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EVALUATION REPORT

NATIONAL ECONOMIC DEVELOPMENT FUND

July 12, 1973

This document is to be considered
unclassified upon removal of the attachment

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EVALUATION REPORT - NATIONAL ECONOMIC DEVELOPMENT FUND

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June 29, 1973

EVALUATION REPORT

NATIONAL ECONOMIC DEVELOPMENT FUND

INTRODUCTION

This is a report of the Evaluation Team which was requested to assess the performance of the Vietnam National Economic Development Fund (NEDF) from the time of its establishment in March 1972 to May 1973 and to indicate possible changes in the Project Agreement and in development finance policies for the immediate future. While we considered a wide range of economic and investment issues and problems while in South Vietnam, this report focuses upon the provisions of the Project Agreement and specific issues and problems of NEDF in a broader context.

The Evaluation Team consisted of Henry F. Lee, Treasury; George J. Grande, AID; and Kenneth R. Krause, Agriculture. The Team arrived in Vietnam on May 22, 1973 and departed on June 8, 1973.

To discuss the issues relevant to NEDF as a part of overall economic development, we had access to all relevant reports and both extensive and intensive discussions with NEDF and other GVN officials, bankers, businessmen, academics and legislators and USAID personnel. The operational history of the fourteen months of NEDF operations is provided by regular reports and publications of the NEDF and we have made no attempt to restate it here. We viewed our mission "to assess NEDF" and therefore, we describe the general issues and circumstances in the context of what NEDF has done and what could be done.

This report contains a section on selected portions of the Project Agreement between USAID and the GVN and another section on specific topics -- some related to the provisions of the Project Agreement and others to general topics which emerged from our study and conversations.

SUMMARY COMMENTS ON SELECTED PORTIONS OF THE PROJECT AGREEMENT

The following comments are summary statements of problems and/or issues related to specific sections of the Project Agreement for NEDF entered into between AID and the GVN. Sections not referred to indicate satisfactory performance. Further discussion of these problems and issues appear later and are treated from a broader perspective.

II. Purposes of the Fund

The "primary purpose" is to "stimulate private sector investment in ways which will lead to higher output of the economy and independence from foreign aid as soon as possible" and "a second, closely related objective" is to improve medium and long-term lending institutions. Performance of the primary purpose is difficult to assess since the Project Agreement does not provide adequate guidance. Since this permitted different interpretations there appeared to be differences of opinion on performance. The second purpose is explained at greater length in the Project Agreement. Performance has been satisfactory. Please refer to page 11 and following for further discussion on this subject.

V. Sources of Funds

In the second paragraph of this section, all repayments of principal are to be returned to "counterpart". It is not clear whether this means to NEDF and/or GVN control and disposition or to U.S.

controlled counterpart. We are advised counterpart is returned to the same account from which it originated but the language does not make this clear. This is important to the consideration of NEDF lending piasters from repayments of principal. The original concept was to avoid accumulation of repayments. This feature would make effective the temporary nature of the Fund. It would also require the NEDF to seek new funding from the GVN and other donors.

Earned surplus is to be disposed of by decision of the Board of Directors at the end of each accounting year. The first year's surplus is almost 30 million piasters. The Fund charges 10 percent to the ICIs who in turn earn 5 percent. At these rates the Fund, which is housed by the National Bank, will earn substantial income in relation to operating expenditure. There appears to be a need to indicate that surpluses "earned" beyond approved budget expenditures[1/] should be transferred to the GVN Treasury or GVN counterpart account unless the Board of Directors can justify the retention of specific amounts for particular purposes. The concept here is to remove the temptation to expand unnecessarily or to finance unrelated activities.

VI. Fund Responsibilities

C. Relations with ICIs

Performance under this section, aside from personal relationships, appeared to be adequate insofar as the specific provisions are

1/ During the first year of operations no formal budget was prepared owing to a lack of data on which to base a meaningful presentation. This is no longer the case. An approved budget should now be an absolute requirement.

concerned. This is documented by the publications of the Fund and supported by general comments. However, personal relationships were alleged to be sensitive due in large part to personalities and in part to the competitive relationships among ICIs. Further discussion of this appears later herein.

D. Fund Review of Projects

Performance of terms in this section appeared to be adequate and progress toward improvements could be noted. The problem of some necessary duplication of review still remains however.

VII. Fund Operations

A. Eligibility of ICIs

This section indicates that all commercial banks chartered by the National Bank of Vietnam are eligible to submit projects to the Fund for prior approval financing and in the following paragraph the Fund is empowered to establish criteria for renewal of eligibility. Recently the Fund determined that since rural banks are legally commercial banks, these banks are ICIs that can apply directly to the Fund for medium and long-term financing. Although rural banks are considered to be privately owned banks, about half of their capital is provided by GVN/USAID counterpart through a grant to the Agricultural Development Bank (ADB) program that established rural banks. Direct lending to the rural banks from other than the reconstruction fund would normally be very difficult because rural banks would not be able to meet the eligibility criteria. However, the Fund decided to provide informal

technical assistance, with the agreement and participation of the ADB, to prepare applications for funds. The first loans in this category were made on May 30 from a one billion piaster special fund for reconstruction. While this is a special case the principle that rural banks are ICIs is established. This could cause future difficulties between the Fund and ADB since the ADB and the Fund could be competing with each other to provide rural banks with medium-term funds.

C. Eligibility of Projects

There were comments to the effect that the project selection should be based upon expressed priorities. Another comment was to consider priorities for certain geographic areas for a variety of reasons. These considerations presumably involve a trade off with financial analysis. While grant counterpart might be used to provide funds for these reasons, terms and conditions of future external loan funds would very likely not permit wide variations of concessional terms.

There were some long discussions about the operational definition of a project, particularly with respect to the Agricultural Development Bank and Rural Banks. It is understood that the line of credit granted to the ADB includes projects whose value is less than the minimum for project approval. In addition, medium term equipment loans which are also smaller than the minimum project approval amounts, are being financed from lines of credit. Alternatively, it would also

be possible to define line of credit financing to include only equipment loans and require "projects" to be financed by the project approval procedure. In this case, the ADB would be required to group "projects" until the total reached the minimum permitted. Of course the minimum for the ADB could be reduced to fit the size of the agricultural projects if it is believed to be necessary to hasten the approval process. However, this alternative does appear to be more cumbersome than the current practices.

