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WASHINGTON, D. C.  
DEPARTMENT OF STATE  
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19 June 1963

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MEMORANDUM FOR: Mr. Walt W. Rostow  
Counselor and Chairman of  
Policy Planning Council  
Department of State

SUBJECT : Prospects for Continued Moderate  
Economic Recovery in Communist China

You may find this recent study of Communist Chinese economic recovery prospects worth some attention. Our analysts conclude that, from the purely economic point of view, China's prospects for achieving status as a major world power in this decade have vanished. They believe that even a moderate recovery over the next five years will depend on realistic rather than ideological management of the domestic economy.



Acting Deputy Director (Intelligence)

Attachment

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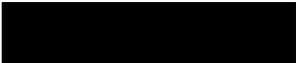
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DEPARTMENT OF STATE

1963 JUN 20 AM 11 37  
Economic Intelligence Report

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PROSPECTS  
FOR CONTINUED MODERATE ECONOMIC RECOVERY  
IN COMMUNIST CHINA



June 1963

CENTRAL INTELLIGENCE AGENCY

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EO 12958, 25X  
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Withdrawal No. 6-13 (70 D 199 Box 4/25)

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Economic Intelligence Report

PROSPECTS  
FOR CONTINUED MODERATE ECONOMIC RECOVERY  
IN COMMUNIST CHINA

  
  
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CONTENTS

	<u>Page</u>
Summary and Conclusions . . . . .	1
I. Background . . . . .	3
II. Economic Performance in 1962 . . . . .	4
A. General Performance . . . . .	4
B. Agriculture . . . . .	5
C. Industry . . . . .	7
D. Petroleum . . . . .	8
E. Foreign Trade . . . . .	9
III. Prospects . . . . .	11
A. Immediate Prospects . . . . .	11
B. Future Economic Policy . . . . .	12
C. Agriculture . . . . .	13
D. Industry . . . . .	15
E. Foreign Trade . . . . .	17
F. Population . . . . .	18

Tables

1. Communist China: Dependence on Imports of Selected Items, 1962 . . . . .	6
2. Communist China: Retained Grain Imports, by Country of Origin, 1961-62 . . . . .	6
3. Communist China: Estimated Supply of Petroleum Products, 1962 . . . . .	9
4. Communist China: Imports and Exports, by Major Commodity Groupings and Sources, 1959-62 . . . . .	10



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PROSPECTS FOR CONTINUED MODERATE ECONOMIC RECOVERY  
IN COMMUNIST CHINA\*

Summary and Conclusions

General economic activity in Communist China improved slightly during 1962, compared with 1961, and the most serious economic difficulties were eased. China achieved a substantial increase in the production of vegetables, sweet potatoes, poultry, and fruit and a slight increase in the production of grain. In industry, production of some priority goods such as agricultural chemicals increased, and improvements were made in the operation of industrial plants. The moderate economic policies that were adopted in the wake of the disastrously overambitious "leap forward" of 1958-60 were continued throughout 1962.

The outlook for the immediate future (1963-64) is for a continuing moderate recovery of industrial output based mainly on the fuller use of existing capacity. Because it depends so heavily on weather and on the morale of the peasants, agricultural production is more difficult to anticipate. Assuming normal weather conditions and a continuation of the present limited concessions to private activity in rural areas, agricultural output should continue to grow slowly. Food supplies, however, will remain stringent.

Faced with overriding problems of feeding a huge and growing population, modernizing agriculture, and raising the level of industrial technology without Soviet support, China's prospects for achieving status as a major world power in this decade have vanished. Prospects for even moderate recovery in the next 5 years depend heavily on whether or not the leadership will contain its strong ideological compulsions and continue a realistic course in managing the domestic economy.

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\* The estimates and conclusions in this report represent the best judgment of this Office as of 15 May 1963.

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I. Background

The fundamental fact faced by economic policymakers in Communist China is the existence of a huge and growing population in combination with a relatively small amount of arable land, a low level of technology, and a small amount of capital plant. Immediately after seizing power in October 1949 the Communist leaders put into operation a program for "forced-draft" industrialization of the economy. Key features of the program for the rapid buildup of industrial capacity and output were: (1) the allocation of an increasing share of national output to investment and (2) the importation from the USSR and the European Satellites of complete equipment and supporting technical services for modern industrial plants.

