

United States Relations With

China

With Special Reference
to the Period 1944-1949

BASED ON THE FILES OF THE DEPARTMENT OF STATE

U. S. GOVERNMENT PRINTING OFFICE: 1949

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REPEAL OF CHINESE EXCLUSION ACTS, 1943

As a further indication of American policy, the President, on December 17, 1943, signed an Act, which had been passed by large majorities of both Houses of Congress, removing long-standing legislative discriminations against Chinese. The Act repealed the Chinese exclusion laws, established an annual Chinese immigration quota, and made legally admitted Chinese eligible to naturalization as American citizens. The enactment of this legislation had been specifically recommended by President Roosevelt in order to "correct an historic mistake" and give "additional proof that we regard China not only as a partner in waging war but that we shall regard her as a partner in days of peace."

AMERICAN ACKNOWLEDGMENT OF CHINA AS A GREAT POWER

American recognition of the status of China as one of the Great Powers was demonstrated on two other occasions in the fall of 1943. The United States insisted that China be included as a signatory, together with the United Kingdom, the U.S.S.R., and the United States, of the Declaration of Four Nations on General Security, signed in Moscow on October 30, 1943, which recognized the right and responsibility of China to participate jointly with the other great powers in the prosecution of the war, the organization of the peace, and the establishment of machinery for post-war international co-operation.³² The Cairo Declaration, issued on December 1, 1943, by President Roosevelt, Prime Minister Churchill, and Generalissimo Chiang Kai-shek, following their meeting at Cairo, Egypt, in the latter part of November 1943, declared their "purpose" that "Manchuria, Formosa, and the Pescadores shall be restored to the Republic of China."³³ On his return from the Cairo Conference President Roosevelt could say, in his Christmas Eve message to the Nation: "Today we and the Republic of China are closer together than ever before in deep friendship and in unity of purpose."

³² Subsequently China participated as a Great Power in the Dumbarton Oaks conversations in the summer and fall of 1944, and was one of the sponsoring Powers of the United Nations Conference on International Organization, which met at San Francisco in 1945, and which formulated the Charter of the United Nations. The Charter granted China a permanent seat on the Security Council.

³³ See annex 33.

"The Acting President's request appears to be overlapped by the meeting between him and you and your foreign colleagues on April 17, and to be overtaken by events

"As you are aware, the only Congressional authority presently existing for aiding the Chinese Government is the legislation extending the availability of the residual China Aid Act funds. The Department's views on this subject were set forth in the Secretary of State's letter to Senator Connally, of March 15, re the McCarran proposal. For your information, the text of the letter to Senator Connally was not released by the Department which wished to avoid possible adverse effect on the Chinese Government and Li's position in the negotiations with the Communists."

On April 23 the Acting President, the Prime Minister and the remaining officials of the Ministry of National Defense left Nanking for Shanghai, en route to Canton. The Chinese Communist forces were by this time across the Yangtze River in strength and Nationalist Armies deployed for the defense of the river had been ordered to withdraw to the south. Chinese Communist forces occupied Nanking on April 24 and were in a position to move toward Shanghai. In succession, the Communist forces occupied Hankow on May 16-17, Shanghai on May 25, and Tsingtao on June 2.

The general effect of these developments on the National Government's position was described by the Embassy in a report of May 1:

"Despite the desperate plight of the Government and agreement among all leaders of the necessity of continuing resistance to the Communists, the basic conflict of authority between Li and the Generalissimo has not been resolved. The Generalissimo came out with a public statement expressing confidence in final victory, though the war may continue for three years, and pledging support to Li. However, there is no indication he really intends to relinquish power and Li and Pai are increasingly bitter. This struggle probably will continue to hamstring Government resistance."

XI. FORMOSA

The case of Formosa is a pertinent one in the record of American efforts to encourage reform within the Chinese Government. By the terms of the Cairo Declaration of December 1, 1943, the United States and China declared their intention that Formosa should be restored to China. In September 1945 the administration of the island was taken over from the Japanese by Chinese forces assisted by small

American teams pursuant to the Japanese Instrument of Surrender and General Order No. 1 issued by the Japanese Government at the direction of the Supreme Commander for the Allied Powers, dated September 2, 1945.

China found Formosa in favorable circumstances since Japan had made constructive use of the great natural resources of the island and the living standards of the population were higher than anywhere on the Chinese mainland. It possessed a good industrial complex and was more than self-sufficient in foodstuffs. The native population for 50 years had been under the rule of a foreign invader and therefore welcomed the Chinese forces as liberators. During the Japanese occupation the principal hope of the people had been reunion with the mainland. Instead of utilizing this highly favorable situation to its own advantage the National Government appointed to the governorship General Chen Yi, a long-time associate of the Generalissimo, who some years before had given up the governorship of Fukien under curious circumstances. The new Governor arrived with an imposing retinue who proceeded with great efficiency to exploit Formosa. In addition the local population was ruthlessly excluded from any important role in public life and was made to feel that it was again under the rule of a conqueror.

The economic deterioration of the island and the administration of the mainland officials became so bad that on February 28, 1947, popular resentment erupted into a major rebellion. In the ensuing days the Government put down the revolt in a series of military actions which cost thousands of lives. Order was restored but the hatred of the mainland Chinese was increased.

After the rebellion the American Ambassador in Nanking attempted to persuade the Generalissimo that National Government tactics in the long run could never succeed and that the Government by its policy was destroying a source of wealth it desperately needed at that time. The Generalissimo, who professed to be unaware of conditions as they were reported to him by the Ambassador, and who relied on the findings of a Chinese investigating mission whose findings were in large part published and exonerated Chen Yi, was led to request that a memorandum be prepared for him setting forth in detail conditions as American officials saw them. This was done.⁵⁷

The facts set forth were such that General Chen Yi had finally to be relieved of his post as Governor, and in May 1947 a civilian, Wei Tao-ming, former Ambassador to the United States, was named as his successor. During the ensuing year and a half, Governor Wei made an

⁵⁷ For text of memorandum to the Generalissimo, see annex 169.

honest and earnest effort to remedy the situation. The military was kept out of sight, some Formosans were taken into the Government, encouragement was given to the local economy and the Governor himself attempted to isolate the island from the inflationary and destructive forces on the mainland, though many of the key officials were not responsive to his authority. Although it cannot be said that economic conditions improved, it can be said that the situation did not become measurably worse.

During his Mission to China, General Wedemeyer on August 17, 1947, reported to the Secretary of State as follows:

"Our experience in Formosa is most enlightening. The administration of the former Governor Chen Yi has alienated the people from the Central Government. Many were forced to feel that conditions under autocratic rule were preferable. The Central Government lost a fine opportunity to indicate to the Chinese people and to the world at large its capability to provide honest and efficient administration. They cannot attribute their failure to the activities of the Communists or of dissident elements. The people anticipated sincerely and enthusiastically deliverance from the Japanese yoke. However, Chen Yi and his henchmen ruthlessly, corruptly and avariciously imposed their regime upon a happy and amenable population. The Army conducted themselves as conquerors. Secret police operated freely to intimidate and to facilitate exploitation by Central Government officials. . . .

"The island is extremely productive in coal, rice, sugar, cement, fruits and tea. Both hydro and thermal power are abundant. The Japanese had efficiently electrified even remote areas and also established excellent railroad lines and highways. Eighty percent of the people can read and write, the exact antithesis of conditions prevailing in the mainland of China. There were indications that Formosans would be receptive toward United States guardianship and United Nations trusteeship. They fear that the Central Government contemplates bleeding their island to support the tottering and corrupt Nanking machine and I think their fears well founded."

In January 1949, as the Communists were preparing to cross the Yangtze, Governor Wei was summarily removed and replaced by General Chen Cheng, who proceeded to restore military rule. In recent months the population of Formosa has been increased by an estimated 400,000 civilians and over 300,000 military refugees from the mainland. With them they brought the mainland inflation and increased the population to a point which the island may not be able to support. In March 1949 American officials who had surveyed the economic

deterioration reported that "mounting economic dislocation will intensify economic friction leading to increased political tension unless remedial action is taken."

In summary, the views of American officials have been that the island is badly and inefficiently run at a time when the best possible efforts are needed unless developments on the mainland are simply to be transferred to Formosa.

Statement by the Chinese Minister of Information (Liang)¹⁰

May I add a few remarks here concerning Liu Tse-hua's report on the Kuomintang-Communist conversations in the People's Political Council?

To the best place, Mr. Liu said in his report, published in the local newspaper on September 18 and in the *Shi Wu Jih Pao* on September 17, "Minister S. C. Liang once stated in a press conference that conversations between the Kuomintang and Communists have come to a standstill." This is a misinterpretation, as I never said a thing like that. What I did say is "the negotiations are still continuing," and "though the conversations are not progressing at a pace as anticipated, it would be incorrect to say that they are running altogether smoothly."

Secondly, Mr. Liu reported, "Minister Liang told the pressmen of Chungking at a press conference held on July 28 that a part of the Kuomintang-Communist problem has been solved but another part is tractable." Words again differed from my original version which says "Under the present circumstances, a part of the Kuomintang-Communist problem has been solved but it is too much to expect a total solution yet." You may recall that I made those remarks in a statement on the possible trend of the Kuomintang-Communist conversations, and made them on your repeated request.

Summary Notes of Conversations Between Vice President Henry A. Wallace and President Chiang Kai-shek, June 21-24, 1944¹¹

CONVERSATION AT PRESIDENT CHIANG'S RESIDENCE, JUNE 21—5 p. m.

Present: President Chiang
Vice President Wallace
Dr. T. V. Soong (translating)

President Chiang asked Mr. Wallace whether he had any message from President Roosevelt. Mr. Wallace replied that he had nothing in writing but that he had notes on a conversation with President Roosevelt just prior to his departure from Washington. Mr. Wallace said that President Roosevelt had mentioned the inflationary situation in China but that he (Wallace) did not wish to discuss the subject in Chungking due to the absence in America of the Minister of Finance, Dr. Kung. Mr. Wallace said that President Roosevelt had talked about the Communists in China. President Roosevelt had assumed that, in as much as the Communists and the members of the Kuomintang were all Chinese, they were basically friends and that "nothing should be final between friends". President Roosevelt had cited the Bryan Treaty and had quoted Al Smith and Charles Francis Adams to support his point. President Roosevelt had indicated that if the parties could not get together they might "call in a friend" and had indicated that he might be that friend.

¹⁰ Based on a press conference of Sept. 18, 1944 (*China Broadcast*, 1947-1948, p. 94).

¹¹ By John Carter Vincent, Chief of the Division of Chinese Affairs, who accompanied the Vice President to China. The files of the Department do not contain any indication of the existence of a report in written form made by Mr. Wallace to President Roosevelt or of the nature of any oral report made.

. . . Mr. Wallace expressed the opinion that there should not be left pending any question which might result in conflict between China and the U.S.S.R. President Chiang suggested that President Roosevelt act as an arbiter or "middleman" between China and the U.S.S.R. (NOTE: President Chiang's suggestion was apparently prompted by Mr. Wallace's earlier statement that President Roosevelt was willing to act as an arbiter between the Communists and the Kuomintang. Mr. Wallace made no comment at the time. However, after discussing the matter with Mr. Vincent that evening, Mr. Wallace made it clear to President Chiang the next morning before breakfast that President Roosevelt had not suggested acting as arbiter between China and the U.S.S.R. and that, whereas he felt that the United States would be quite willing to use its good offices to get the U.S.S.R. and China together, it could not undertake the role of "middleman" in negotiations between the U.S.S.R. and China or become a party or guarantor of any agreement reached between China and the U.S.S.R.)

Mr. Wallace said that he felt that the people of the United States were deeply interested in seeing an increase in Chinese agricultural efficiency which will permit a sound industrialization. The United States desires a strong, democratic China which would make for a healthy political situation in the country. The United States had always had this idea and it felt most strongly in that regard now. Mr. Wallace believed that no matter how dark the present situation was in China, if China exerted herself to the utmost, it could with help from the United States and a kindly attitude on the part of Great Britain, realize its destiny. There would be no time to lose in effecting improvements once the war was over.

President Chiang expressed a desire for friendly understanding with the U.S.S.R. Mr. Wallace mentioned a conversation which he had had in Tashkent with Ambassador Harriman. Ambassador Harriman had told Mr. Wallace of a recent discussion he had had with Mr. Stalin during which China was discussed. President Chiang asked to see a copy of the memorandum which Mr. Wallace had mentioned. Mr. Wallace said he did not have a copy. He recalled that Mr. Stalin had stressed the need for a united China eager to carry on the war against Japan. Mr. Wallace suggested that Dr. Soong discuss the matter with Mr. Vincent, who had probably a better idea of the contents of the memorandum since he had had a number of conversations with Ambassador Harriman. (NOTE: That evening Dr. Soong asked Mr. Vincent about the matter, requesting to see any notes that Mr. Vincent might have made. Mr. Vincent said that he had only his memory to rely upon and informed Dr. Soong of those portions of the memorandum which he thought it appropriate and judicious to give him. Specifically he told Dr. Soong that Mr. Stalin had agreed to President Roosevelt's point that support of President Chiang was advisable during the prosecution of the war; that Mr. Stalin had expressed a keen interest in there being reached a settlement between the Kuomintang and the Chinese Communists, basing his interest on the practical matter of more effective fighting against Japan rather than upon any ideological considerations; that Mr. Stalin had criticized the suspicious attitude of the Chinese regarding the Sakhalin Agreement with Japan; and that Mr. Stalin felt the United States should assume a position of leadership in the Far East.)

Toward the end of the conversation Mr. Wallace described to President Chiang the developments in agriculture which he had observed in Siberia. The discussion ended sometime after 6 p. m.

DISCUSSION WITH PRESIDENT CHIANG, JUNE 22—4:30 p.m.

Present: President Chiang
Madame Chiang
Vice President Wallace
Dr. T. V. Soong
Dr. Wang Shih-chieh
Messrs. Vincent, Lattimore, and Hazard

Mr. Wallace mentioned the poor showing the Chinese troops had made. He referred specifically to a story he had heard about the Chinese peasants attacking the soldiers in the Honan campaign because they were running away from the Japanese. President Chiang then undertook to explain the situation. He said that Chinese reverses were due to a loss of morale on the part of the soldiers; that this loss of morale was to a large extent due to the economic situation. Mr. Vincent asked President Chiang whether he understood correctly that it was the morale of the troops rather than lack of equipment which had caused the reverses. President Chiang replied, "both". (Note: The next day, at the request of Madame Chiang, President Chiang explained his reference to the effect of the economic situation on the morale of the troops. He said that the soldiers at the front were worried about their families who were suffering at home because of the inflation. He also said that the condition of the troops themselves was adversely affected by inflationary high prices and scarcity of goods. In this latter connection he stated however that the situation was better now than it had been some months ago.)

President Chiang then described what he considered to be basic in the present unfortunate military situation in China. He said that the Chinese people have fought for seven years under conditions of great hardship, and that they had expected help from abroad; that they had expected an all-out Burma campaign early this year and this would have resulted in bringing relief to the Chinese Army; and that the failure to initiate an all-out Burma campaign had had a decidedly adverse effect on Chinese morale. The Chinese people felt that they had been deserted. President Chiang then referred to his conversations with President Roosevelt at Cairo. He said that President Roosevelt had promised an all-out campaign in Burma early in 1944 but that at Tehran President Roosevelt had reversed his decision, indicating that the necessary amphibious landing craft would not be available for such a campaign. President Chiang said that this reversal of decision had had a very unfortunate reaction in China. He referred to his conversation with President Roosevelt, at which time he had told President Roosevelt that, unless very early action were taken to open up Burma he could not count upon a continuance of effective Chinese resistance to the Japanese. Recent developments had proven him correct in his estimate. Mr. Wallace said that he recalled having a conversation with President Roosevelt, either personally or in a Cabinet meeting, regarding this matter but that he did not recall the details. He asked Mr. Vincent regarding the matter but Mr. Vincent said he did not have any detailed information concerning the Cairo conversations. (Note: The day of Mr. Wallace's departure—June 24th—President Chiang asked Mr. Wallace to inform President Roosevelt that he, President Chiang, understood the necessity under which President Roosevelt was working when he reversed his decision regarding the Burma campaign; that he was therefore not criticizing President Roosevelt for his decision; but that he wished to remind President Roosevelt that the prediction which he, President Chiang, had made at the time was sound.)

President Chiang then discussed his relations with the American Army in China. He said that American army officers clearly indicated their lack of confidence in China but that he, President Chiang, "continued to have full confidence in his army". He asked Mr. Wallace to report this to President Roosevelt and to tell him that, in spite of the attitude of the American Army, he would be guided by the advice of President Roosevelt. President Chiang, somewhat apologetically, (but with obvious intent to get across a point) mentioned what he described as a minor incident involving General Stilwell. He said that in the early stages of the Honan campaign he had asked General Stilwell for diversion to his air force of 1,000 tons of gasoline, but that General Stilwell had very abruptly refused the request, saying that the Chinese Army could get the gasoline from its own "over the hump" supplies. President Chiang indicated that it was difficult for him to operate in the face of such an uncooperative attitude. In response to Mr. Wallace's query, President Chiang said that he lacked confidence in General Stilwell's judgment. He went on to say that critical comment in the American press of the Chinese Army and the attitude of the American Army in China had adverse effects on Chinese morale but that he retained the confidence of his army and confidence in his army. Mr. Wallace commented upon the remarkable degree of faith which China had in the Generalissimo. At this point (5 p. m.) President Chiang, Mr. Wallace, Dr. Soong, Dr. Wang Shih-chieh, and Mr. Vincent went into the drawing room to continue the discussion, which lasted until 7:30 p. m.

Mr. Vincent made a brief recapitulation of that portion of the preceding conversation which had dealt with the military situation in China and the question of the present unfavorable position of the Chinese Army and asked President Chiang whether he had any suggestions with regard to measures which might effect an improvement. President Chiang said that he had nothing to suggest at that time. He, President Chiang, went back again to the Cairo Conference decision regarding the Burma campaign, stating that if it could have been carried out the effect on morale in China would have been very great even though the material assistance which might have been afforded China would not have been large, and that the current defeats would have been avoided.

Mr. Wallace asked President Chiang about the "New Life" movement. President Chiang gave a brief description of the movement, stating that its purpose was to train the people in having more disciplined lives and to raise their standards of thinking and conduct.

President Chiang next referred to criticism of China appearing in the American press and said that this criticism should be stopped. He said that the Chinese people were losing hope of receiving aid from abroad.

President Chiang next launched forth into a lengthy complaint against the Chinese Communists. He said that China suffered greatly because of the Communists. He said that the people of the United States did not understand the situation. Although the Communists were not entirely responsible for the situation in China, their subversive actions and propaganda had had a very unfavorable effect on Chinese morale. He referred to the first year of the war when he had received the cooperation of the Communists "within the law", but said that the Communists now were not subject to discipline and refused to obey his orders. He said that the attitude of the Chinese toward the Communists was an important factor in the situation; that the Chinese people did not regard the Communists as Chinese, but regarded them as "internationalists", subject to the orders of the Third International. Mr. Wallace mentioned the

fact that the Third International had been dissolved but President Chiang indicated that the situation had not been altered by that fact.

Mr. Wallace mentioned remarks that were made to him by Mr. Martel Hall, Manager of the Peking branch of the National City Bank of New York, who had traveled from Peking through Communist territory to Chungking in 1943. Mr. Hall had spoken in terms of high praise of the Communists, had said that they continued to have confidence in the Generalissimo, but that they felt the Generalissimo was not correctly informed with regard to the situation in Communist areas. President Chiang said that Mr. Hall, like many other Americans, (he mentioned specifically Colonel Carlson) was under the influence of Communist propaganda. President Chiang said that he did not like to use harsh language regarding the Communists; that he would welcome them back into the Government fold; but that the fact was that the low morale of the people and the army was due to Communist propaganda. He said that the Communists desired a breakdown of Chinese resistance against the Japanese because this would strengthen their own position. Mr. Wallace expressed amazement at this statement. President Chiang admitted that the Communists desire the defeat of Japan but that they were now convinced that this defeat could be accomplished without Chinese resistance. They therefore hoped for the collapse of the Kuomintang prior to the end of the war because such a collapse would enable them to seize power, whereas, if the Kuomintang continued in power until peace the Communists would have no opportunity to supplant it. President Chiang referred to the clever Communist propaganda to the effect that they were not tied to the U. S. S. R., that they were in fact nothing more than agrarian democrats. As a matter of fact, the Communists follow the orders of the Third International. The Chinese Government cannot openly criticize the Communists for their connection with the Third International because it is afraid of offending the U. S. S. R. Mr. Wallace referred to the patriotic attitude of the Communists in the United States and said that he could not understand the attitude of the Chinese Communists, as described by President Chiang. President Chiang said that this difference in the attitude of the American and the Chinese Communists might be explained by the fact that there was no possibility of the American Communists seizing power, whereas the Chinese Communists definitely desired to do so in China. He then said that the United States was far removed from the U. S. S. R. but that the U. S. S. R. would not feel safe if the Communists were not in power in China. He then laughingly remarked that the Chinese Communists were more communistic than the Russian Communists.

Mr. Vincent inquired as to the progress of conversations between the Communist representative in Chungking, Lin Tzu-han, and the Kuomintang representatives of which Dr. Wang Shih-chieh was chief. President Chiang said he desired to make the Communists live up to their propaganda in regard to their desire for cooperation and offensive action against the Japanese. He said that there had been Communist proposals for a settlement and Kuomintang counter-proposals. The Kuomintang proposal was very simple: support the President, support the Government, and support the war effort. The Chinese Government requires obedience from the Communists and incorporation of the Communist Army within the Chinese Army as its first essential to a settlement. Secondly, the Chinese Government requires that territory now under Communist control become an integral part of China administratively. If the Communists would accede to these two demands they would receive equal treatment with other Chinese in China, they would be guaranteed political amnesty, and given the right to continue

as a political party with freedom of assembly and discussion. President Chiang also said that if the Communists would accede to these requirements, the group of American officers would be allowed to proceed to North China as requested. They would not have direct contact with the Communists but would go under the auspices of the Chinese Government to train "converted" Communist troops. Mr. Wallace asked President Chiang whether he was optimistic with regard to a settlement. President Chiang said it was possible if the Communists showed sincerity. If a settlement were reached President Chiang said he could carry out his program for democracy earlier than now expected. He said that he would try his best to reach a settlement.

