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**FAR EAST/PACIFIC BRANCH
OFFICE OF REPORTS AND ESTIMATES
GENERAL INTELLIGENCE AGENCY**

WORKING PAPER

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OFFICE OF REPORTS AND ESTIMATES, CIA
FAR EAST/PACIFIC BRANCH

INTELLIGENCE HIGHLIGHTS NO. 38
2 February - 8 February 1949

25X8A SECTION I. SUMMARY OF FAR EAST TRENDS AND DEVELOPMENTS

While press reports of "invasion" of South Korea were exaggerations of another border incident, the Democratic Peoples' Republic plans a political invasion of the south at the end of March when it will sponsor underground elections there (p. 3). Meanwhile, the UN Korea Commission faces the problem of divided South Korean opinion on the subject of US troop withdrawals (p. 4).

In China, LI Tsung-jen spent another week in futile peace efforts and okayed CHIANG Chih-chung's negotiations with the USSR which may lead to complete realization of Soviet ambitions in Sinkiang (p. 6). While the issuance of new regional currencies emphasized the Nationalist Government's disintegration (p. 9), Shanghai shippers took heart over the possibility of resumed coastal trade with Communist-held North China (p. 9). CHEN Cheng, Governor of Taiwan, appealed for continued US aid (p. 7) and Communists in Tientsin confiscated US relief stockpiles (p. 8). There was little military activity anywhere in China (p. 8).

Ho Chi Minh ordered a general counteroffensive against the French in Indochina (p. 4).

In Burma, the dissident PVO group rallied to the Government side in its present struggle with the Karens, while C in C Smith Dun gave up his command (p. 4).

A new plan for settlement of the Indonesian dispute, which the interned Republican leaders view with skepticism, has been advanced by the Dutch (p. 5).

The marginal notations used in succeeding sections of this Weekly ("A", "B" or "C") indicate the importance of the items in B/FE opinion with "A" representing the most important.

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KOREA

North Koreans will sponsor underground elections in South. On 30 March, Northern Koreans are scheduled to elect members to the township and county Peoples' Committees for the first time. Pyongyang radio's announcement of the coming election stated that southern Korea will be invited to participate. Underground revival of Peoples' Committees in the South is undoubtedly designed to continue the Soviet policy of creating confusion in the US-sponsored Republic and to emphasize that the Democratic Peoples' Republic desires "unification" of the peninsula despite US occupation of the southern zone. "B"

Peoples' Committees were organized throughout Korea at the time of Japan's collapse and were designed to form the basis of an indigenous Korean government. They were the local organs of government and, in USSR-occupied Korea, were recognized and utilized as the structure upon which to base the Communist regime. In US-occupied Korea, however, the committees were ordered to disperse and ill will against the US resulted. At present, the Republic of Korea fills nearly all such local offices by appointment and has no immediate plans for local election. Southern Koreans still have fond memories of their dispersed Peoples' Committees and nationalistic pride may well be aroused by an effort to revive this experiment in self-government, even if sponsored by the northern puppet regime.

Press "Invasion" reports exaggerated. The west coast border clash headlined last week as an invasion of the south by North Korean forces proved, upon investigation, to be a small-scale affair. Since all US troops were withdrawn from 38th Parallel outposts on 15 January, a number of incidents have occurred. They appear to be small-scale reconnaissance operations, designed to discover South Korean unit strengths, locations and identities and test their state of alertness. None, however, have been of invasion magnitude - last week's affair included. Such reconnaissance probes can be expected to continue. "B"

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KOREA (Cont.)

UN Commission problems. By 5 February, all but two of the UN Korea Commission delegates had arrived in Seoul. The Commission will confer with Republic of Korea officials before acting to implement its mission of unifying Korea and observing or making recommendations regarding the withdrawal of foreign troops. Its work will be hampered both by the probable refusal of Democratic Peoples' Republic officials to deal with the Commission and by conflicting viewpoints as to its proper function and actions in the south. "B"

The principal southern issue will arise over the question of withdrawal of US troops. President Rhee will attempt to obtain a Commission recommendation in favor of continued US occupation. In opposition to Rhee, as many as 40 younger members of the National Assembly may follow the lead of Vice Speaker Kim Yak Soo in asking the Commission to recommend immediate withdrawal of US forces. Leftists in South Korea, who hitherto have been hostile to all UN attempts to mediate in Korean affairs, may decide to adopt a temporary line of ostentatious cooperation, in an effort to convince the Commission that there is no danger of civil war and that Korean unity can be peaceably achieved when US troops withdraw.

