

Far Eastern Survey

AMERICAN INSTITUTE OF PACIFIC RELATIONS

ECONOMIC AID TO CHINA

BY HARLAN CLEVELAND

EDITORIAL NOTE: *The following article, prepared at the request of the FAR EASTERN SURVEY by Mr. Harlan Cleveland, Director, China Program, Economic Cooperation Administration, describes how the program of economic aid to China, authorized by Congress in 1948, has actually operated under disturbed conditions. It is thus in the nature of a report to the public on a significant aspect of recent American policy, and an aid to understanding of issues now in controversy regarding future American relations with China.*

CHINA, THE MOST POPULOUS country in the world, lends itself to description by superlatives. It is the battleground for the greatest civil war of modern times. Its economy has been subjected to the longest sustained inflation in history. It also ranks as the most sorely troubled of the nineteen countries presently being assisted by the Economic Cooperation Administration.

Since last spring, in the midst of growing turmoil and disintegration, the United States has been helping the Republic of China and its people with various forms of economic assistance under the China Aid Act of 1948. This aid has not halted the civil war or solved the Chinese problem—but this should come as a surprise to no one, since ECA did not set out to work a miracle. The China Aid Program of 1948 has shown that economic aid can be administered and supervised with reasonable effectiveness even under conditions of near-chaos. Learning from the experience of previous aid programs, ECA has rediscovered the truth that nothing in China is easy, but nearly anything is possible.

The China Aid Program submitted to Congress last February was limited in scope. It did not look forward, as did the Marshall Plan in Europe, to the achievement of recovery in a four-year period. It was not presented

as something which by itself would or could reverse the trend of China's civil war. Its terms of reference were presented in President Truman's message to Congress of February 18, 1948.

The continued deterioration of the Chinese economy [said the President] is a source of deep concern to the United States. Ever since the return of General Marshall from China, the problem of assistance to the Chinese has been under continuous study. We have hoped for conditions in China that would make possible the effective and constructive use of American assistance in reconstruction and rehabilitation. Conditions have not developed as we had hoped, and we can only do what is feasible under circumstances as they exist.

We can assist in retarding the current economic deterioration and thus give the Chinese Government a further opportunity to initiate the measures necessary to the establishment of more stable economic conditions. But it is, and has been, clear that only the Chinese Government itself can undertake the vital measures necessary to provide the framework within

JANUARY 12, 1949 VOL. XVIII No. 1

ECONOMIC AID TO CHINA

by Harlan Cleveland

A report on the nature and results of our 1948 contribution toward China's industry, commodity supply, and rural reconstruction.

THE JAPANESE IN BRAZIL

by Emilio Willems

The pressure of social contact and the defeat of Japan are factors in the choice between tradition and assimilation.

THE FUTURE OF JAPANESE SHIPPING

by Daniel Marx, Jr.

Changes in United States policy toward Japan have increased Japan's potential merchant marine.

which efforts toward peace and true economic recovery may be effective.

And again, at the end of the message:

. . . Nothing which this country provides by way of assistance can, even in a small measure, be a substitute for the necessary action that can be taken only by the Chinese Government. Yet this program can accomplish the important purpose of giving the Chinese Government a respite from rapid economic deterioration, during which it can move to establish more stable economic conditions. Without this respite the ability of the Chinese Government to establish such conditions at all, would be doubtful. The achievement of even this limited objective is of such importance as to justify the proposed program of aid.

Original Program Modified

The original program developed by the State Department called for \$570,000,000 over a fifteen-month period for economic aid alone—including \$510 million for commodity-type aid (roughly equivalent to the estimated deficit in China's balance of payments during the fifteen-month period from April 1, 1948 to June 30, 1949) plus \$60 million for reconstruction projects. While the authorization bill was going through, and was being merged with the rest of the foreign aid program in a single bill, the \$570 million figure was cut to \$463 million with the period correspondingly reduced from fifteen to twelve months.

