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29 SEP 1950

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Document No. 001  
 NO CHANGE in Class.   
 DECLASSIFIED  
 Class. CHANGED TO: TS S C  
 DDA Memo, 4 Apr 77  
 Auth: DDA REG. 77/1763  
 Date: 25/1/78 By: 023

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~~TOP SECRET~~**H I G H L I G H T S**

As the time when UN forces in Korea would reach the 38th Parallel grew appreciably nearer and North Korean forces were being withdrawn to defensive positions on the border, the world still waited anxiously for a UN decision on the future disposition of Korea as well as for some firm indication of the steps the USSR would take to keep control of North Korea.

Meanwhile, the Communist threat in Indochina was increasing. Rebel attacks on French border posts were continuing and served to point up the vulnerability of the French military position (see page 2). If these attacks develop into a coordinated, large-scale Viet Minh offensive, an action which may soon be within Viet Minh capabilities, French maintenance of control over Indochina--by means of their own forces alone--will be seriously threatened. Despite this growing threat to their military control, the French have been slow to implement their announced program of expanding the Vietnamese Army, apparently fearing that such a step would weaken their ability to contain Vietnamese nationalism.

As the Western Powers continued to discuss the vital question of European rearmament, they were beset by a number of economic problems, including the prospect of further delays in a strengthened export control program (see page 5), a stiffened German attitude in negotiations on the Schuman Plan (see page 6), and the specter of inflation in Western Europe (see page 6).

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## INDOCHINESE MILITARY DEVELOPMENTS

**French Vulnerability** The fall of the isolated French border post at Dongkhe, coupled with a series of attacks on other posts in Tonkin, points up the vulnerability of the French military position. Although these attacks do not necessarily herald the start of the long-awaited rebel offensive, the French are already being pinned down at widely separated points and must rely on air transport to reinforce the points under attack. The Viet Minh action at Dongkhe was undertaken by an estimated six battalions and was preceded by artillery preparation on a much larger scale than that used in similar strikes last spring. If these attacks develop into a coordinated, large-scale Viet Minh offensive, an action now well within Viet Minh capabilities, it is doubtful whether the French (even if supplied with US military aid) would be capable of maintaining control over Indochina with their own forces.

**Vietnamese Army** Despite the growing threat to their military control, the French have been slow to implement their avowed program of expanding the Vietnamese Army, apparently still confident that acquisition of US arms will enable them to achieve military victory. An expanded Vietnamese Army with greater responsibilities not only would strengthen Indochina's defenses, particularly with regard to maintaining law and order in rear areas but, by demonstrating French willingness to grant greater independence to the Indochinese, would be a substantial step toward gaining the broad popular support essential to suppressing the increasingly powerful Viet Minh insurgent movement.

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**French Obstructionism** Current French actions regarding plans for an expanded Vietnamese Army apparently stem from the fear that creation of such a force would threaten French ability to contain Vietnamese nationalism within the bounds so far imposed. In addition, the French actions demonstrate the deep-seated distrust felt by most French officials toward the Vietnamese. Most of the "practical" objections being raised by the French to expanding the Vietnamese Army would not be insurmountable if the French were not so anxious to preserve their present position and so fearful of granting the Vietnamese more power. (Even full cooperation by the French in increasing the Vietnam Army would not jeopardize French control, which would be assured by the 8 March Agreements which guarantee to France the final decision on military, diplomatic, and financial matters affecting Vietnam.)

**Major Problems** Thus far the French have adopted a cautious policy toward the arming of Vietnamese troops. Since 1946, only four all-Vietnamese battalions have been activated; the regular Vietnam Army theoretically comprises nine battalions, which cannot be used as independent units because the Vietnam Army has no communications, quartermaster, medical, or ordnance services. Only five of these battalions are operational with French Union forces. French reluctance to expand or strengthen the Vietnam Army is indicated by insistence on allocation and distribution of US military aid under French control, failure to make plans for necessary financing, inability of French officials to agree on a course of action or policy, and refusal to expand local militia. Although the French are themselves probably unable either to finance an expanded Vietnamese Army or provide the necessary military training, they have formally opposed the attachment of US military instructors and technical experts to the Vietnam Government. Meanwhile, high

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**T O P   S E C R E T**

French officials disagree among themselves regarding the Vietnamese Army, not only as to the need for such an army but as to the measures necessary for its formation. In addition to lacking faith in the ability and integrity of Bao Dai to direct a Vietnam Army, French officials have until recently consistently opposed expanding local militia, despite the notable successes achieved by the North Vietnam militia organized by Governor Tri. Since the increase in Viet Minh pressure on northern border posts, however, High Commissioner Pignon has promised Governor Tri that militia strength would be increased if a means to finance it can be arranged. Unless US aid is made available for this purpose, there will be little practical effect from this ostensible change in French policy.