For this program to succeed, food production had to be continuously expanded at the same time that important resources were being used to build up industrial and military strength. Largely because the Communist regime brought peace and order to war-torn China, food production through 1957 did in fact keep up with the growth of population. The regime, however, by spreading food supplies evenly over the population and by reducing deaths from flood and disease, brought about a rapid increase in the rate of growth of population, and the margin between food production and the minimum needs of the population remained perilously thin.

In 1958 the regime tried to step up the tempo of its industrialization program by launching the "leap forward." The central premise underlying the "leap forward" philosophy was that China's huge and rapidly growing rural population should be treated as a major economic asset. During the period of the First Five Year Plan (1953-57) the Soviet model of industrialization had been followed closely, and a Soviet-type planning and statistical system had begun to take shape. In contrast, the "leap forward" was a Chinese-style economic program. China was to "walk on two legs": at the same time that the industrialization program was to be speeded up, the peasants were to be mobilized into huge new supercollectives, or "communes," and the economy was to be carried forward by sheer weight of numbers.

The failure of the "leap forward" policies is now abundantly clear. It is apparent that the leadership permitted its agricultural policies to become divorced from reality. On the basis of directives from the center, traditional methods of cultivation were replaced by panaceas such as deep plowing and close planting. Overnight, untrained cadres were placed in charge of construction of a huge number of irrigation and flood control projects; many of these projects proved useless or even

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subtracted from production. The indiscriminate use of rural labor in such dubious projects as the small iron furnaces even led to labor shortages at harvest time. This manmade damage to agricultural production was compounded by poor weather in 1959-61.

At first the results for industry under the "leap forward" seemed spectacular, but these short-run successes were achieved at the expense of long-run development prospects. Standards of quality were lowered, the care and the maintenance of equipment were neglected, and political fanatics rather than competent technicians took over the planning and administration of industry. By mid-1960 a pullback from the "leap forward" in industry was overdue. What might have been an organized retreat turned into a rout, however, when the USSR unexpectedly withdrew its technicians and when the regime encountered the worst agricultural crisis in its history.

With failures in agriculture and industry and the loss of Soviet technical help, Peking's hopes of achieving world power status in this decade vanished. The traditional Communist approach of all-out emphasis on expansion of heavy industry ran counter to the realities of the domestic situation and had to be set aside, at least temporarily. Faced with basic problems of overpopulation, backwardness in agriculture, and a low level of technology in industry, the regime was forced during the winter of 1960/61 to adopt economic policies of moderation and retrenchment aimed, above all, at encouraging recovery of agricultural production. The regime then announced that the breathing spell in the economy would last 2 or 3 years.

## II. Economic Performance in 1962

### A. General Performance

In 1962 the moderate economic policies adopted in the winter of 1960/61 were continued. Private activity in agriculture and in rural trade was still permitted. Major industrial goals included the expansion of production to support agriculture and the mining and timber industries. Emphasis was placed on improvement of quality, on reduction of costs, on increases in output per worker, and on better care of equipment.

The communiqué issued after the 10th Plenum of the Eighth Party Congress, which met secretly in Peking on 24-27 September 1962, suggests that the retrenchment and consolidation prevailing in 1961 and 1962 will be generally continued for the time being but that some tightening up of discipline in economic affairs is considered to be necessary to prevent further ideological concessions. Specifically, the Party appears to have decided (1) to retain the concepts "leap forward" and "communes" at least as slogans if not as operative guides to policy; (2) to permit

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no further retreat in collectivization of agriculture, and, as a corollary, to restrict private "capitalistic" tendencies in the countryside; and (3) to retain the recent emphasis on more conservative management policies for industry, policies which are similar to those that prevailed in 1957.