Much of the debate in Congress centered around the provision of military aid. The House of Representatives wanted China included in the Greece-Turkey or "Truman Doctrine" pattern, which might have involved large-scale, supervised military aid. The Senate was less enthusiastic about military aid, and devised the formula finally adopted, which provided funds that could be used for military aid, without giving the Executive Branch much responsibility for supervising their use. In the final version of the Act, \$125 million was provided for "additional aid to China through grants, on such terms as the President may determine." This sum for "additional aid" (i.e., military supplies) was to be deducted from the approved figure for economic aid, thereby reducing the economic assistance still further from \$463 to \$338 million.

Later, when appropriations were being considered, the House Appropriations Committee cut the total of \$463 million to \$400 million (for fifteen months), while maintaining the earmarked \$125 million for "additional aid." This had the effect of reducing economic aid further to \$275 million. As finally passed the appropriation bill provided \$275 million for economic aid and \$125 million for other aid, for twelve months.

The job of administering the \$275,000,000 of economic aid was given to the Economic Cooperation Administration, set up in the same act to handle the European Recovery Program. ECA was to aid China by using the "applicable provisions" of the European legislation.

To get ECA's China operations under way, Administrator Paul G. Hoffman turned to Roger D. Lapham, who had recently completed a four-year term as Mayor of San Francisco, and who agreed to take on the exacting and unpredictable task of representing the Administrator in China as Chief of the ECA Mission there. Roger Lapham was the first ECA Mission Chief to be appointed; he arrived in Shanghai at the beginning of June, only ten weeks after the Act itself had been passed. After reshaping and adding to the China Relief Mission staff, which provided a ready-made nucleus for ECA's operations in China, Mr. Lapham now has about 100 Americans and nearly 400 locally hired staff.

To "backstop" the Mission, pull together the threads of the China Program within ECA, and handle China policy matters generally on the Administrator's staff, a China Program Division was established in ECA's Washington headquarters.

The "Principle of Jointness"

While the financial aspects of China aid follow the same legal form as ERP, the task of "following the dollars" in China involves special techniques. Most important of these is the so-called "principle of jointness," under which each significant decision about the program or its use must be the product of joint agreement between the Chinese and the United States governments (the United States being represented by ECA). The Economic Aid Agreement of July 3, 1948, between China and the United States provided specifically that:

All commodities provided by the Government of the U.S.A. pursuant to this Agreement shall be processed and distributed by commercial enterprises or by private or Chinese Government agencies, and in accordance with terms and conditions, agreed upon from time to time between the Government of the U.S.A. and the Government of China. [Article IV, paragraph 1]

In the same article, the principle of jointness is also applied to "the prices at which supplies furnished by the U.S.A. pursuant to this Agreement shall be sold in China." Another article in effect gives the United States joint control, with the Chinese Government, of the "counterpart fund"—an account made up of funds deposited by China in its own currency, matching the dollar aid granted to China by the United States.

Final passage of the China Aid Act, and its appropriation act, put up to ECA and the Chinese Government the question: how should the funds be used? Some \$70 million out of the total was already earmarked for reconstruction projects and parts for existing capital equipment.¹ The remaining \$204,000,000 (leaving out

¹ The reconstruction program, discussed in detail below, has been suspended for the time being in view of the uncertain military situation, according to an announcement by Paul G. Hoffman in Washington on December 21, 1948.—*Editor's note.*

a little more than a million for administration) was not enough to finance the whole of the deficit in China's international balance of payments, which had been an implied purpose of the original proposal. The estimated deficit was, indeed, nearly twice that figure.

Since China's most obvious economic problem was inflation, there were some who hoped that imported goods bought with ECA's money could soak up enough Chinese currency to make a real difference in the inflationary pressure. A close study of the facts showed that this idea was a lovely mirage.