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**T O P   S E C R E T**

**TOP SECRET****WESTERN ECONOMIC PROBLEMS**

**Export Controls** Early agreement by the ERP countries on an expanded program of export controls on strategic items is not likely to result from the recent decisions of the Big Three Foreign Ministers meeting in New York. The remanding of the whole question to "the technical level" has once again set the stage for a long grind of negotiations. Agreement on an ERP-wide export control list or any substantial additions to the present international control list will tend to be obstructed by three of the decisions reached at New York. The agreement to have British, French, and US representatives draw up the initial list will create difficulties because the other ERP countries may feel slighted at having been excluded from the discussions and, when requested to approve, may raise charges of pressure tactics. Acceptance by the Foreign Ministers of the British concept that quantitative controls should be restricted to "selected items" required "in key industrial sectors" will seriously limit the number of additional items subjected to export control. Finally, the negotiators have been provided with a convenient excuse for excluding strategic items; the Foreign Ministers have agreed that in considering which items to place on the control list, account should be taken of what effect the proposed controls would have on the economy of Western Europe. Despite these obstacles to early agreement on a more stringent export control program, the flow of war-potential goods to the Soviet orbit may slacken as a result of increased requirements for expanding Western defense programs and a stricter British enforcement of export controls following the recent parliamentary debate of the government's policy on the matter.

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**Schuman Plan** As negotiations continue on the Schuman Plan, the Korean war and the recent Foreign Ministers Conference have produced a marked stiffening in the attitude of the German delegates which, if persisted in, may seriously threaten the original concept of a supra-national authority. The Germans feel that their international position has been improved by the Korean war. The Germans not only expect a greater German rearmament effort but are already tending to regard the Korean war as sufficient reason for removing restrictions on German steel production; in fact, steel plants are already accepting orders at a rate far beyond present limitations on production. The Germans are therefore trying to use their stronger bargaining position to retain a national competitive advantage within the proposed single market, apparently believing that they no longer need to make concessions in the Schuman Plan negotiations. They are insisting that their own high tariff be adopted against outside countries and oppose an increase in German wages, especially in the coal mines, as well as an increase in German coal prices that might benefit the coal industries of other countries. Although the stiffened German attitude may be a tactical device to gain advantage in the forthcoming negotiations for revision of the Occupation Statute, the danger is increasing that the Germans may effectively sabotage certain important aspects of the Schuman Plan.

**European Inflation** One of the most serious potential repercussions of increased world tension and consequent NAT rearmament is a renewed specter of inflation in Western Europe. Early indications of inflation are already apparent in some Western European countries, and there has been a marked rise in key raw materials prices following the Korean war. The European governments, including the UK, as yet show little disposition either to retrench financially

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by cutting non-essential expenses or to redirect their economic recovery programs in order to minimize the inflationary impact of rearmament. Although the rearmament program can probably be achieved without significantly lowering living standards, largely through increased productivity in the NAT countries; these countries must take more active measures to maintain financial stability and must modify their recovery programs if they are to prevent renewed inflation that could threaten the Western rearmament effort.

**Aid to Asia** The Commonwealth consultative conference on economic aid to Southeast Asia which convened in London on 25 September faces the central problem of financing a comprehensive plan for capital development in Southeast Asia at a time of increased defense expenditures in the UK and Australia. As planned last May at the Sydney Commonwealth meeting, the conference's discussion of Australia's proposal to foster capital development will follow lines suggested by detailed questionnaires returned by the intended aid recipients. The general report based on these questionnaires places primary emphasis on increasing food and agricultural production and on the necessity for internal financing. Although it is generally anticipated that the cost of an effective program to stabilize the economic and political situation in Southeast Asia will be in excess of present Commonwealth capabilities, assistance by international agencies and more advanced countries will be viewed as but one element in the total picture and efforts to enlist US aid may be deferred pending exhaustive screening of individual programs.

**Air Transportation** The recent reallocation of European routes for PAA and TWA has caused considerable alarm in France, and in the forthcoming discussions between the US and France of US air traffic rights the French may insist on

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limiting US commercial traffic. Failure of the US to agree to a satisfactory compromise might even result in the abrogation of the US-French bilateral agreement. If the US is forced to accept traffic limitations for PAA and TWA, not only will these airlines require increased government subsidies but a precedent will have been established for the restriction by other countries of US air operations on international trunk routes. European airlines, operating in a crowded and highly competitive field, have been searching for means to reduce financial deficits; the US reallocation of routes will intensify US competition with European carriers, and in the case of France, will increase US flights between Paris and Rome. France, however, may be willing to postpone the issue by agreeing to a compromise similar to that recently accepted by Brazil whereby US airlines will "voluntarily" reduce frequencies while statistics are compiled to permit re-examining at a later date the capacity offered by carriers of both countries over the routes concerned.

