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Passage No. 111

Direction: Study the following information carefully and answer the question given below.

Paragraph 1: Financial markets don't much like uncertainty. Thanks to Italy's politicians, in recent days they have had plenty. By May 30th some calm had returned: it seemed possible that a pair of populist parties, the *Five Star Movement* and the *Northern League*, would form a government after all. Markets had been in turmoil for two days, unsettled by a **farcical** back-and-forth between the populists and the country's president, who had rejected the parties' choice of a Eurosceptic economist as finance minister. The politicians may have done the markets a service, by shaking them out of **complacency**. Investors may have returned the favour, by shaking some sense into the politicians—at least for now.

Paragraph 2: Italy is perennially slow-growing and groans under public debt of around $2.7trn, or132% of GDP. The drama reawakened dormant worries about those two problems—and the deeper fear that the euro zone's third-biggest member might be sneaking towards the exit. So the yield on Italian two-year bonds, negative as recently as May 15th, leapt to almost 1% on May 28th. It carried on climbing the next day, touching 2.73%, the highest since 2013, before retreating. Ten-year yields also rose, if less spectacularly. Yields on German Bunds, Europe's safest government bonds, declined.

Paragraph 3: Share prices tumbled. Banks in Italy, holders of €600bn of government bonds, were hit hardest. UniCredit, the country's biggest, fell by 9.2% and Intesa Sanpaolo, the number two, lost 7.2% on May 28th and 29th. Other European banks' shares were also roughed up. The worries rippled across the Atlantic. The S&P 500 index slipped by 1.2% on May 29th, with banks again leading the way down. The yield on ten-year Treasury bonds fell from 2.93% to 2.77%, the biggest drop since the day after Britons voted for Brexit in June 2016. So far, this adds up to a nasty bout of the jitters rather than full-blown panic. Italy's two-year bond yield is far below the 7.6% it hit in November 2011, at the depths of the euro zone's previous crisis. The effect on the euro area's other problem members has been limited—even though yields in Greece, Portugal and Spain, where the prime minister faces a confidence vote on June 1st, reached their highest this year on May 29th.

Paragraph 4: Foreigners are also unlikely to have suffered much direct harm from the fall in bond prices (the corollary of rising yields). Nor has the run-up in yields yet threatened the sustainability of Italy's debt. On May 30th Italy sold a total of €5.6bn-worth of five-, seven- and ten-year bonds at yields of 2.32%, 2% and 3% respectively. Granted, that is dearer than in the recent past, but it is well below the average coupon of 3.4% on its existing stock of debt. And the longish average maturity of its bonds, around seven years, gives it breathing space. Alberto Gallo of Algebris, an investment firm, estimates that yields would have to be at least 4-4.5% for several months before higher coupon payments would make debt unsupportable. That is not unimaginable, but is some way off.

Paragraph 5: One reason for that is the backing of the European Central Bank. Under its quantitative-easing programme, which has held down borrowing costs across the euro area, the ECB has bought

€340 bn worth of Italian bonds; it holds around a sixth of the stock. In effect, it has been a willing buyer as foreigners have quit. Yet none of this means that markets could not turn against Italy with greater violence—if, say, a populist government undid recent reforms, opened the fiscal taps or picked a fight with bureaucrats in Brussels or Frankfurt. Although the biggest banks are now in decent health (or getting there), they own lots of government bonds. One bank, Monte dei Paschi di Siena, is still in intensive care. The bad-loan burden, though reduced, remains heavy. Departure from the euro area would be unthinkably costly—for both Italy and the zone. Just like when Argentina abandoned dollar parity at the start of 2002, the value of Italians' bank deposits would plunge. Italy is not Greece, in that it is in far better shape. But it is not Greece, too, in that it is much, much bigger. In 2012 Mario Draghi, the ECB's president, quelled the crisis that looked likely to destroy the currency club by saying that the ECB would do "whatever it takes to preserve the euro".

Questions:

1. Which of the following is/are synonyms of **farcical?**

I. Skeptical
II. Preposterous
III. Ludicrous
IV. Perplexed

A. Only I B. Only II and III C. Only I, III and IV D. Only II, III and IV
E. All of the above

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2. Which of the following is/are antonyms of **complacent?**

I. Vitriolic
II. Slack
III. Humble
IV. Gloat

A. Only IV B. Only III C. Only I, III and IV D. Only II and IV
E. Only I, II and IV

3. Which of the following statements from paragraph 2 shows that investors were losing confidence in Italy?

I. Its debt hit a level of $2.7 trn, many times above its GDP.
II. Yield on Italian bonds rose in general.
III. Yields on German Bonds fell.

A. Only II B. Only III C. Only I and II D. Only II and III
E. Only I and III

4. Which of the statements below strengthen the argument -'So far, this adds up to a nasty bout of the jitters rather than full-blown panic'?

