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Intelligence Memorandum

The Outlook for Hong Kong

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Central Intelligence Agency
Directorate of Intelligence
25 August 1967

INTELLIGENCE MEMORANDUM

The Outlook for Hong Kong

Summary

Renewed Chinese Communist pressure on the British over the situation in Hong Kong raises new questions concerning the immediate future of the colony and the prospects over the longer term. The increasingly fluid situation in Peking and the continuing "revolutionary" disorder throughout China make confident predictions of Chinese behavior more difficult than ever.

Nevertheless, China's demeanor in the past three months has led us to conclude that the Chinese authorities intended from the outset to keep the Hong Kong issue hot and to continue their support for dissident elements in the colony. We have also concluded that Peking undertook a campaign aimed at gradually eroding the position of the Hong Kong authorities and thus preparing the ground for a new attempt by the local Communists to seize de facto control in a year or so. We believe that in the meantime the Chinese Communists will refrain from actions against the colony involving the risk of war, or even moves which would so disrupt Hong Kong as to put it out of business and thus deny Peking the vital foreign exchange earned there.

Note: This memorandum was produced solely by CIA. It was prepared by the Office of Current Intelligence and coordinated with the Office of Economic Research and the Office of National Estimates.

The latest Chinese Communist actions appear to bear out this analysis. The handing of an ultimatum to the British and the assault on the British Embassy in Peking followed a series of humiliating British rebuffs to Chinese demands. These moves may have been partly in response to pressure from hard-pressed Communist leaders in Hong Kong for more significant support than Peking had been contributing to their campaign. The sacking of the embassy did, however, fulfill Peking's threat to the British of "serious consequences" without involving serious risks.

The Hong Kong Communists have probably been encouraged by these actions and can be expected to step up their efforts to create disorder. Recent Chinese Communist behavior and propaganda suggest, however, that Peking does not intend at this time to go much beyond the kind of action already taken to support the local Communist apparatus.

It does not appear likely that the Chinese Communists intend to attack across the border, but there are two possible actions stemming from mainland China that could make the situation very difficult for the Hong Kong authorities. Red Guard radical mobs, acting either on their own or under orders from Peking, could attempt an aggressive action against the colony. It seems likely, however, that the Gurkha troops could contain such a move. More serious difficulties could arise if military authority in neighboring Kwangtung Province broke down and masses of Chinese refugees fled to the freedom of the colony.

The British have shown themselves capable of handling Communist terrorism and violence within Hong Kong itself. Nevertheless, the long term outlook for the colony is uncertain at best. Business confidence has been shaken and capital is beginning to flow out from the colony. Unless peace, however uneasy, is restored to the colony, a trend could develop which might sharply reduce the rate of economic growth and lead to growing unemployment. This would provide the Communists with new opportunities and that may be what they are seeking. A change in leadership in Peking,

however, and a consequent change in Chinese Communist policies would probably reduce the force behind the Hong Kong Communists' trouble-making potential and allow the colony to recover some of the losses it has suffered.

Recent Background

1. The burning of the British Embassy in Peking on 22 August came at the end of a period during which Peking had probably become increasingly frustrated by the failure of the Communist apparatus in Hong Kong to shake the position of the authorities. In the aftermath of the Sha Tau Kok incident on 8 July the colonial government launched a vigorous counterattack against Communist efforts to create large-scale disorder.

2. Troops were used to back up police for the first time on 12 July in a successful raid which cleaned out a leftist union headquarters which had been used as a command post for organized rioting which had plagued the colony for nearly a week. The morale of local Communist organizations was severely shaken by this raid and by subsequent moves against other control centers which put many Communist leaders behind bars.

3. The number of violent incidents and large-scale disorders fell off and by the end of July it appeared that despite continued sporadic terrorist attacks on the police and against public transportation services, the authorities were well on the way toward breaking the back of the Communist apparatus. A food strike was cancelled and the strike against harbor facilities was increasingly ineffective.

4. Throughout this period Peking's propaganda, while encouraging the local Communists to carry on with their fight against "oppression," continued to stress that the main burden in the struggle would have to be carried by the "compatriots" in the colony. When three NCNA representatives in Hong Kong were arrested around the middle of July, the Chinese Communists protested vociferously and staged small demonstrations in front of the British Embassy in Peking but took no further action.

5. New small-scale border incidents took place in early August but these do not appear to have been the result of orders from Peking, or even from provincial authorities. Chinese troops guarding the

border intervened on a number of occasions to prevent major troubles from developing in Kwangtung. The most serious of these incidents took place on 11 August when a gang of Red Guard ruffians crossed the border and attacked the police post at Man Kam To. The Red Guards disarmed sentries and forced a British police official to sign an agreement to remove barbed wire barriers near the frontier, and to pay compensation for alleged injuries to a local farmer.