D. Loan Policy of the Fund and of ICIs

(1) Credit Term

The maturity and grace periods have been criticized because they are not long enough to fit particular projects. The case most often mentioned is the seven year gestation period for rubber trees. It is suggested that this section might be reworded to accommodate special cases if the Fund decides to make such loans.

(2) Purpose of Loan

This section states that funds cannot finance working capital or be used for project refinancing unrelated to new investment. This presents difficulties with proposals to refinance government enterprises to improve the chances of divestiture. The refinancing issue is that concessional long-term funds (at 15 percent) would replace short-term debt (at 24 percent) for working capital to improve the profitability of government enterprises so that the divestiture to private investors would be successful. These issues are considered later herein.

(4) Special Arrangements for Agricultural Loans

The ADB is permitted to group its loans to meet the minimum Fund loans to ICIs of the equivalent of US$150,000 for project prior approvals or US$35,000 for line of credit. It is understood that these minima are too large for ADB. It is alleged that the grouping of ADB loans requires potential borrowers to wait for an inordinate time while the ADB searches for loans that will add up to the minimum. This is particularly true in the case of line of credit financing.

This was somewhat confusing and may have been due to a misinterpretation of the Project Agreement. Disbursements under a line of credit agreement by ADB should be permitted in any amounts.

(5) Interest Rate and Fees

The Board of Directors sets interest rates for the Fund and the maximum rate for the ICIs. The Fund rate is set at 10 percent and the margin for the ICIs at 5 percent. There were quite a few adverse comments on this split. There are proposals to lower these rates for priority sector loans to 8 percent to the borrower. While these rates are set somewhat arbitrarily because the Fund resources are counterpart grants, external loans to the Fund will require coverage of foreign exchange interest rates and exchange risk. This may require the Fund to reconsider its rate structure. A more detailed discussion follows.

IX. Technical Assistance

There appears to be an imbalance in this section providing technical assistance (TA). The "privately-owned" ICIs will pay for TA but TA will be provided to "publicly-owned" ICIs by USAID. While this was intended to exclude privately-owned commercial banks, especially the foreign-owned commercial banks, it also excludes the privately-owned development bank (SOFIDIV). Since the granting of TA by USAID is on a "permissive" or "need" basis, there should be no hesitation to include them. Moreover, the language is confusing when it is applied to the ICIs. For example, ICIs include Credit Commerciale, a government-owned commercial bank (the largest bank) and other commercial banks which are privately owned. Rural banks, which are ICIs, are owned in part by the government through contribution of their capital. Even if TA were to be offered, they would probably not be able to take advantage of it.

Alternatively, the "privately-owned" ICIs probably need TA more than the "publicly-owned" ICIs. Moreover, the private ICIs have other disadvantages which reduce their competitive ability to provide medium and longer-term loans.

There were suggestions that the privately-owned ICIs might be given a larger margin to finance technical assistance. This does not appear to be appropriate--first, because it increased differential interest rates unnecessarily and would not be easy to manage when foreign loans are involved and--second, because local currency does not assure the foreign exchange needed to pay for foreign technical assistance.

XI. <u>This Project Agreement may be modified from time to time by mutual consent of the parties</u>

This "catchall" provision can serve as the basis for consideration of Fund loans which appear to be expressly prohibited in the Project Agreement. This is particularly so in the "refinance" cases. (See page 20).

III. DETAILED COMMENTS ON PROJECT AGREEMENT

II. Purposes of the Fund

The purpose of the NEDF as stated in the Project Agreement is to stimulate private sector investment in ways which will lead to higher output of the economy and independence from foreign aid as soon as possible and to improve medium and long-term lending institutions.

Although the efforts of NEDF have resulted in some stimulation of private sector investment, we believe this is too broad a directive and that it has resulted in the preparation by NEDF of a number of studies (some of formidable size) which in some instances the USAID Mission considers of questionable usefulness. It is the view of the Evaluation Team that the ProAg should be revised in order to more clearly and specifically define what is expected of the NEDF.

Progress toward the second objective, the improvement of medium and long-term lending institutions, is more apparent although only in part due to NEDF efforts. Most notable improvement has been made in the operations of SOFIDIV and the IDB. The quality of project preparation and review has markedly improved. Improvement in ADB operations is apparent, but not as striking. This is primarily owing to the fact that ADB had limited experience in loan development before the NEDF came into being.

It should be noted here that the improvement in SOFIDIV operations has been accomplished in spite of a number of disadvantages under which that organization was obliged to operate. Staff members

of SOFIDIV are not and have not been exempted from military service (as those from ADB and IDB were and are). This resulted in a constant drain of the younger staff members and made it difficult to recruit young staff members with the necessary talents -- particularly those with foreign training who could contribute to the improvement of project preparation.

It is also noteworthy that Technical Assistance has been provided to ADB and IDB whereas SOFIDIV has received no such assistance. It is the recommendation of the Evaluation Team that similar assistance be made available to SOFIDIV.

Interest of the commercial banks in development lending has been limited and the amount of assistance requested/offered to these banks has been almost negligible. This lack of interest on the part of commercial banks is not difficult to understand. The banks are shareholders of SOFIDIV and they look to that organization to maintain a specialized staff to handle medium and long-term lending. They have done this because longer-term funds involve concessional or subsidized money, project preparation and approvals that require a special organization to deal with the GVN and with possible foreign lenders for longer-term project funding. The commercial banks have been reluctant to get into this business since it would mean that each bank would have to develop project capability in these areas. There are few commercial banks that have this special competence at the present time. SOFIDIV makes it possible for all of the commercial banks who own capital stock in that organization to feel that they have access to,

or can provide longer-term credit facilities to their customers through their equity relationship with SOFIDIV. All of the more prominent commercial bankers are on the Board of Directors of SOFIDIV.

Another related problem is the treatment of foreign commercial banks by NEDF. Since the GVN has not encouraged foreign bank branching and the foreign commercial banks are not interested in domestic credit per se, projects proposed by foreign commercial banks would probably focus on foreign participation. The question is, what should the position of NEDF be? Should NEDF help finance technical assistance? Probably not. Should foreign enterprises be permitted higher equity ratios? How much financing should NEDF provide? Should it be only for the local cost portion of fixed assets?

