

Very high degree of secrecy in recent weeks. Literally the Foreign Minister and the Japanese Ambassador have been alone in their conversations, and no detailed report has been made to the Central Executive Committee or to other considerable groups of high personages.

Hsü Mo: "We must enable the Japanese to find a way of retreat that will save face for them."

Eight demands, mainly of an economic nature, have been made upon Sung Cheh-yuan by the Japanese generals. They have been sent to important men in relevant Ministries here for comment. Part have been disclosed vaguely in the press: Development of Tangku as a port; extension of cotton production on Japanese lines; reorganization of the Lungyen mines; construction of the Tientsin-Shihchiachuan Railway. Others are kept in strict confidence thus far. None of them sounds startling in itself, but the total program is so extensive as to put Japanese hands into most parts of Hopei and across the borders of neighboring provinces. Moreover, the "proposals" are from military men, who merely say that they will take the responsibility for securing the money from Japan. It is unnecessary to point out what a Japanese-controlled port at Tangku would do to Tientsin and to the remains of the Chinese Customs system in the north; or that a Japanese cotton program would affect local administration, banking, transportation, and Chinese mills and distribution; or that the railway to Shihchiachuan will involve a police and military lane to the gates of Shansi, amputating Hopei and Chahar from the rest of China, and focusing more of economic interest under proper control at Tientsin.

Some members of the group around Wu Ting-ch'ang and Chang Kia-ngau are reported to be talking actively with the Japanese on lines of extensive economic cooperation in North China, and are quoted as saying that for the time being North China should be "allowed to become like Canada within the British Empire". That seems to be a faulty rationalization of defeatism (or of "realism", if one prefers the term). On the other hand, Loy Chang is quoted as saying three days ago that the Government was taking a very firm stand all along the line.

Suma: Much more mild and cautious than usual. Interpreted by an experienced foreign correspondent as not knowing what to do next, and unable to maintain the customary bluster. Nevertheless, he repeatedly sneered at the suggestion that the Chinese might fight.

Kung is really sick, aside from being much troubled at the pressure Wu Ting-ch'ang and Chang Kia-ngau continually bring upon him and his adherents.

Chiang Kai-shek is showing a generally firm attitude, without fear of the Japanese. He has given considerable encouragement to Fu Tso-yi in Suiyuan (Fu saw him at Loyang) and to Sung Cheh-yuan. The latter is somewhat bucked up, and is in better touch with Chiang than ever before. But Sung is much embarrassed over the aviation agreement which Chen Chu-cheng succeeded in getting him to sign, and even lied about it to intimate messengers. Chiang forgave him, as the basis of a new start in cooperation; and agreed that he should not come south for conference. Han Fu-chu is expected to visit Peiping at the request of the Central authorities,



as part of the generally improving cooperation.

Gunther Stein, who ranks very high indeed in knowledge of Japanese economics and general policy, is convinced that money will not be forthcoming for significant investment in China; and that the program of economic expansion will break into military and political control of Chinese resources. The phrase "canalization of Chinese economy" is frequently used. He also fears action by army groups or navy groups, particularly the latter. Indication of naval boldness is provided in Stein's expectation that if Britain is involved in a European war, the Japanese navy will take the Netherlands Indies.

Stein believes that the Russian question is far greater in Japanese eyes than the Chinese. (Interesting confirmation is provided in Hsü Mo's revelation that more than once the Japanese diplomats have said they required a pledge of cooperation against "international communism".) Therefore they will not bog the army in China. The Japanese were much disturbed by the last big border scrap just a few days before the Mutiny, in which 3,000 men were engaged. The Mongols were running tanks and all sorts of good equipment without any Russians in evidence; which was disturbing to the usual raiding program.

There is all the material for Greek tragedy in Stein's utter pessimism regarding any serious revision of Japanese policy. He considers that their present position is not only economically difficult, but politically impossible. If China really develops herself, Japan's precarious hold on Manchoukuo cannot be maintained, and even Korea and Formosa would be endangered in any conflict. Moreover, the view of China and Russia as two hostile neighbors continually increasing in strength as against Japan's limitations, is full of despair. The only way out is to bring a considerable part of China's potentialities, especially those that might be most easily joined with Russia or most easily used against Manchoukuo, within Japan's control and use. Probably also to strike at Russia in the one moment before "too late" has become hopelessly "past", in connection with the expected German attack. Thus Japan must go on, though she is already beyond true strength and soundness. Stein's opinion is that the Russian war will come during the year July 1937 to July 1938, with timing determined in Europe. (All this is my form of statement, which I hope is fair to Stein's views).

An American observing officer (naval?) is quoted as saying that the Chinese Government has aviation fuel supplies for two weeks of wartime consumption.

Waichiaopu friends insist that Chang Chün stuck firmly to his guns in the seventh interview, though they have no details to disclose.

*A Mitsui director said the industrialists would not put money into lands they expect ultimately to be Soviet or Chinese — including Manchoukuo.* B.