[REDACTED] Official claims [REDACTED] note advances in some areas of production in 1962; [REDACTED] indicate a slight improvement in the supply of some foods and other consumer goods; and weather data suggest slightly better growing conditions during the year for the country as a whole. These bits and pieces, together with Peking's more optimistic outlook since September, indicate moderate improvement in an extremely difficult situation. Even with improvement in 1962, serious problems still remain in every major sector of an economy that probably is no more productive today than it was in 1957.

#### B. Agriculture

The agricultural situation in Communist China in 1962 was slightly improved in comparison with the abnormally low levels of 1960 and 1961. Production of grain in 1962 is estimated to have increased slightly and to have been equal to the 185 million tons\* harvested in 1957, when the population was about 10 percent smaller. Estimates of output are based primarily on weather data, although the probability of a somewhat larger acreage of fall grain crops and slightly increased supplies of chemical fertilizer also have been taken into consideration. The expected level of grain imports by China in the 1962/63 consumption year (July-June) is also indicative of the inadequacy of the harvest of 1962 (see Table 1\*\*). Contracts have been signed for net deliveries of about 3.3 million tons of grain during the first 6 months of 1963 -- about the same as that imported during the similar period of 1962 (see Table 2\*\*\*). The estimated 5 million tons of grain being imported during the entire 1962/63 consumption year amounts to about 4 percent of total food grain supplies. In 1957, however, China was a net exporter of grain.

The further decentralization of authority within the collective farm system in 1962 (the production team of about 30 households is now the basic unit for carrying on day-by-day agricultural activities and for handling the distribution of income) probably had little effect on the output of rice, wheat, and miscellaneous grain. Encouragement by

\* Tonnages are given in metric tons throughout this report.

\*\* Table 1 follows on p. 6.

\*\*\* Table 2 follows on p. 6.

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Table 1

Communist China: Dependence on Imports of Selected Items a/  
1962

	Thousand Metric Tons				Dependence on Imports (Percent)
	Total Availability	Domestic Production	Net Imports		
			From the Soviet Bloc	From the West	
Food grains <u>b/</u>	120,000	115,000 <u>c/</u>	300	4,600	4
Rubber	110	Negl.	Negl.	110	100
Chemical fertilizer (gross basis)	3,500	2,100	Negl.	1,400	40

a. Data are rounded.

b. Food grains include tubers, on the basis of 4 tons of tubers being equivalent to 1 ton of grain.

c. Available for human consumption after an estimated deduction of about two-fifths from a gross output of 185 million tons. This deduction accounts for losses resulting from the milling of grain, from handling, and from damage in transportation and storage and for such nonfood uses as reserves for seed, feed, and industrial requirements.

Table 2

Communist China: Retained Grain Imports, by Country of Origin  
1961-62

	Thousand Metric Tons				
	1961		1962		Total
	First Half	Second Half	First Half	Second Half	
Australia	1,426	1,126	1,001	207	3,760
Canada	956	1,130	1,374	635	4,095
France	27	230	234	284	775
Other	242	334	569	625	1,770
Total	<u>2,651</u>	<u>2,820</u>	<u>3,178</u>	<u>1,751</u>	<u>10,400</u>



the further development of military industries and agricultural chemical industries. It is not known what technological progress was made in 1962 in the type of industries needed to support an advanced weapons program, but increases in the output of chemical fertilizer and insecticides suggest improved technical ability to operate plants in the chemical industry. Nevertheless, there probably are some chemical fertilizer plants as well as other heavy industrial plants -- for example, aircraft, shipbuilding, and truck plants -- that are producing below capacity because of technological deficiencies. These difficulties may exist in the plants themselves or in supporting industries that supply components and materials.

Aside from heavy industrial plants that are having technical and supply difficulties, unused capacity now exists in many major industries. The reason for this situation in light industry is clear: light industry has been unable to obtain the necessary raw materials from agriculture. The reasons for idle capacity in heavy industry are more complex. One important reason in addition to the technological factors mentioned above is that the drastic cutback in the investment program and the sharp decline in industrial output have reduced the need for basic heavy industrial items such as steel, electric power, construction materials, and several major types of machinery.