V. Sources of Funds for NEDF

a. Piaster Funds

So far AID grants from counterpart permitted NEDF to determine interest rates and other terms and conditions. However, some consideration should be given to the source of the local cost portion of fixed assets loans once AID and other grants begin to decrease or become inadequate. Grants from the budget are an obvious source but this might only contribute to larger deficits to be covered from Central Bank borrowings. Consequently in the initial gestation period these expenditures would be inflationary.

Another theoretical possibility is the issuance of ICI bonds to the public at attractive interest rates. Since a one-year time deposit

is 24 percent, a longer term bond rate would probably have to be substantially higher. Probably too high in the current context of a depressed investment climate.

A future problem is to find a source of non-inflationary, long-term piaster funds that can be lent to ultimate borrowers at concessional rates. This is compounded in Vietnam because the current rate of 15 percent is a real negative rate considering price increases of about 25 percent per year. This might be one more reason to consider reduction of inflationary pressures.

Another future problem might be the determination of interest rate policy for grant counterpart funds and counterpart from foreign loans. As described in the following paragraph, the interest rate on the counterpart from foreign loans would include the exchange risk to the ultimate borrower while current rates for grant counterpart funds are arbitrarily established at real negative rates to encourage investment. The problem is to establish a unified rate structure that would cover exchange risk and still provide concessional funds to approved projects.

b. Foreign Exchange Loans

NEDF will be confronted in the near future with the impact of foreign loans on interest rates and other terms. The issue is of course the size of the exchange risk. It is understood that the Taiwan loan terms are 4 percent for 15 years. If the rate of inflation remains at about 25 percent per year, the exchange rate conservatively will probably depreciate by at least 10 percent per year (making very

optimistic assumptions about increases in production and productivity.) If the NEDF margin is reduced to say 1.5 percentage points, the rate to the ICI will be 15-1/2 percent and to the ultimate borrower about 20 percent. Since inflation is about 25 percent this is still a real negative rate. But it does indicate a significant difference with the current thinking on lowering the 15 percent rate to 12 percent and lower further the rate to 8 percent for priority sector lending.

Since these loans will be medium and longer term say up to 15 years including grace periods, it would be difficult to fix contractually an interest rate based on current inflation rates. As a result some consideration might be given to methods to adjust the interest rate each year depending on some formula. One method might be to adjust by the percentage depreciation of the exchange rate of the previous year for the current year calculations.

Another issue is the use of reflows. Currently repayments on loans made from grant counterpart return to "counterpart". To relend these reflows, NEDF would need to receive further allocations from counterpart. But, in the case of counterpart from foreign loans, NEDF loan repayments would return to GVN control where it would have to be reallocated to NEDF. That is if the foreign loan is for 15 years and NEDF lends the funds initially for say 5 years, should NEDF have the use of these funds for further lending? Since interest charges will continue, the relending of these funds involves the same interest as the original loans.

Sharing the exchange risk would probably not be feasible since the size is so much larger than the interest rate. Moreover, the ultimate borrower is the beneficiary of the inflationary pressures through increases in his output prices. As a result, the ultimate borrower should bear the exchange risk with perhaps an adjustment factor to account for the variability of inflationary pressures.

VI. Fund Responsibilities

c. NEDF Relations with ICIs and GVN Agencies

Relations with ICIs appear to be improving--at least from the standpoint of loans approved. In the first nine months of 1972 more than 80 percent of the funds went to the IDB and SOFIDIV, both of which had acquired a considerable backlog of industrial projects. This is despite personal difficulties between the presidents of NEDF and IDB. SOFIDIV is rapidly increasing its borrowings from NEDF as they become more skilled at project identification and preparation. Relations with SOFIDIV's managing director and staff are understood to be excellent.

Relations with the ADB, however, are more complex. This is due in part to the degree of control exerted by the Minister of Agriculture on the operations of ADB and the strained personal relations with NEDF management. Nevertheless, loans to ADB and rural banks have recently begun to increase sharply. This is primarily due to USAID advice to focus on the agricultural sector, to President Thieu's recent speeches stressing the need to focus resources on agriculture to help resettle refugees on new and abandoned lands to increase agricultural production, and to the special fund for reconstruction granted to NEDF.

There appears to be a possibility of future conflict between NEDF and ADB over NEDF direct lending to rural banks. ADB agreed to permit NEDF to make direct loans to rural banks from a special fund of one billion piasters to finance fixed assets in war-damaged enterprises. While this arrangement will result in quick disbursement of loans to

this special limited class of borrowers, it also sets a precedent that since rural banks are legally commercial banks, rural banks are eligible for direct, ordinary NEDF loans. This will result in competition with ADB branches in their efforts to provide medium term loans to rural banks from NEDF funds. While this bank competition is appropriate, competition among qualified rural banks would be preferred as ADB gradually withdraws from the short term deposit and credit business. Since ADB contributes about one-half of the original capital of rural banks and supervises the rural banks, there appears to be a possibility of future conflict. This can be avoided if ADB focuses on larger projects with its resources and the rural banks emphasize smaller or supplementary projects. In addition, the ADB is limited to agricultural loans while rural banks may lend to both agriculture and industry.

VII. Fund Operations

D. Loan Policy of the Fund and of ICIs

Loan policy of the Fund and the ICIs is outlined under Section VII, D of the Project Agreement entered into between A.I.D. and the Directorate General for Budget and Foreign Aid of the GVN. Compliance with the terms of the Agreement is considered to be satisfactory--particularly so since the arrival of the Checchi contract advisors to the Fund.

(1) Credit Term

Section VII, D (1) of the Project Agreement provides that loans extended by the NEDF will be of 2 to 10 years' duration with the possibility of a grace period of not to exceed 25 percent of the term. It has been noted that this provision may be unduly restrictive in some instances. A case in point is the financing of trees for rubber plantations. Rubber trees are not productive for a period of seven years and provision should be made to allow for an ample grace period during the time when the trees are not in production and include some of the cost of caring for the trees. This might require an extension of the two to ten year loan period and would almost certainly require an extension of the possible grace period. Provision for projects of this type could be made in one of two ways:

a. Duration of loans could be extended to 15 years maximum by modification of the Project Agreement and the grace period could be extended in the ProAg to accommodate a seven year gestation period should this be necessary.

b. Present wording of the Prof.g could be left as is with an addition to the effect that loan duration and grace period might be extended on a special consideration basis for projects where circumstances might warrant.