6. The next day the British coolly repudiated the "agreement" on the ground that it had been signed under duress and proceeded to close the border except for the rail crossing at Lowu. This prompted a protest note from the Chinese Foreign Ministry on 14 August which the British rejected, although they later lifted restrictions at most of the border crossing points.

7. Three days later, on 17 August, the Hong Kong authorities closed down three leading pro-Communist newspapers which had been printing inflammatory editorials and arrested key staff members. This appears to have been the last straw for Peking. The Chinese Communists' prestige was already deeply engaged and their inability significantly to affect the situation had been repeatedly demonstrated. Under these circumstances Peking apparently decided that something had to be done and on 20 August the Chinese Foreign Ministry delivered a threatening note to the British chargé demanding that the ban imposed on the newspapers be lifted and the arrested newsmen released within 48 hours.

8. The British promptly rejected this note and the Hong Kong Government proceeded with the trials of the pro-Communist newsmen. Peking's response when the deadline set by its "ultimatum" had passed was to send a Red Guard mob to sack and burn the British Embassy. This outrage, the most serious action against a foreign embassy since the Boxer Rebellion, was probably regarded by the Chinese Communists as involving small risk and certain to succeed. It appears intended to intimidate the Hong Kong authorities, to satisfy the requirement

that the "serious consequences" threatened in the note be visited on the British, and to boost the sagging morale of the Communist apparatus in Hong Kong.

The Immediate Future

9. Hong Kong Communist leaders have probably been encouraged by this new indication that Peking is willing to support them. A Communist spokesman in the colony has threatened an increase in terrorist activity. His declaration at a news conference on 22 August that the "liberation of Hong Kong has begun," however, appears to be nothing more than a boastful propaganda statement. The Chinese Communists may augment local pressure against the Hong Kong authorities by staging new border demonstrations similar to those which have already taken place, but they will probably not go much beyond such action at this time.

10. A blustering People's Daily editorial broadcast on 20 August--the same day the "ultimatum" was delivered--asserted that Hong Kong was Chinese territory, and declared that the "compatriots" in the colony had the "powerful backing of their motherland." In discussing the return of Hong Kong to mainland control, however, the editorial said only that it was unthinkable that the colony would "always" be under British rule and declared that "imperialist blood debts" would be liquidated "sooner or later." Peking's propaganda still maintains that the local Communist leaders in Hong Kong must depend for the most part on their own resources in the struggle against the British. A 22 August NCNA account of the attack against the British carries this theme and implies that the "heroic fight" against the British will depend to a great degree on the "perseverance" of the "Hong Kong patriots," who have the "backing" of the Chinese People's Republic.

11. Although a military attack across the border from the mainland thus does not appear likely, there are two possible actions that would make the situation exceedingly difficult for the British in

Hong Kong. It is possible that superheated Red Guard radicals, under the guise of "volunteers" aiding their compatriots in Hong Kong, may attempt a concerted attack over the border. Under the conditions now prevailing in China such a mob might not be under orders from Peking, but could be carrying out Mao's ambiguous decrees that it "is good to make revolution."

12. Such an attack could probably be repulsed by the Gurkha troops that are now manning the Hong Kong side of the border. Defense preparations have been underway for some time now and the local authorities think that they can contain this kind of aggressive action. In the event there is such a showdown, the Chinese population of Hong Kong would probably universally support the British, since even the leftists appear to be in terror of Red Guard excesses.

13. A more difficult problem to handle would arise if there were a sudden, large-scale migration from Kwangtung Province over the border. The situation in Kwangtung is at present a very fluid one, with disorders and turmoil reported increasing. If there were a complete breakdown in military authority there, it is possible that masses of refugees would rush for Hong Kong. It is even possible that the Peking authorities might instigate such a migration.

14. In the spring of 1962, either through a misunderstanding of what Peking wanted or through a breakdown in authority in Kwangtung, there was such a large-scale influx of mainland Chinese into Hong Kong. The colony was hard pressed to accommodate these masses and should a new drive for the free air of Hong Kong exceed the 180,000 Chinese that came across in 1962, this might swamp the ability of the local authorities to handle the situation.

15. Short of these two situations, the immediate threat to the colony appears to be renewed efforts by the local Communists to harass the security forces and to terrorize the population. The Communists probably hope that through these tactics they gain willing support or coerce tacit acceptance of

their actions. The Hong Kong authorities have shown that they can deal with these tactics, however, and there is no indication that the British are willing to back down now.

