

ECONOMY OF CHINA

29 March 1955

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Dr. Alexander Eckstein, Research Associate, Russian Research Center, Harvard University, was born 9 December 1915 in Yugoslavia. He came to the United States in 1936, attended the University of California, and received his B.S., in 1939, and his M.S. and Ph.D. in agricultural economics in 1941 and 1952, respectively. He also did graduate work in International Economic Relations at the Graduate Institute of International Studies, Geneva, Switzerland, from 1949 to 1950. Dr. Eckstein was in the Military Intelligence Service of the Army, 1943-46. He began his civilian career as an economist with the Food and Agriculture Organization of the United Nations. Subsequently, during 1949 and 1950 in Geneva, Switzerland, he worked as a Social Science Research Council Fellow on his doctoral dissertation on The Economic Development of Hungary, 1920-1950, and for four months as a consultant to the United Nations Economic Commission for Europe, coauthoring the chapter of the Economic Survey of Europe in 1949. As International Trade and Development economist in the Department of State, Division of Research for the Far East, June 1951-September 1953, he supervised work on fiscal, trade, industrial, and land reform policies in the China area and headed a small research team in Hong Kong, Formosa, and Japan for three and one half months. Since assuming his present post at Harvard, Dr. Eckstein has been doing research on the conditions and prospects for economic growth in Communist China and is currently working on a book on the national product of Communist China. Dr. Eckstein is one of the authors of The Prospects for Communist China published in New York, 1954, by Wiley and Sons; author of "National Income and Capital Formation in Hungary, 1900-1950" of the forthcoming Income and Wealth, Series V; and a contributor of articles of the Journal of Farm Economics, and Journal for Economic Development and Cultural Change, and World Politics. This is his first lecture at the Industrial College.

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COLONEL WIRAK: General Niblo, ladies and gentlemen: The lecture this morning is on the "Economy of China." This is a timely topic. Only last month Mr. Mao clarified what would happen to the imperialistic aggressor who stands in the way of Formosa's liberation. He threatened that the People's Republic of China would "sweep them clean from the surface of the earth."

With this threat in mind, the subject today is more than academic interest. To help you gain an insight on Communist China's real strength and something of its potential for war, we looked for and found an expert on China. He is associated with the Russian Research Center at Harvard University and is well-known to Washington people who specialize on China.

It is a pleasure to welcome to this platform and to present to you Dr. Alexander Eckstein.

DR. ECKSTEIN: Thank you, Colonel Wirak. The country we are dealing with here today is one which is much more backward and underdeveloped than those you have been discussing in your earlier lectures. It is also an area about which we have much less statistical and other types of economic information.

It is a country of roughly the same size as the United States. However, its per capita product, the output per person in the whole economy, is only about 50 dollars as compared to close to 2,300 dollars in the United States. So you can see there is a tremendous gap in the standard of living and in the per capita product of China as compared to the United States. This comparison tends to exaggerate the difference, but it does give you some idea of the magnitudes involved.

About 85 percent of the Chinese population is rural as compared to about 15 percent in the United States. This very backwardness creates some special problems for the researcher looking at China. One could say that doing economic research on China is a job of economic archaeology--you pick, you dig, you try to fit small pieces together. It is something like crossword puzzle research.

The problem one faces is to some extent paradoxical. Before the war, statistics in China had been notoriously bad. However, we had access to the data. There was no bamboo and no iron curtain. We could get all the data that there were. Now statistics are much better than before, although they are still very poor. However, we have no access to them. So we are worse off than we were before.

Before I proceed, I would like to raise a question that comes up all the time: Can you believe Chinese Communist statistics? Can you believe Chinese Communist economic data? This problem also arises with the Soviet Union, but it arises even more pertinently in connection with China.

I can only express my own personal opinion, based on my own research, but I must say that I am thoroughly convinced that the Communists do not keep two sets of books--one for external consumption and one for internal use. The problem is not one of outright falsification of data, but rather one of distortion, of omissions, and of presenting the data in the most favorable light possible from their point of view.