INDOCHINA

Viet Minh victory plans. An order for a general counteroffensive against the French, issued at the end of January by Viet Minh Commander-in-Chief Vo-nguyen-Giap, was confirmed by President Ho Chi Minh following a recent meeting with his ministers. In calling for redoubled efforts to achieve ultimate and total victory, Ho emphasized that French strength must not be underestimated. At the same time, Ho once more denied the French allegation that he had signed a secret treaty with the Chinese Communists in June 1948. "B"

BURMA

Race war continues. Two significant developments in the Karen-Burman struggle came this week. First, the Peoples' Volunteer Organization (PVO), which has been in armed rebellion against the Government since July, 1948, is emerging in increasing numbers to assist Government forces in the fighting, particularly in and around the important port of Bassein and at Insein, 10 miles north of Rangoon. It seems likely that similar action has been taken by PVO groups throughout Lower Burma and that other Burmans, Communists included, may disregard their political differences and follow the lead of the PVO's in taking up arms against the Karens. "B"

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BURMA (continued)

Secondly, Lt. Gen. Smith Dun, Burmese Commander-in-Chief, has left Rangoon for Kalaw, in Northern Burma, ostensibly on sick leave. Smith Dun, a Karen, has been replaced by Bo Ne Win, a Burman and Left-Wing Socialist. Smith Dun's departure will probably cause further Karen desertions from the Burmese Army. Both these developments make the possibility of a general, amicable settlement between Karens and Burmans increasingly remote.

INDONESIA

Dutch present new plan. A new scheme for the transfer of Netherlands sovereignty to an Indonesian federation is currently scheduled for discussion on the Island of Bangka. The all-Indonesian meeting is supposed to include Republican President Soekarno, Premier Hatta and a delegation of Federalists. If the Bangka conference accepts the Dutch plan (Netherlands relinquishment of sovereignty within two months to a "Republic of the United States of Indonesia"), both Dutch and Security Council timetables for elections and the granting of sovereignty would be considerably accelerated. "A"

Republican leaders, however, view the plan with skepticism, regarding it as a Dutch device to circumvent the 28 January UN resolution. Until recently, they have declined to participate, as individuals, in discussions with the Federalists, but have insisted that they be recognized as representatives of a reconstituted Republican Government.

The Federalists, through whom the Dutch have attempted to win Republican support, have shown an unexpected independence of their own. They have been reluctant to condemn the latest SC resolution and to commit themselves to any specific course of action. While certain of the Federalists are avowedly pro-Republican, the great majority are anxious to stall without committing themselves until it is clear that either the Dutch or the Republicans will retain the balance of power in Indonesia.

CHINA

LI Tsung-jen's continuing efforts to negotiate peace with the Communists appear to be facing diminishing prospects of success. In addition to the Communists' intransigence, there is a growing split within the ranks of the National Government over whether or not to continue negotiations. Premier SUN Fo in Canton has declared that the Government will fight on if honorable peace negotiations fail. The Cabinet, which has "B"

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given LI little support, has departed from Nanking and refuses to comply with LI's request to return. LI fears that the Generalissimo also is attempting to sabotage his peace efforts, despite reported assurances from CHIANG of his continued support. While it is to LI's personal advantage to continue negotiations, few Nationalist officials are likely to accept any binding peace commitments LI might make with the Communists.

Sinkiang to become Soviet buffer. Soviet Ambassador Roshchin's transfer to Canton, and CHANG Chih-chung's mission to Tihua, may be related in a Soviet maneuver aimed at consolidating Soviet control in Sinkiang, thereby realizing a strategic security objective of the USSR. "A"

For the past year Roshchin has been identified with the prospect of Soviet mediation in the Chinese civil war. Last month, when the USSR formally declined to mediate, Soviet sources confirmed reports that Roshchin would leave presently for Moscow. Last week, however, Roshchin followed the Chinese Ministry of Foreign Affairs to Canton, the only Ambassador to do so. It is perhaps implied thereby that Roshchin's mediation mission also remains, or that the USSR desires the Chinese Government to believe that Soviet mediation is still possible. Moreover, the Chinese Government organs now in Canton are the proper authorities for ratifying international agreements.