I. The bond yields in Italy are still far below the levels reached during the 2011 Euro-zone crisis.
II. The effect of the issue has not impacted other members very hard.
III. The ratings given to many Italian Bank stocks by credit agencies has not changed at all.

A. Only I B. Only III C. Only I and II D. Only II and III
E. All of the above

5. Which of the following could be a possible reason for the line- 'Foreigners are also unlikely to have suffered much direct harm from the fall in bond prices'?

I. Italy's huge public-debt market gives it a decent weight in global bond indices.
II. Foreign investors have cut their Italian holdings from €473bn to €250bn during the last year.
III. Exposure of banks outside Italy has fallen by almost half since 2009, to €133bn.

A. Only II B. Only I and II C. Only II and III D. Only I and III
E. All of the above

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6. As per paragraph 4, which of the following does not adversely impact the sustainability of Italy's debt?

I. The rate offered on the bonds has increased when compared to the past.
II. The current rate offered on bonds is around the average rate of the existing debt.
III. Most of the debt is short to mature in terms of maturity.

A. Only II B. Only I and II C. Only III D. Only II and III
E. None of the above

7. Which of the following is/are true in context of the passage?

I. Italy's Populists prefer the option of leaving the EU.
II. Bond yields and bond prices are inversely related.
III. Italy is not much bigger than Greece in terms of the size of its economy

A. Only III B. Only I and II C. Only I and III D. Only II and III
E. All of the above

8. Which of the following is/are true with respect to the ECB's Quantitative Easing Program?

I. The program is used to buy bonds from the markets.
II. This is used for bringing down the borrowing costs of debt.
III. It is used to uphold credit ratings assigned to bonds.

A. Only III B. Only I and III C. Only II and III D. Only I and II
E. All of the above

Correct Answers:

1	2	3	4	5	6	7	8
B	B	D	E	C	A	B	D

Explanations:

1. **Farcical**: relating to or resembling farce, especially because of absurd or ridiculous aspects.

Eg: He considered the whole idea farcical.

Synonyms: Preposterous and Ludicrous.

Skeptical and *perplexed* both mean *puzzled.*

Hence, option B is correct.

2. **Complacent:** showing smug or uncritical satisfaction with oneself or one's achievements.

Eg: We can't afford to be complacent about security.

Synonyms: Slack, gloat.

Thus, II and IV are incorrect.

Vitriolic means *hurtful/spiteful*.

Only *humble* is correct as the antonym of *complacent*.

Hence, option B is correct.

3. Statement I is merely a fact and merely states the debt conditions in the country.

Statement II is correct. When investors lose confidence in the markets, the bond yields increase.

Statement III is correct as investors have been shifting from Italian to German bonds which provide more safety. This led to a decrease in the yields of the bonds.

Hence, both II and III are correct.

Option D is the correct answer.

4. As per the passage, bond yields rise when investors lose confidence in the ability of bonds to repay the debt. Here, the levels have not hit the heights that were achieved during the 2011 crisis and thus, statement I is correct.

Statement II is correct clearly.

Statement III is correct as a fall in the ratings would have indicated deterioration of conditions in the economy.

Hence, option E is correct.

5. Statement I is incorrect as if the Italian debt market has a huge share in the global bond indices, it would have an adverse impact on foreigners.

Statement II and Statement III are both correct as if the banks and other foreign investors have cut down on Italian holdings, they would not suffer much from the current situation.

Hence, option C is correct.

6. Refer to: 'Nor has the run-up in yields yet threatened the sustainability of Italy's debt. On May 30th Italy sold a total of €5.6bn-worth of five-, seven- and ten-year bonds at yields of 2.32%, 2% and 3% respectively. Granted, that is dearer than in the recent past, but it is well below the average coupon of 3.4% on its existing stock of debt. And the longish average maturity of its bonds, around seven years, gives it breathing space.'

I is incorrect as an increase in rate would decrease the sustainability of Italy's debt.

III is incorrect as the debt should be long term in nature so as to be sustainable. A short term maturity would put more burden in terms of repayment.

II is correct.

Hence, option A is correct.

7. Refer to:

'Between the populists and the country's president, who had rejected the parties' choice of a Eurosceptic economist as finance minister.'

I is correct as the populists chose a person who is a Eurosceptic economist as their finance minister.

Refer to:

'Foreigners are also unlikely to have suffered much direct harm from the fall in bond prices (the corollary of rising yields).'

II is correct.

III has not been mentioned in the passage and is incorrect.

Only I and II are correct.

Hence, option B is correct.

8. Refer to: 'Under its quantitative-easing programme, which has held down borrowing costs across the euro area, the ECB has bought €340 bn worth of Italian bonds; it holds around a sixth of the stock. In effect, it has been a willing buyer as foreigners have quit.'

I and II are correct while III has not been mentioned in the passage.

Hence, option D is correct.

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