#### D. Petroleum

It is estimated that the total amount of petroleum products available in Communist China in 1962 was slightly less than the total available in 1959, the last year for which data were published, but supplies apparently were adequate to meet the essential needs of both civilian and military consumers. The domestically produced share of the total amount of petroleum products available [redacted] have increased to about 70 percent in 1962 (see Table 3\*) compared with about 50 percent in 1959. The eight major refineries [redacted] maintained a high level of operation throughout the year. The primary sources of crude oil continue to be the oilfields at Yu-men, Karamai, and the Tsaidam Basin and the shale oil plants at Fu-shun.

Imports of petroleum products are estimated to have declined from 3.2 million tons in 1961 to 1.9 million tons in 1962, with the sharpest decline taking place in imports of motor gasoline -- from 1.0 million tons in 1961 to 0.3 million tons in 1962. The decline in imports of motor gasoline is believed to have been absorbed mainly by the civilian motor transport industry rather than by the military services, whose requirements probably increased late in 1962 because of military operations in Tibet. Communist China continued to rely

\* Table 3 follows on p. 9.

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Table 3

Communist China: Estimated Supply of Petroleum Products a/  
1962

Product	Total Supply	Imports		Domestic Production	
	Thousand Metric Tons	Thousand Metric Tons	Percent of Total Supply	Thousand Metric Tons	Percent of Total Supply
Aviation					
gasoline	60	60	100	Negl.	Negl.
Jet fuel	450	450	100	Negl.	Negl.
Motor gasoline	1,300	320	25	980	75
Kerosine	1,140	500	44	640	56
Diesel fuel	1,230	300	24	930	76
Lubricants	400	230	58	170	42
Residual	1,600	Negl.	Negl.	1,600	100
Total	<u>6,180</u>	<u>1,860</u>	30	<u>4,320</u>	70

a. Data are rounded.

on imports of aircraft fuels and high-quality lubricants, which remained in 1962 at the level of 1961. China has the capability of producing jet fuel, although such production would necessarily reduce output of other petroleum products, and difficulties with quality probably would be encountered. China probably does not have the capability to produce highest aviation gasoline and certain high-quality lubricants.

#### E. Foreign Trade

The economic and political difficulties with which Communist China now finds itself confronted have had a marked effect on its foreign trade. The reduction in agricultural products available for export, the deterioration in Sino-Soviet relations, the cutback in investment, and the decline of industrial output have combined to lower the total volume of trade and to alter sharply its direction and composition. Total trade (imports plus exports) in 1962 may have amounted to \$2.3 billion to \$2.5 billion\* compared with \$4.2 billion in 1959 (see Table 4\*\*). The regime

\* All dollar values in this report are in current US dollars.

\*\* Table 4 follows on p. 10.

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Table 4

Communist China: Imports and Exports, by Major Commodity Groupings and Sources a/  
1959-62

	1959				1960				1961				1962 b/	
	Total	Soviet Bloc c/	Non-d/	Total	Soviet Bloc c/									
Total imports	2,040	1,330	710	2,000	1,200	800	1,440	570	870	1,045	270	775		
Foodstuffs	10	Negl.	10	40	Negl.	40	580	70	450					
Of which:														
Grains	Negl.	Negl.	Negl.	Negl.	Negl.	Negl.	370	20	350					
Sugar	Negl.	Negl.	Negl.	30	Negl.	30	150	50	100 e/					
Raw materials	810	240	570	890	250	640	590	230	360					
Of which:														
Petroleum products	120	120	Negl.	130	130	Negl.	130	130	Negl.					
Rubber	120	Negl.	120	90	Negl.	90	60	Negl.	60					
Chemical fertilizer	70	Negl.	70	40	Negl.	40	40	Negl.	40					
Machinery and equipment	980	910	70	900	830	70	250	220	30					
All others	240	180	60	170	120	50	80	50	30					
Total exports	2,190	1,570	620	1,920	1,290	630	1,460	820	640	1,315	605	710		
Agricultural products	1,110	720	390	870	510	360	400	150	250					
Edible	820	520	300	630	350	280	200	50	150					
Inedible	290	200	90	240	160	80	200	100	100					
Minerals and metals	270	220	50	260	210	50	300	180	120					
Chemicals	90	70	20	80	60	20	60	40	20					
Manufactured goods	720	560	160	710	510	200	700	450	250					
Of which:														
Textiles	620	500	120	630	480	150	570	400	170					