It is probable that the USSR does not desire a strong China - even a Communist China - on the Soviet borders, and therefore is seeking to form a buffer area through Manchuria, Inner Mongolia, and Sinkiang. The Sino-Soviet Treaty of 1945 provided for a strong Soviet position in Manchuria; although MAO Tse-tung stated publicly his desire that Outer Mongolia be restored to China, that area became a Soviet satellite, and may draw Inner Mongolia into its orbit; and now the Soviet position in Sinkiang should be greatly strengthened by the "local agreement" which CHANG has gone to Tihua to negotiate.

The agreement reportedly would grant the Soviet Union mining, trade and aviation monopolies in Sinkiang for the next forty to fifty years. The mining monopoly would give the Soviets full rights to exploit Sinkiang's little-known resources of oil, wolfram and gold. Oil deposits in Sinkiang are rumored to be sufficient to supply the entire Soviet Far East, though this would require many years of development. The mining monopoly would also make possible Soviet exploration to check on unconfirmed reports of uranium in Sinkiang.

A Soviet trade monopoly would provide for exchange of Sinkiang's raw materials, principally wool, for manufactured goods from the USSR. In addition there would be a new civil aviation agreement renewing the virtual air monopoly held by the USSR under the Sino-Soviet Aviation Agreement which was denounced by China last September.

CHANG's mission might well prepare the ground for making a Soviet satellite not only of all Sinkiang, but perhaps of parts of Ningsia.

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Chinghai, and Kansu. While the Sinkiang provincial government has long desired resumption of trade with the USSR, the present Chinese Government would seem to have little to gain, in that its life expectancy is certainly not the 40 or 50 years which the Sinkiang pact envisages. Thus the Chinese Government may be seeking, in return for approval of the "local agreement," a means for preserving its own life: specifically, by Soviet mediation in the civil war. It is improbable that the USSR will or can mediate successfully to that end; but the USSR could easily promise to attempt it, and Acting President LI Tsung-jen appears sufficiently naive and desperate to accept such a promise.

The Chinese Communist radio has not yet mentioned the Sinkiang negotiations. Tihua, however, is one of the 16 major centers to which, according to the Communists, the Peiping surrender formula will be applicable. Thus the proposed "local agreement," if it were to remove Sinkiang from the eventual control of the Chinese Communists, would seem to qualify as one of the "traitorous" treaties which the Communists have denounced. It is therefore possible that the USSR and the Chinese Communists are plotting this maneuver in concert: i.e., that the USSR will promise to attempt mediation, will additionally promise CHANG and the Moslem governors of Ningsia and Chinghai that their authority will be preserved, and will then allow the area to pass into Chinese Communist control. It seems more likely, however, that the USSR, if not seeking direct control of a Northwest "autonomous" regime, is at least seeking a position strong enough to permit the Chinese Communists to enter the Northwest only on USSR terms.

The participants in a Soviet - Nationalist agreement, if the Chinese Communists were genuinely excluded from it, would obtain widely varying returns: the USSR would get Sinkiang; the Chinese Government - a sack of wind; CHANG - a comfortable berth, subject to sudden relocation; and the Moslem leaders - continued, although insecure, authority. The Chinese Communists would be confronted with a serious dilemma: whether to accept in silence this major loss in territory and face, as was the case in regard to Outer Mongolia, or to denounce the agreement and attempt - with their increased strength since 1945 - to rectify it, in which case their relations with their one important international friend would be severely compromised. While a Soviet maneuver in denying the Northwest to the Communists or restricting their authority therein would certainly increase the chances for Titoism in China, the Soviet annexation of the border regions would make the fact of Titoism, if it does appear in China, less dangerous in its effects upon the USSR.