President Chiang again reverted to the subject of Communist propaganda. He asked Mr. Wallace to inform President Roosevelt that Communist propaganda has his highest respect. President Roosevelt should bear in mind that the Communists could not openly use the U.S.S.R. for support but that they could and did use the U.S.A. (opinion) to force the Kuomintang to accede to their demands. Such tactics make a settlement difficult. The best assistance that the United States could give in this matter would be to display "aloofness" to the Communists. They would then show a greater willingness to reach a settlement with the Kuomintang.

At this juncture, Dr. Wang Shih-chieh said he wished to offer some explanation on the Chinese Government's proposal to the Communists. He said that whereas the Chinese Government required that the Communists submit to its authority it was not the intention to interfere in local administration and that it was not the intention to remove local officials or even army officers who showed themselves cooperative.

Mr. Wallace said that the Generalissimo's description of the situation filled him with "hope and fear". He said that China's relations with the U.S.S.R. were threatened by the attitude demonstrated in conversations which he had had with Mr. Wei and Admiral Shen (Minister of Agriculture) and by President Chiang's remarks. Mr. Wallace did not mention what it was in the situation that filled him with "hope".

Mr. Wallace stated that American Army officers felt that Chinese interpretation of the significance of the transfer of Japanese troops from Manchuria to China was incorrect. Mr. Wallace also pointed out that if, as President Chiang stated, the Chinese Communists were linked with the U.S.S.R., then there was even greater need for settlement. He also expressed his appreciation of the frankness with which President Chiang had spoken.

President Chiang again advised that we adopt an attitude of "coolness" toward the Communists. He said that the United States Army was anxious that all military power in China be utilized against the Japanese but the United States Army did not realize the threat which the Communists constituted to the Chinese Government and overestimated the utility of the Communists against the Japanese. He went on to say that he understood President Roosevelt's policy and asked that President Roosevelt be informed that he, President Chiang, desired a political solution of the problem.

Mr. Wallace asked whether it was not possible to reach an understanding on a "lower level" with a view to maximum use of forces in the north. Mr. Vincent asked what President Chiang thought would be the adverse effects of sending the United States Army intelligence group to Communist areas *now* without awaiting a settlement. President Chiang said that "haste does not make for speed". He said, "please do not press; please understand that the Communists are not good for the war effort against Japan". With this evasive reply the conversation was concluded.

DISCUSSION WITH PRESIDENT CHIANG, JUNE 23—9 A. M.

Present: President Chiang

Vice President Wallace

Dr. Hollington Tong (translating)

Dr. Wang Shih-chieh

Mr. Lattimore (assisting in translating)

Mr. Vincent

Mr. Wallace reported conversations with General Marshall and with Secretary Stimson before leaving America in regard to China's situation in an endeavor to persuade President Chiang that we are not interested in "Chinese Communists" but are interested in the prosecution of the war. (He and Mr. Vincent had decided upon this line of approach the night before in order to avoid further lengthy discussion of the Communists *per se*.) He spoke of the military situation in East Asia in general terms and of the need for taking all steps that might further hasten the end of the war and reduce the loss of American lives. He felt that the United States Army intelligence group in North China would be able to gather intelligence which would save the lives of American aviators. Mr. Vincent again stressed the point that whereas he appreciated that President Chiang was faced with a very real problem in handling negotiations for a settlement with the Communists, the American Army was also faced with a very real problem with regard to obtaining intelligence from North China. He mentioned specifically the need for intelligence by the B-29 group at Chengtu. He pointed out that the American Army had no interest whatsoever in Communists but that it had for very urgent reasons an interest in carrying on the war against Japan from China. He urged that President Chiang's problem of reaching a settlement with the Communists and the United States Army problem of obtaining intelligence be treated as separate—as indeed they were.

President Chiang, completely reversing his position of the evening before, said "that can be done". He said that the group could go as soon as it was organized without reference to a settlement with the Communists. He said, however, that they must go under the auspices of the National Military Council rather than under the auspices of the United States Army, and added that Chinese officers must go with them. He then stressed the point that the Communists did not take his orders and gave concrete illustrations. He said with some feeling that the United States Army must realize how essential it is to have a unified command. Much pressure has been brought to bear by the United States Government to have the Chinese Government reach a settlement with the Communists but the United States Government has exerted no pressure upon the Communists. He said that the American Government should issue a statement that the Communists should come to terms with the Chinese Government. He said that the United States Army attitude supported the Communists and requested Mr. Wallace upon his return to America to make it clear that the Communists should come to terms with the Chinese Government. In response to a remark by Mr. Wallace, President Chiang said there were no present questions which would cause conflict with the U.S.S.R. Mr. Vincent again pointed out that solution of President Chiang's important problems of relations with the Communists and the U.S.S.R. need not precede the despatch of military observers to North China. President Chiang said that the military observers would be permitted to go.

President Chiang said, "I am confident that what President Roosevelt stands for is good for China and for the furtherance of the war." "But," he said, "one of the things for which we are fighting this war is the maintenance of order. Please tell President Roosevelt that I will follow his advice but I must insist on the maintenance of law and order and upon the observance of discipline."

Mr. Wallace again stressed the point that there should be no situation in China which might lead to conflict with the U.S.S.R. President Chiang said that the Chinese Government had gone far out of its way to come to an agreement with the Communists in order to avoid conflict with the U.S.S.R. and added that anything not detrimental to the sovereignty of the Chinese Government would be done to avoid conflict with the U.S.S.R. At this point Mr. Wallace again said that the United States could not be expected to be a party to negotiations between China and the U.S.S.R. He also said that President Chiang's formula for settlement with the Communists might prove transitory unless China reached an understanding with the U.S.S.R. He referred again to Ambassador Harriman's discussion with Mr. Stalin as indicating the necessity for an agreement with the U.S.S.R. President Chiang stated that he fully shared Mr. Wallace's views and that the Chinese Government would seek an early opportunity to have discussions with the Government of the U.S.S.R. Although Mr. Wallace had indicated that the United States might not be able to assist in the negotiations he continued to hope that there could be found ways whereby the United States could be of assistance.

Mr. Wallace stated that another reason why a settlement with the Communists might prove temporary was the economic situation in China and expressed a hope that measures could be taken as soon as possible to improve the economic lot of the Chinese people. President Chiang endorsed this view. Mr. Wallace said that in so far as the Communists have power and influence it is due to economic conditions. He said that the Communist revolution in Russia in 1916 was brought about primarily by economic distress. He admitted that it was very difficult to do anything now after seven years of war, but he pointed out how easy it would be to attribute to the Communists social unrest in China when actually this unrest would be due to economic distress.

President Chiang indicated that the making of concessions to the Communists did not matter as long as discipline could be maintained. Mr. Wallace said that unity should express itself in welfare of the people if communism was to be avoided. Mr. Vincent suggested that the best defense against communism in China was agrarian reform. Mr. Wallace said that when the war was over it would take much energy and foresight for the Chinese Government to avoid the fate of the Kerensky government in Russia. President Chiang said that the Chinese Government was proceeding with these considerations in mind.

The conversation ended at 11 a. m. and was resumed at 5 p. m. In the meantime, Mr. Wallace had visited the Embassy in Chungking, had received a message from President Roosevelt advising him to press President Chiang to permit the despatch of the Army observer group, and had arranged that General Ferris join the conversation in the afternoon. Participants were: President Chiang, Mr. Wallace, Dr. Soong (translating), Dr. Wang Shih-chieh, Mr. Lattimore (assisting in translating), Mr. Vincent, General Ferris and Mr. John Service (aide to General Ferris).

Mr. Wallace read to President Chiang President Roosevelt's message. Mr. Vincent made a brief recapitulation of the morning's conversation and asked President Chiang whether his understanding was correct that the observer group

might proceed to North China as soon as it was organized. President Chiang replied in the affirmative. Mr. Vincent then asked for an explanation of the conditions under which the group might proceed. There ensued some discussion as to whether the word "auspices" was a correct translation of President Chiang's Chinese term describing the relationship of the National Military Council to the United States Army group. It was decided that whereas "auspices" was not an exact translation, it was about as good as any that could be found and that whatever the translation, President Chiang did not intend that the group would have to operate under orders from the National Military Council.

General Ferris then asked for clarification on a number of points: whether the United States Army group would be allowed direct communication facilities with the American command. President Chiang said they would be. General Ferris said that all information gathered would be made available to the Chinese military authorities. General Ferris asked a number of questions. President Chiang said that he should confer with General Ho Ying-chin in regard to details. General Ferris asked for President Chiang's full support and received the President's assurances in that respect. President Chiang referred to the use of the word "mission" in describing the group and said that he did not believe that it should be so called. At Madame Chiang's suggestion (she had joined the group some minutes before) it was decided to call the group the "United States Army Investigation Section".

President Chiang said that he wanted the American Army authorities to bear in mind that in as much as the Communists did not accept orders from him he could not guarantee the protection of the group while in Communist territory but that he would give all possible aid. General Ferris asked when the group might go. President Chiang said it could go as soon as it was organized. General Ferris said that it would probably comprise 15-20 men. He asked President Chiang whether there would be Chinese officers accompanying the group, and whether the group would be allowed freedom of movement. He pointed out that the members of the group would not of course remain together but would "fan out" on individual assignments. President Chiang said that General Ferris should see General Ho with regard to the composition of the group. General Ferris expressed the hope that General Ho would place no impediments in the way of the group's carrying out its mission. President Chiang said, "See General Ho tomorrow at 4 p. m. He will have my instructions." (Note: At this point General Ferris and Mr. Service withdrew.)

Mr. Wallace presented to President Chiang a scroll sent by President Roosevelt to the people of Chungking. President Chiang said, "Representing the people of Chungking, I accept this scroll as a priceless symbol which they will hold forever in gratitude and reverence."

President Chiang then said he had a few questions to raise with Mr. Wallace. He requested Mr. Wallace to mention to President Roosevelt the question of Allied Military Government of Occupied Territories (AMGOT) in the Far East, and suggest to President Roosevelt that there be an agreement between British, American and Chinese authorities on this question. President Chiang said that at Cairo he had raised with President Roosevelt the question of a Chinese-American economic commission to handle projects of post-war reconstruction in China. He hoped that Dr. Kung would have an opportunity to discuss this matter while he was in Washington and requested Mr. Wallace to lend whatever assistance he could. Mr. Wallace expressed approval of the idea and said he would do what he could.

Mr. Wallace referred to a comment he had made to President Chiang soon after his arrival in Chungking regarding the absence of any Russian territorial ambitions in the Far East. Without modifying that statement he wished to add an explanation which had occurred to him since the first conversation. He said that the U.S.S.R. wanted a warm water port in the Far East and that President Roosevelt had suggested that Dairen might be made a free port. Mr. Wallace said that in making this remark he was not acting under instructions from President Roosevelt or speaking officially. President Chiang said that he had discussed the matter with President Roosevelt at Cairo and had indicated his agreement provided the U.S.S.R. cooperated with China in the Far East and provided there was no impairment of Chinese sovereignty.

President Chiang referred to the present economic distress (lack of consumer products) in China and said that Dr. Kung was going to ask for an increase of "over the hump" tonnage to provide for the importation of 2,000 tons of civilian supplies each month. He said that it was very important that this request be granted from the military as well as the economic point of view. In response to Mr. Wallace's question President Chiang said that these civilian supplies would be comprised of cloth, medicines and spare parts. Mr. Wallace mentioned the possibility of using C-54s now that Myitkyina was in Allied hands but he pointed out that it might prove very difficult to persuade the American Army to permit civilian supplies to take up air cargo space. President Chiang asked Mr. Wallace to take a personal interest in the matter.

President Chiang asked Mr. Wallace to inform President Roosevelt as follows: "If the United States can bring about better relations between the U.S.S.R. and China and can bring about a meeting between Chinese and Soviet representatives, President Chiang would very much welcome such friendly assistance." If the United States would "sponsor" such a meeting President Chiang would go more than halfway in reaching an understanding with the U.S.S.R. A conference with regard to Pacific affairs was desirable and the United States would be the logical place for such a conference. Madame Chiang interpolated to suggest that it be called the "North Pacific Conference". Mr. Vincent inquired whether they were not speaking of two related but separate matters, that is, discussions between Chinese and Soviet representatives in regard to their problems, and a conference of nations bordering on the North Pacific to discuss more general problems. He said that it would seem desirable to have the Sino-Soviet discussions prior to any North Pacific conference. Dr. Soong said that a North Pacific conference might be used as a cloak for discussions between Chinese and Soviet representatives. Mr. Wallace said that Dr. Soong would be of value in Washington in laying the foundation for such a conference. President Chiang said that he could not be spared from Chungking and added, laughingly, that with Dr. Kung gone and Madame Chiang planning to go abroad, Dr. Soong was his only mouthpiece in speaking to Americans.

The conversation ended at this point—7 p. m.

June 24th—During the hour's ride from President Chiang's residence to the airport (10 to 11 a. m.) President Chiang made the following comments (Madame Chiang interpreting) which he requested Mr. Wallace to consider as a message from himself to President Roosevelt:

1. The attitude of President Roosevelt at the Cairo Conference, his warmth, etc., has immense historic value to the people and army of China.

2. President Chiang is gratified over the abrogation of the unequal treaties and efforts on behalf of the Exclusion Act.

3. Mr. Wallace's visit to China, as the representative of President Roosevelt, to bring about accord with Russia shows great friendship for China.

4. Mr. Wallace's visit at this dark hour will help the morale of the troops and give hope that America will continue to aid China.

5. Assure the President that President Chiang understands the necessity under which the President acted when he changed plans at Tehran. Nevertheless, President Chiang foresaw what the change meant. When President Chiang sent a strong, frank memorandum to President Roosevelt it was because he fore-saw what is now happening. If the Generalissimo sees that China's collapse will come he will tell the President, but China has not yet arrived at the state of collapse which he predicted to the President. Things are not today as bad as he feared.

6. President Chiang greatly respects the President's character, his views, etc.

7. President Chiang was deeply touched when Mr. Wallace told him about how badly the President felt about the Tehran change relating to the Generalissimo personally. Therefore, he again appreciates most deeply that Mr. Wallace should come out on behalf of Russo-Chinese friendship.

8. The Chinese Communist question is an internal political problem but he would nevertheless welcome the President's assistance. He feels that the Chinese Communists are not men of good faith. Their signature is no good. He would not like to see the President blamed for Communist failure to carry out commitments. Just the same he is happy to have the President's help if the President, after mature consideration, decides he would like to give his help. The Generalissimo would not consider the President's participation as meddling in China's internal affairs, but the Generalissimo is a true friend who knows the Chinese Communists through and through and thinks that no matter what the Communists say they will do, it will not be carried out, in which case the President's prestige would suffer a great loss. The Generalissimo wants the President to know that the conflict between the Communists and the Central Government is not like that between capitalism and labor in the United States—the situations are not analogous.

9. The Generalissimo is eager to have closer cooperation and understanding with the President—but how? Too many channels through State Department. Churchill has personal representative in Carton de Wiart who handles both political and military matters. Could President Roosevelt pick someone like this? He could perform an invaluable service. Today military cooperation is very difficult because of personnel. He feels that Chennault is most cooperative. Stilwell has improved, but has no understanding of political matters—he is entirely military in outlook.

10. The Generalissimo has the utmost confidence in Dr. Kung. In helping Dr. Kung the President will be helping the Generalissimo.

11. The Generalissimo is shaping everything toward the democratic path. He wrote *China's Destiny* to get the Communists to fall into line. The Generalissimo wants the Communists to be a political party. He plans such advances in agrarian program that the Communists will have no opportunity to stir up social unrest.

12. He hopes after the war to get the interest rate for farmers down to 10 per cent and hopes to promote land ownership by breaking up large land holdings.

determinative for the restoration of peace in the country. The decision thus proclaimed by the President has since received the general support of the people, who have through various messages and public statements echoed their prompt support for a peaceful settlement of the question at issue between the government and the Communists.

The United States Government has on many occasions in the past demonstrated its friendly concern over the state of affairs in China and has cooperated with the Chinese Government for the promotion of international peace. The Chinese Government wishes hereby to assure the United States Government of its sincere desire for a peaceful settlement with the Chinese Communist Party and particularly avail itself of this opportunity to ascertain in the views of the United States Government on this subject. The Chinese Government will welcome any suggestion by the United States Government which may lead to an early restoration of peace in China. The Chinese Government further signifies its readiness, through the possible intermediary of the United States Government, to initiate negotiations with the Chinese Communist Party with a view to attaining the end stated above.

Similar notes are being communicated to the French, the Soviet and the British Governments. An early reply from the United States Government will be greatly appreciated.

169

Memorandum on the Situation in Taiwan²⁸

Background

The Formosan Chinese greeted the surrender of Japanese authority to the Chinese with immense enthusiasm on October 25, 1945. After fifty years under Japanese control and intensive economic development they welcomed a return to China, which they had idealized as the "Mother Country". The richness of the island and the relatively light population pressure had made rapid economic and social developments possible. Agriculture, food processing and light industry in the best years produced an overseas trade valued at U.S. \$225,000,000. To improve Taiwan's economic value the Japanese had raised the general standard of living. Public health standards were high and literacy widely spread among the masses. Formosans had come to place a high value on orderly procedures in the courts and on the orderly enforcement and observance of government regulations, for they found order both profitable and necessary in a complex and semi-industrialized economy.

With the removal of the Japanese the Formosans looked forward to a return to profitable trade and an expansion of their already established industries, with the markets of China ready to receive all that they could produce. The surpluses which had always gone to Japan would now, they thought, go to China. They expected to return to control of the properties taken from them by the Japanese through fifty years and expected a larger share in the management of their own enterprises. Under pressure of the Japanese overlords who were alien to Taiwan, they had developed an island-wide sense of social solidarity. They were free of all internal political strife. The Japanese had rigorously excluded all Communist influence and activity, and had indeed filled the people with fear, dislike and distrust of Communist doctrines. They revered the Generalissimo,

²⁸ Submitted by Ambassador Stuart to President Chiang Kai-shek on Apr. 18, 1947.

believed the Three People's Principles meant new opportunities, and looked forward expectantly to participation in the Central Government. The year 1946 was one of increasing disappointment. Though the majority of petty officials, clerks and office boys of the new Administration were Formosans, they were virtually excluded from all important government offices and from important administrative posts. The legal necessity to place all confiscated Japanese properties and enterprises under Government control led to the creation of syndicates and combines in every field in which the Japanese had had an interest. Though the Government owns (and must heavily subsidize) these companies, the salaried and privileged administrators are in a position to squeeze freely. It is alleged that raw and finished materials and agricultural products find their way into the hands of unscrupulous officials for their use in private trading and smuggling. Judging from Taiwan's former capacity to produce and the fact that its enterprises continue, qualified Formosans estimate that published records show only one-tenth of actual receipts. As an example, it is alleged by persons formerly connected with the Department of Agriculture and Forestry that fishing boats were withdrawn from their normal bases in 1946 and were used for smuggling in the interests of the authorities concerned.

Formosans have been virtually excluded from the higher levels of economic administration. These persistent allegations of corruption lead them to place responsibility on members of the Government who appear and reappear in lucrative posts as Commissioners, members of Committees, and Directors in a manner which concentrates full control of the total economy in the hands of a clique close to the Governor.

There was a progressive decline in Formosan economic enterprise, especially where there was competition with ex-Japanese interests. Unemployment among Formosans has progressively increased, either through direct discharge (frequently to make room for unqualified newcomers) or by the suspension or abolition of various established enterprises which failed to be profitable under the new management. Whereas about 50,000 Formosans had been employed normally in industrial work, by January 1947 UNBRA officials estimated that less than 5,000 were so employed. Whereas the top government officials created a Taiwan Industrial and Mining Enterprises Syndicate with a capital of two billion Taiwan yen, in which the Commissioners and their associates play leading roles, the Department of Mining and Industry announced an appropriation of only eight million Taiwan yen for loans in aid of private (i. e. Formosan) industrial enterprises after June 1946.

The Quarantine Service broke down and the Public Health Service was badly shattered. Cholera epidemics occurred for the first time in about 30 years; bubonic plague appeared after an even longer absence. Educational standards in the schools were markedly lowered. Friction spread through the schools between Formosans and mainland students and teachers. Trouble between mainland police and local petty officials increased. The press was filled with public charges and counter-charges of corruption and lawless acts among government officers. Formosans claimed that corruption and nepotism among mainland officials increased rather than abated during the year. The cost of living soared. Bank of Taiwan wholesale commodity price indices show advance as follows from November 1945 to January 1947: foodstuffs 3,323 to 21,058; clothing 5,741 to 24,483; fuel 963 to 14,091; fertilizers 139 to 37,559; building materials 949 to 13,612. (Pre-war June 1937 is used as a basis.) Prices shot up most rapidly during February 1947. These figures on the whole reflect the drain of Taiwan wealth from the island, with little or no return to it.

Although the two rice harvests of 1946 were good, a rice shortage grew acute in December 1946 and January 1947. The Government instituted a tax in kind for rice lands, ostensibly to secure an equal distribution, and repeatedly threatened to use military force to punish private hoarders which it blamed for the shortages. In fact there is substantial evidence to support the Formosans in their charges that large quantities of grain were smuggled out or went into private control of officials. It is popularly believed that the army is shipping unpublicized quantities to the northern front on the mainland.

Three governmental acts

Against this background of increasing economic and social dislocation three governmental acts in January and February appear to have crystallized Formosan resentment toward economic policies and toward individuals in the Government.