The Long-Term Outlook

16. Nevertheless, the long-term outlook for the colony is uncertain at best. As yet the economy of Hong Kong has sustained no serious short-run damage. The major manufacturing industries have not been disrupted and continue to earn profits and provide employment. Entrepot trade has probably been reduced to some extent but still continues in large volume. Tourism, which provides the colony with a third of its nontrade foreign exchange earnings, has been temporarily curtailed to some degree, but it is still difficult to get reservations at first class Hong Kong hotels.

17. Despite this picture of "business (almost) as usual," however, a crack may be opening in the foundations of the colony's prosperity--the confidence of the local business community in the future of Hong Kong and the willingness of outside entrepreneurs to invest there. Hong Kong businessmen are a tough-minded lot. Many are "refugees" from pre-Communist China who got out in time with capital enough to make a new start. They recognize the vulnerability of Hong Kong to Chinese Communist pressure--including outright seizure--and most of them have never planned investment on a timetable that extended much more than five years into the future. As these men look ahead now after three months of Communist harassment, however, what they see is the prospect of a long campaign against the government--continuing labor agitation, terrorism, and persistent efforts to destroy public security and make the colony untenable. In the background, so long as the militant Maoists are disrupting the mainland, they see the threat of a political explosion which might engulf them.

18. There are signs, perhaps nothing more than straws in the wind, that the confidence of the Hong

Kong business community has been seriously shaken. If a pessimistic trend should develop, the consequences over time would mean stagnation or even ruin for the colony. The Hong Kong situation is such that the economy must maintain dynamic growth or face collapse. The near-continuous boom which has been going on for nearly two decades has rested mainly on the willingness of foreign capitalists, chiefly overseas Chinese, to invest money in the colony. As the colony prospered new capital was attracted from outside which accelerated the rate of economic growth still more.

19. Outside capital has become increasingly important in maintaining this cycle, but the willingness of foreign investors to put money into Hong Kong is strongly conditioned by their reading of local attitudes. Pessimism on the part of local business leaders leads to growing caution among outsiders. Current symptoms of uneasiness in Hong Kong are already having this effect. There has been a flow of capital from the colony and bank loans to small businessmen have become tighter. There are reports that some wealthy Chinese businessmen have concluded that the boom is over and are planning to liquidate their assets. Partly in response to this, American and Japanese investors, who have been largely responsible for developing new industries in recent years are now expressing serious reservations in regard to further investment in the colony.

20. There is a real danger that without a return to stability and business confidence in the next six months or so a long-range downward trend might develop. Lack of new investment and a reduction of the rate of the colony's economic growth would, over time, bring about rising unemployment. This would provide the Communists with new opportunities and perhaps with much-needed local support. Strikes and demands for economic and political benefits might then be far more successful than they have been in the past few months and this would further sap the business community's confidence. It seems probable that this is the outcome that the Communists are presently banking on--not a takeover of the

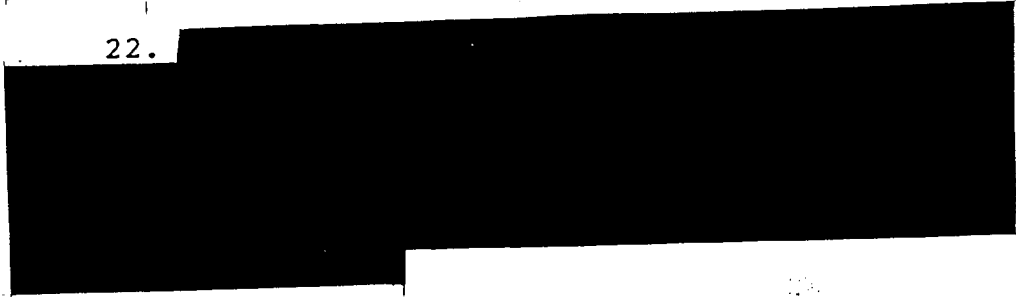
colony from the outside by military means but a steady erosion from within that will give the local Communists the whip-hand and result in a situation resembling that of Macao.

21.



1.5(c)(d)
3.4(b)(1)(6)

22.



1.5(c)(d)
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23. Finally, as long as the Maoist fanatics continue to insist on a literal playing out of the current interpretations of Mao's thought, constant pressure on the colony can be expected. If new leaders come to power in Peking, however, and turn to more moderate and pragmatic designs in an effort to restore inner stability on the mainland, the force behind the Communists' campaign in Hong Kong will probably abate. An equilibrium can be re-established and Hong Kong, which will have suffered a blow from which it will be slow in recovering, will settle into an uneasy peace with somewhat reduced prosperity.