(2) Purpose of Loan

a. Several cases have arisen wherein borrowers have resorted to commercial bank or other financing as an interim measure owing to delays encountered in final approval of NEDF loans for whatever cause. The assumption of this funding by the NEDF is termed to be "refinancing". It might better be called "refunding".

The USAID Mission has questioned financing of this type by the NEDF as contrary to the provisions of Section VII, D (2) of the Project Agreement which provides that NEDF may not fund "project refinancing unrelated to new investment". The Evaluation Team believes that every effort should be made to expedite the processing of NEDF loans in order to put an end to the need for such refunding. However, in the limited number of cases where delays cannot be avoided and resort to other financing must be made, we are of the view that refunding should be permitted up to the level of the initial loan proposal and subject to approval of the loan.

b. In conjunction with the divestiture program, concessional long-term refinancing of short-term inventory debt for several government-owned corporations has been proposed as a means to make them more attractive for purchase by the private sector. It has been suggested that the Prof.g be amended to specifically permit refinancing

of those companies.

The Evaluation Team does not feel that a modification of the ProAg to permit such refinancing would be prudent. We do believe, however, that consideration of such financing should not be excluded from the scope of NEDF activity. We would hope that refinancing of this type could be kept at a minimum. In cases where it is agreed to be essential, USAID/NEDF might agree to review the possibilities for financing without resorting to formal change of the ProAg.

c. With regard to refinancing of expansion and/or modernization investments thought to be essential to the success of the project, USAID/NEDF may wish to agree to some refinancing that would not exceed the amount of net new investment less working capital. The issue here again is long-term concessional loans to replace short-term working capital debt. The appropriate solution like these cases cited above would be further capitalization of the enterprise. If it is determined that further capitalization is not available and the enterprise is considered to be so essential, USAID/NEDF may wish to refinance. But, of course, this raises questions about the viability of the enterprise itself whether it remains government-owned or is divested to the private sector which will still have to carry the debt however long the term.

The Evaluation Team suggests that these applications be taken up on a case by case basis. NEDF and USAID should consider the opportunity cost of refinancing in these cases, i.e., would it be better for the economy for NEDF to finance many new small and medium-

sized private sector enterprises or to "refinance" government enterprises as described above for divestiture purposes to the private sector.

NEDF has adhered carefully to the Project Agreement requirement that loans be made only to the private sector. Air Vietnam informally contacted the fund with a proposal to finance the purchase of 727 Boeing jet aircraft. The proposal was never formally submitted.

In the above mentioned possibility of refinancing government enterprises which are about to be divested, NEDF financing (if approved) would be effective after the divestiture to private investors.

NEDF loans to new and high priority government enterprises could be considered under Section XI of the Project Agreement which allows for modification by mutual consent.

(4) Special Arrangements for Agricultural Loans

Section VII D of the Project Agreement sets the limits for industrial and agricultural loans and for lines of credit. By special arrangement, the ADB is permitted to finance agricultural and agri-business development projects in amounts less than minima subject to certain established provisions. The team had access to an internal report prepared by AMCOA on this subject and benefitted from their insights. The Evaluation Team is at a loss to explain the present interpretation of the provision that disbursements from lines of credit will be established in $25,000 amounts. It appears that the ADB, the NEDF and the USAID Mission understand this provision to require that

$35,000 in eligible applications must be compiled before any funds can be released under a single line of credit. This is not the purpose of a line of credit and certainly was not the intention of the founders of the Fund. $35,000 was set as the amount of credits that could be extended before reporting to NEDF/USAID would be required. It was not the intention that all credits under the line should be held up until this amount had been reached. To so require is to completely defeat the purpose for establishment of the line of credit procedure. This was discussed with NEDF and USAID who agreed that this practice should be discontinued at once. It is assumed that appropriate action will follow.

(5) Interest Rate and Fees

The maximum interest rate on NEDF funds to the ultimate borrower is presently 15 percent--10 percent going to the NEDF and 5 percent going to the ICI plus commitment fee. [The ICI also takes a lien on the physical assets of the borrower. In the event collateral is inadequate, and if the project is felt to be particularly worthwhile, the Fund can enter into a guarantee agreement with the ICI to take a part (up to 50 percent) of the credit risk. In such cases, interest rate to the ICI will be reduced and that of the NEDF increased in accordance with the degree of risk. Any losses would be borne pari passu.]

It has been proposed that the Fund accept a lesser portion of the interest and that the amount payable to the ICI be increased. In line with this proposal, it should be pointed out that

the 10 percent/5 percent division between NEDF and the ICIs was arrived at on an arbitrary basis to serve as a starting point with the idea that it could very easily be subjected to change should experience determine or circumstances warrant.

This is a particularly appropriate time for reconsideration of interest rates since the GVN is now about to undertake implementation of a $5 million loan from the Republic of China and a loan of $50 million is presently under active consideration by A.I.D. Since repayment in foreign exchange will be required for both these loans, and since repayment must come from projects undertaken by the NEDF and the ICIs, the matter of interest charges takes on new and immediate significance. It is the recommendation of the Evaluation Team that this highly complex matter be made the subject of an immediate and intensive policy review.

NEDF charges a commitment fee of 0.5 percent on unutilized balances to urge borrowers to use committed loan funds. This is the same procedure used by the ICIs. This does not appear to be an issue. However, the size of the charge does not appear to be a stimulus for expenditure since other interest rates are so high.

IV. GENERAL COMMENTS

I. Status of NEDF

NEDF was created with the idea that it should be a temporary organization and it should continue to be considered as temporary as to specific objectives but not necessarily temporary in terms of organization. As presently constituted, it has no long-term role in overall aid financial programming unless it can be given additional functions. It should be borne in mind, however, that the Fund is a GVN organization and therefore its continued existence depends primarily upon its continued usefulness to the GVN.

The Fund could be transformed into another type of organization or it could be given specific tasks from time to time in its present form. For example, it could be assigned to coordinate foreign development loans for the private sector through the ICIs.