(1) Throughout 1946 Formosans sought permission to elect city mayors and *hsien* magistrates, in order to ensure themselves of some direct control over local police and over economic functions and public services. The announcement of China's new Constitution was greeted with relief. Prominent Formosan leaders counseled that demands for local elections could wait until the Constitution would become effective at the end of 1947. In early January, however, the Governor General announced that although the Constitution would be effective on the mainland on December 25, 1947, it would be impossible for the Government to allow local elections of mayors and magistrates in Formosa until December 1949. This had an effect which stirred political discussion to a new pitch. Formosans state that until they can elect their own representatives at all levels of local government they will have no security of person; they cannot control the local police, ensure the enforcement of law nor enjoy security of property.

(2) On February 1 the Government announced a new policy for the disposal at auction of certain large categories of Japanese property—principally real estate abandoned by the Japanese and now occupied by Formosans on a low rental basis. The announced procedures were such that it was widely believed that Formosans without great wealth and its influence would be unable to buy real estate which they had believed would be available, especially in view of the fact that it had been taken from them more or less forcefully by the Japanese over the course of fifty years.

This announced procedure was interpreted as a threat to the security of low-income level Formosans who, having lost their former homes during the war, are not anxious to face eviction from houses now occupied if, as they anticipate, new mainland landlords should suddenly greatly increase rentals. (Rental is the one item in living costs which has not risen excessively since 1945, due to the removal of several hundred thousand Japanese.)

(3) The third governmental act was a February 14 announcement of a series of complex financial and trading regulations which Formosans believed effectually concentrated monopoly control in the hands of a small group of officials. It is believed by some observers that these were announced precipitously and rashly in the belief that the crisis in Shanghai was about to provide an opportunity long awaited to establish a semi-autonomous economy for Taiwan, giving into the hands of a few mainland people an absolute control of all external trade and a general control of internal production and business as well.

As an island people, Formosans have been sensitive to overseas trade, and after the Japanese surrender they anticipated the reestablishment and expansion of seaborne commerce. They had proposed to organize their capital for production and individual business, out of which they had expected to be taxed in support

of the Central Government and of the local island administration. These new measures seemed to the Formosans not only a threat to return them to the subservient position they had suffered under the Japanese, but to threaten to destroy the very means to create wealth within the Island.

THE FEBRUARY INCIDENT

Spontaneous protest and unorganized riots

On the evening of February 27 certain armed Monopoly Bureau agents and special police agents set upon and beat a female cigarette vendor, who with her two small children, had protested the seizure of her small cash as well as her allegedly untaxed cigarettes. She is reported to have died soon after as a result of the beating at police hands. An angered crowd set after the agents, who shot at random, killing one person before they escaped into a civil police station. Their Monopoly Bureau truck and its contents were burned in the street, although the agents were allowed to be taken away, on foot and unmolested, from the police station by military police called for that purpose.

On the morning of February 28 a crowd estimated at about 2,000 marched in orderly fashion from the area in which the incident had occurred, past the American Consulate and toward the Monopoly Bureau Headquarters. Placards and banners announced that they intended to protest the action of special armed agents, to demand a death sentence for the responsible man, and to demand the resignation of the Monopoly Bureau Director.

Unfortunately, as they made their way across the city, two Monopoly agents were discovered in a side street molesting a vendor. They were beaten to death by an angry crowd which was not taking part in the initial demonstration. This happened near the Taipeh Branch Monopoly Bureau Office buildings which the crowd began to sack. Its contents were burned in the streets. Mainland employees were driven out and if caught were beaten mercilessly. The crowd's anger enlarged to include employees and property of the Trading Bureau, another monopolistic organization greatly disliked. The Consul and the Vice Consul observed the orderly gathering before the Monopoly Bureau Headquarters, where no Monopoly Bureau official would receive the petition which had been brought about noon. Monopoly Bureau police and a few military police were guarding the entrances.

Meanwhile at about one o'clock someone announced to the radio audience that demands were being made on the Government to put an end to its monopolies. All Formosans were urged to support the movement.

The parade, meanwhile, left the Monopoly Bureau for the Governor's office where it was intended to present the petition for reform. At about two o'clock it reached a wide intersection adjacent to the government grounds. Without warning a machine gun mounted somewhere on the government building opened fire, swept and dispersed the crowd and killed at least four. Two consular officers drove through the square immediately after the shots were fired. Two of the dead were picked up a few minutes later by an UNRRA officer.

This shooting was the signal for a citywide outburst of anger against all mainland Chinese, regardless of rank or occupation. Many were beaten, cars were burned and in some few cases offices and houses of minor officials were sacked and the contents burned in the streets. It was observed that the Formosans refrained from looting. One Formosan was found attempting to take cigarettes from a burning heap; he was forced to kneel and beg forgiveness

from the crowd and was then driven away. Another was severely beaten. Tires and other equipment were observed to have been left untouched on overturned cars, and remained in evidence until the Formosans lost control of the city March 9. Martial law was invoked in the late afternoon February 28. Armed military patrols began to appear in the city, firing at random wherever they went.

At 10 o'clock a. m., March 1, the Chairman of the Taipei Municipal People's Political Council invited the Council, representatives of the National and Provincial P.P.C. Councils and the Taiwan representatives to the National Assembly, to form a committee for settling the so-called Monopoly Bureau Incident. It was decided to send a delegation to call on the Governor General, requesting, among other things, that a committee be formed to settle the problems jointly by the people and the Government. These men recognized that with the firing on the crowd at the government building, the issues had become much greater than mere punishment of Monopoly Bureau agents and a financial settlement for the injured and dead. They urged the Governor to lift martial law so that the dangers of a clash between the unarmed civil population and the military would be averted. This the Governor agreed to do at midnight, March 1, meanwhile forbidding meetings and parades.

On that day busses and trucks, filled with squads of government troops armed with machine guns and rifles, began to sweep through the streets, firing indiscriminately. Machine guns were set up at important intersections. Shooting grew in volume during the afternoon. At no time were Formosans observed to have arms and no instances of Formosan use of arms were reported in Taipei. Nevertheless, the military were evidently allowed free use in what appeared to be an attempt to frighten the people into obedience.

At approximately 5 o'clock, the Governor General broadcast a message which appears to have increased the anger of the people. He stated that the Monopoly Bureau incident had been settled by a generous payment of money. Without referring to the machine gun fire from his own office he accused the Formosans of increased rioting, but generously promised to lift martial law at midnight.

"There is one more point," the Governor broadcast. "The P.P.C. members wished to send representatives to form a committee jointly with the Government to settle this riot. This I have also granted. If you have any opinion, you can tell me through this Committee." (*Hsin Sheng Pao*, March 2, 1947.)

While he was broadcasting, members of the American Consulate staff witnessed a severe clash between armed government forces and unarmed crowds. Mounted troops had killed two pedestrians near the compound. A crowd gathered. A few hundred yards away Railway Administration special armed police suddenly opened fire from within the Administration building and killed two more pedestrians. The crowd turned on any mainland Railway Bureau employee found nearby. Two more pedestrians who looked like coolies were shot about 300 feet from the Consulate gates. Then as the bodies were carried off the crowd was observed to assemble again some distance from a mounted patrol near an intersection. Suddenly, with no warning, a long burst of machine gun fire swept the area. Some of the wounded and dead were carried past the Consulate gates; it is stated reliably that at least 123 were felled by this burst and that 25 died. How many of the injured walked away is not known.

On this afternoon 25 mainland officials from the neighboring Railway Administration compound took refuge in the Consulate. Although the crowd observed them enter, no attempt was made to pursue them. They were removed eight hours later under police guard.

Organization for settlement recognized by General Chen

The temper of the populace was uncertain. Inflammatory handbills and posters began to appear in increasing numbers. There was a general demand that the Government of Taiwan must be thoroughly reformed.

At 12 noon March 2 the "Untaxed Cigarette Incident Investigation Committee of the Taipei Municipal P.P.C." called on the Governor General, and with this began the attempt to meet and clarify the fundamental political and economic problems which lay back of the uprisings. The Governor had with him the Secretary-General, the Commissioners for Civil Affairs, Communications, and Industry and Mining.

The Governor appears to have been told by the Committee that there could be no peace as long as roving armed patrols were permitted to sweep the streets with gunfire and so paralyze all normal activity.

It is believed that if fully determined the people could have overpowered and ended the patrols which were moving only in the central part of the city.

The Governor therefore agreed to several "temporary demands", i.e., stipulations of conditions to be maintained while the people organized their fundamental demands for reform in government. These included (1) an agreement that a schedule of fundamental reforms should be prepared for discussion by March 10, after representatives of the people throughout the island could be consulted; (2) a promise that the Government would not bring additional troops into the city while these consultations were in progress; (3) a volunteer youth organization under the supervision of the Mayor and the municipal Chief of Police (a mainlander) would maintain law and order temporarily; (4) communications would be restored at once in order to avoid a food shortage.

The Governor agreed to broadcast at 3 o'clock p. m. and agreed to reduce the armed patrols gradually, meanwhile ordering them to patrol with rifles and other arms down on the floor of the trucks and busses, for use only if crowds were found disturbing the peace.

At 2:30 o'clock the first general meeting of the Governor's representatives (the Commissioners of Civil Affairs, Police, and Communications, and the Taipei Mayor) and the Settlement Committee met in the Public Hall, with a capacity audience of spectators. It was announced that as a result of the morning conference the Governor had decided to readjust the Committee to bring into it representatives of the Chamber of Commerce, the Labor Union, student organizations, popular organizations, and the important Taiwan Political Reconstruction Association which has been for many months the most outspoken and emphatically nationalist group urging reform in General Chen's government.

The following temporary demands were formulated:

1. All people arrested in connection with the riots will be released;
2. The Government will pay death gratuities and compensations to the wounded;
3. The Government will not prosecute persons involved;
4. Armed police patrols will be stopped immediately;
5. Communications will be restored immediately.

While in session the meeting was disturbed by volleys of shots outside. When the Governor's promised 3 o'clock broadcast was postponed for almost two hours, it began to be rumored that he was delaying in hope that troops would reach the city from the south and he would not be forced to make public acceptance of the demands.

At approximately 5 o'clock, March 2, the Governor again broadcast, concluding his speech with the statement:

"A committee will be organized to settle the incident. Besides Government officials and members of the P.P.C., representatives from the people of all walks of life will be invited to join the committee so that it may represent opinions of the majority of the people." (*Hsin Sheng Pao*, March 3, 1947)

On the night of March 2, word reached Taipei that the Governor actually had attempted to get troops to the city. Citizens near Hsinchu city, however, were reported to have halted the troop carriers by removing rails from the main line.

From this time (March 3) the confidence of the people appears to have been undermined. The moderate and conservative element represented by the Committee members were willing to trust the Government's word and to proceed with negotiations. The more skeptical elements agreed to support the Committee in its efforts but at the same time determined to prepare resistance to any military action which might be set against them.

This delegation, received by five Government Commissioners and Chief of Staff Ko, urged that the patrols be withdrawn, for they were still firing wildly in the streets despite the Governor's promises. After long discussion the Government representatives agreed:

1. All troops to be withdrawn by 6 p. m., March 3;
2. Public order to be maintained by a temporary Public Security Service Corps including gendarmes, police, and youths;
3. Communications to be restored at 6 p. m.;
4. Military rice stores to be released to avert crisis;
5. Any military personnel making a disturbance to be sent to General Ko for punishment;
6. Any civilians disturbing the peace to be punished according to law, on the guarantee of the Committee;
7. Troops absolutely would not come from the south to the north. (General Ko is reported to have promised "to commit suicide" if his personal guarantee were broken.)

Meanwhile, a Taipei City Provisional Public Safety Committee was organized by the Settlement Committee. Its members were recommended by the Committee and were to constitute a "Loyal Service Corps." Its effective period was to end on the day normal conditions were restored in Taipei. Meanwhile, events at Taipei were known throughout Taiwan. It appears that Formosans became deeply alarmed at persistent rumors that troops were coming from the mainland, and began to arm themselves to resist a military occupation, insisting, however, that they wanted reform, not civil war. Formosans began to take over local administrative posts everywhere held by mainland Chinese. Government troops offered some resistance but it appears that in many places mainlanders agreed to relinquish their posts peacefully, as at Huallenkang (Karenko). The aborigines are reported to be cooperating fully with the Formosan Chinese. Without prearrangement or preparation, by March 5, Formosan-Chinese were in the ascendancy or in control throughout the island.

This called for larger organization in order to prevent ruffians under guise of "local patriotism" from taking advantage of confusion. On March 4, the Settlement Committee enlarged its representative character by creating 17 sub-divisions or local Settlement Committees throughout the island. Circumstances beyond control forced the Committee to so enlarge its duties, and in doing so it announced:

"We should acknowledge the aim of this action, that there is no other desire except to demand a reformation of Government." (*Hsin Sheng Pao*, March 5, 1947)

This was without doubt necessary, for the absence of mainland office-holders from their duties threatened to paralyze the administration.

The Governor and his Commissioners received the Committee's representatives at 3:30 p. m., March 4, and the Governor took occasion to remind them that his duties were related to both national administration and local government and expressed his hope that the people would come forth with more proposals for local administration. He stated that he had ordered the police and gendarmes not to carry weapons.

March 5 was quiet at Taipei. Shops were open and primary schools resumed classwork. The city appeared to be returning to normal while the Settlement Committee worked toward a reform program which would remove the sources of conflict between administration and people.

There was intense popular anxiety, however, for rumors of impending troop movements grew stronger. It was said that the March 10 date set for presentation of the reform proposals would be too late. Each rumor strengthened the arguments of the men who desired to organize resistance and made the task of the officially recognized Settlement Committee more difficult. In an attempt to clarify its own position and to strengthen its influence over dissident elements the Settlement Committee published basic Articles of Organization clearly defining its temporary character.

A Youth League of considerable potential significance came into being, stressing as basic principles a desire to make Taiwan a model province of China and to hasten Dr. Sun Yat-sen's program of National Reconstruction. The founder, former president of the Chamber of Commerce, Chiang Wei-chuan, said:

"We absolutely support the Central Government but will eradicate all corrupt officials in this province. This is our aim which I hope every one of you fully grasp." (*Chung Wei Jih Pao*, March 6, 1947)

Spurred by fears of a military invasion, on March 6 the Settlement Committee completed its draft of items of reform which the Governor had agreed to discuss and to refer to the Central Government wherever necessary. The Committee's executive group acted as sponsors and included four members of the National P.P.C., six members of the Taiwan Provincial P.P.C., five members of the Taipei Municipal P.P.C. and two "reserve members". Everyone of these men had received the approval of the Government as P.P.C. members and represent in fact the most conservative elements in Taiwan. One is a former Consul General at San Francisco, and ex-Mayor of Taipei. The reform proposals, made possible March 7, are set forth on pages 15-18 of this despatch.

The Army's explicit promise that the Central Government would not send troops

On March 8 Major-General Chang Wu-tao, Commander of the Fourth Gendarmerie Regiment, at 12:00 noon called on the Settlement Committee at its headquarters. According to the press and to witnesses he made the following categorical statement:

"I can guarantee that there will be no social disturbances if the people do not try to disarm the soldiers. I want especially to report to you that the demands for political reforms in this province are very proper. The Central Government will not dispatch troops to Taiwan. I earnestly entreat the people of Taiwan not to irritate the Central Government, but to cooperate to maintain order. I can risk my life to guarantee that the Central Government will not take any military actions against Taiwan. I speak these words out of my sincere attachment to this province and to the nation. I hope Taiwan will become a model province after these political reforms." (*Hsin Sheng Pao*, March 9, 1947.)

The landing of Government troops and subsequent terrorism

Foreign observers who were at Keelung March 8 state that in mid-afternoon the streets of the city were cleared suddenly by machine gun fire directed at no particular objects or persons. After dark ships docked and discharged the troops for which the Governor apparently had been waiting. Fairly reliable sources estimate that about 2,000 police were landed, followed by about 8,000 troops with light equipment including U. S. Army jeeps. Men and equipment were rushed to Taipei. It is reported that about 3,000 men were landed at Takao simultaneously. Troops were reportedly continuing to arrive on March 17.

Beginning March 9, there was widespread and indiscriminate killing. Soldiers were seen bayonetting coolies without apparent provocation in front of a Consulate staff residence. Soldiers were seen to rob passersby. An old man protesting the removal of a woman from his house was seen cut down by two soldiers. The Canadian nurse in charge of an adjacent Mission Hospital was observed bravely to make seven trips under fire into the crowded area across the avenue to treat persons shot down or bayoneted, and once as she supervised the movement of a wounded man into the hospital the bearers with her were fired upon. Some of the patients brought in had been shot and hacked to pieces. Young Formosan men were observed tied together, being prodded at bayonet point toward the city limits. A Formosan woman primary school teacher attempting to reach her home was shot in the back and robbed near the Mission compound. A British business man attempting to rescue an American woman whose house was being riddled with machine gun fire from a nearby emplacement was fired upon and narrowly escaped, one bullet cutting through his clothing and another being deflected from the steering gear of his jeep. Another foreigner saw a youth forced to dismount from his cycle before a military policeman, who thereupon lacerated the man's hands so badly with his bayonet that the man could not pick up his machine.

Anyone thought to be trying to hide or run was shot down. Looting began wherever the soldiers saw something desirable. In the Manka area, near the Consulate, a general sacking by soldiers took place on March 10; many shopkeepers are believed to have been shot.

On March 11 it was reported that a systematic search for middle school students had begun during the night. School enrollment lists were used. A broadcast earlier had ordered all youths who had been members of the Security Patrol or the Youth League to turn in their weapons. Concurrently, all middle school students were ordered to remain at home. If a student was caught on the street while trying to obey the first order he was killed; if the searchers found a weapon in his house, he met a like fate. If a student was not at home his brother or his father was seized as hostage. A reliable estimate was made that about 700 students had been seized in Taipei by March 13. Two hundred are said to have been seized in Keelung. Fifty are reported to have been killed at Matsuyama and thirty at Kokuto (suburbs of Taipei) on the night of March 9.

From March 8 the Government instituted searches for all members of the Settlement Committee and for all editors, lawyers and many prominent businessmen who had in any way been identified with the activities of the Committee between March 1 and 8. Wang Tien-teng, Chairman of the Settlement Committee, was seized and is alleged to have been executed about March 13. Tan Gim, a leading banker, was taken from his sick bed; Lim Mo-sei, editor of the *Min Pao*, was seized in the night and taken without clothing. Gan Kin-en, head of a large private mining interest, was arrested.

Middle school and normal school teachers began to be seized or to disappear March 14. One teacher who had been deprived of his license as a public prosecutor after exposing a case of police corruption in early 1946, was taken on March 15. Another public prosecutor involved in the arrest and punishment of mainland police officers convicted in court of killing an official of the Taichung Court, is said to have been literally dragged out of the Taipei Higher Court by the convicted man who had apparently won release after March 8. A minor accountant in the Taiwan Navigation Company at Keelung was called out and shot, with the explanation that the Manager did not think well of him.

On March 13 a tense crowd was observed near the homes of the Vice Consul and the U.S.I.S. Director; wailing women who came away incoherently said that two students had just been beheaded. UNRRA personnel observed bodies lying along the road between their hostel and the city office. Unclaimed bodies were reliably reported to be lying in the ditches and along an embankment within 2,000 feet of the foreign mission compound. A foreigner reported that on March 10 while at the Army Garrison Headquarters he observed some 15 well-dressed Formosan-Chinese bound and kneeling, with necks bared, apparently awaiting execution. On March 14 and 15 many bodies began to float into the inner harbor at Keelung. Foreigners saw sampans tow them in for possible identification by anxiously waiting people. It is estimated by a reliable Keelung observer that some 300 people had been seized and killed there.

After three days in Taipei streets, government forces began to push out into suburban and rural areas. Mounted machine gun patrols were observed along the highroads 15 to 20 miles from Taipei shooting at random in village streets in what appeared to be an effort to break any spirit of resistance. Manhunts were observed being conducted through the hills near the UNRRA hostel. Foreigners saw bodies in the streets of Tamsui.

By March 17 the order of seizure or execution seemed to have become, successively, all established critics of the government, Settlement Committee members and their aides, men who had taken part in the interim policing of Taipei, middle school students and teachers, lawyers, economic leaders and members of influential families, and finally, persons who in the past had caused members of the Government or their appointees serious loss of face. On March 16 it was rumored that anyone who spoke English well, or who had close foreign connections was being seized "for examination", and that many Japanese technicians in the employ of the Government were being taken.

On March 9, the Committee began to publish retractions, modifications and denials of acts and proposals made during the preceding ten days. Only the Government's paper, the *Hsin Sheng Pao*, appeared March 9. On that date the Taiwan Garrison Headquarters issued the ambiguous statement that "all illegal organizations must be abolished before March 10 and meeting and parades are prohibited . . ." (Communiqué no. 131, March 9, 1947).

On March 10, General Chen issued the following statement:

"On the afternoon of March 2, I broadcast that members of the national, provincial and municipal P.P.C.s, Taiwan representatives to the National Assembly and representatives from the people may jointly form a committee to receive the people's opinion concerning relief work for the February 28 incident.

"Unexpectedly, since its formation, the committee has given no thought to relief work such as medical care for the wounded and compensation to the killed and so forth. On the contrary, it acted beyond its province and on March 7 went so far as to announce a settlement outline containing rebellious elements. Therefore, this committee (including hsien and municipal branch

committees) should be abolished. Hereafter, opinions on political reforms concerning the province may be brought up by the Provincial P.P.C., and those concerning the *hsien* and municipalities by their respective *hsien* or municipal P.P.C.s. People who have opinions may bring them up to the P.P.C. or to the Government-General direct by writing." (*Hsin Sheng Pao*, March 11, 1947)

On March 13, it was announced that all but three government-sponsored papers were banned or suspended for having published accounts of the uprising and activities of the Committee. The *Min Pao* press was destroyed effectively on March 10.

By March 17, the Government forces were pushing down the main railway lines toward the center of the island. Martial law was rigorously enforced from 8 o'clock p. m. until 6:30 o'clock a. m.

