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INTELLIGENCE HIGHLIGHTS

WEEK OF 20 JANUARY - 26 JANUARY 1948

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Operation "Crank-up" apparently to be launched. The US member of the FEC has made a statement to that body that the US is planning measures to make Japan "self-supporting at the earliest possible time". In this connection, the Army is to ask Congress for funds for the fiscal year beginning 1 July not only to supply necessities for the Japanese people but also raw materials, spare parts, and other items required for the expansion of peaceful production.

This may be the first official announcement of "Operation Crank-up", a plan variously rumored throughout the latter half of 1947. Under "Operation Crank-up", the US, it has been said, would lend Japan up to a billion and one-half \$ US for the rehabilitation of the Japanese economy.

At the least, the US statement to the FEC is a recognition that Japan will continue to be a drain upon US resources until it can be put upon a self-supporting level. This goal, however, cannot be attained until Japan is able to enter actively into the export market; Japan's economy is geared to foreign trade. In the past, Japan customarily imported raw materials or semi-manufactured articles and processed them for export. Hence, it needs primarily external aid for the procurement of imports for processing. This the US Congress is apparently about to be asked to take under advisement.

Zaibatsu banks escape dissolution. It is reported that the Zaibatsu banking interests will not be subjected to dissolution measures to the same extent as other Zaibatsu interests. The reason for the exemption is said to be the importance of credit facilities in the rehabilitation of the Japanese economy.

Before the war, the Zaibatsu controlled the banking structure of Japan and thereby were enabled to extend their active business trusts. Apparently, the need for strong un-hampered credit facilities in the crucial months ahead has led to at least a postponement of the break-up in "excessive economic concentration" so far as the banks are concerned. Whether Zaibatsu interests will continue to control the banking structure is extremely doubtful, however.

Inflation in Japan. Further analysis of the inflationary tendencies in Japan shows that the fears of a runaway inflation leading to economic crisis in the immediate future are exaggerated

The March 1946 figure of 12 billion yen note issue appears to have been an

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abnormal one; the official figure of note issue as of 31 March 1946 was 23 billion yen. Hence note issue had multiplied approximately 10 times from 31 March 1946 to the end of 1947. This compares with a 30 times increase in CN dollars during the same period.

For the year 1947 through August, increase in note issue, effective price index and wages of mining workers (underground) appear to have kept apace (approximately 2 1/2 times). Hence, the inflation appears to have been kept within bounds. Nonetheless, labor does have cause to complain. Average wages of other workers during the same period increased only about twice; underground miners are favored. Governmental employees who cannot bargain collectively and are kept to a fairly rigid wage base are particularly hurt. Further, wages customarily lag. So long as the industrial level remains fairly constant, labor will be squeezed by the increasing prices. Nevertheless, the situation continues critical. Increasing note issue together with a low industrial level must have serious economic consequences. Operation Crank-up is intended to obviate these.

KOREA

Future Soviet capabilities. The recent Soviet refusal to permit the UN Commission to operate in North Korea should not be taken as an indication of lack of Soviet confidence in the survival-power of its puppet North Korean People's Committee. Soviet boycott was quite clearly indicated from the time the subject was placed on the UN agenda, and the failure of the USSR to execute a diversionary maneuver for the purpose of camouflaging its defiance of a UN resolution can in no sense be attributed to a lack of political resources occasioned by loss of the diplomatic initiative to the US.

The USSR is in continuous process of stripping down its armed forces in Korea to a point where unilateral withdrawal is an imminent capability, and of increasing Korean participation in the North Korean People's Committee to the point where it is capable of emerging full-blown as an "autonomous" state. The Kremlin is clearly committed to the policy of eventual domination of all of Korea and has apparently decided to utilize the People's Committee as a base for this expansion. Its recent actions indicate that it has discounted the UN Commission, together with "world opinion" which the Commission represents, for what they are worth. It is probable that the Kremlin will continue for the present its policy of giving the US "enough rope" even to the point of suffering the US to establish an independent South Korean Government, since it probably believes that US forces would then be withdrawn, leaving the infant South Korean regime defenseless. At such a juncture the USSR would be found quite prepared to carry out its self-imposed commitment of "simultaneous withdrawal" since it could then let nature, in the form of the North Korean People's Army, take its course. Such action would be based on the assumption that the only possible US counter-move would be that of a formal protest in the UN. On the other hand, the present Soviet policy possesses the distinct virtue of avoiding any weakening of the USSR's position in North Korea, thus leaving the Kremlin prepared to counter any move to strengthen the US position in the South.

