

Submitted by V. NICHOLSON for the week ending MARCH 30, 1939
 Date MARCH 30, 1939

For the Information of Officers of the Bureau only, and not to be Published under any Circumstances

BUREAU OF FOREIGN AND DOMESTIC COMMERCE
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Post Shanghai, China Date March 30, 1939
 Submitted by A. Bland Calder, for the week ending April 1, 1939
Acting Commercial Attache.

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WEEKLY ECONOMIC REPORT

Japan has been acquiring, since September, 1937, a vast area of territory (6 million square miles) with attractive basic resources

The World Boils and Stews: Central and Eastern Europe, despite some continuance of Slovak-Hungarian clashes, seem to be calming down from the last Hitlerian "Drang" which for a time appeared to have as its slogan - "A Country A Day". The world, including China, has hung breathless awaiting the Mussolini utterances. That hurdle is now passed and nothing especially new has come out of it -- just announcement of more and more armament by Italy, -- no immediate harsh demands on France though "expectancy" for some "appeasement" from that quarter is apparent. China watches this European kaleidoscope closely because it has direct bearing on the Far Eastern situation and upon China's prospects for recovery of a full national existence.

There are evidences that the three aggressor nations (Germany, Italy, Japan) are becoming choked with the dust stirred up by their own momentum and that factors of discord are arising among them.

Hitlerian Germany, as it casts its eyes upon the Oriental scene and attempts to appraise its own actual economic gains in Europe, must realize that the little strips of territory of doubtful economic value which it has seized by threat and intimidation in the past fortnight in Europe, constitute small pickings compared with the enormously greater

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7-7a-2-3-1-7-23
 7-6-23
 18-41
 24-30-32
 7 files

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Japan has been achieving, since September, 1931, on the Asiatic mainland (a million square miles or more with attractive basic resources and large productive capacity, fully supplied with ready cheap labor capable of being exploited under the machine gun). Only some capital and continued non-interference from without are needed by Japan to move ahead under full steam in exploitation. In the absence of a ready supply of capital, progress will be slower, hence less certain because of the possibility that interference will arise during the process of consolidation of gains.

As aggressors, the Germans have in recent weeks been holding the center of the stage, creating a terrific furor, commanding the world's attention, while Japan, less spectacularly but nonetheless surely, has been making definite headway with its program in China. If the Germans are capable of far vision, they must have come to the realization that their gains are "small potatoes" as compared with Japan's. While Germany and Italy have obligingly been holding off Britain, France and Soviet Russia for the past 21 months from interfering in the Far East and from protecting their vital interests there, thus leaving Japan a free hand, Japan has been walking away with such attractive loot as to make Germany appear as a small retailer in the products of aggression in contrast to Japan's relative "wholesale business" in spoils in Asia.

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Japan has had its own way in laying the ground for the "New Order in East Asia" and has been deluding itself with the idea that matters can go on like this indefinitely. Her writers have been lulling the uninformed Japanese populace into a sense of security and her spokesmen have rather blatantly been expressing themselves as easily confident that no economic pressure would be put upon Japan by the United States, Britain or France, holding that the American public, while in sympathy with China, will not go out of its way to help China, that British and French statesmen in their difficulties of coping with Germany and Italy fear that such action would precipitate a world war disastrous to themselves, that an economic blockade of Japan would not be possible without concentrating the world's naval power in the Far East, and that if the three powers were so lacking in "common sense" as to start economic sanctions, Japan would confiscate their property and investments in China, and intimating also that if America were so unwise as to cut off petroleum, it could be secured from the Dutch Indies (grab Borneo) or from Mexico (which latter action would "create a commotion" in the United States). The "New Order in East Asia" envisages Japan as enjoying all the benefits and the rest of the powers "taking it on the chin and liking it".