IV. GENERAL COMMENTS

II. NEDF Operational Issues

In general the internal operations of NEDF appear to be well coordinated. Staff recruitment and facilities appear to be satisfactory. Of a total staff of fifty-one, there are thirty-one professionals, specialists and managers.* They are divided into four departments--Investment Promotion, Finance and Banking, Research and Development and Management and the Office of the President. The Evaluation Team was briefed by each of the department heads on each of their operations. There appeared to be substantial efforts by all departments to improve the investment climate. This involved personal contacts with ICIs--IDB, ADB, SOFIDIV, commercial banks and rural banks,--with other government agencies and with foreign government officials and agencies. In addition, there are numerous publications, speeches, studies and seminars.

USAID assisted NEDF in establishing an accounting system. A copy of the USAID report is available.

There appear to be two issues. First, expenditures for foreign travel, seminars, publications, etc., appear to be excessive. This is due, of course, to NEDF's interpretation of its purposes. Since the primary purpose is stated to be the promotion of private investment, NEDF had to determine what form this promotion should take. More specific guidance from USAID could have resulted in a more productive program.

*See Table following page

NIDEF PERSONNEL
(May 1973)

DEPARTMENTS	Managers		Employees				Change		Total
	Director	Deput. Direct.	Specialists	Secret.	Typists	Lab.	Resignation	Recruitment	
PRESIDENT OFFICE	1		1	3			None	None	5
INVESTMENT Promotion Depart. (51)	1	1	3	1			"		6
FINANCE & BANKING Depart. (52)	1	2	9	1			"		13
BUDGETING & DEVELOPMENT Depart. (53)	1	1	6	1			"		9
MANAGEMENT Depart. (54)	1		1	5	6	3			16
STAFF - Committee *	(1)		(4)						(5)
VN - ADVISOR	2						"		2
TOTAL	7	4	20	11	6	3			51

Number of Ph.D	: 4
Number of Ph.D candidates	: 2
Number of M.S.	: 11
Number of HDC	: 2
Number of DS	: 4
Engineer	: 10
Licencie's	: 4.

From USA	: 13
France	: 8
New Zealand	: 3
Japan	: 4
VN	: 6

* NOT INCLUDED IN TOTAL

Second, income from interest and fees appears to be almost twice as large as expenditures. As a result, "earned" surpluses were almost 30 million piasters as compared to 25 million piasters in total expenditures for 1972. Of course, NEDF occupied rent free offices in the National Bank Building and received other services provided by the Bank.

This raises an interesting point. The Project Agreement stipulates that surpluses will be disposed of by the Board of Directors. To avoid increasing the temptation to spend, it may be appropriate to suggest annual budgeting and an automatic disposal of earned surpluses to counterpart or the GVN unless there is agreement to do otherwise.

The interest income is determined by the rate charged by NEDF (which has been 10 percent). Since the grant counterpart has been provided at no cost, the margin is the interest rate charged. When the volume of loans increase with no change in rate and relatively no change in the number of staff, surplus income will increase sharply. However, when counterpart from foreign loans becomes available, the NEDF margin will have to be relatively small and volume will be the decisive factor.

IV. GENERAL COMMENTS

III. NEDF Relationships with USAID

USAID relationships with NEDF are by necessity governed by performance of the objectives as stated in the Project Agreement. It is our opinion that the Project Agreement is deficient on a number of points in that it fails to clearly direct and define the duties of the Fund. Because of these deficiencies, many different opinions exist within the USAID Mission as to the level of performance of the NEDF staff. Without clear-cut guidelines as to what constitutes "stimulation" to private sector investment, an evaluation of performance is difficult. In like fashion, the degree of improvement of medium and long-term lending institutions cannot be precisely defined. Working relationships can be said to be cooperative and cordial although more exchange of ideas is needed. For example, one of the principal delays in loan approval has been the lack of translator services from Vietnamese to English. We were told that this has resulted in a delay of up to several months in some loan considerations. If continued foreign borrowing is to be encouraged, timely translation services in several languages must be provided for.

We understand that while there have been misunderstandings and differences of opinion in the past, both NEDF and AID officials indicate that relationships have greately improved.

IV. GENERAL COMMENTS

IV. Investment Climate

The investment climate in all sectors in South Vietnam was still depressed in May of 1973, five months after the cease-fire signing. Continued shooting incidents, labor problems, and a 25 percent annual rate of inflation made GVN prospects for rapid economic development less than encouraging.

Everyone contacted was doubtful of an immediate major investment increase in the economy, some, however, were very optimistic for the long-term investment picture. Presidents Nixon and Thieu recently agreed and announced that economic development is a high priority item for South Vietnam. Toward this end, on May 20, President Thieu made a major TV speech in which he told the South Vietnamese people that economic development has high priority for SVN and that NEDF would play a significant role. This creates the climate and optimism that suggest that a "boom psychology" can be created this year. While the rhetorical climate is thus set, the coordination and action climate has not yet been developed.

IV. GENERAL COMMENTS

V. Financial Performance of the NEDF

At the end of May 1973 after the first fifteen months of operation, NEDF committed ordinary counterpart 9.4 billion piasters and disbursed 3.7 billion. This consists of project loan commitments of 4.4 billion and disbursements 0.8 billion and line of credit commitments 5 billion and disbursements 2.9 billion. In the first five months of 1973, total commitments increased 143 percent while disbursements increased 110 percent. This was due to a sharp increase in commitments in this past quarter, March to May 1973, and small disbursements which adversely affected the sharp increase in line of credit disbursements. See Table 1 for quarterly totals.

Among the three development banks, SOFIDIV led the most project loan commitments at 2.3 billion while the government-owned Industrial Development Bank (IDB) committed 2.1 billion piasters as of the end of May 1973. However, the IDB disbursed almost half a billion while SOFIDIV disbursed half of that or a quarter of a billion. Both institutions received 2 billion each in lines of credit but again IDB disbursed 1.3 billion while SOFIDIV disbursed about half of that or 0.6 billion. The Agricultural Development Bank did not have project loans but had lines of credit totaling one billion piasters of which almost all was disbursed. See Table 2 which follows for further details.