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CHINA

Military

There was no major military activity in Manchuria during the past week. The Communists were apparently building up rear area stockpiles in preparation for another campaign and the Nationalists were initiating a new command setup, once again separating the military and the political leadership. The military portion of the Nationalist Manchurian command will be vested in Wei Li-huang, who is highly regarded in US circles as a result of his successes during the latter phases of the Chinese campaigns in Burma. He is said to have a very strong position in Army politics and to be "acceptable" to the Kuomintang Clique.

Military activity in North China was centered around Foching, with both sides reportedly sustaining heavy casualties and in Shantung, where the Communists continue to return to those base areas from which they were driven last year. Communist units in Shansi countered the movements of Yen Hsi-shan by penetrating to within ten miles of Yen's capital at Taiyuan.

[redacted] the Communists in the Taihang region (E. Shansi) openly state that their primary military target for 1948 is to carry the civil war into, and south of, the Yangtze River valley. The great majority of the Communist regulars from the Taihang area have already moved into Hupeh, where Liu Fo-cheng is presently engaged in trying to cut river communications from Szechwan to the east coast. 25X1

Internal Political

The control of the Chinese National Government continues in the hands of the right-wing extremists. Legislative Yuan elections appear as completely proarranged and controlled by the Government as were the National Assembly elections, with popular cynicism and lack of interest even more in evidence. The most noteworthy difference is that while the previous elections were almost entirely run by the CC Clique — which took a majority of seats and dictated the disposition of the remainder to other Government factions as well as minority parties — the present elections reveal that this time more control will be shared by other rightist groups. The San Min Chu I Youth Corps, Hsuan Tieh-wu's Shanghai Garrison Headquarters, the Bureau of Investigation and Statistics' secret police, have built up their election machines and assured themselves, in Shanghai at least, of a larger share of the spoils than previously. Preliminary information from the provinces, however, indicates that in Kiangsu and Chekiang the CC Clique will again dominate completely.

The Chinese press, hungry for news fit to print, found a welcome outlet in the Kowloon incident which ended in violence in Canton and demonstrations in Shanghai. The offense to Chinese sensibilities found expression not only in the volume of the news coverage but in editorial comment in newspapers of all shades of opinion. On every side warning was given

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the British that unless the "brutal insult" was righted popular sentiment might be more forcibly expressed. The uproar extended even to Ta Kung Pao, influential Chinese newspaper which normally maintains a relatively rational and dispassionate attitude. In general, the untoward amount of attention given this minor incident was a diversionary tactic to keep public attention focussed on a foreign issue, while internal matters became increasingly bad (see also "External Political" below).

External Political

Canton-Shanghai disorders. Britain has demanded full compensation for losses at Canton and full enquiry into the identity of organizers and participants in the attack. China has claimed full compensation for the eviction of the Kowloon squatters. Both Governments refrained from mentioning the counterincident.

The Embassy reported on 23 January that Chinese authorities were reluctant to adopt strong measures to suppress the Canton-Shanghai disorders because of the widespread anti-British and anti-US feeling, which had been influenced by "Government dominated" propaganda. Thus strong measures would expose the Government to charge of failure to resist imperialist aggression. Also despite expressed Government intention to safeguard foreign lives and property, anti-British propaganda continues unabated with implied inclusion of the US as likewise imperialist. The Consul-General at Canton has exchanged communications with Governor T.V. Soong on necessary protective measures to US and other foreign lives and property, and is dissatisfied with the Governor's assurances, since the latter lacks the support of many high level leaders in South China.

A Nanking United Press story of 19 January reports Chinese sources as saying that the Canton outbreak was intended inter alia as a reprisal for the sanctuary afforded by the Hong Kong authorities to Marshal Li Chi-shen and other dissidents. In this connection it may be noted that the Hong Kong Government last year gave Li Chi-shen several warnings that he would be ousted from the colony if he continued to violate the terms of his admission there which included abstention from "caustic criticism of a friendly government".

Possible Sino-Soviet rapprochement. The Nanking Embassy reports that on 23 January General Cheng Kai-min (whose general reliability is questioned) states members of the Political Science Group now strongly favor rapprochement with the USSR as means of insuring China's neutrality in an anticipated US-USSR war and desire that Chiang Kai-shek go abroad so that he will not be an obstacle to such a rapprochement. The Embassy further reports that Soviet Military Attache, General Roschin, allegedly had suggested Soviet good offices in ending the civil war. Coupling these two reports, the Embassy believes that it is possible a Soviet mediation offer has been made and that the deteriorating military position has disposed certain elements in the National Government to accept.