a. Data are rounded.  
 b. Preliminary estimates. Trade with the Soviet Bloc may have been as low as \$800 million or as high as \$1 billion.  
 c. Including North Korea, North Vietnam, and Mongolia.  
 d. Cuba is included in the non-Bloc total. Chinese trade with Yugoslavia was negligible in 1959-62.  
 e. Sugar imported from Cuba.

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is now concentrating on imports of foodstuffs and raw materials; imports of machinery and equipment may have dropped by 90 percent between 1959 and 1962.

Trade with the USSR declined from a peak of \$2.0 billion in 1959 to \$500 million to \$600 million in 1962. To meet annual long-term debt obligations to the USSR, Peking is currently required to maintain an export surplus of about \$180 million in trade between the two countries. A protocol signed in April 1963, however, implied that this surplus was even larger in 1962, indicating that the Chinese deliberately curtailed imports from the USSR while exporting as much as possible. This protocol provided for Peking -- "in accordance with the desire" of the Chinese -- to pay off in advance part of a \$320 million trade debt that had been scheduled to be paid over 4 years (1962-65).

Throughout 1962 the Chinese Communists were actively contacting Western European and Japanese suppliers of industrial products, but few contracts of any size or importance were concluded. China's foreign exchange position remained tight, but the regime managed to meet its obligations promptly and even to make earlier-than-scheduled payments on some debts to Bloc and non-Bloc countries.

### III. Prospects

#### A. Immediate Prospects

Although the Chinese Communists seem to have entered 1963 in a mood of cautious optimism, the outlook for the next year or two is for only a moderate upturn in industrial output, on the order of 5 to 10 percent a year. Some further agricultural recovery seems likely, given average weather, but the depressed agricultural scene colors the entire economic outlook. The loss of crucial momentum during the last 4 unfavorable years has created a gap of formidable proportions, which has to be closed. Simply to restore grain output to a point where per capita consumption could be elevated to the 1957 level would require a production increase of about 20 million tons, and for this level to be maintained in subsequent years would require additional increases of about 4 million tons annually.

The Chinese Communists apparently believe that the point of worst difficulties has passed and that the road ahead, although difficult, should bring continued improvement. For example, they have been confident enough over the food outlook to say that more emphasis should be placed on cotton and other industrial crops, but not confident enough to reduce food grain imports, which are to continue in the first half of 1963 at roughly the same annual rate as in 1961 and 1962. Although increasingly optimistic, Peking apparently believes

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that it is premature to order an all-out production drive and seems to be hoping to lay the foundation for an "upsurge" in 1964. In 1963, for the third year in a row, the economy is to give priority to agriculture and to concentrate on "readjusting" industry. According to Peking, readjustment in industry in 1963 means giving support to agriculture, strengthening the mining and timber industries, and raising the technological level in order better to meet agricultural and military needs.

B. Future Economic Policy

The outlook for the Chinese Communist economy over the next 5 years or so will be heavily influenced by the policy decisions of the leadership and by their ability to carry out these policies successfully.

[REDACTED] economic failures have caused a general loss of confidence in the leadership. Even those groups who are committed to the regime and whose loyalty remains fairly strong have been affected. These include Party members (17 million), students (10 million in secondary and higher education), and even military personnel (3 million). Peasant apathy and distrust of Party policies probably is near the alltime high. In industry, in spite of the adoption during the past 2 years of moderate policies designed to correct "leap forward" mistakes, the morale of workers [REDACTED] is still low.