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The signs would indicate, however, that Japan will not have quite
least of all does Japan want to weaken her concentrated naval strength by
such an easy time of it. Japan has looked for pressure only from the
despatching any of it to Europe, a move which would leave Japan's position
Democracies, not from her own "allies", Germany and Italy. But, as
exposed to possible attack by Soviet Russia's fleet of submarines and by the
Germany approaches nearer to the Russian frontier and the time approaches
large air forces at Vladivostok and exposed to possible attack by the United
States. Little has Japan suspected up to now that it would be subject to
pected to halt in their retreat and to strike back or take a stand, the
demands for "appeasement" of Germany. It has envisaged only Great Britain
need for strengthening the Berlin-Tokyo axis by making it into a military
and France in the role of "appeasement". The realization that it is asked
alliance is felt. Apparently Germany has put such a proposition up to
to appease its own ally must be something of a check. The large funds
Japan, along with an intimation that the return of Tsingtao and of the
voted by our Congress this week for air armaments and the President's
mandated islands in the Pacific would be in order. Probably something has
announcement that we shall proceed at once with the construction of two
been said as to what participation Germany wants and expects in the rest of
45,000 ton battleships and shall strengthen out Pacific fleet, must secure
the available spoils in Asia (Dutch Indies, Philippines, French Indo-China,
Japan some weaknesses, particularly as it is flatly stated that Japan's
British and Dutch Borneo, further large slices of China). Furthermore, in
attitude as to naval armaments is our direct reason for building.
exchange for continued support to Japan on the European end of the axis,
with the foregoing aspect of affairs in mind, so may be permitted
Germany (shy on Navy and a little uncertain of Italy) has apparently made
to indulge in just a little "goodwill gesture" over Japan's wishes that
it clear to Japan that it must give assurances and undertakings that
work in opening up, without need of consultation, the inner harbor and locks
adequate Japanese naval forces will be sent to Europe to help Germany if
at Tsingtao to all ships, and to insist that as a further early gesture
needed.
of "appeasement" to the rapidly rising anti-Japanese sentiment in Britain,
These demands reveal Japan's aggressive ally (Germany) in a new light.
Naturally Japan does not want a German naval base at Tsingtao, nor is the
idea of giving over the illegally fortified Carolines to Germany palatable.

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to the Tsingtao docks and to the Yangtze to non-Japanese shipping. It
 Least of all does Japan want to weaken her concentrated naval strength by
 offering a little satisfaction and a variation of the pattern of witness
 despatching any of it to Europe, a move which would leave Japan's position
 an aggressor power suddenly obliged to adopt a policy of appeasement
 exposed to possible attack by Soviet Russia's fleet of submarines and by the
 toward the Democracies. So far, in the present world war, we have seen
 large air force at Vladivostok and exposed to possible attack by the United
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 States. Little has Japan suspected up to now that it would be subject to
 The opening of the Yangtze will be American, British and other non-
 demands for "appeasement" of Germany. It has envisaged only Great Britain
 Japanese trade little good -- certainly no benefits will accrue as long as
 and France in the role of "appeasement". The realization that it is asked
 The Japanese monopolies certain commodities for their own use, and a heavy
 to appease its own ally must be something of a shock. The large funds
 "cut" in direct levies on all non-Japanese trade passing through
 voted by our Congress this week for air armaments and the President's
 and various exchange control with which we should be prepared. For the
 announcement that we shall proceed at once with the construction of two
 45,000 ton battleships and shall strengthen our Pacific Fleet, must cause
 Japan some uneasiness, particularly as it is flatly stated that Japan's
 attitude as to naval armaments is our direct reason for building.

With the foregoing aspect of affairs in mind, we may be permitted
 to indulge in just a little "ghoulish glee" over Japan's action this
 week in opening up, without much ostentation, the inner harbor and docks
 at Tsingtao to all shipping, and to learn that as a further hasty gesture
 of "appeasement" to the rapidly rising anti-Japanese sentiments in Britain,
 France and America, Japan is about to open up the Japanese controlled
 portion of the Yangtze, presumably as far as Hankow, 600 miles up river,
 to international trade. Up to now, Japan has definitely denied access

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to the Tsingtao docks and to the Yangtze to non-Japanese shipping. It offers a little satisfaction and a variation of the pattern to witness an aggressor power suddenly obliged to adopt a policy of appeasement toward the Democracies. So far, in the present world war, we have experienced only one-way traffic in this respect.

