

~~SECRET~~

39615

Estimates

CENTRAL INTELLIGENCE AGENCY

LIMITATIONS OF SOUTH CHINA AS AN ANTI-COMMUNIST BASE

This document has been approved for release through the HISTORICAL REVIEW PROGRAM of the Central Intelligence Agency.

Date 21 Jul 92

HRP 92-7

ORE 30-48

Published on
4 JUNE 1948

COPY NO:81
FOR THE ASSISTANT DIRECTOR
FOR REPORTS AND ESTIMATES

Document No. 001
 NO CHANGE in Class.
 DECLASSIFIED
 Class. CHANGED TO TS S C
 DDA Memo Apr 77
 Auth: DDA REF. 77/763
 Date: 12/1/78 By: 023

~~SECRET~~

DISSEMINATION NOTICE

1. This copy of this publication is for the information and use of the recipient designated on the front cover and of individuals under the jurisdiction of the recipient's office who require the information for the performance of their official duties. Further dissemination elsewhere in the department to other offices which require the information for the performance of official duties may be authorized by the following:

- a.* Special Assistant to the Secretary of State for Research and Intelligence, for the Department of State
- b.* Director of Intelligence, GS, USA, for the Department of the Army
- c.* Chief, Naval Intelligence, for the Department of the Navy
- d.* Director of Intelligence, USAF, for the Department of the Air Force
- e.* Director of Security and Intelligence, AEC, for the Atomic Energy Commission
- f.* Deputy Director for Intelligence, Joint Staff, for the Joint Staff
- g.* Assistant Director for Collection and Dissemination, CIA, for any other Department or Agency

2. This copy may be either retained or destroyed by burning in accordance with applicable security regulations, or returned to the Central Intelligence Agency by arrangement with the Office of Collection and Dissemination, CIA.

WARNING

This document contains information affecting the national defense of the United States within the meaning of the Espionage Act, 50 U.S.C., 31 and 32, as amended. Its transmission or the revelation of its contents in any manner to an unauthorized person is prohibited by law.

ORE 30-48

~~SECRET~~

LIMITATIONS OF SOUTH CHINA AS AN ANTI-COMMUNIST BASE

SUMMARY

The deteriorating military situation of the Nationalist Armies in North China and Manchuria has faced the Chinese Government with the necessity of making plans for a future base of operations. Aside from the remote districts of the far west which are unsuitable for the purpose, the only area with relative stability to which the Nationalists could withdraw would be South China, including Taiwan. It is inevitable, therefore, that a further worsening of the military situation would force the Government to make such a withdrawal in order to survive in its present form. That Chiang Kai-shek attaches great importance to this area is evidenced in the assignment of ex-Premier T. V. Soong to the post of Governor of Kwangtung. Soong's principal mission in this office is to convert agricultural South China into a region which will be relatively self-sufficient and defensible from Communist attacks.

Although the South China region includes one of China's principal "rice bowls" and has many important natural resources such as coal, iron, and other strategic metals, which could make the present goal theoretically attainable, seemingly insuperable obstacles stand in the way of its attainment for current Nationalist purposes.

Chief among them are:

1. *Time.* Even with ideal conditions, it would take at least several years to build all the necessary installations and to create an industrial organization which could efficiently make use of them. It is doubtful, as matters stand, that more than one year would remain of uninterrupted Nationalist activity after withdrawal from the North.

2. *Food.* South China, where the most intensive agriculture has been practiced for generations, is still a marginal area in food production. With the necessity of relying on the food resources of this region for the maintenance of a large army plus the enormous influx of refugees which would follow the Nationalist withdrawal from North China, famine would be a chronic threat. The food problem in South China may be mitigated, however, by rice imports from Southeast Asia.

3. *Overly Ambitious Planning.* Rather than concentrate on a limited program which would deal with such basic elements as transportation, exploitation of valuable mineral deposits, and the full utilization of plants already built by the Japanese on Taiwan, the Government has seen fit to embark on overly ambitious programs and projects such as the "Five-Year Reconstruction Plan of Kwangtung Province" which have little possibility of success even though peace and prosperity attend the effort.

4. *Disunity.* The internal security of South China is threatened both by dissension within the Kuomintang and by the hostility of anti-Kuomintang elements.

Note: The information in this report is as of 11 May 1948.

The intelligence organizations of the Departments of State, Army, and the Navy have concurred in this report; the Air Intelligence Division, Air Intelligence Directorate, Department of the Air Force, had no comment.

