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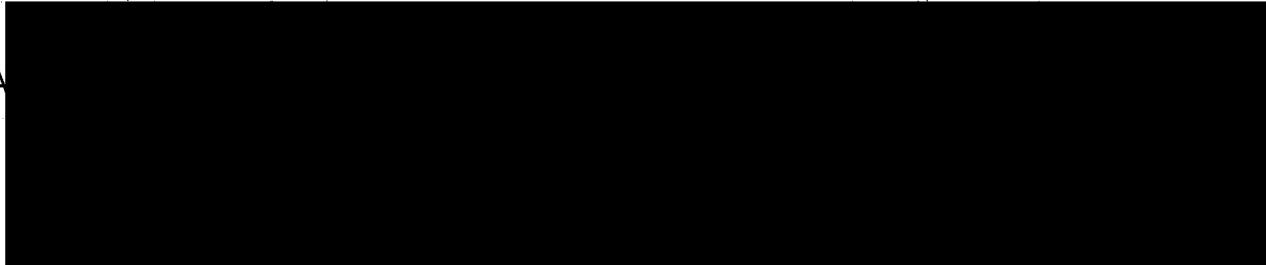
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OFFICE REPORTS AND ESTIMATES, CIA
FAR EAST/PACIFIC BRANCH

INTELLIGENCE HIGHLIGHTS NO. 5
WEEK OF 3 JUNE - 14 JUNE 1948

SECTION I. SUMMARY OF FAR EAST TRENDS AND DEVELOPMENTS

The US Senate Appropriations Committee has voted as a separate item for the next fiscal year, \$125,000,000 for the economic rehabilitation in Japan, Korea, and the Ryukyus Islands (Page 2).



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The reluctance of UNTCOK to regard the new regime in South Korea as national in scope is motivated in part by apprehension on the part of some members of Soviet reaction and by a desire of other members, who have Far Eastern interests, to keep the US in Korea (page 4).

The Chinese military scene, other than sporadic fighting in southwest Shantung and in West Honan remains relatively quiet (page 6). Legislative opposition to the premier's program as well as its open criticism of Chiang's personal position is further evidence of the weakness of the National Government and of the continuing loss of prestige by Chiang Kai-shek (page 6).

In Burma serious political tension resulting from Thakin Nu's announcement of a leftist unity program continues (page 8).

NOTE: In succeeding sections of this Weekly, the following marginal notations are used:

- (1) An asterisk (*) --To indicate that all or part of an item is based solely upon information from State's "S/S distribution" series.
- (2) "A", "B", or "C" --Importance, in B/SE's opinion, of the item, with "A" representing the most important ones.

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In Indonesia the presentation of a "final" US plan for the UN Good Offices Committee (GOC) negotiations has offended the Netherlands Government and may determine the future of the GOC (page 8). A digest of a recent ORE study, Prospects for a United States of Indonesia (page 11).

The Phibun Government in Siam may use strong-arm methods in meeting recent loss of prestige (page 9).

The proposed reestablishment of the Chinese congregation system strains Sino-French relations in French-Indochina (page 10).

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SECTION II. DEVELOPMENTS IN SPECIFIED AREAS

GENERAL

Senate Committee votes rehabilitation aid for Japan

The Senate Appropriations Committee has voted \$125,000,000 for the next "A" fiscal year as a separate item for economic rehabilitation in Japan, Korea, and the Ryukyu Islands under Economic Cooperation Administration supervision. The Department of the Army had requested \$150,000,000 for this purpose. The House had previously refused a similar appropriation for economic rehabilitation in Japan on the recommendation of its Committee on Appropriations. The Committee held that such an activity is related to the general reconstruction program of the ECA and should, therefore, become an integral part of the general economic mission.

The Senate Appropriation Committee also recommended \$1,200,000,000 for government and relief in occupied areas (Germany, Japan, Korea, and the Ryukyu Islands). The Department of the Army had requested \$1,250,000,000 for this purpose. The House voted the sum requested by the Department of the Army but on a fifteen-month basis. Although, the Senate Appropriations Committee reduced the amount requested by the Department of the Army for its government and relief in occupied areas by \$50,000,000, the reduction is more than offset by the addition of the recovery item.