NEDF income in the ten months ending December 31, 1972 amounted to 55.2 million of which 33.5 million came from interest on project

loans (primarily from IDB), 16.6 million came from interest on lines of credit (primarily for IDB) and a .5 million from commitment fees, half of which came from SOFIDIV.

In the first quarter of 1973 total income at 52.8 million almost equalled the previous ten months. Of this, 32.3 million piasters came from interest on lines of credit (primarily from IDB), 18.1 million from interest on project loans (largely from IDB) and 2.4 million was realized from commitment fees (half from SOFIDIV). See Table 3 for details on NEDF income.

Reconstruction fund

The GVN has recently made one billion piasters counterpart available to NEDF for reconstruction lending. To date 520 million piasters have been committed under a Line of Credit, and it is expected that 200 million piasters of this will be disbursed in the next month. NEDF has determined that all reconstruction lending will be under a Line of Credit. Eleven rural banks have been given a line of credit for 20 million piasters each; SOFIDIV 100 million; and three commercial banks from 50 to 100 million piasters each. No minimum amount per lending institution has been set for the special fund. The interest rate is 1 percent and the spread to ICIs is 7 percent. Thus the cost to the borrower is 8 percent. The repayment period is from 2 to 6 years.

NEDF has estimated that it can create effective demand for about three billion piasters in reconstruction lending in 1973.

The estimate is based on recent interest expressed by ICIs and NEDF's rule that only property damaged or destroyed after January 1, 1972, can be financed from the Fund.

TABLE 1

STATEMENT OF CREDIT COMMITMENT AND DEVELOPMENT BY QUARTER

Quarter		Prior Approval		Line of Credit		Total	
		Committed	Disbursed	Committed	Disbursed	Committed	Disbursed
March 1, 1972	May 31, 1972	500.000.000	448.000.000	1.000.000.000		1.500.000.000	448.000.000
June 1, 1972	August 31, 1972	868.725.000	108.805.007	500.000.000	309.855.000	1.368.725.000	418.660.007
Sept. 1, 1972	Nov. 30, 1972		32.796.775	-	218.271.000	-	251.067.775
Dec. 1, 1972	Feb. 28, 1973		149.217.030	1.500.000.000	1341.259.000	1.500.000.000	1490.476.030
March 1, 1973	May 31, 1973	3.046.000.000	53.300.000	2.000.000.000	1019.621.000	5.046.000.000	1.072.921.000
TOTAL		4.414.725.000	792.118.812	5.000.000.000	2.889.006.000	9.414.725.000	3.681.124.812

TABLE 2

STATEMENT OF LOAN COMMITMENT AND DISBURSEMENT AT THE END OF MAY 31st 1973

ICIs	Prior Approval		Line of Credit		Total	
	Commited	Disbursed	Commited	Disbursed	Commited	Disbursed
I. INDUSTRIAL DEVELOPMENT BANK						
Agreement No. 001 (VIMYTEX)	500.000.000	448.000.000				
" 002			500.000.000	453.245.000		
" 008			500.000.000	453.618.000		
" 009			500.000.000	417.443.000		
" 011 (VICASA)	300.000.000	-				
" 012 (VIDOPIN)	600.000.000	-				
" 015			500.000.000	-		
" 020 (VINATEXCO)	256.000.000	-				
" 021 (VIMYTEX)	400.000.000	-				
Total	2.056.000.000	448.000.000	2.000.000.000	1.324.306.000	4.056.000.000	1.772.306.000
II. AGRICULTURAL DEVELOPMENT BANK						
Agreement No. 003			500.000.000	493.000.000		
" 019			500.000.000	489.000.000		
Total			1.000.000.000	982.000.000	1.000.000	982.000.000
III. SOFIDIV						
Agreement No. 004 (COSUVINA)	570.000.000	-				
" 006			500.000.000	320.000.000		
" 007 CITROEN	200.000.000	200.000.000				
" 010			500.000.000	183.100.000		
(FNCB : 30%) 013 DIELAC	900.000.000	-				
" 014 DAVITUCO	290.000.000	53.300.000				
" 016 THỜI ĐẠI	300.000.000	-				
" 017			500.000.000	79.600.000		
" 018			500.000.000	-		
Total	2.260.000.000	253.300.000	2.000.000.000	582.700.000	4.260.000.000	836.000.000
V. BOA (BANK OF AMERICA)						
Agreement No. 005 FOREMOST	98.725.000	90.818.812			98.725.000	90.818.812
Total	4.414.725.000	792.118.812	5.000.000.000	2.889.006	9.414.725.000	3.681.124.812

TABLE 3

STATEMENT OF COMMITMENT FEE AND INTEREST BY QUARTER

Quarter	Commitment fee	Interest Income, PAL	Interest Income, LOC	Total
II. 30.06.1972				
- Industrial Development Bank	327.287	5.646.027	-	5.973.314
- Agricultural Development Bank	212.328			212.328
III. 30.09.1972				
- IDB	587.583	11.292.054	2.161.726	14.041.363
- SOFIDIV	1.408.772	1.643.835	862.848	3.915.455
- Bank of America	120.853	125.441	-	246.294
IV. 31.12.1972				
- IDB	417.890	11.292.054	9.391.164	21.101.108
- ADB	615.097	-	601.534	1.216.631
- SOFIDIV	1.296.774	2.520.547	3.554.846	7.372.167
- BOA	74.237	1.003.666	-	1.077.903
TOTAL 1972	5.060.821	33.523.624	16.572.118	55.156.563
I. 31.03.1973				
- IDB	1.045.478	11.046.575	25.249.365	37.341.418
- SOFIDIV	1.394.594	4.849.315	7.067.013	13.310.922
- BOA	7.738	2.212.400	-	2.220.138
TOTAL Q.I/73	2.447.810	18.108.290	32.316.378	52.872.478

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IV. GENERAL COMMENTS

VI. Projected Credit Requirements

The NEDF staff made "global" projections for effective credit demand from NEDF during calendar year 1973. The projections were made at the first of the year when the investment climate was very severely depressed.

The total private sector loan requests were estimated at 12.6 billion piasters with about 54 percent required for project assistance and 46 percent for line of credit requests.