~~SECRET~~

5. *Civil Conflict.* Cessation of hostilities in the North would only move the principal battlefield to Central China whence, despite distance and poor communications, it would eventually move to the South.

6. *Capital.* In the long run, the economic development of South China will require a substantial volume of capital. South China does not have nor could it create the savings from which capital needed for development would have to be drawn. Foreign investments certainly could not be expected in sufficient amounts for the purpose, nor is contemplated US aid (much of which the National Government intends to divert for the purpose) adequate under the present circumstances. Although there is a possibility that some investment capital from North China may be made available to South China, there is as yet no evidence that this has taken place.

In short, assuming maximum Communist capabilities, any contemplated retreat of Nationalist China into the southern area would be a measure of desperation which, under present circumstances, would offer little future safeguard from eventual defeat and collapse. Aid in the form of capital, food, equipment, and intelligent direction could probably give the National Government reasonable chance of carrying on effective anti-Communist resistance from South China.

~~SECRET~~

~~SECRET~~

LIMITATIONS OF SOUTH CHINA AS AN ANTI-COMMUNIST BASE

1. SOUTH CHINA AS A NATIONAL GOVERNMENT REFUGE.

Since early 1947 the economic and political stabilization of China south of the Yangtze has ranked high among the National Government's non-military objectives. Aside from the general advantages that Nationalist China would ordinarily derive from the stabilization of South China, this area assumes special significance as a base for continued operations of the National Government and from which Nationalist Armies can be supported in the event that North China should be lost to the Communists and Central China become an active military theater. The possibility that the Government's foothold in Manchuria and North China would be lost has, during the early months of 1948, added impetus and a sense of urgency to the Government's plans for this region, which includes the provinces of Yunnan, Kweichow, Kwangsi, Kwangtung, Kiangsi, Hunan, and Fukien. Taiwan, although not on the mainland, plays an important and strategic role in the planning for this region.

Control over the development of the most important area of South China has been placed largely in the hands of T. V. Soong. He is not only governor of Kwangtung Province but, concurrently, is head of the military forces of South China, thus having authority which extends beyond the boundaries of the province.

The present discussion of South China as a refuge for the National Government is based on the assumption that North China and Manchuria will be lost to the Communists. Certain concomitants of such an assumption will have an important influence on the potentialities of economic development, political stability, and military security:

a. If the Communists take over North China, there is reason to believe that military pressure will continue with increasing intensity against the National Government in areas farther south. This would mean that Central China would become the focal point of the civil conflict, that South China — heretofore operating pretty much on a business-as-usual basis — would have to be developed according to the needs of a war economy, and that the Government would have to continue its policy of deficit financing with all the inflationary results that such a policy implies. If the area were to be defended at all, the Government would have to salvage a large share of the combat troops it now has north of the Yangtze. Although the present resources of the South China region are probably insufficient to supply an army of adequate size to protect that region, vital imports could be financed through the export of minerals and tung oil as well as through the use of overseas remittances.

b. The Government would be faced with the serious problem of caring for the substantial number of refugees who would inevitably find their way into Nationalist territory. This influx of a large group of unemployed, poverty-stricken, restless "aliens" would strain the existing delicate balance between food supply and population that now characterizes South China and would intensify the problem of maintaining political stability and internal security.

~~SECRET~~

~~SECRET~~

c. The effort would require time, much of which has already been wasted. The National Government's efforts of almost a year have produced little more than schemes on paper. Even with continued military deterioration and the prospect that by the end of 1948 the National capital may well have to be moved into South China, no significant part of the conversion plan has yet been carried out.

2. ECONOMIC POTENTIAL.

a. *The Present Condition of South China's Economy.*

(1) *Mineral Resources.*

South China has ample deposits of many important minerals. Its greatest deficiency is in coal, the region having but 3% of China's total. However, approximately 20% of the country's iron deposits are located in the area. Hainan Island's substantial deposits of high-grade iron ore as well as small deposits of iron and substantial reserves of coking coal close to the rich antimony, tungsten, and manganese deposits of Hunan and Kiangsi Provinces provide basic conditions for the development of a steel industry. In addition to the above, South China has plentiful tin and a newly discovered small supply of bauxite accessible to the aluminum production plants on Taiwan. There have been unsubstantiated reports of uranium deposits in Kwangsi.