THE DRAFT REFORM PROGRAM

Hereafter, events in Formosa and the development of Chinese administration there may be better understood in the light of the draft reform program—the so-called 32 Demands—which are here set forth. Though the rioting after February 27 was spontaneous and the creation of the Settlement Committee an unplanned event, these requests for specific reforms in local government are rooted in fundamental economic and administrative problems which must some day be solved.

It must be pointed out that the Settlement Committee, aware of its responsible official character, was greatly hampered and embarrassed by many impossible demands made on it by individuals and groups who were not authorized to develop a reform program for the Governor's consideration. For example, there were published demands that only Formosans be allowed to hold arms on Taiwan and that all Central Government troops be withdrawn. Some extreme threats to individuals in the Government appeared in handbill and poster form.

Here the Committee's proposals are regrouped as they appear designed to achieve (1) equality in government; (2) security of person and (3) security of means of livelihood. Certain of the measures were clearly open to compromise and negotiation.

Reforms to ensure equality for Formosans in local government

1. A provincial autonomy law shall be enacted and shall become the supreme norm for political affairs in this province so that the ideal of National Reconstruction of Dr. Sun Yat-sen may be here materialized.

2. The appointment of commissioners shall have the approval of the People's Political Council (after new elections have been held.) The People's Political Council shall be newly elected before June 1947. In the meantime such appointments shall be submitted by the Governor General to the Committee for Settling the February Incident for discussion and approval or rejection.

3. More than two-thirds of the Commissioners shall be appointed from those who have lived in this Province for more than ten years. (It is most desirable that such persons only shall be appointed to the Secretariat and to be Commissioners of the Department of Civil Affairs, Finance, Industry and Mining, Agriculture and Forestry, Education, and Police.)

4. Unarmed gatherings and organizations shall enjoy absolute freedom.

5. Complete freedom of speech, of the press and of the right to strike shall be realized. The system requiring registration of newspapers to be published shall be abolished.

6. The Regulations in force covering the formation of popular organizations shall be abolished.

7. The Regulations governing the scrutiny of the capacity of candidates for membership in representative organs of public opinion shall be abolished.

8. Regulations governing the election of members of various grades in representative organs of public opinion shall be revised.

9. A Political Affairs Bureau of the Settlement Committee must be established by March 15. Measures for its organization will be that a candidate be elected by representatives of each village, town and district, and then newly elected by the prefectural or city People's Political Council. The numbers of candidates to be elected in each city or prefecture are as follows:

[Total 30—figures and allocations here omitted]

10. The Office of the Governor General shall be converted into a Provincial Government. Before this reform is approved by the Central Government, the Office of the Governor General shall be reorganized by the Settlement Committee through popular elections so that righteous and able officers can be appointed.

(Note: It has been indicated by a Formosan lawyer that the thought behind this was to provide for the interim period leading to the peace treaties and the legal return of sovereignty to China, until which time, it is widely held, a legal Provincial Government cannot be established.)

Reforms to ensure security of person and property

1. Popular election of prefectural magistrates and city mayors shall be held before June of this year and at the same time there shall be new elections of members to all prefectural and municipal political councils.

(Note: The reason given for this is the establishment of control over the police systems and to ensure the supremacy of, and respect for the courts.)

2. The posts of the Commissioner of the Department of Police, and of the directors of all prefectural or municipal Police Bureaus ought to be filled by Formosans. The armed Special Police Contingents and the armed police maintained by the Railway Department and the Department of Industry and Mining shall be abolished immediately.

3. No government organs other than the civil police can arrest criminals.

4. Arrest or confinement of a political nature shall be prohibited.

5. All chiefs of local courts of justice and all chief prosecutors in all local courts of justice shall be Formosans.

6. The majority of judges, prosecutors and other court staff membership shall be Formosans.

7. More than half the Committee of Legal Affairs shall be occupied by Formosans and the Chairman of the Committee shall be mutually elected from among its members.

Measures to ensure a revision and liberalization of economic policy and a reform of economic administration

1. A unified Progressive Income Tax shall be levied. No other sundry taxes shall be levied except the Luxury Tax and the Inheritance Tax.

2. Managers in charge of all public enterprises shall be Formosans.

3. A Committee for Inspecting Public Enterprises, elected by the people, shall be established. The disposal of Japanese properties shall be entirely entrusted to the Provincial Government. A Committee for management of industries taken over from the Japanese shall be established. Formosans shall be appointed to more than half the Committee posts.

4. The Monopoly Bureau shall be abolished. A system for rationing daily necessities shall be instituted.

5. The Trading Bureau shall be abolished.

6. The Central Government must be asked to authorize the Provincial Government to dispose of Japanese properties.

Reforms affecting military administration on Formosa

1. The military police shall arrest no one other than military personnel.

2. As many Formosans as possible shall be appointed to Army, Navy and Air Force posts on Taiwan.

3. The Garrison Headquarters must be abolished to avoid the misuse of military privilege.

Reforms affecting social welfare problems

1. The political and economic rights and social position of the aborigines must be guaranteed.

2. Workmen's protection measures must be put into effect from June 1, 1947.

3. Detained war criminals and those suspected of treason must be released unconditionally.

(Note: This is stated as designed to secure the release of a number of wealthy and prominent Formosans who have been held for more than a year on general charges of "treason" and "war crimes", who are alleged to be paying continual ransom to ensure the lives of those detained and to ensure the security of their extensive holdings.)

Demands which are subordinate measures or subject to compromise

1. The abolition or unification of the Vocational Guidance Camp and other unnecessary institutions must be determined by the Political Affairs Bureau of the Settlement Committee, after discussion.

(Note: An internment camp for persons the Government decides to make into "useful citizens".)

2. The Central Government must be asked to return funds for the sugar exported to the mainland by the Central Government.

3. The Central Government must be asked to pay for 150,000 tons of food exported to the mainland, after estimating the price in accordance with the quotation at the time of export.

In preparing these proposals for reform the Settlement Committee believed that it was preparing a basis for discussion with the Governor and through him with the Central Government. For an examination of public statements by the Governor and his representatives and from the direct testimony of Committee members, it is believed that the Committee was justified in considering itself empowered officially to propose such reforms in administration. These were not put forth as minimum or unalterable demands; they were clearly understood to be intended as a means for reflecting popular opinion. March 10 was mutually agreed upon as a date for presentation in order that people throughout Taiwan could contribute their ideas to the Committee.

AFTERMATH AND SETTLEMENT

Public opinion, Nationalism and Communism

However bitter their criticism of local administrative policy before these uprisings, there can be no question that the Formosan-Chinese have felt loyalty

to the Central Government and toward the Generalissimo. Fifty years under Japanese rule had sharpened their sense of Chinese nationality and race and in doing so developed a strong sense of island-wide social unity. Formosans have been ambitious to see Taiwan become a model province of China. From February 28 until March 9, while Formosans were in effective control of the island, the leaders in the Settlement Committee, leaders of the Youth Groups and editors of newspapers which have been most critical of the local government all took great pains to emphasize their fundamental desire to become a model province in China, proud of their race and nationality and proud to be taking part in the National Reconstruction.

(For specific reference, see editorials and speeches quoted in the *Chung Wai Jih Pao*, March 6; *Min Pao*, March 6; *Hsin Sheng Pao*, March 5; and other journals of that week.)

Reference has been made earlier to the intense distrust and fear of communism which was fostered intensively by the Japanese. There are a few Formosans who have been suspected of interest in overseas communism but they have always been counted of little importance. Of direct external influence a few communist pamphlets of mainland origin were found in the autumn of 1946 but they were not especially designed for Taiwan. So long as the living standard remained at a relatively high level there was little danger of communist doctrine finding a reception on Formosa. A large number of Formosans who had been conscripted into Japanese army labor battalions were repatriated from Hainan Island in conditions of extreme poverty in 1946. They had not been treated as "liberated Chinese" but as defeated enemies after the surrender. Failure to find employment on Formosa in the months since has undoubtedly increased their discontent and made them susceptible to the arguments of any confirmed communists who may have come back with them.

It may be therefore said with a high degree of assurance that as of March 1, 1947, communism in any form was of most negligible importance on Taiwan.

However, a local form of communism is not only possible but is believed to be a highly probable development if economic organization collapses under the pressure of continued military occupation.

The military commitment and possible economic consequences

If the Central Government chooses to support a policy of suppression of all criticism of the government and to confirm the authority of present officials by establishment of military garrisons throughout the island, the cost will be very high and will not diminish. Firm control will necessitate the maintenance of troops at all large cities, at all important rail and highway junctions and in the vicinity of the power plants upon which the normal economy depends. The ports and harbors must be garrisoned. Almost 14,000 square miles will have to be policed by military force.

It is not possible before March 17 to assess the truth of some Formosan claims that large supplies of arms had been seized in the central part of the island and transported into hiding. The opportunity presented itself and was probably taken.

It is presumed that the Formosans, if oppression continues, will not attempt a resistance from fixed positions, but will continue to harry Government troops, creating a continuous drain upon men and supplies, and will use the mountainous hinterlands as cover. Perhaps no single province in China involved so little military expenditure as that needed for Formosa before March 1, 1947. It may

now well become one of the most costly, if the economic losses in production and hampered transportation are added to outright military costs.

It is significant that throughout the trouble the local government has emphasized the fact that the Army represents the Central Government most directly. Thus, when it began to be clear that the word given by the highest ranking military officers was to be broken, Formosans began to lose faith in the Central Government as well.

With industry in such a precarious condition in February 1947, it must be presumed that the dislocations attendant upon the present trouble and a military occupation will hasten the disintegration of the industrial structure of Taiwan. China loses thereby an asset of immeasurable value. This established industrial structure (including the food processing units which make agriculture so profitable) has a substructure of semi-skilled local labor. UNRRA investigations have shown that young Formosans are no longer able to go into industrial schools or apprenticeships as in the past, but enter the common labor market as they see industry after industry shrivel up as capital investments dwindle and small industries close. Unemployment will increase with acceleration of this trend.

The rice crisis in January indicated that in present circumstances Formosa may have no immediate food surpluses upon which to draw. The addition of large numbers of troops, feeding on the countryside, will further diminish available supplies. Rice and other foods will go into hiding. Sabotage and slow-down tactics may be anticipated.

The total losses of a military occupation are incalculable. Prominent Formosan-Chinese—conservative, liberal and extremists—and many young men have been killed or seized or are driven into hiding. The educational development of the island, especially in the technical schools of middle grade, will be greatly retarded at a time when China needs every trained man. Highly qualified mainland doctors and foreign medical personnel predict that the public health system may break down badly within the year, bringing on a larger scale the cholera epidemics which appeared in 1946.

A state of near anarchy is a distinct possibility for Formosa by the end of 1947 if drastic efforts to revise policy and effect governmental reforms (free of military pressure) are not undertaken speedily. Having known a relatively high standard of living under the Japanese regime, the Formosans are not going to lose what they have without a struggle directed against the forces which they hold responsible. If the Central Government meets increasing difficulties compounded of economics and military struggles of the mainland, the Formosans will be tempted to increase their resistance in proportion.

For eighteen months Formosan-Chinese blamed the provincial administration and at the same time assured themselves that if the Generalissimo were made fully aware of conditions he would reform the system in effect on Taiwan. Later it was assumed that the application of the new Constitution would bring to Taiwan the measure of self-government needed to restore the total economy to its former high level of production, to the permanent benefit of China.

There may be a sullen peace achieved by military action, but it cannot be enforced. Further uprisings of far more serious proportions than these recent spontaneous outbursts may occur at a time when the over-all peace settlement in the Far East is underway, and problems are being reviewed for inclusion or exclusion in the conference agenda. Anyone who wishes to embarrass China will find good material in a revolutionary situation on Taiwan.

Formosa should be put to work earning foreign credit for China. Its peculiar character as an industrialized and technically developed province should be sheltered from the greater economic difficulties found on the mainland. Taiwan was returned to China as an outstanding economic asset, and example of the advanced technological economy toward which all other provinces of China are striving. Two years of concentrated rehabilitation effort in Formosa hereafter will produce permanent assets of two kinds. Raw materials and products such as fertilizers, cement, foodstuffs and industrial chemicals will become permanently available to China in increasing amounts. Others such as tea, camphor, sugar, industrial salt, pineapples and light manufactures can be directed to overseas markets. A moderate share of the foreign credit so created must be returned to Formosa for rehabilitation and expansion of state-owned industries and the expansion of private enterprise. Formosan-Chinese must be admitted to greater participation in all aspects of economic administration and reasonable profit if the island is to prosper and to return to the high and constant level of production achieved in former years. Economic stability and expansion must be founded on a sound political and social administration. Now is the time to act. To encourage and ensure wholehearted effort the Formosan-Chinese must be allowed to take a larger part in government at all levels. Changes in personnel as well as in the structure of the administration must be thoroughgoing; it is felt that half-way measures and palliatives now will only postpone a larger repetition of the current protests against corruption, maladministration and autocracy in the provincial government. Formosa can be restored to its former high level of political allegiance and of economic production by prompt and fundamental reform.

The following developments have been reported as occurring during the end of March and the first part of April:

The continuing presence of fresh bodies in Keelung Harbor and other evidence indicate that the elimination of the informed opposition is continuing. The bodies of at least two men known to neutral sources as having taken no part in any activities during the recent incidents have been identified. It is reported at Taipei that although shots and screams in the night have become less frequent, they continue, and that there is no palpable difference in the tense atmosphere of the city. Mainlanders generally are reported to be apprehensive of further trouble, and many of them are said to feel that Formosan cooperation under present circumstances will be difficult for an indefinite time in the future. Of serious import is the reported continued undermining of Taiwan's advanced economic structure.

this exchange of notes whenever either of the two governments considers such action appropriate.

9. The Government of the United States of America reserves the right at any time to terminate or suspend its assistance or any part thereof provided under this exchange of notes. Assistance furnished by the Government of the United States of America under Section 607 of the Act and pursuant to this exchange of notes shall not be construed as an express or implied assumption by the Government of the United States of America of any responsibility for making any further contributions to carry out the purpose of Section 607 of the Act or of this exchange of notes.

10. This note and Your Excellency's reply accepting the above proposals on behalf of the Government of China will constitute an agreement between the two governments in the sense of Section 607 of the Act. Subject to the provisions of paragraphs 8 and 9, this exchange of notes will remain in force until June 30, 1948, or, upon the request of either government transmitted to the other government at least two months before June 30, 1948, until the date of termination of the Economic Aid Agreement between the two governments mentioned on July 8, 1948.

I avail myself [etc.]

J. LAWRENCE STUART

The Chinese Minister for Foreign Affairs (Wang) to the Ambassador in China (Stuart)

EXCELLENCY: I have the honor to acknowledge receipt of your note of today's date which reads as follows:

(Here follows text of preceding note.)

On behalf of the Government of China I have the honor to accept the proposals contained in the note quoted above.

In recognition of the importance of the program as one of the essential means of achieving the objectives in which the Governments of China and of the United States of America unite in seeking under the Economic Aid Agreement between the two governments concluded on July 8, 1948 the Government of China undertakes to afford to the exercise of the program the full weight of its support and to direct cooperating agencies of the Government of China including the local officials concerned to give such assistance and facilities as are essential to the success of their undertakings under the program.

I avail myself of this opportunity to renew to your Excellency the assurance of my highest consideration.

WANG HSIAO-CHENG

Economic Aid to China under the China Aid Act of 1948⁵

PART I—INTRODUCTION

At the time the China Aid Act was passed, China was in the grip of the longest sustained inflation in modern history. Her external resources had dwindled from approximately a billion dollars on V-J Day to less than one-quarter of that

⁵ Excerpts from document published by the Economic Cooperation Administration Washington, February 1949.

sum at the beginning of 1948. Foreign trade was at a low ebb. Continuation of deficit financing to support the civil war against the Communists kept the fires of inflation burning; the currency inflation in turn caused production and other constructive business activity to stagnate and contributed greatly to a popular loss of confidence in the National Government. While the military strength of the Communists was increasing, Nationalist strength was being sapped by military defeats, sinking morale among the troops, and a crumbling economic front in the rear of the Government's armies.

Character of the 1948 Economic Aid Program for China

The China Aid Program was not originally conceived as something that could by itself turn back or even arrest these trends. It was described as an effort to "assist in retarding the current economic deterioration and thus give the Chinese Government further opportunity to initiate the measures necessary to the establishment of more stable economic conditions."

The program of economic aid was organized and carried on against a background of continuing civil war and progressive contraction of the area and resources under the control of the National Government. It has been directed toward bringing economic assistance as directly as possible to areas and people who have needed the type of assistance which could be supplied by the use of U.S. dollars.

Food has been provided through a controlled ration system to nearly 13,000,000 inhabitants of seven major Chinese cities. Cotton financed under the program has kept the mills operating in China's largest industry, providing cloth for direct consumption, for barter to encourage the bringing of indigenous food into the cities, and for export to earn foreign exchange that can be used to pay for more imports. Petroleum has kept in operation basic utilities, transport facilities and industries, and also provided goods for which the farmers in the countryside are prepared to exchange their produce. Fertilizer imports have been planned for use in the production of spring crops in 1949. A Joint Commission on Rural Reconstruction has been established, and has formulated principles and a program for attacking some of the root causes of poverty and unrest among China's vast rural population. An industrial program of replacement machinery and reconstruction projects has been initiated with the participation of private American engineering firms; although actual procurement and construction had to be suspended for the most part due to uncertainties connected with the civil war, much useful engineering survey work has been done. A "counterpart" fund in local currency, established by agreement with the Chinese Government and managed jointly by Chinese and Americans, has been used to maintain many hospitals, welfare programs, and dike-building projects.

In spite of the growing chaos around them, these activities, by and large, have been managed with care and have been carried out successfully within their own limited terms of reference. In the case of the commodity program particularly, the supplies provided have been an important and at times crucial factor in keeping unrest to a minimum in the main cities of the coastal areas controlled by the Nationalist Government. In this narrow but significant sense, therefore, the efforts of ECA in China have been constructive and useful. Supplies financed by the U.S. have been and are being effectively distributed to the people intended to receive them.

Economic Aid in a Setting of General Deterioration

But the atmosphere surrounding these efforts has been one of continuing discouragement and defeat for those who had hoped the Chinese National Govern-

ment, after a decade of upheaval and in face of all difficulties, could and would do the things that needed to be done if it were to provide an adequate counter-force to the Communists in China. The incapacity of the Government to put into effect the reforms which it had in January announced its intention of initiating; the inability of the Nationalist commanders to lead and inspire an effective military effort against the growing Communist threat; a series of ill-conceived economic and financial measures which made the situation behind the lines even worse than it needed to be; the widening breach between the people and their Government—all these were factors so demoralizing in their effect that it became only a matter of time until the Government would reach the brink of disaster.

Chinese economic problems cannot be separated from problems which are ordinarily termed political and military. The inflation itself, dramatic as it has been, is only a symptom of broader and deeper problems. The prodigious increase in the issue of currency has been a devastating economic fact, but the reason for it is to be sought in the military fact that more than two-thirds of all currency issued has been used directly to support the Government's military efforts. Sudden increases in the velocity of circulation can be related directly to sudden drops in public confidence due to military defeats.

On August 19, 1948, the Chinese Government published a series of apparently sweeping financial reforms, in an attempt to arrest the runaway inflation of the Chinese National Currency (CN), and draw in for public use the large private holdings of foreign exchange. The drastic and dramatic reforms, including the introduction of a new Gold Yuan (GY) currency, seemed to hold the inflation in suspense for more than a month. But they did nothing to increase revenues or to reduce expenditures; thus they failed to attack the basic cause of the inflation, which is the gross imbalance of the Government's budget. Internal contradictions in the new regulations soon appeared. A new commodity tax was not put into effect because it would have meant breaking the price ceilings set forth in the same regulations. Although the Government reported collection of more than US\$150 million worth of foreign exchange, it had to pay out in return so large an amount of the new Gold Yuan currency, without any compensating increase in supplies or production, that the new currency rapidly depreciated further both in real value and in the esteem of the Chinese people.

With these economic influences at work, the resumption of the inflationary spiral and a breakdown of the attempt to maintain August 19 ceiling prices was inevitable. Attempts to enforce arbitrary price ceilings in Shanghai, and to a less extent in other cities, brought about an almost complete stagnation of economic activity. The more strictly the regulations were enforced, the less food came into the cities, and the worse the situation became. Finally, in November, the regulations became so ineffective and disruptive of economic activity that they were officially revoked in the face of a downward slide of the Gold Yuan which has continued thereafter.

Internal financial deterioration and the maintenance of artificial exchange rates have held down official receipts by the Chinese Government from exports and inward remittances. Although China has had to draw down also some \$100 million from her contracted dollar assets, official holdings of foreign exchange may have exceeded slightly, at the end of 1948, the balance existing when the China Aid Act was passed. This has been due in part to the existence of the China Aid Program itself, which has paid for most of China's basic commodity imports since June 1948. But it has been due also to two factors unfavorable to China: first, the fact that imports outside the ECA program were held to a level so low as to impair seriously production and trade; and second, the

fact that private exchange holdings were called in under the August 19 regulations in such a way as to heighten the inflation and at the same time to wipe out extensively, middle class savings. Thus the balancing for a time of China's official international payments accounts was achieved at a prohibitive internal cost.

China's drawings upon restricted foreign exchange resources were largely for current requirements, not for importations of capital equipment. The Government even sold valuable productive properties in order to meet current outlays.

A further debilitating effect of the civil war was to be found in the phenomenon of "disinvestment" within China, which contrasted with the process of expanding investment in the ECA-aided countries of Europe. In a setting of spiralling inflation and universal uncertainty as to the future, private capital was almost wholly directed into non-productive channels of financial speculation and hoarding of goods for sale at higher prices; banks demonstrated an increasing reluctance to extend long-term credit for industrial investment. As a result, not only did China's productive plant fail to expand, but existing productive facilities deteriorated. The lack of repairs and rehabilitation of productive capacity has lowered output.