NEDF ESTIMATE OF 1973 DEVELOPMENT CREDIT REQUIREMENTS
BY ICIs PRIVATE CORPORATIONS
(in billions of piasters)
ICIs

Type Credit	IDB	SOFIDIV	ADB	Rural Banks	Other ICIs	Total	Percent
LOC	2,352	2,390	1,040			5,782	46
PA	1,588	1,300		450	3,250	6,888	54
Total	3,940	3,690	1,040	450	3,250	12,670	100

It is significant to note that the ADB and rural banks do not figure prominently in the projected line of credit demand. In fact the January 1973 estimate of 1,040 billion piasters for the ADB now appears to be low. This due to President Thieu's speech on May 20 in which he placed high priority on providing credit to farmers to encourage agricultural production. The ADB is in the process of planning a credit program to reflect President Thieu's priorities and suggested funding level.

IV. GENERAL COMMENTS

VII. Stimulating Investment

To offset the negative investment and development climate we suggest that the GVN very soon take specific action in both the industrial and agricultural sectors.

a. The Industrial Sectors

One of the more significant actions that the GVN might take would be to guarantee the sales of private firms if they are unable to move all that they produce at an acceptable price. Such action is necessary since the effective demand is unknown in the short run. This is the case for fertilizer, cement, wood products and other primary products that SVN needs. Guaranteed sales should not, however, be a GVN policy for marginal needs industries and only a percent of sales need be guaranteed for primary industries.

The major advantage of guaranteed sales is that the private firm entrepreneur will know that he won't lose money if he maximizes output. With such a guarantee he will be able to obtain credit from commercial banks since the lender's risk is minimized and depends for the most part on the strength of the government itself.

The sales (or part of total sales) guarantee of primary industrial firms should be for no more than a year at a time and should be frequently reassessed for results and adjusted as needed.

Another proposal for stimulating a boom psychology that has been advanced is GVN subsidized low interest rate equity loans. We

believe that the guaranteed sales proposal is superior since the sales approach requires subsidies only one year at a time while the equity loan proposal would involve subsidies over a ten-year or longer period. Given the likely prospect that effective demand will be strong, we believe that the amount of the subsidy will be small since the GVN needs to procure most of the items for its army and for resettlement programs.

b. Agricultural Sector

There is the temptation to suggest American-like complex agricultural commodity programs whereby the GVN would establish a grain stabilization fund for the agricultural sector and stand ready to buy in the market to maintain a price that would artificially encourage production. We cannot, however, suggest such a program but rather would suggest the intensive extension of credit to small farmers, a supervised agricultural production program, a vigorous extension service with a varied production orientation and an applied research and development program to provide improved seed varieties and crop chemicals.

The GVN may, however, need a price support and purchase guarantee program for encouraging production of new seed varieties--especially corn, sorghum and soybeans. Given the current emphasis on exports, the GVN should be encouraged to develop a reserve of staples such as rice to meet short crop years or emergencies as soon as domestic production exceeds domestic demand. This should be done before any surplus is exported.

The ADC and its branch banks should concentrate primarily on

their traditional role of providing supervised credit to small farmers and to encouraging and coordinating farm inputs and marketing. We also believe that if farmers are provided with an opportunity to purchase inputs (including machinery and equipment) that they will be like farmers the world over and produce more to increase their returns.

We believe that such a program will stimulate agricultural production the most rapidly and over time will maintain an expanding production. Such a program will also keep SVI agricultural prices at world levels.

IV. GENERAL COMMENTS

VIII. Possible New Objectives for NEDF

It is not possible to specify precisely new or additional objectives and functions for NEDF at this time. This is primarily due to anticipated changes in the organizational structure of the Vietnamese Government to implement massive economic development and reconstruction programs and also due to possible changes in the type and volume of AID funding and other funding with relationship to NEDF. The following are some possibilities that have been mentioned or implied in our conversations:

a. The Korean Model: Economic Planning Board

Dr. Nguyen Van Hao, NEDF, suggested that the NEDF could be transformed into a super ministry which would reflect President Thieu's commitments and priorities to implement economic development and reconstruction. If it follows the Korean model, there would be a strong Deputy Prime Minister who would coordinate and implement the government's economic plan among the ministries. In addition, it would have the control over the budget. This would require substantial personal attention by the President and cabinet ministers.

The funds, both domestic and foreign, would follow the normal administrative procedures but the policies, direction, control and priorities would be determined by the Economic Planning Board which would be responsible for achievement of the overall goals.

President Thi in his May 20 speech appeared to have come close to this Korean mod ith some possible differences. The

Leadership Council for Reconstruction and Development, which the President would personally chair with ministers from relevant parts of the government involved directly in economic development and reconstruction, would be assisted by a national commissioner who would have control and supervision of planning, budget and statistics. It is understood that this would organizationally be in the Office of the President. While the Commissioner would presumably have cabinet rank he would not be a member of the cabinet. Of course, the form of the organization is probably less important than the substance but it does not provide the bureaucracy and public with the idea that there is a permanent shift in the structure of government that reflects policy priorities.

b. The Singapore and Hong Kong Model

While it is not necessary to follow in detail any particular form, Singapore's Economic Development Board (now defunct) does provide an intermediate form. Specifically, the NEDB would be changed to focus sharply on particular production sectors and enterprises in agriculture and industry that are judged to be difficult for domestic investors alone. The flexible approach of providing investment and financial incentives to domestic and foreign investors for specific activities on a timely basis contributed to the rapid success of the Economic Development Board. It is true that this organization was thought to have outlived its usefulness and has in recent years become a development bank.

The Hong Kong model is simply meant to indicate that under

certain conditions there need not be a strong governmental organization to plan, promote and implement development.

c. Development Policy Institute

NEDF could become a development policy research organization attached to the Office of the President or Leadership Council for Reconstruction and Development to be chaired by the President. Since this Council will be responsible for suggesting reconstruction and development policies and guidelines, for setting program priorities, for mobilizing, administering, supervising and coordinating domestic and foreign resources for the economy, it would appear reasonable that a policy research unit should be included.