So the job of the investigator is to try to get below this maze and camouflage to discover the concepts and the framework in which economic and statistical data are presented. If one does this type of study, I think one usually finds there is some kernel, some grain of truth, and some system in the presentation of the data. A rather clear-cut illustration of this may be provided by the Soviet experience:

As you may have perhaps heard, the 1941 Soviet Plan was captured when our Army came to Germany. In capturing some of the German units, we found the 1941 Soviet Plan in complete detail, which the Germans had captured from the Russians. The Russians, previous to that, during the war, gave out various types of information--very sparse, very incomplete--concerning plan and performance in 1941 and the few preceding years.

Upon close study it turned out that there was nothing in this plan which was in any way inconsistent with the published data and there was nothing that the Soviets had published which was inconsistent with what was in the plan.

This is not really proof so far as the Chinese experience is concerned; but, since the Chinese do follow the Soviet model,

particularly in economic statistics and planning, this tends to support the belief that the Russians' data have some basis in fact, and that the problem really is one of trying to discover the framework within which they are presented.

What does the national budget mean in Communist China? What does the term investment mean, and so on. These are the types of problems that an investigator is confronted with.

What I would like to do after these few very brief introductory remarks is to discuss some of the major facets of the economy inherited by the Chinese Communists, then, to proceed with an analysis of the limiting and conditioning factors in Communist China's economic development, which is in a sense the problem I should think you would be most interested in from the standpoint of economic potential.

The fundamental fact about China today is that it is unified. For better or for worse, whether we like it or not, for the first time since 1911 certainly, it is under one government, under one administrative center. This has far-reaching economic implications: it means that the transport system-- what there is--is operating under one central direction. It means that trade within the country can flow from different regions. There are no very marked internal barriers to the flow of trade as there have been in the past, due to the civil war, due to Japanese occupation of Manchuria and later also of North and East China.

Another fundamental fact about China, both now and in the past, is the very heavy population pressure. You have a country with a tremendous density of population and with a population which is undoubtedly increasing rapidly.

One illustration of the degree of population pressure is the size of farms. The average size farm in China is estimated to be slightly above three acres, and of course this is an average size, which means that you have many, many farms much smaller than that. This is compared to an average sized farm in the United States of about 80 or 85 acres, I believe.

This comparison, just as the national income comparison exaggerates the difference somewhat since the Chinese have a much more intensive type of agriculture, and in vast areas they produce two crops a year. So an acre in China is not equivalent to an acre

in the United States. But even if you halved the difference, even if you said the average in the United States was 40 or 30 acres, there still would be a very vast difference.

Agriculturally, China is divided very roughly into two regions-- the wheat region in the north and the rice region in the south. The density of population is much greater in the rice region than it is farther up north. Other crops are grown, too, but this is a very distinctive characteristic of the country.

The crop yields, that is, agricultural output per unit of land, are quite high. They are probably as high as application of traditional techniques permit. The Chinese have through the centuries developed highly refined techniques of cultivation, of soil conservation, of fertilization with the means that were at their disposal, not using modern techniques. An appreciable increase in current production can only come with a major technological breakthrough, through the utilization of new techniques particularly the application of fertilizer as was done in Japan in the late nineteenth century.

Now some very brief notes on the industry of China, which is I am sure, something of very considerable interest to you. The large industrial center of China is Manchuria. You really have two major industrial centers and then some subsidiary ones. The major centers are Manchuria on the one hand and the Shanghai area on the other hand. Manchuria, broadly speaking, is the center of heavy industry, developed by the Japanese. Shanghai is the center of light industry, particularly textiles.

When you speak of the center of heavy industry, we have to bear in mind that the scale here is very different from that in the United States. The industries that I am referring to in Manchuria are iron and steel, power, cement, some coal; there is a sizable coal industry in China proper, too. To illustrate this, in terms of past peak performance, the production of pig iron was about 2 million tons; of steel, close to 1 million tons; of coal, 60 million tons; and of electric power, about 7 billion kilowatt hours.

At the same time, the transport system is extremely modest and is largely confined to Manchuria and East China. It is very sparse in the South. The total mileage--again before the Communists came in-- was roughly about 15,000 as compared to about 250,000 in the United States.