These facts, taken together, point to a steady decline in the overall productive capacity of the Chinese economy during 1948.

The relationship between military defeat and economic deterioration has been further demonstrated in the case of coal and food supplies.

Coal production in China during 1948 was at about the same level as 1947. Supplies reaching consuming areas, however, were sharply reduced, particularly during the latter half of the year, as mining centers were cut off or fell into Communist hands. An especially serious loss, toward the end of the year was that of the output from the Kailan Mines north of Tientsin, which were supplying more than half of the coal produced in the whole of Nationalist China.

The output of foodstuffs in 1948 reached a postwar peak at a level roughly equal to that of prewar years. In spite of this recovery in the agricultural regions, China's urban centers were able to meet their food requirements only with the continuing assistance afforded by substantial shipments from abroad. Factors contributing to this situation were Communist occupations of producing areas in Manchuria and much of north China and the consequent disruption of distribution patterns; and, in accessible areas—particularly, during the autumn months—an increasing unwillingness on the part of farmers to market their crops in view of rigid price controls and continuing currency depreciation.

Similar trends could be noted in every other sector of the economy. Mill output of cotton textiles held up during the first half of the year at 1947 levels and then began to drop sharply. Operable rail mileage in Nationalist hands was reduced by 2,500 kilometers despite the rehabilitation of lines in the south. Shipping capacity was maintained but the pressure of military needs reduced the amount available for commercial requirements. Costly air traffic increased under the necessity of supplying cities besieged by Communist armies. During the last few months of the year, important cities in north and central China were virtually cut off from major supply sources and economic activity became thoroughly demoralized. ECA imports, in the latter part of the year, played an increasingly large role in supplying urban areas with essential food and raw materials.

Preliminary Review of the ECA China Aid Program

Within a few weeks after the Economic Cooperation Administration came into being, economic aid to China was an operating reality. Initial funds from the

Reconstruction Finance Corporation were advanced to ECA, a "Program No. 1" for using these funds was approved by the Administrator, and the first procurement authorization was issued. An exchange of notes between the Secretary of State and the Chinese Ambassador in Washington set up interim arrangements for providing assistance pending conclusion of a formal bilateral agreement. Mr. Roger D. Lapham was appointed Chief of the ECA Mission to China, arriving at his post in Shanghai the first week of June. The Chinese Government created a Council for U.S. Aid, a cabinet level committee to deal with the ECA Program. To "backstop" the Mission, a China Program Division was created in the ECA Headquarters office. And on July 3, three months after the Foreign Assistance Act was approved, the formal Economic Aid Agreement between China and the United States was signed by the Chinese Foreign Minister and the U.S. Ambassador to China.

The ECA Mission to China was faced with the problem of getting itself organized quickly for the job ahead. To speed up the process, it took over and adapted to the new purpose the China Relief Mission which had been responsible in China for the U.S. Foreign Relief Program under Public Law 84 (Eightieth Congress). ECA also inherited some continuing functions of a relief character, including the distribution of P. L. 84 supplies which had not reached end-users by the time that law expired, on June 30, 1948. ECA likewise continued support to a number of special projects started by the China Relief Mission and financed from a local currency "Special Account."

Operating under a strict limitation on dollar administrative expenses, the Mission has made a maximum use of alien staff, paid in local currency. ECA has arranged for a part of the work of supervising and controlling portions of the program to be done by private firms and voluntary relief agencies.

The program itself has consisted of three parts: the provision of a limited number of basic commodities (food, fuel, cotton, fertilizer and coal); the initiation of an industrial replacement and reconstruction program; the formation and support of a Joint Commission on Rural Reconstruction in China. In addition, ECA has participated in the management and use of a Special Account, or "counterpart" fund, in Chinese currency provided by the Chinese Government. Of the total \$275 million appropriation for the ECA China Program, \$203.8 million was earmarked for commodities, \$67.5 million for the industrial program, \$2.5 million for dollar expenditures on the rural reconstruction program, and \$1.2 million for administration.

The commodity program called for average ECA imports into China of supplies costing roughly \$20 million a month. As of December 31, \$194 million of the commodity funds had been authorized for procurement, and about \$112 million worth of these supplies had arrived in China. The commodity program was, therefore, well up to schedule. But obligations against the industrial program had been limited to allotments of money for "preproject" engineering survey work. Toward the end of the year, some of the projects were about ready to start actual procurement and construction work; but in December, it was necessary to suspend allocations for such work pending clarification of the political and military situation in China. Similarly, the Rural Reconstruction Commission was only emerging from the planning stage at the end of 1948, and had tapped only a small part of the \$2.5 million set aside for its U.S. dollar expenses.

In all phases of the program, as much emphasis as practicable has been placed on the use of commercial channels of supply and distribution. The food program is the sole exception as regards supply; rice from southeast Asia and wheat and flour from the U.S. have been bought and shipped by the Commodity Credit Cor-

poration, an agency of the U.S. Department of Agriculture. The major portion of the petroleum products, most of which originate in the Persian Gulf, have been procured and shipped by private oil companies. American cotton has been shipped by American firms and received in China by American cotton importers. Fertilizer, coming from a variety of sources under allocations by the International Emergency Food Committee, has likewise been supplied through private commercial channels.

After each commodity shipment arrives in China, the ECA Mission keeps track of its receipt, processing, distribution, and end use. Food is distributed through the first general civilian rationing system ever developed in China's urban areas, with the Chinese Government and ECA each providing a part of the total ration requirements. Cotton becomes yarn, yarn becomes cloth, and the end-products are used for export, for barter and for domestic sale—all under the watchful observation of a Joint Management Board in which ECA participates. Petroleum products are distributed by the importing companies, who themselves assist in end-use control and reporting, and provide detailed sales records for each product to the ECA Mission. As of December 31, 1948, fertilizer had not been distributed since it was for use in 1949 spring production; a part, it was planned, would be handled in direct exchange with farmers for rice, a part sold through commercial channels and a part used by the Rural Reconstruction Commission. The small amount of coal imported before the end of the year went directly to utilities and other users under the supervision of the ECA China Mission. Medical supplies imported by ECA's predecessor in China, the U.S. China Relief Mission, are distributed by a special group set up by agreement between the Ministry of Health and voluntary agencies. Pesticides, also inherited from the China Relief Mission, have been distributed largely through commercial channels, the remainder being earmarked for agricultural demonstration purposes.

The industrial program started with an intensive investigation of proposed replacement and reconstruction projects conducted by a special Reconstruction Survey Group. This group faced a double problem—an extensive need for replacement and reconstruction equipment, and a serious lack of the engineering and management skills needed in China to make certain that such equipment would be effectively absorbed into the economy. The group prepared tentative recommendations for allocation among approved projects from the \$67.5 million set aside for this purpose. The projects thus recommended were largely limited to the field of basic industry and transportation—the largest provisional allotments proposed being for power plants, coal mines, the rehabilitation of railroads, and the manufacture of fertilizer. The Survey Group also developed procedures for making maximum use of private American engineering firms as "project engineers" to help individual projects in drawing up plans, procuring the right equipment, and making sure that equipment is correctly installed and effectively operated. To manage the whole scheme, ECA and the Chinese Government agreed to retain a high-grade American firm of management engineers.

The uncertainties in the China situation had in December caused the suspension of all but survey work under this program, leaving open the possibility of selected projects being carried forward as circumstances permit. The technique adopted for administering this program may prove to be of significance in relation to future programs involving industrial projects in underdeveloped countries.

The Joint Commission on Rural Reconstruction in China was established in accordance with Section 407 of the China Aid Act to "formulate and carry out a program for reconstruction in rural areas of China." Initiated on August 5 by an exchange of notes between the Chinese and U.S. Governments, the Joint

Commission consisted of three Chinese and two American members, appointed in September by the Presidents of China and of the United States.

Intensive planning and survey work were undertaken by the Commission after the members had agreed on the general statement of objectives and principles. In general, the Commission has been moving in the direction of assisting people in rural areas to improve their living conditions, increase food production, and develop local self-government; strengthening and improving the operations of government agencies concerned with rural problems; stimulating local movements and private agencies in efforts on behalf of the rural people; and affording to progressive elements in the population real opportunities to participate in the program. The Joint Commission operates under the supervision of the Administrator, who has delegated his authority in this field to the Chief of the ECA Mission to China. The American members and staff of the Commission are ECA staff members engaged in full-time work with the Commission.

A special concern of the ECA in connection with the China Program has been the development of sources of strategic materials required by the U.S. Although China is a major producer of three such materials—tin, tungsten, and antimony—the limitations upon funds for stockpiling purposes have made it impracticable to pick up antimony and tungsten which are available for purchase in China. Extensive investigations on the development and supply of tin concentrates and tin metal, however, had resulted before the end of December 1948, in a tentative arrangement for tin purchasing as part of a general scheme for rationalizing the supply of metal and the development of processing facilities in Yunnan Province.

The special local currency account, or counterpart fund, provided for in the Economic Aid Agreement with China, differed from corresponding accounts in Europe, two of its features being unique. The first is an arrangement for deposits of local currency, which leaves the timing of deposits in the discretion of the U.S. Government; this discretion is used to relate deposits to actual needs for the local currency, without large surpluses which would rapidly shrink in value. The second unique feature is a "maintenance of value" clause which provides that for certain important uses the Chinese Government would protect appropriations made from the special account against currency depreciation, by expressing the appropriation in terms of some more stable unit, such as U.S. dollars or a basic commodity like rice or cotton yarn.

Since it was clear from the outset that the sterilization of the entire special account would not by itself be an important influence toward control of the inflation, the Chinese Government and the ECA, after consultation with the National Advisory Council in Washington, followed a policy of making expenditures from the account for important public purposes which might not otherwise be provided for, if such expenditures were of demonstrated urgency. The main categories of expenditures have been for administrative costs, the expenses of delivering relief packages and supplies in China, local currency costs of projects sponsored by the Joint Commission on Rural Reconstruction, expenditures on special projects in the field of water conservancy, health and welfare, and the internal costs to date of the replacement and reconstruction program, in cases where money could not be raised from other sources. It was estimated, according to the plans envisaged during 1948, that the total of these expenditures would amount to less than half of the total potential account.

By the end of December 1948, notifications of U.S. grant aid had been given to the Chinese Government to the amount of \$94,470,926. According to preliminary

and tentative estimates, pending final determination upon a formula for computing exchange rates, Gold Yuan equivalent to approximately \$9,543,000 had been requested for deposits, and the equivalent of approximately \$5,839,000 had been spent.

PART II—ECONOMIC AID PROGRAM FOR CHINA TO DECEMBER 31, 1948

Scope and Rationale

The President, in his message of February 18, 1948, to Congress on aid to China recommended authorization of an economic aid program in the amount of \$570 million, to provide assistance over a fifteen-month period extending to June 30, 1949. Of this amount, \$510 million was estimated as required for financing essential commodity imports into China, "which would permit the Chinese Government to devote its limited dollar resources to the most urgent of its other needs," and \$60 million was recommended for "a few selected reconstruction projects to be initiated prior to June 30, 1949." "Essential imports" cited included cereals, cotton, petroleum, fertilizer, tobacco, pharmaceuticals, coal and repair parts for existing capital equipment. Reduced to a twelve-month basis, the program of economic assistance proposed by the President would have called for approximately \$403 million for commodity shipments to China and an additional \$60 million for aid to selected reconstruction projects.

The China Aid Act of 1948 authorized for expenditure during the ensuing twelve-month period (April 3, 1948, to April 2, 1949) \$338 million for economic assistance to China, of which \$275 million has been appropriated, and an additional \$125 million for aid to China through grants "on such terms as the President may determine and without regard to the provisions of the Economic Cooperation Act of 1948."

The program of economic aid to China administered by the ECA during 1948 has been limited to expenditures within the \$275 million appropriated by the Congress.

In Section 407 of the China Aid Act of 1948 (Public Law 472, Title IV), the Congress authorized for "a program for reconstruction in rural areas in China," an amount "equal to not more than 10 per centum" of the funds made available for economic assistance under the Act, which amount could be "in United States dollars, proceeds in Chinese currency from the sale of commodities made available . . . or both." Thus a third category of assistance was specified. The China Aid Act did not further stipulate the relative magnitude of expenditures to be incurred in behalf of the three general types of limited assistance contemplated, namely: a commodities program, an industrial reconstruction program, and a rural reconstruction program.

Related to these three types of aid within China and available for helping to carry them out was a special local currency or "counterpart" fund, established by the Chinese Government pursuant to the terms of an "Economic Cooperation Agreement between the United States of America and the Republic of China." (The text of this bilateral Agreement is quoted below, under the heading, "Documents.")

In administering economic aid to China, as approved by Congress, the ECA has faced the obligation to ensure as efficient use as possible, under prevailing conditions, of the \$275 million appropriation provided by Congress, recognizing that the assistance thus furnished would, to be fully effective, have to be supplementary to, and not a substitute for, vigorous efforts on the part of the Chinese Government and people.

With limited resources and under prevailing conditions in China, it has not been possible for the ECA to undertake a comprehensive approach to China's broad problems of budgetary and financial stabilization and economic recovery. It has been necessary, instead, to concentrate upon a few restricted activities designed to furnish some assistance at critical points in the Chinese economy; to maximize in the aid program, where possible, the use of private trade channels as one means of sustaining a degree of normal economic activity; and to devise effective end-use controls designed to ensure efficient utilization of all the economic aid provided.

Initiation of the Program

On April 30, 1948, notes were exchanged between the Secretary of State and the Chinese Ambassador in Washington, setting up interim arrangements for the initiation of the China Aid Program, pending the negotiation of a bilateral economic aid agreement. These notes (a) confirmed the Chinese Government's adherence to the purposes and policies set forth in Section 2 of the China Aid Act of 1948; (b) specified that prior to the conclusion of an agreement under Section 405 of the China Aid Act and until July 3, 1948, the extension of aid to China as authorized by Section 404 (a) of the Act, would be provisionally governed, subject to agreed modifications, by the Agreement negotiated in connection with the United States Foreign Relief Program, dated October 27, 1947; and (c) recorded an understanding relating to the establishment of special mission for economic cooperation to China, together with an assurance that the Chinese Government would extend the fullest cooperation to representatives of the United States Government concerned with operations in implementation of the China Aid Act.

Bilateral Agreement

Section 405 of the China Aid Act provided that an agreement should be "entered into between China and the United States containing these undertakings by China which the Secretary of State, after consultation with the Administrator for Economic Cooperation, may deem necessary to carry out the purposes of this title and to improve commercial relations with China." Consequently, negotiations were begun in early June between the United States Embassy in Nanking and the Chinese Ministry of Foreign Affairs regarding the terms of a bilateral economic cooperation agreement between the two countries. These negotiations were concluded satisfactorily and the Agreement was signed on July 3, 1948 by Ambassador J. Leighton Stuart and the Chinese Minister of Foreign Affairs, Wang Shih-chieh. (The full text of the Agreement is quoted below in the section entitled "Documents.")*

In general, the Agreement with China followed the pattern of the bilateral agreements being negotiated simultaneously between the United States and those European countries which participated in the Organization for European Economic Cooperation. The language of certain articles was made almost identical for those undertakings specified by Title I of the Foreign Assistance Act which applied in principle to the Chinese as well as to the European situation. Because of certain basically different aspects of the Chinese situation, however, some standard articles were modified considerably in the China Agreement, or unique provisions were added. In view of conditions prevailing in China, the scope of joint control, particularly with respect to prices and allocations, was broader under the terms of the China Agreement than under the European bilateral agree-

* See annex 181.

ments. One unique article in the China Agreement, that calling for improvement of commercial relations, was required specifically by Section 405 of the China Aid Act.

The Agreement with China set forth a number of undertakings by the Chinese and/or the U. S. Government relating to the following:

provision of aid to the Chinese Government in accordance with the terms of the China Aid Act of 1948 (other than Section 404 (b) thereof); measures for improvement of general economic conditions including effective use of aid goods, appropriate use of private Chinese assets in the U. S., development of industrial and agricultural production, creation of more stable currency conditions, cooperation with other countries to increase international trade, and prevention of commercial arrangements which interfere with the purposes of the Agreement;

improvement of commercial relations with other countries, with particular reference to the conditions affecting foreign trade by private enterprises in China; fair and equitable distribution of aid goods, and of similar goods produced locally or imported with other funds, and the method of determining terms, conditions and prices for distribution of aid goods;

deposits of Chinese currency in value commensurate with the value of U. S. aid provided on a grant basis, and the principles governing disposal of such deposits;

facilitating the acquisition by the U. S. from China of materials in short supply in the U. S.;

negotiation of duty-free treatment for imports into China of relief goods by private agencies or individuals;

joint consultation, and provision of information by the Chinese Government, regarding matters relevant to the Agreement;

publicity within China regarding provision of aid under the Agreement;

establishment in China of, and treatment to be accorded to, a U. S. Special Mission for Economic Cooperation;

settlement, by reference to an agreed upon international tribunal, of claims espoused by either government on behalf of its nationals against the other government for compensation for damage arising as a consequence of governmental measures taken after April 3, 1948;

entry into force, amendment and duration of the Agreement.

Advisory Bodies

Two advisory bodies have on request furnished helpful counsel and guidance on broad questions relating to the planning and conduct of the ECA China Aid Program: The National Advisory Council on International Monetary and Financial Problems, established by Congress, and the Public Advisory Committee for the China Program, appointed by the Administrator under authority granted in Public Law 472, Section 107 (b).

Members of the National Advisory Committee for the China Program have been: Isaiah Bowman, president-emeritus of Johns Hopkins University and a member since 1940 of the Permanent International Commission for China and the United States; Arthur B. Foye, senior partner of the international public accountant firm of Haskins and Sells and, since 1945, president of the Far East-America Council of Commerce and Industry; Paul V. McNutt, former ambassador and United States high commissioner to the Philippines, and president and

chairman of the Board of United Service to China; Elizabeth Luce Moore, former chairman of the USO Council, one of the founders in 1940 of United China Relief, and a trustee of Wellesley College, of the China Institute in America, and of the United Board for Christian Colleges in China; and Walter S. Robertson, former minister-counselor for economic affairs at the United States Embassy in Chungking, and a principal assistant to General George C. Marshall during his special mission to China in 1945-1946.

ECA Mission to China

Authority for the establishment of a special ECA Mission to China is contained in Public Law 472, Sections 109 and 403.

The organization of the China Mission began with the appointment of Roger D. Lapham, former mayor of San Francisco, as Chief of the Mission. The appointment was made on May 5, 1948, and Mr. Lapham arrived in China on June 7, accompanied by initial members of a Reconstruction Survey Group. Staffing of the Mission has been kept at a minimum consistent with the efficient performance of ECA economic aid functions in China. As of December 31, 1948, 89 Americans and 355 non-Americans were on duty with the Mission.

Clearances between ECA Headquarters and the China Mission are conducted through a China Program Division in Washington. This is a staff office of 20 persons which facilitates the integration, without needless duplication, of China operations within the general framework of ECA financing and supply operations.

RELATIONS WITH THE CHINESE GOVERNMENT

To provide for an orderly conduct of relations between the Chinese Government and the ECA China Mission, the Government appointed a Council for United States Aid (CUSA), with the Prime Minister as Chairman, which includes in its membership the Ministers of Foreign Affairs, Finance, and Communications, the Governor of the Central Bank, the Chairman of the National Resources Commission, the Mayor of Shanghai and the Chairman of the Chinese Technical Mission to the United States.

The Economic Cooperation Agreement between the United States and the Chinese Governments, signed at Nanking on July 3, 1948, by the United States Ambassador and the Chinese Minister for Foreign Affairs, provided the framework of understanding and agreements on the basis of which ECA operations in China have been conducted. The text of the Agreement appears in the final section of this paper.

TAKEOVER FROM U. S. CHINA RELIEF MISSION

The first organizational problem faced by the Chief of the ECA Mission to China was the need to make provision for the orderly transition from the work of the U. S. China Relief Mission, which had been responsible for the \$45,000,000 Interim relief program in China, previously provided under Public Law 84, to the new program under ECA direction. Arrangements were made for the temporary transfer of considerable numbers of the personnel in the China Relief Mission, in order to ensure the orderly liquidation of that Mission's responsibilities under the supervision of ECA, and at the same time to utilize, for the benefit of the ECA program, the experience of personnel already available in China, who had been working with a program similar in certain respects to the China Aid Program.

Takeover responsibilities included principally the receipt and distribution of residual China Relief Mission supplies, responsibility for residual proceeds from the sale of such supplies, and the carrying on or liquidation of various local currency projects agreed to by the China Relief Mission.

Approximately 25,000 tons of CRM rice and flour valued at about \$3.8 million were on hand on June 30, 1948, which were taken over and distributed under the supervision of the ECA Mission through the rationing system. Approximately \$5.2 million worth of medical supplies and \$670,000 worth of pesticides were on order in the United States, to be delivered during the early months of the ECA program. The general policy governing distribution of medical supplies has been to distribute them for the greater part free of charge and in large part in outlying areas where it has not been feasible to ship ECA bulk supplies. About a third of the pesticides has been reserved for the use of the Rural Reconstruction Commission, the remainder being sold through normal commercial channels or distributed free by the Ministry of Agriculture through agricultural demonstration centers.

There was virtually no cash balance in the CRM local currency account at the time of the ECA takeover. However, commitments had been entered into for over 260 projects predicated on anticipated proceeds from the sale of undistributed rice and flour. The ECA, accordingly, assumed responsibility for the orderly completion or liquidation of these projects. In July and August, the equivalent of US \$197,600 was disbursed from the local currency Special Account for these purposes, about 55 percent for public works, 43 percent for medical purposes, and 2 percent for miscellaneous projects. After August, considerable weeding out was done in order to reduce the number of projects to a number which would permit adequate supervision and these have been included in the overall ECA-CUSA program for the Special Account.