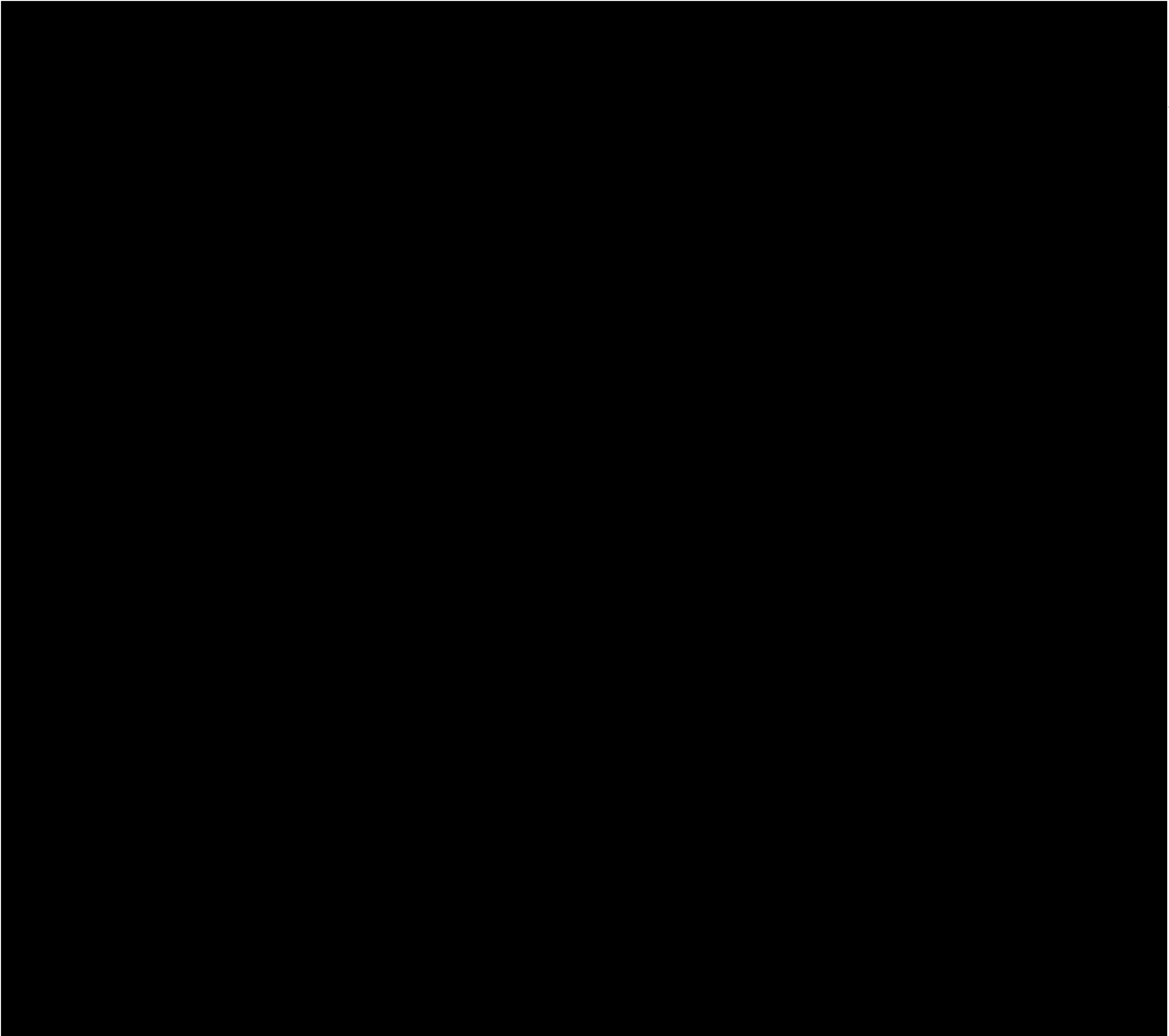
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KOREA

Recognition by the United Nations Temporary Commission on Korea of the recently-elected Korean assembly as a "national" body may be hindered by the opposition of certain members. Consistent with their earlier stand against the holding of elections in South Korea alone, Syria, Australia, and Canada feel that since the assembly does not represent all of Korea neither the assembly nor any government established by it can be designated as "national". India is believed to share this view, which seems to carry sufficient weight within the Commission to produce a highly cautious approach in interpreting its obligations in Korea. Thus, in its press release announcing its readiness to consult with the "elected representatives", UNTCOK carefully avoided any reference to a "national

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assembly " and made it clear that the initiative in consultation must be taken by the Koreans. The Commission's reluctance to regard the new regime in South Korea as national in scope is undoubtedly motivated also by apprehension among some members of Soviet reaction, and by a desire among those members with Far Eastern interests, to keep the US in Korea.