This was, in very broad brushes, the economy that the Chinese Communists took over when they came into power, with a number of exceptions.

First of all, Manchurian industry was dismantled by the Soviets in 1945. This was reflected in a marked reduction of industrial capacity. The degree of curtailment varied from industry to industry. This stripping of industrial facilities was selective; it did not necessarily involve complete removal, but rather removal of the most modern equipment as a result, according to estimates made by our Pauley Reparations Mission, productive capacity in overall average terms was at least halved.

Another major problem facing the Chinese Communists at the time of takeover was the highly disrupted state of the economy. It was an economy which was just at the end of a long period of civil war, a period of extended and very acute inflation, with its production machinery at a very low ebb, and with a completely disrupted transport and distribution system.

So one of the major problems they faced was one of unification and control, trying to gain control over this economy and of combating the inflationary pressures.

In this situation, Mao Tse-tung in 1950 proclaimed certain general goals for the three-year period 1949-52. There was to be recovery in production to past peaks, and these peaks in Communist terminology usually refer to 1943-44 output in Manchuria, the highest on record, and to 1936-37 output in China proper.

The second objective was what you might call the capture of the "commanding heights" in the economy, gaining control over the economy, bringing various sectors of the economy under Chinese Communist control.

The third objective was to attain fiscal and financial stability, to combat inflation, to arrest the continuous price rise and the deterioration of the currency and to bring about a fairly stable price level.

The fourth objective, which in a sense was not an objective of itself, but was a consequence of the first three, was the preparation of the five-year plan and of the economy for long-range development planning that was to start probably in 1953. This is not spelled out,

but the implication was that it would start at the end of this period. On the whole, all of these objectives were attained by 1952, in spite of the Korean War.

The Korean War in a sense worked in two contradictory ways so far as the Chinese economy was concerned. It was a drain on the Communist Chinese economic resources despite the Soviet military aid that was extended. It was a tremendous drain on the transport system. Also, despite Soviet shipments of materiel, a large portion of the supplies had to be provided from Manchuria and Communist China. So there is no question but that it was a very serious economic drain.

On the other hand, it did serve to arouse, at least at the beginning, at least during the period when the Chinese Communists were doing relatively well, the latent or not so latent nationalism of the Chinese people, the suppressed feeling of revenge against past western injustices. This helped the Chinese Communists to mobilize national sentiment and to increase the degree of exertion they could command from the people. It aroused a certain fervor, enthusiasm, and so on, which were important factors in helping the Chinese Communists to extend their controls and to capture the commanding heights.

Now let us briefly examine each one of these factors that I have mentioned. In general terms the Chinese Communist policy during this period, and even now, may be characterized as a policy of "high pressure gradualism," to gaining more and more control, trying to use all means at their disposal, short of outright mass coercion or mass murder; although there have been a number of exceptions to this, such as in 1951 when a vast number of people, estimated at 2 or 3 million, were killed.

This strategy can be clearly detected in agricultural policy, in the field of land reform, and in the nationalization of the urban sectors of the economy.

When the Chinese Communists came in, they instituted a very far-reaching land reform. They transferred titles from landlords to tenants, and also a vast amount of land was redistributed. However, from the Communist point of view, this represented only a way-station. The primary purpose of land reform was to help the Chinese Communists to gain access to power and gain the peasants' good will. Having

gained power, they eliminated the landlords in order to gain control of the villages, and to acquire the capital accumulating functions formerly exercised by them. In effect, through this act rents once paid to the landlords were now appropriated by the state in the form of taxes.

This land reform, however, was just the first stage of a three-stage agrarian policy whose ultimate goal was collectivization. The three stages, spelled out by the Communists themselves, were land reform, the cooperative stage, and the collective stage. At the present time they are in the second stage, the cooperative stage. Land reform was completed roughly in 1952. However, even before it was completed, the second stage was launched.

A similar program is pursued for the nationalization and control of the urban sector. The Communists inherited many public enterprises from the national government. Practically all the Manchurian industry was state operated and controlled before the Chinese Communists came in. Since it had been under Japanese ownership and management at the end of the war, it naturally became war booty and thus automatically came into the possession of the national government of China. Moreover, the national government had operated public enterprises in China proper as well. Thus the Communists had a large state-operated industrial sector to start with.