ORGANIZATION

Headquarters of the ECA Mission to China were established in Shanghai, and regional offices in Nanking, Peiping, Tientsin, Tsingtao, Canton and Taipeh (on Taiwan or Formosa).

The approved pattern of the Mission as of December 31, 1948, is reflected in the accompanying organizational chart. The principal functions of each organizational unit within the Mission are set forth in the Appendix.

Assistance has been given to the Mission by ECA Headquarters in the recruitment of American personnel and the coordination of personnel procedures, fiscal activities, and administrative management in accordance with Headquarters procedures and in compliance with foreign service requirements of the State Department.

ADMINISTRATIVE EXPENSES

The ECA China Program has operated under a limitation, for administrative expenses incurred in U. S. dollars, of \$1.2 million—less than one-half of one percent of the amount appropriated for the current China program. This necessitated rigid economies in the planning of staff requirements, and a maximum use of other agencies and means in order to develop an effective field organization. The \$1.2 million ceiling did not apply to administrative costs provided from counterpart local currency funds in China, from which source approximately three-fifths of the administrative costs of the Mission are being met.

Administrative expenses, with the benefit of special arrangements referred to below, were held, up to the end of December 1948, within an amount provisionally

estimated at approximately \$560,000. However, a large percentage of these expenses were incurred during the last quarter of the calendar year 1948. This was attributable chiefly to two factors: (a) the fact that the ECA China Mission was not fully staffed, and operations in China were not in full swing, until the October-December quarter; and (b) the necessity of incurring increased expenses (notably for extensive transfers of supplies and personnel, including the removal of some dependents) as a result of unsettled and uncertain conditions in north and central China. A third factor contributing to higher costs was beginning to appear at the end of the year, namely, the necessity, with the excessive rate of depreciation of Chinese currency, of meeting certain administrative expenses out of U.S. dollars instead of local currency.

Payment for expenses incurred on behalf of American members of the Mission, including travel for members and dependents, is governed by U. S. Foreign Service regulations which are mandatory with respect to ECA employees.

Military developments in China have made necessary budgetary provisions for the voluntary removal of certain dependents and household effects from threatened areas. As of December 31, 1948, some dependents and women employees with children were being evacuated, and some members of the Mission had been reassigned in accordance with changing program plans.

The use of consulting engineers or engineering firms on a contract basis, in connection with the development of surveys and plans for reconstruction projects in the industrial field, has made it possible to have competent engineering surveys and to prepare for supervising this part of the program without incurring direct administrative expenditures in excess of the ceiling on administrative costs.

A similar saving has been effected in the case of the rural reconstruction program. As indicated above, the Congressional appropriation for this program, to be supervised by a Joint Commission on Rural Reconstruction, was "an amount equal to not more than 10 per centum" of the appropriation for economic aid to China, which amount could be in U.S. dollars, proceeds in Chinese currency from the sale of commodities made available to China, or both. From the ceiling of \$27.5 million thus established for the rural reconstruction program, \$2.5 million was tentatively earmarked for availability in U.S. dollars, to be used principally for salaries, dollar administrative requirements and essential procurement of agricultural supplies and educational media. The Joint Commission's allotments for both program and administration represent a program cost and are thus not chargeable to the limitation on administrative funds for the China Mission.

To avoid needless administrative duplication and expense, administrative arrangements were entered into between the State Department and the China Program of ECA, in which the State Department agreed to provide communication facilities and to assume disbursing functions with respect to U.S. dollars and to perform such minor services, in return for which ECA would reimburse the State Department, either through direct payment or through the provision of agreed services as needed by American or alien personnel.

Economies in time and space facilities were effected by the takeover of office and warehouse space and equipment previously utilized by the China Relief Mission operating under P.L. 84. Effective coordination with the Chinese Government Council for U.S. Aid (CUSA) was facilitated by a provision for CUSA offices in the same location as those of the ECA China Mission.

The civil war, with its attendant disruption of rail services, has made necessary an almost exclusive use of air travel on the part of the members of the

Mission in China, including chartered flights when necessary. Telegraph work-loads in excess of available capacities through diplomatic or military channels have necessitated a considerable use of commercial telegraph facilities for unclassified operational messages.

Through the economies and special arrangements outlined above, direct administrative expenses charged against the ECA program in China were, as of December 31, 1948, within an administrative budget based upon the \$1.2 million limitation for the one-year period of the authorizing legislation. And it was expected that administrative expenses incurred in the course of operations through April 2, 1949, would, despite the rising costs referred to above, be kept within this limitation.

COMMODITIES PROGRAM

The commodities program has had as its aim the provision of a continued flow to China of certain key commodities essential to the maintenance of minimum economic activity and subsistence in the urban centers of China. As indicated above, resources available for ECA commodity imports into China were not of a sufficient order of magnitude to reduce substantially the great imbalance in the Chinese national budget or to solve the nation's balance of payments problem by providing all essential imports which could not be financed by the Chinese themselves. It was essential, therefore, to concentrate upon the commodities which were of most strategic importance in helping to bolster China's internal economy. Commodities procured under the ECA program have included food, cotton, petroleum, fertilizer, and coal. In addition, as mentioned above, some residual medical supplies and pesticides were taken over by the ECA, from the earlier U.S. Foreign Relief Program, for distribution. The scope and character of each of these commodity programs are discussed below.

Procurement and Shipment

Following consultation with the National Advisory Council, ECA decided to finance commodities for China entirely on a basis of grants, not loans. The reason for this action lay in the state of the Chinese Government's external finances, as described in an earlier section of this paper.

Commodity procurement has been conducted by two methods—through private trade channels for cotton, fertilizer, petroleum and coal, and through the U.S. Department of Agriculture for rice, wheat and flour.

Cotton has been purchased through ECA financing by the Chinese Textile Industries, Inc., a quasi-government corporation, from U.S. cotton brokers submitting bids through agents in Shanghai. Fertilizer has been purchased by the Central Trust of China from suppliers presenting bids, over-all quantities purchased being governed by the size of International Emergency Food Committee allocations to China. Petroleum products have been purchased from suppliers on the basis of recommendations submitted by a joint Chinese-American subcommittee of CUSA, these recommendations being based on the prewar supply pattern; although this method of selecting suppliers has to some extent reduced the scope of price competition, prices paid for petroleum have been carefully scrutinized in the light of Section 202 of Public Law 793.

Procurement of wheat and flour has been from United States surpluses, purchases being made by the Commodity Credit Corporation of the U.S. Department of Agriculture from private suppliers on the basis of competitive bidding. These purchases have been against U.S. Department of Commerce allocations, determining the total quantity of U.S. wheat exportable to China. Rice has also been

procured by the Commodity Credit Corporation, pursuant to Section 121, Public Law 472, chiefly in Siam and Burma, purchases being made against IERC allocations.

Up to December 31, 1948, more than 99 percent of the ECA-financed cargo tonnage originating in the United States and delivered to China had been shipped in U.S.-flag vessels; this was far in excess of the over-all requirement for ECA (in section 111 (a) (2) of Public Law 472) "that at least 50 per centum of the gross tonnage of commodities, procured within the United States out of funds made available under this title and transported abroad on ocean vessels, is so transported on United States-flag vessels to the extent such vessels are available at market rates."

Procurement and Pricing of Commodities in China

Aid in providing essential commodities has been regarded by the ECA as a supplement to, and not a substitute for, production and supply efforts by the Chinese Government. This has been especially true with regard to the food program, in connection with which the ECA China Mission has undertaken to secure as effective performance as possible by the Government in providing from indigenous sources a substantial share of the food supplies required for the cities receiving ECA food shipments. In order to minimize the degree of subsidy to private consumers at the expense of government income, the China Mission has undertaken, with varying results, to exert its influence in favor of the selling of rationed food at, or near to, actual market prices; the same is true with respect to cotton goods and petroleum products. Similar influence has been exerted, as far as practicable, with regard to prices for coal, rates for electric power, or levels at which any enterprise, directly or indirectly assisted by ECA, sells its products.

End-Use Control

Measures essential to effective end-use control have been carefully developed for each of the commodity programs, in order to assure that supplies provided through ECA would go to the recipients for which they were intended, to furnish maximum assistance to people and institutions within China, to support efforts of the Government to increase production and stabilize economic conditions, and generally to secure the best results attainable through the expenditure of ECA dollars.

Food has been distributed through controlled rationing systems in major cities of China, and a detailed record has been kept of individual recipients of this aid; ECA representatives attend as observers the meetings of City Food Committees, and ECA Investigators inspect and report on all phases of operations under the rationing program. The cotton aid program is directed in China by a Joint Management Board whose decisions require CUSA and ECA concurrence; a system has been established for following cotton through conversion into yarn, the conversion of yarn into cloth, and the subsequent domestic use or export of the resulting textiles. Petroleum has been distributed primarily by major oil companies which themselves help to make sure that ECA-financed oil goes only to the uses for which it is allocated; a Joint CUSA-ECA Petroleum Committee estimates requirements and supervises distribution. Control arrangements are being developed to insure that fertilizer will be distributed in a way that will achieve maximum effect in increasing food production.

Further details with respect to end-use controls are contained in the description below of the several commodity programs, and in the Appendix.

Food

The interior of China—including countryside, towns and cities—has normally been relatively self-sufficient in foodstuffs, but the larger coastal cities have in recent decades become increasingly dependent, for part of their food supply, on imports from abroad. As previously indicated, the problem of food supplies for these cities became acute in the spring of 1948 due to the disruption of communications and trade by the civil war, spiralling inflation, and increasing strains upon the Government's foreign exchange resources.

INCEPTION OF FOOD RATIONING IN POSTWAR CHINA

Food rationing in postwar China was first developed in the program of the United States China Relief Mission. Under this program the U. S. Government provided—for the five major coastal cities of Shanghai, Nanking, Canton, Peiping and Tientsin—approximately 200,000 tons of rice, wheat and flour, of which more than 150,000 tons was distributed before the end of June 1948. Contributions from the Chinese Government approximately matched this tonnage, with the result that between March and the close of June about 300,000 tons of food was sold at prices considerably lower than those prevailing on the open market to between 11 and 12 million inhabitants of these cities.

Each individual, under the rationing program, was limited to a monthly purchase of 16.5 pounds of rice or flour, although no one was limited in the amount that might, if available, be purchased at inflated prices on the open market.

This program was an innovation in China. Food rationing on a major scale had not previously been practiced there as it has in most other countries of the world where shortages posed a problem of equitable distribution of available supply. Chinese officials considered the matter long and carefully before undertaking the responsibility for a program which depended for its success upon the development and maintenance of relatively complicated administrative machinery. However, once started, the administration of the program was carried out with a record of competence, precision and honesty that became a source of gratification to all parties concerned, including the Chinese officials responsible for the operation.

SEVEN-CITY RATIONING PROGRAM

Following the first arrival of ECA food supplies in China, it was decided that the rationing program should be continued as the best means of applying U.S. aid in an equitable manner, of retarding somewhat the rapid rate of price increase, and of providing an added source of revenue to the Government. Under the ECA program, the number of cities participating in rationing was extended to include Swatow and Tsingtao. In the latter city, the U. S. Navy maintained a base in an area which was surrounded by Communists and cut off from local sources of food supply.

The somewhat fluctuating population of the seven cities participating in the rationing program ranged, in total, between 12.7 and 13 million during 1948.

Under arrangements agreed upon between the ECA China Mission and the Chinese Government Council for U. S. Aid (CUSA), agreement was reached on the setting up, within the Chinese Government's Ministry of Food, of an Office of Emergency Food Procurement (OEFP), which was to handle indigenous purchasing for the rationing program. The OEFP undertook initially to procure from indigenous sources approximately 60 percent of the total food required for the operation of the rationing system, and ECA approximately 40 percent.

EMERGENCY FEEDING PROGRAMS

In addition to this rationing program for seven cities, a limited emergency feeding program for Mukden was developed while that city remained in Nationalist hands. Nearly one thousand tons of flour delivered under this emergency program were cooked and fed directly to key groups of workers with appropriate publicity. The resultant increase in morale was notable until, with the Communist assault on Mukden, the program had to be suspended. Some 400 tons of ECA flour in Chinchor awaiting airlift to Mukden were captured by the Communists during their rapid advance in that sector.

In order to cope with the heavy influx of refugees into Tsingtao from the war zones and to compensate for the reduced supplies of indigenous food coming into the city because of communist occupation of surrounding territory, the ECA China Mission has also provided, in that city, continuing support for a special Refugee Feeding Project originally instituted under the CRM program. This project, conducted outside the rationing program in cooperation with municipal authorities, consists of open-air kitchens which prepare and serve daily portions of rice congee to an estimated 100,000 refugees. Damaged rice, sweepings and poorer grades of rice unsuitable for rationing, which are received in ECA shipments from southeast Asia, are set aside for this project in Shanghai, for transshipment to Tsingtao. The bulk of shipments have been made via vessels of the U.S. Navy, which considers the project a necessary emergency measure effective in the maintenance of orderly conditions in Tsingtao. Requirements for the project are 1,300 tons per month.

AUGUST 19 REGULATIONS AND INDIGENOUS PROCUREMENT

An element of subsidy was inherent in the seven-city rationing plan. But it was never intended that the prices of rationed cereals would be allowed to fall far below open market prices. At first, prices for rationed foods were adjusted monthly to a level approximately 5 percent below prevailing open-market rates and held there throughout the ensuing month, regardless of price rises in the open market. Thus the Government was in a position to obtain much needed revenue from sales of rationed rice and flour, even though some slight subsidy accrued to the people, for the U.S. supplies thus sold cost the Government nothing and all local currency returns from this sale constituted a net gain.

Under the Government's August 19 reform measures, however, ration prices, particularly in the central and north China cities, were set well below market prices, with the result that the dependence of the program on governmental subsidies became heavy during the period until November when these measures were drastically revised. As the military, political and economic situation deteriorated, the Government deemed it expedient to use the rationing programs to provide an outright subsidy to all the people in the urban coastal cities in an effort to mitigate public discontent. At this time, wages were lagging so far behind essential commodity prices that the city populations began to be unable to purchase minimum requirements of daily necessities. ECA officials reluctantly acquiesced in the selling of U.S.-contributed food supplies along with indigenous supplies, at what to the Government were ruinously subsidized prices, but warned that the policy would prove exceedingly costly.

Since ECA funds for food procurement were limited, it appeared advisable at the outset to conserve them in large part to provide foodstuffs for the 1948-49 winter and spring months and thus assure rationing supplies at the time of the year when food is normally less plentiful. The Chinese Government agreed to find and deliver the foodstuffs needed for rationing during the last quarter of

1948, with the understanding that the ECA would undertake to supply a major portion of the ration during the first quarter of 1949 and to deliver additional food thereafter to the extent of availability of funds from the 1948 appropriation.

Difficulties developed in the implementation of this plan. The obtaining of indigenous supplies by the Chinese OEFF was slow and erratic; its attempts to purchase domestic food supplies were inspired by lack of sufficient appropriations and by the disparity between official and black-market prices. There was a failure to act quickly to procure domestic supplies in quantity when the harvests were in. Anticipated purchases of rice in Burma did not materialize. Some flour was collected at Shanghai for the ration in the cities of north China, but commandeering by the military of the ships selected for the transport of these supplies caused considerable delay in their movement. As indicated above, the unsuccessful economic regulations promulgated by the Government on August 19, 1948, resulted in the exclusion from China's major cities of normal free-market supplies of indigenous foods. The acute shortages, dramatized by all-night queues in front of food shops, were intensified by a partial breakdown of the rationing system during October. At the middle of October none of the cities except Canton and Tsingtao had even been able to start the October ration, and one city was still trying to fulfill the September ration commitment.

Throughout this period, the ECA China Mission pressed for the lifting of arbitrary food price ceilings in the cities, for a realistic pricing of rationed foods, and for more vigorous efforts by the OEFF to procure indigenous supplies.

SPEED-UP OF ECA DELIVERIES

Steps were also taken to speed up ECA deliveries of wheat, previously scheduled for the first quarter of 1949, in order to move up to November and December the resumption of ECA's contribution to the ration system. Some success was achieved in the acceleration of ECA shipments to China—which proved to be of crucial importance in allaying unrest in major cities—and in the development of more realistic pricing for rationed food, but indigenous procurement efforts by the Chinese Government continued to lag.

Reported shipments as of December 31, 1948, under procurement programs 1, 2 and 3 (for the second, third and fourth quarters of 1948), were valued at approximately \$37,000,000 for the purchase of 129,000 tons of rice and 107,000 tons of wheat and flour. In addition, about 25,000 tons of rice and flour had been received as residue from the China Relief Mission and 9,000 tons of rice had been borrowed from Hongkong to relieve a threatened November food shortage in Shanghai. Of these amounts, approximately 120,000 tons of rice and 30,000 tons of wheat and flour had before the end of December been released for the rationing programs. Additional Program 3 stocks either en route, loading or waiting for shipment, at the end of 1948, totaled 27,000 ton of rice from Siam and Burma and 56,000 tons of wheat and flour from the United States.

SUPERVISION OF RATIONING PROGRAM

Although administered by Chinese Government officials, the ECA food program in China has been carefully supervised by ECA representatives who have insisted upon the maintenance of high standards of performance and honesty. Mindful of the considerable pilfering and misuse of food supplies previously delivered under the UNRRA program, ECA has paid utmost attention to the problem of end-use control. Strict supervision and careful checking have been applied to every phase of distribution in order to assure that all ECA-financed food supplies allocated to the rationing program actually reach the end recipient. A detailed descrip-

tion of rationing and end-use control under the ECA food program is contained in the Appendix.

The United States has delivered its contributions to the rationing programs regularly and on time. ECA officials in China have manifested constant concern that the rationing program should be conducted for the benefit of the people as a whole. These facts are well known to the millions of persons affected, and has done much to sustain their faith in the friendship of the American people.

Cotton

The first step in the cotton program involved an easing of pressure upon China's strained foreign exchange resources by ECA financing of existing consignment contracts with early delivery dates; these contracts were between the China Textile Industries, Inc., and the agents in Shanghai of American cotton shippers. All of the cotton involved was programmed for supply from the United States. In the course of authorizing procurement of this cotton, provision was made for joint supervision, by the Government and the ECA China Mission, of processing and distribution of raw cotton after arrival in China.

The total cotton program developed under the current China Aid Program involved an expenditure of nearly \$70 million. During October 1948, the first of this cotton reached the mills and the system of control and reporting of end use was perfected. As of December 31, cotton in the amount of 299,038 bales, costing approximately \$52.7 million, had arrived in China and was being allocated and distributed to the mills; 51,000 bales of yarn and 557,000 bolts of cloth (40 yards each) had been received back from the mills.

Under the ECA China aid program, all cotton is procured through private trade channels. Cotton shipments to China are continuing under schedules designed to maintain production and employment while avoiding any undue advance stockpiling.

The Chinese textile industry with about 3,900,000 operable spindles is China's largest manufacturing industry and raw cotton is one of China's vital imports. Not only are the cloth and yarn produced of great significance to the Chinese economy, but a high level of employment among the textile workers is important to the maintenance of relative stability in industrial centers, particularly in Shanghai.

RAW COTTON SUPPLY PROBLEM

Before the war, cotton grown in China supplied the bulk of the fibre required to keep the textile mills in operation. Due to some reduction in cotton acreage and, more important, to the extensive disruption of internal transportation trade caused by the civil war (see accompanying map), indigenous cotton has gone largely into household use and China has had to depend on imports for more than a third of the cotton used in her mills. In the year 1947-1948, mill consumption was about 1,950,000 bales; imports of cotton were about 700,000 bales (as compared with a prewar level of imports of 340,000 bales). Procurement was in considerable part from India, and limited quantities were purchased also from British East Africa, Burma and Egypt.

Provision of the necessary foreign exchange for cotton importation has been for China a problem of increasing proportions. The ECA program, which financed 300,000 bales in 1948 and in January of 1949 was in process of financing an additional 100,000 bales, has been a major factor in the sustaining of production and employment in China's textile industry during the latter part of 1948.

USE AND CONTROL OF ECA COTTON IMPORTS

The plan developed for the use of ECA cotton imports called for the conversion of the cotton into yarn under arrangements involving processing or trading at a fixed ratio under which raw cotton is paid for by the processing and in most cases by conversion of the resulting yarn into cotton cloth. The Council for United States Aid (CUSA) and the ECA Mission to China agreed upon a division of the yarn and cloth produced from ECA cotton, with 50 percent to be used for domestic consumption and the rest to be exported—the proceeds to be used for purchase of additional raw cotton. Exports under this program had up to December 31, 1948, earned an equivalent of more than \$4.5 million in foreign exchange, all sales being to countries of southeast Asia. Domestic distribution is largely by direct sale through commercial channels; some of the textiles, however, have been used in barter schemes, as described below, designed to bring more food into the cities. More than 2,000 bales of yarn and cloth made from ECA cotton were bartered in Nanking, Shanghai and Nanchang for 33,000 piculs of rice at a time when no other grain was moving into these cities from producing areas.

The arrangements adopted followed careful planning and careful negotiation by the Mission with the Chinese Government. The conversion, storage and disposition of ECA-financed cotton shipments to China are under the control of a Joint Management Board, and full records of each stage of the process are kept for end-use control purposes. Details of the end-use control mechanism developed are presented in the Appendix.

Petroleum

Since production of crude oil in China is negligible, the country is almost wholly dependent upon imports of petroleum products required in the operation of utilities, transport facilities, and manufacture and for household use. The cutting off of coal from north China, as a result of the civil war, increased greatly during the year the relative importance of petroleum products for power and industrial units in which they could be substituted for coal.

Taken as a whole, petroleum imports were vital to the operation of China's limited transport facilities and industrial plant. Diesel and fuel oil were essential to the operation of power plants and other utilities. These types, as well as motor and aviation gasoline and lubricants, were essential to the operation of water, rail and air transport. The use of kerosene, normally in wide demand for household lighting and fuel in rural districts and towns lacking electric power, has been restricted by disruptions in transport, but there has been continuing demand in the more accessible areas.