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CHINA

Fighting in southeast Shantung and in west Honan highlighted military activity in China during the past week. Late press reports indicate that the Communists are now engaged in minor raiding activity along the Yangtze River near its mouth. These southern campaigns are characterized by their fluidity and their present inconclusiveness, representing broad-scale applications of well-known Communist guerrilla patterns. Eventually, the full weight of Communist military pressure can be expected in the Northeast, but, as yet, no all-out attacks have been launched in this area. Present Communist efforts in the Changchun sector have resulted in the close investment of that city while the capture of the city's two main airfields has seriously reduced vital airborne supplies. This attack has now taken on the aspects of a holding action, although a full dress assault on the city can be expected if Nationalist resistance proves weak. However, it seems more likely that the main Communist effort will be either in the Chinhsien-Hulutao area or at Mukden. "A"

In the current gloomy Nationalist situation, the Generalissimo is reportedly worried and anxious for immediate, direct US military aid and advice. He is plagued with problems of regional command organization within the framework of his Nationalist Army. Although he apparently realizes the necessity for tightening the command structure, he is constantly faced with the questions of seniority, face, and personal loyalty which he must attempt to equate with the appointment of able, honest men if his regime is to survive. Latest development in this situation is the refusal of General Pai Chung-hai, an able man, to accept the Central China command because of a disagreement over the extent of his power in the area.

Chiang Kai-shek continues to exhibit his inability to cope with the present critical situation in China. While he may be willing to accept more extensive advice from the US, he is not receiving complete cooperation from his subordinates. The legislative opposition to the Premier's program will probably prevent the formulation of any effective policy and is further evidence of the conflicts among governmental cliques. In addition the legislature has even turned its criticism on Chiang's personal position. The Generalissimo is faced with increasing sentiment within Kuomintang circles for his removal and for accommodation with the Communists. Nevertheless there has emerged no leader who is capable of assuming Chiang's position and without him the country would probably revert to a regionalism which would facilitate the extension of Communism over all of China. Despite the fact that such a political collapse remains a possibility, the present chaotic situation could continue for several years. The Communists' problem of consolidating administration over areas under their control may make further extension of their power a slow process. "A"

Chinese anti-American agitation has been continuing with demonstrations spreading to Peiping, Tientsin and Hanking. Ambassador Stuart's speech of "B"

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June 4 defending US policy in Japan and warning against consequences of demonstrations, though generally approved in most official circles, has been widely criticized in the press and by student groups.

Fifth Freedom Traffic, Hong Kong-Shanghai. Despite an agreement under which the Chinese National Government granted the US the right to fly traffic between Shanghai and Hong Kong, the National Government has argued against granting the US the right to Fifth Freedom traffic on through flights between the two ports. They maintain that such traffic constitutes cabotage, inasmuch as China retains sovereign rights over that portion of Kowloon where the Hong Kong airport is situated. The US invoked the UK's participation in this Fifth Freedom traffic in support of its claim for the same right, but the National Government countered with the contention that the participation had been limited by agreement. An authorized British official, however, has denied any limitation of Fifth Freedom traffic between the two ports arising from through traffic, except that the agreement provides for a limit of 50 passengers a week in each direction. The National Government does not want to grant this Fifth Freedom right to the US because in that event it will be claimed by other countries. "C"

Foreign Trade. Initial reaction of exporters and importers to the new exchange link system announced 31 May is generally favorable but cautious. This measure was established primarily to: (1) encourage exports, and (2) provide foreign exchange for imports. To date exports have increased only slightly. "C"

Latest Chinese Customs statistics show that commercial imports for April exceeded exports by almost 50%; with imports valued at US \$25 million and exports US \$16.8 million. The deficit balance for the previous month reached US \$15 million compared with US \$1.7 million for February and US \$3.2 million for January. Petroleum continued as China's principal import in April followed by metals and ores, while piece goods remained the leading export followed by yarns and sugar.

Currency/Prices. Prices rose sharply following recent adverse military developments in Shantung. Exchange controls over foreign currencies failed to halt the upswing.