Similarly, the largest banks in China had been either under public or semipublic control. Therefore, it was not very difficult to penetrate the banking system, to control it, and to gain access to it.

The Communists, using these strategic positions, gradually extended them, not by outright nationalization but rather by buying up private enterprises, by forcing banks to amalgamate, by forming corporations in which the government purchases a portion of shares; then one or two representatives of the government would sit on the Board of Directors, which would be enough because the word of the representative, the views of the representative, the policy he advocated would be the one that had to be followed.

These were the means that have been used and are still being used. By now about 80 percent of heavy industry in China is under public or government control, so is the bulk of wholesale trade, and an increasing share of light industry and retail trade. The sectors which are still privately operated begin to be

subjected to increasing pressures in the past half year through the device of so-called joint public-private enterprises. In Chinese Communist terminology, these enterprises constitute the state-capitalist sector. These are enterprises in which the state has bought a proportion of the shares--maybe half, maybe somewhat less, maybe somewhat more--and which are supposed to be jointly managed by private entrepreneurs and the state, in terms of direction, control and planning, but for all practical purposes are really public enterprises.

Our time is so short, I will have to skip over things very lightly. Now I am going to attempt to discuss briefly the factors conditioning economic growth in Communist China. Before I do that, however, I would like to say a few words about the five-year plan. In early 1952 and 1953, the regime said it was launching a five-year plan. They did not publish a plan, only certain targets for 1953; also, Soviet newspapers published certain long-range targets for the five- or seven-year period, 1952-59, for a few major items, such as pig iron, steel, coal, electric power, and a few other commodities, the output targets of which were to be attained through Soviet aid.

Also we were told that it was the objective of the five-year plan to rehabilitate and to build a vast number of new enterprises and new projects mostly in heavy industry. We were also told that grain production was to be increased by 30 percent. Late in 1954 Chou En-lai, in his important speech before the People's Congress stated in so many words that there really was no five-year plan in the real sense of the word in China, but that the Chinese are still operating within a framework of general five-year objectives. He didn't spell this out, but the implication was that there were only annual plans rather than a five-year plan of the Soviet type.

In connection with the five-year plan, the Communists in many different statements as well as articles have spelled out the type of economic program which they envision for China. It is a program which is closely patterned on the Soviet model. The central objective is industrialization, most particularly the rapid growth of heavy industry. This can be illustrated by the fact that about 50 percent of the investment budget goes into industry. Of this 50 percent, about 80 percent goes into heavy industry and 20 percent into light industry. So the preponderant emphasis is on heavy industry. It receives the highest priorities, with lower priorities accorded to agriculture and to the consumer sector.

There is the hope that, in spite of the low investment priority accorded to agriculture, farm output can be raised. Reliance for this is principally placed on a series of labor-intensive projects involving particularly irrigation, drainage, and reclamation along the big river basins of China; an outstanding example is the Hwai River flood control and irrigation project.

While these projects may turn out to be fairly important in the long run, in and of themselves they are not sufficient to make a very marked impact on the agricultural output of China. The principal problem, as I indicated before, is fertilizer. This requires a large expansion of fertilizer production capacity or larger imports of fertilizer. Both mean sacrificing other objectives. Expansion of domestic fertilizer output means division of capacity from other lines of production. On the other hand, larger imports of fertilizer mean smaller imports of capital goods. Actually, there has been some expansion of domestic fertilizer capacity, but thus far, it has been quite modest.

In essence the Chinese Communists envisage industrial development at the expense of agricultural development. Industrialization is accelerated at the outset, by virtue of the very fact that since agriculture is kept on a short investment ration, a larger share of investment resources can be concentrated in industry. This policy, in turn, sets up its own vicious circles; just because agricultural development is sluggish, while the demand for farm products grows--owing to an increasing population, urbanization, and exports--the regime is forced to extract a rising proportion of farm output if this demand is to be met. This very process, however, further interferes with agricultural development so that the screw must be applied even tighter; and under such circumstances farm output is sacrificed for control and strong compulsions are set in force that drive the system toward collectivization.