The opening of the Yangtze will do American, British and other non-Japanese trade little good -- certainly no benefits will accrue so long as the Japanese monopolize certain commodities for their own use, take a heavy "cut" in direct levies on all non-Japanese trade passing their barriers, and exercise exchange control with which to finance themselves. Japan will undoubtedly attempt to get something in return for this "magnanimous" act. It can almost be taken for granted that Japan will try to secure, in exchange, from Britain's economic royalists in London, some promise of loans for financing the exploitation. The prospects are "hot" enough to cause the British Ambassador to Japan, Sir Robert Leslie Craigie, to hustle over to Shanghai from Tokyo probably for the purpose of surveying the possibilities of working out a "deal" with the Japanese high command here. The Japanese have some "opportunistic" objectives not apparent on the surface and secondary to the main idea which is to "get right" speedily with America and Britain, as a safeguard against possible efforts on Germany's part to hi-jack the Japanese gains in China or part of them.

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In the first place, the Japanese at present haven't enough of the river type boats to carry on the amount of commercial traffic they desire to conduct. Such ships as the Japanese operate on the Yangtze are sniped at from shore by Chinese guerrilla bands. By putting the British boats back on the river and taking refuge in them, the Japanese can bring down urgently needed quantities of cotton and vegetable oils now bottled up in the region around Hankow. They can also tap the Honan tobacco supply for use in Japan and Manchuria, in which latter place American leaf has been shut out as a war economy measure for 1939.

This brings us, however, to the predicament which the British Government finds itself in, as a result of the situation in Europe. The small opportunistic group of "usurers" which constitute the ruling authority in Britain, for which Chamberlain is the mouth-piece or administrator, is apparently faced with a task of "appeasement" at home. The highly articulate labor group and the British general public, now thoroughly disgusted with Chamberlain's blunders and with Britain's rapidly deteriorating prestige, and particularly dissatisfied with their own lot, realizing that they have been "sold down the river" repeatedly, show unmistakable signs of definite intentions no longer to support the government in its policies. The indications become clearer and clearer that the small ruling group in Great Britain fears its own labor crowd more than it fears Germany. The trend in England,

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Page

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11-9184

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therefore, appears to be more and more toward a mild form of class struggle, though some sort of compromise government built around Lord Halifax as Premier and with Eden and Duff-Cooper in prominent roles, may avert an open breach and keep the country united against aggression from without.

It is presumed that Chamberlain will have to go.

To go back to the subject of German-Japanese relations, it is of interest to note that Germany, while trying to make a deal with Japan for a share in China's spoliation, and for Japanese support in Europe in case of war, is at the same time trying to retain China's friendship by feting the Chinese Ambassador at Berlin. The Chinese, despite Germany's withdrawal of military advisory support last June and despite the holding off by Germany of this same Chinese Ambassador for months from presenting his credentials at Berlin, (this in deference to Japan), have been trying to cultivate and hold German good will, because China has been dependent upon Germany to an important extent for munitions on barter deals made prior to or early in the hostilities but incomplete as to delivery.

It is of interest to note also as another factor of Japanese-German discord that Japan has recently made official representations to Berlin requesting a cessation of the supply of munitions to China. German sympathy (industrially and in trade) is with China, but Germany up to now has needed Japan as an ally to play off against Soviet Russia and Great Britain.

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Post

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11-9184

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China this week is pleading with America for a revision of the Neutrality Act on such a basis that we shall not continue to aid Japan and asks us to focus some of our attention on the Far Eastern situation rather than to draft the revision solely to fit the situation in Europe. Certain Chinese editors are becoming fed up with the evidences of American opportunism in continuing to supply Japan with the materials and implements to carry on the latter's aggression in China and are branding our protestations of friendship for China and of love for democracy as hypocritical. There is a currency of feeling among Chinese that our credit of US\$25 million to China last December was passed out as a "sop" to avert too much scrutiny of American opportunism in dealing with Japan.