The Shanghai Market:

	US \$ Exchange (Selling rate)		Wholesale Price of Rice per 172 lb picul
	Official "open"	Blackmarket	
This week (11 Jun 48)	CN \$480,000	CN \$1,600,000	CN \$7,900,000
Week ago (4 Jun 48)	480,000	1,250,000	6,600,000
Month ago (11 May 48)	328,000	1,300,000	5,800,000
Year ago (11 Jun 47)	12,000	38,000	370,000

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BURMA

Political crisis resulting from announcement of Leftist unity program continues. Prime Minister Thakin Nu's recently enunciated leftist unity program appears now to have been an attempt to outbid the insurrectionary Communists and to preserve the coalition Anti-Fascist Peoples Freedom League (AFPFL) which sponsors the present government. The Government's program has not yet been accepted by the Peoples Volunteer Organization (PVO), which is made up of 300,000 - 400,000 loosely organized, unprincipled but relatively well-armed members, and is one of the two major components of the AFPFL. The opportunistic PVO, which among other things advocates outright expropriation of foreign-owned property without payment, seeks to end the civil strife by negotiating for the inclusion of the Communists in the government. There is a strong possibility that members of the PVO, which has no responsible leadership at present, may elect to join the Communists and precipitate a more abrupt disintegration of the AFPFL. Such a development would aggravate the military situation as substantial numbers of the Military Police are presently recruited from the PVO.

Thakin Nu, who insists that the announcement of his leftist program was for domestic consumption, has reaffirmed his belief in the democratic processes of government, but admits that he has created a dilemma for himself.

His announcement that he would retire on 20 July is an attempt to regain his lost prestige by working for unity as head of the AFPFL and not the government. The period during which the duties of Prime Minister are assumed by Bo Let Ya, who has been announced as successor to Thakin Nu, may well be the most critical period. While Bo Let Ya is believed to be competent, he does not appear to be a leader of outstanding caliber, nor has he yet publicly committed himself to any definite program.

Although a cabinet shake-up which may accompany the change in Prime Ministers could conceivably have a temporary stabilizing effect on Burmese politics, it is likely that the PVO, with Communist support, will continue to press their demands thereby prolonging a serious threat to the stability of the Burmese Government.

INDONESIA

Presentation of "final" US plan for GOC negotiations may determine future of GOC. The presentation on 10 June to Premier Hatta of the Indonesian Republic and to Acting Governor General Van Mook of the Netherlands Indies Government of drafts of a "final" US plan as a basis for the continuation of UN Good Offices Committee (GOC) negotiations and the creation of the proposed United States of Indonesia (USI) has thoroughly upset the Netherlands Government and may determine the future of the GOC. The draft plan, which was initiated by the US delegation of the UN Good Offices Committee (USGOC) and after minor changes approved by the

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INDONESIA (continued)

Australian GOC Delegation, was formulated as the result of USGOC concern over the probable Dutch course of action in Indonesia. USGOC believes that the Dutch will take one of two alternatives: (1) insist on a political agreement which will reinstitute the full authority of the Netherlands Indies Government throughout Indonesia and then follow these demands by the use of Netherlands forces to suppress all dissident elements, or (2) report the dispute back to the UN Security Council with the recommendation that it be dropped from the agenda on the grounds that the Republic has not adhered to the principles of the January 1948 Denbyville Agreements. The USGOC draft, which is an attempt to forestall a precipitate Dutch move, contains the following features: (1) convocation of a constituent assembly on the basis of Indonesian-wide internationally observed elections; (2) constituent assembly acting as a provisional parliament and forming a provisional government; (3) full powers of internal self-government to be transferred to provisional government by the Netherlands; with the Republic transferring to the provisional government all the federal functions it now exercises; (4) constituent assembly to draft and ratify USI constitution and ratify Netherlands-Indonesian Union statute (in regard to the foregoing full protection of Netherlands economic interests to be given so far as consonant with full sovereignty of both nations); (5) USI then to be regarded formed as a sovereign state. In essence the plan paves the way for rule by the Indonesians and for the gradual relinquishment of Dutch control.

USGOC is convinced that its plan is a feasible compromise for all parties interested in the future of Indonesia and it cites the following arguments in behalf of the plan: (1) it would preserve Dutch as well as US economic interests in the area; (2) it is the only plan whereby fair representation can be offered to all states in the provisional federal government; (3) it will give assurance to Indonesian nationalists, who, according to USGOC, are still looking to the West for support. USGOC believes that the acceptance of this plan is an urgent matter in view of the situation in Indonesia; the Netherlands Government insists that it is in no position to make a major decision on Indonesia until after the Dutch elections in July and may be expected to resist any early consideration by the GOC of the US proposals.

