

(2) about \$9 million unencumbered. The Chinese wish to spend this before the credit expires at the end of the year but find little of interest in the hands of War Assets. Two specific requests have been received:

(a) about 1000 Browning machine guns and some spare barrels worth \$187 thousand

(b) about \$5 thousand of drop copper wire

C. Under the \$12.3/4 million loan extended by Canadian banks to the Ming Sung Industrial Company, Ltd., guaranteed by the Government of China and in turn by the Government of Canada under the terms of the Export Credits Insurance Act three 270 foot shallow draft vessels being built in Quebec shipyards and together worth \$7.3 million. One of these vessels is ready to leave almost immediately but delivery is being delayed until next Monday, after which further delay will be difficult. The Chinese have requested delivery of a second vessel by December 24th. The third will not be ready until the spring.

D. About \$5 million of small arms and ammunition ordered from the John Inglis Company by T.V. Soong, Governor of the South China provinces of Kwangtung and Kwangsi. Shipments are to begin at the end of the year and extend over a six month period. Payments will be made in United States currency as shipments are made. Cabinet approval for this export has already been given.

3. The National Government may be expected to continue to honour its obligations under the Loan Agreement. However, as it is pushed into smaller and smaller territory by the Communist offensive its real ability to repay the loan is obviously lessened. Initial payments may be made in order to protect the international credit position of the National Government. However, in view of the serious annual deficits in the balance of payments position of the National Government it would be a case of borrowing from Sam to pay Jack to make these payments.

4. In the event that a Communist dominated Popular Front Government is established in China, the question will arise as to the probability of its assuming the obligations of the National Government. While the National Government is in existence it is unlikely that a Communist dominated Popular Front Government will assume any responsibility for the former's debts. However, if such a Popular Front Government becomes the only Government of China and seeks international recognition the question of its assuming the obligations of the National Government of China will arise in more direct form. Statements issued by the Chinese Communist Party indicate that they will not recognize agreements concluded by the National Government against what the Chinese Communists consider to be Chinese interests. However, a Communist dominated Popular Front Government might come to the conclusion that it was in its own interest to recognize that portion of the \$60 million Canadian loan to China that corresponded to the non-military equipment of permanent value to China that was in existence when they took over control of China and that could be identified as having been purchased in Canada under the Loan Agreement. Reasons for their taking this attitude might be (a) a desire to establish international credit with a view to trying to borrow more money (b) to encourage western governments to allow private trade with a Communist controlled China (c) to encourage western governments to support various interna-