China, despite brave resistance, is suffering continuing defeat. Nanchang, capital of Kiangsi Province, fell to the Japanese during the week. Thus, the highway-rail route from the Chekiang coastal ports to Central China is cut. The Chekiang ports are being shelled and bombed, and it looks as if this avenue of economic life may shortly be closed, thereby bottling up Chinese controlled territory more effectively. Bitter reactions are only to be expected under the deep discouragement of these events and under the apprehensions which again arise that Great Britain may now make a materialistic deal with the Japanese at China's expense. All reports prior to the sudden fall of Nanchang indicated that a high degree of morale and esprit de

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for the week ending

MARCH 30, 1939

Post

Date

MARCH 30, 1939

CONFIDENTIAL REPORT - 40

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Soviet Russia has been wise enough to withhold support from Great Britain in the European situation unless and until there are some undertakings on Britain's part to function on a basis of "indivisibility of peace" and "real collective security against aggression", as an ally of Soviet Russia in case of war with Japan in the Far East. Soviet Russia wants to see Great Britain organized militarily, with conscription assured, - fully prepared, - before entering upon any joint commitments. If Britain and Soviet Russia finally work out a scheme for mutual support, it will be encouraging to China, as such an agreement would preclude any British-Japanese deal at China's expense.

The reluctance of Poland and other smaller states to sign eleventh hour British proposed collective security pacts with Britain and Soviet Russia indicates lack of confidence in Britain and unwillingness to repeat Czechoslovakia's error in this respect. The small states in Eastern Europe are in a distinctly unenviable position. They are obliged to play a cautious role, subservient to German influence, rather than to run the risks of placing reliance on the poorly defined policies of Britain and France.

The evidences continue fairly strong that the Chungking Government of China will carry on the struggle of defense, if necessary, to complete defeat, rather than surrender to Japan. All reports prior to the sudden fall of Nanchang indicated that a high degree of morale and "esprit de

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corps" still obtained at Chinese Government centers in West and Southwest China and at the front as well as among the guerrilla forces. But "esprit de corps" and optimism are inadequate as weapons unless backed up by artillery, in which the Chinese are still deficient, the Japanese mechanization being probably 10 to China's 1. The Japanese news spokesmen at Shanghai have officially admitted to foreign news correspondents that their forces in Central China on the Nanchang front have been meeting a "new Chinese army" consisting of young soldiers between 18 and 22 years of age who fight ferociously. Japanese casualties are admitted as being unusually heavy.

In the midst of this conglomeration of world events we were obliged to report by radio during the week that Shanghai's recorded foreign trade for January-February, 1939, had recovered to a level better than that in the same period of 1936 and only 23% under the extraordinarily good levels of January-February, 1937. A basic factor which contributes to this trade revival is the well-known resiliency of the Chinese people which enables them to rebound after every major disaster if given half a chance. But other unnatural factors enter into the explanation of the phenomenon of nearly normal trade levels after nearly two years of disturbances and abnormal conditions in Shanghai and surrounding regions.

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The imports consist in large part of raw materials and supplies which should normally come from a domestic source. Japan has monopolized or taken for its own use the bulk of Chinese available supplies of coal, raw cotton, leaf tobacco and wheat, necessitating heavy imports of these items and of flour from abroad. Other quantities of raw materials are still bottled up in the interior and cannot as yet reach the Shanghai mills. When the supplies become accessible, they may be taken largely by Japan. Production has been reduced in the interior on some of the products to prevent Japan from acquiring them.

The concentration of self-supporting refugees in Shanghai accounts to some extent for an influx of consumer goods from abroad. The fact that Shanghai mills have been able to ship to the Chinese controlled interior has enabled production enterprises here to take more raw products from abroad than may be the case a little later. Destruction of industry in Shanghai during the hostilities is accountable for the necessity now to import certain products formerly supplied locally. Conditions are not prosperous or promising, but a degree of economic life continues in the accessible region around Shanghai and creates demand for the raw products and semi-manufactured commodities which go into factory and handicraft industry.

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CONSULAR REPORTS

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These several points must be taken into consideration in analysing the "recovering" trade of this region. Bear in mind also that Japan's portion of the trade is steadily mounting. In North China, the foreign interests are decidedly gloomy and apprehensive as to the future due to the imposition on March 11 of export exchange control and to some insulation of the North China market from Shanghai and Central China by treating the latter areas as foreign countries so far as trade is concerned.

Date 4/3/39

Subject Trade conditions in the Hankow area

continued stagnant etc. A. Bland Calder,
Acting Commercial Attache.

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