In contrast, however, to this favorable mineral position is the production record for 1947: only 4,000 metric tons of tin; 6,400 metric tons of tungsten; 6,000 metric tons of antimony; negligible output of manganese; 250,000 tons of coal, all from the Hunan mines; and insufficient iron to support even minor industrial activity.

(2) *Agriculture.*

Although Hunan Province is one of the great "rice bowls" of China, its surplus barely makes up for the food deficit of Kwangtung Province. Even in times of peace and relative plenty, the food output in the other provinces of the region is barely sufficient to maintain the population at a subsistence level.

Should the Nationalists retreat from the North, however, the rich agricultural land of northern Hunan, Kiangsi, and Chekiang, although south of the Yangtze, would be exposed to the Central China battle zone and would thus be beyond the boundaries of peaceful territory under Nationalist control. The pressure of population against the food supply would also be aggravated by an influx of refugees. The region's food resources would furthermore have to supply the Nationalist military forces that heretofore have been primarily maintained by the output from Central China. The resultant food deficit would be catastrophic, unless large-scale food imports from Southeast Asia could be obtained.

To mitigate this prospective disaster the National Government would have to make at least a start on the institution of land reforms, the construction of large-scale flood control and irrigation projects, the increase in the production of chemical fertilizer, and the utilization of hitherto neglected but arable land in the western part of the region. It is very improbable that such reforms could be achieved during the period of present concern.

~~SECRET~~

~~SECRET~~

(3) *Transportation.*

(a) *Waterways.*

Although waterborne traffic is often interrupted by bandit operations, the rivers and canals present the greatest immediate possibility for the large-scale movement of persons and food.

(b) *Railroads.*

There are approximately 2,000 miles of rail lines in operation on the mainland of South China. The Canton-Hankow Railway is in very poor condition, but is in limited service throughout its length; the Chekiang-Kiangsi line is operating through most of its length; the Hunan-Kwangsi-Kweichow line is in a state of disrepair and is operating over approximately three-fourths its length. Taiwan has almost 2,400 miles of operating railroads. The shortage of fuel, the deteriorated rolling stock, and the continuing bandit activity, however, present a constant threat to the operation of all lines.

(c) *Highways.*

Most of the roads in South China are primitive and still bear the scars of the extensive damage suffered during the war. The high cost of highway transportation and the lack of motor vehicles characteristic of the whole region, limit the usefulness of whatever highways exist.

(4) *Manufacturing.*

Although there is a wide variety of manufacturing activity in South China, most industrial operations are on a small scale and utilize little or no power-driven machinery. Electric power output is barely adequate to supply the needs of existing industry. Throughout the region there are few plants now in operation that are large by Western standards. By far the greatest proportion of manufacturing plants in the region produce consumers' goods.

Hunan, Kwangsi, Kweichow, and Yunnan Provinces became centers of wartime industrial operations as the Japanese penetrated deeper into China's interior. Many of the factories established in South China were moved from the east coast; many others were constructed in a makeshift fashion from salvaged machinery and equipment. These plants are high-cost, inefficient producers which probably cannot operate without continued government subsidies.

There has been little actual improvement, if any, in the general industrial situation since VJ-Day. Many of the factories in this region have had increasing difficulties in obtaining raw materials and power. Funds that may otherwise have been invested in industrial expansion have been attracted into the profitable black-markets for US Dollars and gold.

One step toward increasing the output of important manufactured goods in South China is the recent agreement between the Reynolds Metals Company and the National Government as a result of which the contracting parties will jointly operate the aluminum plants of Taiwan. The efficient operation and expansion of these plants in conjunction with the exploitation of the readily accessible Fukien

~~SECRET~~

~~SECRET~~

bauxite reserve should permit the operation of a profitable aluminum processing industry in South China. The lack of fabricating capacity in this region, however, is a serious handicap in the development of an integrated aluminum industry.

(5) *Foreign Trade.*

Current exports from South China are considerably below the prewar level, although tung oil and strategic minerals, such as tin, antimony, and tungsten are in world-wide demand. Clearly, any program of economic development should include the reconstruction of those industries which could be important suppliers of foreign exchange.