SIAM

Phibul Government faces loss of prestige. The two-month old government of Premier Phibul has had no perceptible success in the implementation of its major domestic policies, despite promises in April to effect changes in the political-economic situation. In addition, the Phibul government has lost considerable prestige as a result of the extra-legal profiteering by Luang Kach (Army Deputy Cinc) and his associates. Although mounting opposition to Kach is appearing among elements of the Army and Navy, Phibul apparently considers Kach indispensable as a financial backer and catalyst to hold together the anti-royalist and royalist elements in the Army, which

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SIAM (continued)

is Phibul's strength. The unimproved "cost of living" situation, the unsteady financial activities of the November 1947 coup procedure, and the increasing activity of opposition political groups appear to be slowly undermining the Phibul Government.

The doubtful stability of the political situation is tapered somewhat by the optimism resulting from an unexpected post-war high in rice exports which is building up foreign exchange revenues that could materially contribute to the rehabilitation and expansion of Siam's economy. To maintain political control, however, Phibul is currently faced with decisions which include: (1) continuing the present policy of allowing graft in limited high official positions in the interest of efficient administration, (2) cracking down on Kach's activities, hoping to mollify the growing opposition, and (3) continuing present policies, hoping for some success in lowering the high cost of living, but suppressing dangerous opposition by totalitarian measures. In view of the growing political unrest, the government may be compelled to resort to frequent strong-arm methods.

FRANCE IN INDOCHINA

Chinese congregation problem may become diplomatic issue. A recent decree signed by High Commissioner Bollnert, indicates that the French intend to re-establish the Chinese congregation system (registration and organization of Chinese by provinces of origin) in Tonkin. Temporary appointments, pending the setting up of electoral lists, have been made for directors of the Cantonese and Fukinese groups. Since the Chinese want a single association of all Chinese in Indochina without autonomy for groups from individual provinces, there have been strong protests and considerable resentment. The Chinese Consul General in Hanoi has maintained that this move is contradictory to a verbal promise made by the French when they signed the Sino-French Treaty in February 1946 to the effect that the congregation system would not be reinstated. The Chinese Consul General predicts that friendly relations between France and China will be adversely affected if the French fail to use diplomatic channels to reach a settlement of this problem.

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SECTION III. DIGEST OF IMPORTANT STUDIES AND ESTIMATES

The Prospects for a United States of Indonesia

Indonesia is important to the US and to Western Europe as a source of raw materials necessary both to the rehabilitation and development of the economies of those countries, and to the creation of stockpiles of certain strategic materials. Besides being the principal Far Eastern source of oil, Indonesia produces 15% of the world's tin, 34% of the natural rubber, and 90% of its cinchona bark. Because of the need for such strategic materials, loss of Indonesia to Japan in 1942 was keenly felt by the Allies; in another war or in preparation for one, utilization of the whole Indonesian potential would be a valuable asset.

Dutch-Republican strife has, since the war, made full exploitation of Indonesian raw materials impossible. Though future friction between the two sides may not find expression in as much violence as has been seen over the past few years, continuation of the underlying disagreements will interfere with the availability of commodities from the productive areas of Java and Sumatra.

Developments in Indonesia for a considerable period in the future will center around the formation of the United States of Indonesia (USI) as a federal framework of government to be established in the territory of the Netherlands Indies, and the efforts of the Dutch on one side and of the Indonesian Republic on the other to realize in the USI the basic objectives which have dictated their policies since the end of World War II.

Dutch policies and actions will be directed toward the preservation of Dutch influence in the archipelago and will therefore work toward neutralizing that of the Republic by attempting to confine the scope of Republican authority to as small an area as possible and encircling the Republic in a federation of pro-Dutch states. Republican policies and actions will be directed toward the replacement of Dutch influence in the USI and its component states by predominant Republican influence and will therefore work for the revival of its prestige, the rapid delegation of Dutch powers to Indonesian governing bodies, the early creation of a sovereign and independent USI, and the utilization of the federal structure to Republican advantage wherever possible.

A prolongation of the conflict, which now appears probable, will delay the restoration of political stability and the rehabilitation of the area's economy, and may enhance the possibility of a final outcome unfavorable to the interests of the US. The achievement of stability and economic rehabilitation would best be furthered by the development of the USI along a middle course, affording expression to Indonesian nationalism but permitting the continuation of Dutch assistance and guidance in Indonesia. Pursuit of such a middle course, however, is likely to require the continuing influence of third powers in the Indonesian problem. Both the Dutch and the Republic

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on the other hand, will continue their efforts to divert third-power influence in the direction of their respective objectives, the Dutch bringing to bear their position in Europe and the technical advantages they can offer in developing the Indonesian economy while alleging Communist infiltration in the Republic, and the Republic concentrating on the economic assets which it may be able to offer to the world.

The Prospects for a United States of Indonesia

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