Travel Permits. Hollington Tong, of Government Information Office,

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states that possession of a resident (entrance) permit will enable a national of a foreign state which has a treaty with China to travel in that country. Non-treaty nationals and stateless persons must apply to local police stations for travel permits.

Atomic Energy Commission. In an attempt to break the deadlock between the USSR and the Commission majority in the UN Atomic Energy Commission Working Committee, Dr. Wei Hsieh-jen, adviser to the Chinese delegation, on 22 January offered a compromise proposal. The USSR has insisted on separate international conventions, one to outlaw atomic weapons and another to establish a system of world controls, while the US and the Commission majority have supported a single combined plan. Dr. Wei proposed separate conventions with co-ordinated enforcement, so that the implementation of the terms will be co-ordinated.

Chinese Technical Mission to US. Since the arrival in Washington on 16 January of the Chinese Technical Mission, Lei Tsu-yi, who heads the Mission, and his associates have been in daily conference with State Department officials on the aid plan to China, which, it is anticipated, will provide safeguards for the US outlay, and stipulate an appropriate measure of self-help. The Mission will be shown a copy of the proposed US plan before it is presented to Congress (see also "Economic" below).

Economic

Currency. Shanghai markets were unusually quiet during the past week. The US dollar blackmarket selling rate receded from CN \$180,000 on 17 January to CN \$160,000 on 23 January 1948. No change is noted in the official "open" rate of CN \$115,000 which was established on 12 January. It is reported that the issuance of large denomination notes has been suspended (Customs Gold Units notes of 1,000, 2,000 and 5,000 equivalent to CN \$20,000, 40,000 and 100,000 respectively, introduced last month, have been the largest denominations to appear to date); also that sending currency by air is banned. Police controls and loan restrictions have caused the flight of some idle capital to Canton. Money remains relatively tight, forcing interest rates up to near 30% per month.

Demand appears to be growing in up-country areas for silver dollars that are still in circulation. The Communists are also showing less interest in CN currency.

The Chinese press reports that Lei Tsu-yi, now in Washington as head of the Chinese technical mission, would present to the US Government Chiang Kai-shek's two alternative currency reform plans for which large cash or credits would be requested. One plan calls for a new paper currency based on the gold standard and linked to the US dollar at the pre-war rate of 3.33 to US \$1. The second plan is a metal currency supplemented by paper notes and based on the silver standard. The National Government estimates that US \$300 million will be required to finance the currency reform project. The Government does not plan to introduce the new currency until economic stability has been achieved. Shanghai foreign economic

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writers regard the currency reform talk as an "eye-wash" even with US aid.

Prices. Steady arrivals of rice stocks at Shanghai have kept the retail price at CN \$1,400,000 a picul, the same price as reported on 16 January 1948.

Shipping. The Chinese merchant fleet is now reported 31.6% larger than it was a year ago. During 1947, 1,039 vessels were added, bringing the total to 3,317 vessels with gross tonnage of 951,826. The increase is attributed to the purchase of surplus from the US and other countries, and recoveries of vessels from Japan.

The port of Tsingtao is still closed to foreign shipping.

Tientsin was cut off from the sea following Communist capture of several points along the Hai River on 9 January 1948. Withdrawals after two days permitted navigation under military escort.

Railroads. The Feiping-Suiyuan railroad from Langshan to Tama was destroyed 31 December 1947, presumably from war operations.

Passenger service is open on the Feiping-Hankow line as far south as Chosien. From Chosien southward the line is badly damaged but service was reported restored as far as Sunglintien by 6 January 1948.

The Changchun railroad operations are reportedly reduced to 87 kilometers operating from Suchiatun, south of Mukden, to Tiehling, to the north. Rail service from Mukden to Fenhsi was reopened on 3 January 1948.

Highways. Changchun highway communications were recently reported closed in all directions.

Traffic was resumed on 10 January 1948 on the highway from Chuh-sien to Changshan (20 miles) in Chekiang Province after completion of reconstruction work.

Telecommunications. Radiophone service between Canton and Hong Kong has been inaugurated with tolls of HK \$12.00 for the first 3 minutes and HK \$4.00 for each additional minute. Rates from Shanghai to the US are based on US \$12.00 for the first 3 minutes converted at CN \$89,000 to US \$1.

