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Papademos keeps drama out of crisis

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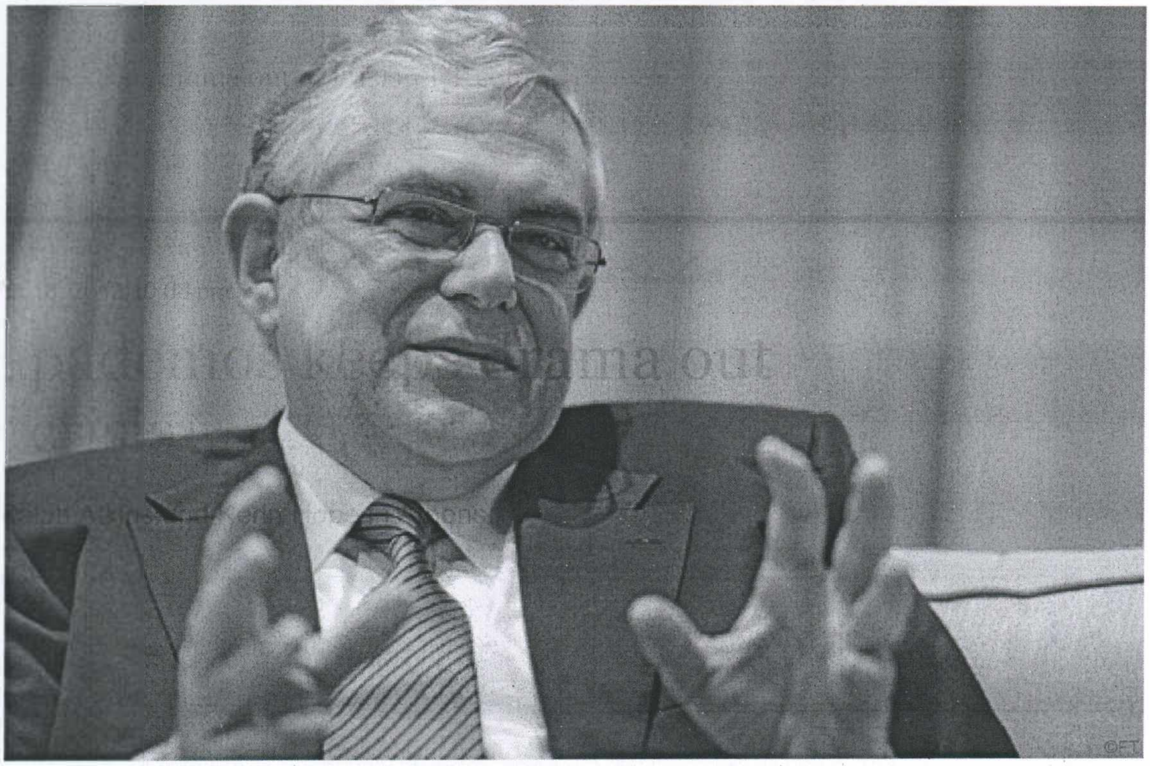
By Ralph Atkins and Kerin Hope in Athens



Lucas Papademos was the perfect central banker – clever but conservative, cautious and low-profile. Since November, however, the former European Central Bank vice-president has had the toughest, most brutally exposed job in European politics: saving Greece's economy from collapse.

He was thrown, reluctantly, into the task when the country's crisis led to a breakdown in normal politics. In an interview with the Financial Times it is clear at least that Mr Papademos's instinct for understatement remains unaffected. At the ECB, the issues were sometimes tough, "but the challenges that I have confronted over the past four months have been wider in scope and greater in intensity".

Those challenges involved averting a disorderly default and catastrophic exit from the eurozone, overseeing the largest debt restructuring in history, and securing a fresh, €174bn bailout plan from sceptical European partners and the International Monetary Fund. He has pushed through savage public spending cuts and forced bickering party leaders to agree a sweeping agenda of structural reforms.

All the while, Greeks have suffered what Mr Papademos describes as "negative aspects" of the crisis – a precipitous fall in economic activity, a severe "credit crunch" and unemployment levels that have soared above 20 per cent. Youth unemployment is above 50 per cent. Across Athens, banks' buildings remain burnt out after riots earlier this year. Protest rallies take place daily in the city's crowded streets.

Outside Greece, there were doubts whether Mr Papademos, age 64, was the right man. The Massachusetts Institute of Technology-trained economist has neither the political flair nor profile of Mario Monti, the former European Commissioner who became Italy's technocrat prime minister in similar circumstances. At the ECB, by contrast, his reputation was for painstakingly precise decision making. Last week, the ECB finally published papers presented at a seminar given in his honour on his departure two years ago – minus Mr Papademos's foreword, which he had still not completed.