The model for this is the Korean Development Institute which is funded partly by AID. The institute has a sister relationship to the Harvard Development Advisory Service which provides a mechanism to hire foreign consultants and specialists and to train and facilitate work of the Korean staff. This would be different from the work of a planning staff.

d. Development Credit in the National Bank

NEDF could be absorbed by the National Bank which is responsible for macro-monetary and credit policies. The Central Bank could, for example, have two deputy governors. One would perform the normal functions associated with short-term credit policies of the commercial banks and possibly the rural banks, that is, control and supervision of deposit banks or deposit banking.

The other deputy governor could supervise and set policies

for development banks, i.e. medium and long-term lending. This could include participation in seeking foreign development loans and would lead to a role in securing government guarantees and in managing the external debt structure. This could be an appropriate mechanism to control and coordinate all foreign loans and other capital flows.

This suggestion would greatly expand the scope of the Central Bank from concentration on short-term urban industrial credit (which is a relatively small proportion of GNP) to include short-term agricultural production credit through rural banks and supervision and control of development credit and banks.

e. Status Quo with Some Changes

NEDF could continue for the next year or two with its current objective of improving the medium and long-term lending capability of the ICIs with some minor changes to accommodate new conditions and funding such as foreign loans. Perhaps NEDF could focus more on small and medium sized enterprises and loans of ICIs in both the industrial and particularly the agricultural sector, by more flexible disbursement policies, especially free lines of credit. Other issues are discussed elsewhere in this report.

PEOPLE INTERVIEWED IN VIETNAM

USAID MISSION SOUTH VIETNAM

1. John P. Robinson, Mission Director
2. Stanley J. Siegel, Deputy Director
3. Willard D. Sharpe, Deputy Economic Counselor
4. Richmond Allen, Chief, Joint Economic Office
5. Llewellyn P. Pascoe, Financial Attache
6. Ernest Kenrich, ADPROG
7. Peter W. Asling, ADPROG
8. Leroy L. Magner, ADPRO/PO
9. Bruce Johnson, ADCCA
10. G. Edward Thompson, ADCCA/PE
11. J. Henry Meisel, ADCCA/PE
12. Rufus A. Lenn, ADCCA/PE
13. James B. Davis, ADFA
14. Maurice V. Sorenson, ADFA
15. Eugene C. Schroepfer, ADFA
16. Ralph H. Gleason, ADFA
17. Robert A. Ralston, ADFA
18. Shelby A. Robert, ADFA
19. Richard J. Foote, ADFA
20. Marvin L. Bush, ADFA
21. William Flested, Consultant, ADFA (Retired President, Federal Land Bank, Wichita, Kansas)
22. Jack M. Murphy, ADFM

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Dr. Nguyen Van Hao, President

Dr. Nguyen Manh Hung, Chief of Staff

Dr. Nguyen Cao Hach, Economic Counselior

Mr. Le Van Phuc, Director, Investment Promotion Department

Mr. Nguyen Kim Cuong, Deputy Director, Investment Promotion Department

Mr. Nguyen Xuan Nghia, Director, Finance and Banking Department

Mr. Cao Nguyen Hien, Deputy Director, Finance and Banking Department

Mr. Phan Huy Kiem, Director, Research and Development Department

Mr. Tran Kiem Canh, Director, Management Department

Mr. Donald R. Jones, Checchi consultant to NEDF

Mr. Richard Kimball, Checchi consultant to NEDF

NATIONAL BANK OF VIETNAM

Le Quang Uyen, Governor

Nguyen Van Dong, Deputy Governor

VIETNAM COMMERCIAL CREDIT BANK

Mr. Dang Co, Assistant Director General

AGRICULTURAL DEVELOPMENT BANK

Col. Nguyen Dang Hai, Director General

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Vu Quoc Thuc - former Minister of State for Reconstruction & Development

Pham Van Thuyet - President of Mekong Company

Tran Nhu Trang, Vice Dean, Deputy of Social Science, Van Hanh University

Tran Thi Hoai Tran, Vice Dean, Faculty of Law, Saigon University

Mr. Nguyen Tien Hung, Professor

GVN MINISTERS

Mr. Pham Kim Ngoc, Minister of Economy

Mr. Nguyen Duc Cuong, Vice Minister of Economy

Mr. Ha Xuan Trung, Minister of Finance

Mr. Vu Khac Dung, Vice Minister of Finance

Mr. Pham Minh Luong, Deputy Minister of Economy

OTHER GVN OFFICIALS

Mr. Nguyen Kien Thien An, Director General, Public Warehouse

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Lam Ven Si, Director General

Nguyen Huu Minh, Deputy Director General

PRIVATE BANKERS IN SOUTH VIETNAM

Mr. J. R. Hudspeth, General Manager, First National City Bank

Mr. Nguyen Tang Kim, Director General, Nam Do Bank

Mr. Lam Vo Hoang, Assistant Director General of the Vietnam Commerce & Credit Bank

Mr. Nguyen Vo Dieu, Director General, Mekong Bank

INDUSTRIAL DEVELOPMENT BANK

Lam Ho, Deputy Director General

INTERNATIONAL MONETARY FUND

Mr. Nguyen Huu Hanh, Alternate Executive Director

INTERNATIONAL BANK FOR RECONSTRUCTION & DEVELOPMENT

Mr. Manfred G. Bichel, Chief Economist

Mr. David G. Beese, Agricultural Economist

Mr. Bernard A. Schmitz, Economist

Mr. Hsien T. Chang, Agriculturist

Mr. Harold R. Young, Engineer

BUSINESSMEN

Truong Van Qui, President - The Confederation of Industrialists and Craftsmen of Vietnam

Houng Pao Jen, President of Vinytex Company

Edwin P. Ketchum, General Manager, Esso Company

Tuong Thai Ton, President/General Manager, Mekong Fisheries Products Co.

POLITICIANS

Mr. Tran Van Tuyen, Attorney at Law, Member of the House of Representatives

Mr. Vo Long Trieu, Member of the House of Representatives

Mr. Ho Ngoc Nhuan, Member of the House of Representatives

Mr. Nhan Minh Trang, Member of the House of Representatives

Mr. Nguyen Van Dieu, Member of the House of Representatives

Mr. Huynh Van Lau, Member of the House of Representatives

Mr. Tran Van Tuyen, Member of the House of Representatives

Mr. Tran Fuy Don, Senator, Chairman Agricultural Committee

Mr. Tran Ngoc Oanh, Senator, Chairman, Appropriations & Budget Committee