The future trend in economic policies is still obscure and is an important element in the uncertainty of future economic developments. The present priority accorded agricultural development is unique to a Communist state, and many leaders in Peking probably will become increasingly impatient with continued deferral of the national goal of building rapidly a modern industrial and military power. There are strong radical as well as moderate elements in the Party leadership, and although both factions seem to be agreed that "leap forward" methods were wasteful, they can be expected to disagree over such matters as how much reliance should be placed on ideological and organizational solutions to economic problems. The radicals probably would like to introduce more experimentation in economic organizations and programs. The moderates as a whole probably would be satisfied with the general Soviet-style approach followed during most of the First Five Year Plan, but they also have a liberal wing, which early in 1962 indicated that it would like to see more stress on profit incentives and a freer type of socialism -- although this kind of thinking has not been in evidence since September 1962. There is little chance that the liberal views will be adopted, but they may serve as a check on the more extreme radical elements in the leadership.

In November 1962, several high-ranking officials, including four Politburo members, were appointed to the State Planning Commission.

It is probable that the augmented commission is serving as a task force to work out guidelines for a Third Five Year Plan to run from 1963 through 1967. The outline of such a plan could be announced at the next session of the National Peoples Congress, which is scheduled to convene in the second quarter of 1963. By publishing a plan for the next 5 years, even though it probably will be general and qualitative rather than specific, the Party may hope to regain a measure of public confidence. The general lines that may be adopted for agriculture and industry have been suggested in articles published since the 10th Party Plenum of September 1962.

C. Agriculture

The regime intends to continue to give priority to agriculture and at the present time appears to be thinking in terms of an agricultural program that will require 20 to 25 years. Moderation and comparative reasonableness are evident both in the gradualness implicit in the effort and in the apparent emphasis on research and extension activities and on production of chemical fertilizers. The question, however, is not whether such a program will bear fruit -- the scope for improvement is so great that it could hardly avoid doing so -- but whether increases of the magnitude required will be forthcoming quickly. It is believed that they will not, in spite of China's being in a position to draw on and profit by the experience of such Asian countries as Japan and Taiwan, which have dramatically increased farm output in recent years.

The Japanese and Taiwanese cases point up two basic factors regarding agricultural modernization. The most widely recognized factor, of course, is the prime importance of chemical fertilizers under Asian systems of intensive cultivation. The "agricultural miracles" in both countries were directly associated with the increased use of fertilizer, and in both countries the rate of fertilizer application far exceeds that in Communist China, as follows:

	Kilograms of Chemical Fertilizer Applied per Planted Hectare (Nutrient Content)
China (1962 estimate)	5
Taiwan (1960/61 crop year)	110
Japan (1960/61 crop year)	228

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Frequently overlooked is a second factor: that agricultural inputs are closely interdependent and that they must be developed in conjunction if they are to produce maximum results. Thus increased yields in Taiwan and Japan reflect not only the heavier use of chemical fertilizers but also many other influences, including improved cultural practices, new crop varieties that are responsive to fertilization, the wider use of pesticides, and better control of water.

The immediate outlook for Communist China is not favorable with respect to any of these factors. China's ability to produce chemical fertilizers is still negligible and has been affected markedly by the current economic crisis and the dispute with the USSR. The installed capacity of chemical fertilizer plants amounts to no more than about 3 million tons (gross basis) most of it provided by the USSR, and during 1962 a combination of poor operating procedures, breakdowns of equipment, and shortages of raw materials is believed to have kept output nearer 2 million tons. Up to the present, China has made little progress in construction of new fertilizer plants by its own efforts, although the regime during the past several years has proclaimed a high priority for building such plants. In 1959 and 1960, construction of eight new plants was begun, each with a capacity of about 100,000 tons (gross basis). Thus far, only two of these plants have been completed; their construction took nearly 3 years; and in both plants, technical difficulties are believed to be causing faltering production. Three more new plants may be completed during 1963, but they also are expected to experience problems for a year or more.

In view of the difficulties that the Chinese have experienced in implementing even this limited expansion program, substantial increases in the availability of fertilizer seem to be out of the question during the next few years. Some increase may be obtained through expanded imports from the West (at a cost of at least \$40 per ton) and from manure as the animal population recovers, but truly significant additions can only come from domestic chemical output. If the Chinese relied upon imports to provide an annual fertilizer supply of 1 million tons (gross basis), the total cost in scarce foreign exchange would be at least \$400 million for a 10-year period. It thus seems unlikely that they will place heavy reliance on imports to meet their long-term fertilizer requirements.