Coal. Communist interruption of North China railways may force China to seek Canadian, Philippine, Siberian or Indian coal for Shanghai.

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FRENCH INDOCHINA

Demonstrations for Bao Dai's return. Early in December 1947 two meetings took place in the Baie d'Along between French High Commissioner Bollaert and former Annamite Emperor Bao Dai at which the political basis for Bao Dai's return was settled. Following these meetings new political groupings gradually emerged in both north and south Vietnam. Rallies were held in the chief cities of Indochina, sponsored by the Vietnamese Nationalists who are opposed to Ho Chi Minh and his Viet Minh, in order to express confidence in the former emperor's ability to lay the foundations for "independence and unity."

With these rallies as a foundation, the "Vietnam Quoc Gia Tan Doan" or "Rassemblement National Vietnamien" emerged in Saigon, its aim being to group all political and resistance elements in a more effective struggle for unity and independence. The outcome of contacts with similar groups, such as the National Rally Movement in Hanoi, was the formation of the "Quoc Gia Lien Hiep", which united such elements in one bloc behind Bao Dai in an effort to realize Vietnamese aspirations apart from the struggle of Ho Chi Minh's Vietnam Republic.

Much dissension among Bao Dai supporters has been evident recently, particularly in the dissolution and re-creation of numerous committees in north Vietnam. Former President Le-van-Hoach of the Cochinchina Government was criticized by some of the north Vietnam groups for his close collaboration with the French, but his faction countered with a new committee of its own.

These demonstrations have been sponsored by the French so that Bao Dai may appear to be recalled to Indochina at the "people's demand." The schism among the Bao Dai supporters, attributed by many to personal struggles for political positions and leadership of the pro-Bao Dai movement in the north, is a clear indication that despite French efforts to build a firm foundation for the former emperor's return, they have failed to create the cooperation among the anti-Viet Minh Nationalists requisite to the success of any government which plans to exclude Ho Chi Minh.

SIAM

Current Siamese politics. The provisional government headed by Premier Khuang Aphaiwong is planning to hold national elections on the 29th of January. Because the upper house of Parliament, the Senate, was re-created as an appointive body following the November coup, these elections will determine the composition of only the House of Representatives which was dissolved in November. By these elections the government will become legalized and permanent within the provisions of the new constitution.

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Premier Aphaiwong and his Democratic Party are expected to win a majority of the House seats, but because of the strength of other parties in Parliament a few opposition leaders may be included in the new cabinet to form a coalition government. In exposing itself to a general election, the provisional government is attempting to demonstrate its stability and to prove to foreign governments that recognition should be accorded to the post-election government.

A growing split between the Aphaiwong Government and Marshal Phibul and his Army supporters is rapidly assuming ominous proportions, primarily because the provisional and basically civilian government is attempting to administer Siam regardless of the wishes of the military. There are many indications that the military may discard Aphaiwong, even if he is duly returned to office by the elections, in the event that his government continues its independent course of action. If the military believe that overt seizure of control is necessary, another coup d'etat will have to be staged since the emergency powers recently held by the military have been returned to the civil authorities.

INDONESIA

Significance of crisis in Dutch-Indonesian negotiations. Implementation of the recently signed Dutch-Indonesian truce will be complicated by Dutch suspicions of Republican sincerity regarding a political settlement and by the Republic's failure to understand the implications of the terms of the documents which were signed on 17 January. The effect of these obstacles on Dutch-Indonesian relations were illustrated by the crisis which developed after the truce was signed and which nearly led to the collapse of the COC-sponsored negotiations. The crisis arose from the belief of the Dutch delegation that the Republic had only conditionally accepted the COC's Six Principles for political settlement which the Dutch had already accepted unconditionally. The interpretation of the Republican representatives regarding the COC's Six Principles apparently led them to believe that the Republic could continue to conduct its own foreign affairs and exercise other sovereign perquisites, despite the clear statement in the Six Principles that such sovereign rights will remain with the Kingdom of the Netherlands until the transfer of sovereignty to a United States of Indonesia. While the crisis was later averted by President Sukarno's unconditional acceptance of the Six Principles, the incident has reinforced the Dutch belief that the Republic would attempt to evade fulfillment of its commitments in any eventual political agreement. The tendency of both the Netherlands and the Republic to derive vastly different interpretations from the same signed commitment, and the habit of each party to regard its interpretation as the only one possible may readily lead to repeated breakdowns of negotiations and finally to a resumption of Dutch "police action" on the grounds that dealings with the Republic are patently impossible. Varying interpretations

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of the Linggadjati Agreement and refusals by both sides to give way finally led after four months of increasingly involved negotiations to the "police action" of 20 July 1947.

