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Office of Current Intelligence

CENTRAL INTELLIGENCE AGENCY.

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## FAR EAST

1. Chinese Communists feel they enter negotiations with strong position:

[redacted] the Chinese Communist Field Commander in Korea, General Peng Teh-huai, advised CCF tactical commanders on 1 July that Chinese delegates to the cease-fire negotiations represent a victorious army, that South Korean demands will be ignored, and that, if negotiations prove unsatisfactory, the CCF will launch their summer offensive. [redacted] on the same date, the logistical commands of the CCF Third and Fourth Field Armies informed General Peng of the movement of 80,000 new "volunteers" from Manchuria to the Korean front. The US Far East Command endorses the 8th Army warning that, should this report be true, no significant concessions can be expected -- at least in the political field. Further, the time gained by the enemy during extended negotiations would permit them to concentrate forces equal to or greater than those employed during the April offensive and to construct and repair forward airfields for close air support.

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2. Chiang Kai-shek expresses his views on Asian situation:

[redacted] Chiang Kai-shek observed privately to the US Charge at Taipei on 30 June that the Chinese Communists in Korea badly needed a respite and quite likely would agree to a cease-fire and armistice. The Chinese Communists will not move into Burma, Chiang stated, because it is a "weak link" that will "break automatically" if Thailand or Indochina falls. Further, any overt move into Burma, he felt, would arouse India. Despite Chinese Communist concentrations near the Indochinese border, he does not expect an early operation there; he concluded, however, that Indochina remains one of the numerous potential targets for aggression that could be exploited on short notice.

Comment: Supported by a large intelligence network, Chiang's observations should be based on the best information

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available. However, Nationalist intelligence reports to US officials regarding Chinese Communist intentions have usually been unreliable. Chiang's departure from the customary Nationalist prediction of imminent Chinese Communist aggression throughout Southeast Asia is of possible significance.

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3. French abruptly delay Vietnamese ECA agreement with the US:

US Minister Heath reported on 28 June that signature of the US-Vietnamese agreement on economic aid, scheduled for 30 June, was cancelled as a result of sudden French insistence that prior approval of the High Council of the French Union must be obtained. Heath, while conceding that the French were acting within legal rights as prescribed by the 8 March 1949 agreement with Vietnam, pointed out that the French were fully aware of US-Vietnamese negotiations and had indicated through the French Economic

Counsellor that the exchange of letters between Bao Dai and Auriol constituted legal approval by the French. He added that the French did not require High Council approval for the agreement on military aid and that the High Council of the French Union is not yet in existence. In summation, Minister Heath characterized the French action as "astonishing" and expressed his inability to explain it.

On 29 June, De Lattre's office released a statement, which the ECA Chief in Indochina described as "amazing," denying French responsibility in this affair, imputing bad faith to US negotiators and intimating that French intervention saved the Vietnamese from a US-laid trap. In reply, Heath drafted an emphatic denial of these French allegations.

On 2 July, the ECA Chief transmitted a report from a reliable American journalist that De Lattre himself had expressly urged Paris to delay the signing of the ECA agreement.

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Comment: On 30 June, Minister Heath cabled a lengthy exposition of the overall situation in Indochina and urged a review of US policy in Indochina looking to the adoption of a more sympathetic attitude toward the French. He stressed the paramount importance of the French military effort and recommended that every effort be made to mollify French suspicions of US actions in Indochina, especially those with regard to ECA. This recommendation was made in the light of a long series of informal criticisms of the ECA program by French officials and the more serious matter of the French veto on signature of the ECA agreement.

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NEAR EAST

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6. No progress in Iraqi oil negotiations:

The Regent of Iraq has expressed his concern to the British Ambassador over the lack of progress in the negotiations with the Iraq Petroleum Company. According to the

Regent, an extraordinary meeting of the Iraqi Cabinet on 30 June concluded that the company was stalling and ended with the Prime Minister offering his resignation and that of his Cabinet. The Prime Minister had previously told the British Ambassador that he felt the IPC was juggling its figures and that its previous offers were possibly unfair.

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The British Ambassador told the Prime Minister that it was the company's impression that Iraq was delaying while awaiting developments in the Iranian situation. He is recommending that the company's negotiator return to Baghdad.

The US Ambassador comments that this development, which comes as a surprise, has no rational explanation; he advises that every effort should be made to reach prompt settlement. He suggests that the Iraq Petroleum Company make an offer before any company negotiator returns to Iraq and that the negotiator should not come until the Iraqi Government has indicated its willingness to discuss the terms of a new offer.

Comment: Orderly negotiations with the Iraq Petroleum Company would be seriously impaired should the present government resign, for such a development would provide an opportunity for pro-nationalization elements to stir up public opinion. It seems possible that if the Iraqi Government does not feel compelled to adopt an uncooperative policy, negotiations will be resumed. The good faith of the company is difficult to estimate, but up to this point it has been anxious to continue with the negotiations, fully aware as it is of the developments in Iran.

#### WESTERN EUROPE

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7. French import plan would bolster rearmament program and appease labor:

The French Cabinet has decided to send a note to the US Government outlining the "exceptional gravity" of the inflationary problem resulting from France's military program and recommending that the problem can be met only by an expansion in the volume of consumer goods. French Finance Minister Petsche, who prepared the note, advises that this expansion can best be accomplished by sharply increasing imports. He argues that these

imports should be financed by US aid and that such aid must be programmed over a relatively long period -- in order to prevent hoarding and to develop the desired confidence among importers, producers and consumers. The note states that France will be unable to fulfill its commitments in Indochina and Western Europe without close cooperation from all NATO countries.

The US Embassy in Paris notes that this French approach for US financial assistance is preferable to the usual French request that the franc counterpart of ECA aid be applied directly to cover budget deficits.

Comment: The inflationary danger in France is accentuated by the prospect that a new government will not come to grips with this problem before late September, and is certain to be too weak to take effective counter-measures. The proposal to curb inflationary pressures by greatly increasing imports of consumer goods was shelved in 1946-47 in favor of a plan for concentrating on long-term investment. The latter plan has had little immediate effect in mitigating the French labor problem.