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Greece takes step closer to default

By Kerin Hope in Athens, Alex Barker in Brussels and Quentin Peel in Munich

Lucas Papademos, the Greek premier, failed to make party leaders accept harsh terms in return for a second €130bn bail-out, pushing Athens closer to a disorderly default as early as next month.

Greek television reported that Mr Papademos has set a deadline of midday on Monday for the three leaders to let him know whether they agree in principle with the proposed austerity measures, before he meets them again later in the day.

After five hours of discussions, the three leaders of Greece's national unity government had not accepted demands by international lenders for immediate deep spending cuts and labour market reforms as part of a new medium-term package.

Mr Papademos said the political leaders had agreed on some "basic issues", including making spending cuts this year of 1.5 percentage points of gross domestic product, or about €3bn, according to a statement from his office.

George Karatzaferis, the head of the small rightwing Laos (People's) party said as he left the prime minister's office, that he expected the talks to continue on Monday. There was no immediate announcement by Mr Papademos.

It was clear however that the talks had reached a dangerous deadlock. "They're asking for more recession than the country can take," said Antonis Samaras, leader of the centre-right New Democracy party as he left the meeting.

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The talks with the three leaders of a national unity government came after the government failed to persuade the so-called "troika"– representatives of the European Commission, European Central Bank and International Monetary Fund – to ease conditions for the rescue deal.

Patience with Greek politicians has evaporated among its creditors. During a conference call on Saturday, eurozone finance ministers bluntly told Athens to deliver on its promises and agree to reforms or face default next month.

Jean-Claude Juncker, head of the eurozone group of finance ministers, told Der Spiegel at the weekend that the possibility of bankruptcy should encourage Athens to "get muscles" when it comes to implementing reforms.

"If we were to establish that everything has gone wrong in Greece, there would be no new programme and that would mean that in March they have to declare bankruptcy," he warned.

Mr Samaras last week threatened to veto the package unless concessions were made on private sector wages, claiming the cuts would prolong a recession already in its fifth year. Mr Karatzaferis also opposes further austerity measures.

The two sides were still far apart over projected cuts of 25 per cent in private sector wages, 35 per cent in supplementary pensions and the closure of about 100 state-controlled organisations with thousands of job losses.

These are part of a €4.4bn package of savings the troika has said should be implemented at once.

Eurozone officials are deliberately refusing to allow Greece to sign off on a €200bn bond restructuring plan because the threat of default is the leverage they have to convince recalcitrant Greek ministers to implement necessary cuts.

While some recognise that Greek politicians must be seen by voters to be putting up a fight, there are fears that the show of brinkmanship could easily go too far and backfire, with disastrous consequences.

The second Greek bail-out, which must be approved in a matter of days, has serious implications for the wider eurozone.

Markets are likely to react negatively to news of the breakdown in talks on worries that Greece will default on a €14.5bn bond repayment on March 20, and that "contagion" could spread to Portugal and Italy.

A further complication is the uncertainty over supplementing the €130bn bail-out to take account of the deteriorating economic position in Greece.

Some officials believe around another €15bn is needed – funds that Germany and other countries have said they are unwilling to provide.

The financing gap is likely to open a fierce debate over the sacrifices required of public bondholders such as the European Central Bank, which is being urged to forgo any profits on bonds that are fully paid on maturity.

The stand-off has also delayed a separate agreement with private bondholders' representatives who flew to Athens to finalise a €200bn debt swap included in the rescue package.

Josef Ackermann, chief executive of Deutsche Bank, has warned that failure to agree on a voluntary debt rescheduling for Greece could open "a new Pandora's box" in the eurozone crisis.

"We are in a make or break situation," said Germany's most powerful banker and senior participant in the talks led by the Institute of International Finance.

Private sector creditors were being "extremely generous" in offering to take a loss of more than 70 per cent on their Greek government bonds, he said, as a contribution to helping Greece manage its debts.

Mr Ackermann told a conference in Munich: "I think the markets are recognising this. But we have to fix the Greek problem."

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