The magnitude of China's inflation is the result primarily of two factors: the size of the government budget deficit and the state of public confidence. The budget deficit had been running at the rate of US\$600,000,000 a year, or about US\$50,000,000 per month. The US\$20,000,000 which ECA's program might be able to throw on the market monthly, even if sold at realistic prices, would not begin to make up the difference.

Moreover, public confidence has been even more important in recent months than the deficit in determining how rapidly money actually circulates. The waxing and waning of confidence in the market can cause fantastic alterations in the rate of the currency's turnover. Between June and August 1948 the rate of turnover of the currency tripled; while the velocity of circulation is difficult to measure exactly, the entire note issue was probably turning over about once a day in August. In these circumstances, a single military defeat can wipe out the effect of the best-laid plans for resisting inflation by economic or financial means alone.

Since there seemed little point in trying to cover a manhole with a saucepan lid, ECA set out to help the Chinese people and their economy in certain limited ways, the effectiveness of which could be reasonably assured. The entire program of commodity imports—\$204 out of \$275 million—was boiled down to four items: food, cotton, petroleum and fertilizer. By the end of November 1948, about half of this commodity program had been delivered to China, and five-sixths of it had been "authorized," only about \$30,000,000 remaining uncommitted.

Food Distribution

To control distribution of food, under the United States Foreign Relief Program, the China Relief Mission in March 1948 had launched the first general urban rationing scheme in China's history. This ration system was continued and expanded by ECA, with \$70,000,000 earmarked for rice, wheat and flour, destined to reach the 12,000,000 people entitled to ration cards in seven cities—Peiping, Tientsin, Tsingtao, Shanghai, Nanking, Canton, and Swatow.

All the food in the program—rice from Siam, wheat and flour from the United States—has gone to the

rationing organizations in these seven cities. The rationing systems have brought to each person in the city population fifteen catties (16.5 pounds) of flour (in the north) or rice (in central and south China). The rations have been given out each month on the basis of a detailed population census in each of the cities served.

The rationing system has not operated on American food alone. In practice, the United States has supplied about half of the food rationed in 1948. The other half has been provided by the Chinese Government through local purchases or imports of its own. In November, ECA had to move up its deliveries because inflation, civil war and administrative difficulties had prevented the Chinese Government from making the contribution it had originally agreed to make.

Taken all in all, two statements can be made about the food rationing program so far: first, it has been a really major factor in alleviating unrest in China's main urban centers. Second, it has generally delivered food to the people who were supposed to get it. Its relative success in doing this and the relatively small amount of diversion (compared to some previous efforts to distribute food in China), have surprised many a China expert.

Other Commodities

Seventy million dollars worth of United States cotton has been programmed to maintain operations in China's largest industry, and it has been the major factor this fall and winter in keeping textile mills going. The resulting yarn and cloth has been earmarked to barter for food in the countryside, to distribute on the domestic market in the cities, and to earn foreign exchange by exportation, primarily to Southeast Asia.

The ECA Mission in China has set up with the Chinese an elaborate system for following the conversion of raw cotton into yarn and yarn into cloth, and for supervising the allocation and distribution of all products made from ECA-financed cotton. By the end of November, a detailed control and records system—which was worked out with the Chinese Government before a bale of cotton moved into production—still seemed to be bearing up under the strain of actual operations.

Petroleum products were put on the list for \$50,000,000, to revive utilities and transportation and keep the wheels turning in China's major centers. The dwindling coal supply from the Communist-threatened north redoubled the importance of oil for China.

Most of the oil products used in China have been supplied by a few large companies, which not only bring the oil to China, but provide for its distribution in the interior. The continuation of this system enables ECA to use the companies themselves, to a certain extent, to assist in end-use control and reporting.

Fertilizer, programmed at \$13,800,000, completes the short list of basic commodities financed by ECA for China. Used at the proper time, a ton of nitrogen in the form of three to five tons of fertilizer is supposed to increase rice production by fifteen or twenty tons. All the fertilizer bought in 1948 is for use on spring crops in 1949. By the end of November most of the fertilizer had been contracted for, but none had actually arrived, so that an end-use control system had yet to be developed and tested.