Overseas remittances were the key factor in compensating for China's chronically adverse balance of trade before the war. In some prewar years total remittances reached an equivalent of US \$100 million per year. Since most overseas Chinese emigrated from South China, the largest share of the funds flowed into this region and represented an important factor in South China's economy. After the outbreak of war the value of remittances declined. All in all, however, South China's situation with respect to international trade is probably better than that of China as a whole.

b. *The Future Possibilities of South China's Economy.*

In addition to the improbability of increasing food output to an adequate level and the bankrupt position of the National Government, South China suffers from a serious lack of investment funds. Private Chinese savings cannot furnish such funds; foreign investment in such a precarious project is unlikely (recent investment by the Reynolds Metals Company and the Westinghouse loan for the production of aluminum in Taiwan are exceptions); remittances from overseas Chinese have fallen off from the prewar level. The only substantial amounts of capital which the Government can now count on for the development of South China are reconstruction funds earmarked from the US Aid Program. Movement of many industrial plants from Shanghai to Hong Kong rather than to South China is symptomatic of the general lack of confidence in the future of the Chinese National Government. In short, future possibilities of South China's economy are dubious.

3. PROSPECTS FOR POLITICAL STABILITY.

T. V. Soong was appointed Governor of Kwangtung Province and Director of the President's Canton Headquarters in September 1947. Presumably, his objective is to create a model administration which will not only serve the National Government in its military activities against the Communists, but will also counteract the Communist program's appeal to the underprivileged and impoverished masses of the region.

Although Soong has been granted extensive military as well as civil authority, there is some doubt as to his actual power. Aside from the presence of armed bandits and Communist guerrillas in South China,* Soong's authority is threatened by representatives of the Provincial administration which he superseded, by dissident Na-

* See Section 4, PROSPECTS FOR MILITARY SECURITY, for discussion of bandit and Communist elements.

~~SECRET~~

~~SECRET~~

tionalist elements who have refuge in Hong Kong, and by the machinations of anti-Soong cliques within the Kuomintang itself. Tendencies toward separatism are deeply rooted in South China, especially in Kwangtung and Kwangsi.

Soong has experienced some difficulty with old officials, who have continued to occupy posts in the new Provincial administration. Many of these have obstructed Soong's efforts toward reform and bandit suppression. In addition Chang Fa-kuei, the superseded Headquarter's Director, has endeavored to undermine Soong's position. Chiang Kai-shek has attempted to placate Chang Fa-kuei and recently has induced him to leave South China for an honorary, albeit ineffectual, post in Nanking.

Hong Kong has become a center of anti-Kuomintang propaganda and operations. The political refugees of Hong Kong have had a strong influence on powerful elements in South China. That Soong regards the activities of these groups as troublesome is disclosed in the fact that he recently initiated calls on two former Kuomintang leaders who are powerful advocates of a coalition government composed of liberal elements and Communists. Subsequent activities of those persons indicate that Soong was unsuccessful in his efforts to bring them back into the Nationalist fold. It is also possible that Soong, in his contacts with these dissident leaders, was endeavoring to secure their cooperation and support, with a view toward the establishment of an independent regime in South China in the event of the collapse of the National Government. It is unlikely, however, that Soong will be disloyal to the Nanking regime so long as it remains fairly effective and is the internationally recognized government of China.

A serious obstacle in the way of political stability in South China stems from power politics within the Kuomintang. The ultra-conservative CC Clique is active in Kwangtung and has been interfering with Soong's Provincial administration. The recent anti-British disorders in Canton are reliably reported to have been inspired, at least in part, by representatives of the CC Clique for the purpose of embarrassing Soong. This group has also been exerting pressure for economic advantages in connection with Soong's plans for industrial development of the region.

Another source of difficulty with which Soong must cope is the attitude of the other provincial governors in South China. In particular, the governors of Hunan, Kiangsi, and Kweichow are supporters of General Chen Cheng, former Nationalist Chief of Staff, who has been unsympathetic toward Soong's activities in the South.

The establishment of close ties between the economies of Kwangsi and Kwangtung is part of Soong's plans for the economic development of the region, but leaders of the former province have always been characterized by a large degree of independence and intractability; the present Governor is a carry-over from the old war-lord regime and has been reported hostile toward the National Government. In Yunnan the war lord Lu Han is once more in authority and is unlikely to cooperate in any plan which will sacrifice his provincial powers to the National Government.

The possibility of maintaining political stability in South China in the event that active fighting spreads to areas throughout the Yangtze Valley cannot be appraised without consideration of the refugee problem that would inevitably accompany a Communist military advance into Central China. A considerable number of home-

~~SECRET~~

~~SECRET~~

less, restless, and unemployed people, with dialects and customs strange to the South, would pose a serious problem of internal security to Soong and the National Government.

Even though Soong possesses uncommon talents for business and administration, it seems most doubtful that he can go far enough toward reconciling the interests of the many diverse groups now working against each other and consequently against the National Government.