Let us briefly look at the factors limiting the pace of economic and industrial growth. In a sense, they are obvious: the problem of mineral resources; the problem of population; the problem of organizational, managerial, and technical skill; the capacity to save or the capacity to invest; the capacity to import; and the problem of transport. I would like first to discuss transport very briefly. A railroad map of China will show the lines which were built before the Communists came in and which were taken over by them.

There is a relatively heavy concentration in Manchuria and in North China; very sparse in South China; and nothing in West China.

The Chinese Communists' efforts are concentrated in West China where there have been no railroad lines in the past. In many ways, from a strictly economic viewpoint, this is illogical. The population center of China, as I indicated before, is in the South. Thus it seems to me it would make much more sense to develop the railroad system in South China, to build many more spur lines, so as to tap more effectively the agricultural surpluses in this region and also to promote a much better commercial interchange in this region. However, the Chinese Communists are concentrating their efforts in West China. Why?

One can advance several hypotheses. It seems to me this is primarily for strategic and domestic political reasons. It is an attempt to integrate West China more closely with the rest of the country and to establish closer contact with Russia by building these two lines up to Alma-Ata and up through here into Outer Mongolia, up to Ulan Bator. This may also make sense from a long-range development point of view because this is where the unsettled, unexplored regions of China lie. They are agriculturally very poor regions, but it is perfectly conceivable that new mineral resources may be discovered there and that certain parts of this whole vast area may very well be conducive or suitable for industrial development, particularly for mineral exploitation in Northwest China. So from a very long-run development point of view, this makes sense; from a short-run development point of view, it is primarily to be regarded in political and strategic terms.

So far as population is concerned, I would just like to make a few observations. Population constitutes a very obscure chapter in Chinese history and in our knowledge of China. We know less about Chinese population, paradoxically enough, than about many other aspects of Chinese society and economic life. We don't know what past rates of population growth have been. There have been some local studies. We have some guesses as to what the birth and death rates have been, but we have no reliable data whatsoever.

The first modern population census in Chinese history was taken in 1953 by the Chinese Communists. They have released some data, but we still don't have a very clear picture of what the rate of population growth is. We do know, however, one thing, the death rates are rapidly declining. This is inevitable, given the fact that

the country is unified, that for the first time in decades there is no civil war.

Under a very ruthless administration, epidemics and famines have been reduced. The scope of the internal distribution system is greatly improved so the effects of famine can be minimized. I am not suggesting that there are no local famines in China today, but only that the government has the capacity to minimize the effects of famine much more than was the case in the past. Also the Chinese Communist government is engaged in a very vigorous program of public health.

It also seems to believe in promoting population growth. However, regardless of this China may, within the next decade or two, be subject to what demographers have characterized as a "population explosion"; that is, a situation brought about by a rapid decline in the death rate with birthrates remaining stable or declining much more slowly. While death rates can be reduced quite quickly with our modern techniques, with the great advances in medicine and public health, birthrates are subject to strong cultural and social resistances. If anything, this phenomenon of population explosion is probably much more acute and pronounced in the twentieth century than in the nineteenth century because the means of reducing deaths is so much more advanced.

This phenomena is not unique to China. It takes place in all the underdeveloped areas. India is facing the problem just as is China.

I notice my time is up. There are many things I have not covered, but I hope I will be able to catch up on them in the question period.

COLONEL WIRAK: Dr. Eckstein is ready for your questions.

DR. ECKSTEIN: One of the things I did not cover is the fact that according to the 1953 Chinese Communist census, the country's population is 582 million.

QUESTION: Doctor, would you give us a little comment on what the language problems are that the Red Chinese face--those that have been with China for so long?

DR. ECKSTEIN: There are two major dialects. There are many dialects, but there are two predominant ones--Mandarin and Cantonese--almost two languages rather than dialects. However, the dominant language, the national language, is Mandarin and is becoming so more and more, certainly among the educated group. Most of the educated people speak Mandarin or understand it.

I doubt that this would be a very major problem. Certainly it is something of a problem. One could broaden this question somewhat and generally raise the question of the north versus the south. There is a considerable cultural gap between the northern Chinese and the southern Chinese, and also a certain degree of historical animosity.

