth and job creation, security and counter-terrorism, and public governance. Given the current difficulties Lebanon is facing, the Mashreq/Maghreb Working Party (MaMa), the preparatory body of the Council of the European Union, is seeking a re-evaluation of Madad Fund in the upcoming weeks.

Regarding the other EU instruments currently in place with Lebanon, it is worth noticing that although they are considered part of the EU comprehensive strategy, they benefit from a very low budget support and they are generally defined by a short-term approach. Particularly, the EU has aimed at supporting the local public administration in the framework of Twinning and at fostering CSOs with the launch of the EU Country Roadmap for Engagement with Civil Society (2014-2017). Twinning projects are financed by grants awarded in the framework of EU external aid programs, and they are part of ENP with relatively high degree of autonomy with respect to ENP areas of focus. Planned in Q3 2019, the Twinning program currently relevant for Lebanon aims at "strengthening capacities and developing sustainable opportunities for a prudent exploitation of Lebanon's oil and gas resources (Lebanese Petroleum Agency)" with a budget allocation of €1.5 million. **Twinning is usually considered central within ENI funding as it frames a cooperation agreement based on the direct involvement of a Member State and it proved to be an effective tool to foster accountability and international practices against corruption in other contexts. Nonetheless, the instrument has acquired very small significance and budget allocation in Lebanon.** Regarding the Roadmap for Engagement with CSOs there is a general lack of transparency concerning concrete actions taken in the 4-years period. As a matter of fact, besides the definition of priorities and areas of focus, often vague and ambitious, **there is no track of follow-up implementation documents.**

To conclude, the EU has so far framed its strategy towards Lebanon relying on local traditional powers, namely the financial sector and the current political leadership who have failed and refrained to provide an alternative economic and political model as the present moment is proving. Furthermore, **since 2019 the EU has voided its Action Plan of the crucial element of political reforms as a condition for aid, most importantly in the form of (1) a substantial change to the electoral system and (2) a credible anti-corruption policy, which would both be in line with current demands from civil society,** making its policies nothing but a direct financial transfer disregarding the volatile status quo. In addition, not only has the EU deliberately decided to engage only on technical terms, emptying its actions of any political considerations, but **it has also failed to provide an accurate assessment of the current situation on the ground through the Action Plan's working assumptions.**

## Part III : Policy Recommendations

### *The case for renewed ambition*

The EU should take advantage of the momentum arising from Diab's designation as PM, as he is facing the following situation: as future head of a government essentially called into life by Hezbollah, his ascension to power will be met with severe resistance from the US-dominated international financial institutions—at the same time, Diab's success is contingent on him averting economic disaster; a success that is, in turn, contingent on securing foreign aid. At the same time, CSOs, whose demands he claims to take seriously, reject him on the grounds of assuming him to be “more of the same”. Diab thus has a lot to prove: he is (1) in need of distancing himself from the establishment in order to gain the favour of the streets, and (2) in need of international support to deliver on his claim of saving the economy. The EU could empower Diab to do the first by ensuring the second—and pursue its own agenda of democratizing the neighbourhood by means of conditionality. The following policy targets should therefore be enshrined in the 2020 Action Plan:

In the **SHORT TERM**:

- **The EU should engage in consultations with members of the civil society** who are actively researching into BDL balance sheets, as opposed to consulting uniquely with the “traditional” political establishment, such as the meeting between the EU's ambassador to Lebanon and [Samir Geagea in mid-November 2019](#) who has been complicit in the current disastrous state of affairs, and whose double position in government and financial institutions compromises them as impartial informants. As the IMF and the World Bank are already doing so, but are hesitant on acting upon their conclusions due to pressure from the US when it comes to engaging a government essentially built by Hezbollah, the EU could thus take a leading role on the issue by building a bridge between CSOs, the upcoming Diab government, and the international scene.
- **The EU should set up a credit line under the [Macro Financial Assistance programme \(MFA\)](#)**, conditional to PM Diab's gradual engagement of the protestors' demands which in fact partially coincide with the EU original 2018 Action Plan, based on the assumption that both the IMF and the World Bank will continue to be hesitant in aiding Lebanon due to aforementioned reasons. The conditions should include specifically:
  1. electoral reform to a non-confessional system;
  2. lowering the voting age to 18;
  3. allowing the casting of ballots in circumscriptions of residence;
  4. a comprehensive anti-corruption policy;
  5. Ministers chosen from civil society (as opposed to private sector and political establishment).
- **The EU should revise the underlying assumptions of security and stability in the country** in its current Action Plan, especially in light of the ongoing protests and the violent response of the security apparatus.

In the **MEDIUM TERM**:

- **The EU should foster and improve allocation of money to human rights monitoring activities and CSOs as defined by the second pillar of the 2019 Action Plan when dealing with the internal security** capacity of the country; specifically, by conditioning its money transfer to:

(1) an increase in transparency of the ISF and municipal police programme, and (2) the implementation of the already approved anti-torture law (No. 65 of October 2017). Furthermore, both requirements could be rendered conditional for upholding the abovementioned credit line.

- **The EU should consider a partial recapitalization of local banks** to save the economy in the medium term. As a matter of fact, if coupled with a much-needed progressive taxation of current deposits held by banks, an equity line provided by the EBRD and EIB could gradually foster credit allocation. The EU should advocate for a national financial strategy that prioritizes productive sectors in order to take benefit of this newly created credit space. Moreover, the EIB and EBRD should revise their criteria for credit allocation in their external mandate framework. The combined support of the two multilateral development banks has thus far amounted to around €1.5 billion, mainly provided in the last three years. As mentioned above, these funds have primarily targeted local commercial banks which accumulated huge amount of profits in the last decade whereas the economy has stagnated at best. As such, in order to restore trust in the Lebanese financial sector and to promote a productive allocation of credit, the EU should improve its monitoring activity and enhance cooperation between its financial bodies and the European External Action Service (EEAS).
- **The EU should revise the fundamentals of its current Twinning program** and shift its focus of assistance to banking supervision in order to build administrative capacities inside the BdL. Currently, the 2019 Twinning program aims at strengthening capacities for the exploitation of Lebanese natural resources, however, as the current financial crisis is showing, more attention should be given to improving institutional governance within the powerful central bank.