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**Article Response**

Attach your article to this form using a staple. Draw graphs on the back.

Article Title: Central Bank Signals Worry on China Prices

Article Source and Date: A version of this article appeared March 13, 2013, on page A10 in the U.S. edition of The Wall Street Journal, with the headline: Central Bank Signals Worry On China Prices.

Economic Topic (and chapter): Monetary policy (Chapter 15)

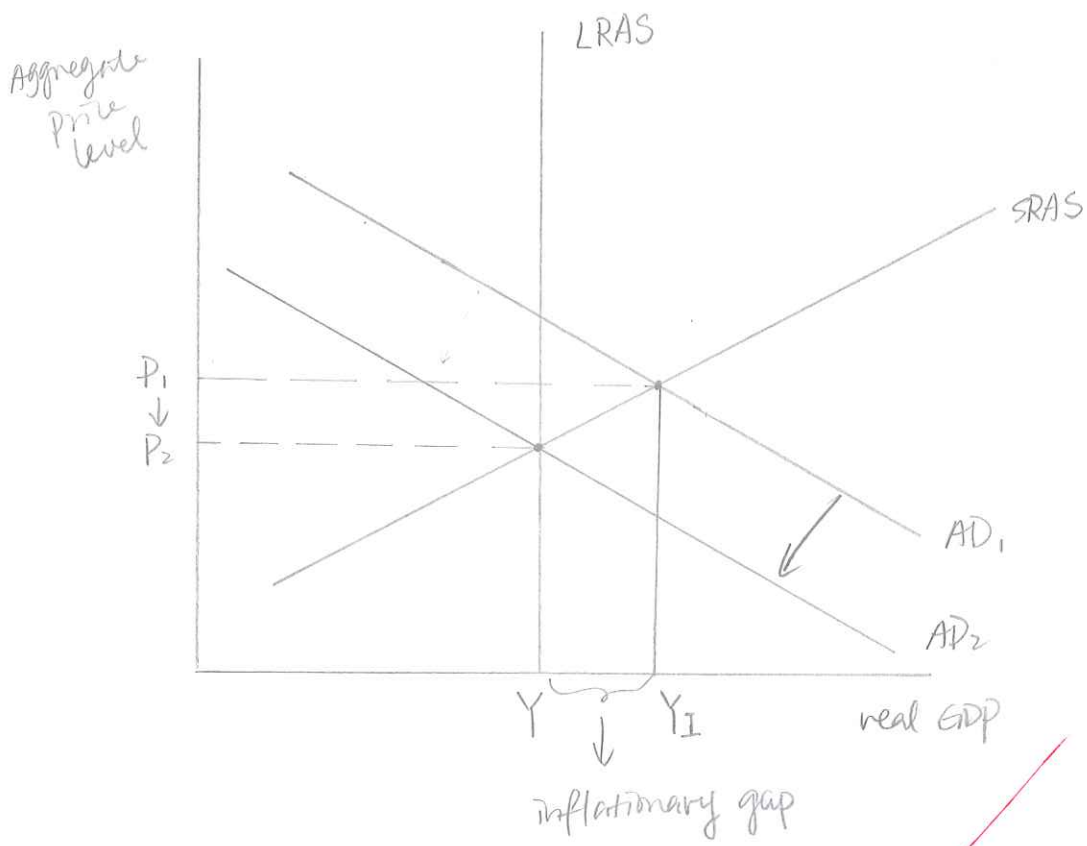
What is the article about? Briefly summarize the issues in a non-technical way.

Zhou Xiaochuan, the head of People's Bank of China, expressed his concern over inflation and China's monetary policy will focus on controlling money supply to control inflation this year. China's CPI last month was up 3.2% from a year earlier, accelerating from January's 2% pace, which signals the central bank must be on guard fight inflation. China will mainly focus on maintaining price stability this year and controlling M2 growth will be the way to do so.

What are the economics of the article? How does a recent topic covered in the course explain the subject matter of the article?