USE OF NORMAL TRADE CHANNELS

The petroleum program involved, at first, negotiations on the part which each of the petroleum distributing concerns and the large end users in China would play in the importation and distribution of the products. The problems involved were largely settled about the middle of 1948, and firm authorizations were thereupon prepared for issuance.

As a result, the importation and distribution of petroleum products under the ECA China Aid Program have been entirely through normal trade channels and the bulk of the business is handled by the Standard Vacuum Oil Co., the Shell Company of China, Ltd., the California Texas Oil Co., and the Chinese Petroleum

Corporation (an agency of the Chinese Government). A number of small importers and distributors have also participated in the program. The oil companies at first charged somewhat higher prices for petroleum products to China than to other destinations in order to recover thereby the foreign exchange component of internal distribution costs. Such price differentials were not satisfactory either to the Chinese Government or ECA; consequently ECA has indicated its willingness to finance only such petroleum shipments as are priced on a cost-and-freight basis and are within the U.S. market price as provided in Section 202 of the appropriation act (Public Law 793).

As of December 31, 1948, the Central Bank of China had financed petroleum brought into China under the ECA China Aid Program to a value of about \$28 million, for which amount the Central Bank of China was to be reimbursed by ECA as rapidly as the requisite documentation is furnished ECA by the Central Bank of China.

In view of the Central Bank's straitened foreign exchange position, ECA Headquarters on November 26, 1948 authorized an advance of \$15 million to the Central Bank to enable it, pending reimbursement by ECA, to continue financing the release and distribution of petroleum products in China. Shortly before the end of the year, the reimbursement procedure was abandoned, and arrangements were made to finance all future petroleum shipments (and releases from bonded tanks of products already in China) by letter of commitment to U.S. banks. In connection with the new procedure, the ECA Mission to China was given the responsibility of approving each shipment or release in advance, in order to avoid undue stockpiling of petroleum products in Chinese ports.

ADMINISTRATION OF PETROLEUM PROGRAM

Requirements programs have been prepared on a quarterly basis by the CUSA-ECA Petroleum Committee, which includes both active members and observers from CUSA and ECA. Up to the end of 1948, prices within China were determined by the Oil Allocation Committee, with approval of the Executive Yuan; the CUSA-ECA Petroleum Committee has sought Executive Yuan approval of a plan to authorize a CUSA-ECA-EIB (Export-Import Board) Price Adjustment Committee in Shanghai to make periodic reviews and price adjustments on its own initiative, in order to keep prices on a realistic basis and prevent the oil companies from sustaining losses because of currency fluctuations.

With ECA assistance, production has been continued at the Kao-hsiang refinery in Taiwan to which, at the end of 1948, 225,000 barrels of crude oil were being provided monthly, for conversion into motor gasoline, diesel and fuel oil and kerosene. The plan under which this assistance has been given was developed on the basis of recommendations by an independent firm of engineers engaged for the purpose by the Chinese Government upon the suggestion of ECA.

End-use control of the petroleum products imported into China has presented fewer administrative problems for the ECA than end-use control of other commodities. Distribution of ECA-financed petroleum products in China is generally of two types: distribution to large users (for example, fuel oil for the Shanghai Power Company) and distribution by individual companies to end users (for example, retail distribution of gasoline through filling stations to car owners). Since the companies are the distribution agents, and the major distributors are two American companies and one British company, these firms themselves provide a considerable measure of end-use control and are able to do most of the end-use reporting required, subject to necessary spot-checking by the ECA Mission.

Fertilizer

Procurement of fertilizer has proceeded within the limitation of availabilities for China from existing world supplies, as reflected in allocations by the International Emergency Food Council. Although increased use of fertilizers offers promise of substantial increases in indigenous food production, its widespread application during the postwar period has been impeded by a lack of extensive previous experience in the use of chemical fertilizers in China, except in Formosa; by a shortage of extension personnel and organization to train Chinese farmers in the effective application of modern fertilizers; and by the difficulty of devising effective distribution and end-use control systems within China. Under plans being perfected at the end of 1948, it was expected that substantial distribution to end users, particularly in Formosa and south China, would occur during the first quarter of 1949, and that a reasonable minimum of fertilizer could be made available in China for the spring planting.

ECA PROCUREMENT OF FERTILIZERS

Under the current China Program, ECA is financing the procurement of approximately 75,000 metric tons of chemical fertilizers, at a cost of approximately US\$8.9 million; this should be of material benefit in increasing rice production in some districts, particularly in sections of Formosa and south China. It was at first planned to spend U.S. \$13.8 million on fertilizers. Subsequently, arrangements were made whereby the Bank of China, the Central Bank and the Taiwan Provincial Government undertook to finance from their own resources the procurement of a portion of the nitrogenous fertilizers allocated to China by the International Emergency Food Committee; ECA thereupon reduced its fertilizer commitment by 4.9 million dollars. Under these arrangements China is in a position to acquire during 1948-49, through ECA and Government procurement, 116,000 metric tons of ammonium sulphate and ammonium phosphate. Having been used by Chinese farmers who have previously employed chemical fertilizers, these types are considered the most practical under prevailing agricultural practice.

AID TO FOOD PRODUCTION IN CHINA

Fertilizers provided by ECA are primarily for use in increasing yields of lowland rice, which should mean a corresponding decrease in dependence upon importations of rice from abroad.

It has been found, through scientific experimentation and practice, that one unit of nitrogenous fertilizer can produce an average increase in yield of at least 2 units of clean rice or about 3 units of paddy rice, all by weight. Theoretically, therefore, one dollar's worth of fertilizer should produce three dollars worth of grain (in terms of each equivalent to the import cost of an equal amount of food). However, owing to high transportation and internal handling costs and low price of rice at producing centers in China, a somewhat smaller gain is realized. Nevertheless, the use of chemical fertilizer is the most effective means known to augment food production in China.

The total annual domestic production of chemical fertilizers in China, at the 1948 rate, was only about 81,000 metric tons (36,000 ammonium sulphate, 35,000 superphosphate and 10,000 calcium cyanamide). A provisional allotment from ECA of \$5.5 million to China's domestic fertilizer industry, aimed to increase substantially production capacity, had to be suspended at least temporarily, toward the end of the year, due to disturbed civil war conditions.

At the end of 1948, the first 10,000 tons of ECA fertilizer was scheduled to reach Shanghai in January 1949. This installment, on the basis of an agreement with the Farmer's Bank, was to be distributed to farmers who, during November and December, had advanced rice for the food rationing program. Plans were developed for the distribution, through commercial channels in south China and Taiwan and through the Joint Rural Reconstruction Commission, of additional shipments totalling about 61,000 tons.

Coal

China's principal coal-producing centers have been in north China and Manchuria. As indicated on the accompanying map, military developments together with the cutting of vital transportation routes during 1948 interrupted the flow of coal from north China producing areas to consuming areas in central China.

Arrangements were made, therefore, for ECA procurement on an emergency basis of limited stocks from Japan through the Supreme Command, Allied Powers, Pacific (SCAP) organization. Before the end of 1948, coal in the amount of 15,000 tons had been obtained from Japan at a cost of about \$280,000, and there was a prospect that further emergency procurement would be required.

Medical Supplies

About \$5 million worth of medical supplies were procured for China under Public Law 84, the U. S. Foreign Relief Program. Most of these supplies arrived in China after the expiration of the China Relief Mission on June 30, 1948; they became, therefore, an ECA responsibility. As of December, nearly 90 percent of the supplies programmed by the China Relief Mission had arrived in China.

The reception, storage and transportation phases of the medical supply program have worked smoothly and losses from pilferage and improper handling have been negligible. Special medical warehousing units established have operated with a high degree of efficiency. On the basis of careful allocation and distribution planning by the Council for U. S. Aid, the ECA Mission to China, the Ministry of Health and the International Relief Committee, the distribution of these supplies was proceeding regularly at the end of 1948.

Distribution from Shanghai was being accelerated in view of the rapidly changing political and military situations; additional warehouses were being stocked in Canton and Taipeh (on the island of Taiwan), leaving in Shanghai only supplies required in that area. It was expected that final distribution of medical supplies to end users would be completed by May 31, 1949.

Pesticides

ECA also took over from the China Relief Mission responsibility for \$537,000 worth of pesticides which reached China during 1948; most of these supplies arrived too late for distribution during the lifetime of the China Relief Mission.

Plans were developed and agreed upon between ECA and the Chinese Government in September, for allocations of 35 percent of these pesticides to the Joint Rural Reconstruction Commission, 15 percent to the Ministry of Agriculture and Forestry for free distribution at agricultural demonstration centers, and the remaining 50 percent for sale through commercial channels. Sales during October and November were principally in south Kiangsu and north Chekiang areas bordering the Shanghai district and were concluded in time to give needed protection to crops. When seasonal demand from farmers in these districts ceased, sales efforts were directed to south China where, with a long growing

season, the need for insecticides continued during ensuing months. In Taiwan, where the use of agricultural insecticides is best known, the only channels through which farmers had been accustomed to obtain their supplies in the past had not, at the end of the year, been utilized in accordance with original plans due to lack of requisite cooperation in making supplies quickly available to consumers.

Special Barter Arrangements

A barter program, of an emergency nature, was developed initially on a small scale. Difficulties experienced by the Chinese in obtaining their quota of domestic food supplies for the rationing program were such that CUSA and ECA undertook to exchange limited quantities of cloth and yarn (manufactured from aid cotton) for rice and other indigenous food grains.

About two hundred tons of cloth were sent to Nanking, for example, to be used in exchange for rice, about 150 pounds of rice being obtained for each piece of grey cloth 40 yards long.

In villages near Shanghai a similar type of exchange was developed, and in Changsha, commercial center of a large rice-producing area in northern Hunan, a beginning was made. Such exchanges up to the end of 1948, were experimental in character. The results attained indicated that considerable quantities of rice could be obtained in this manner, and it was planned that regular supplies of yarn and cloth to be used for this purpose would shortly be advanced to Office of Emergency Food Procurement, with ECA observing OEFFP operations and ensuring strict end-use accounting.

In North China ECA representatives were, at the end of November, negotiating with representatives from General Fu Tso-ji's headquarters and local grain dealers. A contract was under consideration calling for 120,000 pieces of cloth to be used in exchange for domestic wheat, flour, and coarse grains, the food-stuffs to be used in a selective rationing plan for workers in essential services. This plan was disrupted by military developments in the Peiping-Tientsin area.

Two principal purposes were served by such barter of cloth and yarn for food: (a) the obtaining of additional supplies of food for use in the rationing programs and (2) the distribution of yarn and cloth in interior areas, in many cases direct to the farmers without passing through middlemen, thus reducing opportunities for cloth and yarn to fall into the hands of speculators.

Shipping

Mention has been made of the fact that more than 99 percent of ECA-financed commodities shipped from the United States to China during 1948 were carried in U.S. vessels.

Internal administrative rulings defining what types of transportation expenditures are eligible for reimbursing from ECA funds, written principally for application to Europe, are generally applied to China. However, due to emergency conditions in China the Administration has seen fit to depart from its general rules on special occasions. These departures involve the payment of partial freight in dollars to certain Chinese ships chartered to move rice from Siam and Burma. The rice, procured by U.S. representatives using ECA funds, has been moved to China on an exacting schedule to meet ECA's feeding program in principal Chinese cities. About \$727,000 for freight thus provided before the end of December 1948 made possible the movement of 39 Chinese ships carrying about 155,000 metric tons of rice.

These movements of rice from southeast Asia to China have not taken place exclusively in Chinese ships; funds are made available to U.S. representatives to enable them to use American ships interested in the traffic. However, only one American ship was used for this purpose in 1948; the cost via this vessel was \$7.50 per ton as compared with the current Chinese rate of \$2.00 per ton from Siam. The Chinese rate toward the end of 1948 was \$3.50 per ton from Burma as compared with an estimated \$10.00 per ton in American vessels. It is considered doubtful whether the dollars provided the Chinese cover the out-of-pocket expenses of the ships involved, which do receive some additional compensation in Chinese currency from counterpart funds.

The reason for close scheduling of shipping carrying food into China has been to import sufficient amounts to prevent starvation and riots, at the same time avoiding stockpiling of quantities that might be lost as a result of the war. In addition to scheduling rice shipments, considerable authority was delegated to the ECA Mission in China to divert U.S. wheat and flour shipments, as well as shipments of other commodities, to meet changing situations. When the military situation in the vicinity of Tientsin deteriorated, several American ships about to discharge in ports serving that area were diverted to Tsingtao.

INDUSTRIAL RECONSTRUCTION AND REPLACEMENT PROGRAM

A total of \$70 million was originally programmed for industrial reconstruction and replacement projects in China. The legislative history of the China Aid Act indicated considerable Congressional interest in this significant aspect of proposed assistance to China. Extensive, painstaking preparations were made, including the sending to China of a special Reconstruction Survey Group, in order to ensure the most productive use of the funds made available for industrial reconstruction and replacement purposes.

Necessity for Suspension

However, due to developments in the civil war situation in China, it became necessary for the Administrator, on December 21, 1948, to announce that work on the reconstruction and replacement program was, to a large extent, being suspended—exceptions being made in connection with the completion of certain pre-project engineering studies which had already reached an advanced stage of development. Preparatory work on some of the projects, located in areas of Manchuria or north China involved in or threatened by military developments, had already in fact been suspended. The series of defeats sustained by the Nationalist forces in the fall and early winter of 1948, jeopardizing the Government's position not only at its remaining bases in north China but also in the Yangtze Valley, had resulted in chaotic conditions and major uncertainties throughout many of the regions in which reconstruction and replacement projects had been planned.

The suspension did not eliminate the possibility of renewed activity on selected projects in areas remaining accessible, in the event that such a partial resumption of the reconstruction and replacement program should at any future time be deemed feasible and expedient. At the time of suspension, all of the projects were still in the pre-project engineering stage, no funds having as yet been actually committed for procurement.

The following paragraphs present a brief summary of the problems encountered in the field of industrial replacement and reconstruction, the planning and preparatory work undertaken, and the practical arrangements developed for the initiation and execution of replacement and reconstruction projects in China. A

listing, with brief descriptions, of the projects for which "provisional allotments" were made prior to the suspension of this part of the program, appears in the Appendix.

Planning and Preparatory Work

Initial planning had called for an expenditure of \$60 million for reconstruction and \$10 million for replacement work; as a result of the work of the Reconstruction Survey Group, however, much greater proportionate emphasis was placed upon replacements needed to increase the productivity of existing enterprises.

Initial members of the Survey Group reached China on June 7, 1948. The Group, consisting of 4 engineers, 2 economists, a lawyer and a businessman (Charles L. Stillman) who served as its head, operated as a part of the ECA Mission to China. After several months' reviews of conditions in China by the members of this Group, the ECA Mission developed, in agreement with the Chinese Government, a tentative program designed to make a significant start toward the reconstruction or rehabilitation of certain railroads, electric power plants, fertilizer manufacturing units, and coal, tin and antimony mines—all in non-Communist China.

The program finally recommended by the Survey Group and tentatively approved by the Administrator prior to the enforced suspension of this aspect of ECA assistance to China, called for approximately \$25 million worth of new reconstruction or development, \$35 million to be spent for replacement assistance, and \$7.5 million for engineering services and reserves, making a total of \$67.5 million; the remaining \$2.5 million was earmarked for foreign exchange expenditures required in connection with the rural reconstruction program. Most of the projects planned were in the fields of basic industry and transportation—approximately \$13.5 million being provisionally allotted for railway rehabilitation, \$17.25 million for power plants, \$11 million for coal mines and \$5.5 million for fertilizer manufacture.

Following extensive consideration within ECA of the possibility of extending assistance to certain types of replacement and reconstruction projects on a loan basis, and after subsequent consultation with the National Advisory Council, it was tentatively determined that projects currently under consideration would be provided on an outright grant basis, leaving open the possibility of future reconsideration of loan proposals.

Problems of Industrial Reconstruction in China

The Chinese, in taking back control of their country after eight long years faced many problems. The areas reoccupied had been swept over by Japanese armies, by Chinese armies, and by Chinese and American airforces. Communist raids and damage by armies of both sides in the civil war had continued in many regions. Nearly all existing industrial facilities were in deplorable condition due to a variety of causes dating back to the opening of the Sino-Japanese War in 1937. Railroads, partially restored during the UNRRA period, needed further assistance. Further problems were presented for foreign exchange shortages, internal economic and financial difficulties evidenced in extreme inflation, seriously inadequate transportation and a general disruption of Government and of industrial management, both public and private.

Elimination of much foreign participation in Chinese affairs, as a result of the war and the ending of extraterritoriality, inevitably left a gap in the nation's economic and industrial life. Particularly in the industrial areas, foreign participation in management and control of properties had been of significance in their development and effective operation. Following the war, foreign-flag shipping was excluded from Chinese river and coastal waters, resulting

in higher transportation costs and less adequate services. The Chinese were unable to develop comparable services in a short time.

When Taiwan (the island of Formosa) was returned to *de facto* Chinese control after fifty years of Japanese occupation, U.S. military forces removed nearly all Japanese from the island. The removal of those who had exercised management control and possessed requisite technical knowledge meant that this relatively highly developed island had to be staffed at management and technical levels with Chinese personnel who lacked previous knowledge of the properties involved and who faced, in addition to normal maintenance problems, a large replacement problem resulting from bombing damage inflicted during the war by U.S. airforces.

Considerable quantities of industrial materials and equipment had been made available to China through previous aid programs, notably the UNRRA program, and through Chinese Government procurement from the Pacific islands of United States surplus supplies after the war. China had not been able to absorb all of these supplies during the first three post-war years. The ECA faced, therefore, the problem not only of making sure that equipment under the ECA China aid program was put to effective use, but of helping also to get into operation residual stockpiles of equipment already in China.

Most of China's industrial plant had been badly undermaintained throughout the long war years, and requisite training of personnel had been largely discontinued. Although China's industrial development was still in its early stages, the effective functioning of the nation's limited industrial plant was regarded as vital for the production of goods essential to the reducing of China's dependence upon external aid, and for an effective approach to the problem of inflation.

The essence of the problem facing ECA, then, was an extensive need for replacement and reconstruction equipment and a lack of the foreign assistance in engineering and management requisite to the effective absorption of such equipment into the Chinese economy. A solution to this problem required a unique approach. Engineering and management assistance would have to be furnished along with the equipment. The ECA, in approaching this problem, needed also to bear in mind objectives implicit in the legislative history of the ECA: to maximize the use of private trade channels, to encourage both internal production and international trade and to avoid impairment of the U.S. economy.

Insufficiency of technical knowledge and experience in management had been a recurrent problem encountered in efforts to help Chinese industry. This made necessary a provision of technical and managerial help along with material assistance. The Survey Group developed a unique plan of action for the meeting of this need. It recommended that each industrial project applying for, and receiving a tentative allotment for, ECA assistance be required to engage the services of a private engineering firm to help in surveying and planning the work needing to be done and in the procurement and installation of requisite equipment. The Survey Group further recommended that the Chinese Government and ECA jointly engage a high-grade American engineering management firm to assist in supervising the entire scheme, in order to ensure that this part of the China Aid Program would, as a whole, be conducted with the benefit of outstanding engineering talent and experience. These recommendations contemplated ECA payment for such engineering services under the "technical assistance" provision in Section 111 (a) (3) of the Foreign Assistance Act of 1948. These recommendations, in which the Chinese Government concurred, were approved by the Administrator as a tentative basis on which further development of the program might proceed.

In anticipating the types of firms best equipped to undertake, on behalf of provisionally approved projects, the requisite work of pre-project engineering analysis and subsequent assistance in procurement and installation, consideration was given both to engineering firms without previous experience in China and to concerns which had been active in developing production and trade in China. Some of the latter, with worldwide connections, extensive local experience and competent resident managers and staffs of engineers, both Chinese and foreign, could, it was believed, make valuable contributions, under appropriate safeguards, to the success of the program.

Practical Arrangements Developed

After consideration of all aspects of this complicated program, the Chinese Government and the ECA Mission to China agreed to form a non-voting consultative Joint Committee composed of three representatives of the Chinese Government and two representatives of the ECA Mission to supervise the carrying out of the replacement and reconstruction projects. This arrangement was in accord with the principles of the Economic Aid Agreement between China and the United States which specifies that programs are to be carried out by mutual agreement.

It was decided to engage the services of an outstanding American management engineering firm to assist the Joint Committee. This was a distinct change from methods hitherto employed for previous aid programs by either government or by the United Nations for the UNRRA program. Previous practice had involved efforts to coordinate the work of Chinese and non-Chinese staffs, without use in most cases of special engineering consultants or of normal business and trade channels for functions which might be performed efficiently and economically by private enterprise. The Joint Committee, representing both governments, decided to retain in a technical capacity the J. G. White Engineering Corporation of New York City. The principal function of this corporation, it was agreed, would be to furnish technical supervision, with a group of from six to ten U. S. engineers, of the projects approved under the tentatively authorized \$70 million ECA replacement and reconstruction program in China. The staff was not itself to undertake any "projects", but to assist the Joint Committee in selecting, recommending for approval, and supervising a wide range of industrial projects.

The procedure adopted may be outlined briefly as follows:

Private or public enterprises desiring assistance under the program would present initial applications to the Joint Committee which would refer them to the J. G. White Corporation for analysis and recommendation; projects provisionally approved by the Joint Committee were to be given "provisional allotments".

As soon as a "provisional allotment" was made, the successful applicant was to select an engineering firm as its "project engineer", this selection requiring ratification by the Joint Committee set up by the Chinese Government and the ECA China Mission.

The project engineer would draw up a bill of materials with detailed specifications, search world markets for necessary equipment and supplies which could be procured on the most expeditious and economical terms, and present a fully justified "project" to the Joint Committee.

Upon approval of the project by the Joint Committee, the project engineer would arrange for the procurement and delivery of approved equipment and material, and assist the applicant in achieving prompt installation and use.