But in a two-hour discussion on white sofas in his office, a softly spoken Mr Papademos sees the mission of his caretaker government – securing a second rescue plan, a new reform programme and the debt restructuring – as nearing completion. "The process I followed turned out to be appropriate in the end," he says.

Others' verdicts are more direct. Yannis Stournaras, director of the Athens-base Iobe think-tank, says: "The positive contribution of Mr Papademos is that we have avoided a chaotic default."

Mr Papademos is an antidote to usually shrill, domestically-focused Greek politics. He does not point fingers – and refuses to criticise German or other European leaders who have cast aspersions on Greece's reform zeal or demanded the surrendering of political control. But, he says, Greece should go ahead with national elections in early May at the latest, despite Berlin's objections. "The Greek people should now have the opportunity to express their preferences on key policy issues affecting the future of the country."

Mr Papademos has taken steps to ensure continuity. One is to plan a significant strengthening of the Greek prime minister's office.

"Some of the staff, particularly those involved in surveillance of policies, should be permanent and not change every time a new government comes into power," he explains.

Another has been to introduce Greeks to the idea of coalition government – a novelty in its usually divisive political system. "Until November there were different and opposing views on the programme. But over time, and perhaps this has been one contribution of this coalition government, we have forged a higher degree of consensus."

Greece's two main parties that make up his coalition – the PanHellenic Socialist Movement (Pasok) and the centre-right New Democracy – have both expelled members who voted against reforms in parliament, he points out. "During the election campaign you may hear some nuances, but I believe that there is an understanding that the only way forward it to pursue the policies that are included in this [bailout] programme."

In quieter times at the ECB, Mr Papademos oversaw academic research into the effects Europe's monetary union – launched in 1999 – was having on its member economies. In 2005 he attracted headlines when he expressed public concern about economic divergences and the pace of structural adjustment within the eurozone. With hindsight, his concerns were prescient.

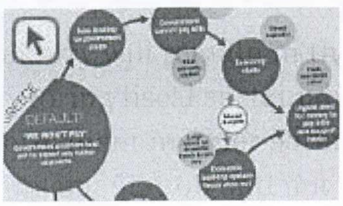
Seven years later he says: "There is no doubt that the crisis demonstrated – let me put it positively – the need to strengthen the economic pillar of the economic and monetary union [EMU]." But he points to the many institutional reforms, some previously unimaginable, introduced in the past two years. "Significant steps have been taken in the direction of completing EMU so as to secure its more efficient functioning – and its future."

For Greece, of course, the problems have been worse than anywhere else. He is wary of a firm prediction that Greece will return to capital markets in 2015 – the aim of the European Commission and IMF. If it does not, further international support will be needed.

Nevertheless Mr Papademos remains optimistic. "In my mind, there is no doubt that the country will remain in the monetary union. The overwhelming majority of Greeks believe that restoring fiscal sustainability and competitiveness can be achieved in a more effective and permanent manner within the euro area rather than outside. What is key is policy implementation and not to repeat past mistakes. If this is done I see no problem."

He adds: "I'm convinced that we are more than halfway along the path to economic recovery – although the fiscal consolidation will last longer. Positive growth rates should be achieved within less than two years."

Interactive graphic: Consequences of a Greek default



This interactive graphic outlines the likely consequences for the eurozone if Greece defaults.

It is a hard balancing act. Mr Papademos wants to convey confidence – but not give the impression he is underestimating the scale of Greece's problems. Many independent economists fear that problems are simply too great and that euro exit is inevitable, even desirable.

But the Greek prime minister argues that reality might not be as bad as imagined. The first rescue programme resulted in the biggest fiscal consolidation ever in an advanced economy, he says. Progress has been made towards restoring competitiveness. He also reveals plans under discussion to better harness European Union financial aid programmes to Greece's benefit – to help banks fund job-creating small and medium-sized companies and to restart a motorway construction programme.

If the programme were completed with these additional policy measures, "it should be sufficient – if implemented effectively – to break what you call a downward spiral and to start a virtuous circle of structural reform, increasing activity and faster fiscal consolidation", he concludes.

It could all prove hopelessly optimistic. Mr Papademos's work may not yet be done. In Athens' political circles there is talk of him emerging as a compromise candidate for prime minister if the elections fail to produce a convincing win for either of the two main parties – or returning as finance minister. Opinion polls suggest that, for all Mr Papademos's assurances, May's elections will create fragmentation, with new parties on the left and extreme-right taking seats in parliament.

He does little to quell speculation about his future. With central banker's scrupulousness, he says: "It would not be appropriate before the election to disclose any such preference."