PHILIPPINES

Defense Secretary may head mission to US. President Roxas has proposed that Secretary of National Defense Kangleon head a mission to Washington to press passage of pending US legislation benefiting Philippine veterans. While Roxas prefers that Kangleon, war-time guerrilla leader on Leyte, head the veterans' mission as a private citizen, Kangleon believes that his assignment to a mission which would be required to register as a lobby would be undignified. The Defense Secretary, now in Tokyo conferring with General MacArthur, prefers to come to the US in his official capacity in order to discuss US policy concerning Philippine defense and to determine the extent of US assistance "in preparation for and during next emergency."

Roxas calls for armed showdown with Hukbalahap. President Roxas, in a two-hour extemporaneous speech at the annual meeting of provincial officials on 22 January, called for an armed showdown "as quickly as possible" with the dissident peasants (Hukbalahap), whom he labeled Communists. Reviewing his administration since May, 1946, the President declared that the policy of "appeasement"--including legislation providing larger rice crop shares for farmers and a land resettlement program, was a "mistake" and a failure because the dissidents did not believe either in private property or individual rights. Telling the provincial governors and mayors to have no contact with the dissidents without the knowledge of the Constabulary, and stating he believed that the armed peasants were determined to overthrow the Government by liquidating its leadership, Roxas, according to an AP report, said: "Thank God this Government has physical strength and power to control this situation."

Roxas' speech came less than a week after the most recent Philippine Constabulary offensive, begun 12 January and aimed at capture of dissident leaders and the breakup of armed elements, ended--as most previous campaigns--in failure. This drive, first termed "Operation Mystery" and finally "Operation Carefree," involved approximately 2000 Constabulary men in a planned 15-day Central Luzon offensive against an estimated 3000 Hukbalahap. The Constabulary task force commander admitted the helplessness of his troops to cope with the strategy of the Huks who disperse rapidly in the face of large Constabulary troop concentrations and then re-form their units when the Government forces move on.

The Roxas speech is not expected to result in any immediate settlement of the law and order problem. The speech, which was doubtless designed as a political maneuver to bolster the courage and gain the support of hardpressed provincial officials and for popular consumption, nevertheless reveals to some extent the sense of frustration the Chief Executive feels at midpoint in his term of office when he finds the most serious immediate problem still remains the establishment of law and order.

Philippine Congress faces stormy session. The Philippine Congress, which convened on 26 January after an adjournment of eight months, is confronted with legislative proposals on two serious and recurrently embarrassing problems--

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establishment of law and order in Southern and Central Luzon and settlement of the collaboration question. It is expected that measures designed to grant amnesty to political collaborators will receive support from Congressmen of both parties. The Congress will be divided, however, on the law and order problem with members of Roxas' Liberal Party unwilling to make concessions to the militant dissidents and the minority inclined toward further attempts to mediate. While President Roxas undoubtedly stated the Administration's stand on one or both of these problems in his State of the Nation message it is likely that he stressed more firmly issues which require additional US financial assistance--veterans benefits, developmental loans, and additional war damage.

The current session of Congress will be in all likelihood a stormy one. Minority strength is presently on the increase, and party feeling is intensifying. Before Congress opened both Liberals and the minority had taken well defined stands along lines which will probably become more sharply drawn as the session continues. Moreover, developments during this session of Congress should definitely shape the presidential campaign of 1949-50. The uncompromising stand of the Roxas Government toward the Luzon dissidents has given the opposition an issue upon which to make political capital, and amnesty, if granted, will release from the stigma of collaboration a highly capable group of men whose political ambitions will become well-defined.

AUSTRALIA

The margin between Australian exports to and imports from the US was unfavorable to Australia in the amount of £ 125,000,000 for the first five months of the current fiscal year. While this figure might seem to belie the effectiveness of the import restrictions and the concurrent export drive initiated in November, it is believed that the full effects of these policies will not be felt for several months. Australian Government officials are looking to the European Recovery Program for the increased purchasing power in Europe which would increase their exports.

NEW ZEALAND

Representatives of the French are consulting with the New Zealand National Airways on French aviation in the Pacific. The French are planning an extension of their air services from Noumea to Papeete and Tahiti via the Fiji and Cook Islands.

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