Generally, the north is much more firmly under Communist control than the south. The south is the region which was invaded and captured last. It is a region which is more or less neglected by the Communists, probably deliberately. There is relatively little industrial development in the south.

I don't know that the language problem itself would be very serious. It is something of a problem, but I don't think it would be very acute.

QUESTION: I was thinking more of the fact that the level of education is very low. The written word is pretty much out of the question, north and south, and it would seem to me that getting the printed matter over to uneducated people would slow it down a lot.

DR. ECKSTEIN: I think that may very well be.

QUESTION: I infer from your talk that the major source of capital for industrial expansion in China is agriculture. Is that true, and, if not, where will the Chinese get capital and what is the possibility of their getting it?

DR. ECKSTEIN: That is one of the questions that was lost in the time shortage. I am very happy you raise it. The rate of investment or rate of savings in China by underdeveloped standards, to the extent that we can establish it with limited data, is quite high. It is roughly 12 percent or more of the national income as compared, let us say, with India, where it is 7 to 8 percent, and in other countries where it is lower. What it was in the past, we don't know, except that it was probably much lower.

Most of this capital is mobilized through the government budget in two principal ways: through agricultural taxation and through the price system. Since most of the trade, both wholesale and retail, is under state control, the state is in a highly monopolistic position, as both a buyer and a seller. Therefore, the state is in a position to pursue a policy where it can buy "cheap" and sell "dear."

So, through this process of setting relatively high trading margins, they in effect get another quasi tax, on both agricultural and nonagricultural products. The burden of this quasi tax is borne by the population at large, since it affects the prices in the whole economy. But agriculture represents such a large portion of the total that it naturally bears a large share of the burden.

I would say that the two principal ways of saving in the Chinese economy are through agricultural taxation and through the price system, through establishing the kind of price relations which I have indicated.

These savings are translated into investment again in two principal ways: One is through projects which can be carried out with domestically produced investment goods or through labor which is domestically available. Another aspect, a very important one, is imports. About 20 percent of total investments consist of imported capital goods; That is the import component of investment is roughly 20 percent. This 20 percent is very strategic and important, because without it the bulk of total investment activity would be seriously impaired. These imports are made up of the kind of capital goods which cannot be produced in China and without which industrialization in China would not be possible.

The bulk of the capital goods is imported from the Soviet Union. This raises the next question as to under what terms and conditions is this trade carried on. This is an area in which our knowledge is highly imperfect. Undoubtedly, there is some Soviet aid that is apart from imports that are financed by exports. This aid is in the form of long-term lending and possibly also some outright grants.

What the extent of this is, we don't know. We thought we knew until about a year or two ago. A series of Soviet-Chinese agreements were concluded in 1950 which provided for a loan of 300 million dollars from Russia to China over a five-year period with annual installments of 60 million dollars. But since then, there have been new agreements which may have superseded or supplemented the earlier one. Therefore we don't know what the present

level of Soviet aid is. My own personal opinion would be that it is appreciably higher than the 60 million dollars previously committed. I would support this opinion, partly hypothetically, by the thought that the nature of the Sino-Soviet relationship since 1950 has been gradually changing, with the rise in Chinese power. In 1950 they were very junior. They are much more senior now.

I think it is logical to assume that in a power relationship such as this where the partners are becoming more and more equal, the Chinese are in a better position to bargain and to demand a higher level of aid. There are some definite bits of evidence which would tend to support this conclusion. If I had to make a guess, I would say that the present level of Soviet aid is somewhere between 100 and 150 million dollars a year.

QUESTION: I am interested in your comments relative to the rate of expansion, not of the rail lines, but other types of transport at the same time you are trying to maintain a war potential in these respects?

DR. ECKSTEIN: You mean in addition to railroads what other means of transport are being expanded?

QUESTION: What I mean is the tremendous effort of heavy industry that must be put into the rail system outlined at the same time that they have to maintain highways; also some type of ocean shipping. At the same time they must also maintain some sort of war potential, drawing on these for support of a war effort. Can you comment on that?