Fertilizer-response estimates for China rest on extremely spotty evidence; a ratio of 2 tons of grain for each additional ton of chemical fertilizer (gross basis), however, is a very rough rule of thumb. On the basis of this ratio, in order to produce 2 million additional tons of grain each year, or one-half of the annual increment needed to keep pace with population growth, China would have to bring into production the equivalent of ten 100,000-ton plants each year.

- 14 -

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That the Chinese Communists themselves believe such a target would prove beyond their capabilities for many years to come is attested to by their objective of elevating fertilizer production to 8 million tons (gross basis) in 10 years, presumably by 1972. This goal apparently represents what Peking feels to be the best that can be obtained from the substantial effort recently announced, including conversion of at least 100 existing machine-building facilities to the manufacture of equipment for fertilizer plants.

Importation of fertilizer plants is a possible alternative. Complete plants purchased abroad with a total annual capacity of 1 million tons (gross basis) of fertilizer probably would cost \$100 million to \$150 million, however -- a sizable amount in view of China's tight foreign exchange situation.

Some increases in output of course may be expected to accrue from such complementary inputs as better water control, pesticides, and improved crop varieties, but the magnitude of these gains probably will be modest for some years. It took Japan and Taiwan more than 50 years to build up the technology and the scientific understanding that underpins the productivity of their agricultural sectors. Although Communist China is in a position to take over and profit from much of this knowledge immediately, to apply it to local conditions will be a time-consuming and complex task, one that will involve patient observation and testing for a number of years. It is also a task that China is poorly equipped to undertake. Because industry took preference over agriculture in the regime's early investment and training programs, China now finds itself with fewer than 1,000 competent agricultural scientists. Until these few scientists begin to be joined by others, perhaps in 3 to 5 years, they will be devoting most of their efforts to laying the foundation for future gains.

It is not possible to say how beneficial the recent decentralization of controls will be on production in rural China, but it is worth noting that most of the new-found zeal of 1962 is believed to have been directed by the peasants to their private plots and not to the collectively cultivated land and that the greater part of the recent increase in food supplies is most likely attributable to private, not collective, production.

#### D. Industry

The current emphasis on industries producing goods for agriculture and for consumers is likely to continue for at least the next year or so. Also, some branches of heavy industry that cannot produce enough to meet the requirements of the economy are likely to be allocated increased resources for expansion of plant and technical competence.

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Industries that probably will be emphasized include mining, producers of chemicals and machinery for agriculture, producers of some chemical raw materials for light industry, and industries that will help to broaden Chinese Communist technological capabilities. The latter group of industries will be needed to develop a native capability for producing a wide variety (but not necessarily a large volume) of complex machinery and selected metals and chemicals, which in turn will be needed in the development of chemical fertilizer industries and the production of nuclear weapons and guided missiles.

Prospects for resuming industrial growth are contingent on recovery in agriculture. Agriculture historically has been the key sector of the Chinese economy, but today it is, as never before, the pivotal component. If a level of agricultural recovery satisfactory to the leadership is achieved -- and this level might well be less than the per capita level attained in 1957 -- industrial production could be pushed rapidly for a year or two because idle capacity exists in many industries. After existing capacity is put to use, growth in industrial production would slow down if present goals for industry -- which stress variety and quality rather than quantity -- and Peking's go-it-alone policy are retained. The slogan of overtaking the UK in 10 to 15 years in total production of basic industrial items is now dead. Similarly, the regime has dropped its one-time goal of producing 40 million tons of crude steel by 1967, and it probably would be satisfied now if it attained half that amount.

Economic elements important to the Chinese Communist advanced weapons program include the extent of Soviet aid, Chinese industrial capabilities, and economic priorities. Soviet technical assistance to industry -- including services of technicians and scientists, technical data, and assistance embodied in machinery -- has been very small since 1960. Independent Chinese technological capabilities in industry seem to have been overrated in the past, judging from the many reports received in 1961-62 about difficulties in operating existing industries and in completing even the simpler construction projects abandoned by Soviet technicians in the mid-1960 exodus. This situation of extremely limited technical resources suggests that the Chinese must allocate their relatively few competent scientists and technicians with great care to activities of the highest priority.