The Foreign Assistance Act laid down the general precept that commodities should be furnished under the aid programs through private commercial channels insofar as that is possible. The China Aid Program was born amid dire predictions that it was to be another nail in the coffin of private commercial arrangements with China. But these predictions took no account of the intent of the law which set up the program, or the intentions of the people who were responsible for administering it.

In fact, all commodities financed under the China Aid Program, with the sole exception of food, have reached China through private channels. Government procurement has been limited to rice, wheat and flour. (Even in the case of wheat and flour, plans were laid to introduce private importation, but had to be temporarily abandoned in November because of the need for detailed control of ship movements involving emergency food supplies for major Chinese cities.) Cotton has been bought from private American shippers through American cotton importers in China. Petroleum has reached China, and in this case has even been distributed inside China, by private companies. Fertilizer suppliers have also been private companies. Moreover, the program for industrial project assistance has been set up to make the maximum use of private companies, both for engineering services and for actual purchasing and delivery of industrial equipment.

Industrial Reconstruction

The commodity program was laid out very quickly after the Act was passed, as most of the information needed was already at hand. But in the case of industrial reconstruction, it was impossible to tell from 10,000 miles away what types of industrial development would make the most sense in China's changing circumstances. To figure out the answer to this \$70,000,000 question, and to recommend how this part of the aid program should be administered, a special reconstruction survey group was formed in May, headed by Charles L. Stillman (Vice President and Treasurer of Time, Inc.), and including four engineers, two economists and a lawyer. The survey group, operating as part of Roger Lapham's mission in China, spent two months deciding what projects should be eligible for assistance. Mr.

Stillman spent another three months with ECA's China Mission perfecting and setting up an organization for handling them.

As finally developed, the program placed major emphasis on "replacement" rather than "reconstruction." With China in the midst of an active civil war, long-range reconstruction seemed to require more optimism than it was possible for either Chinese or U.S. industrial specialists to muster. The program finally recommended by the survey group, and approved by the ECA Administrator, included only \$25,000,000 worth of new reconstruction or development, \$35,000,000 for replacement assistance and \$7,500,000 for engineering services and reserves—a total of \$67,500,000. (The other \$2,500,000 was set aside for rural reconstruction.) Most of the projects were for basic industry and transportation—approximately \$17,250,000 being allotted provisionally for power plants, \$11,000,000 for coal mines, \$13,500,000 for railroad rehabilitation, and \$5,500,000 for fertilizer manufacture.

Lack of technical know-how and experience in management has been one of the main problems which every effort to help Chinese industry has encountered. Each dollar's worth of industrial equipment which is sent to China needs a disproportionate amount of technical and managerial help to go along with it. The survey group's findings confirmed this generalization, and developed from it a plan of action. It recommended that each project approved by ECA be required to hire a private engineering firm to help to do the planning, procure the equipment, and get it installed. And to manage the whole scheme, it recommended that the Chinese Government and ECA jointly use a management engineering firm, the J. G. White Engineering Corp., to make sure that this operation was planned and executed by some of the best engineering brains the United States can produce. Engineering services are paid for by ECA under the "technical assistance" clause in the Foreign Assistance Act.

These recommendations were approved by the ECA Administrator. The procedure represents a fresh and encouraging start on a new pattern for publicly financed industrial projects in underdeveloped areas. The problem of grafting branches of Western technology on the great trunk of Asia's agrarian economy is one of the stupendous tasks of this century. The ECA pattern for China has already made its mark as an original approach to a continuing problem.

Rural Reconstruction

"Rural Reconstruction," for which \$2,500,000 was allotted, rated a special section in the China Aid Act. Section 407 spoke of an agreement to be made with the Chinese Government, setting up a Joint Commission on Rural Reconstruction. Two of the five members were

to be Americans, appointed by the President of the United States. Three Chinese would be appointed by the President of China. The Commission would "formulate and carry out a program for reconstruction in rural areas of China."