I should have referred perhaps also to the iron and steel production which goes into the materials for ships and trucks.

DR. ECKSTEIN: Your question was whether really there are the basic products which make it possible to maintain and carry on this type of program? Well, only partially so. There the dependence upon imports is quite considerable. Great emphasis is being placed upon expanding steel capacity. That is one of the prime objectives. Steel capacity, as I indicated, was greatly dismantled when the Chinese Communists took over. At its peak, Manchuria's steel producing capacity was 1 million tons; the Chinese Communists claim that now it is around 2 million tons. The objective set for the end of the five-year plan--I forgot now the figure--I think it is to be somewhere

around 4 million tons. So you see there was a very rapid rate of expansion in steel. However, the dependence on the Soviet Union is still quite considerable.

QUESTION: Doctor, do the Communist Chinese want to trade with the non-Communist countries in the Far East and with the Western Powers, and do you think it would be possible to work out terms advantageous to the Western Powers and the other non-Communist peoples?

DR. ECKSTEIN: I think the Chinese Communists would definitely be interested in trading with the West, particularly with Japan, but also with other non-Communist countries. I think they would be willing to trade without any special arrangements, that is at world-trade prices, because such trade, after all, would be to their advantage. It would open other sources of capital imports, other than the Soviet Union, and thus make them somewhat less dependent on the Soviet Union. Therefore, it would, in effect, increase the bargaining relationship with the Soviet Union and it would give them access to a much wider choice in the range of products that they could import.

So I think from every point of view--of course there are propaganda elements in it--they would be interested, and I think they really mean it when they clamor for the lifting of strategic trade controls. Trade with the Soviet Union would continue to be high as long as China is controlled by Communists, but the relative proportion, I think would be reduced. Instead of perhaps 50 or 70 percent of the total trade being carried on with the Soviet bloc, venturing a guess, it might possibly be 25 percent.

I think the problem is much more on our side. Are we willing to lift strategic trade controls and what is our judgment as to the relative gains, both strategic and economic, versus the relative losses if we do lift them. I would say the problem is more on our side than on their side in this particular respect.

QUESTION: Doctor, you mentioned as one of the Communists' points--control of inflation that they inherited from the nationalist government. Have they been successful in doing that?

DR. ECKSTEIN: Yes, I think one can in all fairness say very much so. Very briefly, in 1950, which was really the first full

year of Communist control, inflation was still quite rampant, particularly in the early part of the year. Then in March 1950 they instituted a series of stabilization measures, unifying fiscal management, that is unifying provincial and regional budgets and unifying the tax administration in the country, which enabled them to increase revenues; they also introduced quite drastic economies in government expenditures, thereby practically balancing the budget in 1950.

In addition to this, they instituted a series of price controls which were more indirect than direct, that is, price controls through state trading rather than OPS type of measures. They engaged in a series of what you might call open-market operations by which the trading organizations brought up large quantities of agricultural and other consumer supplies and then released them, or dumped them if you like, on the market as a means of countering inflation. These goods would be released at such times and in such places where inflationary pressures were particularly strong.

This stabilization had been effected, through price manipulation, increasing revenue collections and also through institution of a bond issue which was another means of capturing liquid funds in the economy. Once this stabilization had been attained, there was still some price fluctuation in 1950, but by 1951 a fair degree of price stability was attained with what you might characterize as chronic suppressed inflation. By that I mean that there is a very grave imbalance between the stream of money income and the stream of goods and services being brought to the market for consumption. There is an imbalance between the value of consumer goods and services produced and the stream of money income.

This is due to the fact that such a large proportion of the effort is concentrated in heavy industry, which doesn't produce consumer goods but generates money income. So, as a result of this, you have this tremendous pressure of money against goods, which is one of the prime sources of inflation.

However, the regime is sufficiently in control of the situation to be able to sit on this lid partly with direct controls and rationing which was instituted last year and partly through its control of state organizations which exercise virtually monopolistic market power.

COLONEL WIRAK: Doctor, I know there will be a great many more questions in the seminar this afternoon. On behalf of the Commandant and the audience, I thank you for a well-informed talk.

(12 May 1955--250) S/mmg