This article covers the topic of how a country's central bank can influence economy (in this case, fight inflation) by manipulating money supply. Due to the high inflation embedded in the economy, Chinese economy right now has an inflationary gap, meaning the actual output produced by the economy exceeds the potential output. (On the graph, SRAS and AD curves intersect to the left of LRAS line.) In order to close the gap, Central Bank carries out contractionary monetary policy, which decreases money supply by controlling the growth of M2, composed of various kinds of bank deposits. Decrease in money supply leads to higher interest rate, follows by lower investment spending which reduces income, thus consumption goes down, and finally the aggregate demand decrease and AD curve shifts left. Eventually, the new AD curve intersects LARS line at potential output with a lower aggregate price level.

(Graph on the back)



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CHINA NEWS | March 13, 2013, 9:31 a.m. ET

# Central Bank Signals Worry on China Prices

By AARON BACK

People's Bank of China Gov. [Zhou Xiaochuan](#) Wednesday signaled elevated concern over inflation and a slightly tighter bias for central-bank policy this year.



China's consumer inflation rose 3.2% in February from a year earlier. Barclays economist Jian Chang talks to the WSJ's Deborah Kan about what tightening measures central banks can take to control inflation.

Inflation was subdued in China for most of 2012, but with economic growth rebounding since late last year, concerns over rising prices are coming back to the forefront.

China's consumer-price index in February was up 3.2% from a year earlier, accelerating from January's 2% pace. That signals the central bank must be on guard against inflation, Mr. Zhou said—though he said that distortions from the timing of the Lunar New Year holiday, which fell in February this year but in January last year, played a role in the high reading.

China's lower target for money-supply growth this year demonstrates the leadership's emphasis on price stability, he said, and shows that policy is "inclined toward tightening."

### On the Job

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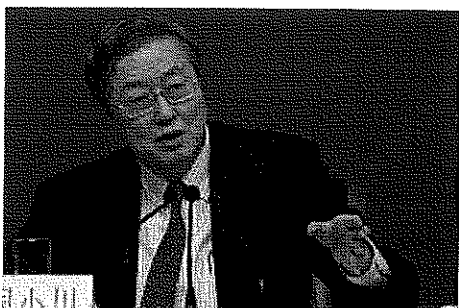
The Wall Street Journal earlier reported that Mr. Zhou is likely to continue his term as PBOC head past the customary retirement age of 65, in a bid to keep policy stable as far-reaching overhauls continue. The National People's Congress, China's rubber-stamp parliament, is

set to vote on Saturday on new heads for various governmental bodies including the central bank.

"The important thing is not whether I personally stay on," Mr. Zhou said Wednesday. "If we follow the correct policies, that will ensure continuity and stability."

Premier Wen Jiabao last week set a target of 13% growth in China's broadest measure of money supply, M2—composed of various kinds of bank deposits. That's down from a 14% target and 13.8% actual growth last year.

"If we can continue to control M2 growth at a reasonable level, there shouldn't be any sudden rise in inflation," Mr. Zhou said.



Agence France-Presse/Getty Images

People's Bank of China Gov. Zhou Xiaochuan at a press conference Wednesday, where he signaled increased concern about inflation

Bank of America-Merrill Lynch economist Lu Ting said that "overall Mr. Zhou seemed to be a bit more hawkish on monetary stance than before, but we see more ambiguity than clarity."

Mr. Zhou also said the PBOC will continue to take measures to rein in property prices, but said this isn't a primary objective of monetary policy. "For property prices, we have some structural policies, which we have been using for years, including down-payment levels, mortgage interest rates, and other measures targeted directly at property," he said. "We will continue to use these measures and in some respects continue to

increase their intensity." But he said these "structural policies" are distinct from overall monetary policy, which is focused more on prices for ordinary goods, as reflected by measures such as the consumer-price index.

—Aaron Back

—Richard Silk contributed to this article.

**Write to Aaron Back at [aaron.back@wsj.com](mailto:aaron.back@wsj.com)**

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