Taiwan Governor bids for US support. In an apparent effort to obtain US good will and support, through ECA and other forms of aid, Governor CHEN Cheng has indicated to US officials he intends to develop in Taiwan an autonomous, anti-Communist administration, which would be independent of mainland China. His known loyalty to CHIANG Kai-shek and

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the latter's careful preparation to make the island his final stronghold belie CHEN's claim that circumstances do not permit CHIANG's return to power, even in Taiwan. Moreover, CHEN's ruthless character and his previous record in military and provincial administration fail to substantiate his promise of a competent and popular regime. Also interesting to note are recent public statements of CHANG Chun in Chungking and WSUEH Yueh in Canton, similar to those of the Taiwan Governor, regarding the prospect of CHIANG's return. Although these statements may partially reflect personal views, it is likely that they constitute maneuvers for US aid and may even have the tacit approval of the Generalissimo.

Inactivity characterizes military situation. This week the Communists continued to mass their columns in an area above Nanking from which they can easily move southward across the Yangtze and occupy the vital cities of the Yangtze delta when the Nationalists complete the evacuation of those points. The exact intention of the Nationalist command, which at present lacks even a semblance of cohesion, is difficult to establish. Some reports indicate Nationalist combat forces have been withdrawn from the Nanking-Shanghai area, while others state this movement has included only service troops. Another report notes that TANG En-po's command--a maximum 150,000 strong--has been tendered defense funds by Shanghai groups in the expectation that these forces would be employed in the defense of that metropolis. Still another report expresses doubt the the bulk of the city's populace wish to see that city involved in any future fighting. It is probable that the great majority of the Nationalists, civil and military alike, have little faith in the success of LI Tsung-jen's present peace overtures. To the north the Communists celebrated their cleanup of North China by holding a big "liberation" celebration in which conquering Communist forces paraded in the streets of Peiping. US observers report that the armaments of the troops which entered Peiping was predominately Japanese with a heavy proportion of automatic weapons, some had US Tommy guns, carbines, and artillery, the motorized equipment was US made, and that the troops themselves, dressed in a conglomeration of uniforms appeared to be in good condition.

Communists confiscate ECA food at Tientsin. The Communist move in abruptly terminating the Tientsin food ration program by confiscation and distribution of ECA flour stocks appears to have been shortsighted. The chief repercussion may be a food shortage accompanied by erratic prices until the harvest season. The Communists have not been sufficiently aware that feeding the 2-3 million people in Tientsin and its environs entails large-scale food imports and an efficient collection and distribution organization. Primarily because of ECA the people of Peiping and Tientsin have become accustomed to a sufficient amount of cheap food during the last six months; if the Communists are unable, by transfers from food surplus areas, to meet this standard, it will be difficult to justify to the people their hostile action toward ECA.

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Local currencies are emerging throughout non-Communist China. In consequence of increasing economic isolation Hunan Province issued a new currency this week called the silver yuan. At Hankow Pai Chung-hsi expressed his disgust with the defunct gold yuan by authorizing free circulation (and bank acceptance) of silver dollars in Hupeh Province. The Taiwan provincial government has banned all remittances of gold yuan from the mainland because of its worthlessness and inflationary effect. The 500% depreciation of the gold yuan this week plus the departure of most of the Central Bank except the currency issuing department for Canton will force the emergence of many other local currencies. The possible abandonment of the gold yuan by the Canton refugee government is reported by a Hong Kong Communist newspaper, which claims that a "Four United Provinces" currency has been printed in Hong Kong (presumably to cover Kwangtung, Kwangsi, Fukien and Kiangsi).

The possibility of coastal trade between Shanghai and North China developed this week. The Kailan Mining Administration in Communist North China has arranged with Central Trust, a subsidiary of the Central Bank, to exchange 100,000 tons of Kailan coal for 300,000 bags of Shanghai flour. Economically, the exchange is ideal since coal is plentiful in North China and scarce in Shanghai, and the reverse is true of flour. The Kailan Mining Administration has assured the ships' entry and clearance at Chinwangtao if they fly only the Kailan house flag.

Shipping circles throughout the Far East are anxiously awaiting the reopening of Communist ports in North China to foreign and coastal trade. The American ship, President Fillmore, has received word from Peiping that arrangements for unloading its cargo at Tangku have been made. In face of foreign competition, the Executive Yuan finally approved Chinese shipping to Communist destinations.

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