Many people in the United States have felt that the Communists in China could not be opposed with military force alone: both Secretary Marshall and General Wedemeyer have spoken with vigor on that point. It has long been clear that unless a real effort were made to meet the social problems of China, the upsurge of revolutionary forces would have too strong a justification to be denied. The term "rural reconstruction" covered a broad attack, cooperatively managed by Chinese and Americans, on problems of land reform, agricultural improvement, better health and education, and above all good local government which would govern for the people and not against them.

The general concern for reform in rural areas had been greatly sharpened in the United States by the effective appeals for funds over a period of many years by "Jimmy" Yen's Mass Education Movement, and by a Joint China-United States Agricultural Mission which visited China in 1946 and came back with some comprehensive and far-reaching action proposals.

In the course of the spring and summer, a formal exchange of letters setting up the new Joint Commission was duly signed, and President Truman appointed as the two American members Raymond Moyer of the Department of Agriculture and John Earl Baker, a relief executive, both of whom had lived and worked for many years in China.

Starting in on a job without precedent, these two men and their Chinese colleagues (one of whom is "Jimmy" Yen) have charted some general principles—to improve living conditions, to increase food production, to develop the potential power of the people to reconstruct their own communities, to offer opportunities to participate to liberals, educated youths and other constructive elements, and so on. At the end of November the Commission was hard at work developing a broad program, without knowing just what lay ahead.

The "Counterpart Fund"

Commodities, industrial projects, and rural reconstruction do not end the list of China program headaches. ECA has been occupied daily with knotty questions about the "counterpart fund," the special account in Chinese currency set up under the Economic Aid Agreement of July 3.

It was especially important in China's case that such a fund be created. The operations of UNRRA, for example, had been crippled by lack of Chinese funds to meet the gigantic internal costs of distributing supplies and installing equipment throughout China. But

it was obviously not sensible to deposit money in an account when that money might shrink away to nothing in a matter of days because of the general depreciation of the currency. An ingenious system was therefore devised to protect the account against inflation.

The Economic Aid Agreement established the principle that deposits would be made in the account only when requested by the United States—with the idea that deposits would be made only to cover actual expenses that had to be met currently, leaving no large balances to wither on the vine. If this had not been done, the deposits made against the first \$20 million worth of ECA goods shipped would by now have depreciated to the equivalent of less than half a million dollars.

The two governments also agreed that allotments made from the account for certain particularly important purposes—such as administrative costs, rural reconstruction, and the internal costs of industrial projects—would be "maintained in value," in terms of some standard measure of value like cotton yarn, rice or American dollars.

The problem of how much to spend out of this account, and when to spend it, can be solved only from day to day by weighing the benefit of spending on particular projects against the danger of adding still further to inflationary pressures. Knowing that the local currency in the account was not going to kill the inflation single-handed, ECA has tried to make sure that a few dozen well supervised projects, ranging from refugee feeding through hospital repair work to major dyke-building jobs, get the financial support they need in Chinese currency. The local funds managed by ECA and its predecessor, the China Relief Mission, have enabled many a worthy institution to carry on in spite of inflation and civil war.

Evaluating the ECA Dollar

In the economic aid program as far as it has gone, there have been certain elementary benefits attributable to the ECA dollar. People and institutions that needed help have been getting it. Even at the halfway mark of this one-year program, it had contributed within limits to stability of urban conditions in a manner difficult to measure but easy to see—especially on the score of food supply and textile production.

But an aid program can have at best only a marginal effect on the situation within China. Military disintegration and political disaffection proceeded so rapidly during the second half of 1948 that perfect performance on the economic front probably could not have made a substantial difference in the outcome at Mukden or Hsuechow. And in spite of a reasonably successful start on the aid program, the overall economic front has been deteriorating more and more rapidly.

The military advance of the Communists during the autumn months, plus the failure of the August 19 currency reform measures, presented ECA with a set of conditions different from those which were considerably existing at the time Congress passed the China Aid Act in April 1948.