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**T O P . S E C R E T**

**LOCAL DEVELOPMENTS**

**ITALY**

**Cabinet Changes**      Prospects for broadening the base of the Italian Cabinet have increased as a result of the recent shift of the Unitary Socialist Party (PSU) from a policy of neutrality to one of active opposition to the USSR. Since the outbreak of the Korean war, Premier De Gasperi has sought the widest possible approval for Italy's clear-cut association with the West, and the PSU's recent decision would permit him not only to include that party in his Cabinet but, as a counterweight, to offer a seat to the conservative Liberal Party, which has consistently supported Italy's pro-Western policy. Such a broadened Cabinet, united in realization of the danger of Soviet aggression, could act with greater decisiveness in support of the Western defensive effort, but would probably cause further delays in much-needed socio-economic legislation. The dominant conservative group of the Christian Democratic Party could use the broadened Cabinet as an excuse for such delays. Moreover, the diversity of views represented in the Cabinet could widen the area of disagreement over such controversial measures as land and tax reforms, and make it more difficult for the government to propose a common, agreed-upon legislative program to Parliament.

**THE PHILIPPINES**

**Cabinet Shuffle**      Several new appointments and further shuffling of the Philippine Cabinet may temporarily strengthen its prestige but the prevailing inexperience and corruption in the government will seriously limit efforts of the new appointees to improve governmental

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## THE PHILIPPINES

efficiency. The appointments actually reflect President Quirino's continued preoccupation with strengthening his personal political position rather than a genuine attempt to enhance the quality of the government. Quirino apparently feels that appointing Vice President Lopez as Secretary of Agriculture and Natural Resources and Lopez' relative, Salvador Araneta, to a newly-created portfolio as Secretary of Economic Coordination will tend to make them less inclined to criticize his administration. The only appointment apparently based purely on merit is that of the new Secretary of Health, Salcedo, whom US officials in the Philippines regard as excellently qualified.

## BURMA

**Moderates Win** The recent expulsion of pro-Communist leaders of the Burmese Trade Union Congress (TUCB) from the Anti-Fascist People's Freedom League, the principal political organization supporting the Burmese Government, indicates that the moderate leadership of the League is determined to eliminate all disruptive influences. Moreover, since the TUCB is affiliated with the Burma Socialist Party, the dominant component of the League, a further showdown between moderates and extremists in the Party seems inevitable. Although the influence of the extremists extends to all levels of the government, their sympathizers constitute a minority, and lack of widespread political and military support precludes the usual reversion to underground operations. A new party formed by the pro-Communists, however, would in all likelihood have the support and encouragement of the Chinese Communist Embassy in Rangoon and could gain strength rapidly if widespread disillusionment with the existing regime should develop.

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**T O P S E C R E T**

**KOREA**

**Military Tactics** As enemy resistance lessened all along the old Pusan perimeter, it is becoming increasingly clear that the North Korean high command intends to make its final defensive effort north of the 38th Parallel. The rapid UN advances in the south cannot be attributed solely to the disintegration of North Korean forces following the Inchon landing and have been made possible largely because as many seasoned combat troops as possible have been withdrawn, leaving only sufficient troops to engage in delaying tactics in key communications centers. Present estimates indicate that the enemy will succeed in withdrawing as many as 30,000 well-trained troops in organized units. These troops will probably man the extensive defensive positions along the 38th Parallel and will be used as cadres for new divisions formed from training centers in the north for a final defense effort.

**BRAZIL**

**Election Prospects** The race for the presidency in the 3 October elections in Brazil appears to have narrowed down to ex-dictator Getulio Vargas and the government-sponsored candidate, Cristiano Machado. Although the political situation remains in complete turmoil, with the major factor of confusion being the multiplicity of local, state, and national "deals" among the political parties, Vargas seems to have gained considerable support throughout Brazil. Barring extraordinary last moment maneuvers by President Dutra's followers or Gomes, the third major candidate, throwing his support to Machado, Vargas appears to be the candidate most likely to win the elections. At this time the extent or direction of Vargas'

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## BRAZIL

possible opposition to US interests cannot be determined. The ex-dictator's campaign equivocations have made it clear that he is still essentially a demagogue and an opportunist. Thus far, he has committed himself only to promote the social welfare and economic development of each locality in which he has spoken. In international matters he has adopted a "center position" apparently similar to Peron's third position. Vargas is thus free to consider, in the light of future developments, such important matters as cooperation with the UN in regard to Korea, the development of Brazil's natural resources, and his stand on the entrance of foreign capital into Brazil's industries and mining and petroleum fields. It is almost certain that Vargas would not take a position openly hostile to the US, but he could and might reverse Brazil's past inclination to be cooperative with the US, particularly in economic matters.

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