4. PROSPECTS FOR MILITARY SECURITY.

The basic reason for the Chinese Government's present emphasis on the economic possibilities of South China is its isolation, in terms of distance and poor communications, from currently active theaters of civil hostilities. In planning for the economic development of South China, the Government is undoubtedly assuming that it can continue to exist even if North China were lost to the Communists and Central China becomes the principal combat zone. Yet, in addition to the economic and political weaknesses described above, military limitations make it questionable whether the National Government could assemble and maintain in South China sufficient armed power to effect continued resistance against the Communists. Internal security problems posed by bandits and malcontents combined with pressure from the Communist Army would require that the National Government support in South China a military establishment quite beyond the sustaining capabilities of the area.

That this region even now has serious problems in maintaining internal order can be seen in the fact that in several provinces Gov. Soong has had to place "bandit suppression" before industrial development. These bandits, some of whom are already oriented toward the Communists, represent the nuclei of valuable potential Communist troop strength. It is believed that Communist organizational cadres and fifth columnists have already infiltrated the area and have begun to lay the groundwork for military actions. The Nationalists, who at the beginning of 1948, had only 70,000 tactical troops in this sector, have been largely unsuccessful in recent local conscription drives.

It is obvious that if the National Government is to mobilize South China as a bastion of anti-Communist resistance, it will be necessary for them to evacuate into the area a considerable portion of the approximately 1,000,000 Nationalist combat troops currently in the area between the Yangtze and the Yellow Rivers, as well as part of the 625,000 combat troops in North China. Several factors militate against this. In the first place, Nationalist military command has typically shown reluctance to abandon any city or region occupied by Nationalist troops even when it is tactically feasible to do so. This reluctance stems, at least partially, from the belief that the denial of these places to the Communists fulfills as great a strategic end as could be served by the deployment of these troops in other sectors of China. Secondly, the difficulties involved in either overland or waterborne transportation would place severe limits on the number of men and the amount of matériel that could be transferred. Thirdly, the maintenance of a large active army is, as indicated, beyond the present or anticipated food and in-

~~SECRET~~

~~SECRET~~

dustrial capacity of South China. (This is especially true if South China is deprived of the resources from the rest of China which, conversely, become available to the Communists.) Therefore, it is unlikely that the Nationalists will choose to evacuate or, when pressed, be able to evacuate, any significant number of tactical troops from present combat zones. They will probably continue to garrison important cities and main rail lines while the Communists envelop such pockets, isolate and destroy individual units, disrupt communications, and continue their economic pressure on the Nationalists, thereby gradually reducing the latter's capabilities of resistance throughout China.

On the other hand, the continued and effective resistance of Nationalist armies supplied from South China depends on substantial shipments from overseas: rice from Southeast Asia, coal from Indo-China, food and industrial materials from Taiwan, raw materials, manufactured goods, and possibly military supplies from the United States. It is likely, then, that the Nationalists will attempt, at all costs, to control the areas along the South China coast.

If the Communists should halt their advance north of the Yangtze in order to consolidate their gains before launching a general military movement into South China, the Nationalists in South China, because they possess very limited capabilities of sustaining resistance to existing internal pressures and inevitable Communist attack, would still require external support.

~~SECRET~~

DISTRIBUTION

The President
Secretary of State
Chief of Staff to Commander in Chief
Secretary of Defense
Secretary of the Army
Secretary of the Navy
Secretary of the Air Force
Executive Secretary, National Security Council
Chairman, National Security Resources Board
Chief of Staff, US Army
Chief of Naval Operations
Chief of Staff, US Air Force
Director of Plans and Operations, General Staff, US Army
Deputy Chief of Naval Operations (Operations)
Director of Plans and Operations, US Air Force
Special Assistant to the Secretary of State, Research and Intelligence
Director of Intelligence, General Staff, US Army
Chief of Naval Intelligence
Director of Intelligence, US Air Force
Secretary, Joint Chiefs of Staff
Secretary, Joint Intelligence Group
Secretary, State-Army-Navy-Air Force Coordinating Committee
Executive Secretary, Military Liaison Committee to the Atomic Energy Commission
Director of Security and Intelligence, Atomic Energy Commission
Chief, Acquisition and Distribution, OICD, Department of State

U. S. GOVERNMENT PRINTING OFFICE
2577-S-1948

RECEIVED

1948 JUN 07 14 40

CIG/ORE

SECRET