During November the critical shortage of vital supplies in the cities, particularly of food, produced some vigorous action by Roger Lapham and the whole ECA organization to move up shipping schedules and pick up urban ration commitments with United States-financed food in December, rather than depending on indigenous Chinese food until January, which had been the original plan. ECA borrowed rice from the British colony of Hongkong, arranged to divert to China a

couple of Army flour ships, and bought coal from Japan to make up in part for dwindling supplies from the Communist-threatened Kailan mines in North China. The whole program was placed on an emergency footing; while the longer-range industrial program continued to make plans and do preliminary engineering work, no equipment had been purchased.

As this is written, ECA's China Program generally is in process of change to meet the new conditions, without any clairvoyant knowledge of what the future will bring. But the people helped by American aid this year, and the techniques developed to make sure that the aid is used properly, will both outlast the one-year Act which ECA is administering in China. Both may play an important part in whatever happens next.

THE JAPANESE IN BRAZIL

BY EMILIO WILLEMS

THE STATE OF SAO PAULO, which absorbed nearly all the Japanese immigrants to Brazil, had received by 1940 a total of 186,769 Japanese. The remarkable fact that more than 100,000 of these arrived after 1930, their departure from Japan coinciding with the seizure of political control of their homeland by a group of radical nationalists, adds significance to the history of their settlement and the extent of their assimilation in the New World.

The Japanese in Sao Paulo numbered only a few hundred before 1909, but by 1914 the total had risen to 14,465. Their colonization during and since that time may be divided roughly into three areas: the Ribeira Valley near the southern coast, the central area near the state capital, and several new or frontier regions in the interior of the state. The Ribeira Valley consists of well-watered lowlands suitable for rice, banana, and sugar-cane cultivation. The first twenty years of Japanese settlement in this area, however, was made difficult by great distances and a lack of adequate roads. The Japanese introduced Chinese tea in the face of competition from the better-known English tea. When English tea imports ceased during the last war, Ribeira Valley tea conquered the market and was exported on a large scale. At the present time tea constitutes the most important crop of the area. Within the two municipios where the Japanese have established themselves there are districts in which Japanese outnumber Brazilians; but these two municipios in 1939 had only 4,516 inhabitants born in Japan out of a total population of 51,703.

The center of the second area of Japanese coloniza-

tion is Mogi das Cruzes, a middle-sized town on the railroad line between Rio de Janeiro and Sao Paulo. There the Japanese established themselves mainly after World War I. The soil in this area has been in use for at least two centuries, and when the Japanese arrived cultivation had been almost abandoned; but the demands of the growing state capital nearby made profitable the raising of vegetable crops even from poor soil. The Japanese were among the first to realize this opportunity. Settlement has been aided by cheap land and easy communication. In this area too the Japanese constitute only a small minority, although by 1934, when they numbered 1,683 out of a total population of 42,783, there were already many second-generation Japanese.

By far the most important of the three areas of Japanese settlement is that which consists of new or frontier regions, the soil of which has been brought under cultivation within the last twenty-five years and in part much more recently. There are five such regions, named for the great railway companies which were the main factors of penetration and land utilization: Mogiana, Araquarense, Noroeste, Alta Paulista, and Alta Sorocabana. The coincidence of Japanese immigration with the opening of such new regions has an important bearing on the character of Japanese settlement there. The trend has been described as follows:¹

In the western parts of Sao Paulo tremendous and rapid advance is being made in the carving out of the forests new farms, in establishing thriving towns and cities based on trade, and in creating new municipios. These newly opened areas are rapidly becoming the centers of production of such staple commercial crops as cotton, coffee, and tobacco. Interestingly

1 T. Lynn Smith, *Brazil, People and Institutions*, New York, 1946, p. 578.

Dr. Willems is a member of the faculty of the University of Sao Paulo and of the Escola Livre de Sociologia e Política.