[REDACTED] To a certain extent, the development of industries supplying materials and machinery to the advanced weapons program must compete for scarce resources with the development of industries supporting agriculture, which is now another high-priority area. In view of the slight improvement in

- 16 -

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the agricultural situation, however, it is likely that some limited program for advanced weapons development is now accorded top priority.

#### E. Foreign Trade

Prospects for increasing the foreign trade of Communist China are limited, partly because of Peking's heightened desire for self-sufficiency. The Sino-Soviet trade pact for 1963 was signed in Moscow on 20 April 1963, after nearly 5 months of talks. No indication of the level of trade anticipated this year was given, suggesting that Sino-Soviet trade in 1963 will continue at roughly the low level of 1962. Although China may turn to the West to replace some Bloc sources of machinery, such purchases probably will be selective. The Chinese will continue to be reluctant to buy machinery that they cannot maintain and repair themselves. Moreover, according to a member of a Chinese technical mission that recently toured Western Europe, it will be Chinese policy to import technology mainly by importing prototypes, including whole plants, to be copied in China, a practice that the Chinese have used to some extent in the past. In view of the backwardness of the Chinese machine building industry, a policy of importing primarily prototypes would be a slow method of building up industrial technology.

The outlook for trade with Japan is obscure in spite of the signing of a long-term trade agreement in November 1962. Japan could be a highly profitable market for low-priced, bulky minerals such as salt, magnesite, coal, and iron ore that are hard for Communist China to sell elsewhere. Perhaps for political reasons, however, China has not made large quantities of such products available at attractive prices and conditions, and erratic and unstable political relations have discouraged potential Japanese industrial users from regarding China as a source for large quantities of such products. Nevertheless, Sino-Japanese trade has been rising slowly and may continue to expand.

Further disruptive effects on China's economy would follow a complete Sino-Soviet break, but the Chinese could recover from this break if they were willing to pay the economic and political costs of increasing their trade with non-Bloc countries. About \$350 million to \$450 million of the exports to Bloc countries in 1962 could be diverted to non-Bloc markets, an amount at least equal to Chinese imports from Bloc countries in 1962. The Chinese could import from non-Bloc countries all of the chemicals and metals imported from the Soviet Bloc in 1962 and nearly all of the machinery and equipment, the petroleum products, and the industrial raw materials. Large-scale diversion of Chinese trade from Bloc to non-Bloc countries would involve initial costs to the Chinese of developing new markets for their exports and new sources for their imports and would require costly and

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time-consuming adjustments to Western specifications for most machinery imports. Chinese attempts to expand exports to non-Bloc countries, after an initial adjustment period, would run into increasing difficulties because the marketing of greater quantities of Chinese products would disrupt some Western commodity markets. In addition, large-scale expansion of trade with non-Bloc countries would place restraints on Chinese foreign policy, including the subordination of political goals in trade with Japan, and would require the Chinese to supply technical data to Western businessmen, to accept non-Bloc technicians in China, and to send Chinese personnel outside the Bloc for training.

F. Population

Regardless of what approach the Chinese Communists may take to economic recovery in the next 5 years, the population pressure on food resources will continue to be a major underlying problem. The rate of population growth averaged an estimated 2.4 percent from 1953 through 1958, slowed down to 1.5 to 2.0 percent in recent years, and probably will rise if average diets improve. There is little that the government can do to control the birth rate effectively, especially in rural areas where social beliefs are hard to change and medical services are poor. Since the spring of 1962 a low-key campaign has been conducted in urban areas to encourage late marriages and family planning, but this policy will have only a negligible effect on the national birth rate. The idea of birth control is not popular among Marxists in any case, and the stress in China, since the 10th Plenum in September, on increasing labor productivity in both industry and agriculture suggests that the leadership continues to hold the orthodox view which regards population primarily as a productive asset rather than a problem.

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