Financing was to be done by ECA by a letter of commitment to a U. S. bank, in

effect guaranteeing letters of credit (a) to suppliers of equipment or materials under approved projects, and (b) to the project engineer for his approved fee.

At each stage of this procedure, the J. G. White Engineering Corporation was to act as technical staff to the Joint Committee, the Committee taking action only after receiving the recommendations of its technical staff on such matters as: approval of the selection of project engineering firms, approval of fees and charges by these firms, approval of the detailed specifications and sources of procurement of equipment for the projects, and approval of prices of materials to be procured. Before any program was approved, the applicant and the project engineer would be required to submit to the Joint Committee a sworn affidavit containing information with respect to their profit margins and their methods of seeking materials, including competitive bidding. Arrangements could be made for the technical staff of the Joint Committee to accept sealed bids on items where relationships between the project engineer and the supplier indicated that such protection would be desirable.

These procedures taken together represented a new pattern for publicly financed industrial projects in underdeveloped areas. As such, they provided a unique approach toward the solution of a large continuing problem, that of grafting branches of modern technology onto the great trunks of agrarian economy in Asia and other underdeveloped parts of the world. An uninterrupted testing of this approach was unfortunately precluded by events in China.

RURAL RECONSTRUCTION PROGRAM

During the deliberations of the House Foreign Affairs Committee in February and March of 1948 on prospective aid to China, consideration was given to the fundamental and extensive needs of the Chinese economy in the field of rural reconstruction. Some new light had been thrown on this problem by a special agricultural mission sent to China by the President in 1946. Valuable experience in dealing with certain aspects of the problem had been gained through the Chinese Mass Education Movement headed by Dr. James Y. C. Yen. Information from these and other sources was weighed by the Committee with the result that rural reconstruction was included in subsequent China aid legislation as a specific field in which program funds might be spent.

Section 407 of the China Aid Act

Authorization for inclusion of a special rural reconstruction program was provided in Section 407 of the China Aid Act of 1948—the full text of which appears in the Appendix. This Section authorized the Secretary of State, after consultation with the Administrator, "to conclude an agreement with China establishing a Joint Commission on Rural Reconstruction in China, to be composed of two citizens of the United States appointed by the President of the United States and three citizens of China appointed by the President of China." Such Commission, it was provided, subject to the direction and control of the Administrator, was to formulate and carry out a program for reconstruction in rural areas of China, including such research and training activities as might be necessary or appropriate for such reconstruction.

The Act authorized an expenditure, for this rural reconstruction program, of an amount equal to not more than 10 percent of the funds made available for economic aid to China under the China Aid Act. This placed an upper limit of \$27.5 million upon the funds which could be used for the rural reconstruction program. It was stipulated that the amount could be made available

in U.S. dollars, proceeds in Chinese currency from the sale of ECA commodities, or both.

Establishment of Rural Reconstruction Commission

Following a period of negotiation, notes were exchanged on August 5, 1948, between the United States Ambassador to China and the Chinese Government Ministry of Foreign Affairs, providing an agreement for the establishment of a Rural Reconstruction Commission in accordance with the terms of the China Aid Act of 1948. The texts of these notes are quoted in the section on Documents, below.

Following the conclusion of this agreement, appointments were made by the Chinese and the United States Governments to the Rural Reconstruction Commission, the Chinese members being Dr. Chiang Monlin (former President of the Peking National University, former Minister of Education, and recently Executive Secretary of the Chinese Government Executive Yuan), Chairman; Dr. James Y. C. Yen (for 25 years the leader of China's internationally known Mass Education Movement); and Dr. T. H. Shen (outstanding Chinese agriculturist). The United States members appointed by the President on September 19, 1948, were Dr. John Earl Baker (former Director of the China International Famine Relief Commission and former adviser to the Chinese Government), and Dr. Raymond T. Moyer (U.S. Department of Agriculture authority on Chinese agriculture). On October 1, the Commission held its first meeting.

Objectives and Principles

The problem of rural reconstruction in China is one of enormous magnitude and complexity. Intensive and lengthy discussion was required to reach general agreement among members of the Commission with respect to questions of aim, emphasis, organization and methods of work. On October 18, 1948, agreement was reached on a general statement of the objectives and principles of the Joint Commission on Rural Reconstruction. The text of this statement follows:

"I. Objectives

- A. To improve the living conditions of the rural people.
- B. To increase the production of food and other important crops.
- C. To develop the potential power of the people to reconstruct their own communities and the nation, thus to lay the foundation of a strong and democratic China.
- D. To help build up and strengthen appropriate services of government agencies—national, provincial and *hsien*—that are established to carry out measures pertaining to rural reconstruction.
- E. To help stimulate and revitalize enterprises of the Rural Reconstruction Movement and other private agencies doing rural reconstruction work.
- F. To offer liberals, educated youths and other constructive elements, opportunities to participate in a program of service.

"II. Principles

1. Relating to Program

- A. The emergency nature of the present situation shall be given paramount consideration in deciding on the nature and location of program and projects.
- B. First consideration shall be given to projects which will contribute most directly and immediately to the welfare of the rural people, with special emphasis to be given to the improvement of their economic conditions.
- C. A literacy program, supplemented by audiovisual aids, shall be an essential

- part of this program, as a means of furthering education, organizing the people, and developing and selecting rural leadership.
- D. New projects in rural reconstruction deserve encouragement, but unless they can show evidence of self-help and self-support for a reasonable length of time, financial aid shall not be considered.
 - E. Projects which already have been proved successful, under rural conditions, and which are reasonably simple and inexpensive, shall be broadcast on a large scale.
 - F. In general, preference shall be given to those agencies engaged in rural reconstruction having a sound foundation and experienced staff and organization.
2. Relating to Procedure
- A. The program formulated by the Commission shall be carried out in cooperation with existing agencies.
 - B. A correlated approach shall be adopted wherever possible, since the various aspects of rural reconstruction are interrelated, the success of one depending on the success of the other.
 - C. A direct extension-type of adult education shall be emphasized as the most effective and quickest means of promoting the understanding, acceptance and correct use of recommended practices.
 - D. Local initiative shall be fostered and local resources, both human and material, shall be mobilized for the purposes of the program.
 - E. Assistance to a project in any province shall be contingent upon the willingness of the provincial and local officials concerned to cooperate fully in efforts to carry it out, and to take other steps, themselves, that are essential to the attainment of results expected of the project."

On October 26, 1948, "A Memorandum of Understanding Between the Economic Cooperation Administration and the Joint Commission on Rural Reconstruction in China, Defining Their Respective Spheres of Administrative Responsibility" was signed by the Chairman of the Joint Rural Reconstruction Commission and the Acting Chief of the ECA Mission to China. This agreement established procedures for the presentation of budget estimates by the Joint Commission and the allocation of U. S. dollar funds for material and technical assistance and of local currency from the counterpart funds for expenses incurred within China. And arrangements were agreed upon for the recruitment, administrative supervision and direction of Commission personnel.

Based on the objectives and principles quoted above, the Commission worked out the main outlines of a program, which was divided into four parts with the following aims:

To increase in supplying areas the domestic production of agricultural commodities currently in serious short supply in China and supplied in part by the United States ECA program, particularly foodstuffs;

To establish centers in which a broad integrated program would be started under appropriate agencies of the Government, through projects related to local government administration, land reform, agriculture, rural public health and rural social education;

To carry out a large-scale effort in adult education as a means of developing the potential power of the people and raising their level of understanding, thus enabling them to participate more intelligently in solving their present problems: and,

To assist significant projects in rural reconstruction established in numerous centers through local initiative and resources.

When Nanking became threatened by military action, it was decided to move the Commission's operational headquarters to Canton. At the same time, a decision was made to focus major attention first on the development of a program in provinces south of the Yangtze River, and to concentrate upon projects susceptible of prompt development and usefulness, in such fields as irrigation, dyke repair, public health, and the control of serious animal diseases.

Surveys and Organization

To put this initial program promptly into effect a trip was taken by members of the Commission to Szechwan and Hunan provinces to inspect existing efforts on behalf of the rural population and to consult with responsible persons concerning projects for which assistance had been requested. Steps also were taken to set up regional officers in Chungking (Szechwan), Changsha (Hunan), and Kweilin (Kwangsi), and a central office in Canton (Kwangtung), while retaining a regional office in Nanking. Tentative plans to carry out some phases of a rural program from two offices in north China had to be suspended on account of troubled civil war conditions there. Headquarters of the Commission were moved to Canton on December 5, 1948.

To assist the Commission in carrying out its plans, competent persons were selected as heads for three of the four divisions of work, and, at the end of the year, able appointees were under consideration for the fourth division and to represent the Commission in three of the most important regional offices. A staff of Chinese and American specialists was being assembled to advise the Commission and help carry out its program, although uncertainties in the general situation caused the Commission to proceed gradually in building up such a staff.

The impression gained by the Commission in visits to provinces in west and south China was that these provinces were at the time relatively free from the acute tension then felt in the lower Yangtze area, and that local officials and private agencies were anxious to proceed with rural reconstruction measures along the general lines formulated by the Joint Commission. Steps were taken, therefore, to get into operation, in an initial program, specific projects to which the Commission was prepared to allocate assistance.

Initial Projects

Projects for which detailed plans were being developed included the following:

A broad integrated program in rural reconstruction in the third prefecture of Szechwan province, initiated by the Mass Education Movement and local leaders, assistance to include grants for the development of educational, agricultural and farm organization projects, and loans for irrigation and weaving projects.

The completion of 11 irrigation projects already underway in Szechwan province, which would provide for the irrigation of 191,000 mow (about 30,000 acres) of land by the end of April 1949.

The establishment of a system to multiply and distribute improved rice, corn and cotton varieties in Szechwan province.

The repair of dykes in the Tung T'ing Lake area of Hunan province, which would restore to production and protect from flooding land normally producing around two-thirds of the amount of rice annually imported into China before the war, to be completed by the end of April 1949.

An integrated program of rural reconstruction in Hunan, for which definite plans were yet to be received and agreed upon.

The establishment in Hunan province, the "rice bowl" of central China, of the beginnings of an improved system of rice production and marketing, including the multiplication and distribution of improved seed varieties and the establishment of more modern milling and warehousing centers.

Projects involving cooperation with various Ministries of the National Government were being considered in consultation with these Ministries after specific project plans were reasonably well developed. Steps were being taken to set up appropriate committees of specialists to advise the Commission and to assist in carrying out phases of the rural reconstruction program; the first committee established was for work in the field of public health in rural areas, with a former Minister of Health as Chairman. In accordance with a request of the Rural Reconstruction Commission, a private public relations firm completed in November a special study of the facilities available for a widespread educational effort under the Commission's sponsorship.

Detailed plans for the irrigation projects in Szechwan, for the dyke repair project in Hunan, for certain parts of the program sponsored by the Mass Education Movement in Szechwan, and for several other projects were being reviewed in December with a view to early allocations of funds. The Commission also expected to make early announcement of projects to which it would initially allocate assistance in Kwangtung province, and trips were planned to Kwangsi, Fukien and Taiwan to study projects for which aid had been requested.

Specific plans for broader programs with a major emphasis on education, it was anticipated, might not be completed before the end of February 1949. Tentative planning, conditional upon developments, called for an extension of some assistance to such integrated programs during the spring of 1949. It was expected, however, under prevailing conditions, that available funds under the current program would necessarily be allocated principally to projects of a short-range nature, emphasizing increases in agricultural production and improvements in rural health conditions.

STRATEGIC MATERIALS

Article VI, paragraph 1, of the Economic Cooperation Agreement between the United States and the Republic of China (the full text of which is quoted in the section on Documents, below) provided that the Chinese Government would facilitate the transfer to the United States, for stockpiling or other purposes, "materials originating in China which are required by the United States of America as a result of deficiencies or potential deficiencies in its own resources upon such reasonable terms of sale, exchange, barter or otherwise and in such quantities and for such period of time as may be agreed to between the Government of the United States of America and of China for domestic use and commercial export of such materials." The Government of China agreed to undertake "such specific measures as may be necessary to carry out the provisions of this paragraph" and "when so requested by the Government of the United States of America, to enter into negotiations for detailed arrangements necessary to carry out the provisions of this paragraph."

Article V, paragraph 4, of the same agreement, provided that expenditures in Chinese currency from the Special Account (described below) would be "only for such purposes as may be agreed from time to time with the United States of America, including expenditures incident to the stimulation of production activity

and the development of new sources of wealth including materials which may be required in the United States of America because of deficiencies or potential deficiencies in the resources of the United States of America."

A preliminary investigation was conducted by members of the Reconstruction Survey Group, with a view to promoting increased production and export to the United States of strategic materials available in China and required by the United States, particular attention being given to tin, antimony and tungsten in south and southwest China. Such procurement, it was felt—to the extent that it could be developed—would, in addition to increasing the supplies of minerals needed by the United States, serve the double purpose in China of increasing local employment and augmenting the country's slender foreign exchange resources.

Production and Procurement Problems

It was found that foreign exchange policies and controls connected therewith since V-J Day, related to the Government's attempts to deal with the inflation, had exerted a depressing influence upon the production and export of these minerals, making it impossible for exporters, by and large, to obtain by negotiations through official channels fair and realistic prices for their goods. Only on rare occasions, when official exchange rates were for short periods realistic, were such exporters able to secure reasonable returns upon their produce. Initial negotiations looking toward the acquisition of these materials were aimed in part at securing the agreement of the Chinese Government to changes of policy designed to remove some of the obstacles to the flow of materials through legitimate channels of trade to the U.S., at prices fair to the producers.

Additional difficulties in procurement and export of such materials to the United States were attributable to shortage of productive equipment in China and to lack of transportation facilities from relatively inaccessible parts of China where such materials existed. Efforts toward helping to meet both these needs were clearly needed if production and procurement were to be developed on any appreciable scale.

Initial Arrangements

Following the aforementioned survey, the ECA China Mission before the end of 1948 began to work out arrangements with Chinese tin interests to make their product available for export to the United States. After receipt of pertinent information from ECA, the Reconstruction Finance Corporation in Washington offered to purchase from China considerable quantities of tin concentrates, to be refined in the U.S. where efficient smelter operation could extract a maximum percentage of high-grade tin; and to buy some tin metal in China for stockpile purposes. Preliminary negotiations were in progress at the end of the year to effect procurement arrangements, which were complicated by the necessity of effecting purchases through barter by the use of commodities or silver, instead of depreciated local currency.

SPECIAL LOCAL CURRENCY ACCOUNT

Provision for the establishment of a special local currency account, or counter-part fund, was contained in Article V of the Economic Cooperation Agreement between the Governments of China and the United States; the full text of this Agreement appears in the section on Documents, below.¹

¹ See annex 181.

Unique Provisions in the Bilateral Agreement

The article referred to provided for two unique features in connection with the special local currency account, or counterpart fund, in China. The first was a provision that deposits would be made in the account only when requested by the United States; thus deposits could be requested at a rate sufficient to cover actual expenses that had to be met currently, without the accumulation of large balances which would rapidly depreciate in value as a result of the inflation. The second was a provision that the Chinese Government would "maintain the value" of allotments made from the Special Account—for such important purposes as administrative costs, rural reconstruction and the internal expenses of industrial projects—by "depositing such additional amounts of currency as the Government of the United States of America may from time to time determine after consultation with the Government of China." The value of allotments, to be thus maintained, could be recorded in terms of such standard and relatively stable measures of value as quantities of cotton yarn, rice or American dollars.

Support for China Relief Mission Projects

Shortly after the establishment of the ECA Mission in China, discussions were initiated with the Chinese Government pertaining to the setting up and operation of the special local currency account. While these discussions were in progress, provisional arrangements were made for the use of counterpart funds made available by the Chinese Government in support of existing projects in the fields of medical services, relief and welfare, conservancy work, and agricultural improvement which had been previously supported from a local currency account created in connection with the operation of the U.S. China Relief Mission. These projects which had theretofore been regarded as ending on June 30, 1948, were in some cases selected by action of the Chinese Government in consultation with the ECA for continuation after that date.

Preliminary Studies and Proposals

After careful study of special questions involved in setting up the special local currency account in China, and in light of discussions with the Government, the ECA China Mission prepared in September 1948 a tentative proposed program of local currency utilization which outlined in some detail projected uses for the counterpart funds in the fields of conservancy, public works, agriculture, medical and health activities and welfare.

Concurrently, analysis was undertaken of the financial and economic problems in China which needed to be considered in determining the manner in which the counterpart funds would be utilized. These problems included: the extensive deficit spending of the Government, concomitant with the continued prosecution of the civil war; the inflationary effect of the enforcement of the Government's short-lived August 19 economic regulations; the continuation of certain inflationary practices of the Government; the progressive deterioration in economic production; the disruption of transportation in disturbed areas; and the loss of public confidence in the currency resulting in widespread hoarding of supplies and excessively rapid turnover of the currency.

Technical problems requiring study included determination of the exchange rates governing payments of local currency counterpart funds into the Special Account; the timing of deposits; and policies to be followed with regard to the disposition of Special Account funds.

Studies and proposals received from the Mission, in relation to these problems, were further analyzed in Washington prior to consultations with the National Advisory Council.

Establishment of the Special Account

Following these consultations, authorization was given to the ECA China Mission to negotiate with the Chinese Government on questions relating to the establishment of the Special Account, deposits into such account, and purposes for which funds from the account might be utilized.

The Special Account was established in the Central Bank of China. It was agreed that, in order to avoid depreciation of cash balances in the account as a result of the inflation, deposits would be made only as called for by the ECA China Mission, in most cases a short time before withdrawal and expenditure.

Utilization of Counterpart Funds

It was further agreed that withdrawals would be made to cover all mandatory expenditures from the account, as called for in the Bilateral Agreement, including the Chinese currency portion of the following expenses: administrative costs of the ECA China Mission; costs of delivering private relief gift packages in China; and costs of the Joint Commission on Rural Reconstruction. It was estimated that expenditures of these types would amount to roughly 12 percent of the total account.

From the outset, it was clear that "sterilization" of local currency Special Account funds could not of itself be the key to controlling the Chinese inflation. The basic cause of the inflation was the magnitude of the Government's deficit financing, which in turn was due to the exigencies of the civil war and shaken public confidence in the currency which led to excessively rapid rates of circulation of the note issue.

On the other hand, it was apparent that an easy money policy in the use of the Special Account would be inflationary, the effect of such a policy being similar to that of greatly increasing the Government's monthly budget deficit through excessive note issue.

The ECA China Mission, in the light of discussions of this problem with the National Advisory Council in Washington followed, therefore, a policy of agreeing only to expenditures from the account which could be regarded as of demonstrated urgency and which in many cases would have offsetting deflationary benefits. Broad categories of non-mandatory expenditures on which the ECA China Mission could agree with the Chinese Government as being appropriate uses for the Special Account included: emergency expenditures which, at the discretion of the Chief of the ECA China Mission, could be considered as consistent with the objectives of the China Aid Act—expenditures envisaged in this category being for such purposes as emergency procurement of indigenous food for the rationing programs; expenditures on certain carefully screened projects, chiefly in the fields of conservancy, health and welfare; and expenditures, when necessary, to insure prompt installation and proper utilization of capital equipment under the replacement and reconstruction program. The total of these expenditures, it was expected, should amount to less than half of the potential local currency account.

Exchange Rates

A persistent problem with respect to the Special Account has been that of agreeing with the Chinese Government upon appropriate rates at which deposits would

be made in terms of U.S. currency—that is, rates reflecting commensurate value in Chinese currency, at given times, for U.S. dollar aid provided. A rapid decline in the value of the new gold yuan and reluctance of the Chinese Government to negotiate formally on a basis other than official exchange rates led, pending a settlement of this question, to deposits being made as advances, without final agreement before the end of 1948 on commensurate value in terms of U.S. dollars.

Deposits and Withdrawals

As of December 31, 1948, deposits into the Special Account totalled, in round numbers, 157,289,000 gold yuan, equivalent (on the basis of rough tentative estimates prior to agreement on applicable exchange rates) to US\$9,543,000. Withdrawals on the same date totalled, in round numbers, 150,333,000 gold yuan, equivalent, according to similarly tentative estimates, to US\$5,839,000—the equivalent of approximately \$1,342,000 being for ECA administrative expenses in China, \$2,498,000 for administrative expenses of the Chinese Council for United States Aid, \$1,803,000 for special projects, \$53,000 for engineering services, and \$143,000 for expenses incurred by the Joint Commission on Rural Reconstruction.

Before the end of 1948, the local counterpart funds thus jointly managed by ECA and the Chinese Government had enabled many worthy institutions and projects to continue operations in spite of inflation and civil war.

385

Summary of United States Government Economic, Financial, and Military Aid Authorized for China Since 1937

[Washington] March 21, 1949

Since the commencement of hostilities between China and Japan in 1937 the United States Government has authorized aid to China in the form of grants and credits totalling approximately \$1,000 million, of which \$1,423 million has been in the form of grants and \$1,381 million as credits. About 46 percent of the total, or \$515.7 million, was authorized prior to V-J Day to contribute toward the stabilization of China's wartime economy and to enable the Chinese Government to obtain military, agricultural and industrial goods essential to the conduct of the war with Japan.

United States Government grants and credits to China authorized since V-J Day have amounted to approximately \$1,401.7 million, representing forty percent of the total, of which \$1,096.7 million has been as grants and \$305 million as credit terms. This aid was designed to assist the Chinese Government in the reoccupation of liberated areas and the repatriation of Japanese, to meet some of China's urgent relief and rehabilitation needs, and, in the case of the present ECA program, to help retard the rate of economic deterioration in China and to encourage the adoption of effective self-help measures on the part of the Chinese Government. The Chinese Government has elected to use \$125 million authorized by the China Aid Act of 1948 (included in the total of grants above) to purchase items of a military nature.

The totals of United States aid given above do not include sales to the Chinese Government of United States Government military and civilian-type surplus property which have been made since V-J Day, except where these sales were made as credit terms. In such cases, the amount of the credit involved has been included in the total of United States credits authorized. Surplus property